Institute For Policy Innovation

Issue Brief

Protecting Secondary Markets for Tickets

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Synopsis

The secondary ticket market emerged naturally as a form of spontaneous order. Consumers and the economy as a whole benefit from these new markets. So as a small number of dominant players attempt to control these new markets and deprive consumers of the benefits of more efficient markets, it is appropriate for governments to enact reasonable policies to protect the rights of participants in secondary ticket markets.

Introduction

One of the most transformative impacts of the Internet has been its facilitation of markets. The Internet has made markets more efficient by cutting out middlemen and gatekeepers, by extending the reach of narrow and regional markets, by transcending artificial political boundaries, and even by facilitating the creation of entirely new markets.

An excellent example of a market extended and made more efficient by the Internet is the market for unused tickets. It has always been true that ticket holders are sometimes unable to attend an event for which they have purchased tickets, or for some reason choose not to go. Their options for salvaging the value of their tickets were limited: They could advertise them in the local classifieds, spend time on the phone calling friends and relatives, or offering them at the last minute for a fraction of face value. Ticket holders always believed the tickets were theirs to sell or to give away as they saw fit, and the market as it existed validated their assumption. Whoever presented the tickets gained admission to the show or to the game without any hindrance.

The Internet has facilitated a dramatically expanded market for unused tickets. Now, if you know you can't use tickets you've purchased, you can list them on an online exchange and draw upon an incredibly enlarged pool of possible purchasers, who in turn now have dramatically increased choices and options for their ticket purchases. It's fair to say that these on-line exchanges have revolutionized the ticket marketplace, and the evidence suggests that these new exchanges have delivered value both to consumers and to the ticket issuers themselves.

Aftermarkets that facilitate the exchange of goods after their first sale, such as garage sales, most securities exchanges, and ticket exchanges are called *secondary markets.*

The Secondary Ticket Market

Importance of Secondary Markets

Secondary markets are a significant source of economic activity. All securities markets, of course, are secondary markets. In many markets, such as for automobiles, the size of the secondary market is roughly equal to and often exceeds the size of the primary market for new vehicles. In the aircraft market, the secondary market is usually larger than the market for new aircraft, and in the housing market, the secondary market is roughly 12 times the size of the primary market for new homes.[1]

The economy clearly benefits from both new and used goods changing hands. In every market where there is a willing buyer and seller, economic value is added for both buyer and seller. Society at large also benefits due to the *allocative efficiency* produced by the transaction.[2]

Secondary markets are of particular benefit when public or private market restrictions have distorted a competitive marketplace, which will become a relevant point to this discussion.

Secondary Markets as Spontaneous Order

It should not surprise us that secondary markets exist, and that they seem to naturally spring out of thin air. The basis of the belief in limited government and free markets is recognition of the principle of spontaneous order and the ability of people to self-organize and to self-govern. Free people naturally create markets and organize themselves for the betterment of the community and for economic efficiency. We don't need governments to do this for us. Government doesn't create markets—markets happen naturally. We are not surprised when a market naturally, spontaneously appears "out of nowhere"—that's simply an example of natural self-organization of people into markets. By contrast, our suspicions *are* aroused when someone tries to eliminate or monopolize a naturally occurring market.

A Win-Win for Consumers and Venues

The secondary ticket market is a great example of a natural secondary market. People have always given away or resold tickets that they didn't want or couldn't use. It's the kind of natural market and self-organization that it is our duty to preserve, if we believe in markets, spontaneous order, self-organization, and limited government.

And secondary markets create greater economic efficiency for all parties involved. A ticket never moves into the secondary market in the first place unless the original vendor has been paid their asking price, so the originator is not harmed. Further, it is in the interest of the original vendor that the seat be filled for any number of reasons, including concessions and souvenir sales.

And the restaurants and other businesses that surround the venues also benefit from having those seats sold. This is worth mentioning because in many case it was this very downstream economic activity that was used to sell taxpayers on the benefits of subsidizing many of these venues in the first place.

