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**Title:** An Investigation Into the Collective Bargaining Relationship Between the NHL and the NHLPA, 1994 - 2005

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# AN INVESTIGATION INTO THE COLLECTIVE BARGAINING RELATIONSHIP BETWEEN THE NHL AND THE NHLPA, 1994 – 2005

An Examination of the Causes behind the Escalation of Player Compensation Between 1994 and 2004 Leading to the 2004-05 NHL Lockout

By

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A paper submitted to the School of Policy Studies in partial fulfillment of the requirements for the Master's of Industrial Relations degree

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ABSTRACT

This paper analyzes the workings of the collective agreement that governed the relationship between the National Hockey League and its Players' Association from the 1994-95 season until 2004. By examining the elements and processes of the collective agreement, the nature of negotiation, and the roles of agents, owners, general managers, and arbitrators, some insight has been achieved with regard to understanding the significant increases in player compensation that occurred over that ten-year period, setting the stage for the 2004-05 negotiations and season-long lockout.

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# Chapter 1 INTRODUCTION

On September 15, 2004, upon the expiration of the NHL-NHLPA collective bargaining agreement, NHL Commissioner Gary Bettman initiated what would become a 301-day lockout of the NHL's players and result in the cancellation of the 2004-05 season. Citing cumulative losses of $1.8 billion to the league's teams over the previous ten years and an escalation in player salaries of 220% over that same period, the NHL and its owners united toward achieving significant change to the collective bargaining relationship by having player compensation rationally related to league revenue. The NHL Players' Association, led by Executive Director Bob Goodenow, publicly entrenched their position as one that would never accept a proposed system by the NHL that operated under a salary cap[i], preferring "market forces" to dictate the terms of players' salaries. As a result of continued positional bargaining, the NHLPA's unwillingness to acknowledge the need for substantial reform to the system, and NHL management's insistence on such reform, on February 16, 2005 the National Hockey League became the first professional sports league in North America to cancel an entire season because of a work stoppage. Players forfeited a combined $1.133 billion in salary before a resolution to the impasse was reached, and the financial implications to businesses and people external to the NHL, yet, dependent on it for revenue (apparel, bars and restaurants, arena staff) were equally remarkable.

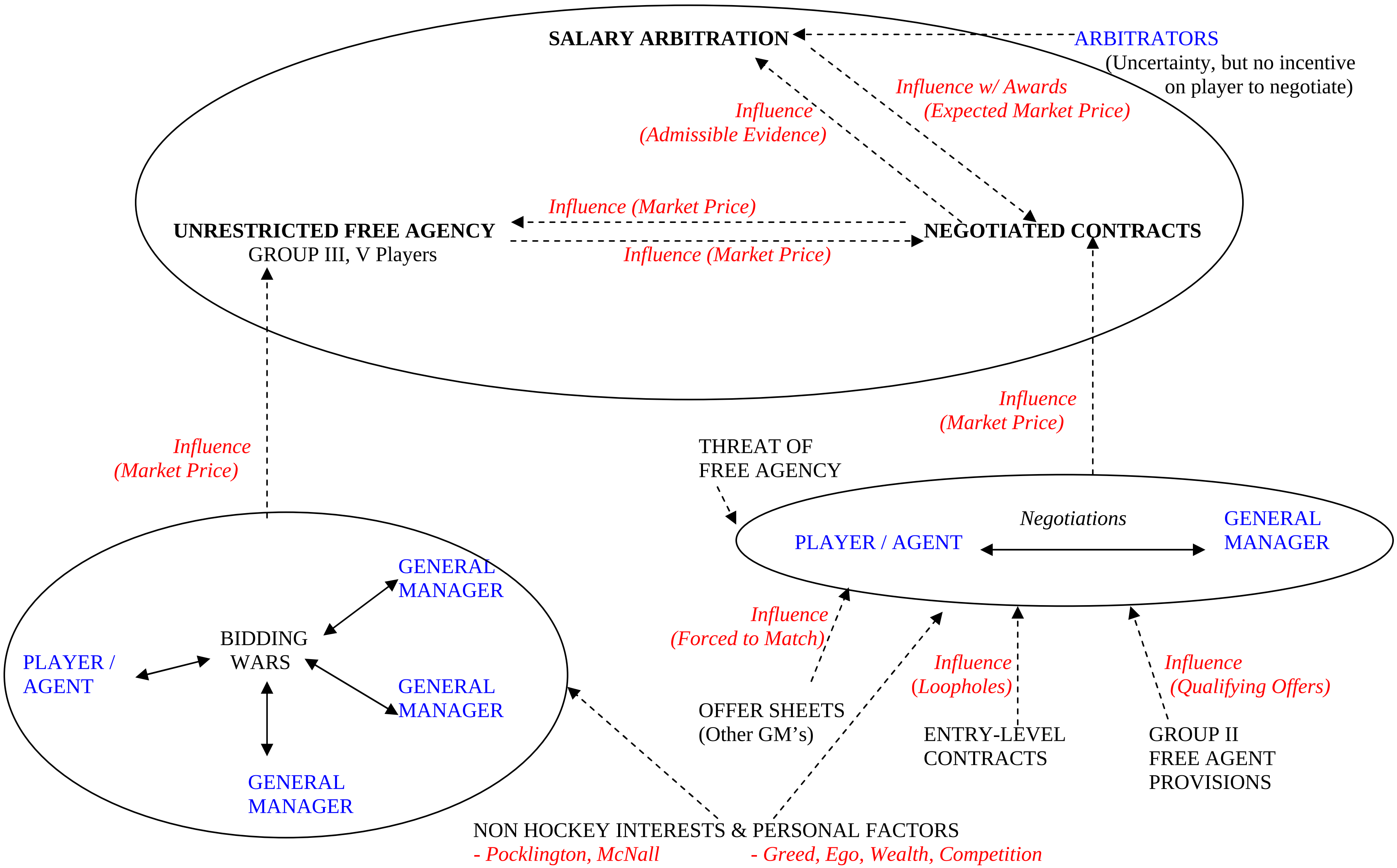
This paper will provide a post-mortem analysis in an effort to explain the root causes behind the substantial inflation of player salaries experienced in the NHL between 1994 and 2004, ultimately leading to the 2004 lockout and a new collective agreement. Particular attention is given to negotiation theory and the nature of arbitration. The resulting analysis makes it clear that the NHL-NHLPA collective bargaining relationship required significant change. The structure of the system was one that fostered inflationary pressures on player salaries, increasing average player compensation to $1.8 million in 2003-04 – a level unsustainable for the NHL's continued operation. Nonetheless, the NHLPA was adamantly opposed to these changes and geared their collective-bargaining strategy accordingly.

A literature review was conducted to ascertain what has been written and offered as explanation of the workings of the just-expired collective agreement, and therefore establishes the current knowledge from which this paper will attempt to move forward.

Chapter Three provides a historical background to the NHL-NHLPA bargaining relationship. This is required in order to properly understand the context in which the collective agreement that governed the NHL and NHLPA between 1995 and 2004 was created.

Chapters Four through Six examine the integral elements of the recently-expired collective agreement – the entry-level compensation system, restricted free agency, and unrestricted free agency – that have contributed to the escalation of player salaries. Chapter Seven analyses the processes of salary arbitration and the role it has played regarding salary determination.

In the course of the analysis set out in chapters 3 though 7, I developed a model as a representation of the various components, forces, and processes at play in the NHL salary-setting system. It is set out and described in Chapter 8. However, in order to provide something of a focus for the reader from the outset and to emphasize the interconnectedness of all of the elements, it is also set out here. While it may appear somewhat daunting at this point, it is hoped that the following chapters will make its workings clear.


SALARY ARBITRATION
ARBITRATORS
(Uncertainty, but no incentive
on player to negotiate)
Influence w/ Awards
(Expected Market Price)
Influence
(Admissible Evidence)
Influence (Market Price)
UNRESTRICTED FREE AGENCY
GROUP III, V Players
NEGOTIATED CONTRACTS
Influence (Market Price)
Influence
(Market Price)
Influence
(Market Price)
THREAT OF
FREE AGENCY
Negotiations
PLAYER / AGENT
GENERAL
MANAGER
GENERAL
MANAGER
BIDDING
WARS
PLAYER /
AGENT
GENERAL
MANAGER
GENERAL
MANAGER
Influence
(Forced to Match)
OFFER SHEETS
(Other GM's)
Influence
(Loopholes)
ENTRY-LEVEL
CONTRACTS
Influence
(Qualifying Offers)
GROUP II
FREE AGENT
PROVISIONS
NON HOCKEY INTERESTS & PERSONAL FACTORS
- Pocklington, McNall
- Greed, Ego, Wealth, Competition

## Chapter 2 LITERATURE REVIEW

Many authors of differing backgrounds have commented on various issues surrounding the National Hockey League. It was necessary to identify those authors who examined the elements central to this paper – salary determination, negotiation, and arbitration – in order to properly conduct a literature review. Each author discusses one or more of these issues to varying degrees of depth, and by doing so, their works establish the frontier of understanding from which this paper moves forward.

Former NHL Executive, player agent, Vancouver Canucks General Manager, and now current Anaheim Mighty Ducks General Manager, Brian Burke published a paper entitled *Negotiations Involving Agents and General Managers in the NHL* (Burke 1994). This paper sets out several ideas regarding contract negotiation, which clearly provide a basis for salary inflation. Even though this paper was written at the beginning of the previous ten years of the just-expired collective agreement, the comments he submits have indeed been validated by experience. Burke notes the incentive for general managers to work with agents to circumvent the confines of a collectively-bargained salary system (p.35). Essentially, general managers and agents will attempt to uncover loopholes in a collective agreement to manipulate the salary structure to best suit their needs. Burke also notes the necessity for flexibility and preparation in negotiation: "The general manager generally has less time to prepare than does an agent" and "The more acceptable alternatives you have, the greater the chances of making a deal" (p.37). When the party controlling the funds is less prepared and an agent can make creative use of loopholes or latently inflationary terms – terms that initially do not appear to have inflationary tendencies, but when manipulated appropriately put upward pressure on salaries – in the collective agreement, a negotiation can be very conducive to resulting in a higher salary for the player.

Although limited in scope for the purposes of my paper, Burke's insight regarding the negotiating behaviours of agents and general managers provides a basis for understanding the many dynamics to be considered.

Professor Ed Ratushny wrote an article entitled *Dispute Resolution in the National Hockey League* (Ratushny 1992) that discussed the NHL's salary arbitration system prior to the 1995 collective agreement. He comments on the nature of the system being inherently biased in favour of the owners and league, most notably, the Rules of Procedure:

> The Arbitrator may, however, consider such information concerning the compensation payable to other players in the League as may be provided by the League to the Arbitrator. This information shall not be disclosed to any person by the Arbitrator.

Therefore, the Arbitrator could receive information from the league, without the player's knowledge. This allowed the league to select comparable players that favoured the team's position, which hampered the player's ability to receive a fair hearing. Salary disclosure helped to minimize the effect of this one-sided rule.

A second bias that existed in favour of the league at salary arbitration, highlighted by Ratushny and unique to the NHL, was that the Rules of Procedure specifically prohibited private communications between the parties to an arbitration and the arbitrator. This appeared to be a rule that preserved the neutrality of the process; however, it must be noted that the President of the NHL was not considered a party to arbitration hearings. Therefore, communications from the President to the arbitrator were not prohibited. This had significance, as any result which favoured one of the parties is in the interests of all of the teams whom the President represents. There was great incentive for the President to influence the outcome of the arbitration hearing, and this was indeed demonstrated in a case between Joe Sakic and the Quebec Nordiques (Ratushny 1992:245). In this case, the NHL President sent a directive to the arbitrator indicating that he should only consider base salary, not performance bonuses, earned by comparable players to determine an appropriate salary for Sakic. By doing so, he suppressed the potential compensation level that could be awarded to Sakic by the arbitrator, effectively removing the impartiality of the process.

Similar to the paper by Burke, Ratushny focuses on one specific element under the NHL's collective-bargaining regime, but in doing so, sets the context in which the changes to the arbitration system under the 1995 agreement must be considered.

Player agent Stephen Bartlett wrote a paper in 1994 entitled *Contract Negotiations and Salary Arbitration in the NHL… An Agent's View* (Bartlett 1994). In this paper he submits that one of the major contributing factors allowing salary escalation has been the public disclosure of player compensation. The impact of disclosure, Bartlett contends, has been greatest upon the negotiation and arbitration processes. No longer is one party holding all of the bargaining power through information. Concerning free agency, Bartlett's states

> With a total free agent, one should be able to get fair market value for the player because there are no restrictions on the marketplace. Representatives are free to shop players to all teams. With some creative selling and promotion, the player will be able to reach whatever price the market will bear. When the bidding stops, you have reached market value. (p.3)

Bartlett clearly identifies the intent and action of agents to “shop” players between teams. The selling and promotion mentioned often refer to creating a bidding war between wealthy team owners. Bartlett’s concept of a bidding war determining “market value” contrasts the notions surrounding bidding wars put forth by Neale and Bazerman, which will be explained in detail later in the paper. What should be noted is that he equates “whatever price the market will bear” to “market value.” In conjunction with this bidding war, Bartlett relates the potential for such an occurrence to be used as leverage in negotiations. Although clearly identifying the bargaining power this position offers, he falls short of establishing the connection between such power and the subsequent profound escalation of player salaries that took place over the 1994-2004 period.

Regarding the arbitration process, Bartlett refers to it as “an important weapon in the negotiation process” (p.11) that can encourage parties to negotiate in good faith. The uncertainty associated with a potential arbitrator’s award can encourage risk-averse parties to reach a settlement. However, this runs counter to the chilling-effect theory, which will be explained later.

Again, as with the above comments by Bartlett regarding free agency and negotiation, the essential elements are here to explain rising salaries, but Bartlett stops short of establishing the interactions between these elements and the inflationary spiral that can result.

Author Mark Edge published *Red Line, Blue Line, Bottom Line: How Push Came to Shove Between the National Hockey League and its Players* in 2004 (Edge 2004). This book considers how the bargaining environment was shaped in the NHL over the previous ten years, what the key issues were in the 2004-05 bargaining dispute, and what can be learned from the other professional sports leagues. This book proposes two factors, both heavily influenced by salary disclosure, which contributed to the salary inflation experienced: the unrestricted free agency system and salary arbitration (p.107). With regard to unrestricted free agency, the idea was to have it occur at an age later in a player's career (now 31 in the NHL) in the hopes of limiting the number of free agents and therefore the number of big-money signings. What Edge then observes is that simple laws of supply-and-demand economics reverse this theory. With fewer free agents available (supply) owners will drive their prices up through bidding wars (demand) (p.7).

Turning his attention to arbitration, Edge observes that salary disclosure has made the process much more effective for players and agents, as their ability to identify and submit meaningful comparables as evidence can greatly enhance their position for a salary increase. Furthermore, Edge indirectly notes that NHLPA Executive Director Bob Goodenow understands arbitrator decision making – specifically the degree to which it is based on comparables. This has allowed Goodenow to devise a strategy for presenting cases at arbitration in an order that gives each one the best chance for success. By ordering arbitration cases in such a manner, Goodenow takes advantage of the importance of the first few settlements – the comparators – in any given year. Goodenow utilizes favourable arbitration settlements at the early stages as comparables and framework for the following cases.

Edge identifies the role arbitration has played in escalating salaries, as well as free agency, but there is little or no mention of how, if at all, these two factors interact in the overall scheme of the NHL compensation setting.

Russ Conway of Philadelphia's *Eagle Tribune* and the author of *Game Misconduct* – the book that uncovered and detailed the corruption of Alan Eagleson – has also offered some valuable insight into explaining the NHL's salary inflation in the 1994-2004 period (Conway 2005). Questionable management and contract offers by GM's have certainly played a role, but the true problem is the "arbitration system that allows players to use the mistakes of free spending general managers and owners to wring fat salaries out of the smarter ones" (p.1). In essence, players and agents use the arbitration system to leapfrog each other as a new pay scale is established with an arbitration award. In turn, owners fear a generous award from an arbitrator and offer large salaries to their players in order to avoid the process. That new salary then sets the precedent for other signings and awards. In other words, there is a secondary impact of arbitration: large salary increases designed to avoid the process.

The setting of unrestricted free agency at a later age in a player's career was meant to limit the number of large signings; however, with arbitration available to players in their mid to late 20's, much younger players are able to earn high salaries. The impact of one big award or signing is that it will then be used as a "comparable" in future awards and negotiations. This creates the leap-frog effect, with the only (and albeit rarely used) alternative to the owners of walking away from an award and losing the player. Conway advances the work of Edge by making the connection between how the arbitration system can influence and interact with conventional contract negotiations. This interaction will be explored in detail in this paper as it has played an integral role in the determination of salaries.

In 2003 author Bruce Dowbiggin published one of the more authoritative works that details the sources behind salary escalation in the NHL over the previous ten years (Dowbiggin 2003). Citing the entry-level contract loopholes, the nature of free agency, the Joe Sakic signing of 1997, and salary arbitration, Dowbiggin discusses arguably the most important factors that contribute to salary inflation. In 1997, the collective agreement stipulated that the maximum allowable salary that could be paid to an entry-level player was $925,000. However, through the use of performance bonuses and creative contract language, Boston Bruins rookie Joe Thornton had the potential for his salary to reach upwards of $2.25 million a season. What Dowbiggin observed, was that "the entry-level cap on rookie salaries was a paper tiger" (p.190). Referring to free agency, Dowbiggin then comments on how both parties at the negotiating table contribute to salary escalation when he states: "Faced with a player he desperately needs – to fill a building, get a new TV contract, or win a title – an owner or general manager will find the money. And an agent with a hot property can and will drag the last dollar from a deal" (p.192). To complete the circle, an agent and general manager creative enough to circumvent the confines of a seemingly restrictive collective agreement will remove the harness of a salary cap. The Joe Sakic signing in 1997 also had a significant impact, as noted by Dowbiggin: that other teams can influence the negotiation process through submitting offer sheets to restricted free agents.

According to Dowbiggin, salary arbitration has also played a significant role, because the system is one driven by comparables. The author then makes a link between contract signings and arbitration quoting New Jersey Devils General Manager Lou Lamoriello as saying "All it took was one or two people to give Group Two players big contracts and then you were dead for arbitration" (p.221).  The ability to use these large negotiated contracts as evidence in salary arbitration indicates a profound linkage between the two elements.  This linkage is not explored in great detail by Dowbiggin; however, this paper will move forward from previous research by expanding on this issue.

Furthermore, agents quickly realized the potential gains to be made in salary arbitration and sought to capitalize upon them.  Owners and general managers were not all able to match the level of preparation for hearings maintained by agents, and thus, awards favourable to the players were given.  The manner in which the salary arbitration system operates and how agents were able to effectively exploit it, contributed significantly to the inflation of player salaries.

Dowbiggin's work builds on Conway's in that he is able to note that interactions do occur between more than just two elements of the NHL's collective bargaining system.  Noting the influence of player agents and general managers with financial means, there are indeed a great many contributing factors to the observed salary escalation.  Dowbiggin has moved from dealing with the issues separately but appears only to deal with some of them in small groups, interacting with only one other element.

In a paper entitled *Legal Analysis of the NHL Player's Contract* (Weiler, 1993), Professor Joseph Weiler comments on the restrictive nature of the NHL free-agency system, stating, "Given the compensation required for signing another team's Group I or II free agent, it's no wonder that few players at this stage change teams" (p.67).  What Weiler fails to note is that even though movement may be limited, the mere threat of movement can entice owners and general managers to offer above market-rate salaries out of fear of losing their star players. As a result, other players across the league have the benchmark for salaries raised. Unlike some previous authors, Weiler does take the next step in identifying that many factors, not just one or two, have resulted in the escalation of player salaries.

> The combination of players who moved between teams, whether as free agents or holdouts insisting on trades or more generous teams, or who received offers from other clubs that their old club decided to match, or filed for salary arbitration and ultimately settled or received an award, has resulted in a rapid escalation of salary levels in hockey (p.74).

Aside from noting the role of the NHL's collective agreement in providing an arena for such consequences, the nature of negotiation between player agents and general managers, and the tendencies and theories of arbitration, Weiler has presented the majority of the contributing factors to salary inflation. Unfortunately, some elements are omitted, but most regrettably a connection between all the factors and the way in which they interact is not present.

The starting point of this paper is where previous studies and commentaries have left off. Brian Burke's commentary on the nature of agent-general manager negotiation is extremely valuable and from the most credible of sources. Ratushny provides a useful perspective on the process of salary arbitration prior to the 1994 collective agreement and, thus, on the degree to which that collective agreement modified the process. Stephen Bartlett's ideas on free-agent bidding wars and the role of salary arbitration, albeit from a somewhat-biased perspective[2], in combination with those notions put forth by Mark Edge, provide useful contributions. Russ Conway advances our understanding by identifying that there are interactions between two of the inflationary elements in the system – negotiated contracts and arbitration. Bruce Dowbiggin's work has been the most comprehensive, as he details how some amount of interaction between elements can occur in more than one instance. Finally, Weiler expands on what was mentioned by Dowbiggin, as further contributing factors such as offer sheets from other general managers and generous owners have influenced salary determination.

