

# The economic arguments supporting a competition law challenge to the transfer system

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## 1. Introduction

Professional footballers enter into employment contracts with football clubs. In addition to the standard employment rules that apply in any jurisdiction there exist additional restraints which constrain, among others, the rights and freedoms of players. These restraints are imposed by the governing bodies of sport. The governing bodies, both national and international, regulate employment conditions, most notably through the player registration system. Players have no choice but to accept the jurisdiction of the governing bodies if they wish to play professional football, and therefore are effectively confronted by a cartel of federations. These federations are, in turn, to a large extent dominated by the clubs that employ the players.

The rationale for the employment rules applied to football markets have been examined by the courts on several occasions, most notably in the Bosman Case at the European Court of Justice. Following that judgment FIFA and UEFA negotiated with the European Commission a set of regulations relating to transfers that are currently enshrined in the FIFA regulations on the status and transfer of players.

These rules significantly constrain the freedom of action of players and limit their freedom of movement, by, inter alia

- Limiting the ability of players to obtain speedy redress when faced with unilateral breach by clubs (e.g. non-payment of wages)
- Limiting the freedom of players to seek alternative employment when they believe that they are being treated unfairly or unreasonably by their employer (e.g. due to the scope of the protected period)
- Limiting competition in the market to an elite group of dominant clubs that are able to finance the huge transfer fees for the top players and drive up the cost of talent in the market.
- Limiting the freedom of players to move to a different club to specific times of year (the transfer window)
- Imposing significant and uncertain penalties on players that seek to move without the consent of his club while under contract, both in terms of punitive compensation payments and sporting sanctions

These constraints also restrict the operation of the market for football players in Europe. Even when players are technically protected by regulations, there are asymmetries in enforcement and significant procedural delays which effectively deprive players of their rights.

The main arguments typically advanced in support of these restraints are

- Maintenance of contractual (employment) stability
- Promotion of solidarity (redistribution of resources)

- Promotion of competitive balance (ensuring competitors have a reasonable prospect of winning)
- Ensuring stability of championships and competitions
- Ensuring stability of clubs

The intention behind the rules of the transfer system were to balance the interests of players and to protect their economic interests while maintaining the competitiveness of clubs.<sup>1</sup>

This paper argues that the transfer system as it currently operates fails to balance the interests of the players with the other purposes of the system. Players currently face significant limits when offering their services, since the scale of transfer fees demanded can restrict the number of possible buyers in the market. Moreover, the consequences of breach of contract (a right accepted with restraints within the transfer system) can be so severe that they effectively represent an insurmountable barrier to entry in the market. Moreover, the uncertainty surrounding the interpretation of the rules further inhibits the proper functioning of the market for players.

This paper shows that either these restraints are failing to achieve their stated aims, and may even be working against them, or that a less restrictive alternative exists who could achieve the stated goal without infringing on player rights to the extent that the existing regulations do.

It argues that the operation of the current transfer system represents an abuse of dominance. The transfer system creates a barrier to entry for clubs that wish to compete with the dominant group. As such, the transfer rules tend to restrain competition between clubs rather than promote it, does little to support competitive balance, solidarity or club stability.

The operation of these rules represent a violation of EU competition law. From the perspective of Art. 101 TFEU, the governing bodies operating through FIFA represent a cartel which, operating under the rules of FIFA<sup>2</sup>, imposes overbroad restraints on competition. In particular it is argued below that the rules currently operate primarily for the benefit of the largest clubs that dominate competition in Europe.

From the perspective of Article 102 TFEU, both FIFA, as an association of national governing bodies, and the largest clubs, which exert enormous influence over those governing bodies, may be seen as collectively dominant in the European football markets. The transfer regulations, given the way that they operate as described in this paper, represent an abuse of a dominant position.

## 2. The evolution of the player transfer system

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<sup>1</sup> "In 2001, in the context of the pursuit of a case concerning alleged infringements of EC competition law and after discussions with the Commission, football authorities undertook to revise FIFA Regulations on international football transfers, based on compensation for training costs incurred by sports clubs, the creation of transfer periods, the protection of school education of underage players, and guaranteed access to national courts. The Commission considers such a system to constitute an example of good practice *that ensures a competitive equilibrium between sport clubs while taking into account the requirements of EU law.*" (Italics added). European Commission (2007) White Paper on Sport, p15. The requirements of EU law in this case refer primarily to the economic right of players to free movement and to sell their services in a competitive market.

<sup>2</sup> FIFA Regulations on the Status and Transfer of Players

The registration system in football goes back to 1890.<sup>3</sup> The system was imposed on the players by the Football League in England, at a time when employee rights were less well protected than they are today. The old retain and transfer system placed ownership of the player's registration with his club, thus endowing the club with all the economic power over the player's future. This system developed in a world where clubs could collectively fix a maximum wage for players and ban women from participation in organized football altogether.

The transfer system in England was first dented by the Eastham judgment in 1963 which entitled the player to leave once his contract was ended. But it was the Bosman judgment of 1995 which led to the biggest reform of the transfer system. The Bosman judgment confirmed that under EU law a club was not entitled to demand a transfer fee for a player that was no longer under contract.

In 1998 the European Commission issued a statement of objections concerning the transfer of players, suggesting that the existing rules contravened Article 85 (now Article 101) TFEU, and that the regulations prevented the free movement of workers in the EEA. There followed negotiations involving the European Commission, FIFA, UEFA, FIFPro, and others. The negotiations concluded with an agreement between the Commission and FIFA which formed the basis of the FIFA Regulations on the Transfer and Status of Players first issued in 2001 and subsequently revised.

The principal elements of the regulatory system relating to the market for professional football players, as explained in the FIFA regulations for the status and transfer of players (2012), require that

- Every player must be registered with a national association either as an amateur or a professional
- Contracts may only be terminated on the expiry of the contract or by mutual agreement
- Breach of contract within the protected period of the contract (the first three years if under 28 and the first two years otherwise) without just cause or sporting just cause must be compensated and in addition sporting sanctions should be applied. If a contract is renewed the protected period starts again.
- Outside of the protected period a player is permitted to breach unilaterally subject to payment of compensation – see Webster and Matuzalem below
- Minimum contract length is the end of the current season, maximum contract length is five years (3 years for players under 18)
- Training compensation is payable in the case of transfers of players under 23. When any transfer occurs before a contract has expired solidarity payments are due to any club that has trained the player
- Player trading restricted to specific windows amounting to no more than 16 weeks of the year in total
- International disputes are to be settled by the FIFA DRC, without prejudice of the right to a hearing before a civil court
- A player cannot enter contract negotiations with another club until six months before the end of his current contract, and another club cannot enter into negotiations with a player unless his

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<sup>3</sup> See Lewis and Taylor (eds) Sport: Law and Practice (3<sup>rd</sup> edition), p1480. A similar system had already been adopted by baseball's National League in the USA in 1879.

current club is notified in writing.