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1. Mayo, John and Wallsten, Scott, "Secondary Markets: The Quiet Economic Value Creator," Georgetown University, McDonough School of Business, December , 2011. This discussion relies heavily on the Mayo and Wallsten paper.

2. Ibid.

It's clear that the secondary ticket market has resulted in benefits to consumers. In 2010, average ticket prices on StubHub.com, the largest secondary ticket seller, dropped by 2.5 percent while at the same time sales grew 26 percent.[3]

According to a study by *Sports Business Journal*, "Since 2007, average ticket sales prices on StubHub, regardless of sport, have fallen each year, dropping from $112 per ticket in 2007 to $104 in '08, $94 in '09, $84 in '10 and $82 [in '11]."[4] The study further found that the vast majority of sports tickets moving on StubHub sold for below face value, which suggests further benefits to consumers and undermines the image of the secondary market consisting mainly of "scalpers" raking in huge profits from the resale of tickets.

All these benefits to consumers are gains to efficiency alone. They come at no expense—they are "free," because, again, the original vendor of the ticket already received the original asking price before the ticket ever entered the secondary market.

It seems like a win-win for everyone involved. So what's the problem?

Why the Controversy over Tickets?

New Internet secondary marketplaces for tickets, most notably eBay, StubHub (a subsidiary of eBay) and TicketsNow (a subsidiary of Ticketmaster), have revealed and unlocked the economic value that was trapped in the poor design of the primary ticket market pricing model, and hidden by the lack of an efficient secondary market.

A functioning market establishes prices. When there is no functioning market, people can only guestimate what prices should be. But a functioning market determines prices and value on a dynamic, real-time basis.

Until the appearance of efficient secondary ticket markets, there was no way to broadly determine the value of a ticket beyond the arbitrary price set by the primary seller. But what if the primary seller either overpriced or underpriced their tickets? How would they even know?

The new online ticket exchanges have revealed and unlocked this value. And it hasn't gone unnoticed. There's a lot more money in the secondary ticket market than most people thought. Today, the secondary ticket market is estimated to be in excess of $25 billion worldwide; in fact, the secondary market represents as much as 20 percent of gross ticket industry revenues.[5]

In reaction, having learned from the new secondary markets, the primary ticket vendors have begun to experiment with different pricing models, including dynamic pricing, designed to reduce the amount of arbitrage they were leaving on the table. That's good.

But the primary ticket industry has also reacted to these new secondary ticket exchanges in a more ominous way.

3. http://www.sportsbusinessdaily.com/Daily/Issues/2011/01/Jan-17/Facilities/Secondary-tix.aspx

4. Bill King and Eric Fisher, "Second Thoughts," *Sports Business Journal*, October 24, 2011.

5. Joris Drayer, "Making a case for the integration of the primary and secondary ticket markets for professional team sports in the United States," *International Journal of Sports Marketing and Sponsorship*, April 2011.

The Empire Strikes Back

Guess who doesn't like seeing the revenue from the secondary ticket marketplace escape their clutches? The near-monopolists who control the primary ticket market—event producers, the venues themselves, some (but not all) major sports franchises, and the major primary ticket issuers—most notably (and almost exclusively) Ticketmaster. They've grown tired of watching companies like StubHub earn revenue by facilitating a much more efficient secondary ticket market, and they want in. But not only do they want to be a part of this secondary market—they're doing everything they can to quash the secondary market.

Teams and venues also don't like tickets to their events showing up at far below the original price. When the original price of a ticket was $20 but it shows up on StubHub for $6, the teams and venues, perhaps understandably, see that as bad PR, though we've established that they suffer no financial loss.

So the primary ticket issuers, in coordination with teams and venues, have begun dramatically restricting the transferability of tickets, in many cases making an outright ban on transferring tickets part of the terms of sale, and otherwise are making it difficult or impossible for ticket holders to exchange their tickets on the website of their choice through practices like restricted paperless ticketing.

