THE 1994 BASEBALL STRIKE: IMPLICATIONS AND POLICY OPTIONS

CHRISTIAN SCHWARZ

Christian Schwarz is majoring in Economics and History and obtaining a certificate in Markets & Management. His interests include sports, reading, music, and immigration studies. He is planning on traveling across country and to Europe after graduation. He plans to pursue a career in law or business or both.

1 The Storm Before the Storm: The History of the Baseball Market

The baseball players began their strike on August 12, 1994. A month of negotiations between players and owners provided no progress and on Wednesday, September 14, 1994, Bud Selig, acting commissioner of baseball and owner of the Milwaukee Brewers, announced a resolution canceling the 1994 baseball season. There would be no World Series for the first time in ninety years.[81] Selig said the season was canceled so as "to protect the integrity" of the regular season, playoffs, and World Series. According to Selig, the cancellation came with "enormous regret," but would allow the owners "to focus all of their efforts on achieving a meaningful reform of baseball's economic system".[82] The cancellation meant enormous losses for owners and players alike. The strike and the season's subsequent cancellation cost the players an estimated $230 million in regular-season income. The average major leaguer lost more than $300,000 and this figure excludes incentive clauses and post-season bonuses[28]. Bobby Bonilla, star outfielder for the New York Mets and baseball's highest paid player in 1994, lost $31,148 per day[11]. The owners lost between $500 and $600 million in potential revenues[28].

1.1 The Owners

What did Selig and his fellow owners see as "meaningful reform of baseball's economic system?" The answer to this question came in January of 1994 when the 28 owner of major league franchises voted unanimously for a revenue-sharing plan that would transfer revenues from highly-profitable, large-market franchises to financially struggling small-market teams. The catch: the revenue-sharing plan was tied to the institution of a salary cap. According to the owners, the necessity of a new system was triggered by the gap in revenue between clubs and the rapid escalation of players' salaries. For an analysis of the dynamics within the baseball market that structured the owners' call for revenue-sharing tied to a salary cap see Marshall[18]. The lucrative local television and radio contracts of large-market teams provide an example of the vast differences in revenue flows amongst major league clubs. These lucrative contracts give

[81] 1904 marked the last time the World Series had not been played. That year National League (NL) champion New York Giants owner, John T. Brush and manager, John McGraw, refused to play the Boston Red Sox because of their dislike for the upstart American League and its president, Ban Johnson.[1]

[82] When asked about being remembered as the first commissioner to cancel a World Series, Selig, responded, "I would feel worse if we continued to ignore our obvious problems and the industry had really awful problems within the next few years."[28]

certain clubs a decided advantage in obtaining the services of players (especially free agents). A comparison of the local television contracts for the large-market New York Yankees and the small-market Seattle Mariners highlights this revenue disparity. In 1988, the Yankees signed a twelve year $486 million contract with the Madison Square Garden (MSG) Network. The Yankees, thus, receive an excess of $40 million in local television revenues annually.[83] By contrast, the 1990 and 1991 local radio and television revenues for the Mariners were $2.3 million and $1.2 million, respectively.[29] The absolute disparity between the team with the highest local TV revenue and the team with the lowest local TV revenue grew from $1.3 million in 1964 to an estimated $52.6 million in 1990. Simply, small-market franchises are at a competitive disadvantage in the bidding for players' services because they have significantly smaller flows of revenue than their large-market counterparts.

The owners (especially those of small-market clubs) believe the rapid escalation of salaries combined with the aforementioned disparity in revenue flows is endangering baseball. Indeed, players' salaries have increased dramatically. From 1976 to 1993, the average salary has risen from $51,501 to $1.2 million. In 1991, 123 players had salaries equal to or in excess of $2 million -- 32 of those 123 players had salaries of $3 million or more.[29] At the December 1990 baseball winter meetings, outgoing Montreal Expos owner Charles Bronfman commented, "Player salaries at the major league level have lost not only all sense of proportion, but sense of reason".[29] Between 1950 and 1976, real average salaries grew at 1.87 percent annually. Since 1976, the real mean salary has grown at a tremendous rate, 13.8 percent annually. The escalation of players' salaries is of great concern to the owners as this development has increased owners' costs - greater shares of their revenues are being passed along to players. In 1974, player salaries were 17.6 percent of team revenues. The dismantling of the reserve clause and the subsequent advent of free agency (positive advancements in players' freedoms and compensations that will be discussed in detail later) saw this percentage grow to 41.4 percent in 1983. Owner collusion (also to be discussed later) saw salaries fall to 31.6 percent of team revenues in 1989, but the percentage grew again to an estimated 42.9 percent in 1991.[29]

The owners' decision to tie revenue-sharing to a salary cap was no simple achievement. Small-market clubs claimed they could not compete in the existing open market and would either fail financially or be driven to seek more lucrative markets. These claims usually fell on deaf ears as large-market owners were either unconvinced

[83] ML regulations require teams to give one-fourth of their local cable money to other teams. This would require the Yankees to give around $10 million annually from their contract with MSG. The Yankees, however, pay only $4.4 million and keep the rest. Yankee owner George Steinbrenner signed several MSG contracts which pay the team unusually large fees for promotional considerations, the rights to video, rights to the teams film library, etc. This practice greatly diminishes the amount of money paid for putting games on cable (the only category subject to baseball's current revenue-sharing plan). Thus, the Yankees pay on 25 percent of $19.9 million and not $40 million.[24]

that some teams were struggling financially or were unwilling to transfer their revenues to poorer clubs. Commissioner Selig (himself the owner of a small-market franchise, the Milwaukee Brewers) commented, "The facts are there are a lot of franchises in desperate situations and not because of bad management."[1] Documents released by the House Judiciary Committee (which has been studying baseball's antitrust exemption) said the industry lost money from 1975 to 1985, but had operating profits from 1986 to 1993.[84] Selig said, "Since 1978, this has been a virtually break-even industry if you include interest costs. And that's pre-depreciation and pre-taxes."[85] Nevertheless, high-revenue clubs were decidedly against redistributing greater shares of their local revenue. George Steinbrenner, Yankees owner and the most outspoken opponent of revenue sharing said, "This [revenue-sharing] is socialism at work and baseball is still a free-enterprise sport."[24] The owners had met previously in 1993, but had failed to adopt a revenue-sharing plan because ten high-revenue clubs had blocked its passage. Entering the January 1994 meetings, low-revenue National League teams (San Diego, Montreal, Pittsburgh, etc.) were threatening not to renew the league's expired television agreement which allowed teams to televise games back to their cities from other ballparks. If a revenue-sharing plan failed to gain approval, these low-revenue clubs would vote to charge visiting teams fees for telecasting games from their parks. Said one high-ranking executive of a low-revenue club, "It's a weapon, and it gets people's attention."[5]