### **3. The Economic impact on players of restraints in the player market**

These regulations significantly restrict the economic opportunities of players:

(i) Transfer fees

The payment of a transfer fee from one club to another acts like a tax on employment- it reduces the attractiveness of the player to potential employers. Like any tax, the transfer fee not only reduces the wage offer that the player receives, but also makes it less likely that he will receive an offer. Taxes are by their nature distortionary- they cause individuals to make decisions other than those they would freely choose to make. The incidence of the tax falls almost entirely on the player, given that the player would otherwise be paid a higher wage. Thus even if the transfer system is rationalized on the basis of public policy (and below it is argued that the system currently operates in a way that cannot be justified by public policy) it remains the case the players are essentially paying disproportionately for the policy..

(ii) Compensation for training and solidarity payments

The requirement to provide compensation for training places a particular burden in the case of younger players. This acts like an additional tax on the mobility of younger players. It pushes down the amount buying clubs will be willing to offer and limits freedom of movement. To the extent that compensation payments are incorporated even when a player moves to a second or third clubs limits mobility yet further.

(iii) The Protected Period

The protected period limits the economic opportunities of players by raising the cost of mobility of the player. The requirement to pay compensation discourages potential employers, while the threat of sporting sanctions acts a significant deterrent, especially since the player will not know what the penalties might be. This significantly constrains the player's ability to realize his earnings potential and limits freedom of movement.

(iv) Transfers outside the Protected Period

Outside of the protected the player is still required to pay compensation for unilateral breach without just cause or sporting just cause, as highlighted in the Webster and Matuzalem cases. In the latter case the size of the compensation was so large (equal to ten years of salary) as to be punitive. The compensation bore no relation to the economic harm caused by the breach.

(v) The Transfer window

Any restriction of the period during which players are allowed to move between clubs limits the economic opportunities of the players and limits their freedom of movement. The current windows are limited to a maximum of 16 weeks (one period of up to twelve weeks and another of up to four weeks), significantly limiting the opportunities of players to move clubs. This restricts potential bidders for the services of players, limiting their freedom of movement, reduces employment opportunities, and pushes down the wage that a potential employer might be willing to pay, given the restriction on potential alternatives.

(vi) The Dispute Resolution System

The process for seeking redress within the transfer regulations is slow and cumbersome. In the event that a player has not been paid he is not entitled to terminate the contract for just cause (and move to another club) until several months have passed. The FIFA Guidelines specifically state that “a few weeks’ delay in paying a salary” does not constitute just cause and gives an example of three months as an example of just cause.<sup>4</sup> Typically a player would need to establish just cause through the FIFA Dispute Resolution Chamber (DRC), a process which might take several months, with the further possibility of an appeal to the Court of Arbitration for Sport (CAS). Thus a player might be without pay for an extended period of time and uncertain as to his status, making it difficult for him to find alternative employment.

#### 4. Harms caused by the current transfer system

As currently applied the transfer system imposes significant burdens on players. A 2012 study by Fifpro of player contracts in 12 countries (including six EU member states) identified a number of hardships faced by players that are in whole or in part attributable rooted in the present transfer system. Non-payment of salaries represented one of the biggest hardships that players faced. Of over 3000 players surveyed, 42% said that they did not receive their salaries on time. In one third of the cases of delayed payment, these delays lasted for more than three months. Thus in the majority of cases the player would not be entitled to claim just cause in terminating their contract. Thus while Article 13 of the FIFA regulations is entitled “Respect of Contract”, players have in many cases no redress even when the club is manifestly not respecting the contract. The situation tends to be worst in those cases where the player does not have an explicit labour contract with the club (for example, in cases where the player is self-employed).

Should players seek redress within the current system they find themselves facing harassment by the club, in an attempt to make the player refrain from taking action. 16% of players sampled had been forced to train alone, 12% stated that they were victims of violent acts and 10% claimed they had been subjected to bullying. Training alone was often accompanied by requiring the player to train at unsociable hours- e.g. at midnight. Sometimes these punishments follow a refusal to sign a new contract.

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<sup>4</sup> FIFA, Commentary On the Regulations for the Status and Transfer of Players, [http://www.fifa.com/mm/document/affederation/administration/51/56/07/transfer\\_commentary\\_06\\_en\\_1843.pdf](http://www.fifa.com/mm/document/affederation/administration/51/56/07/transfer_commentary_06_en_1843.pdf), p39

The employment relationship in football, as in many other businesses, is asymmetric in that the club is more powerful and has more resources than the player. These examples show how the club can exert pressure on the player in order to achieve its own ends while the player has few options when the club fails to respect the contract.

The present system is weighted against the players. The procedures for claiming redress are slow and cumbersome. Often a player has to go unpaid for significant period of time before he is able to sign a new contract. Damages payable to the payer may be substantially offset by the player's subsequent earnings. However, when compensation is assessed on a player who is in breach, that compensation is based on the current market value of the player, with no allowance for the replacements hired by the club.

Failure to pay wages and the economic hardships that it creates also risks the integrity of the system as unpaid players have limited incentives to show loyalty to their club.

The mechanisms by which the rules of the transfer system have been applied have significantly undermined the ability of players to find redress. Absent an agreement with his club to transfer to another club, the only alternative open to the player is unilateral breach. Given both the restrictive requirements associated with a finding of just cause or sporting just cause, the player is in danger of taking on a considerable personal risk. This risk is very hard to quantify in view of the decisions handed down by the Court of Arbitration for Sport (CAS) where most of the key cases have been arbitrated. This is exemplified by the case law, notably the well-known *Webster* and *Matuzalem* cases.<sup>5</sup>

The *Webster* case concerned a player for the Scottish club Heart of Midlothian F.C. who joined the club in 2001 and signed a new four year contract in 2003. The club sought to extend his contract in 2005 and 2006 but the player refused. As the relationship with the club deteriorated Webster decided upon unilateral breach and signed for the English club Wigan Athletic in August 2006. Webster's agent estimated the cost of buying out the remainder of Webster's contract with Hearts at £200,000, but Hearts took the case to the DRC which settled on compensation of £625,000 and suspended the player for two weeks. The case was appealed to CAS, with Hearts claiming £4 million as the rightful compensation. However, CAS actually reduced the compensation to £150,000, representing essentially the wages that would have been paid to the player had he played out his contract.