The problem is not so much the "paperless" part; it's the "restricted" part. Ticket agencies are restricting resale, limiting the ability of a ticket purchaser to give or donate his ticket to another party, and are even in some cases outright banning the resale of tickets.

These are all forms of *excluding rivals from competition*, which is an attempt to extend dominance of the primary market into dominance of the secondary market.[6]

The result of these restrictions reduces consumer choice, degrades the product that consumers purchase, and causes harm to competition, which forces consumers to either pay higher prices, enjoy less value, or (most likely) both.

Ticket agencies claim to be doing this to protect consumers from the harm supposedly posed by "scalpers" and from the occasional counterfeit ticket. But what it's really all about is not being satisfied with controlling the primary ticket market and wanting to also gobble up the secondary market.

> Ticketmaster is "now in a position to control both the primary and secondary levels of the market" says Marianne Jennings, a business professor at Arizona State University who has studied the ticket market. Innovations like paperless tickets "are often touted as being in the best interest of consumers, but in reality, primary ticket sellers have been trying to get rid of brokers and maximize their profits for 30 years."[7]

Of course, proponents of market economics believe it's legitimate to attempt to maximize profits, but these attempts must be made *within* functioning marketplaces, not by conspiring to destroy or subsume functioning markets.

And restricting the sale of a good after its first sale is clearly understood in legal and economic terms to work against secondary markets. Such steps restrict the *free alienability of goods,* or the capacity of a good to have its ownership transferred. In the intellectual property world, the first sale doctrine ensures that the copyright of the creator or publisher cannot be used to restrict resale of the covered good, and patent exhaustion provides a similar guarantee that a patented product can also be resold. These legal regimes have developed over time in recognition of the value of secondary markets.

6. James D. Hurwitz, "Restrictive Paperless Tickets," American Antitrust Institute, January 20, 2012, p. 7.

7. Ibid., 65.

The attempt by the major players in the primary ticket market to quash the secondary ticket market is contrary to the best interests of consumers and to the overall economy. It works against economic efficiency and against the rights consumers have historically enjoyed. It is bad policy, and those who believe in free markets and consumer choice should view this development with suspicion and concern.

The "Scalpers Lobby"

Anyone arguing that a vibrant secondary ticket market is important and defending consumers' interest in transferability will immediately be accused of fronting for the "scalpers lobby." This bit of political rhetoric is designed to slander defenders of markets by suggesting that they are fraternizing with the denizens of dark corners who are engaged in a shameful business. So let's take this charge head-on.

In the ticket business, so-called scalpers function as *speculators*. They serve exactly the same function that speculators serve in securities markets: They are willing to absorb higher risks than most market participants in pursuit of potentially higher rewards.

So is speculation good or bad? While the common perception, based on listening to talking heads in the news, is that speculation is bad, market-oriented economists are almost unanimous that "speculation makes markets both more efficient and more liquid by playing a vital role in causing today's prices to reflect future conditions and, hence, in causing consumers and producers today to act in ways that are consistent with future reality."[8]

In fact, in 1960 future Nobel Prize winning economist Milton Friedman wrote a paper entitled "In Defense of Destabilizing Speculation."[9] In Friedman's paper, he speculated (apologies for the pun) that the concept of speculation had become negatively associated only because of comparisons with gambling, and from there the idea gained currency "much as a rumor does—each man believes it because the next man does." Friedman argued that speculation was helpful precisely because it destabilized inefficient markets by making them more efficient, and argued that, when there are losses from speculation, the losses accrue only to the speculator.

Ludwig von Mises elaborated: "The influence of speculation cannot alter the average level of prices over a given period; what it can do is to diminish the gap between the highest and the lowest prices. Price fluctuations are reduced by speculation, not aggravated, as the popular legend has it."[10]

It's clear that anyone who claims to believe in free markets and economic efficiency will conclude that "scalpers" actually play a constructive role in a secondary ticket market, and that when laws and regulations restricting scalping are enacted, they are enacted for unjustifiable (or at least non-economic) reasons.

