

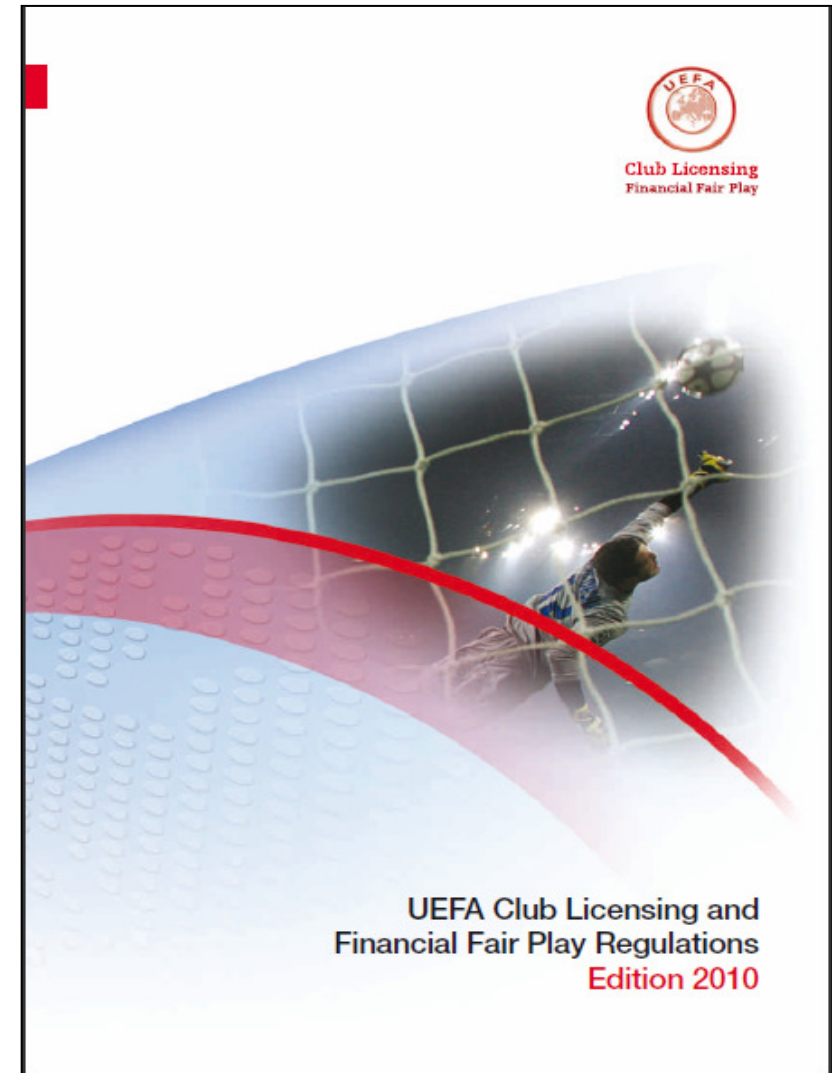
Financial Fair Play – need for regulation off the pitch

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**11th International Hamburg Symposium „Sport and Economics“
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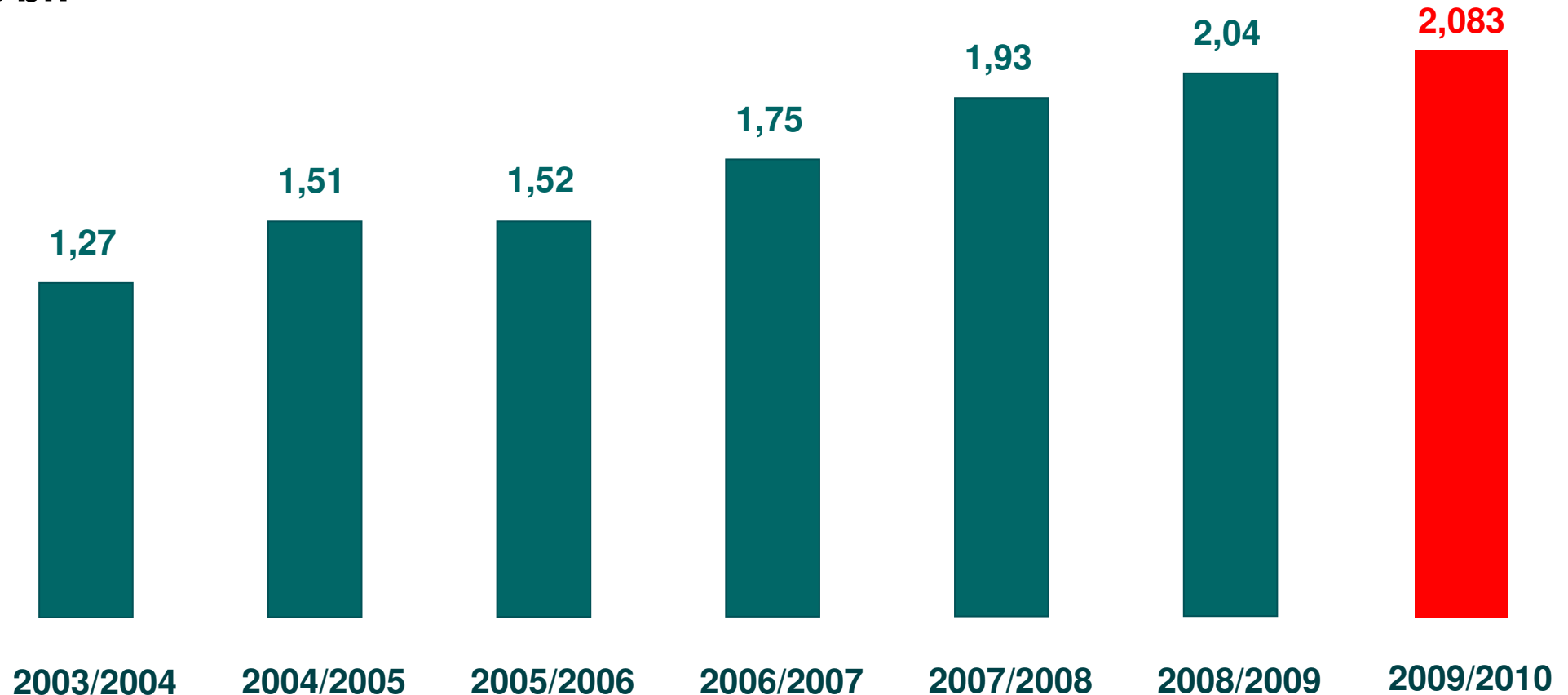
Agenda