The *Matuzalem* case bore some significant similarities to *Webster*, but a very different decision was reached. *Matuzalem* signed a five-year contract with Ukrainian club FC Shakhtar Donetsk in 2004 for €1,2 million. Article 3.3 of the contract between *Matuzalem* and Shakhtar stated that: ". . . [I]n the case the Club receives a [€25 million or more] transfer offer . . . the Club undertakes to arrange the transfer." In June 2007, Italian club U.S. Città di Palermo Spa offered €7 million as a transfer fee for *Matuzalem* to Shakhtar, which it rejected. *Matuzalem* then decided upon unilateral breach and signed a three-year contract with Real Zaragoza of Spain for €1 million per season plus bonuses.

The case went to the DRC which ordered *Matuzalem* to pay €6.8 million in compensation to Shakhtar. This amount was made up by the contract's 'residual value' (€2,4 million), the non-amortized portion of the transfer fee paid by Shakhtar (€3.2 million) and €1.2 million.

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<sup>5</sup> For a review of these cases see e.g. Czarnota, Paul A. "FIFA Transfer Rules and Unilateral Termination without Just Cause." *Berkeley J. Ent. & Sports L.* 2 (2013): i.

This decision was then appealed to CAS which then increased the compensation payable to €11.9 million. The key difference with the Webster case is that on this occasion CAS argued that the club was entitled to a share of the player's value both in respect of the transfer fee paid on acquisition (the unamortized amount) and the value the club might reasonably have realized had the player not chosen unilateral breach. In Webster both of these elements were ignored.

CAS made it clear in this case that the reason for making an award this large was that "The purpose of art. 17 [of the FIFA Transfer Rules] is basically nothing else than to reinforce contractual stability, i.e. to strengthen the principle of *pacta sunt servanda* in the world of international football, by acting as deterrent against unilateral contractual breaches and terminations, be it breaches committed by a club or by a player".<sup>6</sup>

Moreover, subsequent decisions by CAS suggest that this interpretation, together with the implied heavy penalties for unilateral breach on the part of players, is now settled policy, in contrast to the Webster decision.<sup>7</sup> Effectively, the CAS has acted to deter unilateral breach in the name of one aspect of the 2001 compromise agreement, without, apparently, giving much weight to any other aspect of that agreement.

In the event both Matuzalem and the Real Zaragoza had been unable to pay the fine, and as a result FIFA imposed a global ban on Matuzalem's participation in football. The case was then referred to the Swiss Federal Supreme Court which ruled that the ban constituted an excessive restraint on Matuzalem's basic freedoms and was therefore inconsistent with Swiss public policy.<sup>8</sup>

## 5. Rationalization for the current transfer system

It is often argued that transfer systems in general and the current system in particular deliver significant sporting and economic benefits.<sup>9</sup> These alleged benefits include

- a. Stability of contract- clubs should be able to field stable teams, especially within a given season. This also enhances the integrity of competition
- b. Protection of minors – ensuring that the rules do not permit younger players to be traded
- c. Transparency – ensuring that money flows in football can be easily traced.
- d. Solidarity – the distribution of revenues from richer clubs to poorer clubs
- e. Competitive balance – ensuring that weaker clubs have the opportunity to compete without the fear that their best players will be bought by wealthier clubs

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<sup>6</sup> CAS 2008/A/1519 – FC Shakhtar Donetsk (Ukraine) v/ Mr. Matuzalem Francelino da Silva (Brazil) & Real Zaragoza SAD (Spain) & FIFA, paragraph 80.

<sup>7</sup> See e.g. Pearson, Geoff. "Sporting Justifications under EU Free Movement and Competition Law: The Case of the Football 'Transfer System'." *European Law Journal* 21.2 (2015): 220-238.

<sup>8</sup> See Lucien W. Valloni and Thilo Pachmann (2012) "Switzerland- The Landmark Matuzalem Case And Its Consequences On The FIFA Regulations" Downloaded from <http://www.mondaq.com/x/184712/Sport/The+Landmark+Matuzalem+Case+And+Its+Consequences+On+The+FIFA>

<sup>9</sup> See e.g. The Economics and Legal Aspects of the Transfer of Players, KEA/CDES Report, 2013, p3.

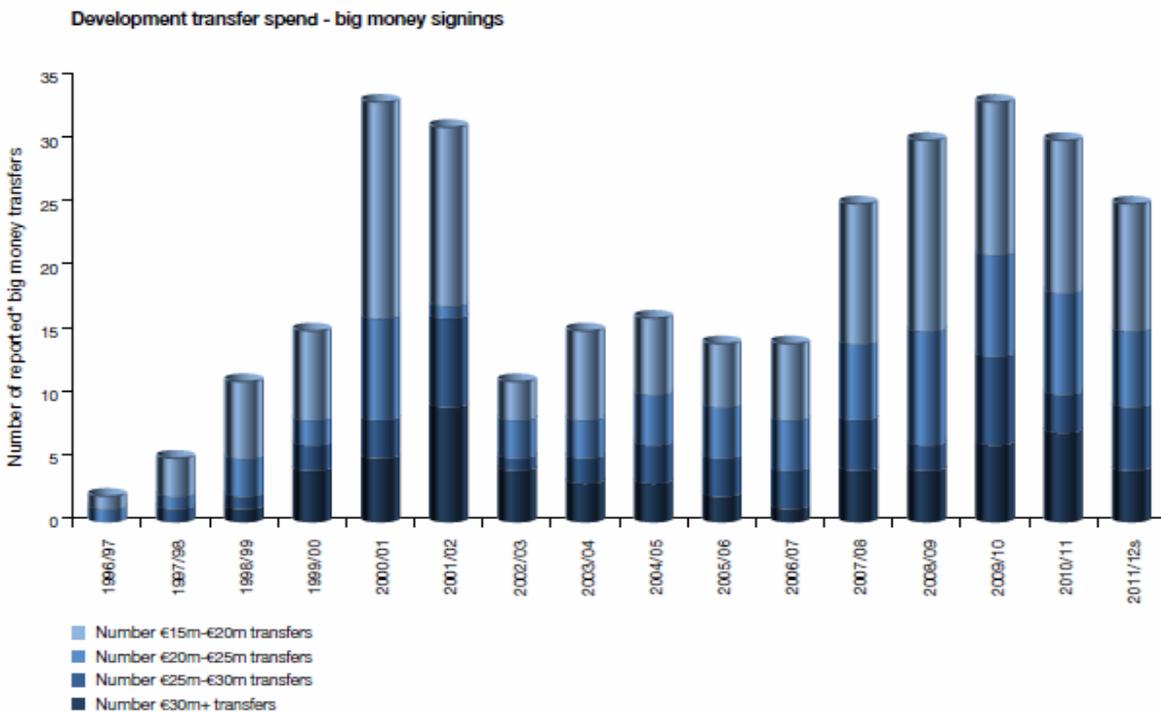
These benefits are then held to outweigh the costs of the acknowledged restraints on the labour market.

