The Impact of Governance on European Football Leagues’ Competitiveness

Bastien Drut
Gaël Raballand
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Gaël Raballand23

Abstract

The sharp increase in TV broadcasting rights and the liberalization of the transfer market has completely reshaped the balance of power in European football, both within and between the different leagues. A trade-off has emerged with leagues whose teams perform well in the Champions League suffering financial inequality and clubs in financial difficulty, while those leagues which are less successful in the Champions League enjoy relative financial equality and less debt. The English, Italian and Spanish leagues are in the first category while the French and German leagues are in the second category. Based on interviews with several stakeholders, this paper demonstrates that this is mainly explained by the extent of financial regulation, which depends on leagues’ and clubs’ governance. It also discusses the role of UEFA and assesses the impact of the introduction of the financial fair-play rule.

Keywords: Ligue Française de Football, Deutsche Fußball Liga, football clubs, competitiveness, governance.

JEL Classification: L83.

1 Bastien Drut, University of Paris West Nanterre La Défense, EconomiX-CNRS, 200 Avenue de la République, Nanterre, 92001, France and Centre Emile Bernheim, Solvay Brussels School of Economics and Management, Université Libre de Bruxelles, Av. F.D. Roosevelt, 50, CP 145/1, 1050, Brussels, Belgium. E-mail: bastien.drut@gmail.com
2 Gael Raballand, Associate researcher, Institut Choiseul, Paris, e-mail: graballand@yahoo.com.
3 The authors would like to thank Boris Helleu and Dirk Meyer-Bosse and all the interviewed people for their help, Alan Whitworth for comments and edits. This paper was presented at the Second European Conference of Sport Economics in Cologne.
1. Introduction

The current financial crisis and Portsmouth’s placement into administration is increasingly worrying the management of the European professional football leagues. The accumulated debts of some of the biggest European clubs amount to several billion Euro. Many clubs are threatened with bankruptcy. The Premier League is particularly subject to criticism (Conn 2010.1).

The sharp increase of TV broadcasting rights and the liberalization of the transfer market (Ericson, 2000) has reshaped the balance of power, both within and between leagues. An opposition has emerged between leagues whose teams perform well in the Champions League but suffer from inequality and financial difficulties, and leagues which are less successful in the Champions League but enjoy relative financial equality and less debt. Focusing on the five big European leagues, the English, Italian and Spanish leagues come in the first category whereas the French and German leagues fall in the second. The sporting success of the former leagues is linked to debt accumulation: clubs borrow to acquire talented players and to pay them high wages. Gay de Liebana y Saludas (2009) estimates the aggregate debt of the twenty Spanish elite clubs at 3.5 billion Euro.

It is well known that the extent of financial regulation explains why Germany and France lag behind England, Italy and Spain. However, few articles explain why financial regulation has emerged in Germany and France and not in the other major leagues\(^4\). Based on interviews with major stakeholders in France and Germany\(^5\), this paper explains how league and club governance

\(^4\) An attempt was done in Andreff (2007a) for the French league. Franck (2010) focuses on Germany to explain the German league competitiveness difficulties.

\(^5\) Representatives from the football leagues, ministry of sport and media were interviewed with a semi-structured approach.
2. Leagues’ Competitiveness

In this section we assess the sporting performance of the five major leagues (England, France, Germany, Italy and Spain). One of the best indicators is the UEFA league ranking because it measures the outcome of games between these leagues’ clubs. It is computed from the results of the leagues’ representatives in the Champions League and Europa League (formerly UEFA Cup) and is used to determine the number of teams (from a league) competing in both Cups in the next season. Figure 1 indicates the trend in rankings since 1994.
The most significant change has been the strong rise of the English Premier League. Ranked seventh in 1996 and 1997, it has constantly improved and is now ranked first. The performance of Spanish clubs has also improved significantly. The Italian Calcio has sustained a high level of competitiveness. The German and French leagues have been ranked below the three other major leagues during most of this period.

The same conclusions can be drawn when analyzing the number of quarter-finalists in the Champions League since 1994 (Figure 2). English clubs have represented almost a third of the quarter-finalists in the last ten years. Italian and Spanish clubs have been just behind, whereas French and German clubs have performed much worse. Moreover, England, Spain and Italy won 11 of the 13 last Champions Leagues. Since 1999, on average, only one out of eight quarter-finalists was not from a major league, illustrating their supremacy within Europe.

