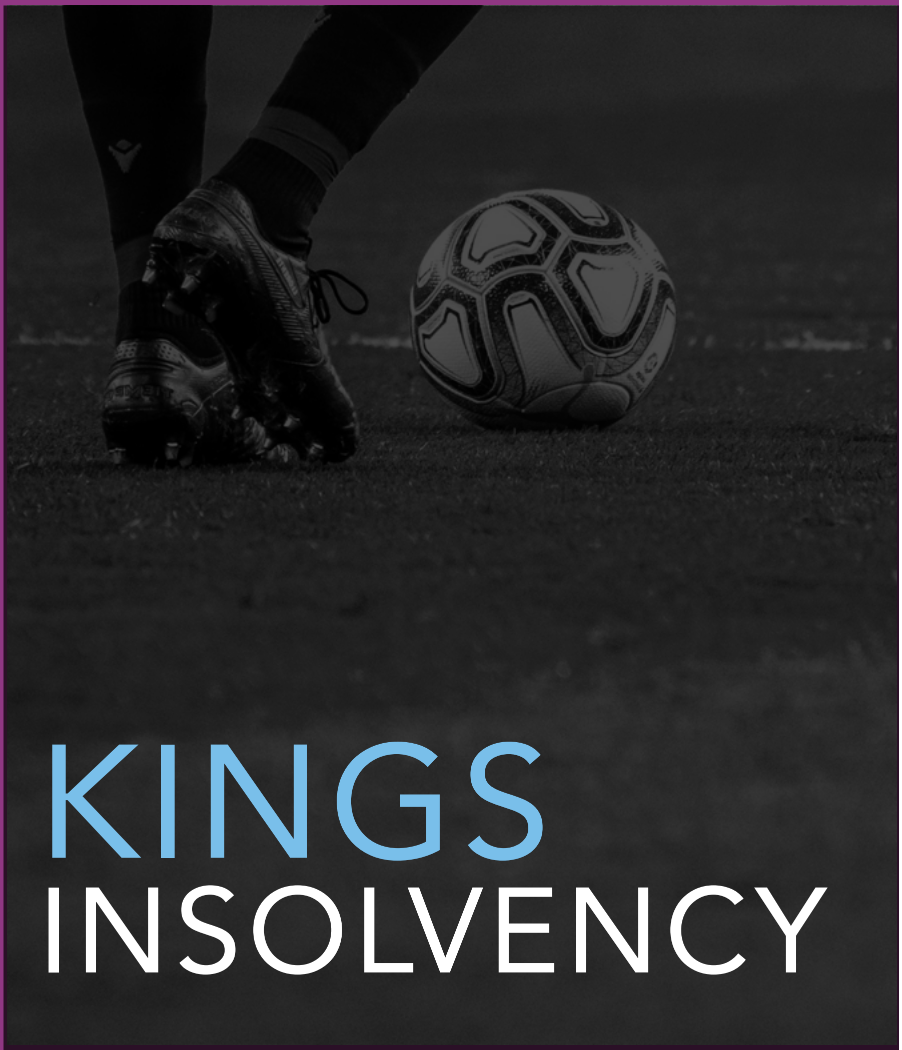

Football Insolvency

February 2021

KINGS CHAMBERS

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EDITORIAL

I am delighted to be the guest editor for the third edition of Kings Insolvency. In this issue Louis Doyle QC looks at the nature and effect of the Football Creditor Rule and considers if it is open to challenge after many years of undisputed application. Steven Flynn provides an overview of the regulatory regime for dealing with insolvent clubs. Also, Nick Taylor provides a case study of the finances and plans of Manchester United.

I wish to give a special thank you to Gerald Krasner and Paul Stanley of Begbies Traynor for their interview with Louis, edited highlights of which appear in this issue. As practitioners on the ground, they provide valuable insight based upon their vast experience of insolvency work in football. Their firm produces the annual health check on all football leagues, a very useful guide to the state of the football industry.

Many businesses in the sports industry are facing unprecedented financial distress as a result of the pandemic. Whether involved directly or indirectly in football, rugby, horseracing and other sports they have suffered the multiple impacts of complete closure during the first lockdown, the early termination of the season, the cancellation of fixtures and the exclusion of fans.

In football, pre-pandemic, matchday income represented about 15% of income for Championship clubs whereas for the League 1 clubs it was 30%. The overall financial health of clubs had stabilised pre-pandemic to some extent in both the English and the Scottish Leagues. However, the pandemic has changed all of that. Fans have not been able to attend so that income is lost along with the sales of merchandise. The premises have not been used for the corporate and other events that also helped to generate income. At the same time the wages have had to be paid where they are not covered by the furlough scheme. For EFL clubs, a large proportion of their income is paid out in player/staff salaries: for Championship and League 1 clubs that figure is about 90% of all income.

Under normal circumstances a business facing financial stress has a number of options including CVAs and Administration with the objective that the company or at least the business will survive. In football there are additional complications.

