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Club governance in European and French professional football clubs

Wladimir Andreff *

***** Professor Emeritus at the University Paris 1 Panthéon Sorbonne

Honorary President of the International Association of Sports Economists and of the European Sports Economics Association

President of the Scientific Council at the Observatory of the sports economy, State Secretary for Sports

Introduction

Mainstream theory of corporate governance (the principal-agent model) can apply to team sports clubs if it is assumed that they maximise profit (namely in North American leagues).

In European professional football, clubs have no profit objective, are used to maximise wins (on the pitch), then overspend on investing in talent (in a so-called ‘arm’s race’) so that they do not stick to their budget constraint (Expenditures > Revenues = Deficit) wich boils down to lax management reflecting bad club governance.

Recurrent lasting club deficits lead to increasing club debts and eventually raise the issue of league financial instability and viability.

A question follows: how improve football clubs’ governance through hardening their budget constraint (Expenditures ≤ Revenues => hard budget constraint).

1. Corporate governance in the principal-agent model

This model applies to any stockholding company floated on the stock exchange and therefore is of interest for the 44 football clubs which have experimented an IPO (initial public offering).

In a corporation, agency relationships link: a/ owners and employees; b/ stockholders (owners) and managers; c/ debt-holders, if any, and owners.

The so-called principal (owner) has less information than the agent (manager, employee) about what is going on within the organisation: a moral hazard situation that may drift into wrong decision-making.

In a football club, agency relatinships between a/ owners and players; b/ owners and managers/coaches; c/ debt-holders and owners.

If the club's objective is win maximisation, managers must be rewarded in terms of wages and bonuses for good management; if profit maximisation, they must rewarded for raising revenues over costs (profit-making).

The problem is: how owners can control and monitor managers so that they do not spend too much on wages and (managerial) in-kind benefits?

As residual claimants, owners stand last in line for the distribution of gains (dividends) or losses (deficits) and aim at reducing manager/employee overspending. Otherwise entrenched managers would expropriate shareholders from residual revenues (profits).

Managers can be monitored by three disciplinary means:

a/ contractual discipline: undisciplined (overspending) managers can simply be fired if they do not avoid loss-making (good management);

b/ takeover discipline exercised by the capital market: a loss-making firm will be taken over by another firm, and incumbent managers will be fired;

c/ bankruptcy discipline: a company repeatedly in the red and indebted will go bankrupt and be liquidated.

Finally, the principal-agent model distinguishes weak (bad) from strong (good) corporate governance structures:

a/ Weak: insider control by managers or by employees (self-management); managers have the last say on strategic decisions, namely when many dispersed shareholders (owners) cannot monitor them; likely to be the case of European football clubs with floated shares at the stock exchange and many shareholders (fans).

b/ Strong: when there is a hard core of (non dispersed) shareholders/owners: tycoons, banks, investment funds.

c/ Strong: insider control by a big boss who is both the single owner and top manager.

What about football clubs with floated shares?

2. Football clubs’ governance from a principal-agent perspective

Overall 44 European football clubs have ever experienced an IPO but 21 have already been delisted due to poor financial performance (Appendix 1)…

…while they should have been profitable according to the P-A model.

The model is not confirmed in football overall, except for a few clubs: Fenerbahce, Galatasaray, Trabzonspor, Benfica, Lazio = in the black (Fenerbahce: only one to distribute dividends; others = deficits (Table 1).

IPOs have been looked for by European football clubs as a new source of finance, not as a means of improving governance and profitability.

IPOs’ revenues have been invested in recruiting superstar players, instead of investing in sporting infrastructures, acquiring stadiums or other tangible assets.

Owners are also reluctant to submit themselves to (stock) market discipline: Aulas has kept 50.01% of all Olympique Lyonnais’ shares after the IPO to keep control .

