

LABOR LAW—COLLECTIVE BARGAINING—ONE YEAR OPTION-OUT
CLAUSE IN A MULTI-YEAR CONTRACT IS NOT A CIRCUMVENTION
OF THE SALARY CAP UNDER THE COLLECTIVE BARGAINING
AGREEMENT IN THE NATIONAL BASKETBALL ASSOCIATION—*In re
Dudley*, 838 F. Supp. 172 (D.N.J. 1993).

In *In re Dudley*, 838 F. Supp. 172 (D.N.J. 1993), Chris Dudley, a member of the National Basketball Players Association (NBAPA), signed a multiyear contract that included a one year option-out clause with the Portland Trailblazers of the National Basketball Association (NBA). *Id.* at 175. The NBA challenged the contract as an attempt by the Trailblazers to circumvent the NBA salary cap, which limited the amount of money the team could expend on players, and, more specifically, limited the amount of money that a team may pay for another team's free agent. *Id.*

Dudley, a second string center for the New Jersey Nets of the NBA during the 1992-93 season, desired to be a starting center with a championship caliber team on the West Coast. *Id.* at 174. Since he was a free agent, Dudley entered into a seven year contract with the Trailblazers for \$10,512,000, including a salary of \$790,000 for the 1993-94 season, the first year of the contract. *Id.* at 175. The Nets offered Dudley a seven year contract worth \$20,748,000, including a salary of \$1,560,000 for the first year of the contract. *Id.* at 174-75. The Nets also guaranteed the first six years of the contract. *Id.* at 174. Because Dudley was a free agent from another team, the Trailblazers limited its offer to Dudley to a defined salary slot under the salary cap. *Id.* at 175. If Dudley was a Trailblazer free agent, as opposed to a Net free agent, the salary cap would not have restricted the amount of money that the Trailblazers could have paid Dudley in a multiyear contract. *Id.* at 174. In an attempt to sign Dudley, Geoffrey Petrie of the Trailblazer front office suggested an option-out clause, exercisable by Dudley after the first year of the multiyear contract which would allow Dudley to option-out of the remainder of the contract. *Id.* at 175. As a result, Dudley would become a Trailblazer free agent for the 1994-95 season, and the Trailblazers would be able to re-sign Dudley to a contract commensurate with his market value without being constrained by the salary cap *Id.*

On September 7, 1993, Special Master Clark held that the option-out clause was not a per se salary cap circumvention and that

the collective bargaining agreement (CBA) between the NBA and the NBAPA contemplated player options which lengthened or shortened the terms of service in multiyear contracts. *Id.* at 173-74. The NBA appealed Special Master Clark's decision to the United States District Court for the District of New Jersey on September 12, 1993. *Id.* at 174.

On appeal, the United States District Court for the District of New Jersey affirmed Special Master Clark's decision by holding that the one year option-out clause did not circumvent the CBA and that the CBA did not prohibit such a clause expressly. *Id.* at 184. The court summarized particular CBA provisions that regulated the salary cap before the court analyzed the points of Special Master Clark's decision. *Id.* at 176-77. First, Judge Debevoise of the United States District Court for the District of New Jersey explained these provisions that required the NBA to pay its players an aggregate dollar amount in salaries and benefits equal to fifty-three per cent of the NBA's revenues. *Id.* at 176. The court mentioned that the objective of the salary cap was to preserve team competition throughout the NBA by preventing the stronger financial teams from signing the best players to the disadvantage of the weaker financial teams. *Id.*

The court then examined another CBA provision that permitted a player to decrease or to increase the term of his contract. *Id.* at 177. Judge Debevoise held that where the parties agreed to include an option in a contract which permits a modification of a term of the contract, and the player receives any form of consideration in connection with the exercise of that option, then the compensation should be considered a signing bonus within the terms of the CBA. *Id.* Because Dudley was a free agent at the exercise of his option-out clause after one year of the contract, the court found that the option-out clause was within the terms of the CBA and not a cap circumvention. *Id.*

The NBA argued that because the contract Dudley signed with the Trailblazers was below Dudley's market value in the NBA, the contract violated the CBA. *Id.* The NBA stressed that the Trailblazers did not have sufficient money under the salary cap to pay Dudley his market value, and Dudley's option to terminate the contract after one year enabled the Trailblazers to escape the limitations of the salary cap. *Id.* As a result, the NBA argued that Dudley's contract violated Section Three of the CBA which proscribes any transaction that the parties designed to circumvent the

salary cap. *Id.*

As a corollary to its Section Three argument, the NBA also argued that the circumstances surrounding the Dudley contract demonstrated an implicit understanding that the Trailblazers would re-sign Dudley after he exercised his option-out clause after the first year of his multiyear contract. *Id.* Such an arrangement violated the CBA's prohibition on undisclosed agreements. *Id.* As a result, the NBA claimed that Dudley's contract violated Section Four of the CBA which proscribes undisclosed agreements concerning future renegotiations. *Id.*