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6 It is worth noting that this British supremacy was rather similar in the late 70s and early 80s (Kuper and Szymanski, 2010).
One might conclude that the quality of French and German football players is lower than that of British or Spanish players, but this would be mistaken. There is approximately the same proportion of French and Spanish players in the poll electing the 11 best European players for the UEFA team of the year (Figure 3).

Many of the best French footballers play in England, Italy and Spain. With increased labor mobility at the European level following the Bosman ruling, the many of the best players leave their own league for a more attractive one (Ericson, 2000). Compared to England, Italy and Spain, the French and German leagues are less attractive for the superstars. Probably for this reason, France is the second largest source of emigrant footballers in Europe after Brazil (Poli, 2010).
England, Italy and Spain have better results in Europe but their national championships are far more unbalanced than in France and Germany (Andreff, 2009). Since 1992/1993, only four teams have won the title in England (Manchester United, Chelsea, Arsenal and Blackburn Rovers) while eight have won the French title (Figure 4). Except for one major club each (Olympique Lyonnais in France and Bayern München in Germany), both of which have won many titles, the championship is relatively unpredictable in France and Germany.
In conclusion, Spanish, Italian and above all English clubs enjoy a clear sporting superiority at the European level compared to their French and German counterparts. However, their national championships are also more unbalanced. These findings are linked to the financial situation of football clubs and therefore to the extent of financial regulation, since recurrent debts can be accumulated in some countries but not in others. The relationship between the wage bill and match results is extremely robust and has been documented extensively (Kuypers and Szymanski, 1999). For these reasons, we analyze in the next section the financial performance of the major leagues.

3. Leagues’ Financial Performance

In the last decade the revenues of the five major football leagues dramatically increased (see Figure 5), reaching 7.9 billion Euro for the season 2008/2009 (a 90% rise since the season
1999/2000). They overshadow other European leagues such as Netherlands, Belgium and Scotland. The sharpest increase took place in the Bundesliga (130% rise) and the smallest in Seria A (57% rise). The English Premier League strongly dominates the other leagues while the French Ligue 1 lags behind.

While the revenue structure differs somewhat among the leagues, the surge in TV broadcasting rights explains the bulk of the boom. According to Deloitte (2010), on average they now account for 31% (Bundesliga) to 60% (Seria A) of total club revenues. However, the absolute sums depend on each league’s attractiveness: TV channels spend more to broadcast games with superstars. This phenomenon is clearly self-reinforcing, since leagues with higher revenues are able to attract superstars because of high wages. This is a key explanation of the league ranking presented in Section 2.

**Figure 5: Major leagues’ revenues from 1999/2000 to 2008/2009**

![Graph showing revenue trends](source: Deloitte (2010).)
However, there are large inequalities within leagues. The ratio of the 4 largest club budgets to the 4 weakest (Figure 6) is highest in Spain (6) and Italy (4.2), where TV broadcasting rights are sold individually. By comparison, the French and German leagues do not have extreme budget inequalities, while the Premier League stands in the middle. The way TV broadcasting rights are shared plays a major role in the competitive balance at the national level.

In aggregate terms, German, Italian and Spanish clubs benefit from roughly the same revenues (Figure 5), but the breakdown is far more unbalanced in Italy and in Spain than in Germany. This helps explain why top clubs in Italy and Spain are more competitive at the European level than in Germany.

**Figure 6: Ratio of the 4 largest to the 4 smallest revenues in the five major leagues, 2008**

![Graph showing the ratio of the 4 largest to the 4 smallest revenues in the five major leagues, 2008. The ratio is highest in Spain (6) and Italy (4.2), with France and Germany having a ratio closer to 1.](image)

*Data source: UEFA (2010).*

While clubs’ revenues are obviously crucial to sporting performance, the extent of spending is even more important. This depends on the preferences of club owners. In Europe it is generally recognised that most club owners are more interested in playing success than in
profit (Késenne, 1996, 2000, 2006; Garcia-del-Barro and Szymanski, 2009). In recent years, most major clubs have spent most of their revenue to hire the best players (Franck, 2010); and many have borrowed heavily to finance what may be considered overspending on wages and players’ transfers. Figure 7 displays the aggregate operational profit, while Figure 8 shows net profits.

**Figure 7**: Aggregate operating profits (in hundreds of million of Euro), 1999/2000 to 2008/2009

*Source: Deloitte (2010). Spanish data are not available.*
Operating profits have been consistently positive in the last decade for English and German clubs and always negative for Italian clubs. It has fluctuated around zero for French clubs.