One of the major concerns, in the EFL, is that the occurrence of an Insolvency Event may lead to a 12 point penalty deduction under EFL Reg 12.1. This may lead to relegation and an even worsening financial position as happened in the case of Wigan Athletic in July 2020. A lack of clarity in the regulations does not help. It is unclear if “Insolvency Event” under the EFL Regulations also includes the new procedures of the Restructuring Plan with its “cross-class cram down” and Moratorium introduced in the Corporate Insolvency and Governance Act 2020. Further, whilst there are temporary protections in place at the moment, including protection from wrongful trading for directors and from the forfeiture of commercial leases, these protections will not last indefinitely.

Early specialist advice is essential to identify a solvent solution if possible, or an insolvent solution if needed.

David Casement QC

Head of Kings Sport Law Department
Football Association Judicial Panel
Judge of the International Court of Appeal - Fédération Internationale de l’Automobile

THE FOOTBALL CREDITOR RULE: RED CARDING THE PARI PASSU PRINCIPLE AND THE ANTI-DEPRIVATION RULE. DO WE NEED VAR?

Louis Doyle QC

INTRODUCTION

The decision of David Richards J, as he then was, in Revenue and Customs Commissioners v Football League Ltd (Football Association Premier League Ltd intervening) [2012] EWHC 1372 (Ch), [2012] Bus LR 1539, [2013] 1 BCLC 285 (to which para references hereafter are made) involved a CPR Part 8 Claim by which HMRC asserted that the Football League's so-called Football Creditor Rule ("FCR") was void and of no effect because, as a matter of law, and social or moral justification aside, the FCR conflicts with two fundamental principles of insolvency law, the pari passu principle and what is commonly termed the anti-deprivation rule, by reason of the Football League's insolvency policy, and, in particular, the FCR affording certain football-related creditors priority over other creditors in the insolvency of a football club.

As David Richards J pointed out at [2], the football creditor rule had been (as it continues to be) subject to a good deal of criticism, in Parliament and in the courts as well as from commentators. It was heavily criticised in the Seventh Report of the Culture, Media and Sport Committee of the House of Commons on Football Governance dated 29 July 2011 which recommended that it should be abolished, by legislation if necessary. Judicially, Norris J expressed himself in In re Portsmouth Football Club (2010) Ltd (unreported) 17 February 2012, as follows in articulating the perceived unfairness of the rule on other creditors:

"I understand the disquiet from the creditors. The general body of taxpayers, and the ordinary consumers who do pay their energy bills, and the ordinary traders and professionals who provide services such as, from the creditor list, coach hire, catering, medical services, ground care and maintenance, must wonder why they should subsidise the club's wage bill, why it is that they are involuntarily lenders to the club of their outstanding bills and why they will only get back pence in the pound for the services they have provided."

THE FCR

Parts of the Football League's articles establish an insolvency policy, central to which is a regime designed to benefit certain types of creditor, termed "Football Creditors". That expression, defined by Articles 2.1 and 80, extends to a considerable number of football-related entities including the Football League itself, the Premier League and Football Association, together with any Member Club (as defined, and which must hold a share in the Football League, often termed a "golden share") and any holding company of The League and any subsidiary company of such holding company. Articles 65 to 80 to govern the financial arrangements of the Football League and the manner in which payments to Member Clubs are to be made.

The effect of the FCR demonstrates obviously enough why HMRC considered the rule open to challenge. In the first instance, no sums of money which might otherwise have been payable to a Member Club under the scheme of distribution shall be legally due and payable unless the club in question has fulfilled all its fixtures for the season in question. Where there is a default in payment to Football Creditors, central funds received by the Football League from broadcasting revenue etc are applied directly in paying those debts. Further, Article 77 provides that any sum which have been paid to the club from what is termed the Football League's Pool Account during the course of the season shall have the status of an interim payment which shall be repayable on demand if the club does not complete all of its fixture obligations. In the event of what is defined as an "Insolvency Event' – meaning, subject to update following the introduction of the rescue procedures introduced by the Corporate Insolvency and Governance Act 2020, but subject to a "if appropriate" sweeping up provision in Article 4.7.6 - a Member Club is given notice by the Football League by way of a Notice of Withdrawal requiring the transfer of the golden share the club holds as a pre-requisite of Football League membership. Other than the in the case of liquidation (which in practice is invariably terminal as an insolvency procedure), the insolvency policy provides that the Notice of Withdrawal may be suspended to allow the club time to restructure its financial affairs or effect a sale. In practice, this is what happens where a club goes into administration or a CVA.

THE PARI PASSU PRINCIPLE

The pari passu principle was first established in English law by a statute of Henry VIII, The Statute of Bankrupts 1542. It requires the assets of an insolvent person to be distributed among the creditors on a pari passu (or pro rata) basis, subject only to such exceptions as the general law may permit. The pari passu basis of distribution means that all creditors will receive the same percentage of their debts out of the available assets. Parties are not free to contract out of the operation of this principle, except by the creation and, when required, registration of valid security over the debtor's assets. Before David Richards J, there was no suggestion that security was created by the rules under consideration.