Clearly, there are many factors to be considered when investigating the sources of salary inflation in the NHL. However, although almost all factors have been identified and explained by some of the above authors as a cause for salary inflation, they have been kept in isolation or restrictive pairings. This limits full understanding of the situation. In short, further analysis is required, and that is what this paper attempts to accomplish: an investigation of all the elements and the potential and actual interactions between them. The concept that more than two elements can, and do, interact with each other, influenced by owners, manipulated by player agents, all in the context of – and governed by – the collective agreement needs to be explored. Through analysis of these interactions, in combination with relevant principles of negotiation and arbitration theory, a clearer picture of this very complex system can emerge. Furthermore, by setting this analysis in the context of the nature of business and economics, as well as the game of hockey from a non-academic standpoint, a new and more profound understanding of the situation can be realized.

Before examining the recently-expired collective agreement in detail, it is important to understand the historical aspects of the National Hockey League and the interests of the respective parties that contributed to the crafting the 1995 agreement.

## Chapter 3 HISTORY OF NHL-NHLPA RELATIONS

### 3.1 The NHL Reserve System

Since its formation in 1917, the National Hockey League has become a multi-billion-dollar industry in North America. Thirty teams, comprised of the most talented players in the world over the age of 18, compete annually for the Stanley Cup. In the "Original Six"[3] days of the National Hockey League, owners had virtually unfettered control over a player's career. They were, for practical purposes, "owners" of NHL players for life. Essentially, those hockey players looking to become professionals would sign a contract with one team and could play only for that team throughout their entire career. Once signed, a player became the property of the team owner to manage and - more importantly, pay – as he pleased. This system, known as the "reserve clause," allowed owners to dictate where individuals would play, the terms of their contracts, and salaries. If an owner so desired, a player's rights could be sold or traded to another team owner at the owner's discretion. With the reserve clause preventing players from being able to play anywhere else in the league unless sold or traded, their bargaining power was all but non-existent. Given that the NHL was the only professional hockey league, the players were hostage to this reserve system as there was no alternative in professional hockey.

The bargaining power of owners was further enhanced by the lack of dissemination of information. Little or no information was available to the players regarding the financial capabilities of their club or the salaries of other players on their team, and owners sought to keep it that way. This inhibited any meaningful negotiation attempts on behalf of the players regarding their salary, as no comparables or credible evidence existed to support their reasoning. Furthermore, the NHL offices and owners discouraged players from disclosing their salaries to each other, enlisting the services of agents, or socializing with opponents.  This meant that, regardless of how profitable a season was for the owner, or how well a player performed on the ice, negotiations were almost moot as all the information was held by one party.  An owner could tell a player that he was only worth $8,000 a year in salary, or that's all he could afford to pay him, and the negotiation all but concluded.

An example of how determined the owners were to depress player salaries by making use of the bargaining-power imbalances, lack of information, and reserve clause, is highlighted by a discussion between Gordie Howe and his teammate Bobby Baun in 1968.  Gordie Howe, one of the greatest professional hockey players in history, was playing for the Bruce Norris-owned Detroit Red Wings.  Norris had promised his franchise player that he would always be the best paid player on the team.  Off the ice, Howe's temperament greatly contrasted his on-ice demeanour – where players often noted his exceptionally sharp elbows – and he contentedly accepted his owner's words as truth.  Howe's salary in 1968 was $45,000 a year.  During a discussion with teammate Bobby Baun that season, Howe was surprised to learn that Baun was making $67,000 a year.  Furthermore, Baun enlightened the previously naïve Howe that another teammate, Carl Brewer, was making $90,000 (Cruise, 1991:8).  When deciding to raise his concern over the misleading promises by Bruce Norris after decades of being a star player, Howe was threatened with a libel lawsuit by Norris and NHL President John Ziegler, as a means to silence Howe's dissatisfaction with his owner's behaviour.

This situation was not unique to Howe, as owners throughout the league engaged in varying forms of such conduct to keep the salaries of their players depressed.  In conjunction with the reserve clause, owners prevented any "marketplace" in which players could discover their value by agreeing amongst themselves to minimize player movement between teams. Fortunately, from the players' perspectives, an end to this type of system was on the horizon. American antitrust laws passed in the latter part of the 19th Century made it illegal for businesses – that were supposedly competing against one another – to conspire together in a "trust" to keep prices artificially high and/or wages artificially low (Edge, 2004:23). The reserve clause in the National Hockey League was challenged and found to be in violation of these antitrust laws (Adams 1992). However, not until the expiration of the collective agreement in 1992 was the reserve clause legally removed, after years of allowing for the collusion of owners, depression of salaries, and treatment of players as property.

One might wonder why, with the NHL Players' Association having been in existence since 1967 and a collective-bargaining regime extant between union and management, the players endured such continuous restrictions on their rights. The answer to this question is Alan Eagleson.

### 3.2 NHLPA Formation and Operation under Eagleson

Alan Eagleson had been affiliated with the National Hockey League, its owners and players, for much of the 1960s as a player agent, enterprising businessman, and developing politician with the Ontario Progressive Conservative party. Throughout the 1966-67 season, Eagleson enlisted every active National Hockey League player to the cause of a players' association. There was much hesitation among the players because of the perceived threat they saw to their careers, especially those in the lower portion of the talent pool, after a failed players' association attempt in 1957, which had been brutally suppressed by the owners.[4] Being the convincing orator, however, "the Eagle" gained the players' trust and commitment and overcame their reluctance, and so began the National Hockey League Players' Association. Owners were naturally displeased with these developments, but since the then notorious Teamsters Union was beginning to cause some rumblings with the league, Eagleson seemed to be the lesser of two evils. This would soon prove to be an understatement, as league president Clarence Campbell observed, "I don't like unions, but I'm glad it's Eagleson at the head of the Players' Association rather than somebody else" (Houston, 1993:51).

It wasn't long before Eagleson began working for his own interests to the detriment of the players. Collective bargaining between the NHL and NHLPA Executive Director was more a farce than anything resembling adversaries properly representing constituents. While the Players' Association in Major League Baseball was moving toward free agency for its players, Eagleson hadn't removed the reserve clause or challenged the artificial restraints on salaries imposed by owners. It was observed by future NHL president Gil Stein during this time that Eagleson and NHL President Ziegler effectively orchestrated the business of the league between themselves, saying, "It does not take a great stretch of imagination to believe that when Eagleson and Ziegler led their respective troops into collective bargaining negotiations, the results might have been pre-ordained" (Dowbiggin 2003:55).

The negotiation relationship pattern of the NHL-NHLPA collective-bargaining regime during Alan Eagleson's tenure can reasonably be characterized as collusive (Selekman & Selekman 1958).[5] Between the parties, trust was established on a basis of "mutual blackmail" potential, in the sense that neither Eagleson nor the NHL wanted the players and agents to become completely aware of their bargaining behaviours, and the degree of friendliness was one of a “sweetheart relationship”. Furthermore, with the assistance of NHL Executives, Eagleson would give attention to areas not really legitimate within the mandate of his principals (the players), but instead to realize personal benefits at their expense. With the lowest average salary in North American professional team sports (hockey, football, basketball, and baseball), the lowest minimum wage, the lowest percentage of gross revenues going to players, and a one-sided and ineffective collective-bargaining arrangement, it was no surprise that Ziegler and Eagleson were friends, nor was there any doubt whose interests were subordinate (Cruise 1991:308). Clearly, the true nature of the collective-bargaining relationship that existed between Alan Eagleson and the NHL was collusive (Selekman & Selekman 1958) in the sense that the players’ interests were sold out for Eagleson’s personal gain.

The ousting of Eagleson as Executive Director of the NHLPA began at an annual general meeting in 1989. His pension mismanagement[6], mysterious issuing of below market-rate loans to Eagleson’s friends with Players’ Association money, and a host of other issues all came to the attention of the players and were aired with enthusiasm. Only by a vote of the NHLPA Executive Board (all handpicked by Eagleson) did he manage to remain in charge. However, steps had begun to find his replacement. By 1992 his legal troubles with the FBI forced his resignation from the NHLPA. Suddenly, with the US and Canadian governments now examining his financial dealings, the players became aware of just how badly they have been led astray (Dowbiggin 2003:60).

Eagleson’s replacement was a Harvard-educated lawyer named Bob Goodenow, who had been working in the NHLPA offices for several years already, but managed to distance himself from the corruption that was being uncovered. Eagleson recommended Goodenow to the owners, indicating that bargaining with him would come with relative ease and continued prosperity. Little did they understand just who Bob Goodenow was, but they were about to receive a quick education on the issue. That meeting in 1989 marked the end of Eagleson's control of the NHLPA and ushered in a new era for the players. The era of Bob Goodenow, salary disclosure, and "Gretzky money" was about to begin.

### 3.3 The Gretzky Deal - 1989

The elements that shaped the crafting of the recently expired CBA can be traced back to 1989: Eagleson was in the process of being ousted, Bob Goodenow was about to take the reins of the NHLPA, the players voted in favour of salary disclosure, and the biggest trade in hockey history was made.

Despite winning four Stanley Cups over the past five years, Edmonton Oilers' Owner Peter Pocklington no longer had the means to finance other failed business ventures with his NHL club's revenues. What he did possess, however, was the greatest player of all time in Wayne Gretzky, and in Los Angeles Kings' Owner Bruce McNall he found a wealthy buyer. With both the means and desire from both parties to create "the deal", it was done and the hockey world was shocked. Wayne Gretzky was traded from the hockey hotbed of Edmonton to the Hollywood glitter of Los Angeles. If the mere fact of the Gretzky trade wasn't resounding enough, the financial terms of the deal were even more remarkable. Gretzky's new contract with the Kings would be an unprecedented $3 million a year in salary (up from $1.7 million) and along with a host of players being sent to Edmonton, Los Angeles also paid $15 million in cash to Peter Pocklington for the rights to Number 99. This was an unprecedented deal that rattled the very foundations of a business with a history of underpaying its players. Not only did it reveal just how great a means some of the owners had to pay players, but also their willingness to do so when the reasons seemed right.

The reasoning behind the Gretzky deal was unique, given the respective needs and capabilities of the two principal parties – Pocklington and McNall. What must be noted was that although this deal had substantial effects on the hockey salary structure, the forces behind its formation were driven by non-hockey needs. McNall needed a star attraction for his team in a market that knew and cared more about Hollywood gossip than hockey. Pocklington needed an influx of cash to keep his financial head above water. In the context of hockey and the NHL, these are, in a sense, irrational influences. Yet, these atypical, non-hockey motivations, induced the two parties to create an unparalleled deal, the effects of which were quickly realized across the league.

Former NHLPA Executive Director Bob Goodenow remarked, "There's no doubt the Gretzky deal catapulted the salary structure… There is an ability to pay that's been unlocked" (Cruise, 1991:334). New Jersey Devils' General Manager Lou Lamoriello commented that "Gretzky's transfer to the second largest media market in the United States, coupled with salary disclosure in the next eighteen months, propelled players into the modern age of salaries" (Dowbiggin 2003:64).

The ripple effect first began with Pittsburgh Penguin Mario Lemieux. Lemieux, who by this time was rivalling Gretzky as the game's top player, sought to renegotiate his deal with the club after the Gretzky signing. With the precedent now set, the Penguins gave their star a new contract at $2.25 million a year. Then, revealing glimpses of negotiating savvy that was still to come, Bob Goodenow (acting as a player agent) negotiated a new deal for Brett Hull. Hull was one of the best scorers in the game at this time, but he had some defensive liabilities. Nevertheless, Goodenow convinced St. Louis that given "Gretzky-type" offensive production, he deserved "Gretzky money", and the result was a four-year deal for $7 million, up from his previous annual salary of $125,000 (an increase of 793% in the first year). The signing of this deal then began to force every team with a superstar to renegotiate contracts and pay them as a star player.

### 3.4 Salary Disclosure - 1989

In 1989, against the strenuous efforts of Eagleson, the NHLPA voted in favour of salary disclosure 469 – 49 (Adams 1989:H2). Salary Disclosure has had a substantial impact on all facets of the collective-bargaining arrangement between the NHL and NHLPA. Allowing the NHLPA to openly publish what all the players in the league were being paid in salary meant that information was no longer the preserve of one side at the table. Agents and players now had valid, comparable data on which to base their cases for a specified salary, and owners had to respect those data. The use of these objective criteria – the salaries of other players in the league – enabled players and agents to marshal the power of "fairness" (Ury and Fisher 1981), in the form of relevant comparisons. In reflection, current New York Rangers General Manager Glen Sather commented,

> The information [before disclosure] wasn't as readily available to everybody, and we kind of had things more in control. They were being paid well, but they weren't being paid as well as they could have been. (Dowbiggin 2003:113)

Agents and players could now look across the league, find players of arguably comparable ability, and justify a given salary proposal.

Availability of this data had a profound impact on the bargaining-power balance: after a mere two years of disclosure, the number of millionaire players[7] went from two (Gretzky & Lemieux) to sixteen. By 1991, the number of millionaire players was 33 (Edge 2004:124). Other owners began to see what their counterparts were offering players in salary and in turn were forced to adjust. What originally began as *de facto* collusion to depress salaries, was now developing into a fight within the community of owners. No longer were they working together for mutual benefit, but instead now forced to equalize and offer increased salaries compared to others in the league to retain their own players. Soon, this equalization would turn into fierce competition. Owners began to fight amongst themselves for a player's services, and in turn bid salaries upward. The pendulum had swung in favour of the players, and all that it needed were clever agents and an NHLPA Executive Director to open the floodgates with respect to player compensation.

### 3.5 Bob Goodenow, NHLPA Executive Director - 1992

In 1992, the NHL players officially accepted their new leader and Executive Director. Robert W. Goodenow graduated from Harvard University in 1974, where he captained their varsity hockey team. In 1979 he graduated from the University Of Detroit Law School and went on to practice in the areas of general, corporate and commercial law, labour law, and athlete representation. Being a hockey player, agent, and labour-relations professional, Goodenow brought promise of true representation of the players' interests, a hard-nosed negotiating style, and absolutely no doubt as to which side of the fence he was on. Immediately, Goodenow sought change for the players, and the NHL management was about to experience the kind of labour pressure he was prepared to inflict in pursuit of his players' interests. Players, wary of Eagleson's behaviour, and still largely ignorant of the realities of a traditional labour-management collective-bargaining arrangement, required great convincing by Goodenow to win their trust and support. Through countless meetings and interactions with hundreds of players, he soon had them rallied and united to fight for improvements (Dowbiggin 2003).

The first conflict came in 1992. After playing much of the 1991-92 NHL season without a collective agreement, and Goodenow and NHL President John Ziegler firing verbal shots back and forth through the media, the NHLPA and its new leader finally took action. In response to the lack of meaningful bargaining by the NHL, the Players' Association voted 560-4 in favour of a strike on April 1st, 1992. Although the season was still being played, Goodenow shrewdly chose the time when owners would be least receptive to a labour disruption. Players' salaries are paid out over the course of the regular season, not during the playoffs. Therefore, the playoffs represent the most significant revenue-generating weeks for the owners. By taking action at the beginning of April, the NHLPA put the playoffs in severe jeopardy and Goodenow calculated that was a risk owners were not willing to take. By April 11, just in time to save the playoffs, the strike ended with respectable gains realized for the players and the owners still in a position to collect their playoff revenues.

It was now very clear that the sweetheart labour deals of the Eagleson era were long gone, and an adversarial collective-bargaining relationship had begun. In terms of the Selekman and Selekman spectrum of labour-management relationships, the NHL and NHLPA had suddenly moved from "collusion" to "containment-aggression" (Selekman & Selekman 1958).

Bob Goodenow's vision for his players is best typified by a story of him sketching his theory on the NHL's economics on a bar napkin in a Toronto Pub:

> Goodenow put the rich clubs, such as the New York Rangers and Toronto, at the top of the napkin. The poorer clubs, such as Pittsburgh and Minnesota, he scribbled at the bottom. In the middle of the beer-stained napkin were teams such as Los Angeles and St. Louis, the NHL's middle class. "Here's where you find the fair market value of a player in today's economy," he said, jabbing the pen into the words "Kings" and "Blues" on the napkin. "Not up here with the Rangers and Leafs. In the middle. But the NHL wants them to be paid down here." He jabbed derisively at the words "Penguins" and "Stars" on the lower portion of his napkin. "And we're not going to get a settlement till we establish this" – he points to the middle-rank teams once more – "with the league." The pen clattered on the wooden tabletop and Goodenow sipped his beer (Dowbiggin 2003:117).

"Fair market value" is indeed a perception that often differs between opposing sides in a negotiation. Yet, it was his purposeful depiction of "fair market value" that drove Goodenow's objectives in collective bargaining and representation of the players. Through his efforts, the NHLPA has become one of the most cohesive and strategic labour organizations in North America, and that cohesion was challenged again when the NHL's new commissioner, Gary Bettman, became part of the scene.

### 3.6 The Advent of Gary Bettman - 1992

Gary Bruce Bettman came into the NHL in 1992, at a time when attendance was flourishing, revenues from new arenas were flowing in, expansion fees were plentiful, and great opportunities existed to grow a partnership with the NHL owners and television. This prosperity, however, was balanced off by the facts that league average salary was up to $570,000, and rookies such as Eric Lindros and Alexandre Daigle had just signed unprecedented multi-million-dollar deals before even playing one game in the

NHL.[8] The collective agreement had expired in 1992, but was extended through the 1993-94 season to allow Bettman to settle into his new position. This marked the fall of 1994 as time for another labour showdown, and the eventual creation of the collective agreement that would be the focus of negotiations leading to the cancellation of the 2004-05 NHL season.

The owners entered this round of negotiations with several objectives: a payroll tax[9] that ranged from 100% to 200% of the amount by which a maximum was exceeded, the removal of salary arbitration, the elimination of guaranteed contracts, (meaning a team would not be forced to honour a player's contract for its entire duration, and could walk away at anytime, if the team so chose), buy-out provisions, reduced roster size, and meaningful restraints on rookie salaries (Dowbiggin 2003:175). Not surprisingly, the Players' Association resisted and, in September of 1994, concluding that more pressure was needed for the attainment of their goals, the owners initiated a lockout that carried through till January of 1995. It was only at this point, when the NHL was pressured by the potential of losing significant television revenues from FOX and the mounting costs of expensive new arenas, did it begin meaningful negotiations with the NHLPA. The league backed off their position of a payroll tax and elimination of salary arbitration, but held firm on limiting the ability of players to move during the prime years of their career. In turn, Goodenow had to make one concession – namely a salary cap on entry-level contracts. This met Bettman's need for restraint on salaries in light of the recent big rookie signings and satisfied Goodenow's concerns as none of his current constituents would be affected by the changes. It soon turned out, however, that this great concession on rookie salaries by Goodenow wasn't the restrictive clause Bettman wanted after all.

The cap on rookies' salaries would exist for up to the first three years of their career, depending on what age the player was when the contract was signed. The maximum allowable salary would be $875,000 in 1996, increasing to $1.075 million over the years of the collective agreement, with no free agency or arbitration rights. Goodenow agreed to allow no significant free agency before age 32 for players until 1999, then not until age 31. Group II free agents (to be discussed later) could be signed by other teams, but teams signing them would have to provide compensation in the form of up to five first-round draft picks. As well, any team that matched a competing offer could retain its player, in theory rendering competitive bids virtually pointless (Dowbiggin 2003:182).

