ECONOMICS OF COLLEGE SPORTS

John Fizel, Rodney Fort

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Introduction

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Economics of College Sports: An Overview

John Fizel and Rodney Fort

INTRODUCTION

College sports are big business. Major college coaches, such as basketball coach Mike Krzyzewski at Duke University or football coach Phillip Fulmer at the University of Tennessee, make headlines when their compensation packages exceed $1–2 million annually, making them the highest paid university and state employees. Coaches often earn additional income through sports camps, media shows, and athletic apparel endorsement contracts. Washington State University, a modestly funded major collegiate sports program, reported athletic revenue of $16.8 million for 1997–1998.[1] College athletic events are held in state-of-the-art facilities, like the University of Maryland basketball program's new $107 million dollar arena. The NCAA reports 2001–02 revenues of approximately $346 million from Division I sports, $14.6 million from Division II, and $11 million from Division III. Television contracts for Atlantic Coast, Big East, Big 10, Pac 10, and SEC conference football are valued at approximately $350 million, not including shares of the $140 million paid out from 1998 post-season Bowl games, while CBS just negotiated an 11-year, $6 billion contract to broadcast the NCAA Division I basketball tournament.

Where do, or should, these lucrative athletic ventures fit in the mission of higher education? To what extent is the central mission of creating an environment for learning and extending the frontiers of knowledge enhanced or limited by college sports? Are declarations by the NCAA to promote amateurism and competitive balance supportive of the university mission? Does the NCAA even follow its purported objectives?

Economics of College Sports contains both empirical and theoretical research to address these and related issues. The book opens with three chapters that provide unique perspectives into the organization of collegiate athletics and the university mission. In the first chapter, Joel Maxcy examines the role and structure of the NCAA in influencing the operations of collegiate athletics and the link between athletics and university educational missions. Specifically, Maxcy addresses how the 1997 restructuring of the NCAA attempted to bring stability to the collegiate athletics and power to university presidents. His analysis suggests that the reorganization has succeeded in appeasing, at least temporarily, the wishes of the least- and greatest-invested universities. The implication of the university presidents' new power to exert control over athletics is less clear.

Paul Staudohar and Barry Zepel critique the findings and recommendations of three major studies that examine athletic programs in the context of the mission of higher education. They conclude that education leaders have the opportunity to greatly reduce the existing conflicts between developing commercialized sports programs and fostering stimulating environments for learning if they adopt the recommendations of these studies. However, there is no centralized authority to mandate support of educational missions, nor do the incentives of the NCAA prompt support of these missions. Implementation requires that university presidents show the fortitude to forego some of the enticements of big-dollar sports and exert their power over athletic activities.

But, what if university presidents believe that institutional academic reputations are based primarily on the quality of graduate school education and the prestigious research activities that emanate from these programs? Athletic revenues may then be an excellent way to fund these programs. And, if undergraduate education is compromised as graduation education is emphasized, then athletic activities may provide entertainment, hence appeasement, for the undergraduate students. This is the "beer and circus" hypothesis that is tested by Evan Osborne in Chapter 4.

Part III includes three chapters on the financial returns to college athletics. "Most college sports lose money" is an assertion commonly made by representatives of college athletic departments and increasingly accepted by the media, despite revenue from monster stadia and arenas that sell out, postseason tournaments, and lucrative private sports contracts.[2] Brian Goff evaluates this premise addressing both the direct and indirect financial impact athletics may have on university costs and revenues. He concludes, with qualifications, that athletic departments do not typically operate in the "red" when the vagaries of accounting convention are replaced with an economic analysis of benefits and costs.

Robert Sandy and Peter Sloane continue to address the direct and indirect impacts of college athletics, but do so in the context of a university contemplating a move in its athletic affiliation from Division II to Division I. Their results clearly indicate a move to Division I is warranted and ask "Why don't all colleges that can possibly beg or borrow the money start Division I-A programs?" The profit incentives achieved by upgrading the affiliation of an institution's athletic programs cause a constant churning within the membership of the NCAA. This churning was the impetus for the restructuring addressed in Chapter 2 by Maxcy.

