English Premier League Business Principles Applied to American Sports

An Honors Thesis (HONRS 499)

By

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May, 2011

Expected Date of Graduation
May, 2011
Abstract
Throughout the history of professional sports in America, there have always been labor negotiations between the respective owners associations and players associations. These negotiations are what laid the foundation for the rules and regulations that govern the sport entity. These negotiations are often complicated since the two parties involved often want radically different things. These complications have, in the past, led to work stoppages and therefore no product to be consumed, thus hurting both parties. The business model that is used in Europe for professional soccer has never led to a work stoppage. By analyzing their business model and comparing it to the typical American business model for professional sports, I will compare and contrast to find flaws in the American system.

Acknowledgements
I would like to thank Dr. Michelle Brimecombe for advising me through the project and for everything she has helped me with throughout the course of my education.
Introduction

In the United States, the four largest sports organizations in order are the National Football League (NFL), Major League Baseball (MLB), the National Basketball Association (NBA), and the National Hockey League (NHL). Combined, these brought in $22.5 billion in revenue in the year 2010 (Gaines, 2011), making the sports industry one of the largest industries in the country. However, with the large amount of revenue brought in by the sports industry, labor agreements between the respective players associations and owners associations are often hard to reach. When dealing with so much revenue, the following question of who gets what will frequently be disagreed upon between the players and owners of their respective leagues. Sometimes these disagreements can ultimately lead to work stoppages. This situation is what the NFL and NBA are dealing with currently.

When the two sides, the owners and players, are negotiating, they are trying to reach what is called a collective bargaining agreement. This agreement is what allows the league to function by dictating what the governing rules of the league will be and how it will operate. When there is no collective bargaining agreement in place by the players, the owners tell their players they are not allowed to come in to work. This is what is called a lockout, and on March 12, 2011 an NFL lockout officially began (Katzowitz & Benoit, 2011). They are now joined by the NBA which has also locked out their players as of July 1st, 2011.

With two of the three biggest professional sports leagues in the world currently having problems negotiating with their players, one starts to wonder if there is something wrong with the way the leagues are run. At the very least, one has to wonder if there is a better way to do business and negotiate with these players associations. Rather than look at other leagues
within our country, it would be beneficial to look abroad and see how things are done differently.

Looking at the business principles used by professional soccer in Europe, specifically England's the English Premier League, one can see some efficient ideas that have led to no labor disputes in its 122 year history. Through comparing and contrasting these business principles with the practices commonly used in the United States, the picture may become clearer why the NFL and NBA are currently experiencing player lockouts and why the NHL and MLB have been locked out as recently as 2004-2005 and 1994-1995 respectively.

Unequal Media Revenue Sharing

The first business principle the English Premier League (EPL) uses that is different from American sports is the use of a revenue sharing system that is not completely equal. In the NFL, television revenue is divided equally amongst all of the teams. In the last NFL collective bargaining agreement (CBA), media revenue sharing worked like this according to Nick Herzeca;

Roughly 2/3 of the NFL's revenue comes from lucrative TV and radio broadcasting deals. The salary cap, the maximum money that goes to the players, utilizes about 2/3 of the team's revenue. Therefore, the TV and radio broadcasting deals pay for the players' salaries. The other 1/3 of the league's generated revenue is derived from stadium sales, such as corporate boxes, seat sales and concession sales. This revenue sharing system gives teams, big or small market, a level, competitive playing field, while still giving entrepreneurial owners the ability to make substantial additional money through stadium income (Herzeca, 2008).
The idea behind the NFL’s system has pushed the league closer to being a league of parity, and this has been a large part of their past success as a league and their growth. However, what the system fails to prevent is some teams spending below the maximum amount allowed by the salary cap. Owners can spend under the maximum and not use their full 1/32 of the media revenue to improve their team by spending it on players. Such is the case in 2009 with the Kansas City Chiefs.

In 2009 the Chiefs had a payroll of about $82 million. That year the salary cap would have been approximately $125 million when you divide the total media revenue, $4 billion, by the thirty-two teams (Munson, 2011). The eventual Super Bowl champions that year, the New Orleans Saints, had a payroll of $122 million (USA Today, 2010) which is about 1.5 times higher than the Chiefs’ payroll. This is the underlying issue of a large problem. The Saints’ success is arguably more responsible for bringing in the $4 billion in media revenue that is equally shared than the Chiefs, who finished in last place in their conference. The media revenue is equally shared, but not equally earned.

The Chiefs owner was allowed to keep the $40 million difference between the media revenue and the team’s salaries. This $40 million could have been used to make his team more competitive. Having his team be more competitive would have arguably made the league more competitive and thus more profitable. This is where the issue lies. He had no incentive to improve his team when he could keep the $40 million.