In assessing these rationalizations it is necessary to consider (a) the impact of removing the restriction entirely and (b) whether there exists a less restrictive alternative.

The first three rationalizations are essentially administrative concerns, which have to do both with the orderliness and integrity of the game, while the last two are intended to influence the outcome of competition in leagues and championships. Even if it is argued that policy makers would not choose to abandon these goals it remains the case that less restrictive alternatives are available.. Moreover, a system of transfer windows, which limits the available dates at which transfers can be made, need not be tied to the system for promoting solidarity among the clubs. There is a clear danger that the rights of players are sacrificed in the pursuit of achieving broader goals.

While the payment of fees is largely justified on solidarity and competitive balance arguments, the rationale for the payment of these fees has long troubled policy makers, particularly when they escalate rapidly. Figure 1 below shows the trend based on an analysis by UEFA of 400 big money transfers. It shows that the number of big money transfers was rising rapidly in the late 1990s and peaked in 2001 just at the time that the European Commission and FIFA reached agreement on principles that have been the foundation of the present system. However, in more recent years the number of these transactions has started to rise again.

**Figure 1: The trend in big money transfer spending 1996/97-2011/12**



Source: UEFA Club Licensing Benchmarking Report 2010, p100

The solidarity argument concerns compensation for clubs that train players and the redistribution of wealth from the more lucrative competitions to the grass roots. Two observations are relevant here. First, in reality most of the money generated by transfers circulates among the larger clubs and very little trickles down to the grass roots.

For example, Deloitte in the 2014 Annual Review of Football Finance (Databook p11) traced the flow of transfers in English football for the season 2012/13 within and between the four divisions. 72% of transfer payments by Premier League clubs to other English clubs stayed in the Premier League. Net payments of transfer fees to teams in the Championship were £32 million, about half the amount of money paid in solidarity payments by the Premier League. Below the Championship the amounts paid were even smaller- £7 million to the third tier and £1 million to the fourth. If no transfer fees were paid the lower tier clubs could be compensated by modest solidarity payments equal to less than ½% of Premier League revenues.

Analyzing transfer flows among clubs over time is relatively difficult given the large number of transactions and limited availability of verifiable data. However, UEFA's analysis of transfer spending and sales for selected countries over a five year period expressed relative to wage spending provides a useful indication (Table 1).

**Table 1: Transfer spending in the top national division as a percentage of wage spending**

National association	transfer spend as a % of wages 2006/07-2010/11	transfer sales as a % of wages 2006/07-2010/11	Net transfer spending as a % of wages 2006/07-2010/11
serbia	24	131	-107
croatia	22	106	-84
czech	18	67	-49
portugal	40	72	-32
sweden	6	27	-21
switzerland	11	26	-15
netherlands	27	41	-14
belgium	20	31	-11
norway	7	18	-11
denmark	17	27	-10
poland	17	23	-6
scotland	20	24	-4
france	31	34	-3
austria	10	12	-2
israel	16	17	-1
rumania	54	48	6
germany	27	19	8
greece	24	16	8
italy	41	31	10
russia	41	24	17
spain	47	30	17
ukraine	51	34	17
england	45	27	18
turkey	32	14	18

source: UEFA club licensing benchmarking report FY 2011, p81

This provides some idea about how dependent clubs from different countries are on net transfer fee income for funding their teams. There is some relationship between wealth and net spending, with the larger football nations (England, Germany, Italy, Spain) appearing in the bottom part of the list. But overall the pattern does not suggest a system in which redistribution through transfer fees plays a significant role. Many mid-sized nations (e.g. Poland and Scotland) generate relatively small amounts through player trading, while a country such as Germany spends relatively little. A few countries such as Serbia, Croatia and the Czech Republic rely heavily on transfer income, but this is as likely to reflect the poor state of the national leagues in those countries. Moreover, the drain of talent represented is likely to undermine any return to popularity with the fans in the short term.

The KEA/CDES study sponsored by the European Commission found that solidarity compensation directly linked to transfers accounts for only 1.84% of total agreed transfer fees within Europe.<sup>10</sup>

Secondly, using transfer payments as a means to promote solidarity is unlikely to be efficient. Lower division clubs collectively provide a sporting infrastructure that nurtures the game for players of all ages. By treating transfer fees as solidarity payments only the contribution of developing young players is being valued. By contrast, the larger clubs benefit from all aspects of football development at the lower levels. Thus solidarity should not be narrowly focused on the production of young talent for big clubs. Moreover, talent development is to a significant extent a lottery, and it makes little sense, in designing a policy which rewards particular clubs for events which are often outside their control.

In reality the transfer system has done little to protect the smaller clubs from falling into financial difficulties. The UEFA Club Licensing Benchmarking Reports have documented consistently the financial problems of European clubs. According to the 2011 Report, 63% of top division clubs in Europe reported an operating loss, 55% reported a net loss, 38% reported negative net equity and auditors raised “going concern” doubts in 16% of cases. Financial distress on this scale is not materially affected by the small amounts of money trickling down from the dominant clubs.