In Chapter 7, Robert Baade and Victor Matheson investigate the economic returns to a city that hosts the final four for the NCAA post-season basketball tournament. They find that promoters overstate the economic impact of these mega-events because they estimate the increased spending by nonresidents but ignore reduced spending by nonresidents and residents alike. In only two of 48 final four events (men's and women's tournament finals) did the host city experience significant positive income growth.

Part IV includes four chapters that explore the relationships between college athletics and labor issues. Perhaps no issue has caused more controversy for athletic departments than gender equity or Title IX compliance. Recently, athletic departments have attempted to meet Title IX compliance standards by expanding women's sports programs and eliminating non-revenue men's sports, arguing that budget limitations require such trade-offs. Michael Leeds, Yelina Suris, and Jennifer Durkin address this issue by testing the relationship between the success of football programs, the largest of college revenue-producing sports, with the Title IX compliance of the institution. They find little evidence that football funds are used to support Title IX initiatives. Indeed, some of the most successful football programs are actually a drain on funding of women's programs.

The second chapter in this part examines the value or marginal revenue product (MRP) of a college basketball or football player. As college sports are increasingly commercialized, athletes continue to be paid far below what they would earn in a competitive market. "The NCAA operates behind a veil of amateurism as its members generate revenues comparable to professional sports, practice and play in facilities that rival those found in professional sports, and pay their top coaches salaries comparable to those paid to coaches of professional teams. Only the student athletes are bound by amateur status and restricted in their ability to share in the bounty generated by their play."[3] The extent of underpayment is estimated by Robert Brown and R. Todd Jewell, who find that the MRP of a star collegiate football player is approximately $400,000 and the MRP of a star collegiate basketball player is approximately $1.2 million. Each is in stark contrast to the full cost of attending college, the compensation limit imposed by the NCAA.

In Chapter 10, John Fizel and Timothy Smaby compare the academic performance of college athletes relative to all baccalaureate students at Penn

State University. Their analysis is disaggregated for individual sports, and for most sports, participation in intercollegiate athletics has no significant impact on the grade point averages of athletes. However, men's football is the exception. Despite the NCAA's SAT and high school course requirements, the university is able to recruit athletes who have significantly lower SAT scores than their cohorts do. Athletes also appear to opt for less rigorous curricula, and are significantly slower in advancing to an academic degree. The exploitation of the premier, revenue-producing collegiate athlete appears to have been extended to the classroom.

In the last chapter of this part, John Fizel and Michael D'Itri examine the impact of coaching turnover and the rationale for turnover on college basketball performance. Turnover, per se, is found to be disruptive to success. Furthermore, the hiring of a new, less efficient coach can cause a long-term decline in performance. Despite these implications, college coaches are typically dismissed based only on winning percentage rather than efficiency.

Part V contains three chapters that investigate competitive balance in collegiate sports. The NCAA states that fostering competitive balance is one of the organization's key purposes, and historically the NCAA has used competitive balance as a justification for the development and imposition of many of its regulations. Craig Depken and Dennis Wilson use three measures to examine competitive balance in college football from 1888 to 2001. They find that competitive balance has declined over time for all measures. Moreover, structural changes introduced by the NCAA exacerbate the decline in competitive balance when using the measure that best captures intertemporal changes. It appears that special interest groups are able to dictate policy development within the NCAA that runs counter to the purported goal of competitive balance.

In the next chapter of this part, David Berri examines competitive balance in collegiate football, baseball, and basketball and compares the competitive balance in each of these sports to their professional counterparts. Collegiate baseball and basketball have less competitive balance than collegiate football. Berri argues that competitive balance is directly related to the population of the athletes available for employment in a given sport which, in turn, is related to the number of choices athletes have available. If athletes have the option to turn pro early in their collegiate careers, the employable population is diminished and competitive balance compromised.

