While we have run a prior article on this subject, guest author Kristi Dosh of It's a Swing and a Miss has gone into further detail on how revenue-sharing and the Competitve Balance Tax (Luxury Tax) functions in Major League Baseball. Enjoy. -- Maury Brown, President, Business of Sports Network, BizofBaseball.com

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I've spent the past four years studying, writing and guest lecturing on revenue sharing and internal taxation in Major League Baseball. Accordingly, I'm fascinated by the debate raging in the media between Randy Levine, President of the Yankees, and Mark Attanasio, the owner of the Brewers. What really caught my eye though was the confusion between revenue sharing and the competitive balance tax. As I've guest lectured on these topics over the past four years, I've found that even your most avid baseball fan doesn't generally know or understand the difference.

So, before I explain the difference, let me set the stage for you…

It all started with this comment to USA Today by Mark Attanasio, owner of the Milwaukee Brewers:

"We're struggling to sign Prince Fielder, and the Yankees infield is making more than our team."

Enter Randy Levine, President of the Yankees, who said this to ESPNNewYork.com :

“I’m sorry that my friend Mark continues to whine about his running the Brewers. We play by all the rules and there doesn’t seem to be any complaints when teams such as the Brewers receive hundreds of millions of dollars that they get from us in revenue sharing the last few years. Take some of that money that you get from us and use that to sign your players.”

“The question that should be asked is: Where has the hundreds of millions of dollars in revenue sharing gone?”

Ok, I’m on board so far. It’s the same old David versus the Yankees story as always in baseball. The real problem comes in how the story has been framed by many media outlets.

Gabe Lacques, who wrote the USA Today piece, wrote this in his article:

“According to the *Biz of Baseball*, the Yankees have accounted for $175 million – or 92% – of all revenue-sharing payments since revenue sharing was instituted.”

Andrew Marchand, who wrote the ESPNNewYork.com story, similarly stated:

“In the initial seven years of the luxury tax, the Yankees have paid teams nearly $175 million in revenue sharing, according to the BizofBaseball.com. That is 92 percent of the total revenue sharing that has been doled out.”

Enter confusion, stage right. Revenue sharing and the luxury tax (which, by the way, was renamed the “competitive balance tax” in the 2002 CBA, which covered 2003-2006) are two completely separate concepts. Aside from the Yankees having to pay both, they have very little

in common.

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Revenue Sharing

Revenue sharing was first approved by the owners in 1994 and included in the 1996-2000 Collective Bargaining Agreement, presumably as an alternative to a salary cap, which was ruled out by the MLBPA. Revenue sharing is based on a club's Net Local Revenue for a given year. Understanding what Net Local Revenue is takes the reading of no less than five definitions in the CBA, but I'm going to provide you the overly simplified version. Net Local Revenue is Local Revenue (gross revenue from all revenue areas like ticket sales, concessions, etc. minus Central Revenue, which is national television and radio, etc.) minus Actual Stadium Expense (which is exactly what it sounds like, the actual monies paid out by a club for its stadium).

The 1996-2000 CBA phased in revenue sharing with the use of three different plans:

Split Pool Plan: each club put in 20% of their Net Local Revenue. Those monies were then divided 75/25, with 75% being split evenly amongst all clubs and 25% being split only between those clubs with a Net Local Revenue below the mean for all clubs. The 25% was not split evenly between those clubs below the mean, but based on their distance from the mean.

Straight Pool Plan: each club put in 39% of their Net Local Revenue and it was split evenly with all clubs.

Hybrid Plan: evaluated the result each club would have under each of the above plans and then assigned the plan that was better for that club as a payor/payee. So, if the Yankees would pay out less under the Split Pool Plan, they were assigned that plan. If the Royals would receive more under the Straight Pool Plan, they were assigned that plan.

Then, to make it even more confusing, the plan was implemented on a percentage basis:

- 1996: 60% Hybrid Plan
- 1997: 60% Hybrid Plan
- 1998: 80% Split Pool Plan
- 1999: 85% Split Pool Plan
- 2000: 100% Split Pool Plan

So, in 1996, a club received or paid 60% of the total result under the Hybrid Plan. The result was that $50 million was moved around in 1996. By 2002, that number would be $169 million.

