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The Professional Football Industry in Canada: Economic and Policy Issues

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INTRODUCTION

The major professional sports industry in Canada spans four sports—hockey, baseball, basketball, and (North American) football. In the former three, there are no independent Canadian leagues. As of 2002, all Canadian-based franchises in these sports were simply members of the major U.S.-based leagues. Canada has two Major League Baseball (MLB) franchises, one National Basketball Association (NBA) franchise, and six National Hockey League (NHL) franchises. In football, however, the situation is different in that the U.S.-based National Football League (NFL) has never had a franchise in Canada. Instead, the independent Canadian Football League (CFL) has long operated. Although the CFL has a history that goes back over 100 years, the league has often been overshadowed on the North American sports landscape by the more powerful U.S.-based leagues.

One result of this overshadowing is that the sports economics literature contains almost no analysis of the CFL.[1] This absence of research is unfortunate, since the economics of the CFL are somewhat peculiar and can provide numerous insights for sports economists. In this regard, the present chapter attempts to highlight two particular issues that differentiate the CFL from the broader North American professional sports industry. First, the chapter explores the reasons for the CFL's economic decline over the past two decades—a decline that occurred during a time period when other North American professional sports leagues experienced unprecedented booms. The

chapter argues that the relative decline of the CFL can be traced to its gradual loss of monopoly power in the sports market. Second, the chapter examines the unique (at least in North American sports) quota system that the CFL employs in its labor market. This system ensures that Canadian players are guaranteed a minimum number of spots on each team's roster. The chapter argues that the quota system has impacts not only on player salaries and team payrolls, but may also act as a de facto quota on the number of black players in the league.

A BRIEF BACKGROUND ON THE CFL'S ECONOMICS

The game of Canadian football can be traced back to the late nineteenth century. The game evolved from English rugby, and gradually transformed itself into a distinct game. By the 1930s, professionalism in the sport was becoming more common, and teams began importing professional players from the United States. Two professional leagues emerged—one in eastern Canada and another in western Canada. These two leagues were separate entities and relatively independent of one another, but they were both members of the Canadian Rugby Union (CRU), the predecessor of the CFL. In 1958, the two leagues agreed to formally integrate, forming the CFL, with four teams in the Eastern Conference and five teams in the Western Conference.

From 1954 to 1986, the CFL (and its predecessor, the CRU) operated with the same nine franchises. This was a period of remarkable franchise stability in the CFL—there were no expansions, no franchise failures, nor any franchise relocations. During the 1980s, however, the CFL began a gradual decline. In 1987, the Montreal franchise folded. In 1993, the CFL, desperate for a cash injection to survive, began a three-year experiment of granting expansion franchises to U.S. cities. By 1995, the CFL operated as a thirteen-team league, with eight franchises in Canada and five in the United States. At the end of the 1995 season, four of the five U.S. franchises folded, and the only remaining U.S. franchise—in Baltimore—was transferred to Montreal, making the CFL again an exclusively Canadian league. In 1997, the Ottawa franchise folded, but Ottawa was readmitted to the league in 2002 as an expansion franchise. Thus, by 2002, the CFL had come full circle in that it was again a nine-team league, with the nine franchises located in exactly the same cities as they had been in 1954.

This franchise instability over the past two decades is a reflection of the general decline in the economic fortunes of the league. This decline can be measured along numerous dimensions. For example, Table 1 illustrates the long-term decline in attendance. Even though attendance rose significantly from 1967 to 1977, these gains were almost completely dissipated over the subsequent twenty years. Between 1977 and 1997, average per-game attendance in the CFL decreased 32%. The decrease in fan interest in Vancouver and Toronto—two of Canada's three largest cities—has been a particular problem for the league. In 1968, these two franchises were flagships of the league—average per-game attendance in Vancouver was 134% of the CFL average, and in Toronto, average per-game attendance was 128% of the CFL average. Contrast this with 2001, when Vancouver and Toronto's attendance had fallen to only 82% and 65%, respectively, of the league average.[2] This long-term decrease in fan support in Vancouver and Toronto has had impacts beyond just these franchises, since the value of national TV contracts is heavily dependent upon viewership in these major population areas.