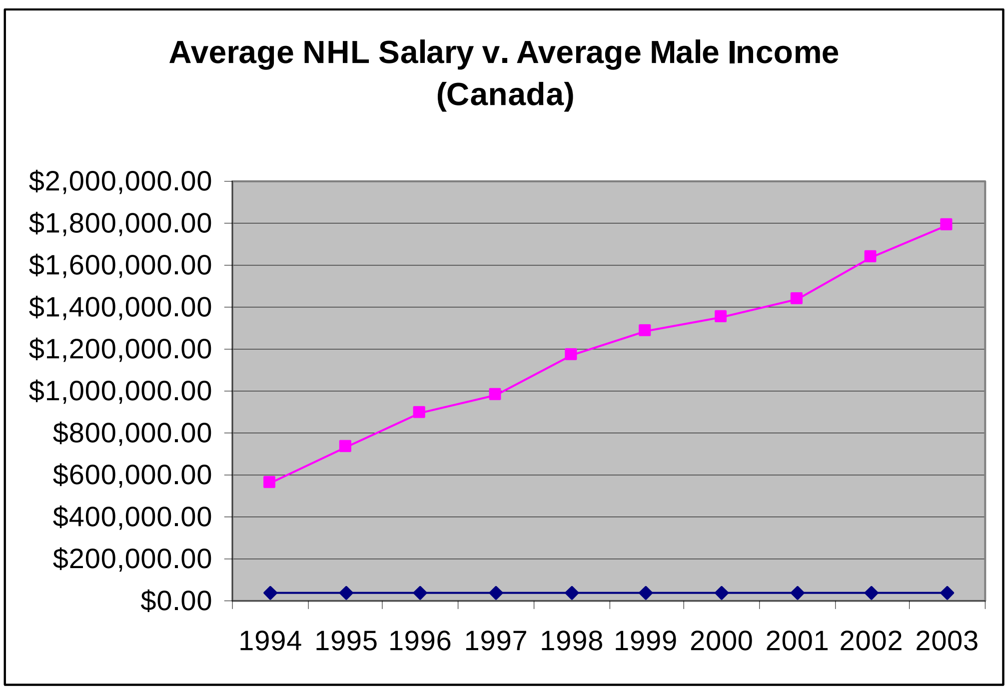
At the time, Goodenow was chastised in the media for giving far too much away and being way over his head in bargaining with Bettman. However, those who jumped to such conclusions were quickly and emphatically proved wrong. What Goodenow did was to preserve the essential elements for creating major salary escalation - free agency, salary arbitration, guaranteed contracts, and no salary tax or cap. As noted by Eric Duhatschek in the *Calgary Herald*,

> By getting a deal without a salary cap/luxury tax, the players effectively put the onus on owners to run their businesses efficiently. Some will try, but others will not be able to change the spending habits of a lifetime. All it takes is a handful of free-spending teams and all the contracts you couldn't comprehend before will appear almost logical in two years (Duhatschek 1995:C1).

Furthermore, Goodenow retained the scarcity of free agents, guaranteeing a bidding contest between owners for those few who hit the market each year, although that was not the intent of the owners at this time. Finally, the restrictive clauses on movement of Group II players through their high-compensation requirements, was to provide ample opportunity for salary escalation as owners matched competing offers to retain their star players. All of these interactions – founded upon terms of the collective agreement, influenced by wealthy and free-spending owners in competition with each other, exploited by clever player agents, and influenced by arbitrators – were the driving forces behind what was to become the remarkable salary escalation over the next ten years.

The following graph shows the growth in average NHL player salary as compared to average income of Canadian males, which increased from $36,700 to $39,100, or 10.6%, from 1994 through 2003. The average player's salary increased by 219.6%, or an average of 12.32% annually, compounded, over this period.

**Figure 3.1**




## 3.7 The NHL Structure 1994 – 2004

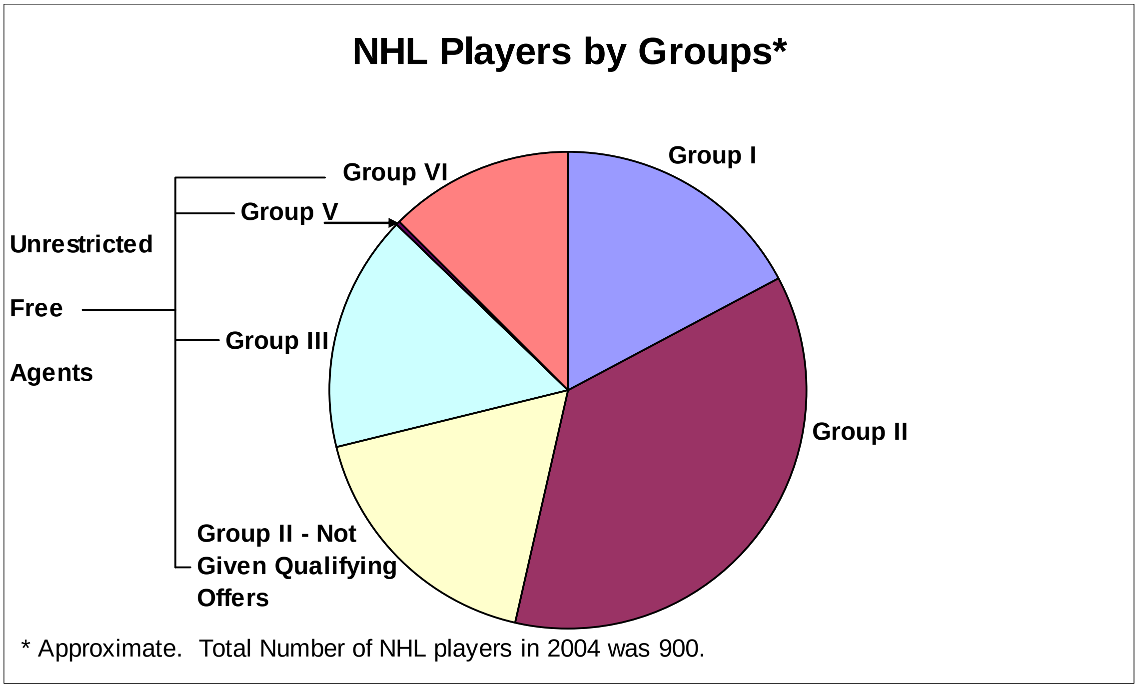
Under the NHL collective agreement signed in 1994, players were divided into one of six possible groupings, labelled, appropriately, Groups I – VI. The description of these groups is as follows:

**Table 3.1**

| | |
|---|---|
| Group I | • Entry-level players who are subject to a specified compensation structure for a given number of years<br>• Typically includes players aged 18 through 22 |
| Group II | • Players who are no longer governed by the entry-level compensation structure, but do not yet meet the requirements for unrestricted free agency<br>• Also referred to as "restricted free agents"<br>• Clubs must tender qualifying offers to retain their services<br>• Clubs have the right of first refusal and draft-choice compensation for these players<br>• No right of first refusal for players aged 26 or older |
| Group III | • Player is an unrestricted free agent after reaching 31 years of age and 4 seasons as pro<br>• No compensation owed to former club for player moving teams |
| Group IV | • "Defected" player – A player who has never signed an NHL contract, but his rights are held by an NHL team, and he is playing for a professional team not affiliated with the NHL<br>• *These players are not considered for the purposes of this paper* |
| Group V | • Player has completed 10 seasons as a professional, did not earn more than last year's league average salary, and has not previously elected to become an unrestricted free agent<br>• Can elect only once in career to become an unrestricted free agent<br>• Prior club receives no compensation |
| Group VI | • Player is 25 years or older, 3 seasons as professional, but has played less than 80 NHL games<br>• Player becomes unrestricted free agent, no equalization |

The distribution of the NHL's players among these groupings is as follows:

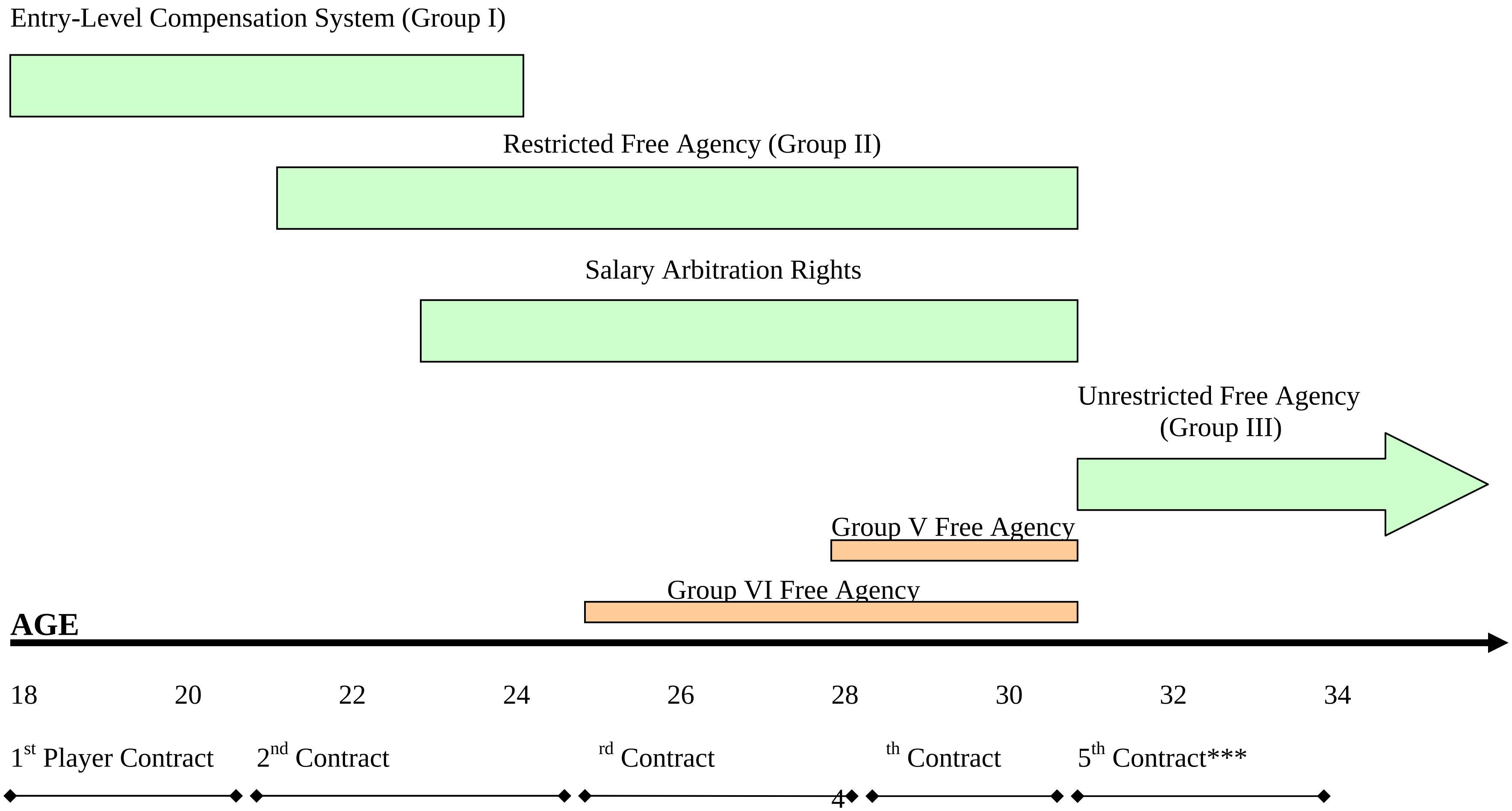
**Figure 3.2**




Throughout his career, a typical player will progress through these groups and be subject to the rights therein, as depicted in the following chart:

**Figure 3.3**

## Potential Progression of a NHL Player's Career




*A player may be eligible for only one group at a time. ** Only Group II players are eligible for salary arbitration. ***Approximate.

3

The period 1994-2004 was characterized by an unprecedented increase in player compensation (see Table 3.3). So dramatic was the increase that it has had a significant impact on the financial conditions of each of the 30 teams, and the NHL as a whole. This fact, which became the dominant reality of the failed 2004 negotiations, is obvious in the following tables.

**Table 3.2**[10]

| | 2002-03 | % |
|---|---|---|
| Combined Revenues | $1,996 | 100% |
| Player Costs | $1,494 | 75% |
| Other Operating Costs | $775 | 39% |
| Total Operating Costs | $2,269 | 114% |
| **Operating Loss, excluding depreciation, amortization, interest and taxes** | **($273)** | |

When examined on a team-by-team basis, the financial situation was as follows:

| Teams Reporting Operating Profits* | Number of Teams | Average (Loss)/Profit ($MM) | Highest (Loss)/Profit ($MM) | Combined (Loss)/Profit ($MM) |
|---|---|---|---|---|
| Over $10MM | 2 | $12.7 | $14.6 | $25.3 |
| $5MM - $9.9MM | 4 | 8.1 | 9.4 | 32.4 |
| Under $5MM | 5 | 2.4 | 4.3 | 12.1 |
| **Totals for Teams Reporting Operating Profits** | **11** | **6.4** | **14.6** | **69.8** |

| Teams Reporting Operating Losses | Number of Teams | Average (Loss)/Profit ($MM) | Highest (Loss)/Profit ($MM) | Combined (Loss)/Profit ($MM) |
|---|---|---|---|---|
| Over $30MM | 4 | ($35.5) | ($40.9) | ($142.0) |
| $20MM - $29.9MM | 2 | (23.2) | (26.2) | (46.4) |
| $10MM - $19.9MM | 6 | (16.9) | (19.0) | (101.5) |
| $5MM - $9.9MM | 6 | (8.2) | (9.9) | (49.4) |
| Under $5MM | 1 | (3.1) | (3.1) | (3.1) |
| **Totals for Teams Reporting Operating Losses** | **19** | **(18.0)** | **(40.9)** | **(342.4)** |

Clearly, with 19 teams incurring an average operating loss of $18 million ($342.4 million combined) and only 11 teams boasting an average operating profit of $6.4 million, the financial conditions of the league were not sustainable.

**Table 3.3**

| | **1992-93** | **2002-03** | **% Change** |
|---|---|---|---|
| League Revenues | $732 Million | $1.996 Billion | 172.7% |
| Player Costs | $414 Million | $1.494 Billion | 260.9% |
| Player Costs as Percentage of League Revenues | 57% | 75% | 31.6% |
| Average Player Salary | $0.56 Million | $1.79 Million | 219.6% |
| Average Team Profit / (Loss) | ($1.54 Million) | ($9.09 Million) | (490.3%) |

The focus of this paper now turns to how, under the structure of this collective agreement and associated processes, this economic situation developed.

# Chapter 4 ENTRY-LEVEL COMPENSATION SYSTEM

## 4.1 Group I Players

When Bob Goodenow and Gary Bettman signed the collective agreement in 1995 after the lockout, one of the supposed major victories for the league was a salary cap imposed on entry-level players. Also known as "rookies" and "Group I players" these are defined as those players who have not previously entered into a contract with an NHL team and are between the aged 18 through 24 years. The collective agreement dictated that, for Group I players, a specified compensation system was to be adhered to for a duration of up to three years depending on the age at which the first contract was signed.[11]

**Table 4.1**

| First Contract Signing Age | Period Covered by First Contract and Years in the Entry Level System and Subject to Compensation Limits |
|---|---|
| 18 – 21 | 3 years |
| 22 – 23 | 2 years |
| 24 | 1 year |

The duration of the entry-level salary-cap system also defined players' accession to the restricted free agency (Group II) provisions. The compensation system is set out in the following chart:[12]

**Table 4.2**

| Draft Year | Maximum NHL Compensation |
|---|---|
| 1995 | US $ 850,000 |
| 1996 | US $ 875,000 |
| 1997 | US $ 925,000 |
| 1998 | US $ 975,000 |
| 1999 | US $1,025,000 |
| 2000 | US $1,075,000 |
| 2001 | US $1,130,000 |
| 2002 | US $1,185,000 |
| 2003 | US $1,240,000 |
| 2004 | US $1,295,000 |

In addition to the salary-cap and time frames, the collective agreement contained Article 9.3(c), which stated:

> The aggregate of all Signing, Reporting and Roster Bonuses attributable to any League Year to be paid to a Group I Player may not exceed 50% of the player's Compensation for such League Year. Games-played bonuses attributable to a League Year shall be included in Compensation for that League Year at their full potential value (assuming all such bonuses are earned) and shall be treated as Paragraph 1 Salary.

This section meant that even if a team were to offer additional signing, reporting, and/or roster bonuses to a player, the total additional or bonus compensation must not exceed 50% of that player's compensation maximum for the league year. Following the above example, if a player's annual compensation is $975,000 then his bonuses must not have exceeded $487,500, giving him a total actual compensation level of $1.4625 million. Finally, compensation for achieving a games-played bonus was counted towards the salary maximum for that player. It was intended to create a sound salary cap to suppress Group I player compensation levels throughout the duration of the collective agreement. However, this was not the case because of the following provision:[13]

> For greater certainty, nothing contained in this Section 9.3 shall be deemed to limit the amount permitted to be paid to any Group I Player in respect of any Exhibit 5 Performance Bonus(es).

## 4.2 Exploitation of the Performance Bonus Clause

The restrictions on entry-level salaries did not suppress compensation as expected; instead, remarkable increases were seen. Given some time, player agents were able to discover and exploit loopholes in the collective agreement – most commonly identified as the performance-bonus clause – in order to get the largest amount of money possible for their clients. Exhibit 5 of the NHL/NHLPA collective agreement outlined provisions for performance bonuses for those players governed by an entry-level contract. Excerpts of that exhibit included the following:

> The following is a list of the performance bonuses that may be included in a player's contract during his entry level period. The Player and the Club are free to negotiate and agree upon any dollar amount to be paid for achieving the minimum or any higher level to which the Player and Club agree. Bonuses paid under this provision are outside the cap.
>
> 3. Individual Bonuses
>     1. Forwards
>         1. Ice Time. Player must be in top nine forwards on club.
>         2. Goals Scored: 20 Goal Minimum
>         3. Assists Scored: 35 Assist Minimum
>         4. Total Points Scored: 60 Point Minimum

For clarity, these bonuses were separate from, and in addition to, those outlined in Article 9.3(c), and were allowable under the collective agreement. Skilled agents were able to see several aspects of this paragraph favourable to increasing player compensation. First, the amount paid in compensation as a result of achieving performance bonuses did not count towards the cap on Group I player salaries. Second, it did not provide a limit on how many times a bonus might be included in a player’s contract. For example, the ice-time bonus was permitted to be included each year. Third, the player and the team were able to freely negotiate and agree upon any dollar amount for these bonuses, providing a basis for persuasive agents and wealthy owners to explore and exploit this provision. Essentially, the team and the player (with help of his agent) were free to negotiate *any* compensation level for any number of performance bonuses without being restricted by provisions of the collective agreement. This compensation was external and allowed in addition to the maximum-salary provision. Thus, in practice, Exhibit 5 of the collective agreement completely removed the ceiling that the league had previously thought to have existed over entry-level contracts.

The first substantial exploitation of the performance bonus clause came in 1997. That year, Harry Sinden, general manager of the Boston Bruins, signed number one draft pick Joe Thornton to the rookie maximum salary of $925,000. Sinden had a great desire to have Thornton in his NHL lineup as soon as possible, despite recommendations that he needed one more year to develop in the minor-league system. Capitalizing on Sinden's desire to have his young star play right away, Thornton's agent, Mike Barnett, convinced him to offer lucrative bonuses for achieving relatively easy accomplishments. Availing themselves of the possibilities provided by Exhibit 5 of the collective agreement, in addition to his annual salary of $925,000 Thornton would receive an additional $250,000 for each category attained, for a potential total of $2.3 million in addition to his salary.[14]

The deal was further enhanced through what were termed "balloon" bonuses. These were multiplier bonuses that increased compensation repeatedly for attaining more than one performance category. For example, by meeting two categories, Thornton's compensation "ballooned" to $1.8 million. Barnett also negotiated a provision that allowed these balloon bonuses to roll over from year to year. This meant that once Thornton scored 20 goals, in one year or cumulatively over two seasons, he received the bonus.

Thornton's deal, via Barnett's creative interpretation of the collective agreement and good negotiation, with the Boston Bruins in 1997 helped escalate salaries for Group I players. The next year, the Tampa Bay Lightening signed the first overall pick, Vincent Lecavalier, to the maximum $975,000 salary for rookies. However, with the performance-bonus clauses negotiated, he could earn almost twice as much as Thornton. Six performance-bonus categories were contractually established in his first year, and five for each of the following two years. Lecavalier's compensation for meeting these performance levels was to be $250,000 per category and similar to Thornton's deal, the same year-to-year roll over stipulation was in place. What set this deal apart was that if Lecavalier managed to attain the bonus for at least two of the five or six categories, he would get paid for all of them – a total of $3 million. This brought the potential compensation level up to an unprecedented $11 million over three seasons (Hodges 1998). Lecavalier did not actually reach such a level but, nevertheless, the framework had been set for the future. Agents and willing NHL owners have exploited this loophole in the entry-level contract structure since 1997, and young NHL players have not had their compensation meaningfully bound by the maxima set out in the collective agreement. For example, in 2002 the Atlanta Thrashers paid two of their rookies, Dany Heatley and Ilya Kovalchuk, $4 million and $4.375 million respectively in annual salary and bonuses.

These precedents have been available as comparables for agents to influence contract negotiations with general managers for their Group I players. How this influence continued past the expiration of a player's entry-level contract, as they enter Group II free agency, is also of significance and will be explained in detail shortly.

# Chapter 5 RESTRICTED FREE AGENCY

## 5.1 Group II Players

One of the major contributing and interacting elements with regard to salary determination was that of contracts negotiated by restricted free agents. Restricted free agents, also known as "Group II Players" in the collective agreement, were defined in section 10.2(a)(i)(A), and are described in Table 3.1. Essentially, this article of the collective agreement dictated that players who were not rookies (Group I players) or unrestricted free agents, were classified as Group II players. Players, depending upon their age when they signed their first contract, could become restricted free agents as early as 21 years of age. As well, they were able to receive offer sheets from other teams at this early stage in their career. These rights as outlined in the collective agreement provisions, established a basis for salary escalation.