Appendix 1: European football clubs listed in stock market, weight in December 2010

Listed football club	Country	Weight	IPO date	Delisted football club	Country	IPO date	Delisted
Aalborg Boldspilklub	Denmark	0.53	09.1998	Aberdeen	Great Britain	02.2000	08.2003
AFC Ajax	Netherlands	3.49	05.1998	Aston Villa	Great Britain	05.1997	08.2006
AIK Football	Sweden	0.27	07.2006	Birmingham	Great Britain	04.1997	10.2009
Arhus Elite	Denmark	2.00	12.2004	Bolton	Great Britain	04.1997	06.2002
AS Roma	Italy	6.50	05.2000	Charlton	Great Britain	03.1997	09.2006
Besiktas	Turkey	8.40	02.2002	Chelsea	Great Britain	03.1996	08.2003
Borussia Dortmund	Germany	9.24	10.2000	Leeds	Great Britain	08.1996	04.2004
Brondby IF B	Denmark	2.89	01.1987	Leicester	Great Britain	04.1997	11.2002
Celtic	Great Britain	3.58	09.1995	Manchester City	Great Britain	02.2002	07.2007
Fenerbahce Sportif Hizmet	Turkey	9.38	09.2004	Manchester United	Great Britain	06.1991	06.2005
Futebol Clube de Porto	Portugal	0.51	06.1998	Millwall HLDG	Great Britain	10.1998	12.2011
Galatasaray	Turkey	11.55	02.2002	Newcastle	Great Britain	04.1997	07.2007
Juventus	Italy	9.45	12.2001	Nottingham Forrest	Great Britain	10.1997	04.2002
Lazio	Italy	1.13	07.1998	Preston	Great Britain	09.1995	09.2010
Olympique Lyonnais	France	6.88	02.2007	QPR	Great Britain	09.1995	05.2003
Parken Sport & Entertainment	Denmark	8.80	12.1997	Sheffield United	Great Britain	12.1996	07.2001
Rangers Int Football Club	Great Britain		10.2012	Southampton	Great Britain	04.1994	04.2009
Ruch Chorzow	Poland		03.2011	Sunderland	Great Britain	12.1996	08.2004
Silkeborg	Denmark	0.88	06.2005	Tottenham Hotspur	Great Britain	10.1983	01.2012
Sport Lisboa e Benfica	Portugal	2.37	05.2007	Watford	Great Britain	08.2001	06.2011
Sporting	Portugal	0.30	06.1998	West Bromwich	Great Britain	02.1998	01.2005
Teteks Ad Tetovo	Macedonia		03.2012				
Trabzonspor Sportif Yatir	Turkey	6.47	04.2005				
	StoXX Index	100.00					

Source: Aglietta, Andreff & Drut (2010) and update.

Table 1: Pre-tax operating net income of listed and delisted football clubs, 2003-2012

(€million)