In the final chapter of the book, Craig Depken and Dennis Wilson estimate the impact of NCAA football probations and investigations on various measures of competitive balance in Division IA football conferences. If an institution pays athletes in an environment where other institutions abide by the NCAA's no-pay rule, the cheating institution can gain a talent advantage which can ultimately generate revenue from post-season play and additional media coverage. If sanctions are effective, cheating should be reduced and competitive balance enhanced. On average, however, Depken and Wilson find that sanctions have reduced competitive balance. They do note that the impact on competitive balance is diminished the larger the conference membership and that some conferences may exhibit an increase in competitive balance.

Economics of College Sports addresses issues in the reemerging and growing area of collegiate athletics. Perhaps the most important contributions focus on the interactions between legal and institutional aspects of the NCAA and their impact on the objectives and goals of university education. However, all of the contributions provide insights that will generate significant discussion about policies necessary to sustain the vitality and integrity of the university education-sports coalition. The major issues include:

- The restructuring of the NCAA
- The university objective function
- Sports corruption and impact on university education
- Implications of Title IX compliance
- Cartel rents for collegiate athletes
- Institutional changes and competitive balance in collegiate sports

We hope you find the research in *Economics of College Sports* to be useful, thought-provoking, and enjoyable.

NOTES

1. See Fort (2003), p. 426.
2. See, for example, *USA Today,* July 15, 1999.
3. See Fizel and Bennett (2001), p. 349.

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Part II

Structure of College Sports and the University Mission

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2

The 1997 Restructuring of the NCAA: A Transactions Cost Explanation

Joel G. Maxcy

INTRODUCTION

The National Collegiate Athletic Association (NCAA) underwent a significant change in its organizational structure in 1997. The restructuring transformed the Association's system of governance from a single body to a federated system where each of its three competitive divisions formulates separate policy. More significantly Division I, the most competitive classification, replaced a one-member, one-vote direct democracy with a representative system where the basis of representation is determined by conference membership.[1] A Board of Directors composed entirely of institutional CEOs now approves all Division I legislation. This change is especially significant because representatives from Division I-A conference institutions, although composing only about one-third of the division's total members, are mandated majority representation on the Board.[2] Divisions II and III continue to approve all legislation by a vote of the membership at an annual convention, but the legislative sessions are now separate and specific to each division.

The restructuring received considerable attention from the media and public forums because of the apparent shift in organizational control from athletic directors to university presidents. Although university presidents (and faculty representatives) had been involved in NCAA governance from its inception, a perception existed that athletic departments, whose objectives are often implied to conflict with the university mission, had gained excessive control of the organization. Under the new structure of the composition of the Board of Directors, university CEOs are given full charge of Division I policy. Additionally, Divisions II and III each established Presidents Councils to oversee the policy changes to be voted on by the membership. These changes were recognized as a shift from an emphasis on business interests to academic interests. It will be argued in this paper that presidential control is primarily a superficial revision. The shift to a federated system where the major revenue-producing football conferences are mandated a majority on legislative issues is in point of fact the significant change.

The proposal to formally restructure was concurrent with serious consideration of an NCAA-sanctioned Division I-A football play-off. All sports with the exception of Division I-A football compete for an NCAA-sanctioned (national) championship in their respective divisions. The NCAA collects all championship event revenue and redistributes a significant portion to individual members. Revenues derived from television rights currently account for about 80% of the Association's gross revenue. This can be seen in the 1998–2000 budgets shown in Table 1. The contract between the CBS network and the NCAA for Division I men's basketball tournament makes up by far the bulk of this revenue. The net revenues from the tournament are reallocated to the membership using a formula that rewards conference tournament performance; nonetheless all NCAA members, regardless of division, receive a share.