Table 1
Change in Average Per-Game Attendance

1967	1972	1977	1982	1987	1992	1997	2001
20,082	23,300	31,307	29,377	25,990	25,367	21,295	24,971

Source: Derived from Canadian Football League, *Facts, Figures & Records* (various editions).

The CFL's revenue problems have correspondingly put strong downward pressure on player salaries, as illustrated in Table 2. Over the past two decades, real CFL salaries have decreased substantially, both in absolute terms and relative to NFL salaries. During the 1970s, the relative salary parity between the CFL and the NFL even allowed the CFL to occasionally sign high profile American players. For example, in 1972, Heisman Trophy winner Johnny Rodgers joined Montreal for $100,000 per season. In 1979, the first overall selection in the NFL draft—Tom Cousineau from Ohio State—spurned an offer by the NFL's Buffalo Bills to sign with Montreal. Also during that era, Montreal signed Vince Ferragamo—a star NFL quarterback who had just led the Los Angeles Rams to a 1980 Super Bowl appearance—for $400,000 per season. However, as the salary disparities between the CFL and NFL became greater, such high profile signings became increasingly rare.

Over the past twenty years, most individual CFL franchises have faced precarious financial situations. Although only two (Canadian-based)

Table 2
Estimated Average Player Salaries

	1975	1985	1995
CFL Salaries (000, 1995 Cdn dollars)	73	86	50
CFL Salaries (000, 1995 US dollars)	72	63	36
CFL Salaries (US dollars) as Approximate % of NFL Salaries	67 %	29 %	5 %

franchises actually folded, most of the other privately owned teams saw rapid turnover in ownership, with their survival depending on the existence of a constant stream of investors willing to intervene to rescue the team, hoping that it would be the one to turn the team around. The community-owned franchises have also faced financial hardships and have often had to rally community support to avoid the prospect of bankruptcy.

During the late 1990s, the CFL did begin to regain some measure of financial stability. The league benefited from the franchise fees extracted from the American expansion teams. Also, the NFL provided the CFL with a $4 million loan in 1997, further lessening the immediate financial crisis the league was facing.[3] Perhaps most important, fan interest increased, with both attendance and TV ratings showing significant improvements. This upward trend has continued into the early part of the twenty-first century, but it is still too early to determine whether it signals a fundamental shift in the long-term fortunes of the league or is simply a cyclical phenomenon that cannot be sustained.

ANALYZING THE CFL'S DECLINE

The decline of the CFL over the past two decades, a time when the professional sports industry in North America was booming, may seem to be a paradox. In essence, however, the CFL's decline may have been *caused* by the boom in the rest of the industry. Prior to the 1980s, the CFL was relatively sheltered from competition and thus possessed significant monopoly power. It is the assertion of this section that the decline of the CFL can be traced directly to the erosion of this monopoly power. Three factors are hypothesized to have been particularly important: (1) increased competition in the output market, (2) increased competition in the input market, and (3) a loss of political influence for the league.

Competition in the Output Market

Part of the CFL's decline can be traced to an increase in the availability of substitute products in the professional sports market. In 1970, for example, only two of the nine CFL franchises faced competition from an NHL franchise in the same city. By 1980, six CFL franchises faced such direct competition from the NHL. Baseball also began to present increased direct competition for the CFL, with Montreal entering the Major Leagues in 1969 and Toronto entering in 1977. In addition, other CFL cities such as Vancouver, Calgary, and Edmonton all received AAA baseball franchises during that era.[4]

The widespread installation of cable TV in Canadian homes during the 1970s also presented a competitive threat to the CFL. Cable TV allowed

Canadians to access the major U.S. networks, providing viewers with a wide range of professional and college sports to which they previously did not have access. In essence, cable TV resulted in the CFL losing its captive market. For some Canadians, increased access to American sports, particularly the NFL, diminished their interest in the CFL.

Exacerbating the problem was that the NFL was beginning to emerge as the dominant league in all of North American team sports. Its enormous growth in popularity further widened the gaps between the CFL and the NFL. In some ways, the CFL became unfashionable. There was the growing perception among some Canadians that the CFL was simply a "minor" league whose extinction was near. Thus, in a sense, the NFL began to emerge as a competitor for the CFL. Even though the NFL had no franchises in Canada, it was beginning to actively compete with the CFL for the interests of Canadian fans.

