Stadia Mania: The Business, Civic And Legal Issues Of New Stadium Construction – Part I

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The New Economics of Sports And The Boom Of New Sports Facilities

When the National Hockey League's ("NHL's") New Jersey Devils took the ice in their state-of-the-art $365 million Prudential Center in downtown Newark, New Jersey in October 2007, they became the sixty-fifth and most recent franchise in the United States' four "major" professional sports (*i.e*., football, baseball, basketball, and hockey) to open a new or substantially renovated facility since 1996. At least thirteen other teams have begun construction on or announced plans to build their own new facilities that are scheduled to open by 2012. While new stadia have been and continue to be introduced in markets throughout the United States, this "stadium boom" is particularly evident in the New York metropolitan area, where in addition to the Prudential Center, major league franchises have recently undertaken no fewer than five significant development projects: next April both the Yankees and Mets are scheduled to begin play in ultramodern, yet classically-inspired new stadia; in 2010 the soon-to-be Brooklyn Nets plan to open their Frank Gehry-designed Barclays Center, the anchor of the $3.5 billion Atlantic Yards development project; the Red Bulls of Major League Soccer ("MLS") have broken ground on a 25,000 seat soccer-specific stadium in Harrison, New Jersey; and the NFL's Jets and Giants have jointly begun work on a new $1.3 billion New Jersey stadium that will feature as its centerpiece a 40 x 400 feet video "frieze" of panels visible through an eight-level louvered exterior.

Several key factors have driven the recent spate of professional sports facility construction. Most importantly, player salaries and other costs continue to rise exponentially. This economic reality has fueled franchise owners' pursuit of new buildings that – with their modern fan amenities, licensing and sponsorship opportunities, and luxury suites and other premium seating – provide substantial additional revenue streams frequently absent from older facilities. Owners claim that these revenue sources are necessary for them to compete and survive economically in today's sports business environment. Furthermore, while some observers remain dubious, owners and other supporters of these projects have in many cases successfully convinced government

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officials, potential investors, and key community leaders that new stadia – particularly those built in urban centers – generate additional economic activity, create new jobs, and encourage commercial and residential development in the surrounding area.[1] Owners have also skillfully leveraged many cities' desire to have professional sports teams – and to enjoy the perceived related prestige, prominence, and enhanced reputation – to obtain "sweetheart" stadia deals by threatening to relocate, or, in some cases, in fact departing one market for another city offering a better stadium arrangement.

The process of securing approval and funding for these stadium projects, as well as the acquisition of the necessary land, management of the construction itself, and maximization of revenue from the new facilities raise myriad economic, political, and legal issues. In part one of this article, we will briefly discuss two of the most prominent of these: (1) public financing of new stadia and (2) the use of eminent domain to acquire all or part of the proposed stadium site at a lower price than might otherwise be paid in a free-market transaction. Part two of this article, to be published in the next issue of *The Metropolitan Corporate Counsel,* will address two strategies available to franchise owners seeking to capitalize on the financial opportunities that new stadia offer: the sale of naming rights to new facilities and the introduction of suites and other high-end seating targeted to new and existing corporate clientele.

Facility Financing: A Public-Private Partnership

Notwithstanding the significant expansion in the number of major league sports franchises over the past two decades, demand for professional teams in metropolitan areas continues to exceed the supply.[2] Due to this relative scarcity, a fierce bidding war continuously rages among cities to secure or retain a professional franchise.[3] Frequently, teams are enticed to move or remain in a particular city through large public subsidies, such as extravagant new stadia built at the taxpayers' expense and leased at low or no rent; tax holidays; and generous concession, parking, and luxury box rights.[4] Indeed, as a final inducement, many cities pay huge "signing bonuses" to the teams in the form of direct payments.

For example, the proposed financing plan for the Mets' new stadium included the following terms, many of which are common in new stadium and arena deals:

(1) The project will be subsidized by granting the Mets access to tax exempt bond financing, which will save the team approximately $105 million over the next forty years.[5]

(2) New York City will invest $105 million for infrastructure and capital improvements, including site preparation, demolition of Shea Stadium, and the paving of parking lots. Like most public projects, the city will raise this money by issuing bonds and paying the principal and interest with general city revenues.

(3) The State of New York will contribute $70 million for infrastructure.

(4) The new stadium will be exempt from the city's property tax.

