Sports Industry Practice Guide

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OVERVIEW

Question 1: Please describe the sports industry and briefly discuss various types of companies and major players.

The sports industry is a general term used to refer to the amateur, semi-professional, and professional markets in which individuals, teams, organizations (including schools), and governing bodies produce, promote, facilitate, and regulate competitions, events, activities, entertainment, and business focused on sports.

Sports lawyers focus their practice and apply their particular expertise within the sports industry. However, sports law is a bit of a misnomer in that there is technically no such thing as sports law; rather, it refers to the application of different areas of law to the sports industry. Legal representations in the sports industry include, among other things, (i) transactional work such as negotiating sales or acquisitions of sports franchises, sports facility development and finance projects, license/lease agreements, management agreements, naming rights and sponsorship agreements, and television, radio, and media rights agreements; (ii) corporate governance work helping navigate league governance, compliance, and enforcement issues and developing collegiate conference compliance strategies and plans; and (iii) litigation in areas ranging from antitrust investigations to insurance coverage litigation.

APPLICABLE SECURITIES LAWS AND REGULATIONS

Question 2: What are the relevant statutes and regulations governing securities offerings by sports companies?

The Securities Act of 1933, as amended (the Securities Act), and the Securities Exchange Act of 1934, as amended (the Exchange Act), are the principal federal statutes governing securities offerings and securities markets in the United States. The Securities Act regulates offerings of securities to the public, while the Exchange Act regulates secondary securities exchanges and its participants (e.g., issuers, underwriters, and broker-dealers) in the United States as well as ongoing issuer disclosure with the Securities and Exchange Commission (the SEC). For a general overview of the Securities Act, the Exchange Act, and other securities laws, see U.S. Securities Laws: An Overview.

Securities Act

The Securities Act requires full and fair disclosure of material information regarding the offered securities and the issuer in public offerings of securities. Issuers disclose such material information through two documents: (i) a registration statement, which an issuer files with the SEC, and (ii) a prospectus, which is part of the registration statement and is distributed to potential purchasers. In general, documents filed with the SEC are available to the public. For additional information, see Registered Offerings: Applicable Laws, Rules, and Regulations.

Exchange Act

While the Securities Act regulates the initial offering of securities, the Exchange Act regulates securities traded in secondary markets and an issuer's ongoing public disclosure. The Exchange Act imposes periodic reporting requirements (e.g., quarterly reports on Form 10-Q and annual reports on Form 10-K) and special reporting requirements (e.g., current reports on Form 8-K and proxy statements on Schedule 14A). These reporting requirements apply to (i) issuers that have more than 2,000 shareholders (or 500 shareholders who are not accredited investors and over $10 million in assets, (ii) issuers that file Securities Act registration statements with the SEC, and (iii) issuers with securities listed on U.S. securities exchanges. For additional information, see Public Company Periodic Reporting and Disclosure Obligations.

SEC Regulations

The SEC is responsible for enforcing the Securities Act, the Exchange Act, and other specialized federal securities laws (e.g., the Investment Company Act of 1940 and the Investment Advisers Act of 1940) and is authorized to establish rules and regulations, issue interpretations on federal securities laws, investigate potential violations of federal securities laws, and initiate actions against violators of federal securities laws.

To facilitate the disclosure of material information about the issuer and an offering, the SEC promulgated Regulation S-K, which establishes detailed disclosure requirements for nonfinancial information filed with the SEC, and Regulation S-X, which prescribes the form and content of financial information included in SEC filings. For additional information on Regulation S-X, see Securities Offerings and Financial Statements.

Aside from establishing disclosure and reporting requirements, the SEC has codified exemptions to registration requirements under the Securities Act.

Section 4(a)(2) (15 U.S.C.S. § 77d) of the Securities Act exempts transactions by an issuer not involving a public offering. Although this is a factual determination, courts have generally held this to include offerings in which the purchasers of the securities: (i) either are sophisticated investors, or are able to bear the economic risk related to the investments; (ii) have access to the type of information normally provided in the prospectus for a public offering; and (iii) agree not to resell or distribute the securities to the public. For further information, see Considerations When Conducting a Private Placement of Securities and Section 4 Exemptions from Securities Act Registration Checklist.

Regulation D is a safe harbor under Section 4(a)(2) and establishes exemptions from registration, including (i) Rule 504 (17 C.F.R. § 230.504) (securities offerings up to $5 million in a 12-month period solely to accredited investors), (ii) Rule 506(b) (17 C.F.R. § 230.506) (unsolicited, unadvertised offerings of unlimited amount to accredited investors and up to 35 sophisticated unaccredited investors), and (iii) Rule 506(c) (broadly solicited and generally advertised offerings of unlimited amount to accredited investors). Rule 506(c) imposes a duty on the issuer to take reasonable steps to verify investors are accredited. Accredited investors are defined in Rule 501 (a) (17 C.F.R. § 230.501) to include certain banks, business developments companies, corporations, and trusts, as well as financially sophisticated natural persons meeting net worth or income requirements exceeding $1 million. For further information, see Choosing Between a Section 4(a)(2) and Regulation D for a Private Placement, Basic Components of Rule 504 and Rule 506 of Regulation D Checklist, Knowing the Components of Regulation D, and Understanding the Classes of Investors in Regulation D Offerings.

Section 3(a)(11) (15 U.S.C.S. § 77c) of the Securities Act exempts intrastate offerings from registration requirements. To qualify for this exemption, the offering must be issued and offered solely to persons resident in a single state, where the issuer of such security is a person resident and doing business within, or, if a corporation, incorporated and doing business within, such state. For further information, see Section 3 Exemptions from Securities Act Registration Checklist and An Overview of Private Offering Exemptions.

On March 25, 2015, the SEC adopted final rules to implement Section 401 of the Jumpstart Our Business Startups Act (the JOBS Act), amending Regulation A. Under the modified Regulation A (commonly referred to as Regulation A+) (Rules 251 (17 C.F.R. § 230.251) through 263 (17 C.F.R. § 230.263)), issuers can offer securities to the public with more limited disclosure requirements than are required of public reporting companies. Regulation A+ is divided into two tiers (Tier 1 and Tier 2) and provides some issuers with opportunities to raise equity capital. Under Tier 1, issuers can raise up to $20 million in any 12-month period. Under Tier 2, issuers can raise up to $50 million in any 12-month period. Investors must be provided with, or given access to, an offering statement filed on Form 1-A (an Offering Statement) with the SEC. Except for an exit report filed on Form 1-Z on the status of the offering, issuers relying on Tier 1 do not have any ongoing reporting requirements while issuers relying on Tier 2 must file semi-annual and annual reports as well interim current reports upon the occurrences of certain events. For further information, see "Regulation A-Plus" Limited Public Offerings under Securities Act Section 3(b)(2), "Regulation A-Plus" Tier 1 and Tier 2 Offerings Summary Chart, and Regulation D, Regulation A+, and Regulation Crowdfunding Requirements Chart.

Blue Sky Laws

In addition to federal securities laws, each state has its own set of blue sky laws (Blue Sky Laws) that regulate securities offerings and sales. Like federal securities laws, they were enacted to promote fair and full disclosure and protect the public from fraud. Each state has its own regulatory authority, which administers and enforces that state's Blue Sky Laws. Generally, unless there is an exemption, Blue Sky laws require (i) issuers to register the offerings with the state regulatory authority and (ii) brokers and brokerage firms to register with the state regulatory authority (which can have a significant impact on smaller offerings because the offering costs are larger as a percentage of the amount of capital raised in such offerings). Although Blue Sky Laws have generally been preempted by the National Securities Markets Improvement Act of 1996 for national securities offerings, there are still notice and filing requirements that must be met. For further information, see The Application of Blue Sky Laws to Offerings after NSMIA, Understanding Securities and Transaction Exemptions under Blue Sky Laws, and The Mechanics of Blue Sky Law Compliance in Securities Offerings.

League Rules and Regulations

Each applicable professional sports league will also have its own rules and regulations governing the admission of new owners of teams (whether majority investors or minority investors). As part of the initial vetting process, prospective investors will be required to fill out applications with the leagues, which will include extensive amounts of background information, including financial information and any criminal or litigation history. Among other things, the leagues are also looking to prevent owners who are affiliated with industries that the leagues consider incompatible with their sport (e.g., gambling/casinos) or who are otherwise controversial. Because the leagues can control who becomes an owner of a member team, they do not want to knowingly harm the reputation of their sport. Beyond the initial screening of potential investors in teams, each proposed investment transaction and investor must also be approved by the league. For small, minority investors, the league itself (through its commissioner) will generally have the power to approve such transaction and investor. For larger investors, including any majority investor, generally a super-majority approval of the league's member teams is required.