Competition in the Input Market

Throughout its history, the CFL has always relied heavily on recruiting American players. In general, however, it has not attempted to compete directly with the NFL for such players. Instead, the CFL found a niche in the market, and focused on recruiting those Americans who were unable to earn NFL positions. For many American players, one of the attractions of the CFL, despite its relatively low salaries, has always been that it allows them to continue their playing careers, with the ultimate hope of rejoining the NFL.[5]

For the CFL, it has been U.S. start-up leagues that have posed the most serious threats in input markets. These leagues have included the American Football League of the early 1960s, the World Football League (WFL) of the mid-1970s, the United States Football League (USFL) of the mid-1980s, and the World League of American Football (WLAF) of the early 1990s. These leagues have tended to employ the same type of second-tier (i.e., non-NFL) players that the CFL employs. Thus, the presence of these leagues not only increases CFL salaries, but also lowers the league's overall talent pool.

Particularly damaging to the CFL was the emergence of the USFL in 1983. Not only did the USFL emerge at a time when the CFL was facing competitive threats in the output market (as discussed earlier), the USFL was particularly successful in luring many of the CFL's top players, coaches, and managerial personnel to the new league. In fact, if one examines CFL attendance and TV revenue figures around the time of the USFL's formation, the influence is clear. The CFL experienced a 13% drop in attendance between 1983—the first year of the USFL's existence—and 1985, the USFL's last year.[6] This seemed to be the beginning of a trend, as attendance continued to fall throughout the remainder of the 1980s. Similarly, TV revenues

per team fell from over $1.2 million in 1983 to only about $325,000 by 1987 (Barnes, 1996).

Loss of Political Influence

Throughout the 1960s and 1970s, the CFL became increasingly concerned about a U.S.-based league (either the NFL or a start-up league) establishing a franchise in Canada. During this era, the CFL actively lobbied the federal government for protection to ensure no rival leagues entered Canada. The CFL presented the issue as one of "national unity." The CFL was the only exclusively Canadian professional sports league in Canada. Its championship, the Grey Cup game, pitted the winners of the Western and Eastern Conferences and captured the competitive rivalries between the two different parts of the country. In addition, the CFL's quota system guaranteed a certain number of roster spots for players of Canadian origin. These arguments by the CFL were consistent with a political strategy that had long been effective in Canada—justifying protection by playing to fears of U.S. domination of Canada.

The issue came to a dramatic head in 1974, when the fledgling U.S.-based WFL proposed to locate a franchise in Toronto. CFL officials viewed such a development as not only a threat to the viability of the Toronto Argonauts, but also (because of revenue sharing) a threat to the entire league. The federal government of the day, led by Prime Minister Pierre Trudeau of the Liberal Party, had a strong nationalistic orientation and believed that Canadian business and culture were being increasingly dominated by American interests. Thus, in April 1974, just months before the WFL was to begin its first season, the government introduced a bill into the House of Commons that would have prohibited any foreign football league from operating in Canada. The bill's preamble stated that the CFL had "developed for itself a unique national institution contributing to the strengthening of the bonds of nationhood" (see Barnes, 1983). Shortly after the bill was introduced, a federal election was called, and the bill never officially became law. The matter became moot when the owner of the WFL's Toronto franchise announced that he was moving his franchise to Memphis.

During the 1980s, Canada's political climate changed considerably. The Progressive Conservative Party—led by Prime Minister Brian Mulroney—came to power in 1983 and subsequently negotiated a free trade agreement with the United States. Since the Mulroney government's political agenda was to remove trade and investment barriers with the United States, the CFL's protectionist desires no longer met with much sympathy. As Barnes (1996) notes, perhaps indicative of the CFL's decline in importance, both to governments and fans, was that no legislative bill similar to that of 1974 was put forward when the WLAF granted a franchise to Montreal in 1990.