Table 1
NCAA Budget 1998–99 and 1999–2000

Revenue	Approved 1998-99 Budget	Approved 1999-2000 Budget	Percentage of Total Operating Revenue/Exp.
Television	226,400,000	241,550,000	79.63%
Championships Revenue:			
Division I men's basketball	18,235,000	19,274,000	6.35%
Other Division I championships	8,481,000	9,393,000	3.10%
Division II championships	540,000	540,000	0.18%
Division III championships	303,000	265,000	0.09%
Total Championships Revenue	27,559,000	29,472,000	9.72%
Licensing and Royalties	18,370,000	21,056,000	6.94%
Investments	7,000,000	7,150,000	2.36%
Sales, Fees, and Services	3,661,000	4,107,000	1.35%
Totals NCAA Operating Revenue	282,990,000	303,335,000	100.0%

Source: The NCAA Online Financial Section, http://www.ncaa.org/financial/.

Post-season play in Division I football consists only of bowl games. Bowl organizers and promoters are independent of the NCAA. Bowl revenue is not redistributed across the Association, as payouts stay entirely within Division I and nearly all go directly to participating schools and their conferences. Since an antitrust ruling against the NCAA in 1984, the number of members able to profit from the considerable and fast-growing television revenues from football is limited primarily to the so-called power conferences of Division I-A. It stands to reason the Association was ready to use calls from the public and sports media as leverage to institute a national play-off that would result in significant revenues collected by the NCAA and subject to redistribution. The arrangement between the Division I-A power conferences and the bowl organizers, who also profit substantially from the current system, was (and is) threatened by an NCAA sanctioned play-off.

The NCAA experienced rapid membership growth throughout the first half of the 1990s. The revenues generated by the Division I men's basketball tournament had grown substantially since the early 1980s. The majority of this increased revenue derived from a series of successively larger television contracts with CBS; in fact, rights fees for the tournament increased from \$28.3 million in 1985 to \$166.2 million in 1995 (Zimbalist, 1999a, 112). The revenue-sharing plan makes the NCAA an attractive alternative in comparison to its only competition, the National Association of Intercollegiate Athletics (NAIA). NAIA members' athletic programs are comparable in size and scope to NCAA Division II and III, and this is where they typically enter if joining the NCAA. The revenue-sharing formula allocates a fixed percentage of the Division I tournament income to Division II and III members (approximately 4% and 3%, respectively). Increased membership therefore reduces the proportion going to an individual institution. It makes economic sense that the lower divisions ask for additional autonomy in determination of their entry rules. Hence a state of affairs is defined by which the bargain for a new organizational structure could be struck.

The NCAA has been the subject of a number of economic studies. Most employ the characterization of the organization as a cartel and focus on monopsony outcomes in input markets, specifically the comparison of the value of college athletes relative to their pay (Becker, 1985; Brown, 1993 and 1994, for example). Zimbalist (1999a) devotes a portion of his analysis to the product market effects of the NCAA cartel. Fleischer et al. (1992) provide a comprehensive analysis of the NCAA organization as a cartel and consider the monopoly effects on output markets as well. The research as to how the NCAA is organized to maintain its economic functions is yet incomplete—and this is amplified by the restructuring. Because of its size, term of existence, and minimal entry barriers, the NCAA is hardly typical of the theoretical economic cartel. Because it functions as a legislative body that both provides public goods and redistributes wealth, it is perhaps most appropriate to evaluate the NCAA under the construct of a political market in reference to the considerable public choice literature stemming from Buchanan and Tullock (1962). This line of analysis is not absent from Fleischer et al.'s economic characterization of the NCAA. But to date, only DeBrock and Hendricks (1996 and 1997) have considered the effect of the Association's voting methods on its organizational structure. The purpose of this paper is to extend the analysis of the NCAA's political markets by focusing on the events and actions leading to the 1997 reorganization. In the analysis of this paradigm shift particular attention will be given to transactions costs (Coase, 1937; Williamson, 1975) and property rights (Coase, 1960; Demsetz, 1967).

The paper proceeds as follows. The following section provides a background on the evolution of the organizational structure of the NCAA and provides the details of the new structure in contrast to the old. The third section discusses the relevant economic theory. Section four integrates economic theory with the forces driving the restructuring. Recent developments, implications, and suggested avenues for additional research conclude the paper.

