Major League Baseball's Salary Arbitration: A Homerun ADR System

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Baseball is the second most-watched sport in the US (tucked behind American football and in front of basketball) and the seventh most watched sport in the world. Major League Baseball ("MLB") is the American professional baseball organization and the oldest of the major professional sports leagues in the US and Canada.

Unlike their counterparts, baseball players make insurmountably more money than any other sport because they have a stable union, and there's no maximum limit amount on the money they can earn; and unlike the NBA (professional basketball) and the NFL (professional American football), baseball has no salary cap, nor is player compensation tied in any way to overall league revenues. Under virtually every previously conceived circumstance, MLB contracts are fully guaranteed. For instance, last year the Los Angeles Angels gave Mike Trout a 12-year, USD 426.5 million contract extension – all of which is fully guaranteed. So how does the MLB maintain the highest paying sporting contracts whilst simultaneously avoiding disputes?

History of the System

The origins of salary arbitration are rooted in the reserve system that was created at the inception of baseball. When professional baseball was born in the 1870s, players were held to one-year contracts; this allowed them to switch teams continuously. As a result, a handful of the team owners made a

“gentlemen’s agreement” that would allow each owner’s team to protect five of their own players. These players became “reserved” to their current team and out of reach of other teams.

By the 1880s, this reserve system disseminated to every team in the league and each player had a reserve clause inserted into their contract, which bound the player to the original team they had signed with, preventing the player from leaving the team until their retirement. In essence, whichever team the player signed with originally, became their home for the rest of their career.

The reserve system first came to a legal battleground in 1922 during the case of *Federal Baseball Club v. National League of Professional Clubs* (the “FBC case”). In the FBC case, the US Supreme Court created an antitrust exemption for baseball. According to Chief Justice Holmes, baseball was exempt from the antitrust laws – which are statutes developed by governments to protect consumers from predatory business practices and ensure fair competition – because they did not constitute interstate commerce. Therefore, baseball did not fall within the scope of the Sherman Act, which outlaws every contract, or conspiracy in restraint of trade, and any monopolization attempted monopolization, or conspiracy to monopolize. Thus, the US Supreme Court upheld the reserve system.

The issues revolving around the reverse system were once again brought into play in 1972 in the case of *Flood v. Kuhn* (the “Flood case”), in which Curtis Flood attempted to bring an antitrust claim against the MLB for the reserve system. However, the court upheld the decision of the FBC case and ruled that Congress had several opportunities to abolish baseball’s antitrust exemption but choose not to do so. As a result, the court determined that the reserve system was acceptable.

With all the problems that the reserve system created, the players – through the assistance of the National Labor Relations Board – developed a union bargaining status and created a salary arbitration provision with the team owners. Shortly after the decision of the Flood case, a new Collective Bargaining Agreement ("CBA") was signed. The CBA created a process for salary arbitration from the fragments of the reserve system.

The Salary Arbitration System

Baseball's salary arbitration is significantly more different than that of conventional arbitration used in labor negotiations. The distinctiveness of salary arbitration in baseball comes from the final offer format, which is referred to as the high/low format. The high/low format means that each party (the player and the team owner) submits a salary proposal to an arbitrator. Subsequently, the arbitrator must choose either the amount proposed by the player or the amount proposed by the team owner. The arbitrator makes their decision based on a set of evidence which is provided by either party pursuant to the criteria outlined in Article VI (F)(12) of the CBA.

As per Article VI (F)(12)(a) of the CBA, the following evidence may be introduced in the arbitration hearing:

- Quality of the player's contribution to the team during the past season including, but not limited to, the player's overall performance, special qualities of leadership, and public appeal;
- The length and consistency of the player's career contribution;
- The player's record of previous compensation and comparative baseball salaries;
- The existence of any physical or mental defects on the

part of the player; and

- The recent performance record of the club including, but not limited to, its league standing and attendance as an indication of public acceptance.

According to Article VI (F)(12)(b) of the CBA, the following evidence is not admissible in the hearing:

- The financial position of the player and the team;
- Press comments, testimonials or similar material bearing on the performance of either the player or the team, and any recognized annual awards for excellence of performance;
- Offers made by either the player or the team prior to the arbitration;
- The cost to the parties of their representatives, attorneys, etc.; and
- Salaries in other sports and occupations.

In January of 1999, the CBA was modified to include Article XX. This Article set forth the requirement that reserved players with greater than three years, but less than six years of service, may demand salary arbitration.

The Problems with the Salary Arbitration System

The provisions of the CBA leave an open space for problems that may arise between the players and the team. However, there are three issues that are quite prominent in the fundamentals of this system.

The High/Low Format

The first issue is rooted in the high/low format of the system. In this format, the arbitrator cannot reach a compromise or a middle ground for the offer; they must either

choose the player's salary proposition or the owners. Thus, owners believe this issue is the root of the extraordinarily high salaries in baseball.

If the team owner was to present an amount that is significantly low, the arbitrator will tend to favor the player and choose the higher amount. In the pursuit of preventing this from occurring, owners often present an amount that is higher than they would like.

The Effect on the Ongoing Relationship

The second issue is embedded in the evidence which both parties present and whether this may affect the ongoing relationship between the player and the team. Looking at Article VI (F)(12)(a) of the CBA which outlines the criteria for evidence that may be introduced throughout the proceedings, the team can essentially present evidence that may degrade the player and his accomplishments. However, since the player will likely be returning to the same team the following year, the team may tend to hold back sensitive information that may offend the player.

During an interview with a prominent arbitrator who handles the proceedings for the New York Yankees, most teams tend to hold back degrading and malicious information about some of their players, out of fear of the repercussions that may occur during the following year.

For instance, during the salary arbitration proceedings between the owner of the New York Islanders, a National Hockey League team, and their then goalie, the owner introduced humiliating evidence into the hearing about the goalie. The goalie felt so betrayed by his team and the whole process that he refused to return to the Islanders the following season. Thus, the goalie was traded because of his refusal to play, which was the direct result of the salary arbitration proceedings.

A Sense of Betrayal

The other major problem that occurs is what happens after either party wins. In the event the owner wins, the player may feel betrayed sensing they had played well in the previous season and that they are owed a salary increase. Thus, the player may avoid playing up to their full potential during the following season as a point of resentment towards the team. With that being said, there is also the possibility that the player may play even better the following season with the intention of being scouted by other teams and not re-signing with his present team.

On the other hand, if the player wins the salary arbitration, the owner may choose to reduce his playing time or change where he bats in the line-up, thus affecting his offensive output. For instance, if the player is a pitcher, the team may put him in a more mediocre role, which may affect the player's ability to negotiate for a higher salary in the future during free agency.

Conclusion

The salary arbitration system has become a crucial component of baseball. From a legal perspective, the system is quite straightforward and astute. However, the fans may become exasperated with the politics and the business of the game. And since the fans are the ones that bring the money into baseball, whether it be through attendance or through purchasing merchandise, they may be reluctant to follow the sport, should the players and the owners continue to quarrel over labor issues and initiate more work stoppages. At the end of the day, the loss of fans means the economic prosperity that baseball has enjoyed for so long and its unwavering position as the second most profitable sport in the world, will soon cease to exist.

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