Teams were afforded a right of first refusal or draft-choice compensation with respect to a restricted free agent. This meant that, should another team in the league make an attempt to lure away a young and talented player through offering a generous contract, the original team would not lose the player outright, as was the case with unrestricted free agents; rather, they had a right of first refusal and draft-choice compensation. The right of first refusal allowed a team to match a competing contract offer by another team for one of its players. Should the original team not elect to match the offer, thereby exercising their right of first refusal, they received draft-choice compensation from the competing team. However, in order for a club to have been eligible to receive these rights, it was their duty to offer a restricted free agent in the final year of his contract a "qualifying offer".

## 5.2 Qualifying Offers

It is argued that qualifying offers presented one of the more patently inflationary terms in the collective agreement. Section 10.2(a)(ii)(A) stated that qualifying offers must be made on at least the following terms:

> If the player's Prior Year's Salary is equal to or less than the Average League Salary for that League Year, 110% of his Prior Year's Salary [is the required compensation level for a qualifying offer]

If a club did not elect to offer the player a legitimate qualifying offer as dictated by the terms of the collective agreement, that player immediately became an unrestricted free agent. Thus, for those players in the league who, during the final year of their recently expired contract made equal to or less than the average league salary for that year, a qualifying offer was only legitimate if the player is offered at least a 10% raise. By simply playing out the duration of one's contract, this provision entitled the player to at least a 10% raise if the club has any interest in retaining their services.

It is submitted that these qualifying offers contributed significantly to league-wide salary escalation between 1994 and 2004. Considering that in 2004, for example, over 50% of the NHL's players were subject to the restricted free agency provisions, qualifying offers were conceivably tendered to a large portion of the player population each year. Approximately half of these players receiving qualifying offers had compensation levels below the average league salary, and were therefore subject to the 10% increase. Assuming some rational relationship between relative performance and relative salary[15] therefore, those players who were perceived to have made the lowest contributions to their teams were entitled to a 10% raise regardless of 1) their contribution over the past year, 2) the team's standing, and 3) the team's financial performance. The apparent nature of this system was, therefore, one that rewarded poor performers with increased salaries of at least 10% which, arguably, made a significant contribution to the total average salary increase of 220% and average annual increase of 12.32% (compounded) between 1994 and 2004.

The terms for qualifying offers continued by stating that:

> If the player's Prior Year's Salary is greater than the Average League Salary for that League Year, 100% of the major league portion of his Prior Year's Salary [is the required compensation level for a qualifying offer]

Therefore, those players who in the last year of their contract made more than the average league salary for that year, a qualifying offer must have been at least equal to the amount they made in the final year of their contract. Although not requiring a raise as with those players of lower salary levels, this did protect players from a reduction in pay regardless of performance. In order to further explore the inflationary aspects of these provisions, the roles of agents and general managers must again be considered in the context of negotiation theory.

When a qualifying offer is tendered by a club to a player at the minimum limits, it does not always automatically become the terms of a new contract. Instead, an agent – or anyone skilled at negotiation – could consider the qualifying offer not as a final proposal, but rather an opening position. Since that is the absolute lowest level that can be offered to retain the player's services, there is no incentive to settle immediately and the agent can endeavour to increase the contract offer through negotiations. The agent can look to play upon the bargaining power afforded to his player in this situation, notably his age and potential, in order to achieve a raise in salary. The general manager is pressured by the need to develop talent internally, and to build a successful team that generates revenue for the club and ensures his job security. These elements, working in conjunction with the abilities of a skilled negotiator provide incentives to increase contract offers.

Essentially, the initial qualifying offer can become the floor from which negotiations will take place, rather than the final settlement. This effect, working simultaneously in many venues for many players throughout the league, potentially encourages salary escalation across the board. Given that there were just over 480 restricted free agents in 2004, and assuming an average player contract length of three years, it could be approximated that there might be as many as 120 players receiving qualifying offers each year. Reasonably, half of these players would have had salaries below the league average, and been entitled to a 10% raise. The other players who had salaries above the league average could also argue that at least a 10% raise was deserved, since that was being given to players deemed to be less productive (as determined by their compensation level). Therefore, it may be suggested that by compounding these increases to a significant portion of the player population annually, a basis for salary escalation was established. Whether bargaining on behalf of a player who is receiving a qualifying offer of 100% or 110%, the principles continue to apply and are well exercised by skilled negotiators.

Another aspect of qualifying offers to be considered is how a player's contract is structured with respect to annual salary. For example, suppose a player is given a two-year contract which pays him $1.75 million in the first year and $2.25 million in the second year. This is not an uncommon situation as sometimes players will be given contracts that project an increase in ability and contribution to the team over time and the salary is adjusted accordingly. This is also consistent with multiyear collective agreements in the private and public sectors. When this player's contract expires, (taking into consideration that average league salary in the 2003-04 season was $1.8 million), he will be eligible for a qualifying offer of $2.25 million, or 100% of his final year's salary. This $2.25 million is required instead of 100% of the average of the contract as a whole, which would be $2 million. By not taking the average salary but rather the final year's salary, a clever agent with a long-term perspective can be enticed to defer the financial weight of a contract to the final year. Contracts weighted toward the final year take advantage of the qualifying-offer provisions in the collective agreement and result in salary inflation.

### 5.3 Interrelationships Between Group I and Group II Contracts

Considering the proposed inflationary tendencies surrounding Group I and Group II players, interrelationships between the two groups will now be explored. Supposing a Group I player received an entry-level contract laden with performance bonuses, his total compensation during the final year of his contract will potentially have been rather substantial. This is especially true if the player developed at a greater pace during his final year, and managed to achieve more performance bonuses than in previous years.

As can be observed in the table outlining the entry-level compensation structure, upon graduating from the entry-level compensation system, the player became a restricted (Group II) free agent. This meant that the rights of Group II players applied, including those with regard to qualifying offers. Therefore, a player who earned an entry-level maximum salary of $1.185 million (maximum level if signed in 2002) in his final year automatically qualified for a 10% raise – since it was below league average salary – if his team wished to retain his rights through tendering a qualifying offer.

For reasons set out above, however, an agent will use this new (minimum required level) salary of $1.3035 million as a base from which a settlement will be determined. Moreover, it can be credibly argued in negotiations that since base salary was restricted by the provisions of the collective agreement, total compensation paid to the player should be used as a reference when moving forward. For example, although a player's salary was limited to $1.185 million, his achievement of performance bonuses pushed the total compensation to over $2 million and that can become the relative benchmark for negotiation. The owner/general manager and agent had agreed to a contract 3 years previously that resulted in this player's compensation being $2 million in his final year. Therefore an agent can make the argument that, given the player's development and improving contributions to the team, he warrants an increase in compensation. For example, following the expiration of his rookie contract ($925,000 salary), Joe Thornton received a deal worth $5.55 million over three years. Vincent Lecavalier followed his entry-level salary of $975,000 with a 3-year deal worth $6.125 million. By allowing total compensation levels to surpass those of the salary maximum levels dictated by the collective agreement – through exploitation of the Group I player's performance bonus clause – the potential compounding effects were significant as the player entered Group II free agency.

### 5.4 Right of First Refusal, Draft-Choice Compensation

As mentioned, the protective provisions that governed restricted free agents were a right of first refusal and draft-choice compensation. The goal of these provisions was to limit the potential mobility of young players, so that clubs that have done well through drafting and development would not lose the time they have invested in a player.

However, the collective agreement stated that restricted free agents (Group II players) were eligible to receive and sign contract offers, known as offer sheets, from other teams. Assuming a team tendered an appropriate qualifying offer to a player, when another team gave that player an offer sheet, the initial team was able to exercise its right of first refusal. This meant that within seven days, if his home team so elected, it could match the offer from the new one. By matching, the home team was automatically entered into a binding contract with the player on the terms of the offer sheet. If they did not choose to match the offer, the initial team was then entitled to be compensated with draft choices. The number and type of draft choices determined by the collective agreement for the 2003-04 season is set forth in the table below.[16]

**Table 5.1**

| Player's New Salary | Compensation Required |
|---|---|
| $727,502 or below | No compensation |
| $727,502 - $1,000,315 | 3rd round draft choice |
| $1,000,315 - $1,182,191 | 2nd round draft choice |
| $1,182,191 - $1,455,005 | 1st round draft choice |
| $1,182,191 - $1,455,005 | 1st and 3rd round draft choices |
| $1,818,754 - $2,182,505 | 1st and 2nd round draft choices |
| $2,182,505 - $2,546,256 | Two 1st round draft choices |
| $2,546,256 - $3,091,882 | Two 1st round and one 2nd round draft choice |
| Over $3,091,882 | Three 1st round draft choices |
| Each additional $1,818,754 | One additional 1st round draft choice to a maximum of five |

Section 10.3(b) of the collective agreement then states that:

> The Prior Club may not trade that Restricted Free Agent for a period of one year from the date it exercises its Right of First Refusal

Therefore, any contract entered into by a team exercising its right of first refusal, cannot be traded away to another club during the following season. This can have a significant impact if a club is looking to trade away some of its higher-priced players at the trading deadline due to its financial situation – an annual occurrence in the NHL for some teams.[17] The provision of a club's right to match can have inflationary impacts on NHL salaries, and this has been most obvious with the cases of Joe Sakic and Sergei Fedorov in 1997 and 1998 respectively.

In 1997, Joe Sakic was 28 years old, and the star centre and captain of the Colorado Avalanche. He was a restricted free agent at the time and had not renewed his contract with Colorado, as they were in the middle of signing their other star forward, Peter Forsberg. That off-season, The New York Rangers had just lost their captain and leader, Mark Messier, to the Vancouver Canucks. New York then saw Sakic as the ideal replacement to lead the Rangers for years to come. It had been a rare occurrence for a restricted free agent, such as Sakic, to receive an offer sheet from a new team. However, Sakic was a rare talent and New York was a wealthy team in need of a star player. To an extent, this situation was analogous to Bruce McNall purchasing Wayne Gretzky in 1989, in the sense of non-hockey interests – New York's need for a "star" – being in play. The New York Rangers decided to offer him a substantial three-year, $21 million dollar deal – comprised of a $15 million signing bonus and a base annual salary of $2 million a year, resulting in an average *de facto* salary of $7 million a year. This was a substantial increase from the $3.1 million Sakic earned the previous season.[18] Faced with the possibility of losing their captain and all-star centre, Colorado reluctantly matched the offer to retain his services. Joe Sakic received his $17 million in bonus and salary the first year and $2 million in the following two years. Suddenly, a benchmark for an all-star player under 31 years of age went from $3.1 million a season to $7 million. Players comparable to Sakic in skill and not yet eligible for unrestricted free agency were able to utilize his compensation level as a basis to determine their own in negotiations as Group II players.

The next year, in 1998, Sergei Fedorov, having witnessed the implications of Joe Sakic's situation, sought a drastic pay increase from the Detroit Red Wings. Fedorov was both an offensive leader for the Detroit Red Wings as well as one of the best defensive forwards in the game. As an unsigned restricted free agent, Fedorov was presented with an offer sheet by Peter Karmanos, the owner of the Carolina Hurricanes. Karmanos, a wealthy owner much like those in New York who attempted to sign Sakic, needed a franchise player to attract the Carolina fans and had the financial means to acquire one. Attempting to create a deterrent for Detroit's owner Mike Illitch to exercise his right of first refusal, Karmanos offered Fedorov a $14-million signing bonus with a $2 million annual salary, much like the Sakic deal. A singular element of this contract was a clause that stated that if the team Fedorov played for made it past the conference semi-finals – almost a certainty for the talented Detroit team but very unlikely for a developing Carolina team – Fedorov would receive an additional $12-million bonus. With great reluctance, but being able to manage the financial burden, Detroit matched Carolina's offer. During the playoffs that year, the Red Wings won the conference semi finals and the $28 million one-year payment was made.

The contracts of Joe Sakic and Sergei Fedorov were central to the substantial inflation in player salaries (LeBrun 2004). They demonstrated how the restricted free agency provisions, notably the right of first refusal, could be manipulated in order to escalate player salaries. This, of course, ran dramatically contrary to the original intent of the provisions to keep salaries depressed. A resulting effect was that owners and general managers were encouraged to tender qualifying offers above the minimum level in order to keep their talented players and to deter offer sheets from other teams. Contracts signed by players in restricted free agency – as exemplified by the Sakic and Fedorov contracts – set a perceived "market price" for players of a given talent. Therefore, although not compelled to, owners and general managers would consider these signings when tendering a qualifying offer to their restricted free agents. The outcome was that of an increased salary level as owners offered large contracts in the hope of deterring competing offer sheets.

The interactions between Group I and Group II contracts, and the observed inflationary impacts of teams exercising their right-to-match competing offer sheets contributed to the escalation in players' salaries. The nature of the qualifying offer provisions, compounded annually over a significant number of players, encouraged higher salaries across the league. As well, the tendency of agents and general managers to consider the contracts of other players as comparables in negotiation, and ability and willingness to pay, furthered this escalation. The role of unrestricted free agency and the manner in which these elements interacted with it will now be explored.

# Chapter 6 UNRESTRICTED FREE AGENCY AND THE NHL "MARKET"

## 6.1 Group III Players

The concept of unrestricted free agency, without compensation[19], was introduced to the NHL in 1992 and, it is fair to say, has had a significant impact on the processes and outcomes of bargaining through bidding wars and the NHL's skewed "market".

Under the six possible player groupings, Groups I – VI, three of these classifications – Groups III, V, and VI – included players who were deemed to be unrestricted free agents. Group III free agents are the most commonly referred to when identifying substantial salary increases and will be explained in detail.[20]

Article 1 of the collective agreement defined unrestricted free agents as:

> A player who (a) has either never signed a Player Contract or whose Player Contract has expired, or has been terminated or bought out by a Club; and (b) who otherwise is not subject to any exclusive negotiating rights, Right of First Refusal, or Draft Choice Compensation in favour of any Club or a player who becomes an unrestricted free agent as a result of a Club exercising its walkaway rights under Article 12.

Simply put, an unrestricted free agent was a player who was currently not signed to a club, and not subject to a club's protective provisions, such as right of first refusal or draft choice compensation. In order to satisfy these requirements, a player must have met the terms dictated by the Group III, V, or VI stipulations. Essentially, this type of player was available to sign a contract with any team in the league, and teams often competed with each other to acquire his services. In theory, the player was able to obtain "true market value" for his services because there were no limitations imposed on his mobility.

Article 10.1(a)(i) of the NHL-NHLPA collective agreement identified Group III players and their rights as:

> Any player who is 31 years of age[21] or older… shall, if his Player Contract has expired, become an Unrestricted Free Agent. Such player shall be completely free to negotiate and sign a Player Contract with any Club, and any Club shall be completely free to negotiate and sign a Player Contract with such player, without penalty or restriction, or being subject to any Right of First Refusal, Draft Choice Compensation or any other compensation or equalization obligation of any kind.

According to Bartlett (1994:3), this provision of the collective agreement theoretically allowed for the operation of natural market forces to dictate the salary of a player who has reached 31 years of age. The interactions between labour supply (the players) and demand for labour (team owners) should result in a market equilibrium price for a given player's services. In theory, equilibrium price reflects the natural market demand for the player.

However, there is a major disconnect between theory and reality here. The traditional notion of a market (at least an "efficient" market) assumes that there is near-perfect information available to all parties, there is an infinite number of buyers and sellers, and no single party is capable of influencing the price. The NHL's "marketplace" clearly does not reflect these conditions for a traditional economic marketplace to operate. Information was not always perfect (particularly for the buyers), nor available to all parties, there was a finite and very small number of buyers and sellers every year, and the parties were directly capable of influencing and determining the price for a player's services, as dramatically illustrated by the Gretzky trade. Furthermore, the traditional market perspective does not take into consideration the remarkable influence exerted by player agents and the competitive nature of wealthy team owners. Given the limited number of exceptionally talented players available each year due to the setting of unrestricted free agency at 31, owners had to compete with each other every year to retain their services. In turn, player agents capitalized upon this competitive environment to acquire substantial contracts for their clients. These contracts then became the *de facto* "market price" for other players of similar ability across the league. (Similar ability, in this case, is a perception in the minds of the owners, which the agents help manipulate and create.)[22] This dynamic spilled over and influenced the "market" well beyond the actual unrestricted free agents in a given year.

### 6.2 The Ability-to-Pay Factor

In a theoretical sense, the "market" price of a player would consider the financial means of the "buyers" of labour; in other words, in an efficient market, rational buyers would never pay a price that exceeds their ability to pay. Thus, a player's appropriate salary when being signed as an unrestricted free agent, should consider the financial means of all buyers (teams) in the market (league). In practice, however, this was rarely the case as hockey teams are owned by individuals and organizations of great variance of wealth and willingness to spend money who are in competition with each other.[23] The resulting (inefficient) "market" was a reflection of the more financially sound and free-spending clubs, and not those with limited financial capabilities. For example, the Toronto Maple Leafs, a high-revenue club[24] funded by Maple Leaf Sports and Entertainment and a wealthy and devoted fan base, could afford to offer much higher salaries to players than the Nashville Predators, who were barely supported by a largely indifferent hockey community. Substantial free-agent signings (in financial terms), such as the acquiring of goalie Ed Belfour from the Dallas Stars in 2002 at an average of $7 million per year, were paid for by an arena that was sold out every night despite the very high ticket prices. The New York Rangers, Detroit Red Wings, Colorado Avalanche, Philadelphia Flyers, and the Toronto Maple Leafs, were all teams who operated in this upper echelon of wealth in the NHL, whereas Nashville, the Columbus Blue Jackets, Florida Panthers, and Pittsburgh Penguins were at the opposite, lower, end of the spectrum.

This divergence in teams' abilities to pay a given salary, together with the fact of their competing with each other, prevented the creation of a true marketplace. Instead, smaller, inflated "markets" were created by the wealthier clubs as bidding wars developed between teams exercising their respective financial capabilities. As a result, the less wealthy teams were unable to remain a part of these inflated "markets" and salaries garnered by unrestricted free agents were not reflective of the league's collective ability to pay, but rather of what a small percentage of teams determined.

When originally implemented, free agency was a provision agreed to by the owners only if it would affect a limited number of players each year. The age of eligibility for free agency was then set at a point perceived to be later in a player's career, such as 31 or 32. Free agency, the owners recognized and conceded, was a means for players to garner higher wages than the suppressed levels imposed by the owners in the past. Having the option of free agency available to only a few players each year, was intended to restrict the number of large contracts being offered. However, supply and demand economic theory contradicted this rationale. With only a limited number of free agents available each summer to be signed by the owners, "market" conditions favoured the players. The top players were coveted by a number of teams and the demand for their services pushed the contract offers higher. Since there were often few, if any, equal substitutes for a given free-agent player in a given year, his unique services often incited bidding wars. Scarcity of available talent forced the demand function of owners and general managers upward, and with it went salary levels as the owners and general managers had an increased perceived, and sometimes actual, necessity to spend.

## 6.3 Negotiating Dynamics Between Owners and Agents

As noted, it must be understood that the NHL has a unique bargaining structure, unlike traditional union-management negotiations: Instead of a single, unified management group bargaining with its employees, there are in fact thirty individual managers participating in thirty different sets of negotiations, and they are in competition with each other. However, these wealthy owners in competition with each other were not the only participants in the inflation of salaries through signing unrestricted free agents; players' agents made substantial contributions to these observed results. Since it was the agents with whom the owners and general managers negotiated, they were an important element in the determination of salaries.

The interactions that take place during the negotiations over an unrestricted free agent have numerous variables. The general manager/owner must be conscious of his financial means, and his desire to acquire this player in order to build a winning team, which could very well determine the longevity of his own career. On the other side of the table, the agent is driven by the desire for his player to earn the money that he is seen to deserve, and to be signed by a team given no reasonable alternative league;[25] added to this, is the agent's own personal interest in the outcome.[26] Taken together, the influence of an agent's desire for a rich contract, in combination with a financially sound owner's desire for a successful team (and subsequent revenue gains), provide great pressure for salaries to rise.

Furthermore, to gain leverage in negotiations, an agent can easily create and enhance a BATNA, his Best Alternative to a Negotiated Agreement – the standard against which any proposed agreement should be measured.[27] A well developed BATNA can give a negotiator the ability to walk away from a table should offers not be sufficient enough to satisfy their interests, and thus, the leverage to extract a better offer from an owner. A BATNA protects a negotiator from entering into an unfavourable agreement and from rejecting one that would be in his or her interest to accept. In short, a BATNA increases confidence and bargaining power. The nature of unrestricted free agency, as stated above, often created a sellers' market in that there were more parties to purchase the services of a player than there were players able to offer those particular services. As a result, a skilful agent was able, not only to negotiate with one team at a time, but with several, in the hopes of receiving multiple offers.

Negotiating with several parties at the same time has significant effects. The agent now has the opportunity to entertain multiple contracts and select the best one for the player. Therefore, an agent is able to put upward pressure on a general manager's offer by informing him of what other teams have offered for the player. This demonstrates an agent's willingness to exercise his/her best alternative should the need arise. Whether or not these statements by the agent are entirely accurate, the result of the process is to have the general manager reconsider his offer and his ability to raise it. This plays directly into the interests of the general manager to build a winning team when negotiating over a star player. In fact, there is a financial dilemma: a star player will cost a substantial amount of money, but a winning team will generate more revenue.