In 2002, revenue sharing was simplified under the next CBA. The Straight Pool Plan was in effect for the length of the CBA at a rate of 34%. So, each club put in 34% of their Net Local Revenue each year, and then the pool was divided evenly between all of the clubs. A Central Fund component was added, which called for 41.066% of the total amount transferred from payor clubs to payee clubs to be pulled from baseball's Central Fund and divided between payee clubs whose average Net Local Revenue over the past three years fell below the average for all clubs over that same time period. The amount distributed was to be deduced from distributions to be made to payor clubs at the end of the season. There's a very specific mathematical formula for this in the CBA, but I won't go into it here.

I know you've all heard the grumblings about teams receiving more in revenue sharing than the spend (*cough* Marlins *cough*). An example I use in my lectures is the 2005 Florida Marlins. Payroll was cut by nearly 75% to a league-leading low of $14,998,500, more than $20 million below the next lowest payroll. Meanwhile, their cut of revenue sharing was reported to be $31 million, leaving them $16 million for other "baseball-related" activities. That's the only parameter given in the CBA for spending revenue sharing dollars, by the way: that it be used for "baseball-related activities."

The 2006 CBA contained a revenue sharing provision very similar to the 2002 CBA. The percentage was decreased from 34% to 31% because of increased revenues league-wide, but the other provisions remain mostly unchanged.

Time for another example I use in my lectures. The Royals revenue sharing receipts doubled from 2002-2007, but payroll only rose by 6%. Meanwhile, the team value has risen from $96m

to $282m. Just food for thought.

Need dessert to go with that? Consider this quote by Mr. Attanasio:

“We do get a piece of revenue sharing, and we appreciate it, and we need it, and we use it. We put it to use. It’s a matter of record that we use our revenue sharing dollars pretty much every year in our budget.”

First off, I’m bothered by the use of “pretty much,” which makes me wonder why not always? Second, when he says it’s a matter of record, don’t be fooled into thinking it’s a matter of public record. It’s not. Every club in MLB guards its numbers very closely, and you will never see the Brewers budget and be able to ascertain for yourself just where that revenue sharing money is going.

As if that weren’t enough, another issue with revenue sharing is the Net Local Revenue calculation, which is easily manipulated. Picture this…Club A’s owner is also the owner of ABC, Corp., which provides concession services. Club A hires ABC, Corp to provide concessions at its ballpark. Club A’s owner overpays ABC, Corp in order to decrease Club A’s Net Local Revenue number, thus increasing Club A’s share of revenue sharing distributions.

Haven’t had enough yet? Another example…Club B’s owner also owns XYZ Media, Inc., which airs Club B’s games locally. Club B negotiates a contract with XYZ Media, Inc. where XYZ Media, Inc. underpays for its contract to air Club B’s games locally, thus lowering its Net Local Revenue number and increasing its share of revenue sharing distributions.

Oh, and if you’re still feeling bad for the Brewers and the other small market teams, consider this: in 2002 three teams were sold and bought. The Red Sox, who are obviously in a large market, sold for $380m (taking on about $40m in debt). The New York Mets, another large market team, sold for $391m. The Marlins, the poster child for small market teams, sold for $158m. Ever heard you get what you pay for?

Luxury Tax

After the infamous strike of 1994, the owners also managed to introduced the luxury tax after being defeated on the salary cap by the MLBPA. Most people think it was aimed directly at Steinbrenner and his seemingly endless wallet, and most people are right.

The only thing the luxury tax has in common with revenue sharing, aside from hitting the Yankees wallet the hardest, is that they made it way too complicated in the 1996 CBA. The luxury tax was only implemented under that CBA for 1997, 1998 and 1999. Thresholds were set and any team who exceed the threshold paid the tax:

- 1997: $51 million threshold (35% tax on amount over threshold)
- 1998: $55 million threshold (35% tax on amount over threshold)
- 1999: $58.9 million threshold (34% tax on amount over threshold)

Simple, right? Yep, so they had to make it a little more complex. Enter the “floating threshold” concept. At the end of each season, if the midpoint between the fifth and sixth highest payrolls was more than the threshold, then that became the new threshold. Then, the threshold for the next year would be adjusted based on that number.