However, the picture differs when we look at net profits, i.e. after taking into account the trading of players. The gap between operating profit and pre-tax profit is more important in England because the value of players’ contracts in the balance sheet is much higher\(^7\). The cumulative losses of Premier League clubs have exceeded 2 billion Euro in the last decade. Italian clubs have also recorded huge losses. By contrast, German clubs have been quite profitable while French clubs have on average broken even over the last decade. For the season 2008-09, A.T. Kearney (2010) estimated that clubs’ return on assets was 2% in Germany, 1% in France, -5% in England, -7% in Spain and -12% in Italy.

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\(^7\) Players’ contracts assets in the balance sheet accounted for 1,239 million Euros in England for the season 2008, 985 in Spain, 821 in Italy, 355 in France and 341 in Germany (UEFA, 2010).
So a large part of sporting success by British, Italian and Spanish clubs can be explained by rising debt, along with sponsorship from wealthy individuals. French and German clubs perform better financially than English, Spanish and Italian clubs, but worse on the field.

This can be translated into a win maximization model without constraint for English, Spanish and Italian clubs. However, the model is different for French and German clubs which are, de facto, not allowed to create recurrent debts.

The next section shows why clubs’ economic model differs in the two countries.

4. The Impact of Governance on Leagues’ Competitiveness

The Common Pattern of the German and French Leagues

Although league and club governance differs in a number of respects in France and Germany, the main common feature is that both leagues exert financial control over clubs. Financial control deters clubs’ owners from adopting a win maximization model, which may (but not necessarily) bring profits but at the expense of competitiveness in the Champions league.

In theory, the Italian and German models for financial regulation are relatively similar (see Table 1). However, only the German model enables to limit overspending and create indebtedness. The Spanish system places little emphasis on financial regulation, while the English approach appears relatively ineffective with the FA theoretically in charge of enforcing financial regulation. At the other extreme, the France is the only country where financial regulation is effectively enforced (which does not mean that clubs do not go in to the red).
Table 1: Financial Regulation and its Enforcement in the Five Major Leagues

<table>
<thead>
<tr>
<th>Country</th>
<th>Existence of financial criteria in the licensing system</th>
<th>Which institution is in charge of monitoring financial criteria?</th>
<th>Has any major club been sanctioned on this ground?</th>
</tr>
</thead>
<tbody>
<tr>
<td>France</td>
<td>Yes</td>
<td>League</td>
<td>Yes</td>
</tr>
<tr>
<td>Germany</td>
<td>Yes</td>
<td>League</td>
<td>No</td>
</tr>
<tr>
<td>England</td>
<td>Yes</td>
<td>Federation</td>
<td>No</td>
</tr>
<tr>
<td>Italy</td>
<td>Yes</td>
<td>League</td>
<td>No</td>
</tr>
<tr>
<td>Spain</td>
<td>No</td>
<td>N/a</td>
<td>No</td>
</tr>
</tbody>
</table>

In France, the “Direction Nationale du Contrôle de Gestion” (DNCG), the financial watchdog of the professional football clubs, may impose recruitment limits and even relegation to a lower division for clubs with a recurrent deficit. This gives clubs a strong incentive to avoid deficits and borrowing (Gouguet and Primault, 2006) since going to Ligue 2 means on average an 80% loss of revenue.

Three main reasons may explain why the DNCG has become the most important tool to limit clubs’ debts: a. the French attitude towards professionalism, which has given power to amateurs and unions to run the League governing body and limits club owners’ power to adopt a win maximization approach, b. strong involvement of public authorities (including local authorities), which pushed for financial regulation, after they stopped financing football clubs, c. the ruling of the supreme administrative court, the Conseil d’Etat, which confirmed the DNCG decision to relegate Bordeaux in 1991 (Revue Juridique et Economique du Sport, 1991 and Gouguet and Primault, 2006).

However, German and French governance contexts are different which explains some of the differences in league management and how leagues instill changes.
Governance of the French league

Although the first professional league dates to the early 1930s in France, professional football was severely criticized for several decades and almost disappeared during WWII.

Aversion to professionalism in France could explain why the ruling institution of the Ligue Française de Football, the LFP board, is so unusual among the major leagues. The LFP board is mainly driven by unions’ representatives, whereas club owners (Ligue 1 and 2) are in a minority. Of the 25 seats on the board, owners have only 11 (to which one seat can be added\(^8\), see Figure 9).