THE CFL'S LABOR MARKET QUOTAS

The Basics of the Quota

Perhaps the feature that most differentiates the CFL from the other major North American sports leagues is that the CFL employs a quota system in its labor market.[7] This quota ensures that a minimum number of roster spots must go to Canadian-born players. Without the quota system, it is presumed that few, if any, Canadian players would be employed by CFL teams. Relative to Canada, the United States produces a large number of talented football players, hence there has long been a desire by CFL teams to recruit Americans. To counter these natural market forces, the CFL has for many years maintained the quota system. The first use of the quota was in 1936, when it limited teams to employing a maximum of five Americans (Barnes, 1996). Since that time, there have been successive increases to this limit, and, beginning in 1996, teams have been allowed to employ seventeen Americans (excluding three quarterbacks, which can be either American or Canadian) on their thirty-nine-man roster; the remaining nineteen players must be Canadians.[8] Given that each team has twenty-four starting players (twelve on offence, twelve on defense), and given that one of the Americans must be a special teams player, this ensures that at least seven Canadians are starters.

The remainder of this section analyzes the economic rationales for the quota and examines some of its impacts.

Modeling the Quota Decision

Officially, the CFL justifies the quota system on the grounds that it ensures a "Canadian-presence" in the game.[9] However, this quota system is presumably a profit-maximizing choice by the league. The quota is essentially a cartel-like attempt to limit competition among the CFL's member teams. Since Americans are generally superior players to Canadians, and hence are paid more,[10] a quota that limits the number of American players on a team should serve to reduce team payrolls. In the absence of the quota, individual teams acting alone may have a profit incentive to increase the number of Americans on their team, perhaps to the point where all players on the team were Americans. Since all teams would face the same basic incentive structure, no team would gain any real competitive advantage over any other, but all teams would see their payrolls rise. Thus, the CFL's quota system may be acting to maximize collective profits by ensuring that teams do not "excessively" compete on the basis of player quality.

However, the quota may also have negative effects on CFL teams, in that it artificially lowers the absolute quality of play in the league. To the extent that absolute quality of play is important for fan interest, the quota will

reduce overall league revenues.[11] Thus, from the CFL's collective perspective, the optimal level of the quota is found by balancing two opposing factors, payroll increases and revenue increases: increasing the quota increases team payrolls, but, to the extent it increases fan interest due to an increase in the absolute quality of play, it may also increase team revenues.

Team-Level Choices

Given the existence of league-imposed quotas, individual teams will allocate their American players to their most profitable uses. For example, Americans will presumably always be used in starting positions, and never as backups. Teams, however, will always have to employ some Canadians in starting positions, since the number of Americans allowed is less than the number of starting positions on a team. Thus, teams are faced with an allocation decision: How should the American players be distributed across positions to maximize team profits?[12] Alternatively, the question can be framed this way: Given that Canadians must fill seven starting positions, at which positions should these Canadians be used? It is hypothesized that the decision can be modeled as follows:

$$A = f(D, I) \qquad (1)$$

where:

A = the probability of using an American, as opposed to a Canadian, in a given position
D = the average difference in talent at the position between American and Canadian players
I = the impact that the position has on overall team success/revenues.

The variable D reflects the fact that the average talent difference between Americans and Canadians will vary from position to position. In general, one could hypothesize that the talent difference is greater at the so-called "skill" positions—positions such as quarterback, running back, receiver, and defensive back. Thus, all else being equal, one would expect Americans to fill a disproportionate number of these positions. Conversely, positions that rely more on strength and technique, rather than on pure athletic ability—positions such as offensive lineman—are positions for which talent differences between Canadians and Americans should be less.

For the variable I, it is hypothesized that Americans will tend to fill those positions that have greater impacts on team success/revenues. As with the variable D, this would seem to indicate that it is the skill positions that are the most likely to be filled by Americans.[13] Not only are these, arguably, the most crucial to team success, they are the highest profile, and the most identifiable by the fans and media.

Table 3
Percentage of Games Started by Americans, by Position, 1995

Quarterbacks	100 %
Running Backs	58 %
Receivers	67 %
Offensive Line	2 %
Defensive Line/Linebackers	73 %
Defensive Backs	89 %
Kickers	0 %

Source: Derived from Canadian Football League, *Facts, Figures & Records* (various editions).

Table 3 examines the distribution, by position, of Americans on Canadian-based teams during the 1995 season.

