

Developing a Sustainable Business Environment in Sports- UEFA Financial Fair Play

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Abstract: The competitive football system in Europe has created a platform for businesses all around the world either ready to buy football clubs or sponsor them. However, this particularly attractive environment makes football clubs want to compete at the limit of their financial resources. In order to prevent long term negative effects of this arms race, UEFA has implemented the Financial Fair Play Regulations (FFP). The purpose of this article is to find the causes that led to the need of controversially regulating the free market in sports. It also helps provide clarity regarding the future of these regulations.

Keywords: *profit maximizers, utility maximizers, financial fair play regulations, evolution.*

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1. Introduction

European football has always been at the top of the sports spectacle with football clubs battling for European glory and for club silverware such as trophies like UEFA Champions League and UEFA Europa League. However, in order to get in European competitions held by UEFA, clubs must first earn a top spot in their national leagues, and in order to do that they usually spend more than they should.

2. History and the necessity of implementation

In 1971 Peter Sloane published an article titled "*The Economics of Professional Football. The Football Club as a Utility Maximiser*". It laid bare the ideological differences between the North American and European sporting cultures. In the United States there has always been an assumption that sport teams should be profit maximisers, and therefore be organized as closed leagues to protect the sport clubs against the economic penalty of relegation. (Sloane, 1971)

Conversely in Europe where leagues were open, and had promotion and relegation, utility maximization that desired to prioritize the sporting success was the objective.

Profit or underwriting losses was only important insofar as it was necessary for a club's long-term stability and survival. And this economic theory is the bedrock behind the implementation of FFP.

There have been various examples of owners in England that tried to run their football clubs as profit maximisers. Alan Sugar a notorious business man tried this model when he was running his club, Tottenham Hotspurs as profit maximisers, and looks back at the experience as having wasted 10 years trying to do something great for that football club. From 1991 to 2001 Sugar ran Spurs within their means, most of their fans hated the period, with the League Cup being the sole trophy in a period of mid-table mediocracy. The club only managed to make 2 mil/year profit, over the first six years, much less than Arsenal London rivals, who were competing at a much higher level.

Importantly Sugars ownership illustrates a paradox in running a football club, as Simon Kuper and Stefan Szumanski explained in their book *Soccernomics*.

"When business men try to run a football club as a business, then not only does the football suffer, but so does the business. In an open system of promotion and relegation, utility maximization is the only way to survive." (Kuper & Szymanski, 2014)

Without financial regulations, football clubs are of risk of over-extending to the point of threatening their own existence. It is a fact that it has proven itself over and over again in the football system.

Leeds United for example, is a clear case in this matter. In the 2000-2001 season the club reached the semi-finals of the UEFA Champions League (UCL), and where one of the most competitive teams in England's Premier League (PL). Under the guidance of their chairman, Peter Risdale, the club had taken a number of loans due to the prospect of achieving UCL football again next season which they narrowly missed out on at the end of the 2000-2001 season and again at the end of the 2001-2002 season. Due to consecutive seasons without the Champions League revenue, the club was unable to repay their loans and we're forced to sell their major players. With Leeds leaking players due to their debts, on pitch performances suffered as well and Leeds was relegated. Leeds failed to stop the rot in the Championship (England's second division) and we're forced to dismantle the squad further and we're forced to sell their training ground and stadium in 2004. In 2007 they entered administration and we're given a 10 pct deduction for failing to control their finances and we're relegated to the 3rd division for the first time in their history.

Leeds fans can feel comfort in the fact that they are far from alone. Between 2000 and 2008, only in England, 42 football league clubs entered administration, 17 in 2002 and 2003 alone. In reaction to this plight of poorly managed football clubs an inquiry was held in the House of Commons Culture, Media and Sport Committee into the governance of English football.

In 2011 and 2013 two of the leading sport economists present Stefan Szymanski and Sean Hamil had opposing views on the habitual loss-making of football clubs. Szymanski argued that a lack of profitability didn't actually matter considering that there was always a new owner ready to step in and pick up the bill. Hamil however stated that financial instability lead to the cannibalization of the rest of the sporting pyramid to pay increased wages, citing the case of Glasgow Rangers in Scottish Premier League, who had also entered administration. There was also the moral issue of tax payers effectively picking up the bill for mismanaged football clubs.