Now even if you can grasp all that, the definition of Actual Club Payroll is sneaking in at stage left to really complicate matters. Actual Club Payroll is 1/28th (there were only 28 clubs then) of player benefit costs, player salaries and other amounts like bonuses and deferred compensation. Throw in that some players are only with the team for part of the year, or have a contract that doesn’t specify amounts for each individual year, and you really have a mess on your hands.

Requests can be made within MLB or by the MLBPA with regards to how the acquisition of a player might affect a club’s payroll total. This was meant to make the luxury tax figure into a club’s decision to sign a player. It was assumed most clubs would try to avoid the penalty. However, the floating threshold concept got in the way in the beginning. The very first year the tax was in effect, 13 clubs were over the midpoint between the fifth and sixth highest payroll and were hit with the tax.

Before I get into how the tax has evolved, I should clarify where the money goes. Under the 1996 CBA, the first $10m went to compensate for any issues with the revenus sharing plan (such as running short under the Hybrid Plan), the next $7m went to the 5 AL clubs and 5 NL clubs with the lowest Local Revenue, the next $3m went to the Industry Growth Fund (which funds training camps and other baseball development activities domestically and internationally), and the next $2.5m went to fund a reserve for any overpayments made into the system. In the end, $30.9m was collected under the 1996 CBA.

The 2002 CBA saw the luxury tax become the competitive balance tax and introduced a somewhat new system. Much higher thresholds were set for 2003-2006:

- 2003: $117m
- 2004: $120.5m
- 2005: $128m
- 2006: $136.5m

Increasing penalties for repeats offenders was also introduced, making it clear that the tax was meant as a deterrent and a penalty:

- 2002 First-Time Offenders: 17.5%
- 2003 First-Time Offenders: 22.5%
- Second-Time Offenders: 30%
- Third-Time Offenders: 40%

The distribution of funds also evolved, no longer providing for funding to low revenue clubs, thus distinguishing it entirely from revenue sharing. The first $5m would go to refund for any miscalculaations, then 50% would go to player benefits, 25% to the Industry Growth Fund, and 25% to developing baseball in countries without high school programs.

The 2006 CBA kept the basic model of the 2002 CBA with adjustments for thresholds and taxation amounts:

- 2007: $148m
- 2008: $155m
- 2009: $162m

- 2010: $170m
- 2011: $178m

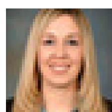
Penalties also increased:

- First-Time Offenders: 22.5%
- Second-Time Offenders: 30%
- Third-Time Offenders: 40%

Distributions remain roughly the same and continued the trend towards fudning player benefits with the tax money. The first $2.5m is set aside for refunds, then 75% for player benefits and 25$ to the Industry Growth Fund. Thus, the tax is not distributed to low revenue clubs.

Now back to the statements by Mr. Lacques and Mr. Marchand. The Yankees have not paid 92% of the total amount of revenue sharing distributed. They have, however, paid 92% of the luxury/competitive balance tax over the years. They are the only club to have paid the tax each and every year since its inception.

If you want to understand more about these provisions and how they evolved, you can check out my article in the University of Denver Sports and Entertainment Law Journal here . I'm also covering all of this in my book, which is coming soon!



Kristi Dosh runs It's a Swing and a Miss, and is both an attorney and a student of the game of baseball. For the past three years, Kristi has contributed to the Braves blog Chop 'n Change . Kristi is also the author of *Can Money Still Buy the Postseason in Major League Baseball?: a 10-year retrospective on revenue sharing and the luxury tax* , published by the University of Denver Sports & Entertainment Law Review (2007). Currently, Kristi is working on a book that will expand upon the ideas considered in her previous legal

journal article.

Kristi guest lectures on the topics of revenue development, revenue sharing, collective bargaining and various other topics related to administration and economics in Major League Baseball to both undergradute and graduate students on a regular basis.

Kristi holds a Bachelor of Arts in Politics from Oglethorpe University and Juris Doctor from the University of Florida. Kristi resides in Atlanta, where she can easily attend Atlanta Braves, Gwinnett Braves and Rome Braves games. She is on a number of boards, including the Advisory Board for L.E.A.D. , a revolutionary inner-city baseball program in Atlanta.