CHAPTER ONE

The Baseball Player's Labor Market Revisited

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A PRACTICE universal among the world's major professional sports leagues is the use of labor-contracting methods that limit the mobility of players among teams. In North America, this practice is embodied principally in player reservation, in drafting methods that assign to individual teams the exclusive and marketable rights to negotiate with particular players, and in league conventions or rules that limit the sale of players for cash.[1]

Why these policies exist and, indeed, persist is an issue of considerable practical as well as theoretical interest. Many American economists who have studied this issue have concluded that, although often justified on other grounds, the sole cause and consequence of these practices is to enhance the bargaining power of teams in their negotiations with players, thereby transferring to the teams rents associated with the display of the unique skills of the players.

This chapter reexamines this issue from a different analytical perspective, one that focuses on the benefits and costs of alternative contracting methods. I argue that previous investigators have omitted from their analyses two matters of great importance to understanding this issue: the existence of contracting costs, and contest legitimacy as an important

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1. Also included within the generic term *player reservation* are mandatory compensatory payments from teams that sign players from another team's rosters and limitations on total salary expenditures made by a single team.

factor influencing such costs. Consideration of these factors suggests conclusions different from those of the previous analyses. The most general and important of these conclusions is that, whatever their distributive effects, the traditional labor-contracting practices of sports leagues have an efficiency rationale that arises from their ability to secure and thereby encourage organization-specific investments in both leagues and their constituent teams.

The Contracting Structure of Professional Sports Leagues

A professional sports league is a distinctive organizational arrangement characterized by several unusual contracting practices. These include the fact that the league itself is a composite structure made up of a number of independently owned and managed teams. Individual teams are granted franchises, which consist of a variety of rights and related restrictions governing many aspects of their operations. The teams collectively own the league, making it, in effect, a franchisee-owned franchiser.

Sports leagues also have unusual policies governing transactions between teams and between teams and players. The most general aspect of these policies is a strong reliance on a set of predetermined, written rules, including a constitution to govern league affairs. This rule structure plays an important role in the allocation of league resources and, among other things, requires a central authority, usually in the form of a commissioner, to oversee its application.

Teams within a sports league generally share revenues, a practice that redistributes funds from the more prosperous to the less prosperous league members. In addition, player transactions between teams are dominated by barter, in which the rights to one player's professional services are exchanged for those to others rather than for money. Indeed, in one major American sports league, the National Football League, player sales are banned, and in others they are severely restricted by custom and convention.[2]

By far the most celebrated and controversial of sports leagues' contracting practices, however, are the restrictions placed on individual play-

2. Interteam sales of players were more common in the early years of baseball and remain common in English football. However, they have played a negligible role during baseball's last fifty years, rarely involving first-line players. Indeed, this factor was cited by Commissioner Bowie Kuhn in voiding a number of such transactions precipitated by the revision of the reserve clause in 1976. See Kuhn (1987, chap. 14).

ers' rights to negotiate with other teams. Of special significance is the reserve clause of Major League Baseball, which "reserves" to a single team the exclusive right to employ a particular player. A closely related feature, the rookie draft, is used to assign the rights to new players among individual teams, usually in inverse order of the team's position in league standings at the conclusion of the previous season.

These rules, especially the reserve clause, have been a source of controversy over virtually the entire history of Major League Baseball, a controversy that continues today.[3] Professional athletes and others acting in their behalf (especially player agents and associations) frequently allege that these restrictive practices are nothing more than monopsonistic methods of reducing players' incomes to benefit those owning the teams. The inevitable result, they argue, is exploitation, which reduces the players' share of the wealth created by the display of their playing skills.

The traditional response to these arguments by team owners and those sympathetic to them is that these rules are necessary if the league is to produce an attractive, commercially viable product. In particular, they contend that in the absence of restrictions such as the reserve clause and rookie draft, "rich" teams from large markets would acquire a disproportionate share of the best players, thus producing unbalanced and, ultimately, uninteresting competitions.