THE ANTI-DEPRIVATION RULE

The anti-deprivation rule used to be termed the fraud on the bankruptcy law rule. The rule renders void any provision by which a debtor is deprived of assets by reason of insolvency with the effect that they are removed from and not available for creditors in the debtor's insolvency. The purpose of the deprivation may, but need not, be to ensure priority payment to a particular creditor or creditors. This principle is subject to a number of specific exceptions and general qualifications which David Richards J considered in some detail at [96] to [100].
The leading case on the anti-deprivation rule is the Supreme Court's decision in Belmont Park Investments Ltd v BNY Corporate Trustee Services Ltd [2012] 1 AC 383, a judgment handed down before HMRC's objection to the FCR was heard before David Richards J. Prior to the Belmont decision, and for at least 200 years, the case law, without judicial intervention, had held that it was possible for an interest in an asset to be granted to a party on terms that the interest ceased on bankruptcy, in contrast to the forfeiture on bankruptcy of an asset held by the individual which provision was void.

Following Belmont, almost every arrangement under which the interest of an individual is limited or said to be conditional by reference to insolvency proceedings falls to be tested for its effectiveness by reference to the anti-deprivation rule, as articulated by Lord Collins (with whom Lord Phillips, Lord Hope, Baroness Hale and Lord Clarke agreed and to whose judgment that provided by Lord Walker was intended to provide only "footnotes"). Briefly, at [75] to [79] in Belmont, Lord Collins considered that, bearing in mind that the non-application of the anti-deprivation rule had tended to arise where the good faith or the common sense of the transaction was a substantial factor, what was required was some deliberate intention to evade the laws of insolvency; in borderline cases, where the intention was not obvious, "a commercially sensible transaction entered into in good faith should not be held to infringe the anti-deprivation rule". As identified below, it was on this ground, with due deference to the words of Lord Collins just quoted, that David Richards J held the FCR not to contravene the anti-deprivation rule.

DISTINGUISHING BETWEEN THE PRINCIPLE AND THE RULE

It will be seen, therefore, that the pari passu principle is aimed at outlawing provisions that would give any creditor an unfair advantage over other creditors whereas the anti-deprivation rule seeks to outlaw a net reduction in the net assets available to creditors in an insolvency, but does not concern itself with distribution as between creditors. In Belmont, Lord Collins put the distinction as follows, at [1], a very similar exposition being provided by Lord Mance at [148]: "The anti-deprivation rule and the rule that it is contrary to public policy to contract out of pari passu distribution are two sub-rules of the general principle that parties cannot contract out of the insolvency legislation. Although there is some overlap, they are aimed at different mischiefs: Goode, Perpetual Trustee and Flip clauses in Swap Transactions (2011) 127 LQR 1, 3-4. The anti-deprivation rules is aimed at attempts to withdraw an asset on bankruptcy or liquidation or administration, thereby reducing the value of the insolvent estate to the detriment of creditors. The pari passu principle reflects the principle that statutory provisions for pro rata distribution may not be excluded by a contract which gives one creditor more than its proper share".

ANALYSIS

The pari passu principle is dealt with in [84] to [90] of the judgment of David Richards J. It applies only where the purpose of the insolvency procedure was to effect a distribution, and, in administration, the principle would only be engaged once the administrator had given notice of a proposed distribution. By that stage, however, the FCR would already have taken effect at an earlier stage.

Article 77.1 allows the board of the Football League to make interim payments from the Pool Account to any club in its discretion, although there is only a liability to make any other payments to a club if the club completes all of its fixture obligations for the season in default of which any interim payment already made becomes repayable immediately on demand. Unless Article 77 was a sham, which was not suggested, it made the legal entitlement to payments from the Pool Account conditional on completion of the season. Applying Belmont, the court could not disregard the legal rights and obligations created by the articles, even if they had been drafted to achieve a particular end. Following this logic, at [125] to [137], if a member club had no legal entitlement to payments from the Football League until the club had completed the season, the club could not be said to be deprived of an asset if, as a result of going into administration or liquidation, it could not complete the season. Likewise, there could not be said to be any asset of the club to which the pari passu principle could be applied in those circumstances.

Article 80.2 further allows the board of the Football League to apply any credit on the Pool Account, which would otherwise be payable to the defaulting club at the end of the season so far as it had not been applied in making any interim payment to the defaulting club, to be applied in meeting liabilities of the defaulting club to football creditors during the season, It had to follow that the only sum which then became payable to a defaulting club which completed the season was the balance, if any, after the Football League had paid football creditors during the season. In those circumstances, the defaulting club was not deprived of an asset, because there was no debt due to it beyond the amount of the balance, if any. That was the result whether or not the club went into liquidation or administration during the season because the anti-deprivation rule only applied on a member club being placed into administration or liquidation, but not if the trigger for Article 80.2 was default in a member club making due payment to a football creditor.

The Football League's power to require the transfer of a member's share, in the event of a club going into administration or liquidation, was not void by reason of the anti-deprivation rule. The Football League's articles and insolvency policy gave it it power to permit an insolvent club to participate in its competitions on terms that other member clubs and other specified creditors were paid in full. That amounted to no more than the exercise by the member clubs, through the Football League, of their right to refuse to participate further with the insolvent club save on those terms (although the judgment takes no account of the possibility that such member clubs might not wish to exercise such a right to refuse to participate in playing against an insolvent club).

Ultimately, David Richards J's conclusion, at [163] to [164], was to the effect that the Football League's insolvency policy, and in particular the FCR, did not involve any divestment of value offending against insolvency law and was one that that was commercially sensible and entered into in good faith between the parties such that, applying Lord Collins broad test in Belmont, there was no conflict between those provisions and English insolvency law.