SECURITIES OFFERING PROCESS

Question 3: What is the typical process for securities offerings by sports companies, including general steps, timeline, key transaction documents, due diligence process, and required regulatory and stock exchange filings?

In the United States, sports entities issue securities primarily through (i) private placements that are exempt from registration and (ii) public offerings registered with the SEC. While public offerings allow issuers to market securities to the broadest range of potential investors, this comes with extensive public disclosure requirements. Generally, professional sports leagues prefer their member teams to remain private so as to maintain tighter control over the teams and their owners and avoid publicly disclosing information, particularly financial information, regarding the league and its teams. Nevertheless, despite current league rules that prohibit public ownership, the Green Bay Packers have been publicly owned since 1923 as a result of being grandfathered in at the creation of the current league rules. Another example of a publicly held sports team is Manchester United plc (Manchester United), which is traded on the New York Stock Exchange. At the time of its initial public offering (IPO) in 2012, the club was only subject to U.K. takeover laws and the league's fit-and-proper-person test, neither of which prohibit public ownership of a club. U.K. takeover laws require an investor that acquires more than thirty percent ownership in a company to launch a takeover bid for the remaining shares at the same price that it purchased its last tranche of shares. The fit-and-proper-person test of The Premier League, the league to which Manchester United belongs (Premier League), requires any owner who acquires a thirty percent stake or greater to undergo an evaluation prior to completion of any takeover attempt. This evaluation looks for the owner's ability to influence another Premier League club, significant interest in another club, bankruptcy filings, and whether the owner's acquisition would be prohibited by law. In 2017, Premier League clubs voted to tighten the league's ownership rules by allowing the league to prohibit an investor from acquiring ownership of a club if the investor is deemed to have misled the league during its purchase attempt. The league also extended its fit-and-proper-person test to include factors such as whether the owner's business comes from illegal or illegitimate sources, which is determined under U.K. law, and whether the owner has engaged in criminal conduct under U.K. law either in the United Kingdom or overseas.

The first step in the offering process for a sports company is for the issuer to decide whether to engage investment bankers. Although not required, issuers usually use investment bankers because of their expertise with financial markets and extensive customer base. Once the issuer determines whether or not to use an investment banker, it must decide what type of securities to offer: equity, debt, or combination of the two. Equity is attractive to investors who: (i) do not want to incur ongoing debt obligations, (ii) need immediate cash flow, and (iii) want obligation/covenant-free financing. Debt may also be attractive to an issuer for a number of reasons, including (i) no dilution of ownership and maintenance of operating control, (ii) principal and interest amounts (for fixed interest securities) that are known figures and can be appropriately planned for, and (iii) no sharing of future profits. Once an issuer has determined whether to issue equity or debt, they must decide what form such offering takes. Equity offerings may involve the issuance of common or preferred stock. Debt offerings include short-, medium-, and long-term notes or bonds. After an issuer decides what type of security to offer, it must decide whether to issue the securities through a public offering or private placement. For additional information, see Debt vs. Equity Classification Checklist, Classification of Securities for Tax Purposes: Debt, Equity or Other, Comparison of Types of Equity Offerings Chart, and Common Equity Securities Offerings Flowcharts.

Securities that are publicly offered must be registered on a registration statement filed with the SEC, which must be declared effective, prior to the offering (unless the issuer is a well-known seasoned issuer, in which case the registration statement is automatically effective). Private placements must be offered pursuant to an exemption available under Regulation D, Section 4(a)(2) of the Securities Act, Regulation S (for foreign private placements), or another exemption.

Private placements offer a number of benefits to issuers. First, private placements have less disclosure requirements generally if they are offered to a select group of accredited investors who do not need the same kinds of protections as the general public. This allows issuers to raise capital while disclosing limited sensitive information, which decreases the financial burdens compared to a public offering. Also, the reporting and disclosure costs in a public offering drastically exceed the costs associated with disclosure of information in a private placement (although emerging growth companies (EGCs) are temporarily exempted from certain public offering requirements). Second, while participants in a private placement were traditionally restricted from engaging in general advertising and solicitation under Rule 504 and Rule 506(b), issuers can now utilize general advertising and solicitation under Rule 506(c), which was adopted as a result of the JOBS Act, as long as the offering is restricted to accredited investors only. As a result, issuers can now take advantage of more relaxed advertising and solicitation rules under Rule 506(c), which makes it easier to raise capital from accredited investors. Third and finally, private placements are less time-consuming and costly than public offerings because they not filed with the SEC.

At the same time, there are also potential drawbacks with private placements. Because private debt offerings are generally not assigned ratings, issuers may need to pay higher interest rates to attract investors. Additionally, private placements are usually limited to a small group of accredited investors, which could make placing the securities more difficult than if they were made to the general public. Rule 506(b), however, does allow offerings of to up to thirty-five unaccredited investors in addition to accredited investors. For more information on private placements, see Top 10 Practice Tips by Experts: Private Placements, Private Placements Resource Kit, and Managing the Private Offering.

Registration Statement on Form S-1 and Form S-3

Prior to offering any securities in a public offering, an issuer must file a registration statement with the SEC. An issuer and its legal counsel are responsible for drafting the registration statement, while the underwriters and their counsel are primarily responsible for reviewing and commenting on the registration statement and running the road show to place the securities. If the issuer is offering securities for the first time, it must file its registration statement on Form S-1. Part I of Form S-1, also known as the prospectus, is a legal document that includes a description of the business, the total offering proceeds and price per share, offering price methodology, the planned use of the proceeds, the issuer's financial results and condition, and information on the underwriters. Part II of Form S-1 is supplemental information including certain financial information, a description of the sales or issuances of unregistered securities and the exemptions relied upon in such sales or issuances (if any), and required exhibits.

Once a Form S-1 is filed with the SEC, the SEC will review it and provide any comments to the issuer. The issuer then prepares and files an amendment on Form S-1/A addressing the SEC's comments. The SEC reviews Form S-1/A and usually has further comments, which are resolved through the filing of subsequent amendments. When the SEC has no additional comments, it will issue an order allowing Form S-1 to go effective. After Form S-1 goes effective, an issuer can begin selling its securities. For further information, see Form S-1 Registration Statements and Form S-1 Checklist.

An issuer who has been subject to Exchange Act reporting requirements for at least 12 months prior to an offering (and is a timely filer) may file a simplified registration statement on Form S-3 if it meets certain transaction requirements. This is the form most often used for resales of restricted securities by an issuer's stockholders.

Form S-3 calls for similar information to that in Form S-1. However, unlike Form S-1, Form S-3 permits both past and forward incorporation by reference, allowing issuers to automatically incorporate by reference reports filed with the SEC prior to and subsequent to the filing of a Form S-3. (Form S-1 allows past incorporation by reference in some instances, but only if the issuer is already a reporting company. So, while each required item of Form S-K must generally be included in Form S-1, many items can be omitted or incorporated by reference on Form S-3. For further information, see Comparison of Form S-1 and Form S-3 Registration Statements Checklist, Using Form S-3 Registration Forms, Form S-3 Registration Statements, and Form S-3 Checklist.

Offering Statement on Form 1-A

Similar to a registration statement for a public offering, an Offering Statement must be filed with the SEC by an issuer offering securities under Regulation A+. The Offering Statement will include information regarding the offering and the securities offered, risks related to the investment, intended use of proceeds, any selling shareholders, the issuer's performance, and financial statements. Notably, financial statements provided in the Offering Statement for securities offered under Tier 1 do not have to be audited by an independent accountant while the financial statements provided in the Offering Statement for securities offered under Tier 2 do.

Offering Memorandum

An offering memorandum is the private placement equivalent to the prospectus in a registration statement. Although under no legal obligation to do so, offering memoranda generally track the disclosure requirements for registration statements for marketing purposes. This approach ensures complete and accurate disclosure to potential investors and reduces potential liability for issuers, underwriters, and their respective counsel. For a form of offering memorandum, see Sample Confidential Private Offering Memorandum.

DISCLOSURE OBLIGATIONS

Question 4: What information must be made available to potential investors in connection with securities offerings by sports companies?

Like other issuers, sports companies must provide full and fair disclosure of material information in connection with either a public offering or a private placement. Issuers offering securities to the public must disclose certain information in connection with the offering in a prospectus as part of a registration statement, while issuers offering securities exempt from registration requirements disclose similar information in an offering statement or offering memorandum. In such disclosure documents, an issuer must disclose all material facts about: the offering, the securities being offered, risks associated with the investment, the issuer, its management, its operations, and financial statements. As discussed in more detail below, Regulation FD prohibits issuers from disclosing any material, non-public information to market insiders and investors without simultaneously disclosing such information to the public.