Figure 9: LFP Board Members

Players’ unions *de facto* have been ruling the LFP following the crisis in French football in the early 1970s. In 1969 the predecessor of the LFP, the Group of Professional Clubs, tried to limit the power of players in contracts/transfers. Eventually, in December 1972 players went on strike for several weeks in protest at these limitations.

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\(^8\) The representative from the Union of Professional Clubs.
Following public mediation games resumed, but club owners had to accept most of the players unions’ demands in the *Sport Charter* (1973) and started to manage the league with unions’ representatives. This can be explained by the fact that, contrary to most sectors in France, 70-80% of professional players are unionized, which makes the main union very representative. A system of common management of the league was established called the “social dialogue”.

It is also worth noting that both referees’ representatives and players sit on committees where, for instance, sanctions are adopted. The multiplicity of narrow interests sometimes makes achieving a consensus difficult.

The major role of unions in managing the LFP also explains why the mandate of the LFP is broader than in any other major league\(^9\). A major part of LFP activities concerns labor law: the LFP checks and authorizes contracts\(^10\) and also mediates between club owners and players when disputes arise. Commercial activities are just one of the LFP’s activities among others,\(^11\) whereas in the DFL, *Premier League and Calcio* models, they are the *raison d’être* for these institutions.

Even more interestingly, the Government set this model in stone with a decree on professional leagues, and included the model in the sports code (2002)\(^12\). Therefore, in France, there is a rigid framework for any professional league, and players’ unions play a major role in decision making.

Financial regulation in France also derives from the importance attached to financial equality and redistribution between clubs since WWII, but also from public intervention. In the

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\(^9\) The only league with major responsibilities in supervising players’ contracts is the Liga.

\(^10\) 6000 documents a year are checked and issued. ISO 9001 was issued to the legal department of the LFP for its involvement in clubs contracting of players.

\(^11\) Financial regulation is another important activity of the LFP, along with disciplinary procedures and managing referees.

\(^12\) Article R132-4.
1970s, several clubs went bankrupt and local councils had to do bail them out. In a context of increased legal mandates following decentralization (in 1982-83) and limited revenues, local councils became increasingly reluctant to finance excessive spending. Therefore, a consensus was found and the DNCG was established in 1984. It took several years for it to gain credibility but, following the relegation of Bordeaux and Marseille in the early 1990s, a strong signal was sent and a wide consensus seems to exist in France on the need for financial regulation (as well as for collective bargaining of TV rights and the importance of redistributing TV rights to small clubs and to amateur institutions)\textsuperscript{13}.

This was given legal power when the supreme administrative court in France, the \textit{Conseil d'Etat}, confirmed that the sanction to relegate Bordeaux to Ligue 2 was legitimate and not disproportionate (Revue Juridique et Économique du Sport, 1991). Therefore, without enthusiasm, club owners had to respect DNCG rules and the win maximization model was not an option anymore in France.

\textbf{Governance of the German league}

Licensing requirements for German clubs are specified in the DFL (\textit{Deutsche Fußball Liga}) status. Among the requirements for a license, there is a financial criterion in the § 8 and annexes VII and IX of the status. A club has to submit the following documents by 15 March each year: balance sheet, profit and loss statement and profit and loss forecast for the next season. All documents have to be audited by an independent auditor and are then examined by the DFL.

\textsuperscript{13} It is worth noting that neither in France or Germany is financial regulation extremely rigid. It does not guarantee that clubs will not face financial difficulties (See Andreff 2007b for the case of France and Dietl and Franck for Germany).
The German licensing process dates from the late 1960s. Financial requirements have become increasingly rigid over time.\textsuperscript{14} The system is illustrated in Figure 10.

**Figure 10 : The German Licensing System Process**

![The German Licensing System Process](image)

Source: Müller (2010).

According to Frick and Prinz (2006), the financial criterion prevents clubs from overspending on wages/transfers. Dietl and Franck (2007) highlight the fact that in practice the licensing system is weak and may lead to creative accounting to inflate assets and hide liabilities. Nevertheless, the extent of financial problems in Germany is not comparable to that of English or Italian clubs.

