The Union of European Football Associations ("UEFA") Financial Fair Play.

By Juan de Dios Crespo and Santiago Santorcuato [1]

SUMMARY: 1 Introduction – 2 How the FFP System Works? – 3 Pros and Cons of the UEFA FFP – 4 Conclusion

1. Introduction

European football clubs' incomes have increased in the last five years. However, in the same period of time, personnel and transfer costs have also increased significantly. In a report published by the Union of European Football Associations ("UEFA"), it has been estimated that about half of the major European clubs are losing money and most of them are set to continue recording significant deficits.

On average, it has been reported that European clubs spend almost 65% of their income on staff; a large number of these clubs especially major football clubs for which players' wages are the biggest expense, spending is more than earnings. There is certainly little doubt, that if this trend of recording losses continues, professional football is headed for bankruptcy, at least in relation to major football clubs.

According to said report published by the UEFA, the average growth of the football industry was 5.6%. This equated to an income increase of up to 13,200 million euros, while losses of clubs have experienced a significant increase from 600 million euros in 2007 to € 1,700 million in 2011.

With an inability to impose sporting sanctions, Spain is at the head of Europe's clubs for bankruptcy. In 2011 out of a total of 24 European clubs in this situation, 22 were Spanish.

For this reason, it could be argued that the crisis of football is not the lack of income, but it is the incurring of excessive expenditures leading to clubs spending more than what they actually earn as revenues every year. Based on these conclusions and after a thorough study of the matters at stake, UEFA designed a new system in order to try to stop the economic crisis of European football by creating the "Financial Fair Play" Regulations (hereinafter FFP).

2. How the FFP System Works?

This system was implemented as early as 2010 in order to avoid clubs from spending more money than they earn. The attempt was therefore to impose a certain balance on club's respective financial accounts. The UEFA Financial Fair Play (FFP or Financial Fair Play) is thus a new system developed in order to end this situation and prevent the disappearance or relegation to lower

---

[1] Juan de Dios CRESPO and Santiago SANTORCUATO, Head and Associate of RUIZ-HUERTA & CRESPO SPORTS LAWERS - www.ruizcrespo.com

divisions of iconic teams in Europe. The FFP purpose had to be implemented gradually in order to be fully operational by 2014.

In this way, the new regulations are directed towards the improvement of the financial capacity of European clubs, who shall only be entitled to incur a certain level of expenses which shall in any case be measured with their corresponding incomes. Basically, the regulation is a compilation of rules whose premise is stabilizing the losses in the football market. Thus, Financial Fair Play (FFP) makes up part of an extensive set of criteria that clubs must comply with in order to be licensed to take part in UEFA's club competitions, primarily the Champions League and Europa League. This requirement imposes on clubs the obligation of avoiding to exceed a certain quantity in their budget and if they do that, they may be punished with the maximum penalty being disqualification from European competitions. An example of this was the recent case of Spanish club, Malaga CF that was banned from taking part in the UEFA Champions League due to its debts to fiscal authorities. It should be borne in mind that UEFA's FFP rules only apply to clubs who wish to compete in the Champions League or the Europa League. Clubs have to apply to UEFA to take part and will only get a license if they meet the FFP rules.

By adopting this system, UEFA tries to ensure the financial control of European clubs, using the Financial Control Panel (FCP), as a control body which has been active since June 2012. This body is responsible for delivering the concessions so that teams can participate in UEFA competitions. However this body is responsible one for punishing and in worst case scenarios, banning from UEFA competitions those clubs that fail to comply. The latest and most famous cases are the ones involving Manchester City FC and Paris Saint Germain, which have been fined EUR 60 million each in the past season for breach of FFP.

