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Unionization in Esports

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Introduction

Much has been made of the players need to unionize across esports[1] though there is little understanding of the implications of such a union, and the complexity associated with establishing one. As a preliminary matter, and for purposes of this paper, the term "esports" should be understood to mean the industry that encompasses the competitive playing of video games, including League of Legends ("LoL"), Overwatch, Defense of the Ancients 2 ("DOTA 2"), Super Smash Brothers and many more.[2] Similar to how there are several different sports that comprise the sports industry, there are many different video game titles that make up the esports industry. As it would be impracticable, and possibly illegal, for NFL, MLB, NHL, and NBA players to form one collective union in negotiations against one collective association of their respective leagues, the same can be said for each individual esport. To the extent there will be unionization, it will come within the confines of each individual esport ecosystem.[3]

It remains unclear how wise unionization would be for the players. As unionization implicates antitrust and employment law, and issues arise under these areas of law due to economic circumstance, the economics of esports must be understood at a fundamental level to properly evaluate the wisdom of unionization.

Part 1 of this paper will provide a glimpse into the murky and unclear esports ecosystem, while also shedding light on how other professional sports leagues have approached the problem of inflated player salaries. Part 2 will explore the interactions of a player's union with player salary caps, drafts, and similar restrictive practices. Finally, Part 3 will recommend an approach on a moving forward basis

[1] *See* Pat Evans, *How Players Associations Could Help Improve Esports' Infrastructure*, FRONT OFFICE SPORTS (Mar. 8, 2019), https://www.sportsbusinessdaily.com/Journal/Issues/2018/03/12/Esports/PAs.aspx; *see also* Maddy Myers, *Pro Gamers Are Getting Serious About Unionizing*, KOTAKU (March 14, 2018), https://compete.kotaku.com/pro-gamers-are-getting-serious-about-unionizing-1823770452.

[2] *See* Dictionary.com, https://www.dictionary.com/browse/esports.

[3] *See* Kieran Darcy, *Riot's Players' Association Lays Groundwork for Unionization*, ESPN (June 12, 2017), https://www.espn.com/esports/story/_/id/19617991/riot-players-association-lays-groundwork-unionization.

I. The Esports Ecosystem

In 2019, the esports ecosystem is dominated by the game developers who control the intellectual property around their games including formation of esports leagues, through application of Section 106 of the Copyright Act. One hundred percent of game revenues inure to the benefit of the game developer despite leagues acting as a marketing tool for the games. Game developers control the flow of esports league-wide revenues, which often include media rights deals, league wide sponsorships, ticketing revenues, and other similar sources of revenues. While recently some teams have been successful in bargaining for a share on league-wide revenue, most team revenues continue be sourced from the monetization of their players as influencer assets in the form of sponsorships.[4] Industry reports note that player salaries alone often exceed the revenue of professional esports teams.

> NewZoo analyst Jurre Pannekeet, who sees the revenues for 14 esports teams, says the majority of teams are operating at a loss, but declined to say how much on average, citing nondisclosure agreements. When pressed whether that majority was closer to 51 percent or 90 percent of teams operating at a loss, he said: "If you looked into it, it's probably closer to 89 percent than 50 percent.[5]
>
> Much of that is likely due to players' salaries, which Fields describes as being 'at completely unsustainable levels.' Some reports indicate that North American League of Legends pros earned $105,000 a year on average in 2017. After the league franchised in 2018, the average went up to $320,000. Some players have made closer to a million dollars per year. 'The revenue has not yet equaled what the salaries demand,' Fields said. Esports organizations have to pay those salaries, on top of the $10 to $13 million that they pay to Riot Games to be in the league at all.[6]

ESPN reports that recently teams have paid between $30 and $60 million dollars to participate in the Overwatch League, which is in its

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[4] Cecilia D'Anastasio, *Shady Numbers and Bad Business: Inside the Esports Bubble*, KOTAKU (May 23, 2019), https://kotaku.com/as-esports-grows-experts-fear-its-a-bubble-ready-to-po-1834982843.
[5] *Id.*
[6] *Id.*

second year of operation.[7] The first year of the Overwatch League reportedly averaged 80,000-170,000 concurrent viewers on its English language Twitch broadcast.[8]