- Look at the figures: Need for action
- Financial Fair Play: what it is about
- Impacts and conclusion



Football enjoying continuous revenue growth

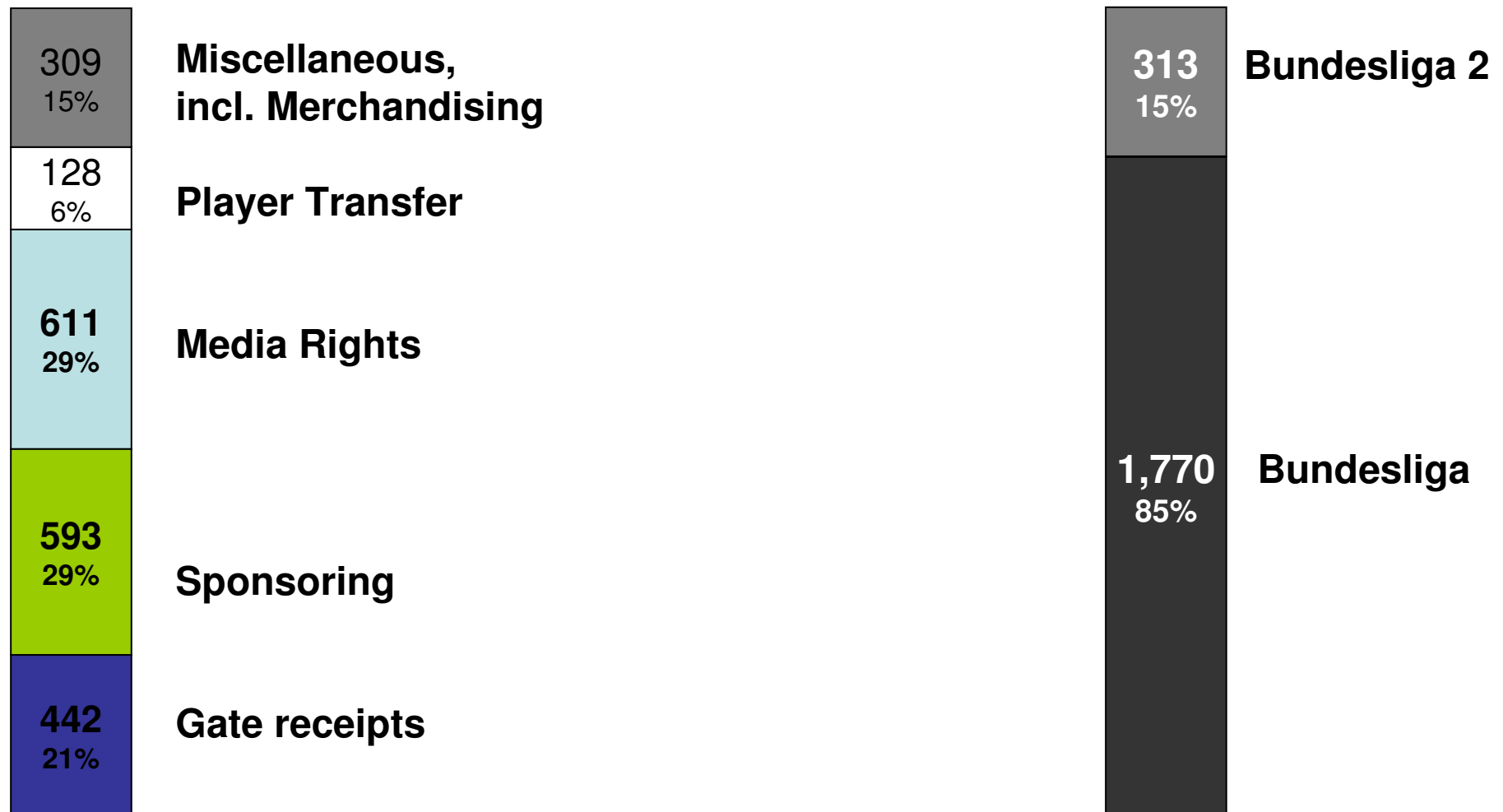
Total Revenues of all 36 clubs playing Bundesliga and Bundesliga 2
€ bn