A. RISK FACTORS

Please describe the common risk factors that are specific or unique to issuers in this industry. Have there been any recent developments or changes that counsel should be aware of when preparing these risk factors?

Brand Reputation

While many companies focus purely on the bottom line, the success of an issuer in the sports industry goes beyond dollars and cents and is intrinsically linked to the strength of its brand reputation. For example, Nike's Annual Report on Form 10-K for the fiscal year ended May 31, 2016 (the Nike 2016 Annual Report) states "our success depends on our ability to maintain and enhance our brand image and reputation." See the Nike 2016 Annual Report at p. 62. Its brand reputation is so intrinsically tied to its success that Nike goes on to say "adverse publicity about regulatory or legal action against us, or by us, could damage our reputation and brand image, undermine consumer confidence in us and reduce long-term demand for our products, even if the regulatory or legal action is unfounded or not material to our operations." Similarly, Manchester United's value is so tied to its brand reputation that potential harm to its reputation was listed as the first risk factor in its Annual Report on Form 20-F for the fiscal year ended June 30, 2016 (the Manchester 2016 Annual Report), which provided that the "success of our business depends on the value and strength of our brand and reputation" and "[our] brand and reputation are also integral to the implantation of our strategies for expanding our follower base, sponsors and commercial partners." See the Manchester 2016 Annual Report at p. 4.

League Governing Bodies

For the few publicly listed sports franchises, the actions of the governing bodies of their respective leagues could have a major impact on the operations of the business. In its Annual Report on Form 10-K for the period ending June 30, 2016 (the MSG 2016 Annual Report), The Madison Square Garden Company (MSG Co.), owner of the New York Knicks and the New York Rangers, provided that the past and future rules, regulations, and agreements promulgated by the National Basketball Association (the NBA) and the National Hockey League (the NHL) could have an adverse effect on its business and results of operations. Similarly, Manchester United stated that current and potential regulation by the Premier League, the (English) Football Association, the Union of European Football Associations, and the Fédération Internationale de Football Association could negatively impact its results of operation. Liberty Media Corporation, owner of the Atlanta Braves, provided in its Registration Statement on S-4 filed December 22, 2015 (2015 Form S-4) that it would have to abide by any Major League Baseball (MLB) rules and regulations, regardless of whether there was a disproportionate impact on the Atlanta Braves as compared to other teams.

Labor Disruptions

Although the threat of labor disruptions can occur in any industry, its effect is unique in the sports industry. In theory, if workers go on strike, a manufacturer can hire replacement workers to produce widgets that are similar in quality to those that the workers who are on strike would make. However, for sports franchises, the players produce a one-of-a-kind product for which there is no adequate substitute. MLB, the NBA, the NHL, and the National Football League (the NFL, and together with MLB, the NBA, and the NHL, the Leagues) have experienced labor disruptions in the past, which have led to abbreviated seasons. Losing portions of a season due to a labor dispute could result in significant losses in potential revenue while still subjecting the franchise to certain fixed expenses associated with the lost games. For example, Liberty Media Corporation, which holds twenty percent of the company that owns the Atlanta Braves, in its 2015 Form S-4, disclosed that the current MLB collective bargaining agreement was set to expire in twelve months, and impending labor negotiations may not be positive, which could have a negative impact on the corporation's future financial success.

Media/Broadcasting Rights

Media/broadcasting rights, both national and local, provide significant revenue for issuers in the sports industry. For most sports organizations, the production, marketing, and sale of media/broadcasting rights is now the largest source of revenue, and, as technology advances, this is expected to continue. Because of the size and importance of this revenue stream, any potential impacts to these rights should be identified. For example, Liberty Media Corporation disclosed that the Braves derive revenue directly from the sale of local broadcasting rights and indirectly from revenue sharing profits from the sale of MLB's national broadcasting rights, and any decrease in broadcasting revenue from either source could have an adverse result on its financial results. Similarly, MSG Co. disclosed that the NHL and NBA have each entered into agreements regarding the national and international telecasts of NHL and NBA games, respectively. MSG Co. further provided that there is no guarantee that either league will be able to renew those agreements on terms equally as favorable or that it would receive the same level of revenues in the future.

For most sports franchises, the negotiation and pricing of their large League-wide media/broadcasting rights contracts are in the hands of their respective League governing bodies and outside of their control. Changes in the terms of such contracts could have a significant impact on a sports franchise's operations. For example, in 2016, Manchester United derived over 90% of its media/broadcasting rights revenue from Union of European Football Associations (UEFA) and Premier League matches, and the contracts for the media/broadcasting rights for these matches are negotiated exclusively by UEFA and Premier League. Further, Manchester United disclosed that the terms of such contracts may not be as favorable as those it may have otherwise gotten if it had negotiated individually with media distributors, and a decline in the prices paid for UEFA and Premier League matches would result in a decline in revenue for Manchester United.

Competition

Sports franchises face increasing competition for consumers' limited discretionary spending on entertainment, both from within the sports industry (e.g., other professional and collegiate sports in their geographic area) and outside of sports in other forms of entertainment (e.g., movies, theme parks, and cultural attractions). In addition, the relatively high price of tickets for live sporting events combined with the advancement in technology of sports telecasts (e.g., higher definition broadcasts on relatively inexpensive larger-screen televisions) have led some fans to choose the in-home viewing experience over attending and paying for the live, in-game experience. Issuers may want to disclose this development as a risk factor. For example, Liberty Media Corporation (part owner of the Atlanta Braves) disclosed in its 2015 Form S-4 that viewership of baseball may fluctuate due to factors outside the corporation's control and broadcasting rights revenues may, in turn, decrease. These factors could potentially have a negative impact on the corporation's future financial success. In addition, the corporation disclosed that competition on the field may also have a negative impact on the company, such as developing, obtaining, and retaining top players, injuries to top players, and overall on-field success for the franchise.

Liquidity

Like other issuers, general economic trends or a change in credit ratings could have an impact on the liquidity of sports companies and result in increased borrowing costs. The Nike 2016 Annual Report disclosed that macroeconomic conditions, including disruptions in the credit markets, could adversely affect its ability to refinance existing debt and that reductions in its credit ratings could result in higher borrowing costs for debt obligations and limited access to credit markets. Additionally, financial covenants, such as maintenance of a certain debt-service coverage ratio, included in indebtedness documents could affect liquidity.

Transfer Restrictions

The Leagues impose restrictions on the ownership of its franchises. For example, MLB requires a three-fourths vote of the MLB clubs to approve the sale or transfer of a control interest in a club, provided that only a majority vote is required to approve the sale or transfer to a spouse or lineal descendant occurring upon the death of an owner. The NBA requires a three-fourths vote of the NBA's Board of Governors to approve a sale or transfer of any membership interest in a team. Additionally, shareholder agreements could limit transfer of ownership interests. For example, MSG Co. disclosed in the MSG 2016 Annual Report that the Dolan family is able to prevent a change of control of MSG Co, which could impact the value of an investment in MSG Co. stock. Therefore, because the Dolan family can restrict transfer of the business, this could potentially have a negative impact on the company's business and the value of investors' investments.

Team Performance

As is the case for any product, superior performance can command a superior price. As one would expect, this is especially true when it comes to sports franchises, where fans demand the best. Manchester United, for example, disclosed that all of its revenue streams are driven by the performance and popularity of its first team (i.e., starters and reserves/substitutes) and that income varies significantly based on the first team's participation and performance in domestic and European competitions. It should be noted that, while team performance can be risk factor, it is only one of many key drivers of a team's overall operations. As demonstrated by the high revenues of teams like the New York Knicks and the Los Angeles Lakers, on-court performance does not necessarily correlate directly with fiscal success.

For additional information on risk factors, see Market Trends: Risk Factors, Top 10 Practice Tips by Experts: Risk Factors, and How to Draft Risk Factors for a Registration Statement.

B. MD&A AND BUSINESS

Please provide the key discussion points that counsel should consider when preparing the business and MD&A sections for issuers in this industry.

As is the case with any issuer, counsel should advise issuers in the sports industry that the business and management's discussion and analysis of financial condition and results of operations (the MD&A) sections of their disclosure documents should not merely recite the numbers in the financial statements, but rather should provide a narrative to current and potential investors of the overall financial and operational health of the business. The sections should point out key financial information (including key performance indicators and liquidity and capital resources) in a straightforward succinct manner that is easily digestible to the general public, and identify known material trends and uncertainties.