With such large costs and uncertain revenues, an estimated 70% to 80% of which come from sponsorships,[9] the highest of which do not exceed a reported $3 million per year,[10] the fact that teams are operating at a loss is hardly surprising. Esports teams are not dissimilar from professional sports teams in this regard and may continue mirroring professional sports teams' path towards monetization and ecosystem stabilization. Professional sports teams have a history of losing money. Prior to the implementation of Financial Fair Play rules in 2013,[11] the preceding five years saw 99% of the English Premier League's revenues consumed by player wage growth.[12] Today, exceeding a 70% wages to ratio threshold subjects any UEFA club to investigation and a requirement for said club to submit "break-even information."[13] Deloitte states: "UEFA's Financial Fair Play Regulations have contributed towards European clubs' much improved financial results and reduced debt situation since 2012." In 2018, the wages to revenue ratio in the English Premier League was a more sustainable 59%.[14]

Similarly, in the 2002-03 NHL season, 73% of all hockey related revenues was paid to players.[15] To combat this the NHL adopted a more stringent salary cap. The National Hockey League formulates its salary cap by projecting the aggregate hockey related revenue of all its member

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[7] Jacob Wolf, *Sources: Overwatch League Expansion Slots Expected to be $30 Million to $60 Million*, ESPN (May 10, 2018), https://www.espn.com/esports/story/_/id/23464637/overwatch-league-expansion-slots-expected-30-60-million.

[8] *See Overwatch League*, TWITCHTRACKER, https://twitchtracker.com/overwatchleague/streams.

[9] *See* Steve Van Sloun, *Esports Franchise Economics*, LOUP VENTURES (Mar. 9, 2018), https://loupventures.com/esports-franchise-economics ("The breakdown of income varies by organization, team, and game. The vast majority of revenue (roughly 70-80%) for esports organizations comes from sponsorships and advertising.").

[10] Wolf, *supra* note 7.

[11] UEFA, the governing European Football body requires clubs to balance their spending with their revenues. In doing so, it restricts clubs from accumulating debt. Teams are permitted to spend up to 5 million Euros more than they per for each assessment period (three years). *See Financial Fair Play: All You Need to Know,* UEFA (June 30, 2015), https://www.uefa.com/community/news/newsid=2064391.html.

[12] *See* Bill Wilson, *Premier League Finances Enter New Era, Says Deloitte*, BBC NEWS (June 2, 2016), https://www.bbc.com/news/business-36412394.

[13] UEFA CLUB LICENSING AND FINANCIAL FAIR PLAY REGULATIONS, art. 62 Break-Even Information (2012), https://www.uefa.com/MultimediaFiles/Download/Tech/uefaorg/General/01/80/54/10/1805410_DOWNLOAD.pdf.

[14] *See Deloitte Annual Review of Football Finance 2019*, DELOITTE (May 2019), https://www2.deloitte.com/content/dam/Deloitte/uk/Documents/sports-business-group/deloitte-uk-annual-review-of-football-finance-2019.pdf.

[15] Jonathan Kotler, Note, *Parallel Unionism in Professional Hockey: Redefining the Nonstatutory Labor Exemption to the Antitrust Laws,* 17 FORDHAM INTELL. PROP. MEDIA & ENT. L.J. 843, 847 (2007).

teams for the following year. It then takes that number and divides it by the number of member teams participating in the league; 50% of this number is equal to the salary cap "Midpoint." NHL teams are prohibited from exceeding 115% of the Midpoint and spending less than 85% of the Midpoint.[16]

Given the success Financial Fair Play Regulations have had on reducing wage expenditure in European soccer, and the salary cap has had in mitigating wage expenditure in the NHL, the economics of the industry may force esports teams to seriously consider the adoption of a similar salary cap model. Though people in the industry have often endorsed the formation of a players' union, such a decision should not be taken lightly. The establishment of a union, and the existence of collective bargaining would necessitate the reality that league owners would immediately attempt to cut their financial expenditures by implementing a salary cap, among other things like a league wide player draft. Before doing so, teams and players should familiarize themselves with the legalities of a salary cap under both anti-trust and labor laws. Players must honestly assess whether unionization is wise in a market where they receive far more revenue than they generate for their employers. That assessment should be colored with an understanding of the benefits of unionization and the relaxation of strict antitrust laws that flow from a collectively bargained relationship.