The Invariance Proposition

In a provocative and seminal paper written over thirty-five years ago, Simon Rottenberg produced an ingenious and seemingly devastating counterargument to the sports world's conventional wisdom regarding the apparent effects of the reserve clause.[4] If player contracts can be freely exchanged, he argued, their allocation should be uninfluenced by their ownership. Because both team owners and players presumably wish to maximize their personal wealth, they should behave identically with re-

3. The reserve clause came into being in 1879, only a few years after the beginning of professional baseball. Among the problems it was designed to alleviate were highly uneven league competitions; the practice of "revolving," whereby teams signed each other's players in mid-season, thus harming the apparent integrity of contests; and escalating player salaries, which threatened the solvency of a number of teams. Shortly thereafter, a virtually identical clause, the retain and transfer rule, was developed in the newly emerging sport of professional football (soccer) in England and for virtually identical reasons. See Seymour (1960, chaps. 7–12); Levine (1985); and Tischler (1981).

4. Rottenberg (1956).

gard to the allocation of the identical asset, in this case the rights to a player's professional services. If, in the absence of the reserve clause, a player would rationally sell these services to a large-city (-market) team because it made him the largest offer, then, under the reserve clause, a rationally managed team owning his contract would do the same. Restrictions on players' mobility influence the ownership of an asset and thus the distribution of income arising from it, but not its allocation.

Rottenberg's invariance proposition proved compelling to many economists, some of whom viewed its logic to be so unassailable as to constitute proof of its empirical validity. Its grip on economists' thinking persists to this day.[5] The now substantial literature on economic aspects of professional sports is in many ways an outgrowth of Rottenberg's ideas and a testimony to their influence. A significant subset of this literature is concerned with policy issues, and much of it is critical of sports leagues' restrictive contracting practices in general and the reserve clause in particular.[6] If, it is argued, these rules do not alter actual contests but only the distribution of wealth arising from them, they are without an efficiency rationale. Instead, they are simply anticompetitive methods of supporting collusion among firms, and justifications offered for them are merely a "cover" for owners' wealth-maximizing behavior.

Contracting Costs in Professional Sports Leagues

Underlying the invariance result is the behavioral assumption of wealth maximization. Restrictive labor contracts are seen as serving this end by minimizing the price paid for an input class. Whatever the validity of such a claim, the potential implications of wealth maximization for contractual choice extend far beyond input prices; any contracting alternative that will reduce the costs of league operation or improve the demand for its product will also serve this end. Further, to the extent that the contractual choices affect real variables—resource supplies or output characteristics, for example—they have implications for efficiency as well.

The analytical methods used to derive the invariance result preclude this possibility by assuming that transactions are costless, a circumstance under which contractual choice is, by definition, unrelated to economic

5. See, for example, Noll (1988); Scully (1989, chap. 4).

6. Demmert (1973); El-Hodiri and Quirk (1971); Holahan (1978); Noll (1988); Scully (1989).

efficiency. Rottenberg's invariance proposition is a particular application of the Coase theorem: the proposition that in the absence of transaction costs and wealth effects, the efficient allocation of resources is independent of their ownership.[7] Yet the literal application of this theorem to sports leagues (or any other real world activity) ignores Coase's subsequent dictum: In the absence of transaction costs, all contracting methods are equally efficient, and the optimal form of contracting is indeterminate.[8] Under such conditions, the invariance proposition, like the Coase theorem itself, is a truism devoid of policy implications or empirical content. Only by including such costs can a meaningful analysis of sports league contracting be undertaken.

Contracting Costs, Resource Interdependencies, and Contractual Choice

The implications of contracting costs for the structure of economic institutions are the primary focus of a substantial economic literature.[9] A principal theme of this literature is that when the productivities of separately owned resources are interdependent, individual resource owners may have incentives to engage in unproductive forms of behavior to enlarge their share of jointly created wealth. Where this is so, contracting practices that limit such behavior and, more specifically, economize on the resources used in engaging in or preventing it, may enhance economic efficiency and thus fundamentally influence the form of institutions.

The concept of team production processes plays an important role in this context. A characteristic of such processes is that cooperation between separate productive agents is an important source of total productivity. The returns to this cooperation are inherently collective and thus cannot be attributed to particular productive agents nor, for that reason, transferred by them to other uses.[10] Two potential sources of inefficiency of

7. Cymrot and Dunlevy (1987); Daly and Moore (1981); Lehn (1982).

8. "While consideration of what would happen in a world of zero transaction costs can give us valuable insights, these insights are, in my view, without value except as steps on the way to the analysis of the real world of positive transaction costs." Coase (1981, p. 187).