IS THE FCR BEYONG CHALLENGE? A POSTSCRIPT

David Richard J's conclusion was that in most circumstances in which the relevant provisions of the Football League's articles and its insolvency policy (especially the FCR) would operate, they would not be rendered void by either of the two fundamental principles. The judge was also careful to spell out (at [189]) that "the FL should not regard the result of this case as an endorsement of its approach to football creditors" because the judgment did not cover every conceivable eventuality. The judge was also careful to point out that the hypothetical nature of the application, and the rather abstract way in which the point in dispute had been put by way of a CPR Part 8 claim, dictated that the court was not confronted with a concrete set of facts against which legal principle could be applied. Nevertheless, the meticulous and painstaking way in which the judgment is framed dictates a high level of confidence in the way in which the court at first instance is likely in most cases to apply the FCR in the face of a challenge based on either the pari passu principle or the anti-deprivation rule, most obviously in the context of administration. The judgment does not, however, write off the merits of a challenge to the Football League's insolvency policy, especially the FCR, in all cases, although it will take a real-life case based on specific facts to form the basis for such a challenge. No such challenger has emerged over the last nine years, most likely because, in order to get around the decision in existence and the reasoning of David Richards J therein, and unless any claimant could satisfy the court either that the earlier decision was plainly wrong, or involved facts not envisaged by the earlier decision, the case would have to reach the Court of Appeal, with all the time and cost involved in that process.

One particular issue that attracted criticism from the judge at [188] was the Football League's approach in treating the anti-deprivation rule as a general avoidance provision which "misunderstand[s] the [rule] which is specific in what it prohibits". In those cases in which the anti-deprivation rule might conceivably become engaged – one example given was in the event of administration or liquidation commencing after the end of a season but where there has been no application of Article 80.2 (board of the FL to apply any sum standing to the credit of the Pool Account, which would otherwise be payable to a defaulting club, in discharging football creditors) - David Richards J identified at [187] that the exact consequences of such engagement would have to be decided in the context of a real case, if and when it ever arose and was brought before the court.

The judgment, handed down on 12 May 2012, is, in theory, not the last word on the application of the FCR, although it has been for almost nine years. With respect, it is hard to read the analysis of Lord Collins in Belmont, in reviewing two centuries of entirely judge-made law and reaching the conclusion that what is needed for the anti-deprivation rule to engage is some deliberate intention to evade the laws of insolvency, without also having in mind the fact that, almost self-evidently, the Football League's insolvency policy, and perhaps most obviously the FCR, carefully crafted in legal terms as both are, has at its very root, and as part of an entirely understandable code of self-protection to which member clubs are required to subscribe as a condition and part of the price of participation in organised football, the diversion from an insolvent football and its creditors of an entitlement to money which is then channelled to an alternative and carefully calibrated sub-set of football creditors who, but for the operation of the FCR, and under the position that would otherwise prevail under the provisions of the insolvency legislation, would not stand so enriched or discharged.

IN THE RED: THE DEVIL IN THE DETAIL OF FOOTBALL FINANCE

Nick Taylor

A review of football and insolvency would not be complete without a brief look at how a club normally finances its activities.

The staggering wages paid to the top players are well known but, like any other business, clubs could not afford to pay those wages for long unless they generated revenue to match. And as there is a strong, although imperfect, correlation between a club's wage bill and their success on the field, there really is every incentive for clubs to ensure healthy and diversified income streams. In addition to revenue, clubs can raise money by borrowing or raising equity, often assisted by the 'generosity' of wealthy owners.

To provide context, this article will focus on a well-known example for which relatively up to date financial information is available – Manchester United Football Club. The example chosen betrays no hidden loyalties, the author lives on the other side of the Pennines and is far more interested in the progress of the newly promoted team based there. However, MUFC is a financially successful club and as its shares are listed on the New York Stock Exchange detailed and regular financial updates are available.

REVENUE

Clubs generate revenue from three main sources – matchday (predominantly ticket sales), broadcasting (self-explanatory) and commercial (e.g. sponsorship, merchandise and retail income). The split depends on the club, the league and the level of competition.

As Old Trafford is the largest Premier League stadium and the club is regularly able to sell out matches it is no surprise that MUFC's matchday revenue regularly puts it at the top of the (accountant's) table, with £90m to 30 June 2020 (especially impressive as a pandemic impacted period). However, with MUFC regularly selling out Old Trafford it can only meaningfully increase matchday now by raising ticket prices, something unpopular with supporters and which it has not done for over eight years.

Matchday is also clearly the income stream which has been most impacted by the pandemic. For some other clubs the lack of attendance at matches will be particularly acutely felt - for example, the two big Scottish clubs, Celtic and Rangers, generate respectively 40% and 60% of their total revenue from matchday.

By contrast, MUFC generate about 18% of their total revenue from matchday - within the typical range for a big Premier League club. For comparison, for Arsenal and Tottenham Hotspur it is around 24% and for Burnley a mere 5%, broadcasting income being a much larger proportion for the smaller Premier League teams.