II. Antitrust Restrictions

A. *History of Antitrust Law*

The history of anti-trust law in sports is a complicated one. The Sherman Antitrust Act of 1890 forbids any "contract . . . or conspiracy, in restraint of trade or commerce." In interpreting this provision, the US Supreme Court has formulated two rules with which to judge whether a particular restraint of trade promotes or hinders competition: the *per se* rule and the rule of reason. The *per se* rule invalidates arrangements that are by nature adverse to competition.[17] Typically actions like price-fixing and group boycotts are subject to the *per se* rule. By contrast, the rule of reason analyzes the reasonableness of a challenged restraint, the aim is to determine whether the restraint is justified by a legitimate business purpose, in its effect and purpose, as well as the availability of less restrictive alternatives and the balance being struck between pro-competitive and anti-competitive effects on the restraint.[18]

In the early 1900's, union actions began to clash with the Sherman Anti-Trust Act. A problem arose when unions, which naturally intend to

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[16] *See Collective Bargaining Agreement*, NHLPA, https://www.nhlpa.com/the-pa/cba.
[17] Standard Oil Co. v. United States, 221 U.S. 1, 65 (1911).
[18] Kieran M. Corcoran, *When Does the Buzzer Sound?: The Nonstatutory Labor Exemption in Professional Sports*, 94 COLUM. L. REV. 1045, 1047–48 (1994).

limit the employer's bargaining power and therefore necessarily fall under the restraint of trade prohibition found in the Sherman Anti-Trust Act, began to organize more aggressively.[19] To satisfy the union lobby, Congress passed both the Clayton Act and the Norris-Laguardia Act. The Clayton Act opined:

> The labor of a human being is not a commodity or article of commerce. Nothing contained in the antitrust laws shall be construed to forbid the existence and operation of labor . . . organizations . . . or to forbid or restrain individual members of such organizations from lawfully carrying out the legitimate objects thereof; nor shall such organizations, or the members thereof, be held or construed to be illegal combinations or conspiracies in restraint of trade, under the antitrust laws.[20]

The statutes provide statutory immunity for union tactics like strikes and boycotts, but do not discuss the collective bargaining agreements unions often reach with management as a result of their organization.

In the 1930s and 40s, Congress passed the National Labor Relations Act and Labor Management Relations Act, each of which sought to promote collective bargaining. The NLRA encouraged self-organization and the process by which workers could designate representatives to negotiate terms and conditions of employment.[21] It states in pertinent part:

> It is hereby declared to be the policy of the United States to eliminate the causes of certain substantial obstructions to the free flow of commerce and to mitigate and eliminate these obstructions when they have occurred by encouraging the practice and procedure of collective bargaining and by protecting the exercise by workers of full freedom of association, self-organization, and designation of representatives of their own choosing,

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[19] *See generally* Allen Bradley Co. v. Local Union No. 3, 159 F.2d 669 (2d Cir. 1947); Allen Bradley Co. v. Local Union No. 3, Int'l Bhd. of Elec. Workers, 325 U.S. 797, 803–06 (1945) (tracing the struggle between the congressional attempt to protect rights of labor to organize and judicial aim of preserving competitive business economy through Sherman, Clayton, and Norris-LaGuardia Acts).

[20] 15 U.S.C. § 17 (1914).

[21] 29 U.S.C. § 151 (1947) ("The inequality of bargaining power between employees who do not possess full freedom of association or actual liberty of contract, and employers who are organized in the corporate or other forms of ownership association substantially burdens and affects the flow of commerce[.]").