The argument that the transfer system promotes competitive balance is open to challenge on a number of fronts. Many of the opinions expressed by Advocate General Lenz in the 1995 Bosman case seem to be equally pertinent twenty years on.

He characterized the argument in favour of transfer fees thus: “That argument amounts to an assertion that the system of transfer rules is necessary to ensure the organization of football as such. If no transfer fees were payable when players moved, the wealthy clubs would easily secure themselves the best players, while the smaller clubs and amateur clubs would get into financial difficulties and possibly even have to cease their activities. There would thus be a danger of the rich clubs always becoming even richer and the less well-off even poorer.”

Looking at the flows of transfer fees in English football he commented

“Those figures are an impressive demonstration of what an important role the lower divisions play as a reservoir of talent for the top division. They also show that income from transfers represents an important item in the balance sheets of the lower division clubs. If the transfer rules were to be

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<sup>10</sup> Ibid p248

regarded as unlawful and those payments thus ceased, one would expect those clubs to encounter serious difficulties. I thus entirely agree with the view, once more put forward clearly by URBSFA and UEFA at the hearing before the Court, that it is of fundamental importance to share income out between the clubs in a reasonable manner. However, I am nevertheless of the opinion that the transfer rules in their current form cannot be justified by that consideration. It is doubtful even whether the transfer rules are capable of fulfilling the objective stated by the associations.”

He pointed out how the transfer system was at root a perverse mechanism for maintaining competitive balance:

“it must first be observed that the rules currently in force probably very often force the smaller professional clubs to sell players in order to ensure their survival by means of the transfer income thereby obtained. Since the players transferred to the bigger clubs are as a rule the best players of the smaller professional clubs, those clubs are thereby weakened from a sporting point of view. It is admittedly true that as a result of the income from transfers those clubs are placed in a position themselves to engage new players, in so far as their general financial situation permits. As has been seen, however, the transfer fees are generally calculated on the basis of the players' earnings. Since the bigger clubs usually pay higher wages, the smaller clubs will probably hardly ever be in a position themselves to acquire good players from those clubs. In that respect the rules on transfers thus strengthen even further the imbalance which exists in any case between wealthy and less wealthy clubs.”

He then observed that there were better alternatives:

“Firstly, it would be possible to determine by a collective wage agreement specified limits for the salaries to be paid to the players by the clubs” A collective bargaining solution would of course, require the clubs to balance their interests with those of the players, in contrast to current system which largely places the burden of system on the players.

“Secondly, it would be conceivable to distribute the clubs' receipts among the clubs. Specifically, that means that part of the income obtained by a club from the sale of tickets for its home matches is distributed to the other clubs. Similarly, the income received for awarding the rights to transmit matches on television, for instance, could be divided up between all the clubs.

...It can scarcely be doubted that such a redistribution of income appears sensible and legitimate from an economic point of view.

...Neither URBSFA nor UEFA disputed that that solution is a realistic possibility which makes it possible to promote a sporting and financial balance between clubs.

...Finally, it must be observed that a redistribution of a part of income appears substantially more suitable for attaining the desired purpose than the current system of transfer fees. It permits the clubs concerned to budget on a considerably more reliable basis. If a club can reckon with a certain basic amount which it will receive in any case, then solidarity between clubs is better served than by the possibility of receiving a large sum of money for one of the club's own players.”

To the extent that the clubs are committed to pursuing competitive balance, the mechanisms suggested by the Advocate General seem as practical and superior to the transfer system today as they did then.

It is noteworthy that, while it has long been held that competitive balance is essential to the production of an attractive competition, research has failed to produce systematic and convincing evidence that competitive balance actually enhances demand. A study by Borland and McDonald (2003) that surveyed the literature concluded that the evidence suggested competitive balance did not matter at some levels (the individual match), but might do at others (the whole season), and was both ambiguous and under-researched in the long run.<sup>11</sup> A recent study for the European Commission<sup>12</sup> reviews the recent literature and concluded

“Various methods have been employed to consider competitive balance and its impact mainly on attendances in both US and European sports. While competitive balance is thought to be an essential part of maintaining a healthy competition, the level of competitive balance necessary has not been determined with any agreement in the literature. Nor has the most appropriate method to calculate it.”

It seems remarkable that neither UEFA, nor any of the national associations, nor any of the leagues have attempted to produce a scientific study of the ideal level of competitive balance in football competition, or even to specify what that might mean in practice.<sup>13</sup> This is not a solid enough foundation for the basis of policy making. As the Commission said in the White Paper on Sport

“The launch of policy actions and enhanced cooperation on sport at EU level needs to be underpinned by a sound knowledge base. The quality and comparability of data need to be improved to allow for better strategic planning and policy-making in the area of sport”.

Yet there are several studies which have suggested that competitive balance is currently deteriorating in Europe.<sup>14</sup>

## 6. Economic arguments

The economic analysis of the benefits of the transfer system has been relatively limited. Some recent papers have addressed aspects of the transfer system and attempted to analyse its efficiency from a theoretical point of view. All of these papers consider the issue of efficient contracting between an employer and employee. The key question for these authors is whether the commitment of the player to a long term relationship with club which is enforceable yields a higher level of investment from the employer in the employment relationship. None of them devote much time to considering why such

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<sup>11</sup> See for example Borland, Jeffery, and Robert MacDonald. "Demand for sport." *Oxford Review of Economic Policy* 19.4 (2003): 478-502.

<sup>12</sup> Study on the Assessment of UEFA's 'Home Grown Player Rule' Negotiated procedure EAC/07/2012, <http://ec.europa.eu/sport/library/studies/final-rpt-april2013-homegrownplayer.pdf>

<sup>13</sup> The Blue Ribbon Panel of experts appointed by the Commissioner of Major League Baseball to examine competitive balance in that sport concluded in 2000 that this could be defined as the notion that every team has the “regularly recurring reasonable hope of reaching post season play”. In the context of European football this would mean that every club might reasonably entertain the hope of being in contention for the Championship in the last 5-10 games of the season. This is not a standard which many (if any) European leagues could currently meet.

<sup>14</sup> See e.g. Curran, John, Ian Jennings, & John Sedgwick (2009). “‘Competitive Balance’ in the Top Level of English Football, 1948–2008: An Absent Principle and a Forgotten Ideal.”, *The International Journal of the History of Sport*, 26:11, 1735–1747) and Feddersen, A., W. Maennig (2005), “Trends in Competitive Balance: Is there Evidence for Growing Imbalance in Professional Sport Leagues?” *Hamburg Contemporary Economic Discussions* 01/2005)

rules would not be efficient if introduced into other employment relationship (e.g. one might consider that the relationship between academics and universities would also benefit from efficient contracting).