... with a well balanced revenue mix

Season 2009/10

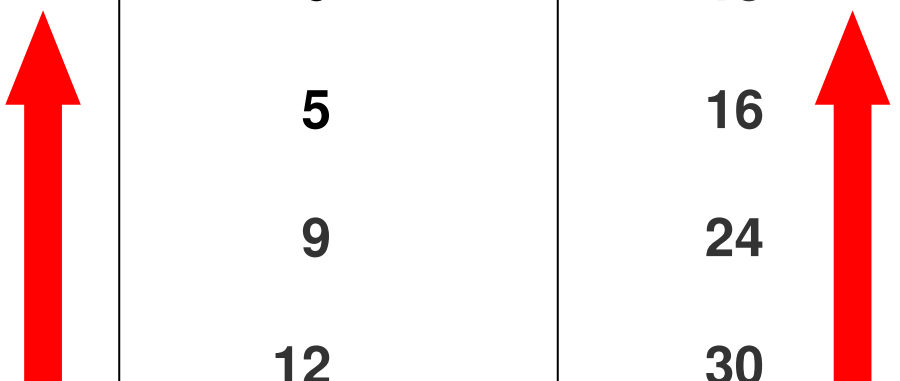
€ 2.083 m revenues split up to



... but declining number of profitable clubs

Members of Ligaverband disclosing after-tax profits

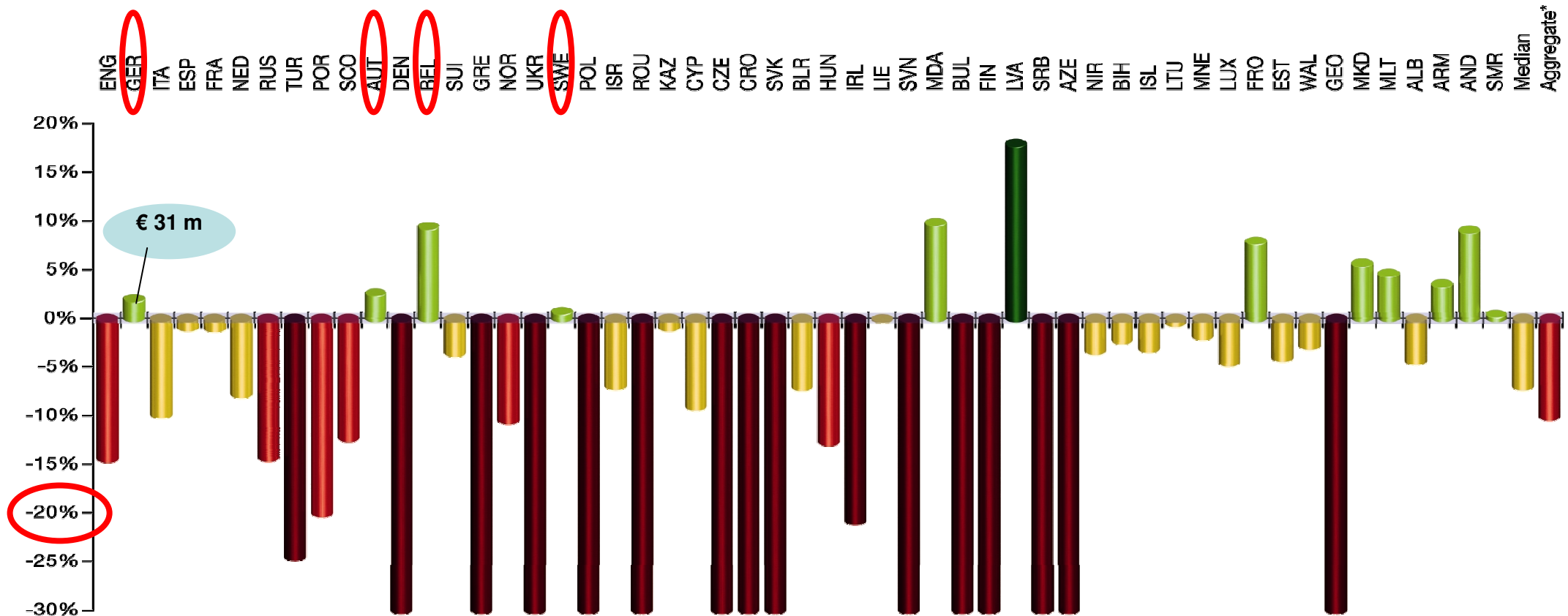
	Bundesliga	2. Bundesliga	out of 36
2009/10 Season	7	6	13
2008/09 Season	11	5	16
2007/08 Season	15	9	24
2006/07 Season	18	12	30
2005/06 Season	12	9	21