The plan that emerged from the January meetings was a compromise between the high and low-revenue ballclubs. John Harrington, Boston Red Sox owner and the spokesman for the high-revenue teams said, "It's got some of the good points of both sides. It's a consensus plan...."[7] Small-market owners wanted revenue-sharing. Large-market owners would not alter the way baseball shares their local revenue without some assurance that something would be obtained from the players. Hence, the consensus: revenue-sharing with a salary cap.[27] The owners' former chief negotiator, Richard Ravitch, hailed the unanimous vote as a victory for baseball. According to Ravitch, revenue-sharing and salary cap would place all clubs in a position to remain financially solvent and, therefore, enhance the competitive balance of the game.[7] The plan called for wealthier clubs to place a percentage of their local revenues into a pool for redistribution to the poorer clubs. Ravitch said, "Clubs that meet certain economic

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[84]The documents said baseball owners lost $104 million during the strike-shortened 1981 season and $206 million more in the following four years. Baseball revenues increased from $167.6 million in 1975 to $1.879 billion in 1993. The 1992 figures obtained by the Associated Press from management sources and 1993 estimates were provided by the owners' Player Relations Committee.[26]

[85]Union head Donald Fehr said the figures were unreliable because teams did not disclose may areas of their finances to their accountants. "On their face [the documents] don't tell you very much. The base measure of the value of a team is the cost of a franchise." Since 1973, no team has sold for less than it was purchased. Team finances are a greatly disputed matter as we will see later.[26]

standards pay, those that meet others receive."[7] The salary cap portion of the plan consists of the following components:

1. Limiting players to receiving 50 percent of industry revenues in compensation;
2. Eliminating salary arbitration;
3. Allowing players to become restricted free agents after four years and unrestricted free agents after six seasons;
4. Making all teams' payrolls fall between 84 and 110 percent of the average payroll of the 28 major league clubs following a phase-in period;
5. And, if the system is implemented, teams must make qualifying offers (equal to at least 110 percent of the given player's 1994 salary) to restricted free agents so as to retain their rights and match contract offers by other clubs.[20]

The current system of revenue-sharing allows for equal distribution of national broadcasting and licensing revenues among franchises. By contrast, franchises share only a small portion of local media and gate revenues. In the NL, each team pays its opponent 25 percent of "net receipts" from any pay television contract prorated per game and gives visiting teams $.43 per ticket sold.[86] American League (AL) teams pay 25 percent of net local television receipts into a league pool to be divided equally among clubs and give 20 percent of ticket sales (after sales tax) to visiting teams.[29] Neither league shares revenues from stadium concessions and luxury boxes.[29] Specific details of the owners' proposed revenue-sharing plan have not been revealed, but one assumes that the new level of sharing will be greater than previously. The salary cap, though, will spread the cost of equalizing revenues to the players, removing some of the high-revenue teams' burden.

1.2 The Players

The Major League Baseball Players Association (MLBPA) stands firmly against the imposition of a salary cap. Commenting about the owners' plan to tie revenue-sharing to a salary cap, union chief Donald Fehr said, "There's nothing like predetermining the end of negotiations before you start."[7] The players see a cap as a restriction of the free market principles that have rewarded them with record salaries in recent years. Understanding the players' resolve to not accept the salary cap requires an examination of baseball's history of compensation and player-management relations. The past twenty-five years have required a constant battle on the players' part to gain freedom from the owners and the reserve clause, institutions that had restricted their freedom and compensation for nearly a century.

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[86]"Net" receipts are not clearly defined and teams can subtract a variety of "actual or imputed" costs from their gross revenues (i.e. rent for broadcast booths, electricity, production costs, team promotions).[29]

The reservation system found its roots in the 1877 National League (NL) winter meetings. Owners were concerned about their escalating costs. They realized the ever-increasing amounts paid out to superstar players (players that every owner wished to bid on) were a significant component of their cost problems. Arthur Soden, one of the owners of the Boston Red Sox, proposed that each team "reserve" five players from the end-of-season player market. Other owners could not negotiate with or employ reserved players and would not play games against teams playing with other teams reserved players.[10] Owners agreed to the terms of Soden's proposition and secretly enforced the reservation system on the players. The owners officially added the reserve clause to the standard player's contract in 1889. It read as follows:

> It is further understood and agreed that the party of the first part [the team] shall have the right to "reserve" the said party of the second part [the player] for the season next ensuing...[subject to the condition that] the said party of the second party shall not be reserved at a salary less than that [paid in the present season]....[10]

The clause allowed owners a perpetual option on the player's services. The reserve clause evolved over the years as it suffered numerous setbacks in court and the owners worked to develop a clause that was enforceable by the courts to maintain their superior bargaining power.[87]

Closely related and intertwined with the reserve clause is baseball's exemption from antitrust laws. As rival leagues surfaced, they challenged organized baseball's monopoly status and practices (i.e. the reserve clause and the blacklisting of players who jumped to rival leagues) that allowed owners to monopolize the supply of players. The first antitrust suit against baseball (the American and National Leagues) came in 1914 from the Federal League. After a year of negotiations, baseball and seven of the eight Federal League teams reached a settlement outside of court whereby the Federal League dropped its suit and was paid to dissolve. The remaining Federal League club, the Baltimore Terrapins, did not accept the settlement terms and filed its own suit.

