

# **Are Voluntary Salary Cap Agreements Self-Enforcing?**

## **Abstract**

In 2002 the leading European football clubs reacted to the increasing player salaries by signing a voluntary agreement to limit player salaries to 70% of revenues. We analyze under which conditions a voluntary salary cap agreement is self-enforcing. Based on a simple model of a league with two profit-maximizing clubs, we show that the self-enforcing character of salary caps increases with the clubs' valuation of future profits and the importance of competitive balance. In European football leagues salary cap agreements are not likely to be self-enforcing because (1) promotion and relegation as well as limited transfer windows reduce the clubs' discount factor and (2) competitive balance is less important in order to activate fan interest than in US Major Leagues.

Key words: salary caps, sport leagues, self-enforcing contracts

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