4 of the 30 largest leagues with positive aggregate result

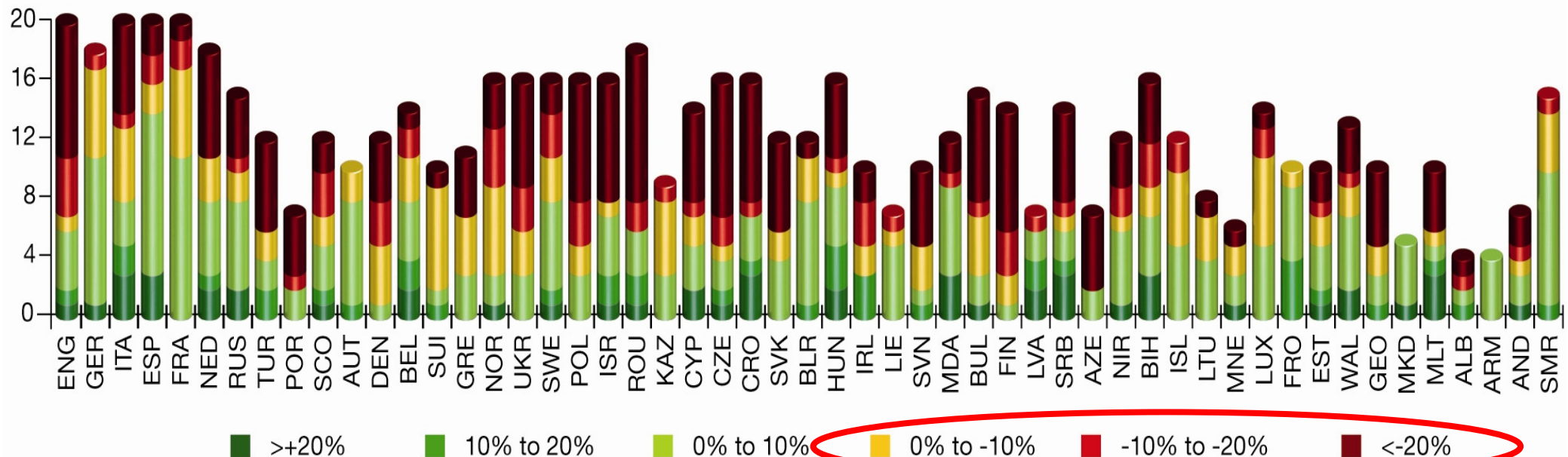
P&L statements 2009

Losses in % of revenues



Top division clubs reporting net losses of € 1,179 m

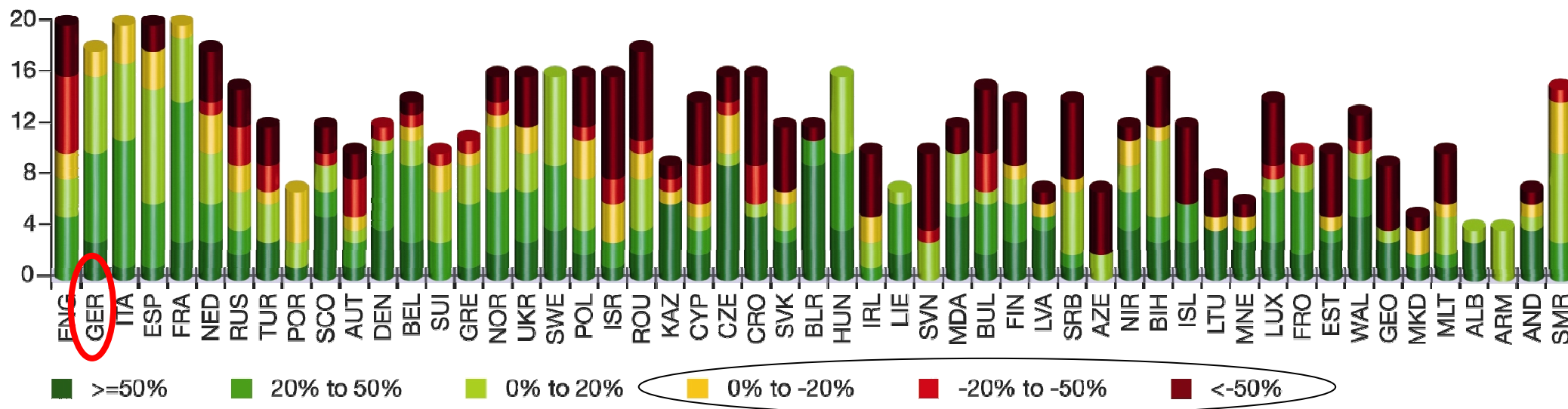
P&L statements 2009



- € 436 m profits incorporated, **85% increase in net losses from 2008**
- **56% of all clubs disclosing losses which amount to € 1,615 m**
- **Half of them (=186) with significant losses (< - 20% of revenues)**
- Wages exceed revenues in 73 Clubs
- **20 clubs reporting net losses of € 875m**

Poor equity situation reflecting continuous losses

Equity ratio of Top flight clubs 2009



- 245 clubs (37%) exhibiting negative equity in 2009
- 180 Clubs with negative equity reporting losses in 2009, including **19 out of the 68 largest revenue clubs**

- 53% of the clubs experiencing a deterioration of its equity in 2009
- 21% of the clubs with no clean audit opinion (going concern or other matter qualification or adverse opinion)

Explanation: The metaphor of the rat race

Participants compete for a prize (a piece of cheese), which grows under-proportionally or not at all in relation to an increase of the input (speed):

“In the rat race the chances of getting the cheese increase with the speed of the rat, although no additional cheese is produced.” (Akerlof 1976)

Instead of increasing the value of output that can be earned back in the market, the additional resources deployed are “wasted”, in extreme cases even completely.

Aiming at raising the probability of winning rank-related extra prizes, clubs face strong incentives to increase their playing strength by heavy investment in talent. As their competitors encounter similar incentives, escalating bidding for talent with spiralling costs emerge since no team can improve its position in the league table without worsening the position of other teams.