9. The general area of contractual choice has been approached from a variety of perspectives or "schools" described by terms such as property rights economics, agency theory, transaction cost economics, and the "new" industrial organization. The work of Coase (1937), Williamson (1983, 1987), Alchian (Alchian and Demsetz [1972], Alchian and Woodward [1988], and Klein, Crawford, and Alchian [1978]), and Jensen and Meckling (1976) has been especially influential.

10. Alchian and Demsetz (1972).

particular importance to the contracting practices of sports leagues can arise under these circumstances. In one, what have been termed "small-number bargaining problems" are created when nonredeployable investments are required for economic efficiency and, once made, are subject to appropriation by strategic (that is, opportunistic) behavior. The second, often associated with the term *moral hazard* and closely related to the first, arises when such investments create indivisible benefits from which others cannot be costlessly excluded, creating incentives for free-riding behavior.

The examination of contracting in such contexts has yielded a number of insights about the efficiency properties of arrangements that, absent such considerations, may appear to be simply redistributive and thus "unfair" because of the restrictions they place on some parties to them.[11] What such arrangements have in common is a set of prior and frequently exclusive agreements that limit the potential for counterproductive behavior by one or more classes of resource owners. Among the contracting practices that have been usefully analyzed from this perspective are vertical integration, various tying arrangements, exclusive franchising, agreements assigning one party unilateral rights of termination, and a variety of means by which a potentially opportunistic party makes a "credible commitment" for the purpose of securing the consent of otherwise vulnerable parties.[12] More generally, such insights have greatly expanded the understanding of hierarchical contracting methods in which individual resource owners join organizations to whose rules they precommit because the coordination thereby achieved will result in greater productivity and individual rewards.

Sports leagues and teams are organizations in which value arises as a result of continued and complex associations among productive resources. Further, the fact that economic rents account for a large proportion of such organizations' expenditures suggests an environment conducive to strategic behavior and that transaction costs related to such conduct may constitute a relatively large proportion of the real costs involved.[13] For these reasons, it seems plausible that the efficiency of sports leagues and thus the long-term interests of the resource owners involved in them might be served by contracting methods that recognize such interdepen-

11. Klein (1980).
12. Williamson (1983).
13. In North American sports leagues, players' salaries generally constitute between 40 and 60 percent of total team expenditures. Obviously, a vast proportion of these payments represent compensation above the players' reservation prices.

dencies and serve to protect investments from actions capable of appropriating or dissipating them. If this is the case, contractual choice can influence the supply of resources, the manner in which they are combined, and the characteristics of the product that results, thereby contradicting the invariance result.

For example, the predictions of the invariance proposition arise from the belief that the highly specialized skills owned by professional athletes do not have alternative uses (earn economic rents) and, hence, that restrictions placed on their negotiating rights (or the removal of same) will not alter their supply and will therefore be without real (efficiency) effects. Such a conclusion rests on the tacit assumption that the supply decisions of other resource owners are similarly unaffected by these restrictions. If, instead, the supply of nonathletic resources varies according to the contractual protection afforded them and if sports league labor-contracting methods afford such protection, the invariance result no longer follows.

Contest Legitimacy and Contracting Costs in Sports Leagues

A second factor, omitted from earlier analyses but of considerable importance to sports leagues' contracting practices, is the concept of contest legitimacy. Sports leagues are unusual institutions in that the product they produce—a series of athletic contests—is a consequence of the joint efforts of separate entities, namely, the opposing teams.[14] This organizationally joint production involves both cooperative (economic) and noncooperative (athletic) elements. Specifically, teams must cooperate on economic matters (for example, playing sites must be determined and revenues divided), yet this cooperation must ultimately produce an athletic contest whose financial success depends, in part, on the perception that it involves strictly opposed behavior by two intense rivals. Contest legitimacy refers to the degree to which a league's fans perceive that the contests are fair and beyond manipulation and that the teams and players involved are doing their best to achieve athletic victory.