It's also worth mentioning that, in many jurisdictions, the penalty for stumbling over anti-scalping laws is grossly disproportionate with the supposed harm of the offense, as Joe Carr, a visitor from Minnesota, found out when Washington DC police threw him in jail for the offense of trying to unload his tickets to a Twins/Nationals game in June of 2013.[11]

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8. Boudreaux, Donald, George Mason University, http://cafehayek.com/2008/07/nonsense-on-spe.html

9. Friedman, Milton, "In Defense of Destablilizing Speculation," *Essays in Economics and Econometrics,* edited by Ralph W. Pfouts, Chapel Hill: University of North Carolina Press, 1960, pp. 133-141.

10. von Mises, Ludwig, *The Theory of Money and Credit,* New Haven: Yale University Press, 1953, p. 253.

11. Joe Carr, "Welcome, baseball fan. Go directly to jail," Washington Post Opinions, June 21, 2013.

Who's On the Other Side?

So much for the "scalpers lobby"—who's on the other side of the issue, trying to subsume the secondary ticket market?

It's primarily Ticketmaster, along with some teams and venues. They covet the revenue that they see going to others in the secondary market, and they want to be able to establish price "floors" in the secondary market once they control it so that venues are not embarrassed by low resale prices.

It's important, however, to note that some venues, teams and leagues have come to recognize the value of partnering with an effective secondary marketplace instead of resenting it. In fact, just last December Major League Baseball renewed its five-year contract with StubHub, and an impressive number of teams work with StubHub as their secondary market partner.[12]

Derrick Hall, president and CEO of the Arizona Diamondbacks, sees the secondary market as an opportunity, not a problem. "When you finally realize that the secondary market is actually an incentive to sell season tickets—which is what we're all in the business of doing—then you embrace it and use it," Hall said. "We don't hit our numbers without StubHub."[13]

But don't underestimate the lobbying power of those who control the primary ticket marketplace and who covet the revenues of the secondary market. It turns out that free tickets to major sporting events and invitations to the owner's suite are powerful incentives.

Major sports franchises have long mastered the art of getting favors from politicians. Almost no major new sports venue has been built in the last 20 years without substantial taxpayer subsidies in the form of tax breaks, loan guarantees, dedicated sales taxes and outright state and local tax revenue. The venues and the teams themselves have learned how to get sweetheart deals through the political process.

When it's the "scalpers lobby" versus major sports franchises, for even many supposedly free market elected officials, protecting the free market is not as important as seats for the big game.

The Other Side's Arguments

Of course, the venues and major ticket agencies claim that their move to restricted tickets is designed to protect consumers. Placing stringent restrictions and even outright bans on transferring tickets is necessary, they claim, to protect fans from counterfeit tickets and to prevent automated software "bots" from buying up all available tickets when they are first placed up for sale.

These may well be legitimate concerns in the ticket industry, but there are other ways to deal with these issues short of subverting the secondary market. Major secondary brokers such as StubHub offer protection against counterfeit tickets and cancelled events. Frankly, the economic benefits of a vibrant secondary market are so demonstrable that they more than offset the relatively small risk of the occasional counterfeit ticket.

Venues also claim they are protecting "real" fans from scalpers and thus from paying inflated prices for events. We've already shown that so-called scalpers probably provide a net benefit to the ticket market, as opposed to harming the market, and that the net effect of secondary markets is to provide greater access to tickets for consumers. The evidence demonstrates that what is in the fans' best interest is a vibrant secondary market where they can both procure tickets and transfer tickets they've already purchased without needless interference from the venue.

12. http://www.stubhub.com/partners/

13. King and Fisher, ibid.

What About Property Rights?