In the EPL, the way they share their media revenue is slightly different than the way it is done in the United States and could help fix this problem. The top team in the EPL receives 1.6 times more than the bottom team gets. The EPL’s current media revenue is about £1.2 billion
which will be generated over the next three years. Out of that, at least £37m will be given to each team in the Premier League through TV revenue (Anderson, 2011).

If we would apply this method to the NFL, we would see that the Saints would have made in 2009-2010 about $151 million. They would have been rewarded for their success and for their larger contribution to the media revenue by having received $29 million more than they spent on their roster. The last place team would have received about $94 million. This team happened to be the St. Louis Rams who spent about $100 million on their roster (USA Today, 2010) and would have only lost $6 million. Teams like the Chiefs could then keep their roster salaries towards the minimum allowed, but there would be less incentive to do so since having a better team would lead to it being more profitable.

This strategy of media revenue sharing has worked more favorably than any other system used in European soccer. As compared to the other European leagues, EPL generates around ten times more than Germany’s Bundesliga, five times what Italy receives, and three times the amount Spain’s La Liga earns. The EPL has the fairest spread of earnings generated from television rights. It has the smallest difference between receipts of the champions and the lowest ranked team (Anderson, 2011). A system like this could be very beneficial to leagues in the United States.

Relegation and Scheduling

In American sports, there will always be “rebuilding”. This term means that a team will get younger on purpose, which a lot of times means getting worse on purpose, in order to set themselves up to be in a good position to win in a few years. In other words, teams plan on being bad in the present in order to increase their chances of being good in the future. This is a
situation that perpetuates the problem of bringing revenue into the league since games between teams rebuilding and teams trying to win now are usually unentertaining.

The best example of this is in the NBA in Los Angeles. Los Angeles is home to two NBA franchises, the Clippers and the Lakers. The Lakers moved to Los Angeles from Minnesota and had their first season there in 1960-61 (Yahoo, 2009). The Lakers (both in Minnesota and Los Angeles) have been to the playoffs fifty-eight times in sixty-three seasons which means they have only missed the playoffs five times in the franchise’s history. They have also won the NBA championship sixteen times out of those fifty-eight appearances (Basketball Reference, 2011).

The other team in Los Angeles, the Clippers, has had far less success than their neighbors. The Clippers have been in three cities so far in their franchise’s history. First, they were the Buffalo Braves from 1970 to 1978. From the 1978-79 season until the 1983-84 season they were the San Diego Clippers. They then moved to Los Angeles to become the Los Angeles Clippers and have been there since the 1984-85 season. In the forty-one seasons the franchise has had, they have only made the playoffs seven times and have not won a championship (Basketball Reference, 2011).

One has to wonder, why are two teams in the same city having such a wide disparity of success? In the NBA, there is no punishment for not doing well. To fix this situation, the NBA should perhaps look into the benefits from implementing a promotion and relegation system. This system has been a part of the English Premier League since the league came into existence twenty years ago.

On July 17th, 1991 the English Premier League came into existence out of the Football League First Division. The top teams in the Football League First Division had grown weary of
the lack of revenue they were making due to the lack of interest in their league. This lack of interest in large part was derived from having a large disparity in talent between the best teams in the league and the worst teams. The fans did not like the lack of competitiveness (Premier League, 2011). In order to ensure there would always be competitiveness, even at the bottom of the standings, the EPL annually demotes the bottom three teams in the league back to the Football League Championship (formerly known as the Football League First Division) and promotes the top two teams in the regular season standings plus the winner of a tournament out of the next four teams (Premier League, 2011).

If the NBA were to adopt this way of doing business; it would mean that there would be more incentive to do well throughout the entire standings. Teams would be less inclined to take a long time to rebuild because they would not want to fall out of the top tier in the NBA. In reference to the Clippers and Lakers comparison, the Clippers would be less satisfied with missing the playoffs and would be forced to try to win more consistently. As a result, this would force them to spend more on their roster than their league low $32 million, which is $29 million less than the second lowest team (USA Today, 2010).

The NBA could still maintain their status as a franchise sport, something that is highly valued by the owners. This means that each team in the NBA is still a member of the league even after the league is divided in two. Instead of the top tier being its own league, which is the case in the EPL, it would rather be a set of conferences like there is now. The only difference would be that instead of there being Eastern and Western conferences there would be a top tier conference and a second tier conference. Within both of these conferences, there would be two divisions.
The financial implications of this would mean that the top tier would need to receive more of the shared revenue than the second tier in order to create the incentive necessary to try and stay in the top tier. However, with the way the finances are structured in the NBA, creating a large disparity would mean that some franchises would ultimately cease to exist due to financial difficulty. Therefore, since the NBA would be maintaining unity and its status as a franchise sport, it would be wise to take the shared revenue and give a larger percentage to the top division than the bottom.