(i) Feess and Muehlheusser (2003)<sup>15</sup>

They argue that the development of players requires long term investments and therefore enabling clubs to demand a fee for releasing a player. They argue that the system introduced in 2001 favoured the players and clubs seeking to hire players away from their current club. As a result, they argue, there is a risk of underinvestment.

They also consider the question of whether limits on contractual freedom are harmful. Generally economists argue that restricting freedom to contract can lead to inefficiency, but they point out that actions which may appear beneficial to the individual may not be socially beneficial. For example, if there is a shortage of places in a school and all children are equally able then requiring the children to sit exams to qualify for entrance is socially wasteful- a random allocation achieves the same outcome with no effort. While this is true, applying such logic to the market for football players, where abilities are not equal and much of the attraction of the sport lies in observing differences in ability, then any system which restrains the player from demonstrating his distinct ability may be socially inefficient.

(ii) Dietl, Franck and Lang (2008)<sup>16</sup>

This paper deals head on with the conflict between standard employment contract law in most EU states, which gives employees the right to terminate their contract at will without liability for damages, and the restraint of the transfer system. As they say "The crucial effect of the transfer system is the creation of a unilateral property right for the clubs over the services of players."

Their analysis is based around the idea of insurance. Young players cannot easily tell if they will be successful or not, both because talent only emerges over time and because injury can so easily end a career. Given this risk, it seems natural that players would benefit from signing a long term contract and so insure themselves against the risk. Likewise it seems natural that football club would offer this insurance given that they employ many players, and so the up and downs for the club will even out over time.

However, given that in many countries employees are free to move jobs without compensation the incentive for the clubs is not to provide the insurance via a long term contract. In effect, they argue that the transfer system give clubs the incentive to sign long term contracts and so enables young players to buy the insurance that they want.

There are three main objections to this analysis. First, clubs are not very good at offering insurance, since they are often threatened with insolvency themselves. Second, player may not be very risk averse- professional athletes by and large tend to be risk takers, and therefore not interested in paying for

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<sup>15</sup> Feess, Eberhard, and Gerd Muehlheusser. "Economic consequences of transfer fee regulations in European football." *European Journal of Law and Economics* 13.3 (2002): 221-237.

<sup>16</sup> Dietl, Helmut M., Egon Franck, and Markus Lang. "Why football players may benefit from the 'shadow of the transfer system'." *European Journal of Law and Economics* 26.2 (2008): 129-151.

insurance by restricting their rights.<sup>17</sup> Third, the analysis takes no account of the other effects that the transfer system may have on the operation of the player markets.

## **7. Dominance and raising rivals' costs**

Arguments about the transfer system have focused on the employment relationship, while ignoring the competitive structure of the football system as a whole. The economic models described here model three parties- a player, the club that holds the player registration and the club that wants to acquire the player registration. This analysis disregards the competitive relationship between the buying and selling clubs, let alone their relationship to other clubs against whom they compete.

This section presents an economic argument against the transfer system which in practice seems incompatible with competition law.

### *Dominance*

Dominance is characteristic of football, in the sense that leagues organized along national lines are typically dominated by a small number of clubs (usually fewer than five).

From a competition law perspective dominance is defined relative to a market, and so the first step is to identify the relevant market. The competition authorities when examining the sale of broadcast rights have tended to define the relevant market as the market for top quality football on TV, usually incorporating the top division games in any given country, Champions League and other UEFA club competition games, domestic Cup competitions and national team games. In terms of the market for player services the market is likely to be defined in terms of all professional clubs. Since there is substantial player mobility between countries, and especially within the EU, this means the market will potentially include thousands of clubs.

According to the Commission the definition of dominance is settled case law:

“dominance consists of three elements, two of which are closely linked: (a) there must be a position of economic strength on a market which (b) enables the undertaking(s) in question to prevent effective competition being maintained on that market by (c) affording it the power to behave independently to an appreciable extent.”<sup>18</sup>

The classic definition of ‘dominance’ can be found in the United Brands case: “a position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on the relevant market by giving it the power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers” (case 27/76, point 65).

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<sup>17</sup> Of course, a paternalist approach is to say they should have it even if they say they don't want it, but this seems hard to justify in the modern age.

<sup>18</sup> DG Competition (2005) “discussion paper on the application of Article 82 of the Treaty to exclusionary abuses” <http://ec.europa.eu/competition/antitrust/art82/discpaper2005.pdf>

Taken individually, even the largest European clubs are unlikely to meet this standard. For example, Manchester United may be considered to be in a position of economic strength, but is unable to prevent effective competition in the market for players from, for example, Chelsea, Bayern Munich and Barcelona, and therefore cannot act independently of these rivals.

However, there also exists in competition law the concept of collective dominance. A group of companies can be found to be collectively dominant if they act together or present themselves together from an economic perspective. The finding of collective dominance must flow from an economic analysis of the companies and the markets in question. It is not necessary to establish that specific agreement exists for a finding of collective dominance.<sup>19</sup> It is more a matter of possessing a shared economic interest relative to other competitors in the market.

In accordance with EU case law three cumulative conditions must be met for a finding of collective dominance: first, each member of the dominant oligopoly must have the ability to know how the other members are behaving in order to monitor whether or not they are adopting the common policy; second, the situation of tacit coordination must be sustainable over time, that is to say, there must be an incentive not to depart from the common policy on the market; thirdly, the foreseeable reaction of current and future competitors, as well as of consumers, must not jeopardise the results expected from the common policy (see e.g. T-193/02, Laurent Piau, point 111).

It seems plausible to argue that the largest clubs are collectively dominant. In terms of economic strength, The UEFA Club Licensing Benchmarking Report for the financial year 2012 found that the 728 top division clubs in Europe had a total revenue of €14.1 billion, while the Deloitte Football Money League for 2011/12 found that the 20 largest clubs had revenues of €4.8 billion, amounting to 34% of the total. Thus the average revenue of the top 20 was 18 times larger than the average revenue of the remaining clubs.