Ticket purchasers clearly believe that when they buy tickets, they can keep them, give them away, or resell them as they choose—in short, that they own the ticket. In a recent Penn Schoen Berland Research poll of 1,000 ticket purchasers, 90 percent believed they have the right to resell or transfer the tickets in any way they choose.[14]

And court decisions, going all the way back to a 1906 California Supreme Court decision and up through 2003's *Arlotta v. Bradley Center*, have generally agreed that reselling tickets at a profit is neither illegal nor harmful.[15]

Nonetheless some venues claim that their tickets are a *license*—that the ticket is *not* the property of the buyer, and that the venue can attach whatever conditions they choose as terms of the license, because (they argue) the ticket remains the property of the venue.

But arguing that the ticket is a license and not real property doesn't actually change anything in this argument. It's just as wrong to use licensing as a means of destroying a secondary market as it is to use some other tool.

More importantly, such license claims are *contracts of adhesion*, which are defined as contracts in which one side has all the bargaining power and the consumer cannot obtain the good or service without agreeing to all of the terms. Courts frequently refuse to enforce such contracts because the results of contracts of adhesion are often so imbalanced in favor of one party over another that there is a strong implication that it was not freely bargained.

For instance, it is likely that the terms on the back of the ticket absolve the venue from any liability resulting from injury in the course of attending the event. But venues are still routinely sued when such injuries occur, and frequently lose or settle such suits.

We would argue that *the consumer belief and expectation that the tickets they purchase are theirs to sell or give away is a reasonable expectation,* and that the novel condition is the argument that they are not.

Even if we accept the argument, contrary to all consumer experience and expectation, that a ticket is a license rather than real property, such licenses are very weak, and using licensing in this way to attempt to defeat secondary markets and deprive consumers of choice is an unjustifiable use of licensing.

Finally, recalling our earlier discussion of the first sale doctrine and patent exhaustion in the realm of intellectual property, those precedents should probably provide some guidance in the secondary ticket market as well when primary vendors claim an IP right to the ticket as a license.

It's Not the Technology; It's the Intent

It's important to distinguish between harmful economic behavior and the technology employed. Technology is neutral—it's what we do with technology that makes it either useful or harmful.

So there's nothing wrong with selling tickets on-line, and there's nothing particularly wrong with the concept of paperless tickets (although the departure from paper tickets obviously makes tickets marginally less easily transferrable).

There are even reasonable terms, conditions and restrictions for venues to place upon ticket purchasers. Obviously the ticket is not an absolute right to attend an event regardless of the holder's behavior in the venue or degree of intoxication.

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14. Survey commissioned by the Fan Freedom Project; cited by Hurwitz, "Restrictive Paperless Tickets" American Antitrust Institute, January 20, 2012, p. 39.

15. 149 Cal 79, 84 P.766 (1906). See also *Arlotta v. Bradley Center,* 349 F3d 517 (7th Cir. 2003)

But as venues, promoters and ticketing companies increasingly try to extend the terms and conditions for a ticket beyond those reasonable and necessary for the first sale of those tickets in order to eliminate or monopolize the secondary market, it's important for government to step in and clearly define the rights of ticket purchasers to participate in secondary markets.

What's the Solution?

Because of the demonstrable value to consumers and to the overall economy, it is appropriate for governments to protect these secondary markets by limiting the venues' attempts to improperly extend their fine-print restrictions so as to quash secondary markets. There are two clear consumer expectations regarding tickets that it should be reasonable to reflect in state regulation and legislation:

- Ticket purchasers have an unconditional right to transfer, sell, give, or donate tickets to whomever they please, and
- Ticket purchasers may employ whatever means or exchange they wish in order to facilitate such transfers.

Conclusion

The secondary ticket market emerged naturally as a form of spontaneous order. Consumers and the economy as a whole benefit from these new markets. So as a small number of dominant players attempt to defeat these new markets and deprive consumers of the benefits of more efficient markets, it is appropriate for governments to enact reasonable policies to protect the rights of participants in secondary ticket markets.

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