Broadcasting for MUFC has two main sources – Premier League and UEFA. Premier League broadcasting is not split equally between the clubs, very roughly clubs receive a flat fee and further amounts weighted by a club's finishing place and how often their matches are broadcast. Nevertheless the gap between the highest and lowest finishing clubs is not enormous. For the 2018/19 season top placing Manchester City received a total of

£151m and bottom placed Huddersfield £97m (£143m for MUFC). The real drop-off is to the English Football League, where each club receives around £3.8m from EFL broadcasting rights, although the parachute and other payments made by the Premier League to EFL clubs can skew things club by club.

Similarly, UEFA broadcasting income ('prize money' in their parlance) is highest for those clubs in the Champions League. MUFC's 2019/20 season in the Europa League correspondingly hurt their revenue, although UEFA's own parachute payments structure to teams who drop out of the highest level is designed to cushion the impact. Even so the drop will have been felt by the club - £22m from UEFA to June 2020 vs £83m for the prior season.

Ultimately, beyond performing on the field a club has relatively little control or influence over its share of broadcasting.

Commercial is MUFC's biggest strength. Almost uniquely, MUFC earn more from commercial revenue than broadcasting and matchday income combined (£279m to June 2020). MUFC have an incredibly strong brand and a number of large commercial sponsors and partners. Adidas alone paid the club £78 million in the last season.

Matchday, broadcasting and commercial represent cash income for clubs. But for those readers with any cause to consider clubs' accounts in greater detail, look out as well for profits or losses being booked when clubs buy and sell players. Transfer fees are capitalised and then amortised over the life of a player's contract. When that player is sold the accounting profit or loss on that fee is booked in the accounts. For some clubs such as Celtic and Chelsea (but not MUFC) selling players at a profit is a commercial aim.

OTHER INCOME

Clubs can also fund their activities by traditional financing activity - loans from banks, owners or raising equity.

For MUFC, as is well known in 2005 Malcolm Glazer gained a controlling interest in the club. Space constraints unfortunately do not allow the full story to be told of the financial engineering that then transpired, but it is a fascinating story perhaps for another time. In short, MUFC was delisted (from the London Stock Exchange) and the highly leveraged nature of the buyout was such that the club went from being debt free to being saddled with debts of £540 million at interest rates of between 7 – 20%. Further debt was injected, significant amounts of interest and dividends were paid by the club and it was eventually relisted, this time on the NYSE. The Glazer family retain ultimate control, and as the Class A shares offered to the public have 1/10th of the voting rights of the Class B shares held by the Glazers, this seems unlikely to change until they decide to sell-out.

MUFC's fans have been famously aggrieved by the Glazer saga, but comparisons with involvements by other wealthy owners are indeed unflattering, with more than £1 billion paid in interest, fees, refinancing and other similar charges since the takeover. MUFC's debt servicing nowadays is far from problematic for its finances, but an average of £22.4m in interest payments for the past 5 years is also not nothing.

In contrast, although in itself unusual, Chelsea's owner Roman Abramovich paid off much of the debt owed by Chelsea when he took over, and loans made to Chelsea during his ownership (which were always interest free anyway) have subsequently been converted to equity. It is interesting in football that two otherwise similar businesses in exactly the same industry can have such starkly different debt levels.

Nevertheless, MUFC remains one of the most financially successful and richest clubs in the world. Looking to the future, football has for a long time been a global sport but the finance chiefs of clubs with brands as strong as MUFC (as well Barcelona, Liverpool, Real Madrid etc.) are continuing to try to actively monetise fan bases in emerging markets. For example, 'electronic' season passes to watch all of a club's games online could be accessed by a fan in Rio de Jineiro or Nigeria with a smartphone, massively expanding the potential broadcasting market. And MUFC have held pre-season tours to Asia to develop interest in that market.

Despite all of this, it is reassuring that, even in 2020, MUFC's financial success is all built off the back of pulling thousands of local fans through the turnstiles each week.

FOOTBALL'S REGULATORY REGIME FOR DEALING WITH INSOLVENT CLUBS

Steven Flynn

INTRODUCTION

Football clubs, unlike most other businesses, depend on the continued existence of their competitors. Without other clubs, there simply wouldn't be anyone to play.

In trying to ensure the survival of clubs whilst maintaining the integrity of the football pyramid, football's governing bodies have adopted regulatory regimes that monitor the financial stability of clubs (through financial fair play and sustainability rules), whilst also seeking to deter financial mismanagement. Clubs that become insolvent are very likely to suffer sporting sanctions. This article provides a brief overview of the English Football League ('EFL') regulatory regime. The Premier League and National League have different regulations that will need to be considered if advising a club that plays in, or may be promoted to/relegated from, those leagues.

PLAYER CONTRACTS

Often the first sign that a club is in financial difficulty are reports that it has failed to pay its players on time or at all. Clubs often see this as an easy option when cashflow is tight, believing that team unity will prevent the players from rocking the boat. To the contrary, failing to pay players on time can have catastrophic consequences.