Baltimore won treble damages of $254,000 in a lower court, but an appeals court reversed the decision, ruling that baseball did not constitute interstate commerce and was, consequently, not subject to the Sherman Act. The case continued to the Supreme Court where the appellate court's decision was upheld. The unanimous decision of the court, written by Justice Oliver Wendell Holmes, read as follows:

[87]In 1890, a newly formed league, the Players League, successfully attracted major league stars. As players jumped leagues, legal challenges ensued. Metropolitan Co. v. Ewing, 42 Fed. 198 (C.C.S.D.N.Y. 1890) concerned Buck Ewing, a NY Giants player who had jumped to the New York Players League Team. The federal district court ruling stated the following: one, the reserve clause was unenforceable (partly because of its vagueness); two, in its 1889 form the reserve clause was a on-year option and not a perpetually renewable option; three the clause gave the teams the first negotiating rights with the player, but was not a claim on the player's services for the next season.[10]

> The business is giving exhibitions of baseball, which are purely state affairs. It is true that... competitions must be arranged between clubs from different cities and States. But the fact that in order to give exhibitions the Leagues must induce free persons to cross state lines and must arrange and pay for their doing so is not enough to change the character of the business...As is put by the defendants, personal effort, not related to production, is not a subject of commerce. That which in its consummation is not commerce does not become commerce among the States because the transportation that we have mentioned takes place. To repeat the illustrations given by the Court below, a firm of lawyers sending out a member to argue a case...does not engage in such commerce because the lawyer...goes to another State. If we are right, the plaintiffs business is to be described in the same way and the restrictions by contract that prevented the plaintiff from getting players to break their bargain and the other conduct charged against the defendants were not an interference with commerce among the States.[8]

Ultimately, the antitrust exemption allowed owners to keep the reserve clause in players' contracts. The court's decision in Federal Baseball effectively disallowed players to challenge the reserve clause as a violation of antitrust laws. This helped maintain the clause for the next 50 years.[88] The decision has been criticized greatly and its definition of interstate commerce has long since been outdated, yet, the ruling still stands today as courts have refused to reverse the ruling and Congress has failed to pass legislation removing the exemption.[89] Currently, the House Judiciary Committee is examining

[88]The reserve clause that remained in players' contracts through the 1950s read as follows:
[I]f, prior to March 1,...the player and the club have not agreed upon the terms of such contract [for the next playing season], then on or before ten days after said March 1, the club shall have the right to renew this contract for the period of one year on the same terms, except that the amount payable to the player shall be such as the club shall fix in said notice....Pay Dirt.

[89]With eight pending antitrust suits, baseball sought Congressional relief in 1951. Hearings were held and several bills were introduced that aimed at granting all sports antitrust immunity. The bills did not pass, but baseball's exemption remained as a subcommittee held that baseball needed some form of the reserve clause to operate. In 1953, Yankee minor-leaguer George Toolson sued the Yankees after they placed him on the ineligible list for refusing to accept a demotion. With appeals, the case found its way to the Supreme Court where the Federal Baseball decision was reaffirmed. The ruling said:
In Federal Baseball...the Court held that...professional baseball was not within the scope of the federal antitrust laws. Congress has had the ruling under consideration but has not seen fit to bring such business under these laws by legislation having prospective effect....The present case asks us to overrule the prior decision, and, with retrospective effect, hold the [antitrust laws] applicable. We think that if there are evils in this field

baseball's antitrust exemption and hearings are expected be held sometime in February.

The reserve clause's next challenge came in 1949 when Danny Gardella filed an antitrust suit against major league baseball asking for damages he suffered while being blacklisted for "jumping" to the Mexican League.[12] A federal district court dismissed Gardella's complaint on the basis of the Supreme Courts ruling in Federal Baseball Club of Baltimore, but a federal court of appeals reversed the districts courts dismissal with a 2-1 vote.[13] Judge Learned Hand argued that the growth an importance of radio and television income "rendered organized baseball a matter of interstate commerce in the 1940s, whatever its status at the time of the Federal Baseball case."[13] Judge Frank's concurring opinion condemned the reserve clause. He wrote that the "`reserve clause'...results in something resembling the peonage of the baseball player...We have here a monopoly which...possesses characteristics shockingly repugnant to the moral principles that...have been basic in America...."[13] Gardella's victory, however, only gave him the opportunity to prove his case in court. Gardella and other players opted to settle their cases out of court and they were subsequently reinstated by the Commissioner. The players remained "peons" until 1968 with the negotiation of the first Basic Agreement.

Signed in February 1968, the Basic Agreement created a "formal grievance procedure" for players and commissioned a study of the reserve clause.[17] Also, the two parties (the owners' Player Relations Committee and the Players Association) agreed the Basic Agreement would take "precedence over the old major league rules" wherever the two conflicted.[17] While not monumental, the Players Association's gains were crucial first steps in what would become the dismantling of the reserve clause. The players gained another victory in early 1969 when the owners, fearing the players threats of a strike, gave them increases in health care, life insurance, and pension benefits as part of a new contract package.

The next challenge to the owners and the reserve clause came after the 1969 season when veteran outfielder Curt Flood asked Commissioner Bowie Kuhn to invalidate the St. Louis Cardinals trade of Flood to the Philadelphia Phillies. Flood wrote, "I am [not] a piece of property to be bought and sold irrespective of my wishes" and he asked to be allowed to "consider offers from other clubs before making any decisions."[17] Kuhn denied the request and Flood filed suit. In Flood v. Kuhn, the court once again upheld Federal Baseball. Justice Harry Blackmun's opinion called baseball's antitrust exemption "an anomaly" and an aberration," but he and the court refused to part from *Federal Baseball.*[90]

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which now warrant application to it of the antitrust laws it should be by legislation. Without re-examination of the underlying issues, the judgments below are affirmed by Federal Baseball.