> for the purpose of negotiating the terms and conditions of their employment or other mutual aid or protection.[22]

In order to give meaning to this declaration of policy without running afoul of the Sherman Anti-Trust Act, courts have recognized what has come to be known as a nonstatutory "labor exemption."[23] In *Amalgamated Meat Cutters v. Jewel Tea Co.,* the Supreme Court stated that "union-employer agreements" are beyond the reach of the Sherman Act. The rule created by *Jewel* suggests that legitimate employee concerns outweigh anticompetitive practices to parties within the bargaining relationship, even if the bargaining yields practices which would otherwise be violative of the Sherman Act.

Since the nature of collective bargaining suggests that workers may end up striking a deal that inhibits their interests, the nonstatutory labor exemption has been used by employers as a shield against anti-trust criticisms surfaced by employees who are unhappy with the results of the bargaining. In the context of professional sports, the nonstatutory labor exemption has been used to defend the imposition of (1) a mandatory, multi-employer imposed fixed individual salary of $1000 per week for all NFL development players,[24] (2) a maximum salary limitation in the form of a salary cap[25], and (3) a college draft, among other things,[26] from antitrust attacks.[27] The standard to meet for the nonstatutory exemption is relatively straight forward and easily attainable within the context of a collectively bargained deal with a labor union.

> First, the labor policy favoring collective bargaining may potentially be given pre-eminence over the antitrust laws where the restraint on trade primarily affects only the parties to the collective bargaining relationship. Second, federal labor policy is implicated sufficiently to prevail only where the agreement sought to be exempted concerns a mandatory subject of collective bargaining. Finally, the policy favoring collective bargaining is furthered to the degree necessary to override the antitrust laws only where the agreement sought to be exempted is the product of bona fide arm's-length bargaining.[28]

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[22] *Id*.

[23] Amalgamated Meat Cutters & Butcher Workmen v. Jewel Tea Co., 381 U.S. 676, 682 (1965).

[24] *See* Brown v. Pro Football, 518 U.S. 231 (1996).

[25] *See* Wood v. Nat'l Basketball Ass'n., 602 F. Supp. 525 (S.D.N.Y. 1984).

[26] *Id.*

[27] *See generally Amalgamated Meat Cutters*, 381 U.S. 676.

[28] Mackey v. Nat'l Football League, 543 F.2d 606, 614–15 (8th Cir. 1976) (internal citations omitted).

In 1995, the Supreme Court of the United States affirmed the DC Circuit Court of Appeals decision which upheld the imposition of a fixed $1000 per week development squad salary on the nonstatutory labor exemption's grounds. The Court of Appeals noted in pertinent part:

> [W]e believe that employees, like all other economic actors, must make choices. If they choose to avail themselves of the advantages of the collective bargaining process, their protections are as defined by the federal labor laws. The system established by those statutes offers employees many benefits: recognition of organized workers as a bargaining unit, thereby giving them bargaining strength; establishment of mandatory subjects of bargaining; protection of the right to strike; allowance for the possibility of negotiated grievance procedures and pooled benefit plans; and judicial enforcement of collective bargaining agreements. Further, it establishes a significant list of employer actions that, if taken, constitute unfair labor practices for which employees and unions may seek redress before the NLRB.[29]

B. Antitrust Law Applied to Esports

Applied to esports there is clearly a choice that players can make. Should they choose to avail themselves of the benefits afforded to NLRB recognized unions, they would gain the benefit of additional bargaining strength, protection of the right to strike, and numerous other statutory rights. They would also open themselves up to the possibility of a collectively bargained salary cap, which would reduce earnings for esports players. Alternatively, the players can refuse to avail themselves of the benefits of unionization, and thus deny teams the nonstatutory labor exemption's protection.

Up until now this has been the choice, either wittingly or unwittingly, of the players. Nevertheless, it is worth noting that several notable esports figures have pushed for the unionization of players in specific esport titles.[30] Such an approach is not necessarily improper; as suggested above this is a calculation that employees must make. Inherent in the calculation is the thought that continuous losses suffered

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[29] Brown v. Pro Football, 50 F.3d 1041, 1057.