As a result, additional effort by contestants will not be rewarded, despite the fact that it has been carefully considered within the framework of maximizing individual objectives.

What fuels the race?

Clubs' incentives to overinvest are boosted by

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

Institutional arrangements to dampen rat races

- ▶ Revenue sharing after central marketing of media rights or redistribution of income; allocation of marketing rights to the league; luxury taxes and draft procedures in North America
- ▶ Input rationing by salary caps, squad size limits or **limitation of cash injections by owners**
- ▶ Internal regulation of clubs' financial behaviour and ownership structure (**Licensing, 50+1 clause, Financial Fair Play, 50+1**)
- ▶ Increase of noise/randomness in competition format through play offs, group stages, seedings

Objectives of Financial Fair Play are

1. to preserve the long-term viability and sustainability of European club football
2. to improve the financial stability of professional clubs by introducing more discipline and rationality
3. to retain brand image, appeal and attractiveness of UEFA's club competitions

The concept consists of two main guidelines:

- **clubs operate on the basis of their own revenues, i.e. live within their means**
- **clubs settle their liabilities with players, social/tax authorities and other clubs punctually**

thereby

- **curbing excessive salary and transfer payments**
- **better protecting professional football clubs' creditors**
- **limiting the level of debt at professional football clubs**
- **promoting investment in youth development and infrastructure**
- **limiting the addiction of individual clubs to „sugar daddies“**
- **limiting the influence of investors, lenders or benefactors on on-field competition**

Bundesliga regulation tops UEFA's financial requirements

Examination of Financial ability following „Lizenzierungsordnung“

**Ligaverband
through DFL**

DFB

**All License
applicants for
Bundesliga
Bundesliga 2
3. Liga**

- k.o.-criterium to prove positive liquidity as of 30.6.t+1
- DFL's discretion to amend budgeted figures (principle of prudence)
- confirmation of Financial ability in autumn
- obligation to increase equity
- obligation to meet budgeted figures
- 50+1-clause

Financial criteria following Club Licensing Regulation 2008

**National
Licensor**

**Clubs
participating
in UEFA's
competitions**

**Audited
Financial
Statement**

**Interim
Financial
Statement**

**No overdue payables as of 31.12.t-1
towards clubs or employees
not settled until 31.3.t**

License decision

Diversity of legal entities in Germany

Member associations (e.V.)

Hamburger SV
Schalke 04
VfB Stuttgart
1. FC Nürnberg
1. FC Kaiserslautern
SC Freiburg
FSV Mainz 05
(FC St. Pauli)

Companies

FC Bayern München AG
(Eintracht Frankfurt AG)
Borussia Mönchengladbach GmbH
TSG Hoffenheim GmbH
Bayer Leverkusen GmbH
VfL Wolfsburg GmbH
1. FC Köln KGaA
Werder Bremen KGaA
Hannover 96 KGaA
Borussia Dortmund KGaA
Hertha BSC Berlin KGaA
FC Augsburg KGaA

Scope of application

UEFA Club licensing

- In the meantime almost all license applicants for top flight leagues

732

UEFA Club monitoring

- All licensees qualifying for UEFA club competitions

236

New rules fight financial foul and financial doping

Fair Play on top of club licensing

**National
Licensor
and CFCP**

**Licensees
qualifying for
UEFA
competitions
Clubs**

Break even rule

**Enhanced overdue payables
as of 31.12. 30.06. and 30.09.**

Monitoring/ ongoing examination

Financial criteria following Club Licensing Regulation 2008

**National
Licensor**

**All license
applicants**

**Audited
Financial
Statement**

**Interim
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**No overdue payables as 31.12.t-1
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License decision

Notion of “Relevance” in P&L statement

RELEVANT EXPENSES

- Cost of Sales
- Employee benefits expenses
- Other operating expenses
- Player transfer amortisation or expense
- Finance costs

- Related party transactions below fair value - adjusted
- Infrastructure costs
- Youth sector expenses
- Community schemes expenses



RELEVANT INCOME

- Revenue:
 - Gate receipts
 - Broadcasting rights
 - Sponsorship & advertising
 - Commercial activities
 - Other operating income
- Player transfer profit or income
- Finance income

- Related party transactions above fair value - adjusted
- Non-football income
- Non monetary credits



Relevant results for T-2, T-1, T aggregated for monitoring period

Exemption and accepted deviation

- Clubs with relevant income & relevant expense < € 5 mio in both T-1 & T-2 are exempted from break even-requirement
- Aggregate break-even deficit up to € 5 m immaterial
- **Accepted deviation implies that aggregate break-even deficit has been covered by capital injection from shareholders**

Examined during UEFA-season	Financial Statements taken into account	Accepted deviation
2013/2014	2012 (T-1) + 2013 (T)	€ 5-45 m
2014/2015	2012 (T-2) + 2013 (T-1) + 2014 (T)	€ 5-45 m
2015/2016	2013 (T-2) + 2014 (T-1) + 2015 (T)	€ 5-30 m

- **After transition period relevant losses up to Ø € 10 m per year are considered as acceptable**

CFCP disposing of some discretion

After a purely numerical assessment of the break-even result over the monitoring period, the CFCP will, if needed, look at the following other factors in assessing a club

- Quantum and trend
 - Impact of changes in exchange rates
 - Projected break-even result in $t+1$
 - Budgeting accuracy
 - Debt situation
 - Force majeure
-
- Players under contract before June 2010 (for first two monitoring periods)

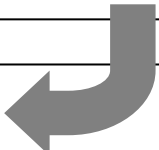
Weaknesses of the new concept

- Enhanced overdue payables rule in force from July 2011 on; step-by-step (reluctant) implementation of break even requirement (first assessment only in season 2013/14, p&l as of 2011/12)
- ECA successfully introducing certain “softener”
- Scope of fines not yet determined (exclusion, withdrawals)
- CFCP to hand over files to UEFA’s disciplinary bodies
- Loopholes and circumventions
- Consequent sanctioning of big brands?