Financial regulation in Germany can partly be explained by the strong role of amateurs in professional football (albeit to a lesser extent than in France) and the aversion of clubs to takeovers by financiers. Indeed, the licensing system was introduced by the national football

\footnotesize{\textsuperscript{14} Not to the same extent as in France. There is no independent body from the DFL to impose sanctions.}
association (DFB) in cooperation with the clubs. Moreover, associations (*Verein* in German) holds 50% plus one voting rights of any football club company (*Kapitalgesellschaft*), which limits the power of clubs owners (Dietl and Franck 2007)\(^{15}\). Interestingly, associations are managed by representatives elected by members.

One of the main problems of this peculiar governance is that, because associations are non-profit organizations, there is no incentive for them to make profits and reinvest operational gains. However, despite their potential weaknesses, Franck (2010) argues that a *verein*-dominated club is unlikely to accumulate debts over a long period (especially since its indebtedness capacity is low).

**The Common Pattern of the English, Spanish and Italian Leagues**

In England, Spain and Italy, there are no strict financial control rules enforced by leagues (even though the football association or regulatory authority may be in charge of such controls)\(^{16}\). Football clubs operate as normal commercial companies, free to borrow, which explains the above financial inequality and competitive imbalance.

Why has financial regulation not emerged in these three countries? Part of the answer lies in the fact that, contrary to France, the State has not played a major role in football regulation in these countries\(^ {17}\).

In England, for instance, in 2003 the Football Association (FA) set up a Financial Advisory Committee with a mandate to monitor the overall financial health of clubs. A Football Regulatory Authority was created in 2005 to enforce clubs’ compliance with financial

\(^{15}\) The notable exceptions are Wolfsburg, owned by Volkswagen, and Leverkusen, owned by Bayer.

\(^{16}\) It is also worth noting that, except for Spain, these leagues have a limited commercial mandate.

\(^{17}\) Growing concerns by politicians in England could change the situation in future. Andy Burnham, former Secretary of State for Culture, Media & Sport, asked the FA and the Premier League to review several rules related to financial regulation in England (Walters and Hamill 2008).
regulations (Walters and Hamil, 2008). Michie (2006) shows how ineffective the FA’s monitoring is. FA rule 34 imposes a maximum dividend payout and outlaws payments to club directors. However, this rule has completely been circumvented and the FA is unable to enforce it. In both France and Germany, despite alleged conflicts of interest, financial regulation is ensured by the leagues themselves. Among the big leagues, there is no example of a football association implementing such controls itself. In England, this can be due to the fact that the FA draws most of its revenues from football leagues and is not in a position to impose rules on large clubs.

When State regulation is not possible the German model, with amateurs/non-profit organizations having a majority of club ownership, seems to limit overspending\(^\text{18}\). In a similar vein Oughton (2005) and others have tried to promote the establishment of a bottom-up approach with the introduction of “supporters’ trusts” (ST) to give supporters voice, and improve governance and corporate social responsibility. They advocate including ST representatives on club boards\(^\text{19}\). This would certainly enhance club governance, but may have limited impact on overspending because – unlike the German case - the club owner remains the main person able to decide how much to spend.

Another reason why financial regulation is so weak in England, Spain and Italy could be the fact that 2 or 3 powerful clubs\(^\text{20}\) have dominated championships and captured power in the leagues. Clubs such as Real Madrid in Spain (backed by the Spanish royal family), Juventus Turin (the Agnelli family), AC Milan (Silvio Berlusconi) are effectively in a situation of moral hazard due to the assurance that they will be bailed out if their debts accumulate; they are not

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\(^{18}\) To a certain extent, it is also the Barcelona model with “socios”.
\(^{19}\) Most Premier League clubs now have STs.
\(^{20}\) Manchester United, Liverpool, Arsenal (and recently Chelsea) in England; Real Madrid and Barcelona in Spain (which have always been in the first Liga since its creation in 1930); and Juventus Turin, AC Milan and Inter Milan in Italy.
therefore in favor of financial regulation, which would ultimately limit their sporting dominance (Aglietta et al, 2008).

Since pressure for financial control has been weak in England, Spain and Italy in recent years, UEFA, under the leadership of its president, Michel Platini, has become increasingly involved in trying to limit indebtedness and hence financial inequality (at least for the clubs involved in UEFA contests). But can it be succeed in the current context?

5. Can UEFA help limit financial inequality?

UEFA was founded in 1954 by twenty national associations. Today it comprises more than fifty associations.

Aware of the impact of large clubs’ overspending on UEFA cup results, UEFA has developed a mechanism (through the licensing system) to limit the indebtedness of large clubs and the gap between the budgets of large and small clubs. This is expected to lead to more unpredictable results and thereby increase the attractiveness of UEFA competitions.

