

# Does revenue growth make football's financial regulation obsolete?

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Play the Game 2017 in Eindhoven

- **Team production, role of the monitor, governing body**
- **Sources of financial means**
- **Financial regulation**
- **Revenue growth – skipped**
- **Conclusion**

# Team production in sports

- **Single team:** goal keeper, forward, ..., coach, administration staff, CEO cannot produce or sell anything
- Two teams playing a single match: can be sold, little revenue potential
- Championship or cup competition: added value through interrelation/interdependence of all matches
- **European club competitions: access via rank in national competition**
- History of lots of seasons of former championships
  - Real Madrid 12-fold cup winner
- **European hierarchical pyramidal structure**
  - **only interrelation of all matches creates added value**
  - **but requires monitoring of participating clubs**

# Requirements for attractive team sports

- Audiences want to face fair play
- Quality criteria of sporting competitions are
- - **suspense and uncertainty of outcome**  
→ competitive balance
  - **integrity and credibility**  
→ no forbidden means to improve performance (athlets)  
→ not too uneven financial resources to compete with  
→ to comply with regulation

**whose task is to preserve quality?**

\* E. Franck: *Die ökonomischen Institutionen der Teamsportindustrie* (1995),  
*Zur Organisation von Sportligen* (1999)

# Tasks of the competition's governing body

- to monitor participants
  - to curb shirking, rule-breaking or circumventing
  - to determine the distribution of centrally marketed revenues
  - to draft, refine and enforce regulation
  - thus protecting integrity, reputation and brand
- to organize (fixtures, referees, disciplinary bodies)
- to sell rights and other items
- to provide services (lobbying, public affairs, technological support/advice referring to artificial turf, hawk eye, ...)

Governing body can be interpreted as a **cooperative organization**

→ democratic voting, clubs are the principals, commissioner is agent

# Decision making by UEFA

- UEFA is the association of 54 national associations in/ near Europe
- Setting rules cannot be simply imposed top down by the Executive Committee (17 members) and UEFA administration; headed by the General Secretary

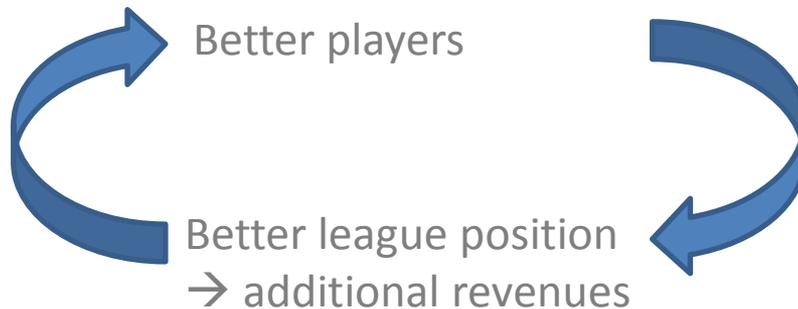
but requires intense and complex bottom up consultation processes involving members and stakeholders such as

- national associations and their representatives
- clubs (represented by ECA)
- leagues (EPFL)
- players (FIFRO)
- all gathered in the **Professional Football Strategy Council**

→ **intransparent/unobvious decision making**

# Financial resource determine playing strength

- Labor market in team sports works well:
  - talent/ ability can be easliy observed, performance related salaries
- Global sourcing of playsers possible since Bosman 1995
- Path dependent competitionn in team sports\*



- $\emptyset$ -player salaries **Top 6-Cluster 94 Mio €**, **third cluster only 37 Mio €\*\***

\* S. Rottenberg *The Baseball Players' Labor Market* (1956)

\*\* Saison 2015/16 laut DFL-Report 2017, S. 31

# Three main sources of clubs' financial means

- **income by nature**



relative level of starting conditions

- size of local market; derived: size stadium
- history, trophies, heroes of the past
- number of seasons in top-flight league

- **income by success**



path dependency in leagues

- consumers' preferences for excellence\*
- additional revenues depending on rank
- distribution of centrally marketed revenues

- **cash injections**



benefactors and owners

- via balance sheet, not via p&l account
- financing losses or heavy investment
- long-term planning security

\* S. Rosen *The Economics of Superstars* (1981)

