Shifting the goalposts?

James Mendelsohn examines the status of the 'football creditor rule' applied when there are insolvencies in the national game

Last February, Glasgow Rangers became the highest-profile British football club to enter administration. Notwithstanding the large amounts of television and sponsorship money in the game, numerous clubs on both sides of the border have entered insolvency in recent years – nearly 40 clubs in England alone have done so over the last decade. One aspect of football club insolvency has particularly exercised the minds of lawyers – the so-called 'football creditor rule'.

The football creditor rule

The rule is found in the articles of association of both the Football League and the Premier League. Should a club become insolvent, 'football creditors' are to be paid in full ahead of any other creditors. For example, players' wages or transfer fees due to other clubs are to be paid in full before organisations which provide first aid or catering during matches.

The effects can be striking. When Crystal Palace FC entered administration in 2010, football creditors were paid in full, whilst the other unsecured creditors received a dividend of less than 2p in the pound.

The basis of the rule is that it is untenable to allow a club to remain in the league if competitor clubs are not paid in full. Last year, however, the Parliamentary Culture, Media and Sport Committee called for the rule's abolition, whilst Damian Collins MP described it as "morally unjustifiable." In *Revenue & Customs Commissioners v Football League Ltd* [2012] EWHC 1372 (Ch), decided in May 2012, HMRC asserted that it contravened two fundamental principles of insolvency law: the *pari passu* rule and the anti-deprivation rule.

Pari passu

This rule requires the assets of an insolvent person to be distributed to the unsecured creditors *pari passu* (rateably and equally) – all creditors should receive the same percentage of their debts out of the available assets. Hence, if the available assets of an insolvent company realise £50,000, and its creditors are owed a total of £500,000, they will each receive a dividend of 10p in the pound.

Parties may only contract out of the operation of this rule by creating security over the debtor's assets. Clearly, the football creditor rule does not create security. Moreover, it leads to situations where some creditors may receive all they are owed, whilst others may receive nothing. Unsurprisingly, therefore, many consider that it infringes the *pari passu* principle.

The anti-deprivation rule

This principle, formerly known as the 'fraud on the bankruptcy law', renders void any transaction which puts the assets of an insolvent person beyond the reach of its creditors. It is given effect in law by sections 238-241 of the Insolvency Act 1986, whereby a liquidator or administrator can recover assets sold at an undervalue within two years prior to a company becoming insolvent, or reverse 'preferences'; for example, the director of a company being repaid a loan in full ahead of other creditors within two years of insolvency. Similar provisions exist within the context of personal bankruptcy (sections 339-342 of the Insolvency Act 1986).

Unsurprisingly, since the football creditor rule appears to put the assets of an insolvent club into the hands of football creditors and therefore beyond the reach of other unsecured creditors, many believe that it infringes the anti-deprivation rule.

The goal of administration

In a lengthy judgment based on a detailed examination of the Football League's articles, however, the High Court has now ruled in *Revenue & Customs Commissioners v Football League Ltd* that the football creditor rule infringes neither the *pari passu* rule nor the anti-deprivation rule. David Richards J held that the *pari passu* principle was only relevant where the aim of the insolvency procedure was to make a distribution to creditors. That would always be the purpose of liquidation.

However, the primary goal of administration was to rescue the company as a going concern. Distributions would only be made in situations where the administrator thought that goal was not reasonably practicable (Insolvency Act 1986, Schedule B1, paragraphs 3(1)-(4)). The *pari passu* principle would only apply, if at all, in scenarios where the administrator was unable to rescue the company and, therefore, gave notice of a proposed distribution. Typically, however, the provisions relevant to football creditors would have taken effect at an earlier stage.

Meanwhile, the judge held that the anti-deprivation rule applied to administrations from their commencement. Having analysed exhaustively provisions relating to the payment of TV monies and the shares held by clubs in the Football League, he held that insolvent clubs were not thereby deprived of assets which might otherwise be available to creditors. Moreover, he held that League clubs were entitled to refuse to participate further with insolvent clubs save on the terms set out in the football creditor rule.

Although it is sometimes thought that the football creditor rule has no parallel in any other industry, the court highlighted similar rules governing the insolvency of companies participating in a stock exchange. Such rules had been held not to infringe the anti-deprivation principle.

The outcome will doubtless disappoint the non-football creditors of insolvent clubs. Nevertheless, the court emphasised that the judgment did not constitute a moral endorsement of the football creditors rule, and permission to appeal was granted. Clearly, those interested in football finance need to watch this particular ball carefully.

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