For issuers in the sports industry, it is important to frame financial and business information not just in the context of the specific industry the company is in (e.g., apparel industry for Nike or sporting goods industry for Easton) but in the greater sports industry context. For example, with the rise in awareness regarding the connection between concussions and repeated impact in contact sports, it is important for sporting goods manufacturers such as Easton or Riddell to identify such trends and distinguish how the discussion in these sections is impacted.

For additional information on MD&A, see Management's Discussion and Analysis of Financial Condition and Results of Operations and Management's Discussion and Analysis Section Drafting Checklist.

C. OTHER PROSPECTUS DISCLOSURE

Is there any other additional or special disclosure that should be included in the prospectus or registration statement for issuers in this industry, either required by the SEC or from market practice?

As referenced in the responses to Questions 2 and 4.A above, sports franchises are subject to any rules and regulations promulgated by their respective leagues' governing bodies and—subject to the leagues' governing documents—are beholden to the commissioner/president of those leagues, who generally hold broad discretionary powers. As a result, such issuers should include additional disclosure related to particular rules and regulations that may affect the franchise disproportionately as compared to other franchises. Additionally, sports franchises should disclose how disputes related to league rules and regulations or disputes involving other clubs are settled. Notably, all MLB teams must submit such disputes to the commissioner of baseball, whose decisions on such matters are binding and non-appealable. As a result, sports franchises or owners of franchises that are publicly listed should disclose how this process could have a material effect on the operations of the issuer.

D. ADDITIONAL DISCLOSURE ISSUES

Other Disclosure Issues: Please discuss any other special disclosure issues or advice applicable to issuers in this industry.

Emerging Growth Companies

Because sports franchises generally have less than $1.07 billion in annual revenue, they usually qualify as EGCs under the JOBS Act, which is discussed in further detail below. An EGC under the JOBS Act is any company that has less than $1.07 billion in annual revenue, less than $700 million in ordinary shares held by non-affiliates, no more than $1 billion in non-convertible debt over a three-year period, and has had its IPO within the previous five years. If a company qualifies as an EGC, it can take advantage of reduced public reporting and disclosure, which is intended to incentivize investment in EGCs and spur economic growth. These reduced requirements include, among others: only two years of audited financial statements, two years of related MD&A, and an exemption from the auditor attestation requirement under the Sarbanes-Oxley Act of 2002 (SOX). EGCs can also opt out of the reduced reporting. For example, Manchester United qualified as an EGC at the time of its IPO in 2012. However, in its registration statement, it acknowledged that it was not taking advantage of these reduced requirements in its prospectus (although it reserved the right to do so in future filings, which is permitted for certain, though not all, of the EGC benefits). If sports franchises decide to become publicly traded, the less burdensome reporting and disclosure requirements for EGCs under the JOBS Act offer less risk for the franchise by reducing costs associated with an IPO. For additional information, see Emerging Growth Company Practice Guide, Top 10 Practice Tips by Experts: Emerging Growth Companies, IPO Requirements for Emerging Growth Companies Checklist, and Market Trends: The Jobs Act.

UNDERWRITING AGREEMENTS

Question 5: What types of underwriting arrangements are commonly used? What are some of the standard clauses and clauses that are heavily negotiated in an underwriting agreement in connection with an offering by a sports company?

A sports entity issuing debt or equity securities enters into an underwriting agreement or purchase agreement with one or more lead investment banks as underwriters or initial purchasers, pursuant to which the banks work with the sports entity to draft the offering documents and identify and secure third parties to purchase the debt or equity. The following paragraphs discuss (i) the most common types of commitments made by underwriters pursuant to underwriting agreements (or initial purchasers pursuant to purchase agreements) and (ii) the key negotiated provisions in these agreements.

Firm Commitment vs. Best Efforts Underwriting Arrangements

Underwriters generally make one of two types of commitments under underwriting agreements: a firm commitment or a best efforts commitment. Under a firm commitment, the underwriters agree to purchase all of the debt or equity securities offered by the issuer even if the underwriters are unable to secure additional purchasers. In contrast, under a best efforts commitment, the underwriters agree only to use their best efforts to secure third parties to purchase all or a predetermined amount or percentage of the securities offered, and the underwriters are not required to purchase any of the securities unless they secure third parties to purchase such predetermined amount or percentage. The investment banks who act as initial purchasers in a private placement have a firm commitment to purchase the securities, whether or not they can resell them. If investment banks in a private placement have only a best efforts commitment, they are known as placement agents instead of initial purchasers. For additional information, see Underwriting Registered Securities Offerings and Drafting the Purchase Agreement for a Rule 144A/Regulation S Debt Offering.

The purpose of a sports entity's financing often drives the type of underwriting commitment it requires. Sports entities make debt or equity offerings for a wide range of purposes, including securing funds to build a new stadium or arena, financing another project, acquiring a team, and/or obtaining additional operating capital. Due to the need to have certainty regarding the availability of funds, sports entities are more likely to require firm commitment underwriting when seeking financing for a stadium, arena, or other project or when acquiring a team. On the other hand, a best efforts commitment is more likely to suffice when the sports entity intends to use the proceeds for general operating capital purposes as opposed to financing a particular transaction.

Key Negotiated Provisions of Underwriting and Initial Purchase Agreements

Representations and warranties of the issuer. Underwriting agreements generally contain extensive representations and warranties from the issuer, which are often the most heavily negotiated terms of the agreement. These representations and warranties serve to allocate risk between the issuer and the underwriters, provide a measure of due diligence protection for the underwriters, and, if they are breached, give the underwriters a basis for terminating their underwriting commitments. Typically, the representations and warranties cover a variety of topics, including, among others, corporate standing and authorization, compliance with laws, accuracy of the offering documents and financial information, no defaults or violations of other contracts, insurance matters, intellectual property matters, and licenses and permits. For a form of underwriting agreement containing standard representations and warranties, see Underwriting Agreement (Primary Offering). An underwriting agreement with a sports entity issuer may also contain representations and warranties regarding the absence of defaults by the issuer under League rules, regulations, and governing documents, the receipt of all necessary League approvals, the existence of pending or threatened labor matters (including strikes, lockouts, and other work stoppages), the continuing effectiveness of the team's franchise, the issuer's ownership or lease of its stadium or other facility, and the absence of any intent or commitment to relocate the team. When negotiating representations and warranties on behalf of a sports entity issuer, as is the case for most types of issuers, the best practice is to seek representations and warranties that are limited to the issuer's knowledge and/or that will only cause a default under the underwriting agreement if the violation of the representation and warranty would reasonably be expected to have a material adverse effect on the business, operations, or financial condition of the issuer and its subsidiaries, taken as a whole.

Indemnity provisions. The other most highly negotiated provisions of an underwriting agreement are the indemnity obligations of the issuer and the underwriters. Both the issuer and the underwriters are exposed to potential liability under the securities laws for material misstatements and omissions in the offering documents. The indemnity provisions serve to allocate that risk among the parties. The broadest indemnity is given by the issuer in favor of the underwriters, their affiliates, and their respective officers, directors, employees, and owners, and generally requires the issuer to indemnify the underwriters for any untrue or misleading statements or omissions in the offering documents or other information provided to the underwriters. However, the issuer's indemnification obligation should not cover any information furnished by the underwriters specifically for inclusion in the offering documents or for any liabilities directly arising from the gross negligence, willful misconduct, or breach of any agreement by the underwriters. In contrast, the obligation of the underwriters to indemnify the issuer and its affiliates is generally much narrower, covering only those liabilities directly arising from an untrue or misleading statement or omission in the information furnished by the underwriters specifically for inclusion in the offering documents. Furthermore, the liability of the underwriters under their indemnification obligations is generally several and not joint and is capped at the amount of the net proceeds of the offering or some other fixed amount. For additional information, see Liability under the Federal Securities Laws for Securities Offerings — Indemnification, Contribution, and Insurance.

CONTINUOUS DISCLOSURE AND CORPORATE GOVERNANCE

Question 6: What specific continuous disclosure and corporate governance requirements apply to sports companies?

U.S. federal securities laws impose ongoing disclosure requirements on public companies. Public companies comply with such disclosure requirements through periodic filings under the Exchange Act. Such periodic filings include annual (Form 10-K), quarterly (Form 10-Q), and current (Form 8-K) reports as well as proxy statements (Schedule 14A). For additional information, see Periodic Reports Filing Deadlines Checklist, Top 10 Practice Tips by Experts: Periodic and Current Public Company Reporting, and Periodic and Current Reporting Resource Kit.