Because athletic contests are live performances whose production and consumption occur simultaneously, managerial actions that alter a team's composition or performance are immediately evident to informed spectators. As a result, contest legitimacy can be affected by managerial as well as athletic conduct. When this is so, the demand for a league's contests

14. Markham and Teplitz (1981); Neale (1964).

is sensitive to the nature of the economic transactions that take place within and among its constituent teams. Such effects can constitute an important opportunity cost associated with contractual choice and thus have decisive effects on it.

Such decisive effects appear to be present in major sports leagues. For example, contest legitimacy alone rationalizes limitations on any transactions other than those between a player and his own team in which individual athletic services are exchanged for monetary payments. The reason for this is simple: such exchanges can harm legitimacy by creating questions about the motivations of the selling party and thus can threaten the economic viability of the league and the wealth earned by its resources. If a player sells his services to a gambler or an owner sells his best players to a competing team, the league's legitimacy, and thus its economic welfare, is threatened. Thus it is hardly surprising that professional sports leagues adopt contracting procedures that restrict such transactions and go to considerable expense to ensure their enforcement.

A second implication of legitimacy concerns the manner in which leagues and their constituent teams are owned and organized. A league's legitimacy is enhanced by the independent ownership and management of individual teams and, conversely, is damaged by ownership integration and the potential conflicts of interests such arrangements might involve.[15] In turn, such separate ownership means transactions that in virtually any other industry would occur within a single organization instead take place between separate organizations (teams).

Although it is difficult to "prove" that the independent ownership of teams and the dominance of barter in major American sports leagues owe their existence to contest legitimacy, it is even more difficult to understand why a league would adopt these contracting rules in the absence of such a factor.[16] The existing, essentially neoclassical, analysis of a sports league views the contracting structure of a league and the demand for its output as exogenous and independent. Such methods cannot explain why these

15. In fact, in baseball's early days a number of individuals owned several teams, a practice known as "syndicalism." Immortals such as Wee Willie Keeler and Cy Young, for example, were shifted between teams by the decision of a single owner. Seymour writes of this period: "Declaring for honest competition, they [club owners] rejected syndicate ball by confirming separate ownership of clubs, and in time specifically prohibited anyone from holding stock in more than one club in a league." Seymour (1971, p. 39).

16. In leagues in which player sales or "transfers" are common, such as the English football league, legitimacy is established by other means, including promotion and relegation among league divisions, a strong tradition of nonfinancial objectives among ownership, and limitations on wealth extraction by owners of residual income claims.

institutions rationally choose to deny themselves the obvious efficiencies of unified ownership or impose on themselves the exchange inefficiencies of barter in players.[17]

Because legitimacy is a desirable characteristic of contests, the efficiency of a particular configuration of resources within a sports league is not independent of the contracting methods by which it has been achieved. This implies a dynamic inconsistency or path dependence because the contracting processes required to achieve efficiency over time will not necessarily result in resource allocations required for efficiency at an isolated moment. Thus some of the static optimality conditions associated with the invariance proposition—that each player be assigned to the team where his marginal returns are greatest and that, in the aggregate, the marginal returns to talent be equal across teams—no longer necessarily hold.[18]

Contracting Costs and Economic Efficiency in Sports Leagues

In a world of transaction costs and variable resource supplies, rather than under the static optimality conditions discussed above, efficiency requires the creation of a set of contracting rules that will lead rational, interdependent agents (players, fans, managers, owners) to behave in a manner that maximizes the wealth created by their joint activities. Such an outcome is characterized by the production of optimal output (contest) characteristics at the minimum social cost.

The traditional literature has emphasized two principal characteristics of a sports league's output that are important to spectator demand and thus to the wealth created by such an endeavor: (1) the absolute quality of athletic performances, and (2) league balance or relative parity of teams' athletic quality. To these characteristics must be added (3) contest legitimacy, for the reasons described above. The pertinent question concerns whether and how these characteristics are influenced by sports leagues' labor-contracting practices.

17. The advantages of unitary league ownership for residual claimants include the reduction of variance in returns to ownership (diversification across teams), ease of achieving product characteristics (for example, competitive balance), and the enhancement of bargaining power.

18. This is because the transaction costs, in terms of damage to league legitimacy, exceed the allocative gains associated with achieving the static neoclassical optimality conditions.

The contractually relevant interdependencies among the resources employed by sports leagues occur at two organizational levels. First, a variety of productive resources—athletic skills, managerial expertise, risk-taking abilities—must be combined into teams. These teams are then used as intermediate products or inputs into the production of a final product, the contests produced by the league.