# Quite distinct financial resources

schematic

Example Bundesliga



Bayern  
Dortmund



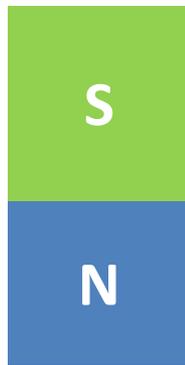
Leverkusen  
Wolfsburg



Köln  
Hamburg, Stuttgart



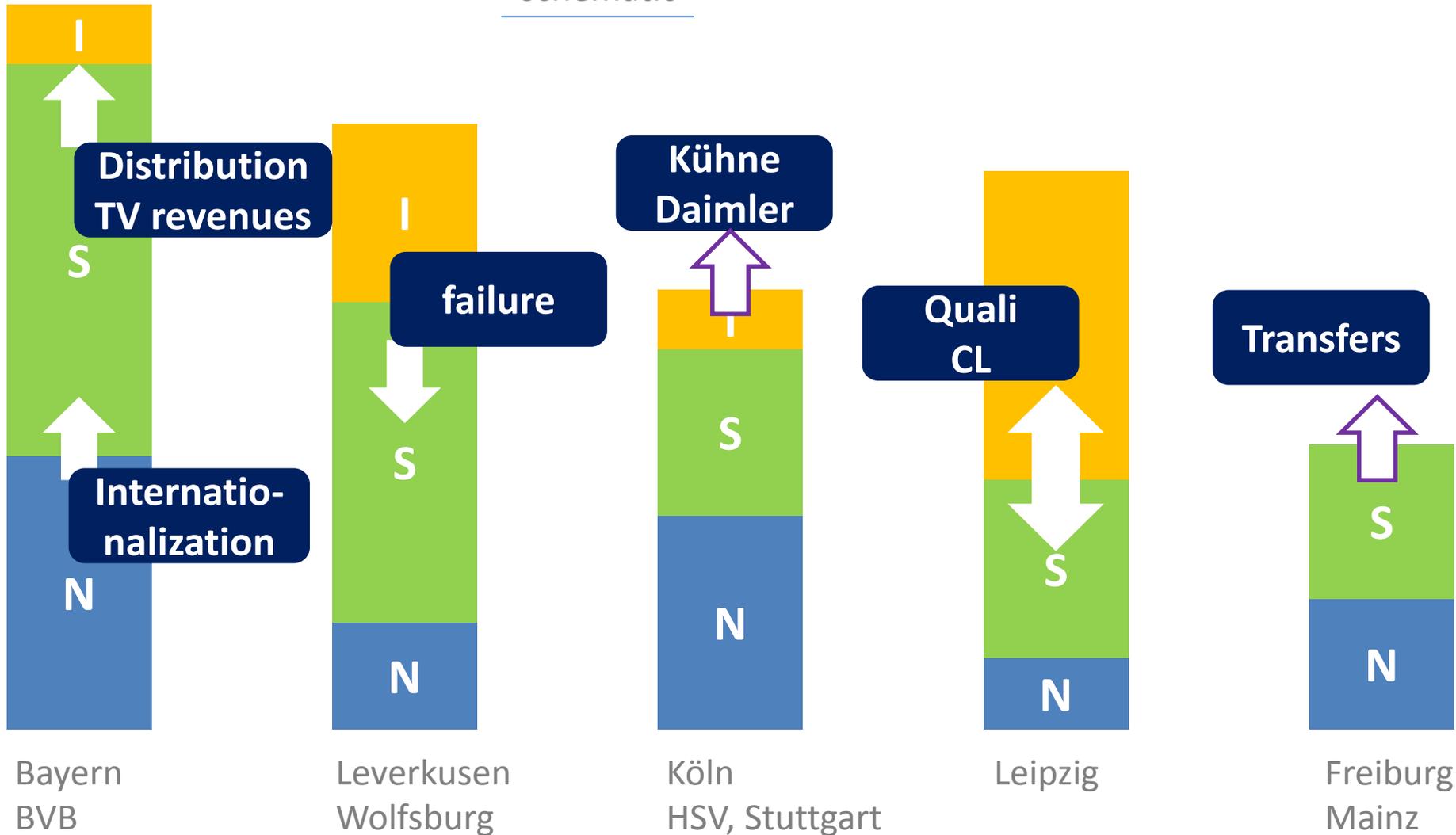
Leipzig



Freiburg  
Mainz

# Financial resources change over time

schematic



# Financial regulation

- Financial requirements established in licensing systems
- At European level: UEFA's Fair Play Regulation  
- break-even requirement
- At national level:  
Germany: ownership regulation via 50+1 rule