The precise membership of the collectively dominant group might vary from time to time. Between 2000 and 2008 the G14 operated as a lobbying group on behalf of some of the largest clubs ranging from 14-18 members. Since then the European Club Association embraces a broader membership but still reserves a disproportionate share of representation for the dominant clubs in each country.

In the context of sporting competition collective dominance should also be understood to possess a sporting as well as an economic dimension. Thus, for example, the three most successful clubs in each of a sample of 20 European leagues were found to have won 79% of league championships over the last 25 years.<sup>20</sup>

The economic strength of the dominant group affords them an opportunity to limit economic competition and thus giving them the freedom to act independently in the market. The principal mechanism for limiting economic competition is influence over the rule setting of national and international governing bodies. In most countries the dominant clubs have a powerful voice when it comes to establishing regulations.

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<sup>19</sup> C395-96 P and C396-96 P *Compagnie Maritime Belge Transports*

<sup>20</sup> Szymanski (2015) *Money and Soccer*, chapter 1

The dominance of the largest clubs is not only economic. It is reflected in the administrative organizations of European football. For example, the European Club Association (ECA), the main interlocutor on behalf of clubs with UEFA, has only 105 voting members even though there are around 700 clubs playing in the top divisions of European football. Moreover, a club loses its rights as an ordinary member if relegated from their division.<sup>21</sup> Membership is also weighted toward the larger associations. Half of the executive board consists of the clubs that have traditionally dominated European competition.<sup>22</sup>

To give another example, only two clubs are currently represented on the Board of Directors of the English Football Association, they are Manchester United and Middlesbrough.

### *Abuse of dominance*

Neither dominance nor collective dominance are cause for concern per se. However, if dominant firms take steps to limit the capacity of their rivals to compete – exclusionary practices - such behaviour may be considered abusive and therefore illegal. Examples of exclusionary abuses include predatory pricing, single branding and rebates, tying and bundling, and refusal to supply. The consequences of these actions is to foreclose the markets to other competitors, and generically they can be described as doing through the mechanism of “raising rivals costs”.

In the context of football, restraints on the mobility in the player market create barriers to entry by increasing the cost of fielding a competitive team. The agreement between FIFA and the Commission in 2001 was intended to place a limit on the escalation of transfer fees. By specifying that the size of the fee should be limited by actual damages suffered by the releasing club, and in addition training expenses incurred, the Commission argued that the regulations FIFA were “an example of good practice that ensures a competitive equilibrium between sports clubs.” If fees rise above these levels then it is necessary to ask whether the rules as applied continue to represent good practice.

The example of the rise of Manchester City in the English Premier League illustrates the extent to which the transfer rules represent a barrier to entry. The club was acquired by Mansour bin Zayed bin Sultan bin Zayed bin Khalifa Al Nahyan, commonly known Sheikh Mansour, in September 2008. Table 2 illustrates how the new owner bought his way to the top of the Premier League.

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<sup>21</sup> <http://www.ecaeurope.com/about-eca/eca-membership1/ordinary-members/>

<sup>22</sup> Bayern Munich, AC Milan, Barcelona, Juventus, Real Madrid, Arsenal and Porto. Of these only Arsenal has not won a Champions League trophy.

**Table 2: Manchester City's investment in Intangible fixed assets since 2008**

Season ending	League position	Revenues £m	Wages £m	Tangible fixed assets additions £m	Tangible fixed assets disposals £m	net expenditure on intangible fixed assets £m	Tangible fixed asset net expenditure as % of wages
2009	10	87.0	82.6	103.2	-12.3	90.9	110%
2010	5	125.1	133.3	139.8	-17.5	122.3	92%
2011	3	153.2	174.0	155.1	-11.4	143.7	83%
2012	1	231.1	201.8	122.9	-27.6	95.2	47%
2013	2	271.8	233.1	101.1	-22.1	79.0	34%
2014	1	346.5	205.0	116.1	-34.6	81.5	40%
Total		1214.7	1029.9	738.2	-125.6	612.6	59%

Source: financial accounts of Manchester City Limited

In order to raise the club from an average mid-table position in the Premier League to a consistent finish in the top four (Champions League qualifiers) and to win the Championship (2012 and 2014), the club needed to invest in a squad of players capable of competing at the highest level in England. Research on football club sporting performance consistently shows a very high correlation between the wages paid by the club and league position, as shown in the figure 2 below.<sup>23</sup>

Wage payments rose very quickly from 2009 to 2012, more than doubling. But in order to employ the players who received the wages, the club had to spend heavily in the transfer market. In the financial accounts player registrations are represented as intangible fixed assets, players bought are shown as additions and players sold are shown as disposals. Between 2009 and 2011 the club spent more on adding to their intangible fixed assets than they did player wages. Net investment in player registrations, after allowing for disposals amounted to £357 million, compared to £390 million on wages. If we allow that 10% of wage spending was not player related, then the club actually spent more on transfer fees than it paid out in player wages.

<sup>23</sup> The financial data from the club accounts shows wages paid to all employees, not just the players. However, most of the wage expenditure of football clubs goes to the players.

**Figure 2: Wage Spending and League performance**



Source: Money and Football (2015), based on company financial accounts

This illustrates the high entry cost for clubs aspiring to compete at the highest level, with a large fraction of the transfer fees being paid to other clubs at the elite level.

The extent to which transfer fees at the highest level circulate among the top clubs can be illustrated. UEFA conducted an analysis of transfer fees among top division clubs over a five year period 2010-2014.<sup>24</sup> Total transfer spending by European clubs (which includes over 700 top divisions clubs and many playing in lower divisions) equaled €10.9 billion. In recent years annual spending has been running at the level of around €3 billion per year. The Deloitte Football Money League for 2015 identified the twenty largest clubs globally by revenue (all are UEFA based). Transactions among these twenty clubs alone amounted to €1.7 billion – between 15% and 20% of all transfer transactions in Europe. These transactions related to just 131 players and represented 58% of all sales by the top 20 clubs and 32% of all their purchases.

Table 3 below illustrates the web of transactions among the top clubs.

<sup>24</sup> See UEFA Club Licensing Benchmarking Report Financial Year 2012. For individual transactions they relied on data from the website transfermarkt.co.uk. I have used the same source.