Peculiar economics of the „Citizens“

In £ mio

Fiscal year	2008/09	2009/10	Premier League
Revenues	87	125	2.030
Wages expenditure	83	133	1.389
Wages/revenue ratio	95%	107%	68%
Transfer spending	138	145	559
Pre-tax loss	-93	-121	-445
Clubs disclosing profits	6	4	



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 (?)

Potential impacts of Financial Fair Play

minor in Germany

German clubs operate, thanks to the licensing procedure, perhaps to their mentality, a business model predominantly close to break-even

Being member associations or companies controlled by such associations (50+1), clubs are subject to strict budget constraints and the step-in of sugar daddies is broadly ruled out

More star players will join the Bundesliga or stay, resulting in more attractiveness of the national championship and an improvement of their competitiveness in European club competitions

substantial in England

the Premier League's business model apparently is increasingly based on rich benefactors willing to inject capital, provide soft loans or secure debt thus mobilizing further financial means to spend for playing talent in addition to the highest revenues

English clubs, particularly those controlled by benefactors or by owners imposing large debt onto the club's balance sheet, cannot continue to run their business as they used to and should adapt their strategy

Recent survey

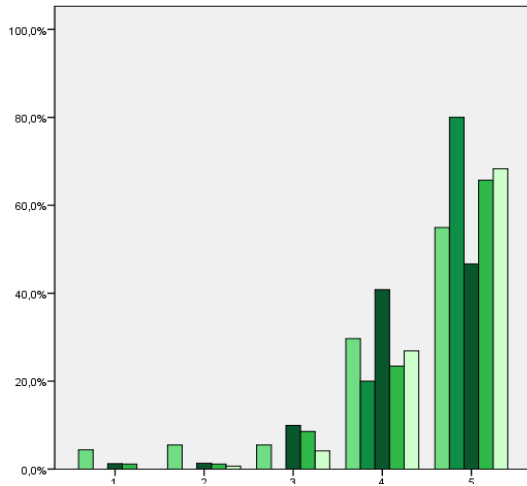
Web-based inquiry across Europe questioning the objectives of the Fair Play concept conducted by the University of Chemnitz (G. Hovemann, J. Lammert, S. Komsalov) confirms support and sympathy of football fans

England	93 respondents
France	10 respondents
Germany	745 respondents
Italy	175 respondents
Spain	<u>147</u> respondents
TOTAL Big Five	1.170 respondents

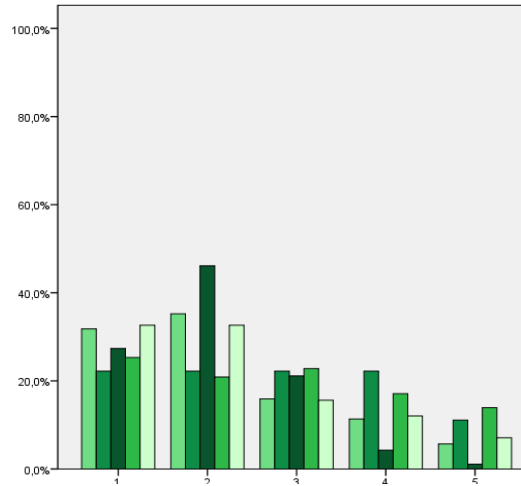
see <http://www.tu-chemnitz.de/hsw/sportwissenschaft/financialfairplay/>

Common consent for UEFA's initiative, success questioned

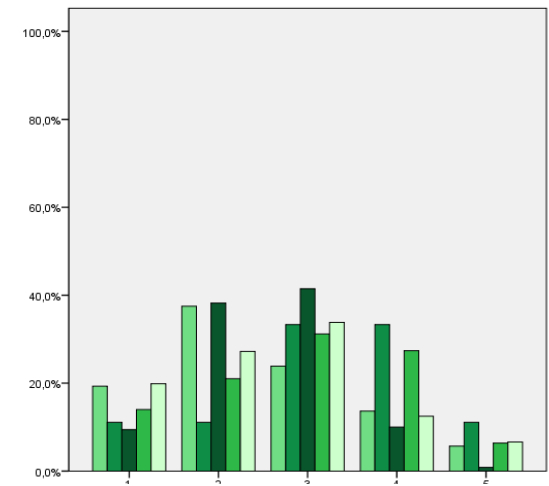
Scaling 1 to 5 meaning
Not at all important ... very important