Also, there is a non-financial utility associated with winning. The true interests of the parties surrounding a negotiation in the context of professional hockey may not be "rational," in the sense of strict economic utility. Pride, ego, and achievement are all powerful forces in human interactions, especially given the competitive nature of bidding for an unrestricted free agent. Driven by these "interests," owners and general managers may be willing to associate greater non-financial utility to acquiring a player and this can be reflected by an inflated contract offer.

A credible BATNA, as expressed to an interested owner, is evidence that the agents negotiate with multiple teams simultaneously. By evaluating and understanding the position and resistance points of the party with whom he/she is negotiating[28], the agent can pressure a general manager's position upwards, but not necessarily out of his potential settlement range. Resistance points can change during the course of negotiation, as a result of the conditions and commitment of each party. Although the final figure may not fall outside the GM's original desired settlement range, an agent can shift this zone as long as he/she does not wander past the perceived marginal revenue of the player, theoretically. In practice, however, research (Bazerman & Neale 1992) suggests this is done all the time in negotiations where there are two or more bidding companies.

From the perspective of the owner/general manager, the availability of alternative offers for a player's services strongly influences their course of action. As these people are forced to compete with each other (driven by similar interests in terms of, both financial and non-financial utility,) and given the nature of negotiation and collective bargaining theory, offers for unrestricted free agents are made with the intent of outbidding their counterparts. Ideally, an initial offer will give the impression that they are serious about acquiring a player's services without showing their hand and final resistance point. However, the process of bidding between teams for a player enhances this drive towards one's own resistance point in the hopes of "winning" the negotiations. What must be noted here is that the focus of the negotiations has switched from one between the agent and general manager to one in which general managers and owners of competing teams are silently negotiating with each other. All the while this is being fuelled by an agent who has pitted these parties against one another, and, in the best sense of the term, "manipulating their perception of utility" (Walton & McKersie 1965).

Bidding wars for a particular good or service have a tendency to result in an irrational escalation of commitment – meaning that the parties continue a previously selected course of action beyond what rational analysis would recommend (Bazerman, Neale 1992:10). Regarding unrestricted free agents, it is plausible that clubs will enter the bidding war not expecting the bidding to exceed the true value of the player. The potential gain, in combination with the possibility of "winning" the auction for his services, is reason enough to enter. However, once engaged in bidding, it takes only a (relatively) few more dollars for a team to stay in rather than accept a sure loss (Bazerman, Neale 1992:12). Potentially, teams will be enticed to continue bidding, in the hopes that others will quit. As a result, the "winner" of these bidding wars that involve many bidders for a player, easily end up paying more than the player is worth (Bazerman, Neale 1992:154). With a greater number of bidders, bargaining theory suggests that parties have more confidence in the value of the player, even though there is no objective basis for such confidence. The greater confidence can convince an owner that it is even more necessary to make a higher bid to defeat the other bidding teams. As a result, it is possible, indeed probable, that these bidding wars for unrestricted free agents between teams often lead to irrational results. As more parties become involved by making contract offers, the "winning" bid will likely overvalue the player. Research has shown this to be true in other areas of business (Bazerman, Neale 1992), and there is no reason to think it would not apply in the NHL.

An owner's resistance point varies directly with his perception of the financial and non-financial utility a player can bring to his team (Walton, McKersie 1965:59). Subsequently, the greater the utility attached to a player, the higher the resistance point of an owner. The agent can play an integral role in modifying the utility of a player through manipulating the owner's perceptions. (Walton and McKersie, 1965: 72)

Furthermore, a general manger can even negotiate with himself as time passes and his previous offer has not been accepted. As time increases so does the pressure to settle for fear of losing out on acquiring the player.[29] Therefore, with limited agent-GM interaction, a situation arises in which it would not be surprising for the GM to submit a new, increased offer, simply because he does not know what others may be submitting and does not want to fall behind.

This dynamic is compounded by the information factor: that is, the level of information available to the negotiating parties strongly favours agents as they are aware of all the offers being presented to the player, but, the owners and general managers can only speculate. (This is an ironic reversal of the asymmetry of information that existed before salary disclosure.) Owners compete with each other and therefore will not share strategies or offers to certain players whom they are looking to acquire. Agents, on the other hand, are the recipients of all the potential offers and able to manipulate and increase them through skilful negotiating tactics, again, referring to manipulation of an owner's perception of the utility attached to the player being sought. They are more aware of what price a "market" is willing to bear for the services of their client, as opposed to the owners who can only make educated guesses at a price that would bring settlement. The result of this imperfect information is that owners and general managers will employ hunches instead of a proper analysis concerning a player's potential contribution to the team. Competing owners, therefore, can end up negotiating with each other – and with themselves – in an environment of asymmetrical information. Subsequently, this lack of information, compounded by the fear of offers from other teams, and a desire to win the bidding contest, can lead to an overvaluation of the player (Bazerman, Neale 1992:157).

The following are some examples of substantial free agent contracts:[30]

**Table 6.1**

| Year | Player | Team Signing with | % Salary Increase | $ Salary Increase (Millions) | Salary (Millions) |
|---|---|---|---|---|---|
| 1998 | Curtis Joseph | Toronto | 139% | $3.2 | $5.5 |
| 1998 | Ron Francis | Carolina | 163% | $3.1 | $5.0 |
| 1999 | Theo Fleury | New York Rangers | 254% | $6.1 | $8.5 |
| 1999 | Valeri Kamensky | New York Rangers | 216% | $4.1 | $6.0 |
| 2001 | Martin Lapointe | Boston | 320% | $4.0 | $5.25 |
| 2001 | Jeremy Roenick | Philadelphia | 70% | $3.5 | $8.5 |
| 2002 | Bobby Holik | New York Rangers | 174% | $6.1 | $9.6 |
| 2002 | Bill Guerin | Dallas | 71% | $3.6 | $8.7 |

It would appear that the unrestricted free agency system, dictated by the terms of the collective agreement, profoundly raised the salaries of unrestricted free agents. Three elements – 1) the terms of the collective agreement creating a sellers' market through scarcity of available free agents each year; 2) owners and general managers being driven by their financial and non-financial interests to acquire a star player in their pursuits of increased revenue, job security, ego, satisfaction, and desire to "win" (both the bidding war and the Stanley Cup); and 3) agents creatively establishing a forum of bidding wars and competition when seeking contract offers – all put upward pressure on the salaries of unrestricted free agents. Furthermore, these elements interacted in a manner that reinforced and compounded each other.

### 6.4 The Broader Influence of Unrestricted Free Agency Salaries

It can be inferred that the collective agreement, in an indirect manner, acknowledged that these Group III free-agent signings were inflated. This acknowledgement takes the form of a provision that disallowed any contracts garnered by unrestricted free agents to be admissible in salary arbitration.[31] (The arbitration procedure and its role concerning salary determination will be discussed in detail shortly.) However, despite this provision, unrestricted free agent signings were still able to exert considerable influence on other negotiations between players and owners, notably Group II restricted free agents. Although not afforded the same mobility and opportunities, Group II players could use the signings of unrestricted free agents, inflated through bidding wars, as comparables and support in their own contract negotiations. This, in essence, took the form of using the contract between one owner/general manager and an unrestricted free agent and inferring that to be the "market price" for a player of his abilities. This resulted in an escalated contract offer by an owner to retain the services of a Group II player, as they were conscious of this perceived "market price" and sought to deter competing offer sheets. Subsequently, that new contract offer, dictated by the signing of an unrestricted free agent, then became a comparable in negotiations for all other Group II players. In other words, large signings of unrestricted free agents established a *de facto* “market price” for a player, which, when used as a comparable in negotiation, put upward pressure on the salaries of restricted free agents. This also had an impact on negotiations for players who were moving from Group I status to restricted free agency, given the compensation earned in their previous contracts – potentially inflated through exploitation of the performance bonus clause – and the current “market price”. The role of the NHL’s salary arbitration system and its interaction with these elements will now be considered.

# Chapter 7 SALARY ARBITRATION

## 7.1 Salary Arbitration in the NHL

Salary arbitration has existed in the National Hockey League since 1967; however, for many years its effectiveness was limited by the lack of salary disclosure. The NHL system required an arbitrator to determine the salary and bonuses to be paid to a player (contract length is one or two years, depending upon what has been requested by the club) after hearing the parties' cases. The arbitrator could choose a value submitted by one of the parties or any value they deemed appropriate within the range defined between the parties' positions.

One of the most effective pieces of supporting evidence for a case at arbitration is an accurate comparable: a player of similar ability. Parties can have a greater chance for success in arbitration by effectively utilizing comparable players who have salaries that reflect their bargaining position – that is, the salary they are seeking. Before salary disclosure, players and their agents were at an obvious disadvantage with regard to salary arbitration hearings. When salary disclosure was finally introduced into the NHL in 1989, however, the leverage at arbitration hearings was no longer on one side of the table. Agents now had access to all of the information that was previously held only by owners and general managers. This allowed them to present a more convincing argument before the arbitrator, as they could recognize and submit meaningful comparables that were more appropriate for their desired salary position. This has led to settlements that are increasingly favourable to a player's salary.

## 7.2 The Arbitration Process

Article 12 of the collective agreements set forth the terms and conditions for arbitration, and those who were eligible as displayed in the following chart:

**Table 7.1**

| First Contract Signing Age | Minimum Level of Professional Experience Required to be Eligible for Salary Arbitration |
|---|---|
| 18 – 20 | 5 years professional experience |
| 21 | 4 years professional experience |
| 22-23 | 3 years professional experience |
| 24 | 2 years professional experience |
| 25 | 1 years professional experience |
| After 26 | Player is already eligible |

The above table was based upon the same basic model as the restricted free agency provisions – that is, one's status under the agreement depended upon his age at the first contract signing and length of service in the NHL. Furthermore, the same definitions for one year of professional experience exist as with restricted free agents and entry-level players: ten NHL games constitutes one year. Thus, salary arbitration rights were afforded to players as young as 23 years of age. The premise behind allowing this at such an early point in a player's career was to offset the perceived bargaining-power imbalance between players and management. This perceived imbalance was due to the structure of restricted free agency, more specifically, its apparent similarities to the "reserve clause" of the past. As these players were not eligible for unrestricted free agency, their leverage in negotiations was seen to be limited. Without the option to pursue salary arbitration, the only other action available to a player and his agent – other than negotiation – was to hold out for a better deal and refuse to play. It should be noted that if an eligible player elected to sign an offer sheet he received, he then waived his right to salary arbitration.

When a player wished to proceed to salary arbitration, he submitted a request in writing by July 15th of that year to the NHL, NHLPA, his team, and NHL Central Registry. Once all of the requests for arbitration were received, the NHL and NHLPA jointly appointed eight arbitrators who were members of the National Academy of Arbitrators to hear the cases.[32] As a matter of consistency, and in the interests of the parties to reduce uncertainty – a concept which will be explained in detail later – these eight arbitrators varied little from year to year. The arbitrators were then randomly assigned to the cases and scheduled by the NHL and NHLPA to hear them before August 15th of that year. As per Article 12.5(n), the expenses of the arbitrator and his/her fees were shared equally among the parties.

### 7.3 Statistical Analysis of Arbitration Awards

The effect of the NHL's salary arbitration system on compensation levels warrants some statistical investigation. An examination of the arbitration awards given in 2001, 2002, and 2003, seems to depict arbitration as a significant source of salary escalation. Of the 28 awards received by players over those years, as shown in Table 7.2, the average salary increase was 77.07%, with a maximum increase of 389% (Petr Sykora in 2001) and a minimum increase of 14.05% (Ryan Smyth in 2003). Compare this to the annual increases in league average salary which were 14.5%, 8.9%, and 2.2%[33] in 2001-02, 2002-03, and 2003-04, respectively. Clearly, an increase in salary of 77.07% over the three year period in salary arbitration significantly outweighs the average salary increases for the NHL at 8.53% over the same years.

**Table 7.2**

**Arbitration Awards 2001 - 2003**
(In $M)

| | | Award | Previous Salary | % Increase |
|---|---|---|---|---|
| 2003 | Brian Rolston | 3.175 | 2.2 | 44.32% |
| | Pavol Demitra | 6.5 | 3.975 | 63.52% |
| | Ryan Smyth | 3.45 | 3.025 | 14.05% |
| | Kimmo Timonen | 2.0 | 1.4 | 42.86% |
| | Tom Poti | 2.8 | 1.8 | 55.56% |
| | Daymond Langkow | 2.7 | 2.25 | 20.00% |
| 2002 | Jason Arnott | 3.65 | 2.6 | 40.38% |
| | Jason Smith | 2.3 | 1.525 | 50.82% |
| | Antti Laaksonen | 0.75 | 0.475 | 57.89% |
| | Tom Poti | 1.8 | 0.925 | 94.59% |
| | Radek Bonk | 3.2 | 1.75 | 82.86% |
| | Niklas Sundstrom | 1.8 | 1.3 | 38.46% |
| | Brenden Morrison | 2.15 | 0.775 | 177.42% |
| 2001 | Bill Guerin | 5.1 | 3.212 | 58.78% |
| | Miroslav Satan | 3.25 | 2.5 | 30.00% |
| | Aaron Miller | 1.6 | 0.9 | 77.78% |
| | Filip Kuba | 0.735 | 0.36 | 104.17% |
| | Sergei Zholtok | 0.75 | 0.505 | 48.51% |
| | Cale Hulse | 1.1 | 0.85 | 29.41% |
| | Bobby Holik | 3.5 | 2.7 | 29.63% |
| | Petr Sykora | 3.3 | 0.675 | 388.89% |
| | Wade Redden | 2.8 | 1.95 | 43.59% |
| | Daymond Langkow | 1.95 | 0.93 | 109.68% |
| | Jan Hrdina | 1 | 0.7 | 42.86% |
| | Alexei Kovalev | 4.25 | 2.3 | 84.78% |
| | Robert Lang | 2.9 | 1.105 | 162.44% |
| | Martin Straka | 3.5 | 2.2 | 59.09% |
| | Pavol Demitra | 3.7 | 1.8 | 105.56% |
| | AVERAGE | | | 77.07% |

*Players who went to arbitration more than once during this period are shaded

The reasoning for these substantial increases must be considered. As stated, arbitration was intended to be a means for players to receive an appropriate salary level, which, for one reason or another, (in their view) they were not able to achieve through negotiation with the team. Reasonably, one can infer that appropriate compensation is a reflection of the player's contribution to the team. A basic measure of a player's production is that of points per game, for forwards at least – the average number of points a player scores in each game throughout the season. This considers one of the more basic measures of a player's contribution to a team, and controls for when the player is unable to play.

Utilizing the points per game measure for forwards and defencemen known for their offensive contributions, an analysis was done to identify a relationship between this measure and arbitration awards. The analysis determined how many dollars a player received for his productivity (as measured by points per game) in the season before receiving his arbitration award, and in the season following receipt of the award. The results are shown in Table 7.3.

**Table 7.3**

| | | Award ($M) | Previous Salary ($M) | % Increase | PPG before | PPG after | $ / PPG Before | $ / PPG After | % Change |
|---|---|---|---|---|---|---|---|---|---|
| 2003 | Brian Rolston | 3.175 | 2.2 | 44.32% | 0.728 | 0.585 | $3.02 | $5.42 | **79.58%** |
| | Pavol Demitra | 6.5 | 3.975 | 63.52% | 1.192 | 0.853 | $3.33 | $7.62 | **128.58%** |
| | Ryan Smyth | 3.45 | 3.025 | 14.05% | 0.924 | 0.720 | $3.27 | $4.79 | **46.50%** |
| | Kimmo Timonen | 2.0 | 1.4 | 42.86% | 0.571 | 0.556 | $2.45 | $3.60 | **46.94%** |
| | Tom Poti | 2.8 | 1.8 | 55.56% | 0.600 | 0.358 | $3.00 | $7.82 | **160.56%** |
| | Daymond Langkow | 2.7 | 2.25 | 20.00% | 0.634 | 0.642 | $3.55 | $4.21 | **18.54%** |
| 2002 | Jason Arnott | 3.65 | 2.6 | 40.38% | 0.653 | 0.781 | $3.98 | $4.67 | **17.36%** |
| | Antti Laaksonen | 0.75 | 0.475 | 57.89% | 0.378 | 0.338 | $1.26 | $2.22 | **76.78%** |
| | Tom Poti | 1.8 | 0.925 | 94.59% | 0.379 | 0.600 | $2.44 | $3.00 | **22.85%** |
| | Radek Bonk | 3.2 | 1.75 | 82.86% | 0.771 | 0.667 | $2.27 | $4.80 | **111.59%** |
| | Niklas Sundstrom | 1.8 | 1.3 | 38.46% | 0.325 | 0.303 | $4.00 | $5.94 | **48.50%** |
| | Brenden Morrison | 2.15 | 0.775 | 177.42% | 0.866 | 0.732 | $0.90 | $2.94 | **228.28%** |
| 2001 | Bill Guerin | 5.1 | 3.212 | 58.78% | 1.00 | 0.85 | $3.21 | $6.03 | **87.65%** |
| | Miroslav Satan | 3.25 | 2.5 | 30.00% | 0.74 | 0.89 | $3.36 | $3.65 | **8.63%** |
| | Aaron Miller | 1.6 | 0.9 | 77.78% | 0.26 | 0.23 | $3.45 | $6.96 | **101.88%** |
| | Filip Kuba | 0.735 | 0.36 | 104.17% | 0.40 | 0.39 | $0.90 | $1.90 | **110.97%** |
| | Sergei Zholtok | 0.75 | 0.505 | 48.51% | 0.45 | 0.53 | $1.12 | $1.40 | **24.89%** |
| | Bobby Holik | 3.5 | 2.7 | 29.63% | 0.63 | 0.67 | $4.32 | $5.25 | **21.53%** |
| | Petr Sykora | 3.3 | 0.675 | 388.89% | 1.11 | 0.66 | $0.61 | $5.02 | **725.00%** |
| | Wade Redden | 2.8 | 1.95 | 43.59% | 0.60 | 0.43 | $3.24 | $6.51 | **101.04%** |
| | Daymond Langkow | 1.95 | 0.93 | 109.68% | 0.76 | 0.44 | $1.22 | $4.46 | **264.51%** |
| | Jan Hrdina | 1 | 0.7 | 42.86% | 0.55 | 0.72 | $1.27 | $1.39 | **9.15%** |
| | Alexei Kovalev | 4.25 | 2.3 | 84.78% | 1.20 | 1.13 | $1.91 | $3.75 | **95.89%** |
| | Robert Lang | 2.9 | 1.105 | 162.44% | 0.98 | 0.81 | $1.13 | $3.60 | **217.49%** |
| | Martin Straka | 3.5 | 2.2 | 59.09% | 1.16 | 0.77 | $1.90 | $4.57 | **140.41%** |
| | Pavol Demitra | 3.7 | 1.8 | 105.56% | 1.02 | 0.95 | $1.76 | $3.89 | **121.01%** |
| | **AVERAGE** | | | **79.91%** | 0.726 | 0.638 | | | **116.00%** |
| | | | | | | -13.81% | | | |

The above table shows that players who went to arbitration received awards that, on average, increased their compensation level by 116.00% based on the change in productivity from one year to the next. In other words, players received a significant increase in salary for a given level of production – 116.00% increase in dollars per points per game. The question must be asked as to why such remarkable increases in salary were awarded and found to be appropriate by the arbitrator. Arbitrators consider the player's production when rendering an award. They then compare this player to other, (often higher-paid) players of similar productivity levels. By doing so, arbitrators implicitly assume that a similar production level will be maintained by the player in the future. If the player's production falls below that of the previous year – the level upon which the arbitrator based his/her decision – the team is then overpaying for that player's services. The data for the years 2000 through 2004 reveal an average increase of 116.00% in compensation which, on its face, seems very high. However, the productivity of these players actually declined by an average of 13.81% in the year following their arbitration award. Therefore, this increase in compensation of 116.00% became the benchmark for an old productivity level, less 13.81%. In other words, the player's new salary (as determined by the arbitrator) and his production after receiving the award could be used as a basis for comparison for all other players negotiating with their teams, but at the lower performance level. This, then, had the potential to increase compensation levels for a given (or lower) level of productivity across the league. While an arbitrator obviously cannot control for possible declines in production, it would be appropriate to at least merit some consideration when rendering an award. The salary arbitration structure in the NHL, and how it interacted with an arbitrator's decision making process, as well as the incentives on owners and players, must be further examined.