NCAA ORGANIZATIONAL HISTORY

Fleischer et al. (1992) and others provide an ample history of the NCAA. In brief, the NCAA evolved from a public-good provider (the establishment of rules to reduce violence in football) to a cartel organization that assumed economic control of most college sports markets.[3] Although there is some overlap, the focus here is to trace the organizational changes following a history provided by Mott (1996).

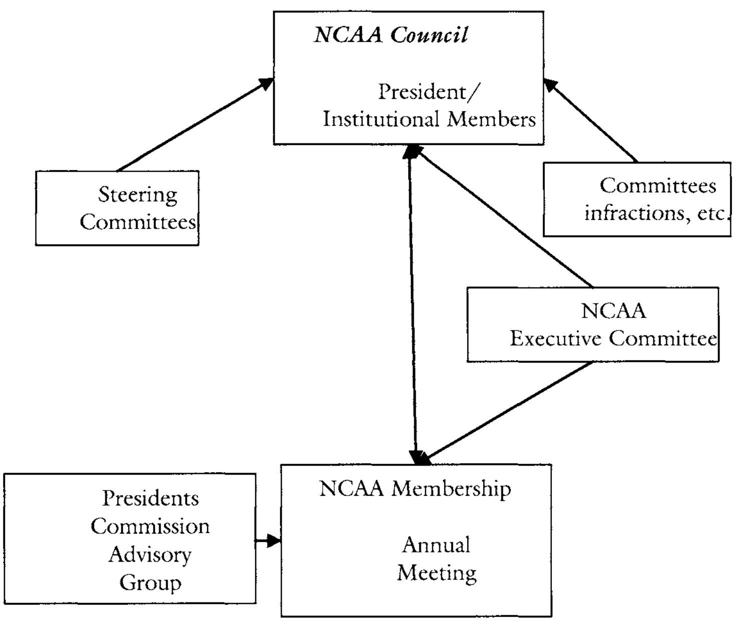
Representatives of universities and colleges founded the organization and held the first convention in 1906. A constitution was drafted and ratified by 38 original members. The organization convened annually, and rule changes and other legislation were determined by vote of the membership. Approval required a simple majority. The members also elected a slate of officers officially called the Executive Committee to preside over the organization. This method of governance remained largely unchanged until 1922.

By the early 1920s the membership of the rapidly growing Association exceeded 100. The NCAA had extended its scope of governance beyond football and included most men's intercollegiate athletic sports offered at the time. In 1922 the first NCAA-sponsored and -sanctioned national championships were held in track and field. With the Association's role in governing intercollegiate athletics increasing in both breadth and depth, a significant organizational change was implemented.

In 1922 the NCAA established the NCAA Council, which essentially came to act as a corporate "board of directors" (Fleischer et al., 1992, 71). The Council replaced the Executive Committee as the NCAA's policy-making body and was granted the authority to act on behalf of the Association between annual conventions. At the time it was established, it was deemed the 14-member Council comprise at least one representative from each of the NCAA's nine geographic districts, with the five other members to include the Association's elected officers. The Council's purpose was to recommend and promote policy in the organization's best interests. The Council's economic mandate grew to include interpretation of the NCAA constitution and bylaws as well as the arbitration of disputes in regard to rule violations. All legislation continued to require approval by a majority vote of the membership. This basic legislative structure remained in place until the 1997 restructuring, although the membership had grown to over 1,000, included women's sports, and had divided into three competitive divisions. An organizational chart of the NCAA before the 1997 restructuring is shown in Figure 1.

From its early days the NCAA has faced internal conflicts primarily based on the institutionally divergent levels of investment in intercollegiate athletics. In 1922 University of Michigan Athletic Director Fielding Yost presented a paper to the convention proposing that the Association be separated into divisions according to the "attitude toward athletics" (Mott, 1996, 10). The

Figure 1
NCAA Organizational Chart Before Restructuring



Source: Arthur A. Fleisher, Brian L. Goff, and Robert D. Tollison, *The National Collegiate Athletic Association: A Study in Cartel Behavior* (University of Chicago Press, 1992).

opposing sides in the legislative battles of the 1930s and 1940s were drawn largely—although not completely—along these lines. Despite these conflicts and concerns over "level playing fields" there was no separation of the Association based on level of competition until the 1950s. In 1957 the NCAA sponsored the first lower level or "College Division" men's basketball championship. Throughout the 1960s the NCAA added College Division championships in other sports. By the 1968–69 academic year the membership sponsored College Division championships for nearly all sponsored sports, and individual institutions were asked to choose the level where they wished to compete; 223 opted for the more competitive University Division while 386 chose the College Division.