EFL Regulation 63.7 states that 'The terms of a Standard Contract between a Club and a Player must be strictly adhered to'. Failing to pay a Player on time is a breach of EFL Reg. 63.7 and an act of misconduct. During the 2019/20 Season, a number of EFL clubs were the subject of disciplinary proceedings as a consequence of failing to pay players on time. The most notorious of these was the case of Macclesfield Town ('MTFC'). Between November 2019 and 27 May 2020, MTFC was charged with 84 breaches of EFL Reg. 63.7. Despite warnings and loans being provided to the club, MTFC repeatedly failed to pay its players and staff on time. These acts of misconduct contributed to MTFC being deducted 15-points, which resulted in its relegation from the Football League and subsequent dissolution.

INSOLVENCY EVENT & FORCE MAJEURE

When things have got to the stage where a club suffers an 'Insolvency Event' (widely defined to include entering into a CVA or being subject to an insolvency regime outside of England and Wales), EFL Reg. 12.3 states that a 'Club shall be deducted 12 points'. A club may appeal against this automatic deduction of points but 'only on the ground that the relevant Insolvency Event(s) arose solely as a result of a Force Majeure event' (EFL Reg 12.3.10(b)).

Force Majeure in this context is very narrowly defined as an event outside of normal business risks 'over which the Club…could not reasonably be expected to have control and its Officials had used all due diligence to avoid that event happening' (EFL Reg. 12.3.11). The word 'and' is emphasised because there can be a distinction between the actions of a club and its officials. In the 2019/20 Season, Wigan Athletic AFC suffered an automatic 12-point deduction after going into administration. Wigan appealed. The League Arbitration Panel found that some of Wigan's officials had exercised due diligence but that the true cause of the club going into administration was that its ultimate owner had made a commercial decision not to put any more money in. This meant that Wigan's reliance on the

COVID-19 pandemic and plea of Force Majeure was rejected.

The EFL Regulations include examples of what will constitute Force Majeure events. These include instances where a club suffers 'material adverse effects upon the loss of anticipated income streams' (e.g., a broadcaster failing to pay monies due under a deal as happened with ITV Digital), or default by another club that is 'significant enough to have a material and adverse effect' on the club. This second example is to limit the risk of a domino effect where one club brings down a number of others. The finances of football clubs are entwinned such that the insolvency of one club is likely to be felt throughout the ecosystem.

The EFL Regulatory regime is such that any club hoping to rely upon a Force Majeure appeal should undertake a detailed review of the causes of its financial misfortune. Only if it is a truly exceptional event is such a plea likely to succeed.

Even if a club has grounds upon which to maintain a plea of Force Majeure, then raising the finances to pursue an appeal can prove difficult. A deposit of £5,000 is required (EFL Reg. 12.3.13) and all 'costs incurred by any party to the proceedings…shall be met by the Club in any event' (EFL Reg. 12.3.19). Costs can quickly escalate. Reports in the summer of 2020 claimed that Wigan were expecting costs of in the region of £500,000. An appeal should not be lodged unless it has good prospects of success.

GROUP UNDERTAKINGS

EFL Reg. 12.3.2 deals with instances where a Group Undertaking of a Club suffers an Insolvency Event. In such circumstances, the EFL Board has the power to impose a deduction of 12-points, having regard to all the circumstances. Such a deduction is not automatic, and a club is allowed to make representations on why a sanction should not be imposed.

WHICH SEASON?

In the event that a sporting sanction is to be imposed, then EFL Regs. 12.3.3 to 12.3.8 detail when the points shall have effect. These provide for a number of different scenarios, including the deduction taking effect in the season following the Insolvency Event where the club would have been relegated in any event. This is to prevent a club whose relegation has been confirmed avoiding the practical effects of a points deduction. Bolton Wanders suffered an Insolvency Event in the 2018/19 Season, but the 12-point deduction was not effective until the 2019/2020 Season. The effect was that Bolton were relegated two-seasons in a row. Anyone advising a club in financial difficulty would do well to consider the timing of the Insolvency Event in the hope of avoiding a club going into freefall.

FAILURE TO PAY UNSECURED CREDITORS

If a club can be saved, then the EFL Insolvency Policy mandates that unsecured creditors receive a minimum of 25p in the pound (or 35p in the pound if paid over three years). Failure to meet this requirement will result in a further 15-point deduction the following season.

TRANSFER OF SHARES

Where rescue is impossible, then Article 4.5 of the EFL Articles of Association empowers the EFL Board to serve notice requiring the transfer of a club's share in the Football League to such person as the Board shall specify. This was what happened in the case of Bury FC, meaning an end to its 125-year membership of the Football League. In circumstances where the Board requires the transfer of a share, the price to be paid for what can be a very valuable asset is set at 5p. The limited value of the share when subject to a mandatory transfer emphasises the importance of being fully aware of football's regulatory regime when advising a club in financial difficulty.

Kings Insolvency 2021 Seminar Programme

On Thursday 25th March 2021, we will present a seminar looking at corporate rescue and directors' duties. Further details and speakers to follow.

The next edition of Kings Insolvency will feature details of our seminar programme for the remainder of the year on both corporate and personal insolvency. Our hope, of course, is to deliver these events live and in person but we may have to adapt depending on how circumstances develop and allow for that.