Bills have been introduced and hearings have been held on a regular basis, but Congress has yet to reverse baseball's antitrust immunity.[15]

[90]407 U.S. 258 (1972)

Remedial legislation has been introduced repeatedly in Congress but none has ever been enacted. The Court, accordingly, has concluded that Congress as yet has had no intention to subject baseball's reserve system to the reach of antitrust statutes...If there is any inconsistently and illogic of long standing that is to be remedied by the Congress and not the Court.[91]

Once again the Court had failed to reverse Federal Baseball and the reserve clause, for the time being, remained in tact. But the case had successfully placed the reserve clause in the public eye and the players began to stockpile substantial victories at the collective bargaining table.

The second Basic Agreement signed in 1970 raised the minimum salary to $15,000, ensured that players would not receive a salary cut greater than 20 percent of his previous year's salary, and gave the players the right to impartial arbitration of grievances outside the commissioner's office. A third Basic Agreement followed in 1973. This agreement gave all players with two years plus one day of major league service the right to outside and impartial arbitration in salary disputes and adopted the "five-and-ten" rule (the Curt Flood rule) which allowed players with at least ten years of major league service who had played for the same club for at least the least five years the right to veto any trade.[29] The player population affected by the five-and-ten rule was admittedly small, but it granted players the first glimpse of freedom from the reserve clause since its adoption in 1879.

The players achieved their greatest victory in December 1975. Dave McNally and Andy Messersmith had played the 1975 season without contracts because they had been dissatisfied with the contracts offered by their clubs. The two players were challenging the renewal provision in the reserve clause: would the clubs retain their rights after the renewal year or would the players become free agents? The case went before a three-man arbitration panel headed by Peter Seitz. Seitz issued a 61 page decision in favor of Messersmith and McNally. The decision resulted in a new Basic Agreement between players and owners. Signed in July 1976, the agreement granted free agency to any player with six or more years of Major League service.[92]

Emerging from the 1976 Basic Agreement was a salary system consisting of four basic components: a $19,000 minimum salary, salary cuts of no greater than 20

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[91]Ibid.

[92]The agreement created three types of free agents: reentry, nontender, and non rerenewal. "Reentry free agents were players with six years of service and they were subject to the repeater rule -- five years must pass before a player could repeat as a free agent. Nontender free agents were players whose club refused to offer them a new contract under the 20 percent rule. Non renewal free agents were players who were granted their outright release." Teams were compensated with a draft pick for the loss of a player through free agency.[29]

percent of a player's previous salary over one year and 30 percent over a two-year period, arbitration eligibility for players with more than two but less than six years of major league service, and free agency for players with six or more years in the majors.[17] From these components, a three-tiered salary structure developed - players with less than two years of service, arbitration eligibles, and free agents.

Following the new Basic Agreement, player salaries rose dramatically (see Table 2). In the first year of the free agency salaries increased from $51,501 to $76,066. This increase however, was not spread equally across the player population. Rather, the 40 percent of players who were veterans realized an average increase of $50,000 while younger players made only small gains.[29] The 1976 agreement expired on December 31, 1979, but negotiations for a new agreement did not begin until February 1980. The players sought to lower the eligibility requirements from six to four years of major league service while the owners hoped to halt the rapid salary growth and weaken free agency. These negotiations were lengthy and slow-moving and with an agreement still not reached a year after negotiations had begun, the players struck on May 29, 1981. The strike lasted 51 days and shortened the season by 713 games.[93] The resulting compensation package gave teams losing a Type A free agent (a player statistically ranked in the top 20 percent at his position) a pick from a major league player pool. A team signing a Type A free agent had to place all but twenty-four "protected" players into the pool. Teams choosing not to sign a Type A free agent could protect twenty-six players, and five clubs could avoid the pool by promising not to sign any Type A free agent for three years.

This agreement expired in 1984 and, once again, the owners and players returned to the bargaining table. After a two day players' strike, the two parties reached the following agreement: the players obtained a $32.7 million annual payment to their pension fund, the requirement for arbitration eligibility would be increased from two to three years in 1987, the minimum salary increased from $40,000 to $60,000, the free agent reentry draft and the major league pool were eliminated, compensation for the loss of a Type A free agent was changed to a first round draft pick from the signing club, and compensation for a Type B free agent (a player statistically ranked between the 20th and 30th percentiles at his position) was created.[29]

Having steadily lost ground at the bargaining table, the owners' next action to curb salary increases came in the form of collusion. Between the 1985 and 1986 seasons, only four of the thirty-three free agents signed with new teams. As a result, free agent salaries grew only five percent and two-thirds of the free agents received one-year contracts. The MLBPA filed a grievance (Collusion I) against the owners in February 1986. These strange occurrences continued in the next off-season as free agents' average salary declined 16 percent. Once again, the MLBPA filed a grievance. In all, three grievances were filed and the players were victorious on each occasion. The MLBPA

[93] The strike ended seven days before the owners' $50 million strike insurance policy with Lloyds of London ran out. The policy gave owners $100,00 for each canceled game.[29]

settled with the owners for $280 million in total collusion damages.[29]

Negotiations between players and owners after the 1984 Basic Agreement's expiration, once again, proved contentious. The players wanted the requirement for arbitration eligibility shifted from three years of major league service to two. The owners, by contrast, wanted to create a pay-for-performance formula for all players between two and five years of major league service (eliminating salary arbitration altogether), and to institute a salary cap equal to 48 percent of revenues from ticket sales and broadcast rights.[29] The 1990 Basic Agreement did not institute a salary cap or create a pay-for-performance formula, and the arbitration eligibility requirement remained at three years of major league service. But the players did win decreased arbitration service requirements for 17 percent of players between two and three years of service. Also included in the agreement was an increase in the minimum salary to $100,000 in 1990 (and subsequent cost-of-living increases), a $20.8 million increase in the owners' annual contribution to the players' pension fund, and treble damages for the players if the owners colluded again in the free-agent market.[29] This agreement expired on December 31, 1993 and, as the paper details, owners and players have made little progress in negotiations for a new Basic Agreement.