**Table 3: Player Trades among the top clubs 2011-2015 (£): Selling = rows, Buying = columns**

	AC Milan	Arsenal FC	Atlético Madrid	Bayern Munich	Borussia Dortmund	Chelsea FC	Everton FC	FC Barcelona	FC Schalke 04	Galatasaray SK	Inter Milan	Juventus FC	Liverpool FC	Manchester City	Manchester United	Newcastle United	Paris Saint-Germain	Real Madrid	SSC Napoli	Tottenham Hotspur	Total
AC Milan									21120000		4400000	3960000	17600000				55440000				102520000
Arsenal FC								55440000		3080000	5280000	4400000		31020000	27020000						117528000
Atlético Madrid						51040000	3520000		9680000	1760000			1760000								133760000
Bayern Munich			19360000						4400000									26400000	26400000		48940000
Borussia Dortmund				32560000					8800000	2200000								8800000			58520000
Chelsea FC		3520000					34200000				1320000		14260000			14080000	39360000	47960000	7040000		148720000
Everton FC		10560000																		3170000	55440000
FC Barcelona	26400000	37400000	1850000			29040000		4400000						13200000	28510000			3080000			146610000
FC Schalke 04				26400000										26400000							27940000
Galatasaray SK			11440000																		11440000
Inter Milan	13640000								6600000				8800000	29260000		4970000	10120000		7920000		81310000
Juventus FC	9680000								6160000				4820000				7040000				27700000
Liverpool FC	1140000		2640000			69520000		88880000		6600000											162840000
Manchester City	36520000											7930000							3520000	7610000	67450000
Manchester United		17600000			7040000		5280000					1320000				2990000		2200000			216780000
Newcastle United		13200000				7480000							43120000				22000000				85800000
Paris Saint-Germain													16720000								16720000
Real Madrid		44000000		8800000	7040000				3080000		17600000	4400000		66000000					51480000	8800000	211200000
SSC Napoli									2070000	1100000	13728000						82230000				99128000
Tottenham Hotspur							5060000										109120000				114180000
<b>Total</b>	<b>90900000</b>	<b>122760000</b>	<b>33710000</b>	<b>104280000</b>	<b>14080000</b>	<b>157080000</b>	<b>43308000</b>	<b>144320000</b>	<b>32560000</b>	<b>25610000</b>	<b>11748000</b>	<b>44968000</b>	<b>111480000</b>	<b>143880000</b>	<b>192570000</b>	<b>7960000</b>	<b>227870000</b>	<b>157080000</b>	<b>62040000</b>	<b>21120000</b>	<b>1749324000</b>

Source: transfermarkt.co.uk

This pattern is also confirmed by the research carried out for the European Club Association (ECA) and by reports from the FIFA Transfer Matching System (TMS). The ECA analysis of transfers among clubs for the period 2011-13 showed that transfers among clubs in the top leagues of the five largest UEFA members (England, France, Germany, Italy and Spain), only 27% of transfers by number (297) were among the top ten clubs in each league, but this accounted for 49% of transfers by value. Of all the potential flows of money with the top divisions, 25% of the money simply circulated among the top 5 clubs although this accounted for only 81 players (7%) of the total.<sup>25</sup>

TMS has analysed global transfer activity and found that between 2011 and 2013 the largest 25 football clubs accounted for between 51% and 58% of all transfer fee spending.<sup>26</sup>

This suggests that a significant fraction of the transfer market is controlled by elite clubs who circulate top players among themselves. From a sporting perspective, it is well known that the elite group of clubs dominate competition and that this dominance has been increasing since the advent of the Champions League. From an economic perspective the transfer market is used by the elite clubs to maintaining high barriers to entry through the escalation of transfer fees.

If it were not for the requirement to pay very large transfer fees to acquire the best players it seems likely that more clubs would be able to compete with the elite group. The requirement to spend heavily in the transfer market, before achieving any success in competition, represents a barrier to entry. If transfer fees strictly reflected training costs or foregone revenues, then they would be substantially lower and the barrier to entry would not be so high.

### *The expansion of restraints on competition*

The extent of restraints on competition has been expanded in recent years by measures adopted by UEFA. The Financial Fair Play regulations have restricted the capacity of clubs to challenge the elite by investing in playing talent, in the way that Manchester City did, by requiring break-even. This means that

<sup>25</sup> [http://www.ecaeuropa.com/Research/Study%20on%20the%20Transfer%20System%20in%20Europe/ECA%20Study%20on%20Transfer%20System%20in%20Europe\\_WEB%20version.pdf](http://www.ecaeuropa.com/Research/Study%20on%20the%20Transfer%20System%20in%20Europe/ECA%20Study%20on%20Transfer%20System%20in%20Europe_WEB%20version.pdf)

<sup>26</sup> [http://www.fifatms.com/Global/MarketInsights/Market%20Insights\\_EN.pdf](http://www.fifatms.com/Global/MarketInsights/Market%20Insights_EN.pdf)

over a three year period spending on player wages and transfers cannot exceed revenues from ticket sales, broadcast rights, sponsorship and merchandising, except by a small amount. This renders the strategy adopted by Manchester City unfeasible, even in cases where the owners have the financial capacity.

An economic analysis of these rules by Peeters and Szymanski (2014) showed that these rules will put downward pressure on player wages by limiting competition and adding to the barriers to competing with the elite clubs.

To a lesser extent the home-grown player rules also limit competition for the elite clubs. Any new club seeking to compete with the established elite within a reasonable time frame will need to bring in players from outside their local market. The elite clubs already possess large academies and extensive scouting system that enables them to bring talented young players to their club at a very young age. A club aspiring to compete with the elite would only be able to develop such a network over a number of years, and with competitive success would not be able to generate the revenues to fund it.

## **8. Conclusion**

The transfer system as it currently operates is intended to achieve a number of pro-competitive benefits in football markets by placing restraints on football players. These restraints significantly impact the economic and social well-being of the players both in theory and in practice. Even if it were possible to justify these restraints because of the wider benefit to football, there is little evidence that these wider benefits have materialized. But in reality, it remains the case that there are better alternatives to achieving the stated policy goals, as observed by Advocate General Lenz in the Bosman Case twenty years ago.

As it currently operates the transfer system sustains the dominance of the elite clubs by ensuring that they are the only ones with the financial muscle to afford the transfer fees payable for the very best players. Thus, as it currently operates, the transfers system is not only unfair to players, it also promotes the opposite of what was intended.