[30] *See* Ryan Morrison, *Future of Esports Players Unions*, ROBOT CONGRESS EPISODE 72 (May 8, 2018), https://open.spotify.com/episode/2QRwje2t0OEb7mehDRdzhp?si=NetyaTdpSNWXDQr6sfxhSw (Ryan Morrison advocating for a union collectively bargaining on behalf of the overwatch league players); Scott Smith (@SirScoots), TWITTER (June 26, 2015), https://twitter.com/SirScoots/status/614424193015222272 (Sir Scoots advocating for a CS:GO Player Union).

by the industry is not a sustainable solution and may lead to the unilateral imposition of a salary cap without employee consent. Given the unique three-party structure of esports, one that sees revenue and governance split between league operators (who may double as the game developer), teams, and players, the imposition of a salary cap need not even come directly from the team owners. A leaked Overwatch League Memorandum revealed the possible existence of a competitive balance tax in the Overwatch League[31], and while such a cap has never been confirmed, its possible existence raises interesting questions as to whether league organizers would unilaterally seek to protect the health of the leagues by imposing such a soft cap. While such an action may lead to a lawsuit, it would not be unfounded and may ultimately be permitted on an anti-trust basis, by the rule of reason.

In 1994 a District Court in the Southern District of New York stated in dictum:

> Even under a rule of reason analysis, however, it appears that the Players have failed to show that the alleged restraints of trade are on balance unreasonably anti-competitive. The pro-competitive effects of these practices, in particular the maintenance of competitive balance, may outweigh their restrictive consequences. Indeed, the Salary Cap seems to operate as a mechanism to distribute 53 per cent defined gross revenue to the Players.[32]

Ultimately the District Court's decision was determined on labor grounds after appeal to the Second Circuit Court of Appeals.[33]

In 1976 the Eight Circuit Court of Appeals reviewed what was then known as the "Rozelle Rule", a rule which was unilaterally implemented in 1963, and provided that when a player's contractual obligation to a team expired and he signed with a different club, the signing club was obligated to compensate the player's former team. The court ultimately found that because the Rozelle Rule originated before the existence of a collectively bargained agreement, it was not the result of bona fide bargaining and thus not shielded by the nonstatutory labor exemption.

The inquiry then turned on whether the Rozelle Rule was shielded by the rule of reason. While ultimately the *Mackey* court found that the restraint was unacceptable due to its numerous anticompetitive effects, which were "significantly more restrictive than necessary", the court

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[31] *See* Richard Lewis, *Leaked Overwatch League memo drastically shifts housing requirements, confirms "luxury tax"*, DEXTERO (Aug. 7, 2019, 9:14 PM), https://www.dexerto.com/overwatch/overwatch-league-leak-housing-requirements-luxury-tax-888650.

[32] Nat'l Basketball Ass'n V. Williams, 857 F.Supp. 1069, 1079 (S.D.N.Y. 1994).

[33] *See* Nat'l Basketball Ass'n v. Williams, 45 F.3d 684 (2d Cir. 1995).

noted that the NFL had a "strong and unique interest in maintaining competitive balance among its teams."[34] Such an analysis may be even more pervasive in the esports industry, an industry where 70% of revenues are derived from sponsorships and where league operators represent another party with whom league revenues must be split.

Absent regulation to the contrary, top teams may continue to tighten their grip on the sponsorship market as their high match viewership represents value to sponsors. The European Premier League tells us that sponsors often flock to teams that demonstrate a history of competitive excellence.[35] "Clubs are in fierce competition when it comes to commercial deals, as they tend to be sold on a club-by-club basis. This model may seem advantageous for certain clubs as it provides an opportunity to obtain a competitive advantage over other teams."[36] While those teams may be able to better afford high player wages, in order to maintain competitive league balance less well-known teams have been forced to aggressively raise capital to afford players of a high competitive caliber. Without a return on investment, a trend of rising player costs, and an additional stakeholder to share league revenues with, the sustainability of the esports team model for all but a few teams has been called into question, and some have speculated that the industry may experience a significant market correction whereupon there is a consolidation of teams and thus less players employed in the industry.