It is clear therefore that the implementation of the licensing system has as its main objectives, the following:

a) Increase economic and financial capacity of clubs, by finding new sources of wealth, such as the efficient exploitation of the commercial rights.

b) Introduce more discipline and rationality in the finances of football clubs, increasing their transparency and credibility.

c) Ensure clubs to settle their liabilities to other clubs, players and social / tax authorities.

d) Encourage clubs to compete with their own income ("Break-Even").

e) Reduce pressure on wages and transfers of players, in order to limit the inflationary effect.

f) Encourage long-term investment in the youth sector and own infrastructure, fixed assets like stadia or training camps in order to generate income and avoid short-term speculation.

g) Control the entry of "patron" in football (Sheikh Abdullah Bin Nasser Al-Thani, Málaga Ali Syed at Racing Santander, Sulaiman Al Fahim, Manchester City, etc.). UEFA considers that the kind of income that generates this type of investment is volatile and creates distortions.

h) More discipline and rationality in club football finances (decreasing pressure on salaries and transfer fees and limitation of the inflationary effect);

Among the principal objectives of the UEFA FFP is the rule known as the "Break-Even" Rule. This rule is the backbone of the FFP system and is meant to provide a certain degree of stability to European Clubs and rationalize their economic activity in the long-term through evaluation of clubs on a renewable period of three years. UEFA believes that it would be unfair to assess a club's Break Even results over just one season and has therefore introduced the concept of Monitoring Periods. Initially the clubs were assessed over two seasons (2011/12 and 2012/13) combined in order to see an acceptable level of loss.

Thus, Article 60 of the UEFA Club Licensing and Financial Fair Play Regulations (hereinafter the “CLFFP”) defines this notion of break-even result as *"the difference between relevant income and relevant expenses"* and adds: *“If a licensee’s relevant expenses are less than relevant income for a reporting period, then the club has a break-even surplus. If a club’s relevant expenses are greater than relevant income for a reporting period, then the club has a breakeven deficit”*.

Thus, this rule of the UEFA FFP regulations is an obligation for clubs over a fixed period of time to achieve a break-even situation when expenditures are measured in relation with incomes deriving from football-related activities. However, the UEFA FFP rules cover much more than what is in principle necessary in order to achieve said 'Break Even” situation. Thus, for example, it is therein specified that clubs shall keep up-to-date with their taxes, their transfer fees and pay players’ wages on time.

Although the balance means that spending must be equal to incomes, there is a certain deviation (or margin) of accepted losses. Nevertheless, UEFA does not consider all expenses as losses. On the negative side, UEFA takes into account particularly players’ transfers and salaries, but the expenses related to the training and education provided to their young players, clubs infrastructure, youth sector, investment and social projects will not be considered as losses. Furthermore, UEFA permits the exclusion of certain expenditures from the overall calculations, taking into consideration the development of the game and the FFP rules without interfering, for example, the investments and developing of the clubs that would be hit by an FFP penalty.

Consequently, clubs can therefore exclude infrastructure development costs and youth development/community development costs. Under this plan, Manchester City FC announced that they should be able to exclude around £10m per year as a result of the youth/community exclusion.

There is also another factor subject to exclusion: clubs can exclude certain wages for their long-standing players. This is because when the rules were first proposed, some clubs were already committed to paying high wage bills for some players on existing contracts and for that reason, they would fail the Break Even test as a result. As per the above, UEFA therefore allowed clubs who had failed the Break Even test to run the test again, but deducting this time wages paid to players as per employment contracts in force prior to June 2010 contracts. However clubs can only deduct the wages paid to their long-standing players and can only use the exclusion if they can show their Break Even deficit is being reduced each year.

Thus, the sources for relevant income are revenues from gate receipts, broadcasting rights, sponsorship and advertising deals plus profit made from the transfer of players while, on the other hand, for the expenditure are the cost of transferring players, salaries and employee benefits expenses and other operating expenses. At the end of the day, big clubs are just as big brands and will always find ways to make money, whether an endorsement deal with a pre-season tour of new partners or investment, the options are there to be exploited.

The regulations take into account players' transfers too. As we all know, when a club wants to hire some player who is contracted with another club, the buying club should pay a transfer fee to the selling club in order to acquire the services of the said player. However, from a Break Even perspective the financial cost of acquiring a player has to be written-off over the entire duration of the contract.

Accordingly, when a club signs a player, it has to pay certain sums of money, via an immediate bank transfer. From a "Break Even test" perspective, the purchase price would be amortized evenly according to the duration of the contract, i.e. amortized on a yearly basis through an equivalent percentage of the total transfer fee.