**→ need for regulation?**

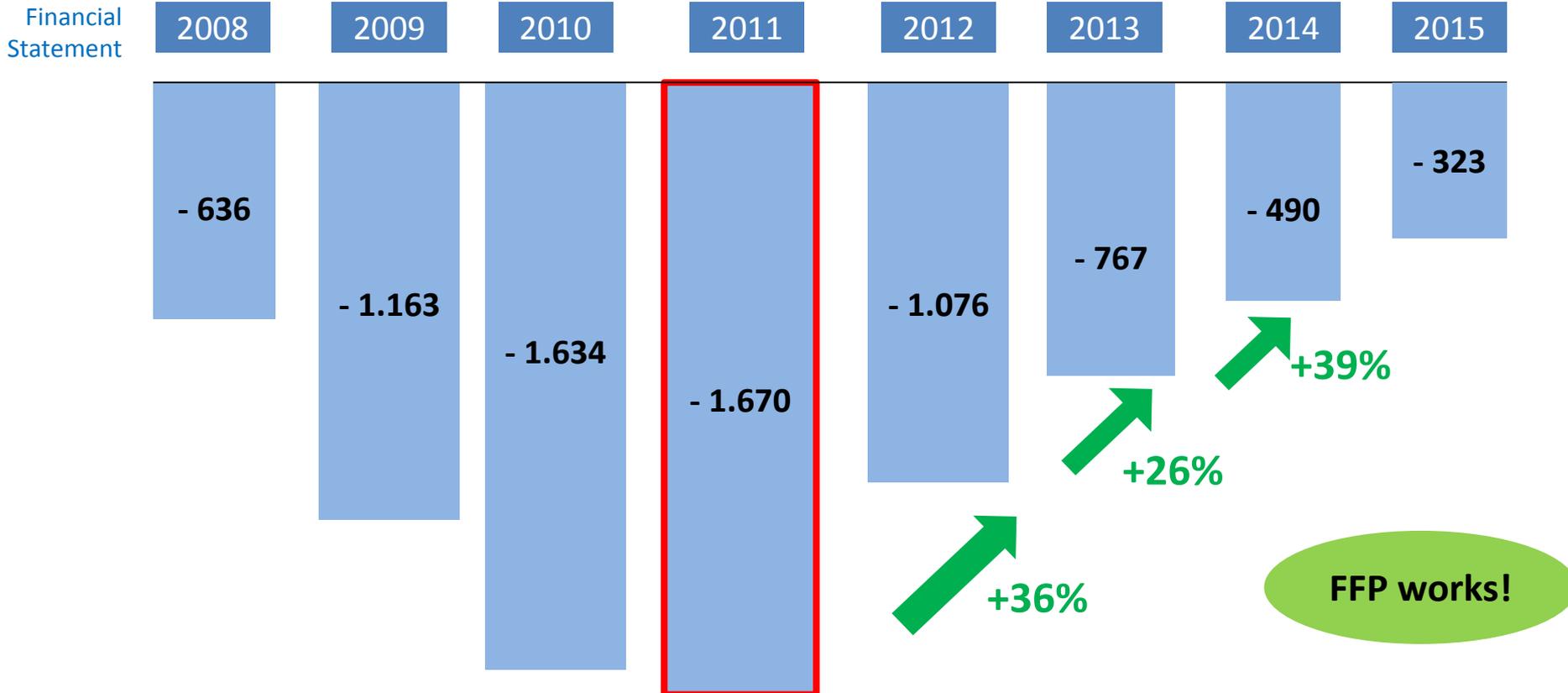
# Poor financial performance in 2011

Number of clubs exhibiting a profit/ a loss amounting to ... % of total revenues in 2011