A hypothetical situation of this would be to give $\frac{6}{11}$ of total shared revenue to be divided equally amongst the top tier and give the remaining $\frac{5}{11}$ths to be divided equally amongst the second tier. Then, if a new salary cap was instituted that was equal to $\frac{5}{11}$ths of the total shared revenue, all teams, both in the second tier and top tier would have an equal opportunity to compete, and the remaining $\frac{1}{11}$ would be strictly financial incentive to do well. The problems that would be created as a result of a restructuring of the league would be the layout and size of the conferences and the way the schedule would be composed to create a competitive balance.

To help solve these problems, it would be best if the league were to be expanded by two franchises. Out of the thirty biggest metropolitan areas in the United States, there are currently ten metropolitan areas that do not currently have an NBA franchise located in their area. These metropolitan areas include Kansas City (29th), Cincinnati (27th), Pittsburg (22nd), Baltimore (20th), Tampa Bay (19th), St. Louis (18th), San Diego (17th), and Seattle (15th) (US Census Bureau, 2010). Each one of these cities has teams that are in the NFL and MLB, so they have shown the ability to support professional sport franchises in the past. By putting an NBA
franchise in two of these cities, the NBA could increase the number of franchises they have to thirty-two. This would allow the league to create two balanced conferences of sixteen teams, creating a similar layout that is currently used by the NFL.

The schedule being altered would also be necessary. Each team in the NBA currently plays eighty-two games a season. That number would be impossible to reach if the league wished to have perfectly balanced scheduling. Therefore, the number of total games would have to be reduced to seventy-six. There would be four divisions total (two in each conference), and each team would play every team not in their division twice, including teams in the other conference, and the remaining seven teams in their division four times. This regular season schedule would determine who plays in the playoffs of each conference and what their seeds would be.

In the playoffs, average television ratings increase each round. In 2011, the first round average Nielsen rating was 2.7 (Seidman, 2011). In the second round, the average rating was 3.0 (Gorman, 2011). Then the conference finals saw a larger jump up to 6.2 (Sports Media News, 2011). The NBA finals then averaged 10.1 (Barron, 2011). From this information, it becomes clear that the first and second rounds are not watched very much. Restructuring could improve this dramatically.

With relegation the format of the playoffs would be much different. In the top conference, only the top eight teams would compete. This playoff format would expect the same ratings as the current NBA finals, conference finals, and 2nd round. However, the league would make more revenue off of the bottom conference’s tournament than they do currently with their first round.
In the lower conference, the top two teams in the regular standings would automatically be promoted to the higher division for the following season. However, they would still be allowed to compete in the playoffs. It would decrease the financial incentive to finish in the top two to remove the possibility to earn more revenue by hosting home playoff basketball games, especially when the teams earned home court advantage by having very good regular season records.

The entire lower conference would compete in the playoffs to see who would become conference champion. The other two promotions, other than the top two regular season teams, would be received by the two teams that finished the best in the playoffs. If multiple teams finish in the same round, then the team with the best regular season record would receive the promotion. A hypothetical situation that would cover these situations could be the following: if the 1 seed lost in one of the first two rounds, and the 2, 3, 4, and 5 seeds made it to the semi-finals with the 2 and 5 advancing to the finals. Then the teams that would advance would be the 1 and 2 because of their automatic promotions, the 5 because they went the farthest of all teams without automatic promotions, and the 3 because they finished in the same round as the 4 but had a better regular season record.

Conclusion

When examining the business principles that the EPL uses, it is hard not to notice that the main goal for a lot of what they do is to increase competitiveness in all games. They have created a system that perpetuates competition at all levels of the standings by making them mean something. Having a league that decreases the number of meaningless games is the best way to ensure that the league is popular. Popularity, in return, will lead to more revenue. Of all
the business principles that the EPL uses, the theme remains the same: No matter where any given team is in the standings, they have something to play for.

At the bottom of the league, teams are playing to avoid being relegated down to a lower league. At the top of the league, teams are trying to finish in the top four to play in the Champions League. The Champions League features the best teams from the other soccer leagues in Europe that EPL teams play in addition to their Premier League season. Teams competing in the UEFA Champions League group stage this season can expect to receive a minimum amount of €7.2m (UEFA, 2010). Even if a team is in the middle of the standings, the amount of the shared television revenue received is based on where the team finishes, so there is still pressure on doing well to try and pass as many teams as possible.

Meaningful games to popularity to maximum revenue possible. That is what American sports can take away from the EPL. All avenues should be explored, even some innovative ones not used in our country, in order to bring as much money into the leagues. When there is more money then it will be less scarce and both the players and owners will receive more of it. More money for both sides is the best way to lead to players and owners being content and feel as though they have gotten what they deserve. By exploring a different way to do things, the EPL’s way, the leagues in our country could help decrease the labor disagreements that take place in our professional sports.
Works Cited