If you have have any suggestions for future seminars, or would like more information, please contact **seminars@kingschambers.com.**

FOOTBALL INSOLVENCY INTERVIEW

On a damp and windswept morning in Manchester in early 2021, and with a view to getting a handle on some of the practical issues raised by the insolvency of a football club, we interviewed, from a safe distance, Gerald Krasner and Paul Stanley, licensed insolvency practitioners in Begbies Traynor. In the interests of space, what follows is an edited version of the interview.

You're both long-established insolvency practitioners with plenty of experience in sports related insolvency. By way of introduction, what, at a general level, can you tell us about the nature of a football club insolvency appointment?

Paul Stanley: "Most football clubs are run at a loss. In order to pay running costs and essential creditors, an administrator is faced with cash flow issues from day one. At Wigan, for example, we were appointed on 1 July 2020 where wages had not been paid for June and where there were deferred wages of 30% per month going back to March. The club was losing about £800k per month, had no immediate funds to speak of, and so on day one we needed to find cash, and fast. There was no ability to raise finance in the timescales available and the major assets - the stadium and the training ground - were held outside the football club in companies which had their own creditors. The transfer window was not due to open until the end of July by which time the entire playing staff could have walked away from their contracts and moved away to other clubs for free. The English Football League were unable or unwilling to waive the transfer window for a single club, despite the circumstances. We were able, however, by concession, to sell 3 academy players to Premier League clubs. Those sales raised just under £2 million and solved the first month's funding issues. That was just the beginning.

Gerald, you're well known in football terms for your time with Leeds United. We'll come back to that. What's your career history with football insolvency?

Gerald Kranser: I started in insolvency 1978 and got my licence in 1986 when they were first issued. Excluding Leeds United, I've been involved with 4 football clubs formal insolvencies; the CVA of Boston United, and the administrations of Bournemouth, Port Vale and, currently with Paul, Wigan Athletic. I've advised a number of clubs on insolvency matters but obviously can't name them or say more. I've also done a number of lectures to fellow IPs and lawyers on various aspects of football insolvency.

Any particular highlights?

Gerald Krasner: Off the top of my head, highlights would certainly include: seeing Bournemouth promoted to the Premiership within 5 years of the club's administration; acquiring Leeds United and becoming chairman in 2004; being asked by an eminent QC to provide a detailed opinion on problems of a particular club facing insolvency; and saving Boston, Bournemouth and Port Vale. The jury is still out on Wigan, but we are working on that.

Paul, funding is, obviously enough, always a key factor in an administration. Any observations on funding as an issue in the context of a football club administration?

Paul Stanley: Most football clubs are run at a loss. In order to pay running costs and essential creditors, an administrator is faced with cash flow issues from day one. At Wigan, for example, we were appointed on 1 July 2020 where wages had not been paid for June and where there were deferred wages of 30% per month going back to March. The club was losing about £800k per month, had no immediate funds to speak of, and so on day one we need to find cash, and fast. There was no ability to raise finance in the timescales available and the major assets - the stadium and the training ground - were held outside the football club in companies which had their own creditors. The transfer window was not due to open until the end of July by which time the entire playing staff could have walked away from their contracts and moved away to other clubs for free. The English Football League were unable or unwilling to waive the transfer window for a single club, despite the circumstances. We were able, however, by concession, to sell 3 academy players to Premier League clubs. Those sales raised just under £2 million and solved the first month's funding issues. That was just the beginning.

Gerald, what can you tell us about your experience with Leeds United?

Gerald Krasner: I was never actually administrator of Leeds United although some people seem to remember it that way, maybe because I was both an IP and club owner. Together with some clients, we acquired the club in 2004 and carried out a restructuring exercise. In 2005 we sold Leeds to Ken Bates who put the club into administration some 2 years later, at which point KPMG dealt with it. I seem to recall you being involved in that, Louis. When we bought the club, it was circa £107m in debt, a relatively small sum in top-flight football terms today, but a very large one in those days. The main stories will have to stay private for legal reasons, but when I got to the bottom of the accounts it quickly became apparent that Leeds would have had to win the Premiership, the FA Cup, the League Cup and the European Cup just to break even. They didn't win any of them, of course. In buying the club we had to avoid any form of insolvency procedure. The holding company was quoted, with some 22,000 shareholders so, to avoid having to call a shareholders' meeting - God alone knows where we could have held such a meeting - we had to pay down the holding company creditors which cost us another £600k. I'm giving you sight of the very tops of the treetops here. The whole story would take rather longer.

Can you tell us something about the particular issues a football insolvency can present and how you think those issues can be capable of resolution?

Gerald Krasner: Cashflow is without doubt the biggest problem. The effect of the football creditor rule dictates that, without cash, an administration will not work. It's also almost impossible to do a pre-pack any more due to the English Football League's fit and proper person test.