Maintenance of the overall health of the industry provides a compelling argument for the imposition of a salary cap on antitrust rule of reason grounds, even absent the existence of a collectively bargained agreement. While this reasoning was ultimately shot down on factual grounds in *Mackey,* the esports industry, and the market forces at play, may provide a compelling enough reason to swing the balancing test in favor of the teams, provided such a cap were instituted on the least restrictive grounds possible.

III. Next Steps

The structure of the esports industry provides unique challenges toward maintaining its economic stability. Players and teams must be

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[34] *Mackey*, 543 F.2d at 621–22.

[35] DELOITTE, *supra* note 14, at Chart 8 Premier League and Championship clubs' average revenues (In 2017/18 40% of a UCL club's revenue was generated from commercial sources (primarily sponsorships, whereas only 25% of a UEL team's revenues were generated from commercial sources, and only 13% of other premier league team's revenues were generated from commercial sources. Here UCL teams comprised Chelsea, Liverpool, Manchester City, Manchester United and Tottenham Hotspur, and UEL teams comprised Arsenal and Everton. In the history of the English Premier League, only six (6) teams have won the league championship title (Manchester United, Chelsea, Manchester City, Arsenal, Blackburn Rovers, and Leicester City).).

[36] *Id.* at 23.

cognizant of the challenges that they face in years to come. This necessarily includes market realities which will impact the long-term viability of the industry. As a matter of first concern, players should immediately begin taking steps towards familiarizing themselves with team economics. Losing money in perpetuity is not a viable path toward success and it should not be assumed that this is a market condition which teams, and their investors, are prepared to live with forever.

After this has been done, players will need to make a calculated decision about whether they should get out in front of a potential salary cap by organizing and beginning the collective bargaining process. Players must weigh what they would gain in the form of a more standardized player contract with agreeable uniform terms and other benefits against the status quo, which can be attained by standing idly by whilst market competition prolongs player wage inflation and in turn necessitates potential league operator intervention or a consolidation of industry competition. It should be noted that consolidation of industry competition will result in fewer jobs.

There is also the issue of game developer power, a separate yet equally important topic of consideration for players. While Riot Games has taken initial steps towards erecting a fully functional players association, executives within professional sports have wondered aloud whether Riot's funding of the association presents an apparent conflict of interest.[37] The concept that league organizers might attempt to cull player-team coordination is not a new one. This question was explored by Bryce Blum and Stephen Fisher in a March 2014 Foster Pepper White Paper.

The formation of a LoL Players Association is significantly more complex than in other sports, primarily because three parties would need to be involved in the bargaining process. The players and teams sign two sets of contracts – one with each other and the other with Riot. The two primary bargaining topics within professional sports leagues are similarly split: player-team contracts govern the majority of the terms and conditions of employment, while the LCS rules and the contracts signed with Riot control the means of allocating players and restricting their mobility. This complexity would not prevent the three parties from engaging in formal collective bargaining; however, the precise structure and nature of the bargaining would need to be carefully considered.[38]

While much is made of the relationship between teams and players, and league operators and teams, very little is ever made of the

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[37] Darcy, *supra* note 3, (Paul Kelly, former executive director of the National Hockey League Players' Association: "Obviously there is certainly the potential for conflict of interest, and the potential for [Riot] to assert control over the players through [the association] if they're the primary or only funding source.").

[38] *See* Foster Garvey, https://www.slideshare.net/slideshow/embed_code/key/Moo4dR8qWoO52p (exploring whether teams and players should negotiate against Riot) (last visited Oct. 10, 2019).

relationship between league operators and players. Teams are seen as a pass-through entity by which league operators impose contractual terms, and reap some benefits of league monetization, including by way of merchandising, media rights, and league wide sponsorships. In the path toward a more stable ecosystem, teams and players, though traditionally adversaries in professional sports, find themselves aligned in significant ways as their continued existence and financial stability results directly from the success, and available revenue streams, of the league.

To be clear, this note does not advocate for the unionization of players in esports; its purpose is to bring awareness to the economic issues presently facing the esports industry and to discuss possible ways to resolve these issues. At some point in the not-too-distant future, the status quo will cease to be a viable option. At that inflection point players will be faced with a choice. They should fully understand the consequences and economic realities associated with that choice.

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