The "financial fair play", as it is called, will prohibit the participation of indebted clubs in European competitions in future21. The rules are designed to move clubs towards break even from the season 2011-12. Clubs will be allowed to record maximum total losses over the following three years of €45m, termed an “acceptable deviation” computed on a three-year period22. From 2014 to 2017, the overall permitted loss will fall to €30m. After that, UEFA hopes that clubs will genuinely break even23.

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21 It is based on the German licensing system concept.
22 Clubs can be subsidized by an owner but only if he/she invests the money permanently in return for shares, not by lending it. This is only allowed if such excess is entirely covered by contributions from equity participants (Müller 2010).
23 Infrastructure costs, youth development activities and community scheme expenses are not included in expenses for the computation of break-even (Müller 2010).
Platini described the need to staunch overspending as "a question of survival for our sport", adding: "the clubs will comply," "or they will not play." According to Platini, "all the clubs were in favor. The biggest clubs were in favor because their owners do not want to keep overspending. And the smaller clubs realized it was good for them, too." (Conn, 2010.2).

Several clubs, particularly English clubs, have yet to comply. In the Premier League, Chelsea, Manchester City, Liverpool and Manchester United have all sustained substantial losses in recent years24.

The Premier League argued that clubs should be allowed to be continually subsidized by owners. However, it was overruled, with UEFA insisting it wanted to steer clubs across Europe towards a more sustainable existence. A Premier League spokesman stated that: "we envisage a difficult period of adjustment for our member clubs who play, or aspire to play, in European competitions" (Conn 2010.2). UEFA’s general-secretary, Gianni Infantino, explained that if Manchester United or Manchester City qualify for the Champions League as a result of vast overspending, they will ultimately be excluded from European competitions, although "there may be intermediate measures" in the short term. "We would have to ask why, maybe there would be a warning first, but certainly, we would have to bar clubs in breach of the rules from playing in the Champions League or the Europa League. Otherwise, we lose all credibility."

Indeed, this reform is credible only to the extent that some clubs would be excluded from the contest. One of the first victims of the licensing system has been the exclusion of the Spanish club Real Mallorca from the 2010/2011 Europa League because of a debt accounting for 85 million euro (30 million of which is due to the public treasury).

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24 Three-quarters of Premier League clubs will need to reduce significantly their spending on players’ wages if they are to qualify for European competitions (Conn 2010.2).
However, is it realistic to think that UEFA is going to exclude Chelsea, Manchester and Real Madrid from the Champions League for several years? Based on the DNCG, UEFA probably needs to exclude some major clubs and then have its decision confirmed by the European Court of Justice. If this is not possible, this measure may seem more symbolic than truly effective (Raballand and Drut 2010).

Moreover, it will be difficult to take such bold decisions since in the last decade UEFA has enjoyed major commercial success with the Champions League and the boom in TV broadcasting rights (see Figure 11). UEFA currently generates large revenues through the Champions League, of which a substantial part is retained.

UEFA faces a trade-off, therefore: either it sanctions large clubs, with the risk of losing revenues and creating major tensions with these clubs, or it retains the present system at the risk of growing discontent from fans over predictable results and the possible bankruptcy of some clubs. UEFA runs the risk that the largest clubs will create their own competition if financial control is enforced (which was a major threat in the early 2000s). It is more financially attractive for UEFA to have a final between Barcelona and Chelsea than between Donetsk and Borisov, but a Barcelona - Chelsea final every year may have a negative impact on the competition in the long term (in terms of reputation and audience)).
6. Conclusion

Based on multiple interviews of stakeholders in France and Germany, this paper explains how league and club governance in France and Germany has enabled financial regulation to emerge and therefore a second “model” to exist. It highlights the key role played by the State and other institutional factors. There is currently a trade-off between leagues enjoying playing success in the Champions League, but also financial inequality and clubs in the red (England, Spain and Italy), and leagues with weaker Champions League results but relative financial equality and limited debt (Germany and France).

In the last five years, the gap between the leagues and clubs’ vulnerability has been growing to the point that the EU and UEFA are now trying to regulate and limit overspending. However, how realistic/likely is it that UEFA will impose meaningful sanctions on the most famous clubs in Europe? The answer is critical. If UEFA goes ahead and implements recent
measures, a degree of equalization of results could be seen (although the dominance of large clubs will not disappear). If not, the gap between a handful of big European clubs and the rest will probably continue to grow.
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