(5) The stadium will be exempt from city, state, and Metropolitan Transportation Authority sales taxes on purchases of construction material, fixtures, and equipment.

(6) The city will forgo a portion of the stadium's parking revenue.

(7) The Mets will receive increased rent credits.

(8) The city and the state will both make direct "capital replacement" payments into a reserve fund for the stadium.

(9) The city has granted the Mets a mortgage-recording tax exemption.

(10)Finally, the Mets will pay no rent for the use of the new stadium, although the team will pay for its maintenance. Given the dilapidated status of the current stadium and the obligation of the city to pay for its upkeep, the city projects that it will save $31 million under this new arrangement.[6]

In total, the direct subsidies, exemptions, and bond financing will save the Mets approximately $276 million, while costing New York City $155 million in lost revenue and the State of New York $89 million.[7] The Yankees received a very similar financial package from the city and the state, with the team receiving $276 million in benefits over a thirty-year period, at a cost to the city and state of $170 million and $85 million, respectively.[8]

This Land is My Land; This Land Was Your Land: Eminent Domain

In addition to the various incentives noted above, the government's power of "eminent domain" is a tool often used by the public-private partnerships formed to develop new stadia and arenas. That power – if successfully exercised – usually involves a government condemnation of privately owned land in order to allow that land to be developed for a "public use," so long as the private owner receives "just compensation" from the government.[9] At a minimum, the exercise of the power of eminent domain allows stadium construction to occur on privately-owned land that would otherwise likely be unavailable for development for such a project. Moreover, eminent domain can significantly reduce the project costs borne by the team by allowing developers to secure necessary land at a lower price than might otherwise be paid on the open market.[10]

Perhaps the most famous example of a government's successfully exercising this power for the benefit of a sports franchise occurred in 1957 when the City of Los Angeles condemned 300 acres of prime real estate in Chavez Ravine in order to lure the Brooklyn Dodgers out of New York. The most recent example of the use of eminent domain to benefit a New York metropolitan sports team[11] involves the New Jersey Nets, who are currently embroiled in a bitter contest with Brooklyn residents related to the team's efforts to build the Barclays Center. The Nets case provides a good example of how courts analyze – or at least should analyze – a government taking related to the construction of a sports arena.

Although there are multiple litigations that relate to the Nets' project, it is the case now on appeal to the United States Court of Appeals for the Second Circuit that most squarely addresses the government's eminent domain power.[12] In the trial court, United States District Judge Nicholas G. Garaufis dismissed the challenge brought by plaintiffs – all of whom own or rent land in the area condemned by the government – finding that the project met the public use requirement. In reaching his decision, Judge Garaufis noted that, under the relevant precedent, "a taking fails the public use requirement if and only if the uses offered to justify it are 'palpably without reasonable foundation,". . . such as if (1) the 'sole purpose' of the taking is to transfer property to a private party."[13] Applying that standard to the proposed Atlantic Yards development, the court found that plaintiffs' challenge failed because their complaints "when examined carefully, concern[] only the measure of a public benefit – as opposed to its existence."[14] And on this point, the judge stressed – relative to the Nets and the Barclays Center in particular – that plaintiffs failed to "allege that having a professional team in Brooklyn is not in itself a benefit to the public."[15] Finally, the Court rejected plaintiffs' notion that the government's offered public uses are "mere pretexts" for a desire to "bestow a private benefit" on the development corporation, noting that plaintiffs' allegations were implausible given their concession that the "[p]roject will create large quantities of housing and office space, as well as a sports arena, in an area that is mostly blighted."[16] In sum, the Court dismissed plaintiffs' challenge because of the project's acknowledged benefits to the public. Other public-private partnerships contemplating development of a new stadium should take heed of the benefits discussed in Judge Garaufis's decision as they plan their projects.

The current wave of stadium construction shows little sign of waning. The financial bonanza that new facilities promise and the inevitable rise in player salaries and other costs ensure that owners of sports franchises will continue to pursue more modern and more lucrative new stadia. And the limited number of major league teams in the United States strongly suggests that there will almost always be some city whose government and civic officials are prepared to subsidize new stadium development projects at substantial public cost in order to retain an existing team or lure a new one. In part two of this article, we will briefly examine two important ways that the franchise owners who most directly profit from new stadium projects reap the economic benefits made possible by the current stadia mania.

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