On the other hand, UEFA is aware that club owners can inflate artificially their profitability, for instance, through artificial commercial deals. For this reason the UEFA FFP rules require any transaction from a 'related part' (i.e. a company or body connected to the club owners) to be assessed to ensure a genuine transaction at a 'fair value'. Thus, UEFA has the power to adjust any artificial 'mates rates' deals and apply a lower value to the Break Even calculation.

Finally, a further requirement of the FFP is that no club is entitled to have overdue amounts owed to football clubs, employees or tax authorities.

Notwithstanding the foregoing, it should be pointed out that even if clubs have losses, they may pass the Break Even test. UEFA understands that because players are often under long contracts, clubs cannot reduce their spending quickly. For this reason, UEFA appreciates that it would be unfair to fail clubs who make a small loss; consequently they have introduced a concept called the 'permitted Break-Even deficit'.

As a result, clubs can make a loss up to a certain level but if they go over the permitted thresholds, they will fail the FFP Break Even test. In this regard, the permitted Break Even deficit is set at a fairly high level (€ 45m) for the first Monitoring Period, and is then progressively reduced in subsequent periods. The permitted loss falls to €30m for the three year period that covers 2013/14, 2014/15, 2015/16 (that works out to as an average loss of €10m per season). In summary, under the new rules, if the club owners exceed the permissible thresholds between the different monitoring periods and consequently, their clubs incur losses in excess during a period of three years, they must be subject to penalties and even exclusion from the Champions League and Europa League.

UEFA is keen to ensure that clubs have no debts and for this reason insists that any club losses over € 5m during a single Monitoring Period are fully funded by their owner. In practice this means that clubs can only lose up to the maximum € 45m during the first Monitoring Period if their owner is able to spend their own money for any loss over € 5m and, in UEFA's terminology, 'convert the loss into equity'. This equation can be exemplified using the equation of an owner of a club with a loss of € 25 m during the first Monitoring Period. However the club would be able to still pass the Break-Even test due to the fact that the loss is below the € 45 threshold. However as the € 25m loss is above the €5m figure it will be the club’s duty to design a financial plan, for example by means of finding additional shares and/or getting new sponsorships in order to cover this difference between € 25m and € 5m.

Nevertheless, it can be asked FFP, who is in charge of controlling the system? For a rigorous application of the FFP regulations a body called the Financial Control Panel to the Club was created, which since 2012 is a UEFA disciplinary body and has a bicameral system. The Chamber is responsible for conducting investigations on European clubs, adopting provisional measures and referring any case whenever necessary to the Court Chamber, which will be entitled to decide who will be subject to the corresponding disciplinary measures envisaged and accept or reject the clubs’ request for registration to European competitions. This independent board assesses whether clubs have broken the FFP rules, including the Break Even rules. Between December 2013 and April 2014 this body will advise clubs of the outcome of their assessment and any punishments. The most serious punishment would be a ban from UEFA competitions.

3. Pros and Cons of the UEFA FFP

As stated above, it can be concluded that the UEFA Financial Fair Play has its benefits as well as its evils.

Among the benefits are the following:

- there is decreased risk of default for players and employees.
- There is benefit for taxpayers.
- There is assistance provided in the detection of management problems.
- There is protection of clubs from incompetent managers
- The system contributes to a healthier football industry.

On the other hand, the evils include:

- the system motivates people to enter the football industry at all costs
- Some players will have their fixed wages decreased and variable payments will increase.
- The sporting merit may not be sufficient to qualify for a competition

4. Conclusion

With the implementation of this system, UEFA shows that there has been a significant reduction in losses of first division clubs in Europe and this demonstrates that the financial fair play might be working. This proposal tends to equalize the revenue with expenses, allowing a fair market with equal economic conditions. Thus, clubs must accurately choose where they will spend their money demonstrating that the financial control of football clubs was necessary.

The controlling mechanism should adjust the system with the arrival of rich tycoons in the football market. But, the Financial Fair Play does not prohibit the "state aid" for clubs. It is believed that it would require a strict prohibition of receiving this kind of aid for professional sports companies.

So far, the proposal seems to be working well and UEFA will have to correct and update the regulations as drawbacks arise in its application. It must, however, be observed that UEFA took the first and fundamental step and must be commended for financial regulation of European football.