Although lengthy, the examination of baseball's history of player compensation and player-management relations proves essential in understanding the players' position in negotiations. Players have just recently been freed from the constraints of the reserve clause, and they are tentative about giving up their new found freedom. Further compounding the situation, this freedom has been extremely financially rewarding for players. The owners contend that baseball, the business, is financially unhealthy and that, consequently, a reform of baseball's economics is desperately needed. Clearly, if franchises were financially unhealthy, the players interests would be best served by making some concessions at the bargaining table (i.e. accepting the salary cap). For instance, if two franchises were nearing bankruptcy, a real possibility would exist that the major league player population would decrease by more than 50 players - the players' union would, in all likelihood, avoid such consequences at great costs. The players, though, have firmly opposed a salary cap. From this action, and their public statements, we can surmise that the players believe the business of baseball is generating sufficient revenues to maintain the financial livelihood of all 26 franchises and that players feel their sacrifice (in the form of a salary cap) is not necessary.

Pushing aside temporarily the question of why players are so opposed to a salary cap (that will be explored in the analytic section) other questions need to be answered: specifically, why do the players feel that baseball is financially healthy or why do players not perceive a salary cap as necessary?

First, the players point to the rapid increase in franchise values. According to union head Donald Fehr, "The best measure of a value of a team is the cost of a franchise."[26] The Baltimore Orioles provide an excellent example of the increase in franchise values. Edward Bennett Williams purchased the Orioles for $12 million in 1979. After his death in 1988, Eli Jacobs bought the club from Bennett's estate for $70 million. When Jacobs went bankrupt in 1993, Baltimore labor lawyer Peter Angelos and his partners bought the club for an amazing $173 million. The franchise value had grown by over 1400 percent in less than fifteen years.[3] The escalating values of major league franchises are not a large-market/high-revenue phenomenon.[14] The Seattle Mariners, for instance, were sold in 1981 for $13.1 million. The team resold for $76 million in 1989. The team changed hands once again in 1992, this time selling for $100 million. Another example of the increasing value of franchises is the fee paid by expansion teams to join the league. The expansion fee rose from $7.7 million in 1977 to $95 million in 1993, and is rumored to rise to $125 million with the league's next expansion. The average franchise price increased 263.6 percent from the 1970s to the 1980s.[23] Sports economist Gerald Scully has studied the rate of appreciation of sports franchises. He found that team prices increase fifteen percent annually. As shown, franchise values have increased dramatically in recent years. Players believe this trend reflects baseball's health, and, thereby, they dismiss owners' claims of financial difficulty.

Second, players see the growth in total revenues for baseball as a sign of the game's financial health. Total revenue has grown from $162.6 million in 1975 to $1.879 billion in 1993.[94] Financial World magazine estimated that total revenues jumped $190 million between the 1992 and 1993 seasons.[95] Increasing attendance, according to the players, expresses the game's popularity and contributes to total revenue growth in the form of gate receipts, stadium revenues, and licensing revenues.[96] Like franchise values, attendance has increased dramatically since 1976. On average, attendance increased by over 800,000 people per club from 1976 to 1991.

Corresponding with increases in attendance are increases in gate receipts and stadium revenues. Between 1992 and 1993, gate receipts and stadium revenues jumped $151.4 million and $24.5 million, respectively. Major league teams have also generated substantial revenue flows with the licensing of sports merchandising. Prior to Peter Ueberroth's term as commissioner (1984-1989), individual teams handled their own licensing and generated, on average, only about $30,000 per year.[3] Ueberroth centralized the teams' licensing efforts with the creation of the Major League Baseball

[94] These numbers were compiled from the House Judiciary Committee's examination of baseballs antitrust examination, Associated Press reports, and estimates from the owners' Player Relations Committee.[26]

[95] Financial World defines total revenue as the sum of gate receipts (gross gate receipts, excluding sales tax), media revenues (includes national TV, local TV, cable TV, pay-per-view, and radio), stadium revenues (includes suites, luxury seating, concessions, parking, venue advertising, and other venue events where applicable, and licensing and merchandising. 1993 figures were obtained from [23]. The 1992 figures were obtained from [23].

[96] Figures 2.1 and 2.2 show the steep increase in attendance between 1901 and 1990 for the American and National Leagues. Table 4 lists the total attendance and the average attendance per club for selected years.

Properties (MLBP). MLBP initiated a 8.5 percent standard royalty rate on net sales.[97] By 1992, MLBP had issued more than 400 licenses and total retail sales of goods licensed climbed by over $2.4 billion. This development gave a newfound windfall of revenue for owners, and, by the players accord, proves that baseball is financially healthy.

Media revenues, players also emphasize, have grown consistently and provide owners with secure, long-run revenue flows. By 1990, television revenues had reached over $600 million. The national television contract has been a significant factor in the growth of overall revenues. In 1989, CBS signed a four-year $1.1 billion contract with baseball. Many predicted the price paid by CBS was too high and that baseball's next television contract would be significantly smaller. These prophecies unfolded and CBS lost an estimated $500 million with the four-year venture.[98] Baseball's next television agreement produced The Baseball Network (TBN) - a joint venture between baseball, ABC, and NBC. Unlike previous contracts baseball received no rights money up front, but would receive 80 to 90 percent of all revenues generated through the network's advertisement and sponsorship. Experts project owners will receive half the revenues they had received under the previous contract.[99] This development partially undermines the players contention that baseball is healthy. Nevertheless, players perceive franchise values and total revenue growth as positive indicators of baseball's health. Gene Orza, Associate Executive Director of the players' union, says, "What they say on their profit and loss statements does not matter. It's the viability of an institution. It's the record attendance, people going to more games than ever before."[100]

[97] Net sales equal wholesale sales minus the quantity of discounts and returns.[3]

[98] Ibid.