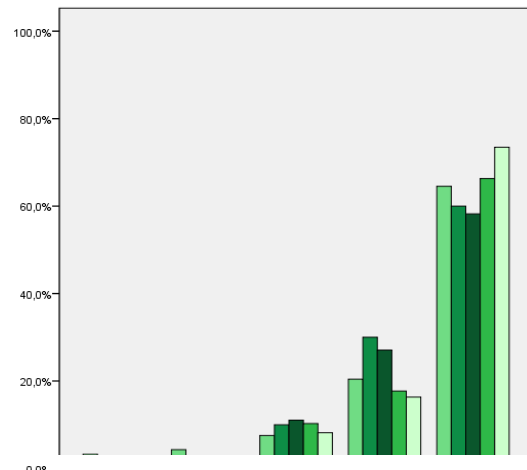
Worthwhile



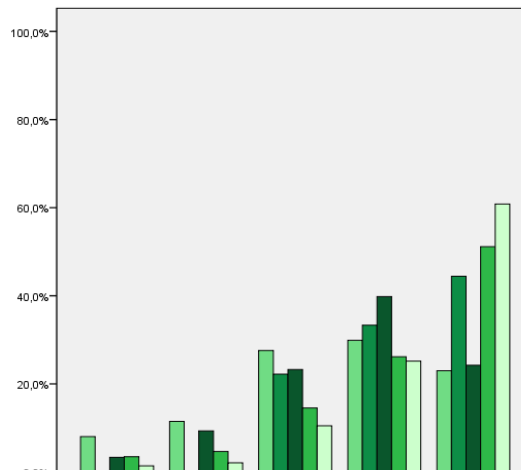
Strict application



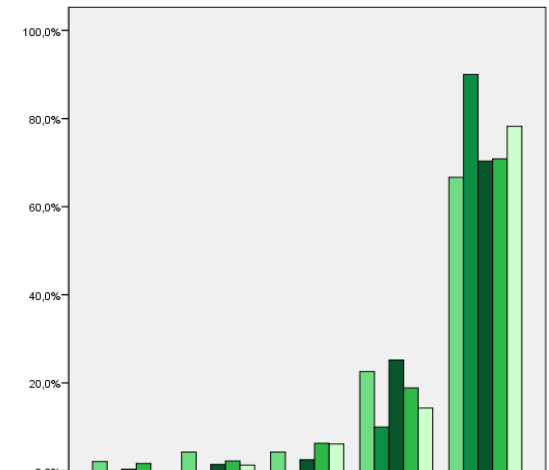
Objective achievement



Expenses < revenues

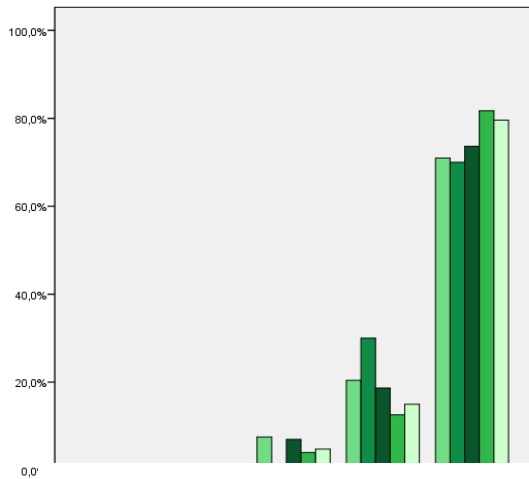


Preservation of
attractiveness

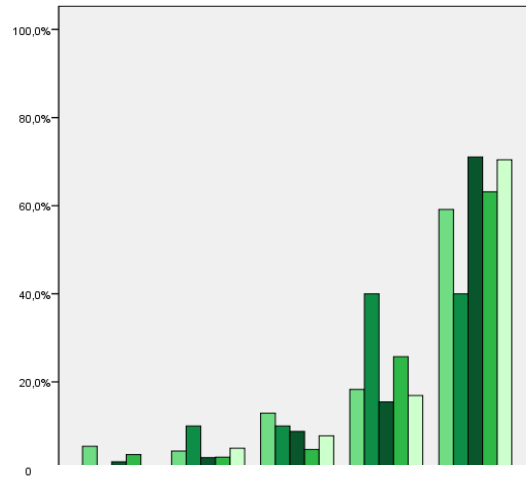


Limitation of debt

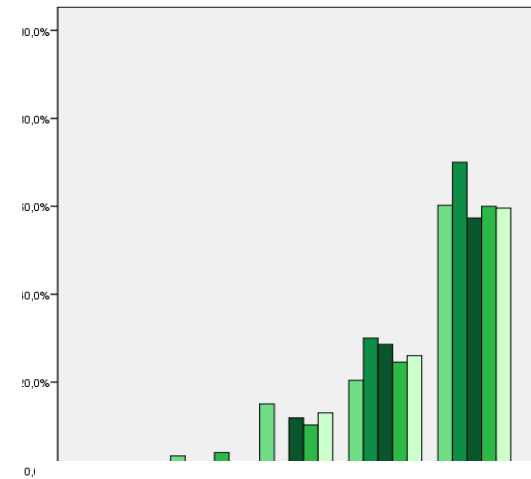
Results don't vary across different nationalities



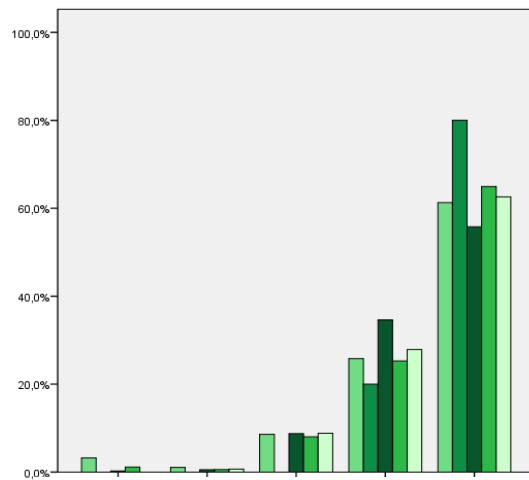
Promotion of investment
in youth development