Because the United States District Court for the District of New Jersey could only reverse the decision of Special Master Clark when the decision was clearly erroneous, Judge Debevoise analyzed the Special Master Clark's decision in detail. *Id.* at 180. Special Master Clark first distinguished the Dudley contract from Albert King's contract in the *Matter of NBA*, 630 F. Supp. 136 (S.D.N.Y. 1986). *Id.* at 178. Special Master Clark opined that in the latter case Albert King received re-labeled payments that were greater than what the salary cap permitted, but Dudley, unlike King, signed a new contract with the Trailblazers, which, in time, may surpass the amount of money Dudley would have received from the Nets. *Id.*

Special Master Clark held that because the NBA previously had approved an option-out clause after two years in a multiyear contract and an year option-out clause after one year in two year contracts, the one year option-out clause for the multiyear contract that Dudley signed with the Trailblazers was not dissimilar such that Dudley's option-out clause constituted a salary cap circumvention. *Id.* Special Master Clark further held that because the Trailblazers would be able to offer Dudley a contract without any salary cap restraints after one year of the multiyear contract, the threat to the salary cap was not any different than if Dudley signed with the Nets. *Id.* As a result, the Special Master decided that the Dudley's contract with the Trailblazers did not violate Section Three of the CBA. *Id.*

Special Master Clark dismissed the NBA's Section Four argument regarding an undisclosed agreement between Dudley and the Trailblazers. *Id.* Special Master Clark's reasoning was that Dudley's desire to be a starting center with a championship caliber team on the West Coast, with a style of play conducive to his talents, and with the one year option-out clause provided Dudley with an opportunity for the Trailblazers to reward him for a productive

season and justified the discrepancy in his first year salary between the multiyear offered by the Trailblazers and the multiyear contract offered by the Nets. *Id.* at 178-79.

Special Master Clark also held that the NBA's argument that Dudley's valuable option-out clause was compensation and, when added to Dudley's base salary, the value of the contract exceeded the salary cap, was groundless. *Id.* 179. Special Master Clark studied the CBA, previous player contracts, and the NBA's prior conduct with respect to option-out clauses and determined that the option-out clause was not compensation. *Id.* at 180. Special Master Clark mentioned that in related cases the Atlanta Hawks and the Chicago Bulls relied on the NBA's acquiescence that the option-out clause conformed to the salary cap, and the Hawks and the Bulls changed their positions in reliance on NBA's acquiescence. *Id.*

Judge Debevoise stated that Special Master Clark's decision relating to which circumstances would present an impermissible salary cap circumvention was the only issue under consideration. *Id.* Judge Debevoise said that Special Master Clark's finding required an evaluation of the evidence presented to Special Master Clark in order to determine whether an agreement to circumvent the salary cap existed between Dudley and the Trailblazers. *Id.* at 181. Judge Debevoise indicated that unless Special Master Clark's findings were clearly erroneous, the court would have to accept the findings. *Id.* at 180.

In evaluating the evidence that the NBA and the NBAPA presented to Special Master Clark, Judge Debevoise said that a high probability existed that Dudley and the Trailblazers would enter into a new contract upon Dudley's exercise of the option-out provision after the first year of the multiyear contract, but that such a probability did not amount to an undisclosed agreement between Dudley and the Trailblazers, the type of which Section Four of the CBA proscribes. *Id.* at 181. As a result, Judge Debevoise accepted Special Master Clark's conclusion. *Id.*

The court noted that Special Master Clark minimized the adverse effects of the option-out clause on the salary cap. *Id.* at 182. Special Master Clark reasoned that if Dudley exercised his option-out clause after the first year of his multiyear contract with the Trailblazers and received a new contract from the team, such a clause would not weaken the salary cap any more than if the Nets offered Dudley a similar option-out clause in its multiyear contract. *Id.* Judge Debevoise reasoned that such an option-out clause after

one year of a multiyear contract may weaken the objective of the salary cap. *Id.* The court also commented that the length of time before a player may exercise an option-out clause in a multiyear contract is important, but Special Master Clark was unable to accept the proposition that a one year option-out clause in a multiyear contract is different so as to constitute a salary cap circumvention than an accepted option-out clause after two years in a multi-year contract or an accepted option-out clause after one year in a two year contract so as to constitute cap circumvention. *Id.* at 182-83.

The court agreed with Special Master Clark's treatment of the theory that "only the future will tell whether taken all together such contracts raise salaries in the long run." *Id.* at 183. Although the court mentioned that the widespread use of option-out clauses in multiyear contracts could have a devastating impact on the salary cap, Judge Debevoise could not reject Special Master Clark's conclusion because such a determination by Special Master Clark was not clearly erroneous. *Id.*

In summation, the United States District Court for the District of New Jersey held that Dudley's option-out clause was within the purview of the CBA. *Id.* at 184. The court also said that the option-out clause was not an agreement "defeating" or "circumventing" the salary cap as set forth Section Three of the CBA. *Id.* The court adopted Special Master Clark's holding by stating that such contracts were within the contemplation of the NBA and the NBAPA as reflected in the CBA. *Id.*

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