Listed clubs	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
AFC Ajax	-7.3	15.2	6.0	-6.7	-13.0	12.8	-0.8	-0.8	-0.8	-0.8
AS Roma	-90.4	-12.1	-27.0	10.4	39.2	22.0	2.7	-26.7	-29.1	-59.1
Besiktas	n.a.	n.a.	n.a.	-3.6	1.5	0.8	-10.4	-20.1	-59.2	-33.9
Borussia Dortmund	6.8	-61.8	-72.7	-13.1	16.7	8.8	-0.9	-0.9	20.9	39.2
Celtic	-6.5	-8.9	-9.5	-3.6	23.3	7.0	3.1	-1.6	1.0	-8.2
Fenerbahce	n.a.	8.8	33.2	27.2	29.7	32.3	30.5	31.0	24.5	15.9
Futebol Club do Porto	-15.9	27.8	0.6	-27.3	24.1	10.8	27.2	-1.0	-5.0	-19.0
Galatasaray	n.a.	28.6	19.2	26.6	40.8	42.5	41.9	13.3	-28.2	2.6
Juventus	-6.3	-6.2	-7.7	-17.3	-7.7	-3.9	17.9	-23.3	-99.8	-25.7
Lazio	-144.8	39.3	-25.5	6.7	15.2	29.7	23.4	11.4	7.2	-9.2
Olympique Lyonnais	n.a.	n.a.	18.6	25.3	29.9	31.9	9.9	-53.0	-35.8	-33.6
Rangers Football Club	n.a.	n.a.	n.a.	2.2	-7.2	10.5	-12.8	6.4	2.5	2.7
Sporting Lisboa e Benfica	n.a.	-5.0	2.4	3.0	21.6	3.3	-33.5	6.8	13.9	15.3
Sporting	-25.0	-8.4	62.8	1.9	17.8	-0.6	-12.1	-9.7	-44.0	-40.5
Trabzonspor	n.a.	n.a.	n.a.	13.1	17.7	13.3	21.1	20.6	29.7	5.5
Delisted clubs	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**
Arsenal	n.a.	n.a.	n.a.	26.6	33.8	73.0	72.2	86.1	34.4	63.9
Aston Villa	-16.4	-15.2	-3.6	-11.4	-11.1	-9.7	-8.5	-8.9	-9.0	-9.6
Birmingham City	4.9	8.5	-3.6	-6.6	-20.9	0	-24.7	1.2	-13.8	-4.9
Charlton Athletic	0.4	17.1	3.0	-2.3	-2.3	-2.0	-1.7	-1.8	-1.8	-2.0
Chelsea FC	-46.3	-47.1	-47.9	-48.1	-46.7	-41.1	-35.7	-37.4	-37.9	-40.7
Leeds United	-59.8	-60.9	-61.9	-62.2	-60.3	-53.1	-46.2	-48.3	-49.0	-52.6
Manchester City	-18.6	-22.1	-16.4	-6.9	-10.9	-34.4	-84.4	-149.4	-223.6	-130.1
Manchester United	56.3	40.5	41.2	41.4	40.1	35.4	30.7	32.2	32.6	35.0
Newcastle United	13.3	12.3	7.6	-9.0	-7.7	-6.7	-7.0	-7.1	-7.6	-7.6
Nottingham Forrest	-20.8	-21.2	-21.6	-21.7	-21.0	-18.5	-16.1	-16.8	-17.1	-18.3
Southampton	2.6	7.6	3.5	-1.4	1.7	-3.4	-2.9	-3.1	-3.1	-3.3
Tottenham Hotspur	-9.0	-2.2	8.6	5.0	42.2	10.9	45.4	-0.2	4.5	4.8
Watford	-9.5	-3.7	-1.5	-5.0	8.3	1.1	-1.4	-3.7	-5.7	-5.7

Source: Datastream and Amadeus Database

Of course, most delisted clubs are also in the red (Table 1).

IPOs had not fuelled the expected disciplinary shock on to the clubs' managers, did not improve club governance and did not put an end to deficits. The recipe (floating shares) derived from the P-A model is wrong for European football.

Shareholders (mostly fans) had lost money with a declining market value of club shares: Juventus from 4€ down to 0.19€, Olympique Lyonnais from 24€ to 2.82€, etc.

Causes: a/Losses on the pitch trigger a depreciation of the share market value.

b/ The DJ StoXX Football market is narrow and illiquid (few share trading), thus affected by high volatiliy and low investment profitability.

c/ Uncertainty about the fundamental value of clubs assets when they are intangible (the value of players' contracts) and volatile: depends on players' performance on the pitch, good shape, injuries, relations with the coach.

French legislation (2006) allowing football club shares to be publicly offered links IPOs to the acquisition of tangible assets: O.L. IPO was backed by the OL land project, FC Istres' one by the construction of a re-education centre for high level sportsmen/women (did not avoid a 60% share depreciation).

3. Soft budget constraint in win-maximising clubs: deficits and bail-outs

In the P-A model, not-for-profit organisations must be financed by donations and managed by donators (ex: former *associations loi 1901*, *eigentragener Vereins*, etc.),but now professional football clubs are all incorporated.

An alternative analytical approach focuses on any organisation's budget constraint (since Kornaï, 1980). Hard budget constraint (HBC) is a precondition for an organisation's survival in a (capitalist) market economic environment while it is not in an administratively regulated (socialist) economy. HBC if:

$$E_{it} \leq M_{i0} + R_{it} \text{ , whatever } t$$

Eit: current operational expenditures; *Mi0*: initial money endowment;
Rit: current operational revenues of organisation *i*.

If: $E_{it} > M_{i0} + R_{it}$, whatever t => SCB (soft budget constraint).