When a club is put into administrations, the football creditors rule ensures that all football related debts such as the ones to the players, coaching staff, and other clubs are to be paid first and in full. This essentially means that the public institutions are one of the last creditors to be repaid their debts. HM Revenue & Customs (from the UK) typically only receives between 5%-10% of what they actually are owed. Equally problematic is

the fact that despite going into administration, football clubs may rarely go extinct. In 2002 Leicester City entered into administration and paid HMRC 700 000 £ of the 7 mil £ it owned. 14 years later Leicester won the Premier League. (Kuper & Szymanski, 2014)

The wider context of European football finances is equally important to understanding why regulation was necessary. In the late 1990's European football club revenues dramatically increased thanks to Pay-per-view- TV. The Bosman case however allowed players to have more bargaining power, meaning the increased revenue largely translated to an increase in player wages. In an interview with the BBC Alan Sugar described this phenomenon as having "*the prune juice effect*" ("*it goes in one end and it goes out on another*") when discussing the Premier League. With large sums of money on the football clubs hands, the risk of financial mismanagement was much higher (Iancu et al., 2019).

3. UEFA's action plan

The real threat from UEFA's point of view were the clubs themselves. After the economic crisis in 2008 the European governing body came to the following conclusions (Hoye et al., 2015, p. 101):

1. This chronic loss-making was not sustainable
2. The threat of a breakaway European Super-League (with no promotion or relegation) was increasing with the "big clubs" growing tired of chronic loss-making.

Arguably the big clubs had their own interest, after seeing how clubs like Manchester City and Paris Saint-Germain FC, became over-night successes after being injected huge sums of capital, they felt like their best players and football success might be bought over-night, as Lazio Rome had done 10 years before.

A 2018 study called Report Calcio, made by numerous sports consulting companies and based on UEFA data, taking into account each of the top division clubs of each of the UEFA member associations, meaning over 700 football clubs, reflects how exactly the financial crisis from 2008 had its mark over the European football. While football clubs were probably one of the few companies that had increased their revenues (Figure no1.), their cost (Figure no.2) rose as well.

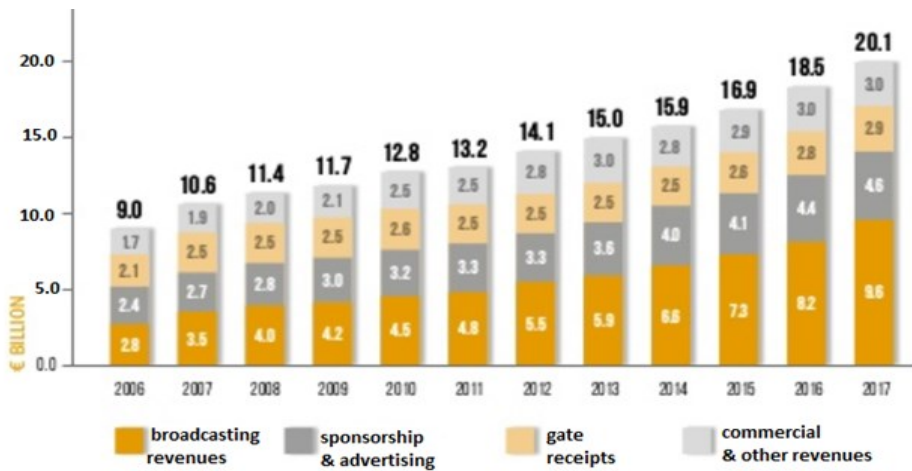


Figure 1. Aggregated total revenues – European Top Division clubs
source: self-processing financial data of the Top 5 European Leagues from various sources including The Report Calcio Study (2019)

The revenues generated by the major European leagues since the 2017 have increased even more rapidly due to the fact that the broadcasting revenues have almost doubled, with new contract for both England’s Premier League, and Germany’s Bundesliga, bringing clubs from the first divisions more than 3 billion/year (England) and 1.3 billion/year (Germany). This has resulted in the increase of transfer sums paid for players and the increase of player wages.



Figure 2. Aggregated total costs – European Top Division clubs
source: self-processing financial data of the Top 5 European Leagues from various sources including The Report Calcio Study (2019)

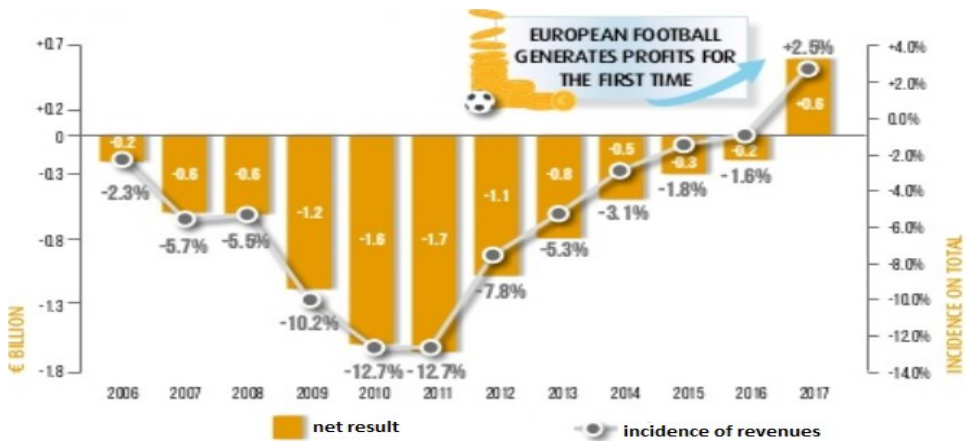


Figure 3. Aggregated net results – European Top Division clubs
source: self-processing financial data of the Top 5 European Leagues from various sources including The Report Calcio Study (2019)