Although it may have seemed logical to have the divisions separated for the purpose of policy formation as well, this did not occur. The membership continued to vote on legislation as a unified body. There was a fear that divided voting would splinter the membership. The Association instead instituted a policy of "conscience voting" where members were asked to abstain from voting if they had no interest in the legislation. There is speculation that conscience voting was not adhered to and this system encouraged the typical coalition strategy of logrolling (Mott, 1996, 11). The institutions with high athletic investments, which constituted a minority, were not satisfied with their lack of decision-making autonomy within the organization. This gave rise to changes in the 1970s that set the stage for restructure 20 years later.

In 1973 the NCAA voted to create a three-tier system still based on the level of competition. The new divisions were simply numbered I, II, and III. The least competitive, Division III, was reserved for institutions choosing a very low level of investment in athletics, and declined to award athletic grant-in-aid scholarships. At the same time it was agreed to assure a Division I majority on the 14-member Council. Bylaws were changed so that eight slots were reserved for Division I members. The remaining six slots were allocated to Divisions II and III with no stipulation as to the breakdown between the two divisions. The organization expanded to include steering committees for each division.[4] The steering committees' functions included recommending legislation appropriate to the division, but the Council retained ultimate authority and all legislation was still enacted by conference votes of the entire membership.

Institutions were given the freedom to choose their level of competition and 235 initially opted for Division I. The institutions with the greatest investments in football programs quickly showed signs of dissatisfaction with the composition of the highest division. These schools argued that they should vote separately in matters relating to "big-time" football. At issue was NCAA's restrictive television policy. Individual schools were allowed a maximum of two appearances on national television per year. The NCAA controlled all television rights, precluding individual members or conferences from negotiating independent contracts. In 1977 a group of high-investment programs, including all members of the Atlantic Coast, Big 8, Southwest, Southeastern conferences, and Notre Dame, formed an alliance called the College Football Association (CFA). The CFA desired more autonomy for its members and aggressively lobbied for organizational changes, actually threatening secession from the NCAA if concessions were not made. The two other major conferences, the Big 10 and Pac 10, did not join the CFA, limiting their cartel power.[5]

The NCAA divided Division I into two subdivisions in 1978 mainly in response to pressure from the CFA membership. The I-A and I-AA distinction divided schools into two groups based on strict criteria of institutional investment in football programs. This marked the establishment of a formal internal barrier to entry.[6]

The restructuring of Division I granted the football powers some additional autonomy but still did not allow them to vote on legislation independently. More importantly, the NCAA did not change its television policy. The Association had controlled television rights and negotiated a national contract since the early 1950s.[7] The revenues collected from the contract were reallocated to the membership. Those schools appearing in televised contests received greater shares, but the NCAA restricted both the total number of televised games and individual appearances. High investment football programs were left to profit independently of the NCAA only through gate revenue and their conference relationships with post-season bowl games.

Unsatisfied with the restrictive NCAA policy, the CFA negotiated an independent television package with the NBC network in 1980. The NCAA threatened expulsion of the CFA members not only for football, but also for all NCAA sanctioned sports. Rather than follow through on the contract, the CFA responded by filing an antitrust suit against the NCAA. The United States Supreme Court heard the case in 1984 *(NCAA v. Board of Regents of University of Oklahoma & University of Georgia Athletic Association)* and ruled against the NCAA. This opened the door for individual schools and conferences to negotiate their own television contracts. The CFA entered into national-network contracts on behalf of its members. The Big 10 and Pac 10 conferences, which had refused to join the CFA, nonetheless reaped the benefits of the antitrust victory and signed a lucrative joint national television contract (Zimbalist, 1999a, 101). Conferences and individual institutions also sold television rights regionally and to increasingly influential cable networks.