### 7.4 Structure of the System

The NHL's salary arbitration process was unique compared to traditional interest arbitration in a public-sector union-management relationship. The main distinction was that it was a one-way process, meaning that only the player could elect to take his team to arbitration over a salary dispute, not the other way around. Therefore, salary arbitration could be used as bargaining leverage on behalf of the players (a BATNA) but was not available to clubs. That is not to presume that arbitration settlements would continually be favourable to players. Yet, one cannot ignore that players had the discretion to pursue negotiation or arbitration as a means to achieving a more attractive settlement, and the data (average increase of 77.07%) suggest that this must have been a sobering prospect for owners. Acting rationally, owners would have pursued arbitration if they felt the settlement would be more favourable than what was being presented in negotiation, but given the outcomes, this would have appeared to be an unlikely decision. However, this was an asymmetrical choice and the owners did not have access to this option.

The salary arbitration system in the NHL appears to be one that was conducive to a “chilling effect” on parties, particularly players and agents, in negotiations. Chilling effect refers to arbitration reducing the incentive to bargain in the short run (Rose 1994:198). Parties can develop a perception that arbitrators are likely to take a split-the-difference approach that falls somewhere between the parties' last bargaining positions. As well, parties are sometimes reluctant to make tough concessions necessary to further the bargaining process (Hebdon 2003:667). Essentially, the chilling effect reflects the unwillingness of the parties to compromise during negotiations in anticipation of an arbitrated settlement (Rose, Piczak 1996:644). In other words, arbitration reduces the incentive of one or both parties to compromise. Given that players were able to elect arbitration to achieve a more attractive settlement, it could reasonably be suggested that this “chilling effect” existed and contributed to a greater number of arbitration awards.

The structure of the NHL’s arbitration system must then be considered in the context of an arbitrator’s re-hire incentive. In a traditional union-management relationship, arbitrators are typically appointed by mutual agreement of the disputing parties. It is the arbitrator's role to then objectively come to a binding decision which is based on the evidence and arguments. These parties are also responsible for the arbitrator's compensation. As a result, in order to succeed as an arbitrator, the arbitrator must be acceptable to the parties – that is, the disputing parties must find settlements to be of a reasonable nature and unbiased. If one party finds an arbitrator's rulings to be unjustified or unreasonable, they will have less incentive to agree to that arbitrator hearing a future dispute. Therefore, it can be understood that the arbitrator has a strong personal interest in how his/her award is received by the parties and perceived by others. In the long run, an arbitrator's employability is a function of being perceived to be fair, objective, and neutral.

In the NHL, both the league and the NHLPA had to agree to the eight arbitrators appointed to hear the cases. This mutual selection was intended to promote unbiased awards from the third parties, as the National Academy of Arbitrators has a rather extensive membership list and alternative arbitrators were available. However, the incentive to use new arbitrators – those inexperienced with the workings of the NHL, its teams, and salary structure – was limited. Reasonably, all parties preferred that third party be familiar with the NHL and its operations for obvious reasons. Since salaries in professional hockey differed to such a degree from those in the standard private or public sector unionized positions, agents and players wanted arbitrators who were sensitive to this fact and able to render appropriate awards. Taking these preferences into consideration, the list of desirable arbitrators in the minds of both the NHL and NHLPA was significantly reduced.

If we return to the supposed re-hire incentive, the limited number of desirable arbitrators and the fact that the process was one-way, directed by the players, raises an interesting and troubling question about the appearance versus the reality of an arbitrator's objectivity. First, a limited number of NHL-familiar arbitrators meant that the likelihood of one being selected when the list of cases to be heard for salary arbitration that year were compiled was relatively high. Second, since it was a player-elected process, arbitrations took place only if the player felt that the settlement received from an arbitrator was likely to be superior to the one presented in negotiation with the team. Third, arbitrators were only compensated if the case was heard. Therefore, in order for an arbitrator on the list to hear a case, the player must have perceived the potential award to be more attractive than what could have been achieved through negotiation. Therefore, an interesting question relates to the incentives that were placed on arbitrators under the NHL's salary arbitration system – the degree to which a given arbitrator might be particularly conscious of a player's satisfaction with the award as it might relate to future employability. This proposition finds a parallel in public-sector collective bargaining.

There is a hypothesis, held by many on the management side in the public sector, that there is an inherent bias on the part of some full-time professional arbitrators in favour of the union when it comes to interest/salary awards. This is due to the arbitrator's desire to be employed by the union to hear future rights (grievance) arbitration cases, which is, to put it bluntly, where arbitrators make their money.[34] The hypothesis suggests that arbitrators may be more sensitive to the union's side because there are likely to be many locals of that union, (CUPE, for example, has over 2200 locals) but only one employer. Therefore, a union receiving a favourable salary arbitration award with one of its locals might be encouraged to employ the arbitrator for its future rights disputes, and recommend the arbitrator to its other locals as an acceptable third party. In turn, should they be displeased with the outcome, other locals will be advised not to use the arbitrator. In short, the arbitrator has a greater number of future employment opportunities through a union with its many locals and members, compared to a single management entity. This is a roughly analogous situation to the NHL salary arbitration system, as there are far more players than management parties and only the players can initiate arbitration. Therefore, in an effort to ensure future employability, the arbitrator has greater incentive to render awards that are positively received by the players. It must be emphasized that there is no direct evidence of this happening in the NHL. It is raised only as one possible factor explaining what seem to be extraordinarily high arbitration awards.

### 7.5 Evidence in Arbitration

Article 12.5(f) of the collective agreement specified the terms and conditions for admissible evidence in salary arbitration hearings. The jurisdiction of the arbitrator regarding evidence was very broad, as Article 12.5(f)(i) stated:

> The Arbitrator in his discretion shall be the judge of the relevancy and materiality of the evidence offered and/or the weight, if any, to attach to any evidence and shall not be bound by any formal legal rules of evidence.

Evidentiary rules regarding admissibility allowed the following:

A. the overall performance, including official statistics prepared by the League (both offensive and defensive) of the Player in the previous season or seasons;
B. the number of games played by the Player, his injuries or illnesses during the preceding seasons;
C. the length of service of the Player in the League and/or with the Club;

D. the overall contribution of the Player to the competitive success or failure of his Club in the preceding season;
E. any special qualities of leadership or public appeal not inconsistent with the fulfillment of his responsibilities as a playing member of his team;
F. the overall performance in the previous season or seasons of any player(s) who is alleged to be comparable to the party Player whose salary is in dispute; and
G. The Compensation of any player(s) who is alleged to be comparable to the party Player, provided, however, that in applying this or any of the above subparagraphs, the Arbitrator shall not consider a player(s) to be comparable to the party Player unless a party to the arbitration has contended that the player(s) is comparable; nor shall the Arbitrator consider the Compensation or performance of a player(s) unless a party to the arbitration has contended that the player(s) is comparable.

Therefore, statistical information regarding length of service and performance for the club was central, along with intangible qualities such as leadership. The provision then went on to allow the compensation figures of players alleged to be comparable to be admitted as evidence. Immediately, by permitting the compensation of players alleged to be comparable, a link was established between contracts negotiated throughout the league and salary arbitration. The potential for influence to be exerted in either direction was significant. However, to moderate this effect, the collective agreement then set forth the following rules determining inadmissible evidence:

The following categories of evidence are inadmissible and shall not be considered by the Arbitrator:

1. Any contract the term of which began when the player party to such contract was not a Group II Player;
2. Any contract entered into by an Unrestricted Free Agent, including contracts signed by players after the player's Club has exercised a walk-away right pursuant to Section 12.6;
3. Qualifying Offers made by the Club pursuant to Section 10.2;
4. Any prior offers or history of negotiations between the Player and the Club;
5. Testimonials, videotapes, newspaper columns, press game reports or similar materials;
6. Any reference to actual or potential walk-away rights;

7. Any award issued by an arbitrator as to which a Club exercised its walk-away rights pursuant to Section 12.6;
8. The financial condition of the Club or the League.

The first two provisions attempted to sever the connection between contracts negotiated throughout the league, particularly those by unrestricted free agents, and salary arbitration.

The final example of inadmissible evidence, “The financial condition of the Club or League,” is noteworthy. Essentially, the collective agreement prevented an arbitrator from considering a team’s ability to pay when determining an appropriate salary. It is interesting to consider that by submitting comparable players, parties were attempting to give the arbitrator a perspective on what is true “market value” for such a player. As noted earlier, however, it is in a real sense fallacious to talk about a true “market value” for a player, given the inherent imperfections in the market, which seem to work in favour of the players. Even assuming a market for the sake of argument and analysis, however, market conditions changed from year to year in the NHL and, therefore, by allowing the compensation of comparable players into evidence, but not the financial condition of the league or team, the arbitrator was forced to determine an award based upon a one-sided perspective of the player market. The arbitrator was potentially influenced by the conditions and decisions of the past, rather than the current issues facing the league or team. The arbitration system appeared to be centred upon what should be awarded (based upon the arguments of the parties), rather than what can reasonably be afforded. As a result, awards may have been given that forced an inflation of a “market price” for a player, which the league and one or many of its teams were unable to bear.

The above demonstrates an interconnectedness and influence between past and present arbitration awards. This influence has then been exerted toward contract negotiations throughout the NHL. Owners and general managers were wary of a potential arbitration award and its subsequent impact on the team and its financial condition. Past awards may have enhanced this hesitation and, more importantly, there was a level of uncertainty in placing a substantial financial decision in the hands of a third party. Subsequently, a player may have received an inflated contract offer from his team, as they attempted to avoid taking the dispute to arbitration. As inflated contracts were tendered to restricted free agents in the hopes of deterring a competing offer sheet, the same occurred with regard to preventing salary arbitration. The greater the perceived potential arbitration award – influenced by past awards and current comparables – the greater the incentive for a team to offer their player a contract to eliminate the desire for third-party intervention. The interrelationship between these elements arguably caused further salary escalation.

### 7.6 Walk-Away Rights

When the arbitrator rendered his/her decision, it set forth the base salary, bonuses, minor league clause (if necessary), and reasons for the award including relied-upon comparables. Since the process was driven by the players, an apparent balancing mechanism to offset this power existed for the owners, known as walk-away rights. However, it must be noted that this mechanism was rarely used by owners, especially in comparison to the number of players who proceeded to arbitration each year. Article 12.6(a) outlined these rights by stating:

> If a Club has elected to arbitrate a one year contract, and the award issued is for $550,000 or more per annum, then the Club may, within 72 hours

> after the award of the Arbitrator is issued, notify the player, the NHLPA and the NHL in writing that it does not intend to tender to the player a Player Contract based on the award as determined by the Arbitrator. Upon receipt of that notice, the player shall automatically be deemed to be an Unrestricted Free Agent, subject to the provisions of paragraphs (c) and (d) below.

This provision gave teams the right to not be bound by the terms of a contract which they could not afford, or were not willing to pay. If a team felt that the award of the arbitrator was unreasonable, then they were able to walk away and the player became an unrestricted free agent, whatever his age. It must be noted that this option was likely to be considered differently by a team when dealing with the award of an average player compared to that of an all-star. Teams had greater incentive to accept a large award in order to retain the services of a valuable player, which further compounded the escalation of salaries. However, if the financial means or interests of the team simply did not warrant the acceptance of such a contract, their rights were further protected. Article 12.6(c) dictated that:

> If the player accepts an offer from a New Club in respect of that year of the contract which the Prior Club has walked-away from that is less than 80% of the award for such year, the Prior Club may, within seven (7) days after the date it receives the applicable Offer Sheet, elect to match the offer of the New Club and the Player and the Prior Club shall enter into a Player Contract on those terms and conditions

Therefore, if a team exercised its walk-away rights regarding an arbitration award, and another team attempted to sign the player for 80% or less than the arbitrated decision, the original team could match the offer. If done, the player and his original team were immediately deemed to have entered into a contract for that value. Although a rare occurrence, this was similar in principle to the right-to-match provision for restricted free agents. This provision was an attempt to moderate the effects of an excessive arbitration award. However, this moderation failed to consider the financial capabilities of the wealthier teams in the league. What may have been an unreasonable award – at 100% or 80% of its value – to one team, was potentially feasible and of interest to another club. Actions such as these only served to further the inflation of salaries across the league, as an arbitrated decision was being supported by a team's contract offer.

A final aspect to consider regarding the collective agreement arbitration terms is Article 12.6(c)(ii):

> The player may within seven (7) days after receipt of notice from the player's Prior Club that the Prior Club elects to walk-away from the arbitration award, in respect of the Prior Club's request for a one year contract, by written notice to the Club, elect to enter into a Player Contract with the Club on the terms and conditions set forth in the Prior Club's Qualifying Offer. If such election is timely exercised, the Club must enter into such contract

This provision meant that if a club elected to walk away from an award, the player had the right to enter into a contract with that club based upon a previously tendered qualifying offer. This gave the player significant leverage and, again, encouraged inflation of salaries. A player who was tendered a qualifying offer, had the right to go through arbitration in the attempt to receive a higher salary. Evidence has shown that arbitrated awards tended to increase a player's salary, as outlined in the study of awards between 2001 and 2003, which showed an average increase of 77.07%. If the club felt this award was too great and walked away, the player could always enter into a binding contract based upon the terms of the qualifying offer. Before this option was taken, the player had the chance to explore contract options with other teams as they were declared an unrestricted free agent.

### 7.7 Incentives to Go to Arbitration

The provisions of salary arbitration, and the manner in which they interacted with the other elements of the collective agreement, allowed players three significant methods to increase their salaries.

1) Salaries could have increased from the arbitrated award.
2) A player who had their award walked away from by a team automatically became an unrestricted free agent and benefited from the inflationary aspects of any ensuing bidding wars that took place.
3) A player could enter into contract with his team based upon the terms of the qualifying offer should that team have elected to walk away. Given that qualifying offers were 100% to 110% of the previous year's salary – but often negotiated in excess of this level as a means to deter competing offer sheets – players had three viable means to increase or at the very least maintain their compensation levels.

Ultimately, there seemed little incentive to settle during contract negotiations with a team provided by the terms of the collective agreement. Indeed, the collective agreement appeared to encourage taking the matter to a third party from a player's perspective.

As a means to counter this, teams were forced to offer inflated contracts to their players so that a settlement would be achieved without the intervention of a third party. An examination of contracts signed by players who filed for arbitration in 2001, but managed to negotiate a settlement beforehand, supports this position, as shown below

## Table 7.4

**Arbitrated Awards**

| 2001 | Award | Previous Salary | % Increase |
|---|---|---|---|
| Bill Guerin | 5.1 | 3.212 | 58.78% |
| Miroslav Satan | 3.25 | 2.5 | 30.00% |
| Aaron Miller | 1.6 | 0.9 | 77.78% |
| Filip Kuba | 0.735 | 0.36 | 104.17% |
| Sergei Zholtok | 0.75 | 0.505 | 48.51% |
| Cale Hulse | 1.1 | 0.85 | 29.41% |
| Bobby Holik | 3.5 | 2.7 | 29.63% |
| Petr Sykora | 3.3 | 0.675 | 388.89% |
| Wade Redden | 2.8 | 1.95 | 43.59% |
| Daymond Langkow | 1.95 | 0.93 | 109.68% |
| Jan Hrdina | 1 | 0.7 | 42.86% |
| Alexei Kovalev | 4.25 | 2.3 | 84.78% |
| Robert Lang | 2.9 | 1.105 | 162.44% |
| Martin Straka | 3.5 | 2.2 | 59.09% |
| Pavol Demitra | 3.7 | 1.8 | 105.56% |
| **Average** | **2.63** | **1.51** | **91.68%** |
| League Average | 1.6426 | 1.434885 | 14.48% |

**Settled Before Arbitration**

| | New Salary | Previous Salary | % Increase |
|---|---|---|---|
| Mike Leclerc | 0.80 | 0.44 | 81.82% |
| Jiri Slegr | 1.80 | 1.20 | 50.00% |
| Hal Gill | 1.10 | 0.80 | 37.50% |
| Brian Rolston | 2.00 | 1.473 | 35.78% |
| Bates Battaglia | 0.75 | 0.495 | 51.52% |
| Marek Malik | 0.90 | 0.60 | 50.00% |
| Jamie Allison | 0.575 | 0.60 | -4.17% |
| Greg de Vries | 1.00 | 0.725 | 37.93% |
| Jamie Pushor | 0.95 | 0.725 | 31.03% |
| Brad Lukowich | 0.75 | 0.385 | 94.81% |
| Mathieu Dandenault | 1.10 | 0.725 | 51.72% |
| Janne Niinimaa | 2.70 | 1.81 | 49.17% |
| Dan Boyle | 0.575 | 0.4125 | 39.39% |
| John Jakopin | 0.5250 | 0.50 | 5.00% |
| Bryan Smolinski | 2.30 | 1.70 | 35.29% |
| Andy Sutton | 0.525 | 0.5775 | -9.09% |
| Mike Dunham | 2.60 | 1.5000 | 73.33% |
| Jason Dawe | 0.50 | 0.40 | 25.00% |
| Sandy McCarthy | 1.175 | 0.88 | 33.52% |
| Brad Smyth | 0.40 | 0.40 | 0.00% |
| Jeff Toms | 0.45 | 0.42 | 7.14% |
| Darren Van Impe | 1.00 | 0.825 | 21.21% |
| Patrick Lalime | 1.60 | 0.55 | 190.91% |
| Darius Kasparaitis | 1.15 | 1.60 | -28.13% |
| Ian Moran | 0.70 | 0.55 | 27.27% |
| Drake Berehowsky | 1.45 | 0.80 | 81.25% |
| Todd Bertuzzi | 2.00 | 1.175 | 70.21% |
| **Average** | **1.16** | **0.82** | **42.20%** |

Of the 42 players who filed for arbitration in 2001, 27 of them negotiated a settlement without the intervention of a third party. The result of these settlements was an average increase in salary of 42.2%, with a maximum increase of 190%. Considering the average salary increase in the NHL that year was only 14.48%, these settlements, negotiated under the threat of arbitration, were substantially higher. This furthers the notion that teams offered inflated contracts to players in the attempt to avoid arbitration.

However, from the owners' perspectives, this may still have been the more advisable route, because, the average arbitrated award that year was an increase in compensation of 91.68%. The influences of a perceived arbitrated award on the owners and players, as well as the three viable options for players to purse, all served to increase salaries across the league.

## 7.8 Role of Comparables and Statistics in Arbitration

Arbitration in the NHL had similar tendencies to its usage in private and public-sector labour disputes. These similarities arise through the importance of comparables as a means to determine an award. More specifically, the role of comparables is central to an arbitrator's decision with regard to monetary elements.

In the public sector, in order to best identify what an appropriate wage increase should be, arbitrators (assisted by the submissions of the parties at the hearing) will consider what wage increases have been negotiated or awarded in another environment deemed to be a fair comparison (Swan 1978). In the NHL, this refers to compensation of comparable players (in terms of output). It is from these contracts that an arbitrator can determine the monetary elements of their award. Reasonably, an arbitrator who considers the monetary value of a comparable award will look to render one that is similar. However, as noted, in both in the NHL's salary arbitration system and public sector interest arbitrations, there may be little incentive for an arbitrator to award less than what has been determined in comparable situations given the suggested re-hire incentive.

## 7.9 Order of Arbitration

Through the use of player statistics and other arbitrated awards, former NHLPA Executive Director Bob Goodenow and NHL player agents recognized the importance of comparables and manipulated the arbitration system in their favour. Each year, the NHL and NHLPA compiled a list of players who requested salary arbitration according to the order in which their request was received by NHL Central Registry.[35] The NHLPA, under Goodenow's guidance, then looked to order the cases in terms of their strength. For example, cases with the greatest support for large increases in salary from wealthy teams would go first. These awards were then be used to help inflate the later decisions of arbitrators for the weaker cases (Dowbiggin 2003:215). As a result, one generous award at the beginning of the arbitration hearings could influence (and increase) the awards of the later hearings (Conway 2005).

A comparison can be drawn to the way the CAW elects to pattern bargain with the Big Three automotive companies: Ford, General Motors, and Daimler-Chrysler. The CAW targets one of the companies from whom they feel the easiest and most favourable settlement would be received, usually as a function of their profitability. This settlement is then taken to the other two companies in turn and used as the pattern for the deal to be reached there. By ordering the cases in such a manner, Goodenow demonstrated his understanding of the importance of comparables in arbitration and strategic ordering of disputes. Furthermore, he sought to create these comparables each year in order to improve the outcomes for all players.

## 7.10 Asymmetry in the Application of Statistics at Arbitration

It can be argued that successful utilization of player statistics at salary arbitration by the NHLPA played a fundamental role in the inflation of player compensation. Indeed, a member of NHL management was quoted as saying, "The PA used those statistics to turn $600,000 defencemen into $6 million defencemen" (Dowbiggin

2003:216). The types of player statistics recorded by the NHL that were admissible in salary arbitration included, but were not limited to, goals, assists, points, plus/minus,[36] penalty minutes, ice time, games played, power-play goals, and shots. Given that the nature of arbitration is one driven by comparables, each category provided a basis upon which an agent could argue for his/her player to receive increase in salary.