Big Five Leagues	Profitable clubs			Unprofitable clubs			Σ Clubs
	> 20%	> 10%	positiv	< -10%	< -20%	> -20%	
Premier League	3	-	5	3	2	7	20
Bundesliga	-	2	10	6	-	-	18
Primera Division	2	-	6	3	2	7	20
Serie A	-	3	4	5	2	6	20
Ligue 1	-	-	10	7	2	1	20
Total	5	5	35	24	8	21	98
	45			53			

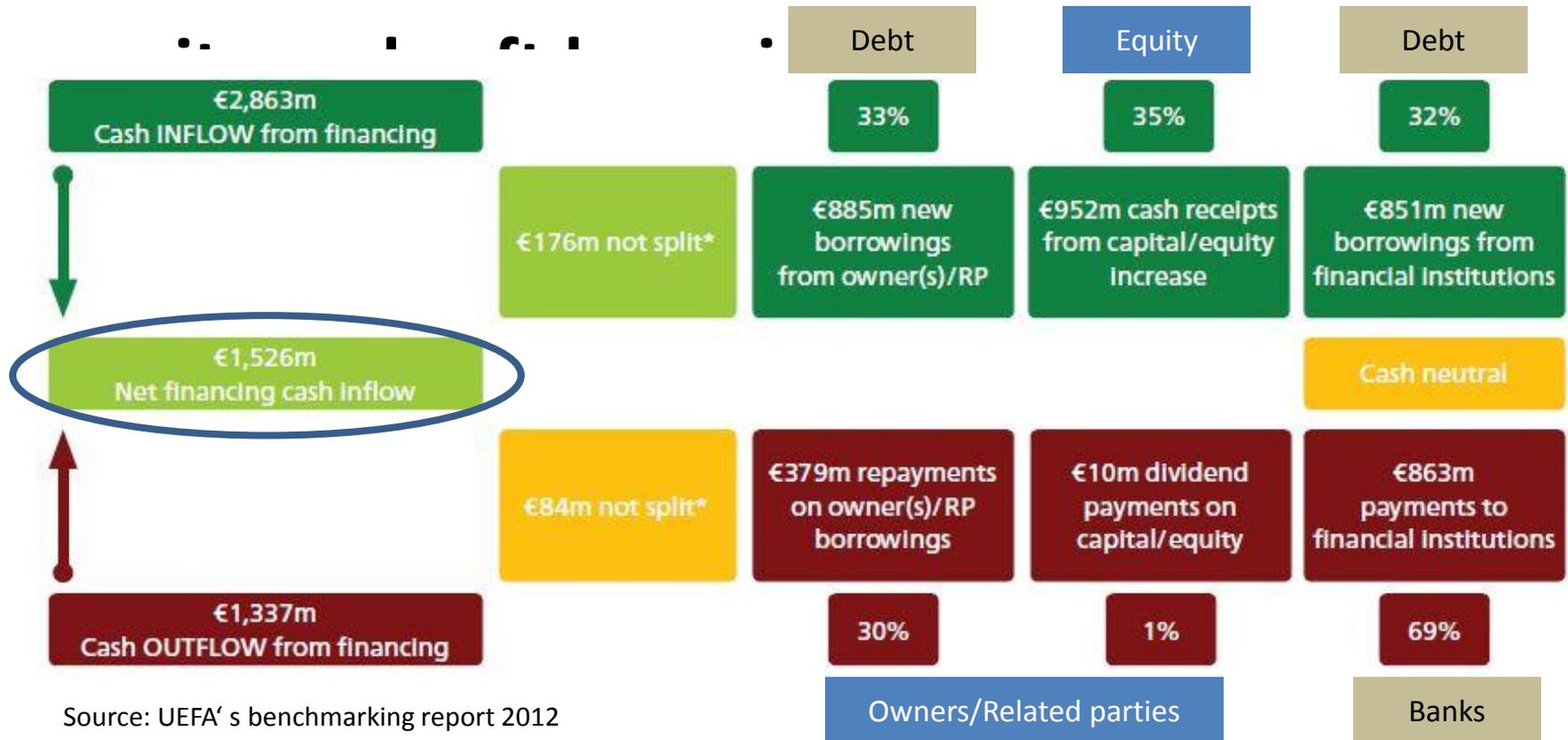
# Top-flight clubs persistently are loss-makers