Discussion of the contractual implications of these interdependencies is simplified by adapting some of the terminology used in the transaction cost economics literature to sports leagues.[19] Transaction-specific resource commitments are nonredeployable investments that, once made, are vulnerable to appropriation by strategic behavior. Such investments can be further subdivided by the source of this opportunistic behavior: Resource commitments that are vulnerable to actions by a resource of the same team are termed team specific; those vulnerable to resources employed by another team, league specific.[20]

Securing Team-Specific Investments

The creation of a professional sports team of the highest athletic quality requires team-specific investments by a variety of resource owners that cannot be costlessly shifted to other uses. The value of these investments is sensitive to the subsequent behavior of other team-specific resources. Moreover, the nature of the process through which teams and contests are produced greatly amplifies the consequences of this team specificity. The skills possessed by some athletes are unique or of "star" quality, capable of influencing team design and thus the nature of other athletic resources employed; in the vernacular, teams are sometimes "built around" such players. Economically meaningful measures of these skills are difficult to specify contractually. Many of the necessary investments, particularly those by owners of nonathletic resources, must be made before and thus, once made, are particularly vulnerable to actions that threaten the contests from which virtually all of the teams' revenues are derived.

The traditional bargaining settings between players and teams have often been described as monopsonistic or, in the case of star players, as bilateral monopolies. Such terms, however, fail to capture all of the rel-

19. Williamson (1987).

20. Although in general all investments in a league are specific in both senses (that is, they can be threatened by actions of resource owners from its own as well as other teams), distinguishing between them has important pedagogical advantages for the subsequent analysis.

evant economic considerations involved because an element of "double moral hazard" is present in that each party may be capable of inflicting economic harm on the other. If this is so, efficient (incentive-compatible) contracts must limit both parties from benefiting from strategic behavior.[21] That is, each party must make what Williamson has termed a "credible commitment" to the other as an implicit bond formed to prevent counterproductive, inefficient behavior.[22]

Team owners' incentives to devote resources to such behavior are limited by their ownership of residual claims as well as the rights of control. By virtue of their ownership of the team's residual income, and thus its most specific resource, franchise owners make such a commitment because they will incur the consequences of any inefficiency within the organization.[23] What is needed is an equivalent prior commitment from the owners of athletic skills whose subsequent behavior determines the value of these investments.

Alchian and Woodward have made a general observation about the relationship between bargaining environments and efficient contracting that is directly relevant to the circumstances confronting a team and its key players:

> An owner of a unique resource will be more tempted to exploit the situation as the composite quasi-rent [cooperative return] grows large and as the unique resource's flow of services becomes more controlled (for example, by failing to pay the rent, or to show up for work). The more likely and foreseeable is this temptation, the greater is the likelihood that precautionary terms will be sought.[24]

It has been suggested that explicit, long-term contracting can efficiently deal with reliant investments in sports leagues.[25] Such a conclusion over-

21. Demski and Sappington (1991).

22. Williamson (1983).

23. In fact, Demski and Sappington (1991) show that an agreement to accept the ownership of residual claims of a firm on the unilateral decision of their current owner can serve as such a credible commitment for a resource owner negotiating with the firm when double moral hazard is present.

24. Alchian and Woodward (1988, p. 68). It would appear that the practical implications of this reality have not escaped those who have played a role in shaping the contracting rules of sports leagues, as a quotation from former Major League Player Association official Marvin Miller indicates: "I never before have seen a group of people [major league players] who are so irreplaceable in relation to their work." Quoted in Jennings (1990, p. 24).

25. Noll (1988).

looks several serious problems in this context. Some forms of long-term contracting have been shown to significantly affect player performance.[26] Indeed, writing efficient forms of such contracts may be impossible given the complex interdependent nature of player and team performances and the fact that many dimensions of this performance are under managerial control. The inalienability of human capital seriously impedes employers' ability to enforce these contracts, as indicated by the frequency with which they are renegotiated while in force under threats by players to take actions capable of degrading team performance (for example, "holding out").