When arbitrating a rights or interest dispute, arbitrators are concerned with rendering an award that seems reasonable and justifiable to the parties, based upon the evidence submitted and previous decisions in comparable situations. More evidence – statistics, in the NHL's situation – supporting an arbitrator's decision is always welcome (from the arbitrator's point of view) because the extent to which an arbitrator's decision appears to be based upon objective criteria of data significantly affects the credibility of the award.

In the late 1990s the NHL developed a more extensive system of statistics, by adding categories such as blocked shots, "hits," and faceoff-winning percentages (Edge 2004:127). As a result, agents and the NHLPA began using these additional categories of statistics to support their cases at salary arbitration through creating new categories of players. Essentially, in earlier times, players were recognized only for their goal-scoring or play-making ability; now however, players were being acknowledged for their different types of contributions. These contributions, argued effectively at arbitration, became deserving of appropriate, and increased, compensation.

It is proposed that a certain asymmetry existed with regard to the application of statistics at arbitration – that is, they were more influential in providing evidence for an increased salary, as opposed to a reduced one. By submitting favourable statistics at arbitration, an agent was able to highlight the positive contributions his/her player has made, both relative to his teammates and in comparison to all players throughout the league. With a greater number of statistical categories came greater opportunities to enhance a player's worth in front of an arbitrator. In contrast, a general manager was faced with a more challenging position to argue negatively based upon these same statistics. For example, the argument that a player did not warrant an increase in salary because he scored only a few goals the past season, could be countered by an agent noting the player's success in other areas, such as winning faceoffs. Therefore, an agent was capable of positioning this player's role within the team, not as a leading goal-scorer, but one who won faceoffs, and did so exceptionally well compared to other players. As a result, an increase in salary became a reasonable expectation. To determine that the value of a player who wins faceoffs is equal to one who scores goals is a very difficult challenge, requiring judgement which is necessarily subjective in nature; however, subjectivity allows an agent to effectively argue this as a comparable benefit to the team and give arbitrators more basis on which to justify larger salary increases. More statistical categories allowed agents to create more categories of players, which increased their ability to put upward pressure on salaries through arbitration. The use of objective criteria justified an arbitrator's decision when considering the evidence submitted by the parties. By skilfully applying these levers at salary arbitration, the NHLPA has been able to increase player salaries almost continually since salary disclosure was introduced in 1990 (Edge 2004:128).

## 7.11 The Broader Influence of Salary Arbitration

Salary arbitration in the NHL has demonstrated inflationary effects on player compensation. Arbitrators, influenced by the salaries of "comparable players" submitted by the parties, statistics, previous awards, and potential re-hire incentives, rendered contracts that significantly increased a player's compensation. These contracts then affected the negotiations of restricted free agents who, in turn, were influenced by a perceived "market price", established by unrestricted and other restricted free agents. Therefore, there was a profound linkage between salary arbitration, contract negotiations for restricted free agents, and the salaries determined by unrestricted free agency that subsequently resulted in an inflationary spiral of player compensation.

# Chapter 8 SUMMARY AND CONCLUSIONS, INCLUDING SOME THOUGHTS ON THE NEW COLLECTIVE AGREEMENT

## 8.1 The Result: All the Elements Interact

The inflationary pressures on player salaries existed throughout each stage of a player's career. A large Group I contract that exploited the performance-bonus clause potentially helped direct negotiations by setting a starting value for a player when he entered Group II free agency. Once a restricted free agent, negotiations over a new contract considered the compensation of other "comparable players" in the league as they established a *de facto* "market price." The contracts of these "comparable players" could be influenced by inflationary qualifying offer provisions, competing offer sheets from other teams, the threat of that player pursuing unrestricted free agency, bidding wars between general managers/owners over the limited number of unrestricted free agents, fulfillment of non-hockey interests, large arbitration awards, and/or hesitancy to proceed to salary arbitration by owners and managers.

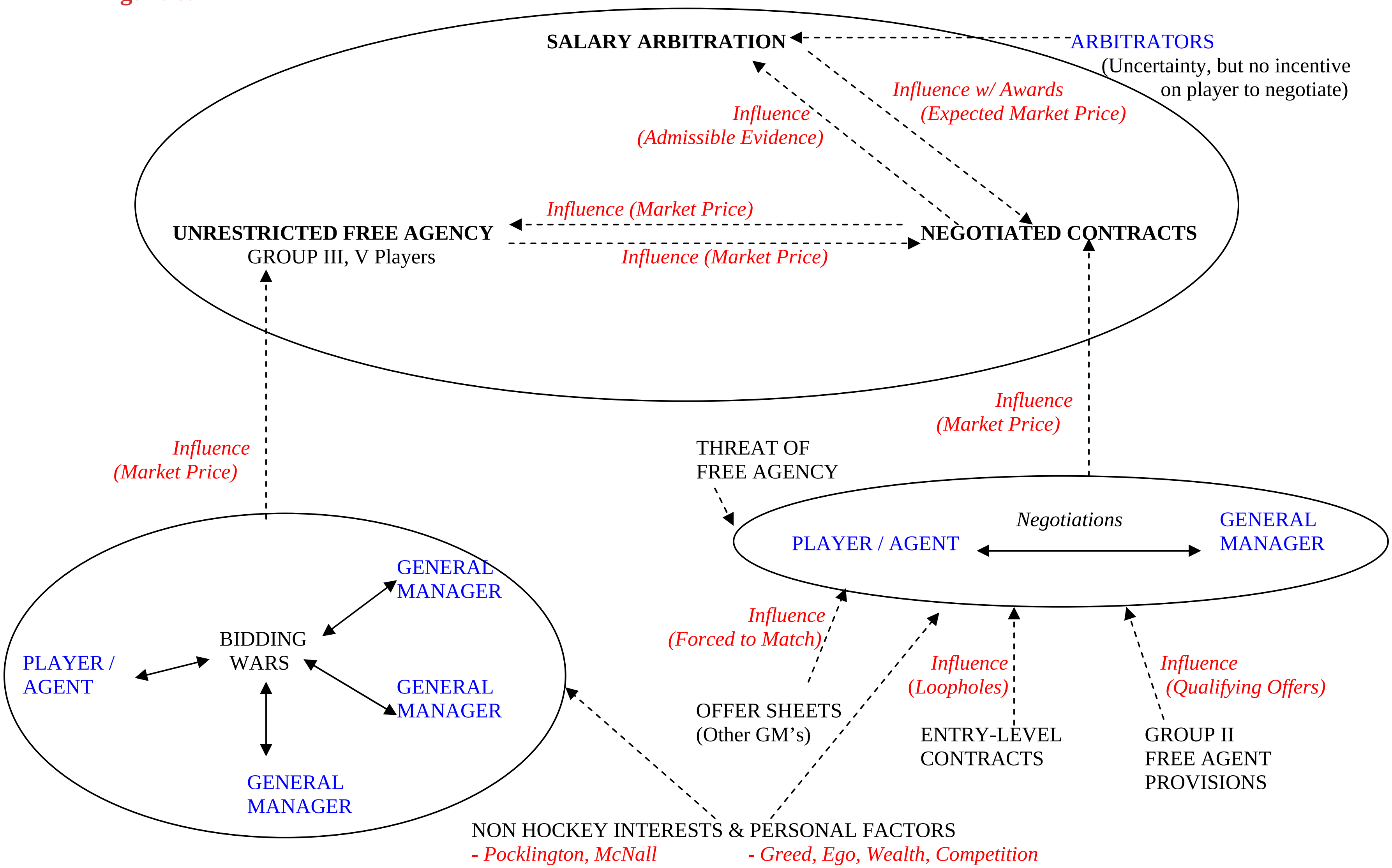
There were numerous variables at work, each with its respective inflationary pressure, that could have influenced the contract negotiations between an agent and a general manager. These variables were not significantly restricted by the collective agreement and, indeed, were able to exert influence across the entire system in a repetitive, compounding manner. The variables, and the processes through which they interacted, are set out below:

1) An unrestricted free agent signing was made, built up by bidding wars (in which, if experience in other negotiation venues is any guide, the winning bidder probably paid too much), and potentially, non-hockey interests (such as the Gretzky and Sakic contracts);

2) This signing then set a *de facto* “market price” for other contract negotiations in the league of both unrestricted free agents, and restricted free agents;
3) Owners and agents, conscious of this “market price,” negotiated similar, inflated contracts for a player’s services;
4) Of these inflated contracts, those belonging to restricted free agents were admissible in salary arbitration;
5) Arbitrators, possibly influenced by the nature of the one-way arbitration process, were forced to consider comparable players and statistics when tendered as evidence to reach an award;
6) Large arbitration awards then encouraged owners and general managers to offer inflated contracts to their players in the hopes that they would not elect salary arbitration;
7) These inflated contracts then set a “market price” for both restricted and unrestricted free agents;
8) All of this taking place in a “market,” the imperfections and inefficiencies of which were manifest and systemically favoured the players.

These interactions are depicted in the following model:

**Figure 8.1**


SALARY ARBITRATION
ARBITRATORS
(Uncertainty, but no incentive on player to negotiate)
Influence w/ Awards
(Expected Market Price)
Influence
(Admissible Evidence)
Influence (Market Price)
UNRESTRICTED FREE AGENCY
GROUP III, V Players
NEGOTIATED CONTRACTS
Influence (Market Price)
Influence
(Market Price)
Influence
(Market Price)
THREAT OF
FREE AGENCY
Negotiations
PLAYER / AGENT
GENERAL MANAGER
GENERAL MANAGER
BIDDING WARS
PLAYER / AGENT
GENERAL MANAGER
GENERAL MANAGER
Influence
(Forced to Match)
OFFER SHEETS
(Other GM's)
Influence
(Loopholes)
ENTRY-LEVEL CONTRACTS
Influence
(Qualifying Offers)
GROUP II FREE AGENT PROVISIONS
NON HOCKEY INTERESTS & PERSONAL FACTORS
- Pocklington, McNall
- Greed, Ego, Wealth, Competition

Every element interacted with, and exerted influence upon, each other, putting upward pressure on player salaries. The continued operation and manipulation of each element by agents, owners, and general managers, the results given further impetus by arbitrators, all motivated by their respective interests, compounded year-after-year on a league-wide basis, resulted in significant salary escalation in the NHL. The structure of the collective bargaining system between the NHL and NHLPA was one that provided a means for salary escalation to occur at every stage in a player's career – from Group I contracts, through Group II restricted free agency and salary arbitration, and finally into Group III unrestricted free agency. The result of such an agreement was an increase in player compensation of 220% over the life of the ten-year collective agreement that expired in September of 2004.

## 8.2 The Nature of the System

The NHL's collective bargaining system between 1994 and 2004 was one characterized by a pattern of unforeseen consequences and decisions based on outcomes. In the negotiation of the 1994 agreement, the salary-cap on entry-level players was intended to curtail player compensation at the early stages of their careers. However, the terms of the agreement provided for the performance-bonus clause to circumvent this cap – an unintended result from the league's perspective. Group II right-to-match provisions were designed to assist teams in protecting their young, talented players. Yet, the offer sheets given to Joe Sakic and Sergei Fedorov in 1997 and 1998 respectively, using creative bargaining strategies unforeseen when the collective agreement was negotiated, caused salary escalation as the teams exercised their right-to-match. Furthermore, in an attempt to attract more fans, the NHL's addition of certain statistical categories ended up providing more opportunities for agents to justify a position for a salary increase at arbitration. Certainly, intent and outcome have not coincided under the 1994 collective agreement, and the nature of the NHL's system is one that catered to outcomes.

When Gretzky was signed by Los Angeles in 1989, his contract then became a precedent upon which others were negotiated, notwithstanding the fact that this was a deal motivated to a great extent by non-"rational" interests, at least in the strict context of hockey. Yet, these interests of the parties were disregarded and the focus was placed on the outcome to direct other contract negotiations, as demonstrated by the subsequent Brett Hull contract. A similar situation occurred with both the Sakic and Fedorov deals. New York was a wealthy team in need of a star attraction, and Carolina's offer of a $12 million bonus to Fedorov should they have reached the conference finals was not meant to reflect his deserved compensation, but to deter Detroit from matching the contract. Again, both were non-"rational" deals in the context of hockey, but ones which exerted influence on future negotiations in the NHL because of their outcomes. They also reflected the competitive environment between teams and the desire to a) make the deal, b) win hockey games, and c) make money.

The arbitration procedure was also subject to this outcome-driven approach, given the importance of comparables. Awards based on the evidence submitted, in terms of comparable players and statistics, reduced the potential for bias on behalf of the arbitrator in favour of one party, enabling his/her award to appear both reasonable and justifiable. However, the motives of the parties behind these objective data could not be effectively considered at arbitration.

The NHL's system was one directed by tangible, recorded outcomes, not the intangible interests that drove certain deals. The numerous variables that influence each negotiation are specific to those parties; yet, it was the result of those negotiations that were considered in future contracts across the league. Therefore, decisions by arbitrators and salaries negotiated between agents and owners that were deemed reasonable and justifiable in one context, influenced other parties in different contexts, regardless of whether or not the same interests and capabilities existed.

## 8.3 The 2004-05 NHL-NHLPA Negotiations

The negotiations between the NHL and the NHLPA from 2004 through 2005 appeared to have typified a distributive, positional approach to collective bargaining. From the outset, both the Players' Association, led by NHLPA Executive Director Bob Goodenow, and the NHL, led by Commissioner Gary Bettman, openly established their incompatible positions and publicly committed to them. By doing so, they sought to "tie their hands" and bind themselves to their respective positions (Schelling 1960). The NHLPA committed itself to the principle that a deal which included a salary cap would never be accepted. By contrast, the NHL positioned itself to accept nothing less than a defined linkage between player salaries and league revenues. Without this linkage, the NHL pronounced, the economic structure of the league would be unsustainable in the future. Given the results of the 2002-03 Unified Report of Operations, as shown in Table 3.2, this position seems well supported. On July 25, 2004, the NHL tabled six proposals to the NHLPA, but all were rejected as they contained some variation of a salary cap. In response, on September 9, 2004, the NHLPA countered the offer with their own: a luxury-tax system that affected teams with payrolls higher than $50 million. Given the continued disparity between the two positions, on September 15, 2004, Commissioner Gary Bettman officially announced a lockout of the NHL's players.

The lockout continued into December, when the NHLPA tabled an offer that included a 24% rollback of existing salaries. In response, the NHL countered with an offer that incorporated the rollback and a salary cap, which was rejected. The negotiating dynamics changed on January 17th, when a small group, initiated by NHLPA President Trevor Linden, began discussions with some members of the NHL. Neither Gary Bettman and nor Bob Goodenow were invited to participate. These talks provided a forum of discussion and varying concepts being submitted from either side; yet, no resolution was found to the dispute. Over the next month, meetings between both parties, discussions within smaller groups, and an intervention by the U.S. Federal Mediation Service all proved unsuccessful. On February 14, 2005, the NHLPA, despite its emphatic position against a salary cap, but possibly realizing that the NHL was not going to concede, tabled a proposal that included a cap of $50 million. This was rejected by the NHL in favour of a $40 million salary cap. Positions were modified slightly over the following two days around a salary cap figure; however, the lack of creativity in bargaining maintained the polarization of the two parties, and on February 16, Gary Bettman officially cancelled the 2004-05 NHL season. According to various accounts, it was this act by the NHL Commissioner that was the turning point in negotiations (Panzeri 2005:19).

The individuals at the forefront of each party, Gary Bettman, and Bob Goodenow, had a similar objective of representing the best interests of their constituents. However, the difficulty associated with this task varied substantially between the two leaders. Gary

Bettman was required to represent the interests of the 30 NHL team owners, and maintain a unified front in the negotiations. The intraorganizational bargaining that ensued presented challenges as each owner has conflicting interests. At the heart of the *intra*organizational and *inter*organizational conflicts lies the perverse incentive system for NHL management: on one hand, like any conventional employer, they want to minimize the amount of money spent on player salaries each year; on the other hand, each team wants to win hockey games and the owners – particularly those who have the financial means – want to be able to spend money in order to acquire talented players to help them. As a result, intraorganizationally, there was a tendency for factions to develop within the party, between the wealthier clubs and those with less profitable teams. However, in order to maintain his given bargaining mandate, Bettman only required the support of 8 of the league's 30 owners, as was dictated by the roles and authority of the commissioner when acting on their behalf. Bettman negotiated this "8 of 30" provision with the owners before bargaining began on the new agreement as a means to more effectively hold the party line. This was a strategically vital move and it allowed for comparably greater ease for Bettman to manage his intraorganizational concerns and force reluctant owners to continue toward the original objectives, even when some of them wanted to concede so as to end the lockout.

By contrast, Bob Goodenow was responsible for representing the interests of over 700 NHL players. He was supported by the NHLPA Executive Committee[37]; yet, the potential for intra-organizational dissonance was understandably higher, based upon the number of constituents alone. As a result, it was a more difficult challenge for

Goodenow to obtain and carry out a bargaining mandate that would be supported by the majority of the players.

Of the three other major professional sports leagues in North America, both the NBA and the NFL have a salary-cap system, while the MLB has a luxury tax. In light of the comparable situations, Bob Goodenow's position of no salary cap – one for which he (initially with the support of the players) was apparently prepared to stay out of work for two years to achieve – appears as an unrealistic goal, particularly in view of a 220% increase in salaries over the life of the previous agreement and the inherently inflationary nature of the salary-determining system under it. The owners knew that the economics of the system had to change, and Bob Goodenow ought reasonably to have known that after ten years of remarkable economic advances for the players, major changes were inevitable. If, as suggested by several writers, (Panzeri 2005:19) the players were caught by surprise when Gary Bettman cancelled the NHL season, then that, too, seems to be more evidence of a flawed strategy by Goodenow. Bob Goodenow should have convinced his players that the threat of a cancelled season was valid and to be considered during negotiations. Subsequently, the players began contemplating the implications of a two-season shutdown, and the united resolve toward a no-cap system began to crumble.

In March of 2005, Trevor Linden and the NHLPA Executive made the decision to negotiate a system with a hard salary cap linked to league revenues. This decision to negotiate on the NHL's terms, was one by Linden and the committee, and not by Bob Goodenow. Linden correctly understood that the players were not willing to sit out another season and a resolution to the lockout was needed. The NHLPA then submitted a proposal that included a salary cap of $50 million and a salary floor of $30 million on

April 4th. Working off that proposal, the NHL and the NHLPA began discussing possible variations of a salary cap and linkage system, with much of the time attempting to understand what is classified as team revenues. Finally, on July 13th, 2005, after weeks of continuous daily meetings, the NHL and the NHLPA announced a tentative deal, pending ratification. Eight days later the deal was ratified by both parties, officially ending the 301-day lockout.

On July 28, 2005, Bob Goodenow announced his resignation as Executive Director of the NHLPA. The reasons behind this decision will not be completely apparent until much later, although there are at least three possibilities. The NHLPA has framed this change in leadership as one that was destined to happen in the near future, because Goodenow's contract had just over two years remaining. Therefore, as the league enters the economic system under the new collective agreement, it is an appropriate time for a new leader to step forward. A second explanation is that, despite the public façade, it was widely understood within the ranks of the Players' Association that Bob Goodenow did not endorse the new collective agreement. He recommended, in his perception of the players' best interests, that they reject this contract and continue with negotiations. Goodenow was vehemently opposed to a salary-cap system as he felt it would turn players against each other regarding compensation (this concept will be explained in detail shortly). A third possible interpretation of Goodenow's resignation was that the Players' Committee felt that he failed in his leadership at this vital juncture. It is possible that they felt that Goodenow should have led them more strategically through the negotiations – that is, he should have recognized the inevitability of major concessions being required by the Association, educated the players to this necessity, and proceeded from there. Over the ten months of the negotiation process, there were stages when he was not invited to participate in discussions. It can reasonably be inferred that his leadership was circumvented by the other members of the Executive Committee, as they, against his recommendations, developed a settlement involving a linkage to league revenue with the NHL. Therefore, the degree to which he was unable to maintain the confidence of his constituents in his perceived best course of action can be questioned.

### 8.4 The 2005 NHL-NHLPA Collective Agreement

Although the new collective bargaining agreement, a document of over 600 pages, has yet to be publicized, some key terms of the deal are available. What is interesting to note is if and how, the inflationary aspects of the previous agreement, have been adjusted. The resulting salary cap figure is one linked to league revenue – 54% of league revenue will establish a team-by-team cap of approximately $39 million in the first year. There is also a salary floor, a level which all teams must be above, of $22 million. By having the salary cap and the salary floor linked to league revenue, there is the potential for it to grow as the financial conditions of the league as a whole improve – theoretically, a true "win-win" outcome of bargaining (Fisher and Ury 1981). This system mimics those of the NBA and NFL, as the NBA has a salary cap of $56 million (57% of league revenue goes to the players), and the NFL has a salary cap of $85.5 million (64% of league revenue goes to the players). The compensation levels of these two sports are higher; however, that is mainly due to the growth of the business over several years of operating under this type of system and a large revenue base. To ensure that this 54% level is maintained, 15% of player salaries will be put into an escrow account. This means that should salaries exceed the 54% level, if revenue fails to meet the projected levels, the difference will be made up with the funds in the escrow account. Conversely, if revenue equals or fall short of this 54% level, the players will have their 15% contribution returned.