Annual Report on Form 10-K

Like other reporting companies, a U.S. public sports company is required to file its annual report on Form 10-K with the SEC. The annual report on Form 10-K (the Annual Report) provides a comprehensive summary of a company's financial performance for that fiscal year and includes the MD&A and risk factor considerations. The MD&A in the Annual Report provides an overview of the results of operations for the prior three years and financial condition for the prior two years. Management will also discuss risk factors, highlighting significant risks and trends (generally listed in order of importance) that could potentially affect a public company's current or future financial condition or operations.

The deadline for filing an Annual Report varies based on the size of the reporting company. Large accelerated filers (generally, companies with non-affiliate equity market value of $700 million or more) must file within 60 days of fiscal year-end. Accelerated filers (generally, companies with non-affiliate equity market value of $75 million-$700 million) must file within 75 days of fiscal year-end. Non-accelerated filers (generally, companies with non-affiliate equity market value of less than $75 million) must file within 90 days of fiscal year-end. For additional information, see Drafting and Reviewing Form 10-K by Jonathan C. Guest, The Hereditary Disease Foundation, Form 10-K Checklist, and Annual Report to Shareholders.

Quarterly Reports on Form 10-Q

Prior to filing the Annual Report at year-end, public companies file quarterly reports on Form 10-Q (the Quarterly Report) with the SEC. Quarterly Reports provide updates on a company's results and financial condition during the year. Like the Annual Report, a Quarterly Report contains information regarding a company's financial performance and results of operations for the first three fiscal quarters (the fourth quarter's performance and results are included in the Annual Report). Unlike the Annual Report, information included in the Quarterly Report is often less detailed, and the financial statements are generally unaudited.

The deadline for filing a Quarterly Report varies with the size of the reporting company. Large accelerated filers and accelerated filers must file within 40 days of period-end. Non-accelerated filers must file within 45 days of period-end. For additional information, see Drafting and Reviewing Form 10-Q and Form 10-Q Checklist.

Current Reports on Form 8-K

In addition to the Annual Report and the Quarterly Report, public companies are required to file current reports on Form 8-K (the Current Report) disclosing certain corporate events that are material to shareholders and potential investors. Such events include the entry into or the termination of a material definitive agreement, the acquisition or disposition of a significant amount of assets, and amendments to a public company's corporate governance documents, among other requirements.

Public companies have four business days to file a Current Report for the events specified in Sections 1-6 and 9 of Form 8-K. Public companies filing a Current Report to satisfy obligations under Regulation FD may have to file earlier. For additional information, see Memorandum to Management on 8-K Triggering Events and Related Disclosure Reporting Procedures, Disclosure of Executive Compensation Decisions on Form 8-K, Drafting and Filing a Form 8-K, and Form 8-K Reportable Transactions and Filing Deadlines Reference Chart.

Proxy Statement on Schedule 14A

Public companies are required to file a proxy statement on Schedule 14A (the Proxy Statement) with the SEC when soliciting shareholder votes at the annual meeting. The Proxy Statement includes the following: (i) voting procedures and information, (ii) proposals to be voted on, (iii) background information about director nominees, including relevant industry experience, positions on other corporate boards, and potential conflicts of interests, (iv) composition of the audit, compensation, and nominating/governance committees, and (v) director and executive compensation. For additional information, see Proxy Statement and Annual Meeting Resource Kit.

League Rules and Reporting Requirements

The constitutions, bylaws, and other governing agreements of the Leagues grant the Leagues wide authority to effectuate rules that could significantly affect the business operations of member clubs. For example, the MLB Constitution grants the MLB commissioner and the Major League Executive Council broad powers to promote and protect the interests of baseball, pursuant to which MLB has promulgated MLB's debt service rule (the Debt Service Rule). Pursuant to the Debt Service Rule, no team may maintain more total outstanding debt, as calculated as an average over the course of each fiscal year (Debt), than can reasonably be supported by its earnings before interest, taxes, depreciation, and amortization (EBITDA). A team's Debt cannot be reasonably supported by its EBITDA if its Debt exceeds the product of its EBITDA during the most recent year multiplied by the EBITDA multiplier applicable to that club. Each club's reporting and accounting practices are subject to the commissioner's review and approval. To ensure compliance with the Debt Service Rule, teams must submit an annual compliance certificate verifying whether it did or did not comply with the rule.

Some rules are put into effect through the collective bargaining process and are reflected in each League's respective collective bargaining agreement (each, a CBA). Many of these CBA rules impact the relationship between teams and players. Under the NBA's CBA, there is a more team-friendly designated player exception, which allows teams to offer their star players longer, more lucrative contract extensions. Other rules impact the day-to-day operations of a sports franchise. MLB's current CBA increased the luxury tax penalties for teams that exceed certain salary thresholds, meaning that a club will have to pay tax to the League on every dollar spent over that threshold.

Further, the Leagues often require their franchises to file annual financial reports. For example, an MLB team must complete an annual Financial Information Questionnaire (the FIQ) and Supplemental Information Questionnaire (the SIQ) with its audited financial statement to be submitted to the commissioner to verify the financial status of the team. The FIQ and SIQ are used to determine allocation of shared revenue. Similarly, NHL teams are required to report their annual revenues and expenses to be used by the NHL's independent auditors to generate a Hockey Related Revenue Package to be used for the independent auditors' reports to the NHL's Revenue Sharing Oversight Committee when determining revenue sharing.

Antitrust Exemption

By virtue of the Sports Broadcasting Act of 1961 (15 U.S.C. §§ 1291-95), the Leagues are statutorily exempt from antitrust legislation for the purpose of collectively selling rights to television broadcasts of games. The Leagues also share an exemption from labor relations regulation: MLB by legal precedent (Federal Baseball Club of Baltimore v. National League, 259 U.S. 200 (1922)); and the NFL, NBA, and NHL by virtue of the non-statutory labor exemption for collective bargaining agreements.

Beginning in 1942, the NFL enjoyed status as a 501(c)(6) nonprofit organization, which exempts business leagues that are not organized for profit from taxation. In exchange for favorable tax status, the NFL was obligated to disclose compensation for all corporate officers, directors, trustees, and key employees earning over $150,000. On April 28, 2015, the NFL relinquished its 506(c)(6) status, thereby relieving the NFL of any ongoing continuous disclosure obligations related to executive compensation.

STOCK EXCHANGE REQUIREMENTS

Question 7: Are there any special listing or corporate governance standards required by major stock exchanges, including NYSE and Nasdaq?

While there are no special listing or corporate governance standards required by major stock exchanges specific to issuers in the sports industry, sports teams should keep in mind that their ownership structure could have an effect on corporate governance rules under the New York Stock Exchange (NYSE) or the Nasdaq Stock Market (Nasdaq).

The Madison Square Garden Company

MSG Co. is wholly owned by the Dolan family. Members of the Dolan family entered into a stockholders' agreement relating to the voting of their shares. As a result, MSG Co. is a controlled company under the corporate governance rules of the NYSE. The controlled company designation means MSG Co. does not have to comply with the NYSE requirement for a majority independent board of directors or for an independent corporate governance and nominating committee or compensation committee. While controlled companies do not have to abide by certain corporate governance standards, sports companies that ultimately elect for such designation need to be cognizant that they must abide by the NYSE requirement for an independent audit committee.

Green Bay Packers

Founded in 1919, the Green Bay Packers (the Packers) are unique in that they have operated as a publicly-held non-profit organization since 1923. Although not publicly traded on a major stock exchange, the Packers have made five stock offerings and are currently held by 360,760 owners (representing 5,011,558 shares). While the Packers are not obligated to meet continuous disclosure requirements under the Exchange Act, they issue financial earnings reports and proxy materials to shareholders in advance of the annual shareholders meeting to comply with Wisconsin corporate law, which requires corporations to prepare annual financial statements and provide such statements to shareholders upon written request.

OTHER KEY LAWS AND REGULATIONS

Question 8: What are other key laws and regulations that a securities lawyer working with a sports company needs to be aware of?

Sarbanes-Oxley Act

In response to major corporate fraud scandals (e.g., Enron and WorldCom), Congress enacted SOX to strengthen corporate governance standards, prevent accounting fraud, and improve financial disclosure requirements. Among other things, SOX established the Public Company Accounting Oversight Board, standards for external auditor independence, corporate and criminal fraud accountability, white collar crime penalty enhancement, and corporate fraud accountability. The two key provisions of SOX are (i) the certifications under Sections 302 and 906 and (ii) Section 404.