Given these factors, efficient contracting between teams and players is likely to be described by hierarchical methods in which substantial rights over the conduct of players are assigned to the owner of residual claims. To protect and thereby encourage reliant investments required for efficient team operation, the rights so transferred or modified must include those whose subsequent exercise could be important sources of costly strategic behavior to the team. Chief among these is the right to be employed by another team in the league, the major comparable alternative source of income to the player and therefore a principal source of credible strategic behavior. The transfer of these rights via exclusive employment contracts thus constitutes a credible commitment from potentially opportunistic resource owners to the team's residual income claimant and thus, indirectly, to all owners of team-specific resources. If the player's income is an economic rent, whereas that of some or all of the other team-specific resources is not, restrictions on the former that protect the latter can enhance the supply of resources to the league and, accordingly, economic efficiency.

Although overlooked by the invariance proposition literature, such prior contractual commitments are common in organizational contexts that require unusual or unique human skills whose subsequent withdrawal could diminish the value of other investments.[27] Indeed, these commitments not only take the form of illiquid claims on residual income and other forms of compensation designed to avoid "agency" problems, but also include "noncompete" clauses, common in many executive and professional contracts, which restrict the employment options of human resources around which otherwise appropriable investments are made.[28]

26. Lehn (1982).
27. Alchian and Woodward (1988); Klein (1980).
28. Rubin and Shedd (1981).

Finally, among the relevant factors shaping contractual choice in a professional sports league is the concomitant need to protect the league-wide resources of competitive balance and contest legitimacy. As discussed below, these considerations reinforce the conclusion that prior contractual agreements that restrict the interteam mobility of players can enhance economic efficiency.

Securing League-Specific Investments

A league involves organizationally joint production through which successively matched pairs of teams produce a series of contests. As a consequence, the value of investments made in an individual team depends not only on its own activities but also on those of the other teams. The existing literature has tended to subsume all such interdependencies within a single variable described as "league balance." This results in oversimplification; many aspects of a single team are capable of influencing the returns earned by resources invested in other league members, including stadiums, market areas, management skills and behavior patterns, and ownership structures.

Such interdependence is not unique to professional sports leagues and is common in other activities that involve the distribution of a product with shared characteristics (in this case, identification with the league) in separate locations. Consider, for example, the case of a nationally distributed but locally produced product such as fast food. Here, a low-quality product delivered at a single location will, through reputation effects, damage the wealth of resources involved at other locations. Efficient production, however, is served by local ownership and control. How can the potential harm from these externalities be minimized? The contracting practice that has come to dominate the supply of such services is franchise arrangements that permit a central organization (the franchiser) to regulate the quality of service at individual locations. The methods commonly used in doing so include a variety of restrictions on the uses made of productive resources.[29]

Similar organizational arrangements are used in sports leagues. In this context, the relevant question becomes, What types of resource allocation decisions by individual franchises might, owing to the resource interdependencies involved, be capable of imposing significant costs on other franchises and, therefore, be appropriate candidates for such restrictions?

29. Mathewson and Winter (1985).

The answer is, Any of those shared output characteristics subject to managerial discretion of an individual franchise. Of these, however, the characteristics of league balance and legitimacy, because they are indivisible across teams, are of particular concern because of the moral hazard problems to which they are subject and the free-riding behavior, with its attendant inefficiencies, that can result.

Transactions that can result in the movement of players among teams are particularly strong candidates for such contractual restraints because of the dominant role played by the interteam distribution of talent in influencing both league balance and legitimacy. Among such transactions, those that result in the exchange of players for monetary payments (that is, player sales) are especially significant. Such transfers necessarily alter league balance (because, by definition, these transactions result in one team's playing strength growing while another's diminishes) and because a separate leaguewide asset—the legitimacy of its contests—can be diminished by such actions. The possibility that some franchise owners might be motivated by a desire for athletic success or other nonfinancial objective underscores this conclusion because such behavior is likely to be directed at altering the interteam distribution of talent and to use player purchases as a primary vehicle for achieving this end.