The data in Table 3 support the hypothesis in that Americans disproportionately occupy certain positions. At one extreme, there is complete domination by Americans in the quarterback position. Americans also dominate the defensive line/linebacker positions and the defensive back positions. At the other extreme, offensive linemen are almost exclusively Canadian.

Salary Effects

The quota system creates an artificial demand for Canadians, not only to fill all backup positions, but also to fill seven starting positions. However, the supply conditions for Canadian players are very different from those for American players. Given the large number of quality football players in the United States, CFL teams face a highly elastic supply of U.S. players. Most American players (excluding the star players) are relatively easily replaced,[14] since there are always a large number of other American players, of almost equal talent, simply waiting for their opportunity.

Conversely, the talent pool of Canadian players is much smaller. For any given level of talent, not only are there fewer Canadians than Americans, but the talent gap between any particular Canadian player and the next best Canadian player is often much greater than is the corresponding gap for American players. In other words, it is much more difficult (in terms of a talent drop-off) for a team to replace any given Canadian player with another Canadian player than it is for the team to replace any given American player (of equal talent to the Canadian) with another American player.

These market conditions should result, for a given level of talent, in Canadian players receiving a salary premium over their American counterparts.[15] Analyzing the 1995[16] salaries of veteran[17] CFL receivers (on Canadian-

based teams) tests this hypothesis. The receiving position is chosen because there is good mix of Canadian and Americans at that position and because performance is relatively easily measured at that position. The model's specification and the regression results are summarized below.

$$\ln(S) = 10.10 + .001954(GP) + .16033(RPG) + .010757(YPC) + .22438(C) \quad (2)$$
$$(3.22) \qquad (7.65) \qquad (1.24) \qquad (3.61)$$

N = 35 (23 Canadians, and 12 Americans)
R^2 = .83

where:

S = the player's 1995 salary
GP = the player's career games played in the CFL
RPG = the player's career receptions per game in the CFL
YPC = the player's average career yards per catch in the CFL
C = 1 if the player is Canadian, and 0 if the player is American.

The variable GP is a measure of the player's CFL experience, and both RPG and YPC are intended to capture productivity.

The results support the hypothesis, in that Canadian receivers do appear to receive a premium.[18] For a given level of experience and productivity, Canadian players earned 22% more than their American counterparts. The artificial demand that the quota creates for Canadian players, combined with the relatively inelastic supply of Canadian players, would seem to force teams to pay a premium for these players. One must still use caution in interpreting the results, since the sample size is, by necessity, small. However, some confidence is gained by the R^2 being relatively high. In addition, the control variables are all of the expected sign, with two of the three control variables having statistically significant coefficients.

Racial Effects

The CFL's quota on Americans dates back to the 1930s. At that time, all American players entering the league were white. Gradually, however, as African Americans were given more opportunities to participate in high level sports in the United States, the number of African Americans entering the CFL began to increase.

With this increase in predominance of African American athletes in the United States, and with blacks comprising a much smaller proportion of the population in Canada than in the United States, the CFL's quota on Americans has become a de facto quota on the number of black players in the league. Table 4 provides an analysis of the racial composition of American versus Canadian players for the 1993 season.

Table 4
Racial Composition of Canadian and American Players, 1993

Americans (N = 201)		Canadians (N = 204)	
Black	White	Black	White
86 %	14 %	20%	80%

Source: Derived from Canadian Football League, *Facts, Figures & Records* (various editions).

Although it is not necessarily the intent of the quota rule to act as a racial barrier, it is clear from Table 4 that the effect of the rule has been to limit the number of black players in the league.

SUMMARY

Because the economics of the CFL are somewhat different from those of other North American sports leagues, the league provides sports economists with some unique research opportunities. This chapter has attempted to highlight two aspects of the CFL that differentiate it from the broader North American professional sports industry. The chapter examines the CFL's economic decline over the past two decades—a decline that occurred during a time period when other North American professional sports leagues experienced unprecedented booms—and argues that the decline can be traced to the CFL's gradual loss of monopoly power in the sports market. The chapter also examines the quota system that the CFL employs in its labor market and finds that this system has impacts on a wide variety of areas—on player salaries, on positional segregation, and on the racial composition of teams.