Despite the Association's considerable loss of control over football revenue there was little movement toward substantive organizational alteration at this time. Increased revenues generated from the men's Division I basketball tournament mitigated the NCAA's loss of revenue from the national television contract for football. Noteworthy at this time, however, was the creation of the Presidents Commission in 1984. The Commission's purpose was to facilitate more institutional control over athletic programs, and it was technically established to provide a system of checks and balances to the Council. Fleischer et al. (1992, 71) discount the importance of the role of the Commission, classifying it as simply an advisory group.

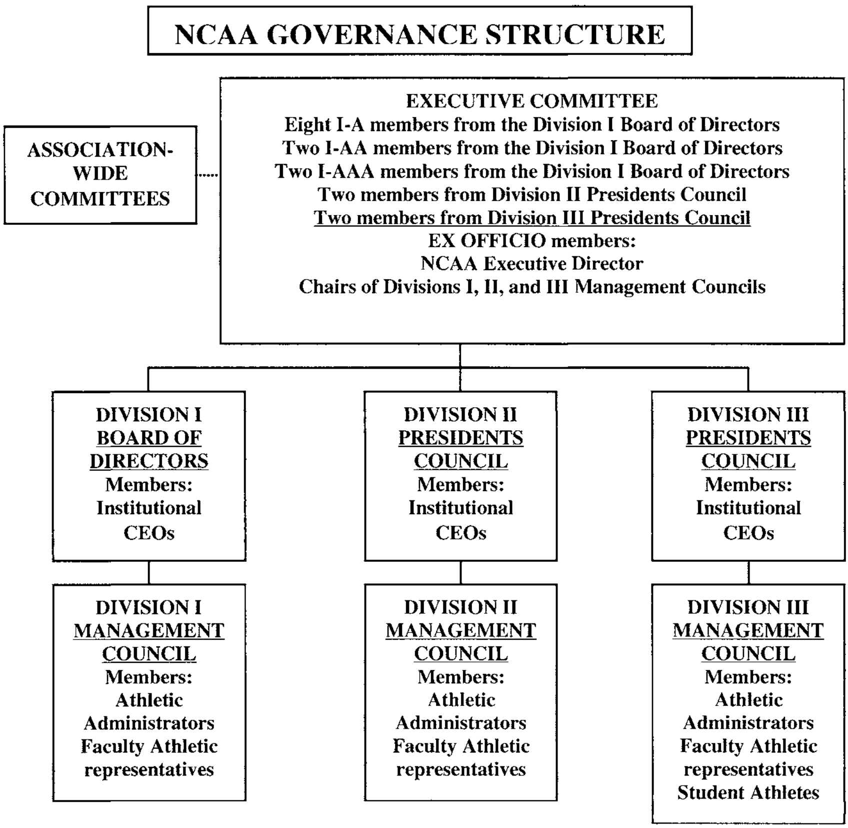
Despite the pressure for decision-making autonomy by the high-investment football conferences, the organizational structure remained intact for 10 more years. The Association voted to explore its organizational restructure at the 1994 Convention. A task force for each division was appointed to devise a restructuring plan in early 1995. A proposal outlining specific plans for restructure was presented in December of 1995. The membership approved the restructuring at the 1996 Convention and the new governance structure took effect on August 1, 1997.