[99] Despite the projected decrease in revenues from the new agreement, the contract has been seen, in many eyes, as the best thing for baseball. Ken Schanzer, TBN's president, said, "A lot of owners, advertisers, and sponsors think this venture is the right way to go in the future in taking control of baseball's destiny." The agreement places the onus for television revenues squarely with baseball, and, in the long-run, this alignment of interest and incentive might generate great revenues. The strike, however, has jeopardized the venture. TBN had set a goal of $330 million in combined revenues for the 1994 and 1995 seasons. Reaching the target triggers the agreement's renewal after the 1995 season. The cancellation of the 1994 season and the possibility of no 1995 season or a 1995 season with replacement players will probably result in revenues falling short of the target, leaving baseball's television future undecided.[25]

[100] Orza's statement has some veracity. Toronto Blue Jays President, Paul Beeston, commented, "Under generally accepted accounting principles, I can turn a $4 million profit into a $2 million loss, and I can get every national accounting firm to agree with me."[6]

1.3 Descriptive Summary

With the players and owner diametrically opposed over the salary cap, negotiations have produced little, if any, progress. On December 22, 1994, the owners declared an impasse in negotiations and unilaterally imposed a salary cap system.[19] Responding to the owners' impasse declaration, Donald Fehr said, "This certainly is a sad day...It's regrettable...But it's certainly not surprising. This has been preordained for a long, long time."[19] Jerry McMorris, Colorado Rockies owner and member of the owners' negotiating committee, said, "Obviously, this is disappointing. We had a couple of serious issues we could never get over."[19] Former Labor Secretary and acting mediator in the negotiations William J. Usery said:

> There was no use to go any further. There had been a deadline set by the owners, and it became clear we would not be able to get an agreement by then. I'm hopeful the parties will soon get back together...Some day, some way were going to save baseball.[19]

Shortly after the declared impasse, both the players and owners filed charges with the National Labor Relations Board (NLRB). The union's charge called for the NLRB to obtain a court injunction which would prevent the salary cap's implementation. The owners charged the players with "surface bargaining" and failure to collectively negotiate wages.[101]

The battle has moved to the court room, and, consequently, the 1995 season has been imperiled. The owners vow to field replacement teams, and the players vow that significant numbers of players will not cross the picket line. With no resolution in sight and much of the country frustrated with the situation, Congress and President Clinton have begun to apply pressure to the two parties. On the first day of the 104th Congress, five bills concerning baseball were introduced.[102] President Clinton set a February 6 deadline for "meaningful progress in the talks" hoping to bring the players and owners

[101]The owners' attorney, Chuck O'Connor said, "What were alleging is this union, like any union, has an obligation to negotiate the collective cost of labor. What this union has said is, `We don't want to negotiate collectively. We want individual negotiations [between the players and the teams].' What we're saying is, `We can't live with that any more.'" Fehr commented, "From the beginning, the clubs have had one and only one thought in mind - forcing a salary cap on the players. As the investigation proceeds, we are confident the [NLRB] will come to see that the clubs entered into negotiations with no intention of reaching an agreement other than on the clubs' preconceived terms."[21]

[102]The intent of the five bills ranged from absolute repeal of baseball's antitrust exemption to "limited repeal of binding arbitration if players and owners cannot reach agreement by a certain date."[4]

back to the bargaining table.[103]

Many hope that the current battle between players and owners will not hurt the game of baseball. As Houston Astro president Tal Smith said, "The game is the thing. No one is bigger than the game. Let's hope that the beauty of the game transcends what's going on now."[16] The strike, though, has little to do with the "game" of baseball, but, rather the "business" of baseball. And what we have seen is a fight between owners and players for the "business" of baseball and the profits it produces.

The analytical section of the paper will explore the strike's dynamics - specifically, why are the players so against the strike, and what conditions currently exist within baseball to elicit their strident opposition to the salary cap? Following this analysis, the paper suggests strategies that the owners could take to dissolve the players' opposition and end the strike.

2 Analytics

The paper's descriptive section thoroughly explained baseball's pre-strike condition. Before the paper continues, though, a brief review is necessary. Escalating player salaries had, according to the owners, endangered the game's competitive balance as small-market teams were unable to compete for players' services. At their 1994 winter meetings, the owners responded to these conditions by voting for a plan that tied new levels of revenue-sharing between owners to a cap on players' salaries. This was the plan owners presented to the players during negotiations to renew the league's expired collective bargaining agreement. The owners claimed the plan would allow the struggling franchises to remain financially solvent, and, therefore, enhance the competitive balance of baseball.[104]

The players stand firmly against the salary cap. Players have just recently been freed from the constraints of the reserve clause, an instrument the owners had used for a century to control players' compensation. Further compounding player opposition to the salary cap, their new-found freedom has proven extremely financially rewarding as salaries have soared in the past twenty years. The players also feel that baseball's growing revenues are sufficient to support the financial livelihood of all 28 franchises; thus, the players perceive a sacrifice on their part (in the form of a salary cap or anything remotely similar) as unnecessary.

Given the positions of the players and owners, negotiations for a new collective bargaining agreement have made little, if any, progress. This diametric opposition over certain issues (most importantly, the salary cap) caused the cancellation of the 1994

[103]Clinton said, "I'm doing whatever I can do personally, but the less I say about it the better."[2]

[104]Some of this has been attributed to differences between large and small market teams. These differences are analyzed in Marshall[18] and are not considered here.

regular season, playoffs, and World Series, and has endangered the 1995 season.

2.1 The Model

The model attempts to capture the salient features within the arena of player compensation that have engendered the ardent player support for the strike. Finding these salient features could give the owners policy options that would effectively undermine player support, and, as a result, end the strike.

The model is structured around a two-team league with four players -- one good player G, two medium players M_1 and M_2, and a bad player B. The two teams are identical (Teams 1 and 2) except for player composition and every team must have two players. There are several advantages to obtaining a good player over a medium or bad player. One, when a good player is substituted for a medium or bad player, a team's probability of winning increases. This produces an increase in revenues for the team. Also, a good player's name has a certain value that attracts fans, and, consequently, increases revenues. The same type of advantages results when a team substitutes a medium player for a bad one.