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NOTES

1. Most Canadian sports economists have focused on the sport of hockey. A particularly popular research question has been whether French Canadians suffer from discrimination in the National Hockey League (see, for example, Lavoie, Grenier, and Coulombe, 1987; Longley, 1995).

2. Data from the 2001 season indicate that, for the league as a whole, the correlation coefficient between attendance and city size is strongly negative, at –0.56.

3. The agreement between the NFL and the CFL allows NFL teams to sign CFL players who are entering their option years. In exchange for this signing privilege, the NFL provided the CFL with a $4 million loan to help the league survive its financial distress. From the NFL's perspective, the reasons for this agreement would seem to be twofold. First, it allows the NFL earlier access to some of the best CFL players. Second, it is hypothesized that the NFL has an interest in seeing the CFL survive, since the existence of the CFL may lessen the likelihood of a rival (to the NFL) U.S.-based league forming. Such a rival league would have to compete not only with the NFL for players, but would have to compete with the CFL. The CFL presents no real competition for the NFL, but it does employ a group of second-tier players who would otherwise be attractive to a start-up league.

4. More recently, the CFL has faced direct competition from the NBA, with both Toronto and Vancouver receiving expansion franchises in 1996 (Vancouver's franchise has since moved to Memphis, Tennessee).

5. For example, star NFL quarterbacks such as Joe Kapp, Joe Theismann, Warren Moon, and, more recently, Jeff Garcia all began their professional careers in the CFL. Each year NFL teams also sign many lesser-known CFL players.

6. As a further example of the effects of the USFL, between 1981 and 1985, CFL players' salaries, as a percentage of gross gate revenues, increased from 58% to 75% (Cosentino, 1995).

7. It should be noted that many professional sports leagues outside of North America do employ quotas. For example, many European soccer leagues restrict the number of non–European Union players per team.

8. The CFL does not actually use the terms "Americans" and "Canadians." Instead, to avoid any notion of discriminating based on national origin, the terms "imports" and "non-imports" are used. Non-imports are defined as any player who has never received football training outside of Canada or who was physically resident in Canada for an aggregate period of five years prior to attaining the age of fifteen years.

9. During the 1980s, a complaint was filed with the Canadian Human Rights Commission on behalf of American players released from CFL rosters. The complaint alleged that the CFL's quota rule was discriminatory. The commission rejected the complaint on the grounds that the quota was necessary to help Canadian football players overcome "disadvantages in preparation and opportunity" (Barnes, 1983).

10. For example, in 1995, rookie (i.e., no previous CFL experience) Canadian receivers were paid an average of $31,000 per season, whereas rookie American receivers were paid an average of $51,000 per season.

11. These revenue-decreasing effects of the quota will be mitigated somewhat if Canadian fans, all else being equal, prefer to watch "homegrown" players.

12. Ball (1976) uses a sociological model to investigate positional "stacking" of Americans in the CFL.

13. It is assumed here that the marginal revenue from using Americans in skill positions rather than other positions is greater than the corresponding increases in payroll. Many American skill position players have limited bargaining power, given both the highly elastic supply of such players, and given the CFL's tight salary cap policies.

14. In fact, it is not unusual in the CFL for an American player to be a starter one week and to be released and off the roster the following week.

15. The market in the CFL for veteran players is relatively competitive. Since 1983, all CFL players playing out their options have been unrestricted free agents and can sign with any CFL team. The CFL was the first North American sports league to have unrestricted (i.e., without compensation) free agency.

16. The 1995 season was used out of conservatis; 1995 was the third and final year of the CFL's American expansion. U.S.-based CFL teams, that were not bound by the quota, employed only American players and signed many American free agents away from Canadian-based CFL teams. Thus, one would expect that the salaries of American players (on Canadian-based teams) would be higher than normal during this season.

17. For the purposes of the analysis, veterans are defined as those players who had played at least eighteen CFL games (the equivalent of one season) prior to the 1995 season.

18. Because most (but not all) Canadian receivers are white and most (but not all) American receivers are black, it is conceivable that the variable C is picking up the player's race, rather than his national origin. To test for this possibility, the variable C was replaced with the variable W, where W is a dummy variable equaling one if the player is white, and zero if the player is black. The regression was rerun, and the variable W was found not to be statistically significant.

Barnes

Sports of the Com in Canada.

1950 1996.