Figure 2 shows the organizational chart of the new structure. As previously noted, the major change occurs in Division I. A representative legislative system based on conference membership replaced direct democracy. A 15-member Board of Directors composed entirely of institutional CEOs approves all legislation, and it is required that nine of the fifteen members represent Division 1-A institutions. Division I also replaced committees with four cabinets with specific responsibilities; these are: academic affairs, eligibility and compliance, business and finance, championships and competition, and strategic planning. The cabinets have either 26 or 34 members and each is required to have a majority of members from IA institutions, 14 and 18, respectively. All cabinets report to the 34-member Division I Management Council, which in turn reports to the Board. The Management Council contains athletics administrators and faculty athletics representatives and is empowered to make recommendations to the Board and handle responsibilities delegated to it. It is also structured so that the Division I-A Conferences always have a majority. No legislation is created in Division I by a vote of the membership. Division-wide voting may be done only through an override vote process that requires a written request from at least 30 Division I members. In 1999 an expansion of the Board of Directors to 18 with 11 members representing 1A was approved. An increase in Management Council membership to 49 was also improved. In each case Division I-A conference members will retain their majorities; however, the proportion of members representing the six so-called power conferences is slightly reduced and Divisions I-A and I-AAA gain.[8]

Divisions II and III have nearly identical structures under the new system. Each has a Management Council and presidential board that are similar to the ones in Division I; however, the presidential body is known as the Presidents Council rather than the Board of Directors. Legislation in both divisions is considered through the traditional one-school, one-vote process at the annual Convention.

The entire Association remains under one umbrella. The Executive Committee, composed of institutional chief executive officers, oversees

Figure 2
Current NCAA Governance Structure



Source: The NCAA Online, Governance Structure http://www.ncaa.org/databases/governancestructure/.

Association-wide issues and is charged with ensuring that each division operates consistently with the basic purposes, fundamental policies, and general principles of the Association.[9] The new role of the Executive Committee is not discernable from the old, as it still does not play an active role in policy formation.

POLITICAL MARKETS, TRANSACTIONS COSTS, PROPERTY RIGHTS, AND RESTRUCTURING

The NCAA is a voluntary organization formed for the purpose of providing common rules and organizing athletic contests among its members.

The organization exists because the collective action benefits its individual members. Given this, it is entirely appropriate to consider the restructured governance under the theoretical construct of the political market. Buchanan and Tullock (1962) assert that collective decisions are determined by an evaluation of the relative weights of two types of costs. The first are the decision-making costs, which include the cost of organizing the group, bargaining, implementing decision-making rules, etc. The second group represents the external costs (net of external benefits) of collective action, which include the costs of inefficient reallocations. This type of externality arises because a majority rule system tends to reward effective coalitions with differentially larger shares of the benefits. Coalitions that form for the specific purpose of obtaining differentially larger shares are described as engaging in what economists call "rent seeking." Buchanan and Tullock claim that decision-making costs are higher under a system of direct democracy but the external costs imposed by effective rent seeking are higher in a representative legislative system, and increasingly so as the degree of representation is diminished. For example, a dictator has minimal decision-making costs but theoretically will impose the highest external cost on other group members. The choice of a representative system versus direct democracy is simply an evaluation of the respective costs. Buchanan and Tullock imply that the representative governance greatly reduces the decision-making costs of direct democracy, and these costs are prohibitive unless the group is small or there are very few issues that must be considered. They do not, however, specifically model the dynamic by which a group that employs direct democracy moves to representative democracy.

Though not directly parallel, the theory of collective action has a number of similarities to the theory of the firm developed by Coase (1937) extended with the transactions-cost economics introduced by Williamson (1975). No claim is made that this observation is unique; there exists an extensive body of public choice literature that invokes transactions costs and principal-agent analysis. It is simply conjectured that it is applicable to this situation.

The two types of categories of costs that determine organizational structure in each theory are directly analogous. Coase's theory provides a more distinct description of the circumstances that motivate a change in decision–making structure. The choice is really nothing more than basic benefit-cost analysis. The optimal firm structure occurs where the marginal cost of learning and haggling over the terms of trade (Buchanan and Tullock's decision-making costs) are equated with the cost of errors associated with concentrating decision-making authority (Buchanan and Tullock's external costs). Changes in the cost structure may tip the balance and motivate an organization to alter organizational structure. Williamson (1975) proposes that informational limitations and asymmetries are also determinants of these "transactions costs" and influence organizational structure.