Thus, whatever their other effects, prior agreements restricting player mobility in major sports leagues can protect the leaguewide assets of balance and legitimacy. The combined effect of the barter constraint, player reservation, and inverse-order drafting procedures is to assign players among teams in an equalizing manner and subsequently to prohibit types of transactions (such as the exchange of player services for cash, whether between teams or between teams and individual players) that are capable of systematically harming league balance or legitimacy.[30]

Summary and Conclusions

This chapter has advanced the argument that prior contractual agreements limiting players' negotiating options within professional sports leagues can serve the cause of economic efficiency by protecting, and thereby encouraging, transaction-specific investments. Such investments have real

30. As noted by El-Hodiri and Quirk (1971) and others, given rational behavior, a team will not trade a good player for a poor one so that the a priori effect of such transactions on league balance is nil.

effects that can include a larger level of league output, higher-quality athletic performances by teams and players, and an enhancement of the legitimacy and competitive balance of contests.

The analysis does not deal with the "fairness" or other noneconomic effects of sports league contracting. Nor does it deny that the "bargaining power" rationale central to previous analyses may play a role in explaining the contracting practices of sports leagues. It does, however, argue that such distributive explanations cannot sensibly claim exclusivity as consequences or causes of these practices and, further, that policies based on such presumptions are likely to lead to unforeseen consequences, including a reduction in economic efficiency.

Relatively little attention has been devoted to empirical tests of the consequences of contracting alternatives in sports leagues. One reason for this is that restrictive labor-contracting practices are common to virtually all major revenue-generating sports leagues and have varied little across time, making comparisons difficult. The principal "evidence" offered in support of the invariance proposition has been its internal logic or consistency with existing concepts of neoclassical economics.[31] However, given its tautological nature, the proposition's logical consistency is neither surprising nor a relevant test of its validity.

The best available evidence with which to judge this issue comes from the use of and changes in contracting practices of sports leagues. In this regard, the following observations are justified.

1. In efforts to test directly the propositions of interest in this chapter, several authors have examined free agent movement and athletic performance in the years immediately following the 1976 revision of the reserve clause in Major League Baseball.[32] They each concluded that systematic changes in real outcomes had occurred following this contractual change.

2. The invariance proposition implies that drafting procedures employed by sports leagues have no effect, being offset by subsequent player sales between teams. Since interteam sales of first-line players are virtually nonexistent in major North American sports leagues (and, indeed, are prohibited in several leagues), transactions that the invariance proposition contends are critical to its validity do not occur.[33]

31. For example, two of the most influential papers in articulating the invariance proposition, by Rottenberg (1956) and El-Hodiri and Quirk (1971), are nonempirical.

32. Cymrot (1983); Cymrot and Dunlevy (1987); Daly and Moore (1981); Lehn (1982).

33. The criticality of cash sales to the validity of the invariance proposition has been noted by several authors, including El-Hodiri and Quirk (1971), Daly and Moore (1981), and Scully (1989).

3. The invariance proposition's hypothesis of ineffectuality of the player draft is not borne out by historical experience. Drafting procedures were instituted in both Japanese and American major league baseball during the 1960s. In both leagues, one of the major motivations for the change was the dominance of large-market teams. In both cases this dominance declined significantly in the decade following the adoption of the draft. Likewise, professional football, which employs a draft, produces contests that are significantly closer, on average, than those produced by major college football, which does not.

4. All major sports leagues in all countries (including revenue-generating amateur leagues in which residual claims are diffuse and the monopsonistic rationale is accordingly weakened) impose restrictions on the movement of players. In the absence of laws or regulations compelling their use, it is difficult to understand the widespread and persistent dominance of such institutional forms if they do not possess efficiency properties. If such properties do not exist, the implied "exploitation" of a unique resource critical to a league's existence would make it vulnerable to competition from leagues employing less restrictive methods.[34] Yet new leagues that have arisen to challenge existing ones have adopted similar player-contracting practices.

In sum, it is plausible to suppose that professional sports leagues, like most other economic organizations, operate more efficiently by using alternatives to market contracting for certain purposes, particularly for transactions involving economic agents whose subsequent behavior is capable of imposing significant costs on their operations. To label such practices as "unfair" or "anticompetitive" misses this point. Such assertions, as well as policy prescriptions based on them, should be reexamined.

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34. As Fama and Jensen (1983, p. 327) note, "Most goods and services can be produced by any form of organization, and there is competition among organizational forms for survival in any activity. Absent fiat, the form of organization that survives in an activity is the one that delivers the product demanded by customers at the lowest price while covering costs. This is the telling dimension on which the economic environment chooses among organizational forms."

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