With HBC, the economic environment of the organisation (club) recognises that it will fail (go bankrupt) in case of recurrent losses and debts.

With SBC, the economic/institutional environment does not accept the club's failure and in some way will bail it out.

Even in some industries of a capitalist market economy, loss-makers are not driven into bankruptcy, and are bailed out with financial subsidies and other instruments (Kornaï et al., 2003). Football is a case in point.

But any organisation (club), even if not-for-profit, must cover its expenditures out of its revenues (a deficit creates a contraint on its liquity and solvency), otherwise it cannot survive without external intervention + it is a clear sign of poor management and bad governance.

SBC occurs if a club can always find someone to bail it out ex post, such as: the football league, a tycoon, a local government authority, a bank or a sugar-daddy investor.

The bailing-out process can be direct, indirect or even implicit, simply a football club survives its failure to (a & b most typical of SBC):

a/ pay its suppliers' bills (ex: overdue transfer fees);

b/ pay taxes (tax and social contribution arrears);

c/ re-pay bank loans (a club's financial debt emerges).

If repeatedly occuring, these means of rescuing a club trigger a certainty for the club that it will always be rescued – a kind of SBC syndrome that can be measured by the degree to which clubs are permitted to fail;

namely if there is no enforcement of the bankruptcy law on to football clubs, and then no exit of a technically banktrupt (and badly-governed) club.

Consequences of SBC: no managerial effort to reduce costs/expenditures, no decision to restrain overinvestment in players' talent, recurrent payroll inflation (= lack of financial discipline and bad governance/management).

4. Soft budget constraint and bad governance in European and French football

European football: let us look at clubs' lasting deficits, debts, and the frequency of bail-outs.

Table 2: from one half to two-thirds of clubs in the red (loss-making), about the same percentage that breached the UEFA Financial Fair Play indicators.

Several clubs spend above 100% of their budget on payroll (94 in 2012).

Deficits (and bad governance) is more the rule than exception, with a slight improvement since 2013 when the FFP started to bite (to be enforced).

Table 3: resulting from recurrent deficits, 35% to 39% of clubs report bigger debts than assets (are insolvent);

A 48% to 57% share of debts in total liabilities is typical of SBC: unpaid taxes and social charges, employee payables (wage arrears), overdue transfer fees.

Table 2: Deficits of European football clubs, top division, 2008-2012

Indicators	2008	2009	2010	2011	2012
Aggregate net losses (€ million) of all	649	1206	1641	1675	1066
European top division clubs (number)	732	733	734	733	729
Number of reporting clubs	644	664	665	679	696
Percentage of loss-making clubs	54%	60%	61%	63%	48%
Proportion of clubs that breached at least one of the FFP indicators	n.a.	60%	56%	63%	57%
Number of qualified clubs which were not granted UEFA licenses	3	6	5	4	6
Number of clubs which were refused licences for financial reasons*	75	86	62	85	75
Number of clubs spending above 100% of their revenues on wages	55	73	78	81	94

* Audited financial statements, overdue employee/tax payables, overdue transfer fees or budgets

Source: UEFA Club licensing benchmarking reports.

Table 3: Debts of European football clubs, top division, 2008-2012

Indicators	2008	2009	2010	2011	2012
Number of reporting clubs	644	664	665	654	699
Number of clubs reporting negative net equity (debts > assets)	224	245	237	255	266
as percentage of all reporting clubs	35%	37%	36%	38%	39%
Bank debt and commercial loans (€bn)	5.5	5.6	5.5	5.1	6.3
Taxes & social charges (€bn)	1.4	1.3	1.2	1.4	1.4
Employee payables (€bn)	n.a	n.a.	0.6	0.7	1.0
Overdue transfer fees (€bn)	1.6	2.1	2.3	2.3	2.4
Total debt typical of SCB (€bn)	8.5	9.0	9.6	9.5	11.1
as percentage of total liabilities	49%	48%	50%	52%	57%

Source: UEFA Club licensing benchmarking reports.

Extremely rare that a European football club goes bankrupt; they continually operate on the brink of insolvency without going out of the business (Storm & Nielsen, 2012). Very high rate of survival in English football – forced administration instead of bankruptcy (Kuper & Szymanski, 2009), also in the Italian *Calcio* and the Spanish *Liga de Futbol*.