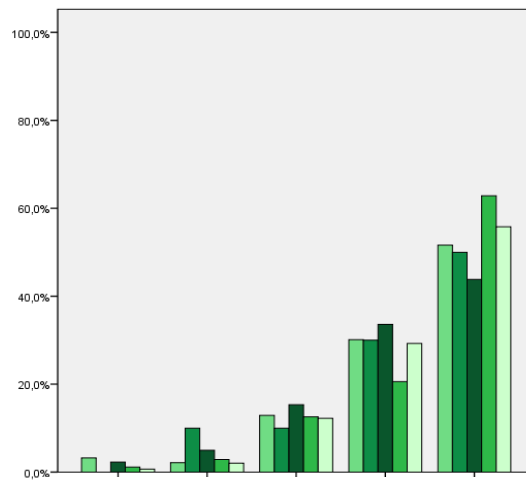
Regulation of external
funding



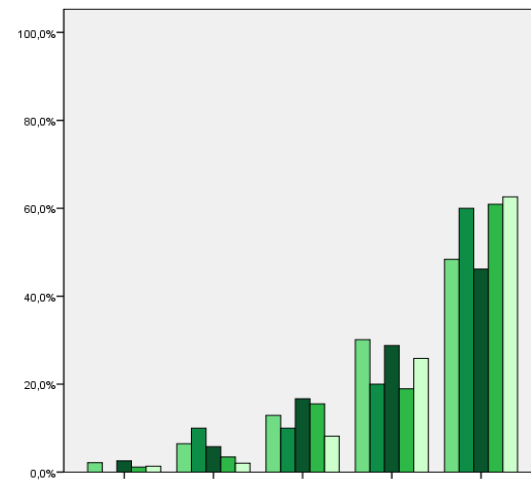
Avoidance of financial
difficulties



Preservation of financial
stability



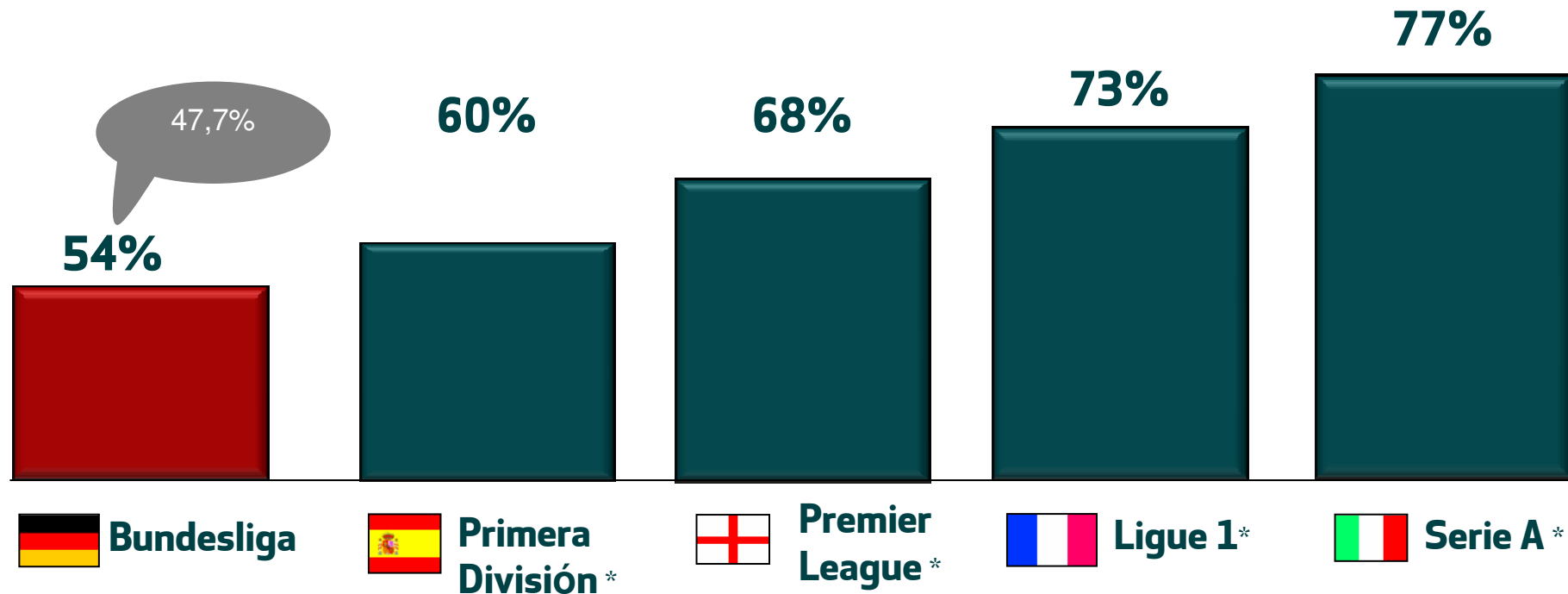
Avoidance of excessive
salaries



Avoidance of excessive
transfer fees

Compliance with fair play via reasonable wages

Wages/ revenue ratio



Thank you
for your attention