One of the main reasons as to why Goodenow was opposed to a salary-cap system was that it puts players in competition with each other for compensation. This runs counter to the original intent of labour unions: to take wages out of competition. A salary cap forces players to compete with other players for a portion of a team's payroll, as there is only a fixed amount available. This type of competition did not exist under the previous system, as owners were the ones competing with each other to offer compensation to the players. Thus, the perverse incentives that have been placed on owners for the previous ten years are now shared to some degree by the players. Players will continue to seek out the maximum compensation levels offered to retain their services, and as stated, this will put them in competition with other players for a share of a team's payroll. However, the greater the compensation received by one player, the less there is available for the team to allot to others. This limits the ability of a team to acquire and retain several star players. With only a limited number of talented players on a team, the potential for success is reduced. This may confront the players with a perverse incentive for the players: on one hand, they desire maximum compensation but, on the other, they also want to play with other talented athletes, of which there may now be a more limited supply on a given team. The new collective agreement, then, may well have shifted a perverse incentive system from the owners to the players.

There is a maximum player salary of 20% of the team cap - $7.8 million under the new system for the 2005-06 season. Although this number can increase with the team salary cap each year, it may be the most effective measure on suppressing large player contracts. The maximum player salary in the league is no longer dictated by the financial means of the wealthy owners, but of the financial condition of the league as a whole. Of all the elements of the new collective agreement, the ability to maintain this linkage between maximum player salary and the financial condition of the league is the most crucial. Essentially, it ensures in an environment governed by communal "ability-to-pay", despite the inherently competitive nature of owners. As a result, other player contracts will be negotiated on a scale in relation to the maximum compensation level. Therefore, when engaging in free-agent bidding wars, owners have a ceiling beyond which their bids may not go. The potential for these wars to become a race to that ceiling is also limited, as all teams will not be able to offer that player the maximum compensation level if they are to fit under the team salary cap.

A question to be raised with this individual cap concerns how it will be managed, explored, and exploited by owners and agents. In the same vein as the performance bonus clause for entry-level players was exploited in the previous agreement, it will be of interest to learn if there is the potential for agents, owners, and general managers to circumvent this salary cap in a similar manner. For example, one might speculate if a star free agent signed by Detroit suddenly begins endorsing Little Caesar's Pizza – Red Wings' owner Mike Illitch's other business – for an additional million dollars a year. The incentive for team owners to use financial compensation as a means to lure star players still remains. The means by which this compensation may potentially be given to players, without restricting a team's ability to succeed under a salary-cap system, could be the result of carefully orchestrated arrangements by owners and agents, external to the collective agreement and to the player's duties to the team. Owners continue to operate in a competitive environment, and their desire for success, compounded by their individual wealth, will encourage a creative circumvention of the salary cap to be discovered.

There is a minimum salary level of $450,000 for each player. This is a significant raise from the previous amount of $185,000. For those players who were previously making at, or just above the league minimum before, this represents a substantial raise in compensation. The effect of these players at the league minimum receiving pay increases will be upward pressure on player salaries for all those above. For example, if a player was making twice the league minimum in the previous agreement, an agent will have an argument that such should be the case under the new agreement to appropriately reflect his player's relative worth. Although a salary increase from $370,000 to $900,000 may not be realistic in the new economic system, an increase to any degree above the league minimum will influence other contract negotiations throughout the league. Again, the importance of objective comparables in negotiation and arbitration becomes relevant.

The entry-level compensation system has been modified with the intent of preventing the inflationary outcomes of the previous agreement from reoccurring. Entry-level players are subject to a maximum compensation of $850,000, and the duration under this system replicates the requirements of the previous agreement. This limit increases by $25,000 every two years, to a maximum level of $925,000 in 2011. Entry-level players may negotiate for performance bonuses up to a maximum of $850,000 in individual "Schedule A" bonuses per year (maximum of $212,500 per bonus). This means that an entry-level player is able to double their annual compensation through these specified bonuses. A player may also be eligible to earn individual "B" bonuses for league-wide excellence, which are paid by the NHL. These will typically be attained by only the most talented of entry-level players. In addition, a player will be eligible to negotiate with his club "excess" individual "B" bonuses, subject to a maximum aggregate of $2 million in any year. These “excess” bonuses seem to provide a basis for the large, performance-laden rookie contracts of the past to be replicated. It will be interesting to discover how the specific terms of this clause are manipulated by agents and teams. Given these terms, it would seem that entry-level players have the potential to receive annual compensation in excess of $3 million. How much further that value can be increased will depend upon the exact terms, or absence of terms, of the agreement. With compensation at such a level, the impacts on subsequent contracts negotiated by those players as they enter restricted free agency, as outlined previously, will be interesting to note.

With regard to qualifying offers, the following changes have taken place under the new agreement. Players earning between $450,000 and $660,000 will be entitled to qualifying offers at 110% of their prior year’s salary. Players earning more than $660,000 and up to $1 million will be entitled to qualifying offers at 105% of their prior year’s salary. Finally, players earning more than $1 million will be entitled to qualifying offers at 100% of their prior year’s salary. These terms of the new agreement will potentially have an inflationary impact on league salaries. For those players making less than $1 million, they will receive increases per the terms of the agreement. As noted, the nature of negotiation surrounding qualifying offers – the incentives of agent to use this offer as a floor in bargaining, and the inflationary aspect of competing offer sheets – can lead to salary escalation. What may be observed is a significant upward pressure toward, and eventually beyond, the $1 million level. Increased minimum salary reduces the range within which players may be differentiated through compensation. As a result, the need and desire of owners to acquire players of greater ability than those being paid at, or close to, the league minimum, will require appropriate (higher) compensation. These incentives, in combination with the negotiating abilities of agents, and the patently inflationary qualifying offers, could have noticeable impacts. Although not initially substantial, over the course of several years, with hundreds of players influencing this process, there may be an opportunity for the inflation of NHL salaries.

The salary arbitration system has been modified so that both players and teams can elect this process, with the provisions regarding when a player can elect this process remaining similar to the last agreement. The arbitrator's role is largely unchanged, as he/she will be required to select a value somewhere between the parties' positions. However, clubs can only take a player to salary arbitration under one of two circumstances:

1) If the player earned more than $1.5 million in their prior year, the club will have the right to elect salary arbitration in lieu of making a qualifying offer, or
2) The club may elect salary arbitration for Group II players who did not elect this process.

By making salary arbitration a two-way process, the intent is, presumably, for teams to have the ability to offer lower compensation levels for under-performing players or, at least, lower than they players would like. Furthermore, this would appear to reduce any possible incentives placed on arbitrators under the old agreement regarding their re-hire motivations. However, despite a two-way process, there is still the opportunity to question the appearance versus the reality of objectivity in this context. As there are far more players than owners, the opportunity for future employment still is weighted toward the satisfaction of players with arbitration awards. Players may still elect to proceed to arbitration at their discretion. Therefore, the likelihood of an arbitrator rendering an award that decreases a player's salary, or the degree to which that happens, is a point of debate; yet, it is unlikely that players will see increases of the same magnitude as before. Finally, it will be interesting if a team's position under the salary cap (the amount of money they are able to spend without exceeding the maximum) can be submitted as evidence in arbitration hearings. Reasonably, arbitrators will be restricted in their awards by the individual player salary cap; however, the extent to which awards deemed reasonable and justifiable will be influenced by the financial situation of the team as a whole will be of interest.

Unrestricted free agency has undergone significant changes in the new agreement. It will stay at 31 for the first year of the agreement, drop to 29 in the second year, 28 in 2007, and 27 in 2008. As well, players who have 7 years of NHL experience can be unrestricted free agents. This means that players who enter the league at age 18 will be eligible for unrestricted free agency at 25 years of age. Players cite this as a significant gain, as unrestricted free agency allows them the freedom to play almost wherever they choose. However, the impact unrestricted free agency has had on increasing player salaries was largely due to the concept of scarcity. With fewer desirable players available each year, the potential for bidding wars to develop was substantial. Conversely, with a greater number of free agents each year, the rules of supply-and-demand economics would suggest that salaries will not experience the same inflation and the salary cap will exert downward pressure. Even with a salary cap, scarcity of free-agents will entice owners to offer contracts closer to the maximum allowable level. With a greater number of free agents each year, in effect, it creates substitutes for the owners. This reduces the incentive to offer high salaries for the rights to a player's services. How this dynamic plays out, and its interaction with other negotiated contracts in the league will be interesting to observe.

The manner in which the elements that influence salary determination in the NHL interact under the new collective agreement will be markedly different than the previous ten years. The inflation of player compensation will no doubt continue to occur in the NHL; however, the linking of salaries to overall league revenues will limit the role that agents, owners, and general managers can play in manipulating the system. The intent is that, under the new agreement, increases in player salaries will be a reflection of the economic growth of the league as a whole, and the "market" for a player's services will be one that is less inefficient and encompasses all thirty teams. It is to be hoped that, however the new system works in practice, it will result in fairness to both sets of parties and, consequently, that a destructive and unnecessary war, like the 2004-2005 lockout, will never recur.

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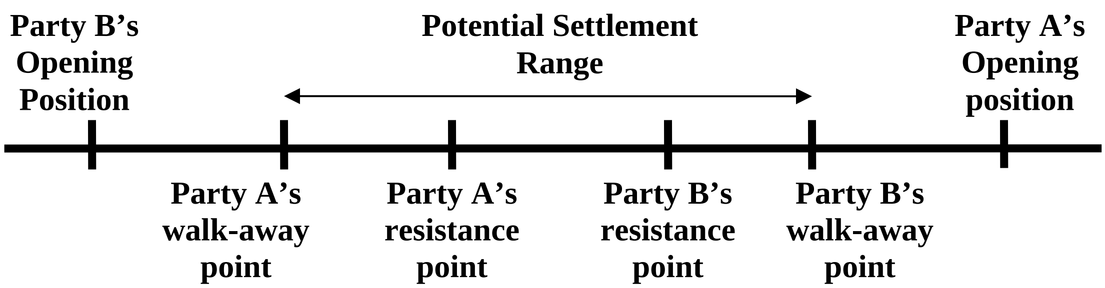
# APPENDIX

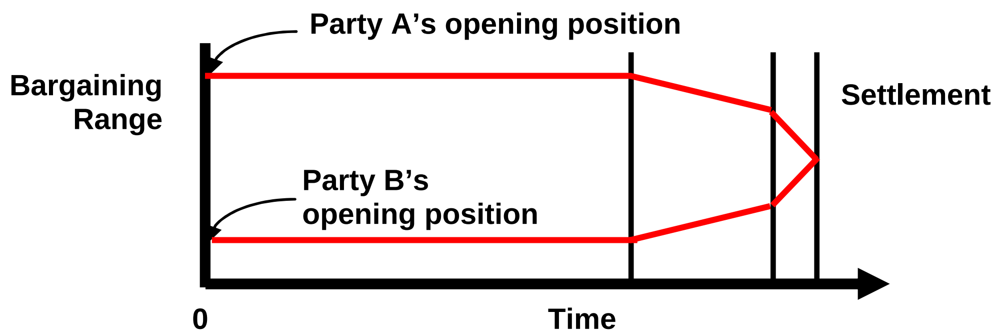
## Appendix 1 Ownership Structure of the NHL Teams

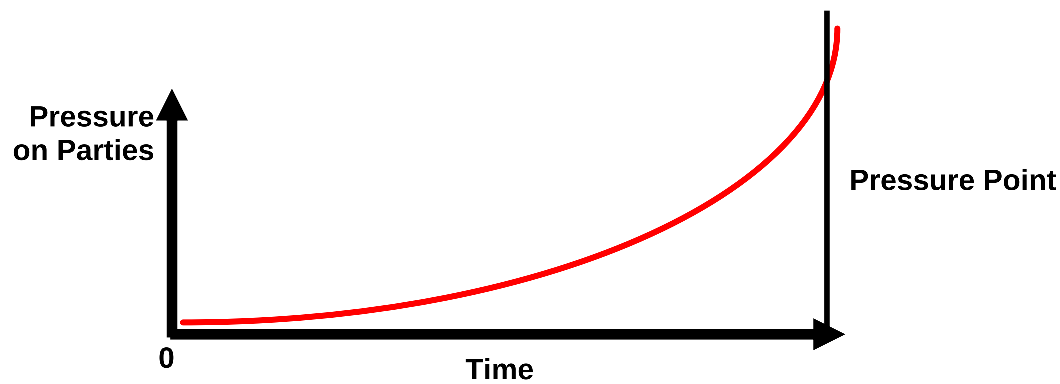
| Team | Principal Owners | Business |
|---|---|---|
| Anaheim Mighty Ducks | Henry Samueli | Internet Communications |
| Atlanta Thrashers | Steve Belkin | Trans National Group |
| Boston Bruins | Jeremy Jacobs | Delaware North Co. |
| Buffalo Sabers | B. Thomas Golisano | Paychex |
| Calgary Flames | Harley Hotchkiss | Real Estate, Oil and Gas |
| Carolina Hurricanes | Peter Karmanos Jr. | Computer Software |
| Chicago Blackhawks | William Wirtz | Diversified Interests |
| Colorado Avalanche | COMSAT Video Ent. | Entertainment, Denver Nuggets |
| Columbus Blue Jackets | John H. McConnell | Worthington Industries (Steel) |
| Dallas Stars | Tom Hicks | Investments, Southwest Sports Group |
| Detroit Red Wings | Michael Illitch | Little Casers Pizza Parlors |
| Edmonton Oilers | 38 Owners | Edmonton Investors Group LP |
| Florida Panthers | Alan P. Cohen | Pharmaceuticals |
| Los Angeles Kings | Phil Anschultz | Railroads, Real Estate |
| | Edward Roski | |
| Minnesota Wild | Bob Naegele Jr. | Minnesota Sports & Entertainment |
| Montreal Canadians | George Gillett Jr. | Booth Creek Management Corp. |
| Nashville Predators | Craig Leipold | Restaurants, Entrepreneur |
| New Jersey Devils | Jeff Vanderbeek | Lehman Brothers Investment Firm |
| New York Islanders | Charles Wang | Computer Associates |
| | Sanjay Kumar | |
| New York Rangers | James L. Dolan | Cablevision, Madison Square Gardens |
| Ottawa Senators | Eugene Melnyk | Biovail, Pharmaceuticals |
| Philadelphia Flyers | Ed Snider | Newspapers, Insurance |
| Phoenix Coyotes | Steve Ellman | Arizona Hockey Management, Real Estate |
| | Wayne Gretzky | Former Hockey Player |
| Pittsburgh Penguins | Mario Lemieux | Hockey Player |
| San Jose Sharks | Greg Jamison | San Jose Sports & Entertainment |
| St. Louis Blues | Bill Laurie | Walmart Heir |
| Tampa Bay Lighting | William Davidson | Guardian Industries Corp. |
| Toronto Maple Leafs | Larry Tanenbaum | Maple Leaf Sports & Entertainment |
| Vancouver Canucks | Francesco Aquilini | Investment Group |
| Washington Capitals | Ted Leonsis | Internet Investments |

## Appendix 2 Positional Bargaining Range Diagram



## Appendix 3 Time/Pressure Influences in Negotiation



## ENDNOTES

[i] A salary-cap system is one in which there is a specified maximum payroll level for all the teams in a league. This type of system exists in the NFL and is a method of controlling player compensation.
[2] To restate, Stephen Bartlett is an agent for many NHL players
[3] When the NHL began there were only 6 cities with teams: Toronto, Montreal, Boston, New York (Rangers), Chicago, and Detroit
[4] At that time, questions were raised about the owners' abuse of the players' pension fund as a means to collect additional revenue, and claims of the league's financial troubles were discovered to be false. As a result, players Ted Lindsay (Detroit) and Doug Harvey (Montreal) enlisted the support of all but one of the players in the NHL to the cause of a players' association on February 12, 1957. In response, the owners attacked Lindsay and his credibility publicly, had an unprecedented 32% roster changeover across the league through trades and promotion of rookies, and some teams even forced players to sign a "loyalty pledge" to their team. Momentum for the association declined, led by the entire Detroit Red Wings team revoking their support, and in 1958 the first NHLPA died. There were never any questions answered regarding handling of the pension fund (Houston, 1993:50).
[5] See Selekman, B.M., S.K. Selekman and S.H. Fuller, 1958. Essentially, relationship pattern is the set of reciprocal attitudes salient to the parties in their interaction. The patterns include (in order of increasing degrees of friendliness): Conflict, Containment-Aggression, Accommodation, Cooperation, and Collusion.
[6] Eagleson collectively bargained an agreement that allowed the NHL to take complete control of the players' pension fund. Essentially, this move permitted the NHL to redirect any surplus money realized from the fund to itself.
[7] Millionaire players meaning those who have an annual salary of $1million or greater
[8] Eric Lindros signed a six-year deal with the Philadelphia Flyers in 1992 for $21.8 million. Alexandre Daigle signed a five-year deal with the Ottawa Senators in 1993 for $12.5 million.
[9] A payroll tax is a system that forces teams to pay extra for every dollar spent above a pre-determined limit. For example, a payroll tax of 100% at $40 million means that for every dollar a team's payroll exceeds the $40 million mark, they must pay an additional dollar into a fund, which is then distributed to the lower-spending teams. It is a method of attempting to control the expenditures of high-revenue clubs.
[10] Financial data taken from 2002-03 NHL Unified Report of Operations, as submitted by the teams
[11] See Article 9.1(b) of NHL CBA
[12] See Article 9.3(a) of NHL CBA
[13] See Article 9.3(d) of NHL CBA
[14] http://www.cbc.ca/sports/indepth/cba/issues/rookiesalarycap.html
[15] It can be assumed that there is an approximate correlation between a player's contribution to his team and his compensation level.
[16] Each year, the NHL holds a draft for its teams to acquire the rights to amateur players. There are seven rounds to the draft. Typically, the team that finished last in the league the previous year will be awarded the first pick, and the second lowest-finishing team gets the second overall pick, and so on. This continues through the 30th draft position (30 teams in the league), and that team picking 30th, will pick 31st, and the order is reversed. The selection order continues to wind up and down the list through the seven rounds. Teams are able to trade future draft picks to other teams.
[17] In the 2003-04 season, for example, the Washington Capitals, who were not destined to make the playoffs that year nor were they projected to make a profit, traded away players Robert Lang ($5 million salary) to Detroit, and Jaromir Jagr ($11 million salary) to the New York Rangers.
[18] www.HockeyZonePlus.com
[19] Unrestricted Free Agency was negotiated into the collective agreement in 1990; however, player movement was still restricted as the original team was required to be compensated (by receiving a right of first refusal, or draft choices) from the team signing away their free agent. The 1992 agreement removed any form of compensation being owed to the prior club.
[20] The other two groups, V and VI, typically have a less noticeable impact as a result of the number and/or relative talent of players falling into these groups.
[21] From the 1994/95 through the 1996/97 seasons, this age level was set at 32.
[22] Manipulation of a player's perceived utility is elaborated on later, with consideration of theories presented by Walton & McKersie 1965.

[23] See Appendix 1: List of NHL teams and owners
[24] During the 2003-04 season, the Toronto Maple Leafs had revenues of $117 million, second highest in the league. The New York Rangers had revenues of $118 million.
[25] Europe is not counted as a consistently viable alternative as North American players will likely refuse to leave their families for a year.
[26] Player agents in the NHL typically receive a percentage commission (around 4%) from a player's salary. Therefore, the higher the salary, the higher the commission earned by the agent.
[27] BATNA: Best Alternative to a Negotiated Agreement. See Fisher, R. and Ury, W. *Getting to Yes*. 1991, p. 100
[28] See Appendix 2: Bargaining range diagram
[29] See Appendix 3: Time/pressure chart in negotiations
[30] www.HockeyZonePlus.com
[31] See Article 12.5(f)(iii)(2) of NHL CBA
[32] See Article 12.2(e)(i) of NHL CBA
[33] The 2.2% increase is remarkably low for the 2003-04 season, given the increase in player salaries of 220% over the ten-year collective agreement, and therefore warrants some explanation. Anticipating what the economic environment was going to be under the new collective agreement, Gary Bettman strongly urged all owners not to sign players to large contracts that extended beyond the 2003-04 season. This was intended to benefit the long-term interests of the owners, should the outcome of bargaining in 2004-05 yield a salary-cap system, as was desired. As a result, player salaries were subject to downward pressures and that is reflected in the league-wide annual increase.
[34] Discussion with Richard L. Jackson, August 3, 2005
[35] Article 12.2(e)(ii)
[36] Plus/Minus – A player rating determined by the difference between the number of even-strength goals scored for his team while he is on the ice, and the number of even-strength goals scored against his team while he is on the ice.
[37] The NHL Executive Committee is comprised of 7 players: Trevor Linden (President), Bob Boughner, Daniel Alfredsson, Arturs Irbe, Bill Guerin, Trent Klatt, and Vincent Damphousse.