Sections 302 and 906 of SOX require an issuer's chief executive officer and chief financial officer to certify in the Annual Report and the Quarterly Reports as to the company's internal controls and that the reports do not contain an untrue statement of a material fact or material omission and that the financial statements and related information fairly present the financial condition and results in all material respects. Section 404 of SOX requires issuers and external auditors to assess an issuer's internal controls for financial reporting and furnish a report on the adequacy of those controls. The report must affirm "the responsibility of management for establishing and maintaining an adequate internal control structure and procedures for financial reporting" and "contain an assessment, as of the end of the most recent fiscal year of the Company, of the effectiveness of the internal control structure and procedures of the issuer for financial reporting." Section 404 has been hotly debated because of the high costs associated with establishing and evaluating internal control structures and procedures for financial reporting. Due to the significant fixed costs involved, the SEC has permanently exempted issuers that are neither accelerated filers nor large accelerated filers from Section 404(b)'s internal control audit requirement. For additional information, see Sarbanes-Oxley Section 302 Certification, Sarbanes-Oxley Section 906 Certification, Preparing the CEO-CFO Certifications, and Addressing Internal Control over Financial Reporting.

JOBS Act

To help smaller companies raise funds through securities offerings, Congress enacted the JOBS Act, which relaxes certain securities requirements for EGCs, a new class of issuer. The JOBS Act also provides an exemption from the requirement of registering public offerings for certain types of offerings. It allows for the use of internet funding portals registered with the SEC, thereby allowing a form of equity crowdfunding. Under the exemption, the annual aggregate limits range from $2,000 or 5% (whichever is greater) for individuals earning (or worth) up to $100,000, to $10,000 or 10% (whichever is less) for people earning (or worth) $100,000 or more (up to a maximum investment of $100,000). The equity crowdfunding exemption is relevant in the sports context as it, in theory, provides fans a path to ownership, league public ownership prohibitions aside. For additional information, see Market Trends: Crowdfunding, An Overview of the SEC's Crowdfunding Regulations, and Crowdfunding Intermediaries.

Regulation FD Disclosure

Enacted in 2000 by the SEC to address selective disclosure and curb insider trading, Regulation FD prohibits companies from disclosing material non-public information to market insiders and investors without simultaneously disclosing that information publicly. If the selective disclosure is made intentionally, the issuer must make the public disclosure simultaneously. If the selective disclosure is made unintentionally, then public disclosure must be made promptly, meaning as soon as reasonably practical, but in any event before the later of (i) 24 hours or (ii) the start of the next day's trading on the NYSE (regardless of where or whether the company's stock is traded) after a senior company official learns of the disclosure. Issuers can meet this obligation by furnishing the information under Item 7.01 on a Form 8-K, or by any other method that is reasonably designed to effect broad dissemination of the information to the public.

In 2008, the SEC issued an interpretive release providing guidance on public disclosure via an issuer's website. In determining whether such disclosure is considered public under Regulation FD, the SEC noted that an issuer should consider whether: (i) the issuer's website is a recognized channel of distribution for such information; (ii) the posting of such information on the issuer's website disseminates the information in a manner that is readily accessible by the marketplace; and (iii) whether the marketplace has had enough time to digest and react to the information. See SEC Release No. 34-58288 (August 1, 2008), available at https://www.sec.gov/rules/interp/2008/34-58288.pdf

Acknowledging the shift in the manner in which investors consume information, in 2013, the SEC issued guidance related to Regulation FD disclosure though social media channels. Echoing its guidance in its 2008 interpretive release, the SEC emphasized that the social media outlet could be a recognized channel of distribution and that investors must be provided with notice of the specific social media outlet being used to disseminate the information. Notably, the SEC indicated that disclosure of material, non-public information on the personal social media account of an issuer's officer without advanced notice to investors that the social media account may be used for this purpose would not qualify as disclosure for the purposes of Regulation FD. See SEC Release No. 34-69729 Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: Netflix, Inc., and Reed Hastings (April 2, 2013). For further information, see Regulation FD, Social Media Practices and Public Companies Checklist, When Is the Issuer Implicated Under Regulation FD? Checklist, and Form 8-K Preparation for Reg. FD Disclosure, Filing Exhibits and Other Events.

REGULATORY TRENDS

Question 9: What are the major regulatory trends affecting sports companies?

Daily Fantasy Sports

In 2006, Congress passed the Unlawful Internet Gambling Enforcement Act (the UIGEA), regulating payment processing for online gambling and effectively making online gambling illegal. As a result, most online poker sites, such as Party Poker, were forced to close their U.S. operations. Curiously, Congress carved out an exception for fantasy sports declaring that they are "games of skill." This resulted in the creation of daily fantasy sports (DFS). Like traditional fantasy sports, DFS players draft teams of players. However, DFS compresses season-long contests into daily or weekly contests. Unlike traditional formats where the norm is leagues filled with friends and colleagues, DFS players generally pay a fee and compete against tens of thousands or hundreds of thousands of players globally for large cash prizes. This distinction has not been lost on the NFL. Roger Goodell, the commissioner of the NFL, stated that his number one concern is that DFS could damage the integrity of the game. Part fantasy sports and part gambling, DFS has exploded with millions of people participating and tens of millions of dollars in prizes awarded. With this sort of money changing hands, it was only a matter of time before regulators got involved.

Whether DFS is gambling is a controversial debate in jurisdictions across the United States. While Congress has yet to weigh in on the topic, state regulators have. As of January 24, 2018, DFS is legal in 18 states (Arkansas, Colorado, Delaware, Indiana, Kansas, Maine, Maryland, Massachusetts, Mississippi, Missouri, Ohio, New Hampshire, New Jersey, New York, Pennsylvania, Tennessee, Vermont, and Virginia) and classified as gambling that requires a gaming license in Nevada. South Dakota operates in a gray area as its attorney general has stated that it will not pursue indictments for criminal actions but would consider civil remedies.

As of January 24, 2018, there were active bills seeking to regulate and legalize DFS in 10 states (Connecticut, Florida, Georgia, Hawaii, Illinois, Iowa, Michigan, Nebraska, Washington, and Wisconsin) and failed attempts to legalize DFS in 13 states (Alabama, Arizona, California, Kentucky, Louisiana, New Mexico, North Carolina, Oklahoma, Oregon, Rhode Island, South Carolina, Texas, and West Virginia).

Gaming

As the states continue to regulate DFS, the logical next step would be to address the regulation of sports gaming within their borders. However, the Professional and Amateur Sports Protection Act of 1992 (PAPSA) has banned sports gaming nationwide, with the exception of a few states. Oregon, Delaware, and Montana had their existing sports lotteries grandfathered in, while Nevada is completely exempt and offers sports betting. Notably, PAPSA excludes dog and horse race gambling.

Despite such restrictions, the multi-billion dollar underground sports gaming industry (e.g., bookmaking operations and offshore websites) is operating free of any regulation or oversight. As shown by the publication of sports betting lines and point spreads on mainstream media outlets like ESPN, there is an obvious appetite among the general public for legalized sports gaming. Support for legalized sports gaming can also be found in state capitols as well. Several state legislators from California, Iowa, Missouri, New Jersey, and Rhode Island have introduced resolutions legalizing and regulating sports gaming in their respective states. Further, outside of the United States, sports gaming is highly regulated. In England, fans can place wagers through everything from mobile apps to stadium kiosks. Against this backdrop, PAPSA, at least in its current form, may no longer be appropriate, and Congress could potentially adopt a federal framework to allow states to regulate sports gaming.

If Congress were to take such an approach, it would have the support of Adam Silver, the current commissioner of the NBA. On January 24, 2018, in what could be a defining moment for sports gambling in America, the NBA formally requested the New York State Senate for a framework for the league to profit from the industry. The NBA is seeking one percent of every bet placed. Not content to restrict gaming to sportsbooks and casinos, the NBA wants lawmakers to allow for more widespread access to gambling. Currently, Article 13(f) of the Constitution and By-Laws of the NBA provides that the membership of a member or the interest of any owner may be terminated by a three-fourths vote of the NBA's Board of Governors if the member or owner "willfully permit[s] open betting, pool selling, or any other form of gambling upon any premises owned, leased, or otherwise controlled by the [m]ember or an [o]wner, except, subject to Article 8(a), for gambling activities that are lawful in the applicable jurisdiction and do not involve in any way, directly or indirectly, gambling with respect to any aspect of the [NBA's] games, events, property, players, or other personnel."

It soon may be necessary for Congress to address legalization of sports betting and adopt a federal framework for regulating it. On June 27, 2017, the United States Supreme Court granted certiorari and combined NCAA v. Governor of New Jersey (832 F.3d 389 (3d Cir. 2016)) and New Jersey Thoroughbred Horsemen's Association, Inc. v. NCAA, two cases regarding the constitutionality of PAPSA and the legalization of sports betting. The Court heard arguments on the combined case on December 4, 2017. The cases relate to New Jersey's efforts to legalize sports betting at casinos and racetracks. If the Supreme Court finds that PAPSA is unconstitutional, this would remove the largest obstacle to states' legalized sports betting efforts and allow Congress to work with the major sports leagues, states, and the casino industry to create a federal framework for regulating sports betting. The Supreme Court is expected to issue a decision in this case by June 2018.