Corresponding with these advantages are differentiable levels of revenues for teams with different combinations of players. For example, a team with a good and a medium player has higher revenues than a team with two medium players which has higher revenues than a team with a medium and a bad player: $R(G,M) > R(M,M) > R(M,B)$. Similarly, a team with a good and a medium player has higher revenues than a team with a good and a bad player which has higher revenues than a team with a medium and a bad player: $R(G,M) > R(G,B) > R(M,B)$. The only revenue comparison that cannot be made occurs between a team with two medium players and a team with a good and a bad player: $R(M,M) <> R(G,B)$. The inability to make the above comparison will surface later in the model and will force the formulation of certain conditions. These conditions will provide insight into the league's structure and to the longevity of the strike.

The two teams obtain their players through a sequence of four auctions. In the first auction, the two teams bid for the good player's services, this process continues until each team has two players. The teams must bid at least W_0 (the reservation wage) to obtain any player's services. More specifically, W_0 is the player's opportunity cost of playing baseball -- the wages he could earn if he were not playing baseball. This opportunity cost, W_0, can also be viewed as the league's minimum wage (all players in the league must receive at least W_0). The wage paid for the good player in the first auction is designated W_1 the wage paid for the first medium player (M_1) in the second auction is W_2; the wage paid for the second medium player (M_2) in the third auction is W_3; and backward induction tells us the bad player always receives W_0 in the fourth auction because, essentially, only one team bids for his services as the other team already has two players. Appendix 2 illustrates the auction's tree diagram and the resulting payoff structure. Symmetry dictates that the outcomes and payoffs will be reversed between teams on the different sides of the diagram. This allows the use of backward induction on one side of the diagram, and the safe application of those results to the diagram's other side.

Assuming team 1 wins the good player's services in the first auction, analysis begins on the diagram's left side. Starting on the bottom right, and comparing outcomes b and c, we move to stage 3 since we know the result of stage 4. The analysis begins with finding the respective wages teams 1 and 2 are willing to bid up to for the second medium player (denoted $\overline{W_3^i}$, $i = 1,2$ for teams 1 and 2). Team 2 will be willing to bid away the extra profit from having two medium players as opposed to a medium and a bad player. Therefore, $\overline{W_3^2}$ equals $R(M,M) - R(M,B) + W_0$. Similarly, team 1 will bid away the jump in profits resulting from having a good and medium player over a good and bad player. Therefore, $\overline{W_3^1}$ equals $R(G,M) - R(G,B) + W_0$. Because the rankings of revenues from having two medium players versus a good and bad player have not been assumed, a condition must be formulated to proceed further. That condition is as follows: $R(G,M) - R(G,B) > R(M,M) - R(M,B)$. Given this condition, team 1 wins the third auction, and thus the medium player for a wage of $R(M,M) - R(M,B) + W_0$.

From here, we continue our backward induction further up the diagram, analyzing the second auction. Given the first condition and the results of the third auction, team 2 knows that the second auction has no bearing on the team's makeup; regardless of the second auction's outcome, team 2 ends up with a medium and a bad player. Its payoff structure, however, does depend on the second auction. If team 2 wins the second auction, its payoff is $R(M,B) - W_2 + W_0$. Comparatively, team 2's payoff from losing the second auction is $R(M,B) - 2W_0$. Once again, team 2 determines its maximum bid $(\overline{W_2^2})$ by finding the wage that makes it indifferent between the two payoffs.[105] Setting the two payoffs equal, we find team 2 offers $\overline{W_2^2} = W_0$ to the first medium player. Team 1 is willing to bid no higher than it did in the third auction because the team knows even if it loses the second auction, it will win a medium player in the third auction. This is of no great consequence, though, because team 2's bid in the second auction (W_0)falls below its previous bid, $R(M,M) - R(M,B) + W_0$. As a result team 1 wins the second auction, bidding W_0 for the first medium player.

In summation, if the first condition holds, ($R(G,M) - R(G,B) > R(M,M) - R(M,B)$), team 1 wins the first medium player at W_0, and team 2 acquires the second medium and bad players for W_0. Importantly, we see the good player earn $W_1 = R(G,M) - R(M,B) + W_0 > W_0$ while all three other players earn W_0.

These results all hinge on the condition: $R(G,M) - R(G,B) > R(M,M) - R(M,B)$. What if this condition does not hold, however, and the reverse is true: $R(G,M) - R(G,B) < R(M,M) - R(M,B)$? This new inequality tells us team 2 wins the third auction, bidding $R(G,M) - R(G,B) + W_0$ (team 1's bid limit). Again using backward induction, we move to the second auction. After equalizing its payoffs, $\overline{W_2^1}$ equals $R(G,M) - R(G,B) + W_0$.[106]

[105] $R(M,B) - 2W_0 = R(M,B) - W_2 - W_0$ Þ $W_2 = W_0$

[106] Team 1's bid illustrates its willingness to bid away the extra profits that come with

Following the same procedure, $\overline{W_2^2}$ equals $R(M,M) - R(M,B) - W_3 + W_0$.[107] Since we know W_3, team 2's bid $\overline{W_2^2}$ can be revised to read $R(M,M) - R(M,B) - [R(G,M) - R(G,B) + W_0]$.

Because we cannot tell which team's $\overline{W_2}$ is bigger, another inequality is necessary. If $\overline{W_2^1}$ is larger, the inequality is:

$$2[R(G,M) - R(G,B)] > R(M,M) - R(M,B).$$

If $\overline{W_2^2}$ is larger we have:

$$2[R(G,M) - R(G,B)] < R(M,M) - R(M,B).$$

As a result of the latter inequality, team 2 wins the second auction and acquires both medium players. Team 1's payoff equals $R(G,B) - W_1 - W_0$ while team 2's payoff equals $R(M,M) - W_2 - W_3$. Substituting the established W_2 and W_3 into team 2's payoff structure, its payoff is $R(M,M) - R(G,M) + R(G,B) - R(G,M) + R(G,B) - 2W_0$. Importantly, we observe both medium players receiving wages greater than W_0. Both players receive $R(G,M) - R(G,B) + W_0$. This occurrence will prove important as we try to explain the strength of the current baseball strike.