In French football, clubs that went once on the brink of bankruptcy (Bordeaux, Nantes, Red Star, Reims, Saint-Etienne, etc.) were all rescued by the league or a municipality or a benevolent not-profit looking investor.

In fact, every year those European clubs in the red are bailed out by tax authorities (tax arrears), the social security (social contribution arrears), banks (accept delayed re-payment), suppliers (overdue transfer fees and wages).

Improving football clubs' governance requires not only a better clubs' inner management, but also an institutional reform of the clubs' economic environment so that clubs do not find any more supporting organisations always ready to bail them out. Slight improvement with the FFP enforcement (Table 4).

Table 4: Top division European football clubs under financial fair play, 2009-2014

Indicators	2009	2010	2011	2012	2013	2014
Aggregate net losses (€ million)	1163	1634	1670	1076	792	486
Club operating losses/profits (€ million)	-249	-336	-382	-112	339	805
Number of clubs with large deficit*	78	107	109	92	83	73
Number of clubs with heavy deficit**	6	9	11	9	7	4
Club net debt (€ billion)	7.6	7.6	6.7	7.3	6.9	6.6
Net equity (assets less liabilities), € billion	1.8	1.9	3.3	3.9	4.6	4.9
Overdue payables 237 clubs (€ million)	n.a.	n.a.	57	30	9	8

* Deficit larger than € 10 million ** Deficit larger than € 45 million

Source: UEFA (2015).

5. Deficits, debts and governance in French football

Though one of the least plagued league with deficits and debts, French *Ligue 1* exhibits a SBC syndrome despite the existence of an inner audit (DNCG – *Direction Nationale de Contrôle de Gestion*) under the aegis of the LFP (*Ligue du Football Professionnel*).

League overall in the red nearly every year since 2000 (Table 5). Clubs in the red had a bigger cumulative deficit than aggregate positive operating income of those clubs in the black.

At club level, the occurrences of deficits are numerous (39% of all operating incomes, 2004 to 2013), scattered across 26 clubs (Table 6) though basically concentrated on a few badly-governed (poorly-managed) clubs: PSG, Nantes, Lens, Lille, Marseille and Rennes.

Ligue 1 aggregate balance sheet shows a growing debt (Table 7). «Other debts», typical of SBC, were representing between 82% (2004) and 85% (2013) of total debt while financial debts were below 20%.

Table 5: Cash balance and transfer fee balance in French professional football

€ million	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Cash balance											
Ligue 1	-35.9	-32.5	27.7	42,7	25.0	-14,7	-114,1	-46.1	-81.7	-17.6	-102.1
Ligue 2	-8.0	5.5	5.0	4,1	1,8	-18,9	-15,9	-18.9	-47.4	-21.3	9.5
Total	-43.9	-27.0	32.7	46,8	26,8	-33,6	-130.0	-65.0	-129.1	-25.6	-92.6
Transfer fee balance											
Ligue 1	17.9	3.0	14.7	31.7	58.8	41.9	-91.7	73.4	-38.9	-26.8	-184.5
Ligue 2	15.5	12.2	11.8	20.1	21.1	37.3	16.5	18.5	35.5	-58.1	22.5
Total	33.4	15.2	26.5	51.8	79.9	79.2	-75.2	91.9	-3.4	-84.9	-162

Source: LFP/DNCG.

Table 6: Occurrences of operational losses in French Ligue 1, 2004-2013
(€million)