Legalization of Medicinal and Recreational Marijuana

Several prominent former professional athletes have been advocating for the use of marijuana as a pain management tool over the past several years, arguing that it is safer and less addictive than the opioids commonly used by teams and players. This issue is particularly acute in the NFL, which is considered by many to be the most physically violent of the Leagues, and the one in which pain medication use and abuse has been widely reported. On November 11, 2016, a number of current and former NFL players published a letter to the NFL calling for the NFL to change its position on marijuana prohibition. This agitation, coupled with the growth in the number of states legalizing and regulating the use of marijuana, has forced the NFL and NFL Players Association (the NFLPA) to take note.

As of January 8, 2018, four states, which are home to seven NFL teams (Washington, California, Colorado, and Massachusetts), have passed laws permitting the recreational use of marijuana, while 11 other states, which are home to 17 NFL teams (Arizona, Florida, Illinois, Louisiana, Maryland, Michigan, Minnesota, Ohio, New Jersey, New York, and Pennsylvania), have passed laws permitting the medicinal use of marijuana. With 24 of the 32 NFL teams playing in states where medicinal and/or recreational use marijuana is legal, the NFLPA announced in November 2016 that it was actively studying the possibility of permitting active players to use marijuana for pain management.

Even if legal for medicinal or recreational purposes, the use of marijuana by current NFL players is still governed by the NFL Collective Bargaining Agreement (the NFL CBA), which has punishments ranging from enrollment in the NFL's substance abuse program without suspension for the first offense to a ten-game suspension for the fifth and each subsequent offense. The NFLPA has created a pain management committee, but George Attalah, the NFLPA's assistant executive director of external affairs, has acknowledged that marijuana use is still governed by the NFL CBA, which means that even if the NFLPA wishes to permit marijuana use, the players will have to bargain with the owners if they wish to have the league revise its marijuana policy.

Player Safety/Concussion Management

Brought to the forefront in part by highly publicized suicides of former NFL stars such as Junior Seau and studies related to Chronic Traumatic Encephalopathy by Dr. Bennet Omalu, litigation and legislative action related to concussion injuries and management has increased significantly in recent years.

The In re: National Football League Players' Concussion Injury Litigation class action settlement (the Concussion Settlement) became final on January 7, 2017, bringing an end to a nearly five-year litigation between the NFL and former NFL players, who accused the NFL of hiding the dangers of repeated head traumas and the link to brain disease. See NFL Concussion Settlement Website at https://www.nflconcussionsettlement.com.

In 2009, Washington passed the Zachery Lystedt Law, becoming the first state to pass legislation regulating concussion protocols for youth sports. The Zachery Lystedt Law prohibits youth athletes from returning to the field without a licensed healthcare provider's permission. Since then, every other state and Washington D.C. has passed some form of legislation regulating concussion protocols for youth sports.

Congress has long been an advocate for former NFL players and has conducted numerous hearings investigating the impact of concussion injuries and efficacy of concussion management protocols. In July 2014, United States Representative Lois Capps from California introduced H.R. 5324, titled the Supporting Athletes, Families and Educators to Protect the Lives of Athletic Youth Act (Safe Play). The purpose of Safe Play is to mandate formal concussion management plans in public schools, including parental notification of suspected concussions, academic accommodations for students who have suffered a concussion, and no further participation in sports pending written authorization from a healthcare provider. As of the time of this writing, Safe Play has yet to be enacted.

Loss of Tax-Exempt Bonds for Stadium Construction and Ancillary Development

For decades, stadium construction and ancillary development costs have been financed by the public, most commonly through the issuance of tax-exempt bonds. See Tax-Exempt Municipal Bonds Under the Securities Laws. Recently, however, public scrutiny over the use of public funds for the benefit of private organizations has increased, and local and federal legislators have introduced bills prohibiting the use of tax-exempt bonds for stadium construction. In March 2016, Congressman Steve Russell of Oklahoma introduced the No Tax Subsidies for Stadiums Act, which would prevent professional sports franchises and any for-profit entities from obtaining tax-exempt financing for sports stadiums and for-profit entertainment arenas. Although the 2016 version was never voted on, Congressman Russell introduced a revised version to the House of Representatives in February 2017.

Despite the potential prohibition of tax-exempt public financing for stadium construction and ancillary development, other alternatives have developed for sports teams seeking new facilities. Investment banks, such as Goldman, Sachs & Co. (Goldman Sachs), have stepped into the role of stadium construction financier. To finance the construction of Levi's Stadium in Santa Clara, California, in lieu of a municipality providing tax-exempt bonds, Goldman Sachs used the proceeds of a construction loan raised from private investors to create a tax-exempt public authority to build and own the stadium. By using a tax-exempt public authority to sell personal seat licenses and sponsorships, Goldman Sachs helped the San Francisco 49ers avoid millions in taxes on those sales.

COMMERCIAL TRENDS

Question 10: What are the major commercial trends affecting sports companies?

OTT Content and Media Rights

Most sports organizations generate their primary source of revenue through the sale of broadcasting and media rights. Traditionally, a broadcaster purchases these rights and then earns fees from selling them to distributors (which, in turn, charge subscriber fees to consumers) and selling air time to advertisers. The key to the system is the traditional pay-TV (e.g., cable or satellite) bundled package in which the consumer has only a limited number of bundles of channels from which to choose, including potentially a large number of channels that the consumer does not want, but for which the consumer will nevertheless pay by virtue of the bundling.

However, the proliferation of cable cord cutting (i.e., consumers ending their traditional pay-TV subscriptions) threatens to disrupt the traditional pay-TV model. There now exists over-the-top (OTT) content, which is audio, video, and other media transmitted via the Internet without multiple-system operators or other multichannel video programming distributors controlling or distributing the content. OTT services, such as SlingTV, Playstation Vue, DirecTV Now, FuboTV, Hulu and YouTube currently offer live television content. Given affordable high-speed Internet, and Internet-connected devices, the traditional pay-TV model continues to erode, with the steady decline of ESPN subscribers serving as the strongest evidence of this. Additionally, non-traditional online outlets such as Twitter, Facebook, and Amazon have shown the potential to broadcast sporting events, serving as further evidence of how the sports media industry is evolving. Against this backdrop, content owners, broadcasters, distributors, and other media companies (collectively, the Media Companies) are investing heavily in their OTT platforms, potentially paving the path eventually for so-called a la carte programming (i.e., a system in which the consumer pays for and receives only those channels he/she desires).

Whereas at one time it seemed that any sports content could fetch a huge rights fee for the sports property, the Media Companies are now focusing on higher value content and rejecting the lower value content with lower revenues and greater uncertainty. The changing focus of the Media Companies on higher value content has created classes of haves and have-nots in the current media environment (e.g., the Big Ten's latest increase in its media rights deal against the dramatic decrease in Conference USA's media rights deal).

Once the Media Companies have fully accepted OTT (whether willingly or as a result of increased market forces), they must figure out an appropriate monetization model to maximize revenue. The traditional subscription model employed by MLB, the NBA, and the NHL through their season pass options on their websites and mobile apps is beneficial to both subscribers and the Media Companies because it offers subscribers access to the content at a fixed cost while providing predictable revenue streams for the Media Companies. However, the principal challenge with this model is the upfront costs associated with amassing a critical mass of subscribers and content. Another potential model is the rental/purchase model (i.e., pay-per-view). This can be an especially attractive model for newer movies or television shows and live sporting events, as consumers value such content at a premium. Although currently provided free of charge through CBS's OTT platform, the NCAA Men's Division I Basketball Tournament, one of the marquee events in sports, could be ideal for the rental model. The main drawback to this model is the lack of a predictable revenue stream as compared to the subscription model. Additionally, as content ages, consumers are less likely to pay a premium for one-time rentals or purchases. This is especially true for sporting events, where consumers want to watch the event live before the outcome is known.

Regardless of which model, or combination of models, the Media Companies decide to pursue, determining how to incorporate advertising revenue will be critical to the viability of their OTT platforms. Because OTT content is provided directly to consumers, who can be tracked by IP address, one of the most valuable revenue streams available to the Media Companies is the vast amount of consumer data collected. The Media Companies can generate reports that can provide advertisers with desirable consumer analytics, including content and usage metrics. For additional information, see Media & Entertainment Industry Practice Guide.