## Aggregated financial results of all 734 European top-flight clubs in million €



Source: UEFA' s benchmarking reports of the respective years

# Owners keep the system running with



# Softening of financial regulation

## only perceived or actually?

- **Germany' s 50+1 clause**
  - „lax“ enforcement policy  
(TSG Hoffenheim: against the spirit, not the letter of the rule)
  - „damburst“ RB: non-persecuted obvious abuse of the legal form e.V.
  - speculation about abolition
  
- **UEFA' s FFP after its revision in 2015**
  - publicly known transfer fees and player salaries (ManCity, PSG, ...)
  - geographical origin of sanctioned clubs (Turkey, Italy, Russia)
  - *mitigating factors* addressed to clubs in Eastern Europe
  - *settlement agreements* addressed to heavy loss-makers
  - *voluntary agreements* submitted by newly acquired clubs (Annex XII)

# Further problems with financial regulation

- Questionable „fair market value“ transactions with related parties

→ how to assess in a legally robust way?

- Dual/ multiple Ownership jeopardizing the integrity of competition

- Red Bull clubs

- Premier League

close ties between two billionaires Usmanov (FC Arsenal)  
and Moshiri (FC Everton) laid bare in leaked files

→ how to safeguard independent club ownership?

## After all: my message

- Even distribution of financial means determines **suspense** of competition
- Degree of compliance with regulation determines **integrity** of competition
- Regulation and distribution scheme are governing bodies' **control levers**
- Observed tendency to a more uneven distribution of centrally marketed revenues rewarding sporting merit and market size
- Paralleled by fading enforcement power with regard to financial regulation
- Persistent revenue growth and improved financial results of the clubs should not distract governing bodies from their original commitments

 **distribution of money and regulation seem to require a review**

# Back up

## What fuels the race?

### Clubs' incentives to overinvest are enhanced by

- ▶ jackpots like Champions League qualification or preventing relegation
- ▶ a stronger relation between talent investments and sporting performance/winning probability
- ▶ increasing revenue differentials
- ▶ a decline in the even sharing of centrally marketed revenues (less revenue sharing)
- ▶ a system of promotion and relegation
- ▶ an increasing revenue gap between first and second division of domestic championship

## Particular appeal of residual control

### Owners are indirectly rent seeking by

- exploiting the club
- using it as a vehicle for other objectives
- gaining access to specific assets or transactions
- benefiting from public attention, interest and recognition
- simply enjoying autonomous decision making

this kind of rents determines the readiness and willingness to pay for a majority stake in a club/ to acquire a controlling interest

## Sugar daddies are not altruistic

**Wealthy individuals with full residual control are pursuing individual goals, so their willingness to pay for their toy results from**

- spill overs to other businesses
- aspiring for social and political recognition
- just enjoying the pleasure to consume a luxurious, glamorous and positional good
- feeling satisfaction derived from winning
- money laundry (?)

## League arrangements to dampen the race

- ▶ Revenue Sharing/Redistribution of income (includes luxury taxes or draft procedures)
- ▶ Input rationing by salary caps or squad size limits
- ▶ Licensing and regulation of ownership structure
- ▶ Increasing the impact of randomness by amending the competition format (play offs; elimination of group stages or seedings)

## Football has established self-regulation because

- overspending is pathologic and peculiar to team sports
- thus there is an obvious need for action
- emergence of the institutional setting of leagues
- notably financial regulation

- Financial Regulation by the monitor
  - what for
  - what it is
  - it is safeguarding the integrity of competition, allowing or prohibiting financial funding by owners and it is governing/piloting/steering each club's share of centrally marketed revenues (media, commercial, ...)

- Three main sources of clubs' financial means

- Two trends:
  - erosion of Financial Regulation and increasing bias/inclination of (non-equally) distributing money
  - examples (anecdotal evidence)
  - reasons
  - tremendous growth: media income, to access overseas markets, potentials of digitalization

1. Conclusion: no reason to believe that more than a few clubs won't overinvest any more: it follows that bodies governing leagues and associations should not neglect/disregard financial regulation, especially exorbitant owner funding trusting (overreliance on to rely on) in endless growth of football revenues and should find back to a more equally evenly distribution of centrally marketed money