Paul Stanley: I've mentioned funding already, but time-wasters can also be a real problem. Given the high-profile nature of the sport, there are many people who try to involve themselves in the sale/purchase process in the genuine but usually seriously misguided belief that they will somehow be able to get a commercial deal through to completion and then take up the mantle of running something as complex and idiosyncratic as a football club with zero experience and no money. In reality, most of these people, despite the outward appearance they seek to convey, do not have either the funds or the financial acumen or even the basic business experience to run a club, but dealing with them can still take up many hours of time, time that, ultimately, is completely wasted or, worse still, counter-productive to the extent that, dealing with matters on a face value basis, it's served to distract the office-holder's focus away from whoever is going to take the assignment to completion at the end of the day. It's also one of the reasons that an administrator is usually well advised to have no dealings with an apparently interested party without proof of significant cleared funds in a UK bank account. That stipulation usually puts the brakes on those who would otherwise like to tell their friends and the wider community that they're putting a consortium together to save the club. Equally frustrating are those whose interests are at odds with the interests of the football club as a whole. An obvious example of that is the property speculator who is only interested in how many houses will fit on a training ground. We've found that, by operating an electronic data room, we can analyse in a meaningful way the time spent by prospective purchasers on property, leases, contracts, forecasts etc. Every case is fact specific, of course, but any so-called interested party purchaser found to have spent, say, 95% of their time looking at a single asset such as the club's property can be detected and, if necessary, on further inquiry, excluded from the process if that is seen as being in the club's best interests.

Do the often highly emotive allegiances of fans and any supporters club offer any advantages or disadvantages?

Gerald Krasner: Paul touched on this in opening. Over the years, dealing with fans has changed considerably. In these days of social media, a number of fans want answers by the day, if not the hour. Personally, I prefer regular press or fan conferences, but that's just not possible under lockdown rules.

Paul Stanley: With an official supporters' club, one particular advantage is that you can sense check ideas or decisions. With Wigan, for example, it's public knowledge that the official supporters' club raised funds to enable expenses to be paid in the first month or so. They also raised funds to help with the purchase of the club. That was an enormous help, especially at such an early stage. The main disadvantage is the fact that fans in general want to know every event and every permutation of every decision involving their club and, of course, and understandably with something as idiosyncratic as a football club in which so much of a non-financial nature has been invested over long years, every fan has his or her own view. Whatever you do or don't do, there will be half who agree and half who disagree. The phrase 'you can't please all the people all the time' is one polite but nonetheless accurate way of putting it.

How important is exclusivity with any potential purchaser of an insolvent club?

Gerald Krasner: Put simply, no serious bidder will commit to a substantial deposit without exclusivity. If the administrators don't need a deposit, they don't need to grant exclusivity.

Paul Stanley: It also works the other way around in that it will usually be important to a purchaser who is putting up a deposit to know that they will get the club if they pass the EFL's tests on officers, directors and funding. A non-refundable deposit can also be a positive in terms of a contribution to trading costs where the process is taking time.

Do you think that sanctions such as the mandatory points deduction for administration are a good or a bad thing where a club is already in serious financial difficulty?

Gerald Krasner: My view is that sanctions may appear harsh but are necessary to keep a level playing field. It is no coincidence that, since their introduction, there have been far fewer football club administrations than previously.

Paul Stanley: There needs to be integrity in the sport. Clubs that overspend or don't pay for players they've signed need to know that there will be sanctions. A points deduction seems as good a sanction as any and will almost always have an immediate and obviously adverse impact on the football club which can be traced back directly to those responsible for the club's failing financial position. It's often missed that the risk of sanctions will also have the effect of forcing an owner to seek a solvent solution before looking at administration, rather than seeing the administration process as a simple and useful device for escaping financial difficulties. If that was ever the position, it certainly isn't any more.

Any views on the funding of football clubs generally?

Gerald Krasner: The football authorities should ask clubs to take out an Insurance bond to provide cash when problems arise. Also, they should require the submission of 6-monthly management accounts within 1-month of a period ending so that clubs can be monitored proactively. That would avoid problems coming out, often when it's too late or the financial position is far worse than it ever needs to become.

Do you expect to see more football clubs failing, especially given the effects of the pandemic?

Gerald Krasner: Definitely, yes, possibly up to 6 in my view. Our firm produces an annual health check on all football league clubs that is available from gerald.krasner@btguk.com

Paul Stanley: I normally would have said yes although, interestingly, the Premier League has pledged that no club will be allowed to fail during the pandemic. In my view, the major issues for football clubs are likely to come out months further down the line when HMRC start chasing the arrears of PAYE and VAT that have built up over the past 10 months.

Paul Stanley

Paul is the Regional Managing Partner of Begbies Traynor's North West region, based in Manchester. Prior to joining the firm in 1993, Paul qualified as a chartered accountant in 1987 with Arthur Andersen, working on audits, management consultancy and buy-out due diligence before specialising in insolvency and investigations. He has acted on approaching 2,000 insolvency and receivership cases, most recently the administration of Wigan Athletic. Paul also sits on Begbies Traynor's management and technical committees.

Gerald Krasner

Gerald is a Partner based in Newcastle, joining Begbies Traynor in 2007 having previously been the head of insolvency division of Bartfield. A qualified chartered accountant, he has worked on numerous insolvency cases, including Krasner v Dennison. Gerald specialises in providing advice to the football sector. In 2004 he became chairman and part owner of Leeds United AFC which had debts of circa £103 million, which he managed to reduce to £24 million before selling the club following year. He was also appointed as administrator of Bournemouth and Port Vale and is currently dealing with the administration of Wigan Athletic.

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Year of silk: 2008

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Year of call: 1996
Year of silk: 2020

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Year of call: 2006

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Year of call: 2019

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