Consumer Analytics

Since the early days of the box score, statistical analysis has long been a mainstay in the sports world. This movement has been accelerated by the introduction of data-driven sabermetrics, made particularly famous by the Oakland A's front office led by Billy Beane, who started using statistics and predictive modeling in the late 1990s to build winning teams at a fraction of the costs spent by larger market teams. More recently, sports companies have been increasingly using customer statistics and behavior to drive the customer experience. Through data mining and analysis, sports companies increase customer loyalty, deliver targeted messaging to specific customers, and identify the customers most likely to leave and develop responses to retain them.

With customers more connected than ever, sports companies are trying to stay in front of customers any way they can. Mobile devices particularly present a unique opportunity to stay in front of customers. Teams are building smart arenas designed to enhance the fan experience, from providing mobile ticketing and cashless commerce to technology ushering fans to their seats. For example, The KeyBank Center in Buffalo, New York has integrated technology that provides fans with real-time wait times for nearby concessions and restrooms with gradient spectrums ranging from green to red by analyzing how many people are in a given area and determining whether they are passing through or waiting in line. While aimed at enhancing the fan experience, the technology also provides the Buffalo Sabres with valuable detailed analytics on consumer behavior so that the team can identify and address inefficiencies.

Stadium Construction and Ancillary Development

As previously discussed, due to increased scrutiny over the use of public financing for stadiums, public subsidies in the form of tax-exempt bonds has decreased. As a result, professional sports franchises and universities have become subject to higher interest rates in the bonds market. A difference of even 3% between the tax- exempt bond and an interest-bearing bond could equal tens, if not hundreds, of millions of dollars in interest payments. With the public and political appetite for stadium construction lower than it has been in the past, public funds available for stadium construction have shrunk, and the cost of ancillary development opportunities are increasingly pushed onto the franchises and universities. The increased financial risk to the professional sports franchises involved with stadium construction and ancillary development comes with the benefit of greater control over both the fan experience and potential revenue generation.

esports

Electronic sports (esports) are a form of competition involving multiplayer video gaming played for spectators, typically by professional gamers. Most commonly, esports takes the form of team-based games played in leagues or tournaments, culminating in one final event. There are three main formats: first-person shooter (where the player is the protagonist), real-time strategy (a sub-genre of strategy video games), and multiplayer online battle arena (where the player controls a single character competing against other characters).

According to Newzoo, revenue in the esports economy was projected to reach $696 million in 2017 and top $1.5 billion in 2020. In 2017, $266 million was expected to be spent on sponsorships, $155 million on advertising, $115 million on partnership deals, $95 million in media rights, and $64 million on ticket sales and merchandise.

While some purists might not consider esports (i.e., competitive video game playing) to technically be a sport, perhaps because of its name (along with the strong interest from traditional sports properties and their owners) there is no question that today esports is considered part of the sports industry. And no one can deny the popularity of esports. Over 43 million unique users watched the 2016 League of Legends Championship (12 million more than the 2016 NBA Finals).

Esports investors include, among others in the traditional sports industry, Golden State Warriors co-owner Peter Guber, Memphis Grizzlies owner Steve Kaplan, New England Patriots owner Robert Kraft, Milwaukee Bucks owner Marc Lasry, and the Philadelphia 76ers. With esports already on the verge of becoming a billion-dollar industry, it is one of the fastest growing and most exciting areas of the sports industry. However, the rapid growth of esports has outpaced regulation and organization in the esports industry. Currently, the esports industry is comprised of multiple, unaffiliated leagues and tournaments, with little standardized regulation or coordination. As a result, going forward there may be some consolidation of properties, leagues, and tournaments with a more traditional, unified governance structure similar to the existing professional sports leagues. In addition to regulations from the internal governance structures of esports leagues, as esports continue to grow, it is possible that lawmakers will seek greater oversight of the industry and additional ways for governments to tap into the growing revenues generated by esports.

While not meant to be an exhaustive list, the following areas are ripe with opportunities in the near future: governance and regulatory framework, media/broadcasting rights, intellectual property and technology, mergers and acquisitions, sponsorships, and financing and capital raising.

PRACTICE TIPS

Question 11: What practice points can you give to lawyers working with sports companies?

Lawyers working in the sports industry must become experts not only in the industry in general, but in the specific team, league, technology, or market which they wish to represent. The same type of transaction may have vastly different market terms and expectations based on where and to whom it is directed.

The sports industry is unique because of the zealousness of the fans. There are not many other industries where so many people hold passionate opinions about business and legal outcomes in which they hold no personal financial stakes. One benefit of this is that successful sports business and legal initiatives can enjoy significant popular support. But, a challenge is that many transactions in the sports industry must be structured not only with an eye to the invested parties, but also to the public at large. Politics and public relations play a far larger role in drafting transactional documents in the sports industry than they do in most others, especially if the transactions include a component of public financing, such as stadium and arena development.

In addition to any federal and state laws, representation of sports teams (professional and amateur) is further complicated by the regulatory framework of their respective governing authorities. As a result, sports teams necessarily have to deal with additional rules and regulations as compared to other types of organizations. For example, the governing authorities of professional sports teams almost all have debt and transfer restrictions. As such, it is paramount for attorneys representing sports teams to understand the subtleties of not just the federal and state laws but also the regulatory framework in which their clients operate.

Patrick G. Quick
Partner, Foley & Lardner LLP

Patrick G. Quick practices corporate law, with an emphasis in securities law compliance, acquisitions, and takeover defense. He regularly counsels several public companies concerning compliance requirements and governance matters and has participated in initial and other public offerings for various entities.

His sports practice includes complex corporate transactions involving the unique interaction among sports teams, U.S. regulators, professional leagues and shareholders (both public and private); along with sports team franchise sales and ownership transfers, including public stock offerings; and equity capital raises, investments and joint ventures, used among other reasons to fund ancillary development. He is a member of the firm’s Transactional & Securities Practice Group and Sports Industry Team.

Representative sports matters include the following, among others: (i) representing Senator Kohl in the sale of the Milwaukee Bucks, (ii) representing Rangers Baseball Express in its acquisition of the Texas Rangers, (iii) representing the Ricketts family in its acquisition of the Chicago Cubs and Wrigley Field, (iv) representing the Milwaukee Brewers in the sale of the club to Mark Attanasio and (v) representing the Green Bay Packers.

Kevin R. Schulz
Partner, Foley & Lardner LLP

Kevin R. Schulz is co-chair of Foley’s *Chambers*-recognized Sports Industry Team and his practice focuses in the areas of mergers and acquisitions (M&A) and commercial transactions. He has extensive experience in the sports industry, where he has represented and counseled a number of clients, including professional sports teams, colleges, sponsors, owners and acquirers of professional sports teams, a professional sports league, sports technology companies, and media companies.

Representative sports matters include the following, among others: (i) representing Senator Kohl in the sale of the Milwaukee Bucks, (ii) representing Guggenheim Baseball Management in its record-setting acquisition of the Los Angeles Dodgers, (iii) representing one of the investors in the investment group that acquired a majority interest in Swansea City of the English Premier League, (iv) representing the University of Oregon in its multimedia rights deal with IMG, (v) representing the University of Miami in the naming rights deal for its basketball arena, (vi) representing Syracuse University in its multimedia rights deal with IMG, (vii) representing Rangers Baseball Express in its acquisition of the Texas Rangers, (viii) representing the seller of a significant minority interest in the Cincinnati Bengals, (ix) representing the Ricketts family in its acquisition of the Chicago Cubs and Wrigley Field, (x) representing the Milwaukee Brewers in the sale of the club to Mark Attanasio, (xi) representing professional sports teams in their media rights deals, and (xii) representing Hi-Rez Studios in its esports video streaming deal with Microsoft.

Mr. Schulz also serves the role of outside general counsel for a number of private companies, routinely advising them in connection with a variety of commercial matters.

Jeremy Polk
Partner, Foley & Lardner LLP

Jeremy Polk is a business lawyer with Foley & Lardner LLP where his experience in the sports industry includes acquisition and working capital financing for sports franchises and their owners. He is a member of the Finance & Financial Institutions Practice and the Sports Industry Team.

Representative sports matters include the following, among others: (i) representation of the Green Bay Packers in connection with their bank and other credit facilities, (ii) representation of the successful bidders for the Texas Rangers Baseball Club in connection with their acquisition financing, (iii) representation of the Milwaukee Bucks in connection with the NBA League-wide credit facilities, (iv) representation of the Milwaukee Brewers Baseball Club in connection with their bank credit facilities, and (v) representation of the seller in connection with the sale of a significant minority ownership interest in the Cincinnati Bengals NFL franchise by the estate of Austin E. “Dutch” Knowlton.