Thus, the late 2000s worldwide recession had however left its mark on the European football clubs in a sense of decreasing the net result of football clubs (Figure no.3.).

This would have increased the chance that one of two scenarios could have happened:

1) the first scenario left the door open for other investors that might take advantage of the club assets (such cases were the ones at Liverpool FC and Manchester United FC), if an interested bank would have been interested in baling out the mismanagement of the club;

2) the second scenario left clubs seeing their image diminish while clubs and staff sue them in order to recover their debts and communities might end up with a bankrupt club that can't pay its takes and/or represent the community.

4. Implementing the UEFA Financial Fair Play Regulation

The only answer to the situation above mentioned would have been a form of financial regulation. But any attempt to regulate the free market would have been seen as a violation of international law. Thus, UEFA has worked closely with the European Commission to come up with a solution in accordance with all the legal framework of the European Union.

The initial solution was effectively a soft salary cap to control club expenditure and turn clubs into reasonable stable institutions, and UEFA called it Financial Fair Play (FFP).

In 2010 UEFA introduced the FFP rules that aimed to keep the clubs from spending themselves into financial difficulty. In UEFA's words: "*to improve the overall financial health of European football*".

Due to several legal challenges brought against UEFA, the severity of the penalties for clubs failing to comply with the rules are subject to change, but as a broad summary the rules state that ***football clubs must balance their books over a period of 3 years***. The penalties for failing to do so include:

- temporary expulsion from European competitions such as the UCL or UEL;

- fines;

- banning clubs for a limited period of time to make any kind of player transfers

As a result, FFP is considered to have contributed directly into (Taormina, 2019):

- turning the European football industry into a profitable one for the first time in its history;

- preventing clubs to build-up debt by putting pressure on more than 50 clubs with smaller loses to raise capital and cover their loses;

- agreeing at least 28 settlement agreements in order to assure that the most excessive loss-making football clubs can be restricted;

- discouraging football clubs in delaying their payments towards players, staff and other football clubs, but also reducing their public debts as well;

- creating a safe business environment that persuades serious long-term investors to either own or sponsor football clubs;

- inspire other football leagues and sports main bodies to introduce parallel domestic rules, based on the FFP regulations;

- increasing the accountability of club directors towards their stakeholders.

Ever since the FFP regulations were only in the discussion faze and until the study above mentioned was published, between a period of time of 10 years (2009-2018), in European football there has been an increase of 19% in foreign investors.

One of the most important effects of FFP is the fact that it encouraged clubs to invest in their fixed assets. By the end of 2018, 163 new stadiums were built in Europe only, with clubs investing more than 20 billion euros in their sports infrastructure. Due to the new facilities being build, the attendance in European football has grown by more than 50% in the last 10 years.

5. Conclusion

The present article has tried to present the need, evolution and main results of FFP regulations in European football. This regulation initially applied for clubs seeking to participate at a top level aiming to take part in the UEFA competitions. Since then, most of the football federations have adapted this method into their own leagues.

However, some important questions remained unanswered:

1. *With the transfer fees climbing every year and player wages and agent fees also increasing how do clubs continue to comply with the rules and avoid sanctions?*

The response to this question is that one such method is player amortization. Player amortization is a term used to describe the way in which football clubs account for the cost of players, by spreading them over the duration of a player's contract with the club.

2. *How are the FFP regulations different than the usual licensing regulation of each sports association?*

The response to this question is that UEFA's official Club Financial Control Body (CFCB) has a role in monitoring both Club Licensing procedures and FFP regulations, but also it can help break settlements and does not directly give penalties or rejects any clubs participation to the European competitions. The licensing process usually offers a *yes* or *no* answer to the admission process, while CFCB controls and offers guidance and assistance before taking legal action against clubs. Clubs can avoid further sanctions through methods such as submitting a future business plan consisting of a balance sheet, profit and loss statement but also of statement of cash flows.

In the end, it's important to understand the fact that FFP regulations have made the European football system as a system based on the utility maximize theory in sports demonstrate that there can exist a profitable business system that emphasizes long term development and success.

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