Clubs	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13
AC Ajaccio										1.8
AJ Auxerre						7.7	4.7		16.4	
SC Bastia		1.9								
Bordeaux Gir.		1.3						7.0	14.3	7.7
Stade Brestois										2.2
SM Caen						0.5		1.6		
Grenoble Foot						5.4	3.0			
Havre AC						0.1				
Le Mans FC							2.4			
RC Lens		5.5	7.5		3.2		13.6	5.9		
LOSC Lille		2.0				0.3	1.1	5.9		3.1
FC Lorient						3.8				
Ol. Lyonnais	6.5									
Ol. Marseille		10.6					0.5	14.7	8.2	18.9
FC Metz			1.5							
AS Monaco					0.2			0.3		
AS Nancy							13.5		2.5	4.1
FC Nantes	6.5	9.7		3.9		0.1	35.4	35.1	28.0	27.9
OGC Nice				2.7			6.2	1.2	7.8	
Paris StGermain	31.0	17.8	13.5	19.0	12.3	5.4	21.9	0.2	5.5	3.5
Stade Rennais		6.1	2.4				2.5		2.4	0.7
FC Sochaux					5.9		11.0			
AS St Etienne						4.1	2.6			
RC Strasbourg			2.6							
Toulouse FC				0.3	2.1		0.2		0.8	
ValenciennesFC							10.9	2.8	4.3	

Source: LFP/DNCG

Table 7 : French Ligue 1 balance sheet (€million)

Ligue 1	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
Intangible fix. assets*	167.1	194.3	262.9	266.6	346.1	339.2	356.5	273.8	443.9	465.2	694.5
Other fixed assets	75.8	90.2	102.4	95.2	116.0	103.7	112.2	114.8	128.9	153.7	367.4
Circulating assets	265.6	274.3	266.1	339.1	369.4	355.3	348.2	363.0	321.1	351.1	502.1
Liquidities	92.5	108.9	187.9	191.9	168.2	149.5	112.4	173.5	114.3	142.6	172.9
Total Assets	601.0	668.7	819.3	892.8	999.7	947.7	929.3	925.1	1007.8	1112.6	1736.8
Own capital	139.4	111.7	159.6	208.6	213.4	265.6	189.0	183.7	143.2	167.5	225.3
Stockholders accounts	60.1	53.1	75.2	51.2	61.8	56.6	104.9	100.9	214.6	83.5	243.8
Provisions, risks	37.3	37.5	52.5	54.0	34.6	32.7	25.4	29.0	24.6	32.1	39.9
Financial debts	66.1	63.0	70.4	71.3	62.4	60.2	94.2	87.2	105.2	105.0	194.3
Other debts **	298.1	403.4	461.6	507.7	627.6	532.6	515.7	524.3	392.8	597.6	806.4
Total Liabilities	601.0	668.7	819.3	892.8	999.7	947.7	929.3	925.1	1007.8	1112.6	1736.8

* Players transfer fees not yet amortised.

** Payment arrears, tax and social contribution arrears.

Source: LFP/DNCG

Note that a club's payment arrears on transfer fees are overdue payables to another club so that most clubs are intertwinned through a chain of bad debts. The same situation across banks creates a so-called systemic risk of the whole banking system to collapse: the bankruptcy of any one club can jeopardise the financial stability of the whole football league.

New fashioned bail-outs have emerged (similar to English Premier League) in French football: by sugar-daddy investors in Nantes (W. Kita), PSG (Qatar Sports Investment), Monaco (D. Rybolovlev), Lens (H. Mammadov).

Finally, French football clubs use the (league-negotiated) TV rights revenues to bail them out (econometric testing in Andreff, 2007 & 2011) after overspending on payroll (wages) that they cannot recoup with revenues (namely when not successful in UEFA contests). Facilitates club's poor management.

6. Recommendations for hardening clubs' budget constraints

R1/ Put a halt on deficits and debts by appropriate incentives and a club governance reform.

R2/ Intensify sticks and carrots (a rewarding club financial ranking) to switch from poor to good management practices.

R3/ Investment by sugar daddies must be tightly regulated.

R4/ Financial accounts must be audited by an external independent (non-football-related professional auditors) body, as in any business/industry.

R5/ Impose on to European clubs an accounting transparency as regards revenues, financial deals, transfer fees, individual wages, payment arrears.

R6/ Very stringent enforcement of measures derived from R1 to R5.

R7/ A salary cap can slightly help, but is not the crux of the matter.

For opening the discussion:

Both French DNCG and UEFA FFP meet R1.

DNCG meets R5 and R2 (except the reward),misses R3, R4, R6, and R7.

FFP meets R3, R4, R2 (except the reward), misses R5, R6, and R7.