Our analysis is not yet complete, though, as we must determine the results if our second inequality is reversed. Doing so gives us:

$$2[R(G,M) - R(G,B)] > R(M,M) - R(M,B).$$

This tells us team 1 wins the second auction, bidding $R(M,M) - R(M,B) + W_0$ for the first medium player's services. As in our first case, outcome "a" prevails, but here the first medium player receives a wage greater then W_0. Both the second medium player and the bad player again receive W_0.

Table 6 summarizes our findings thus far. In both situations I and III, team composition is the same, and the second medium (M_2) and bad (B) players all receive W_0, but the first medium player in situation III receives compensation greater than W_0. Situation II contrasts significantly with the two other situations as team 2 acquires both medium players for wages greater than W_0. These differences, will structure our forthcoming analysis of the strike's strengths, and suggest possible owner policy options to diminish this strength.

2.2 Payroll Cap

Where are baseballs players' salaries currently? Do they fall under situation I, situation II, or situation III? To answer this question and to place the players' strike in its proper context, we must construct a model for the owners' proposed salary cap. The owners have proposed a payroll cap; that is the summation of all individual salaries on a team, SW_i, cannot exceed some limit $\overline{C}$. First, we assume all players must be paid at least W_0. This implies that no good or medium player can receive more than $\overline{C} - W_0$ (the payroll cap minus any player's opportunity cost) because each team must have two players. Second, we assume that $\overline{C}$ is set low enough so that only the good player receives a wage greater than W_0, and, consequently, all other players' salaries are pushed towards the league minimum. Given this payroll cap and the model, which players oppose a salary cap? Clearly, the good player opposes a payroll cap because a limit is placed on his salary; since $\overline{C} - W_0$ is assumed to be low enough to do so. Also, any medium player receiving a competitive wage greater than W_0 would also oppose the cap and support the strike because he would see his wage drop to W_0 under the cap. By contrast, a player receiving W_0 would never support a strike (proposed payroll cap or not) because a strike gives him nothing and costs him lost wages over the period of the strike.

Applying this salary cap model to the three situations, we can determine under what situation a protracted players' strike in response to a proposed salary cap is most likely.[108] In situation I, three of the four players earn W_0 and, thus, would oppose any strike. Situation II contrasts with situation I as three of the four players earn salaries greater than W_0. A strong strike would ensue from this situation because the good and medium players would all support the strike. Situation II falls in between the first two situations because two players earn wages greater than W_0 while the other two players earn W_0. Although we assume that they strike, it is unlikely that the strike would be extraordinarily strong.

3 Implications and Policy Options

The strong strike by major league baseball players that we have observed probably tells us their salaries are best described by situation II. Taking this assertion a step further, we can develop policy options for the owners that would undermine the strike's strength. First, the owners could raise the league minimum (W_0) to match what the medium players currently earn in situation II. As we discussed earlier, players earning the league minimum have no incentive to strike because for them a strike costs them their W_0 over the period of the strike. With a higher league minimum, the strike would lose its strength as the medium players support would be dissolved.

The second policy option requires deeper insight into the inequalities that

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substituting a medium player for a bad one.

[107]Team 2's bid illustrates its willingness to bid away the extra profits of having two medium players rather than a medium player and a bad one.

[108]The players have publicly stated that they believe a salary cap will push all players' salaries, except for the best players, towards the league minimum. Whether or not this belief is true is debatable. But we are looking at wages from the players' point of view so their beliefs are what is pertinent.

allowed us to determine players' salaries under the different condition. Again, the witnessed strength of the strike infers that baseball is in situation II. The first inequality of situation II, says that the difference in revenues between teams with two medium players and teams with a medium and a bad player is greater than the difference in revenues between teams with a good and medium player and teams with a good and a bad player. Essentially, revenues generated by the worst team possible in the league (a team with a medium and a bad player) are relatively low. The second inequality of situation II tells us that these revenues are so low that the revenue disparity between teams with two medium players and teams with a medium and a bad player is at least twice the revenue disparity between teams having a good and a medium player and teams with a good and a bad player. Because the revenues of having a medium and a bad player are so low, teams (team 2 in this analysis) have incentive to bid up the salaries of the medium players. This incentive explains why both medium players receive wages greater than W_0 in situation II.

In situation III, we see the second inequality reversed and, consequently, the second medium player's salary drops to the league minimum. The revenue disparity between teams with two medium players and teams with a medium and a bad player has decreased, and, thus, the second team has less incentive to obtain two medium players.

Situation I's inequality creates greater revenue disparity between teams with a good and a medium player and teams with a good and a bad player. Both medium player's salaries drop to the league minimum because team two has lost all incentive to bid up their salaries as the revenue disparity between having two medium players and having a medium and a bad player has decreased relatively.

What policy options to dissolve the strike's strength, then, do these observations give owners? Assuming situation II is most indicative of baseball's current situation, if the owners acted to decrease the revenue disparity between having two medium players and having a medium and a bad player, any teams incentive to bid up the salaries of medium players would decrease and the medium players' salaries would drop to the league minimum. As stated previously, players making the league minimum have little incentive to strike. Thus, giving the owners another option for ending the strike.

4 Conclusions

The two team, four player model presented provides a context with which to understand the current players' strike. Given the strike's longevity and the player commitment that the longevity entails, baseball is best characterized by situation II with three-fourths of the players earning more than the league minimum. Knowing this gives the owners policy options to potentially dissolve the players' support for the strike. First, the owners could raise the league minimum to the level currently received by the medium players. Doing so would remove these players' incentive to strike. Second, the owners could implement some form of revenue sharing to decrease the revenue disparity between teams with different compositions. According to the model, teams have incentive to bid up the medium players' salaries because the differences in revenues between having two medium players and having a medium and a bad player is so substantial. Lessening this incentive, will push the medium players' salaries towards the league minimum and remove their support for the strike.

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