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UEFA's FFPR & 'third party' rules: an English handicap

Argentinean sports lawyer Ariel Reck and Daniel Geey of Field Fisher Waterhouse explain how Premier League clubs are likely to be at a disadvantage in UEFA competitions, due to rules banning any third-party ownership of players.

Since the Tevez controversy back in 2007, the Premier League (PL) and more recently the Football League (FL) and Football Association (FA) have banned a third party owning an economic interest in a football player who is registered to an FA club. Recently, Bosman[1] lawyer, Jean Marc Dupont, raised concerns about the compatibility of such restrictions with EU law.

This issue becomes even more topical when considered in the context of the UEFA Financial Fair Play Regulations (FFPR). It would appear that PL clubs wanting to participate in UEFA competitions are at a real disadvantage, because clubs who do not play in the PL are able to take advantage of alternative third party finance arrangements to purchase players. This may have the effect of reducing transfer costs for non-PL clubs, thus making it easier for them to break-even under FFPR.

The Porto example

Third party ownership relates to the sale to a third party (i.e. a private investor, another club or a company) of a future transfer value. The entity buying the share (or the previous club keeping it for a subsequent transfer) believes the player has the potential to be transferred for a higher fee than it paid for the transfer share. For the club employing the player, the sale of portions of the economic rights helps it to balance its books and find credit from alternative sources. While risks are high (i.e. the player might not fulfil his potential or get injured), so are the potential gains.

Most football analysts point to FC Porto's transfer policy as one of the key components for continued League, Cup and European success. Such a transfer formula is no secret. The club buys talented and untested players, mostly from South America, bloods them in the European competition and after a number of good seasons, shares the profit of a multi-million Euro transfer with its co-investors.

The old 'buy cheap sell expensive' secret includes a twist. Porto usually buys only a share of a player's economic rights, leaving the rest to the former club or (more often) to third party economic owners. This makes the acquisition cost even lower and minimises the risk of an expensive transfer mistake. Contracts with such third parties include clauses that allow clubs such as Porto to increase their share in the player's rights at given times and for pre-agreed amounts. Such a mechanism allows a club to raise its share in the player's economic right after he has established his worth in Europe. The most recent example is Porto's recent purchase of €13.5 million to Renistas in Uruguay for an additional 40% stake in their Brazilian attacker Hulk[2]. The same procedure was used with many players in their squad, such as Colombian James Rodríguez[3] or Joao Mouthino[4] among others. Clubs like Porto can also create revenues by selling the economic rights to investment companies after acquiring the rights in a previous transfer. This occurs by entering into an agreement with a company who is willing to take a percentage transfer stake in a Porto player in return for a set upfront fee. FC Porto's annual report[5] also sets out a number of interesting statistics including the fact that Porto only owned 100% of the total economic transfer rights to five members of their 27 man squad[6]. Additionally, economic rights can be exchanged or traded for other economic rights owned by the same company[7]. The financial report demonstrates that that the management of these economic transfer rights is inherent to Porto's transfer policy.

Benfica (Porto's rival) is now implementing a similar transfer strategy. It has been reported that Sporting Lisbon have gone even further by recruiting players with resources provided by a fund run by Jorge Mendes[8]. Some have even questioned whether such a transfer model complies with FIFA's regulations on third party influence on clubs (Article 18 bis).

Such practices are now widespread across Europe. Palermo made such arrangements with Javier Pastore's third party investors. Pastore recently transferred to Paris Saint Germain (PSG) for a reported fee of €50 million. Part of the PSG transfer fee was paid to private investors[9].

At the extreme end of the transfer spectrum, Real Zaragoza - a club in administration in the summer transfer window - bought goalkeeper Roberto from Benfica paying only €86,000. The total transfer fee was €8.5 million. It meant that a club in real financial difficulty was almost totally subsidised by private third party economic owners. This will no doubt tempt other Spanish clubs to copy such a procedure to purchase players who would otherwise be outside of their budget constraints.

Financial fair play context

The rest of this article will focus on the intersection between the prohibition on third party ownership in the PL and how that affects English clubs participating in UEFA competitions.

The current context, based on the

PL, FL and FA rules, is that third party ownership of players is prohibited10. It means that a buying club for any player whose registration is not 100% owned by the selling club, must purchase the economic interest in that player prior to registration with a club playing in the PL or FL11. Therefore clubs cannot share the burden with an investor in only purchasing 50% of a player's economic rights.

In order to adhere to the FFPR, clubs must break-even or fall within the acceptable deviation provisions in the FFPR. In order to participate in UEFA competition from the 2013-4 season, clubs will have to submit accounts (2011-12 and 2012-13 seasons) showing that they fall within the regulations. If they fall outside of the provisions, sanctions are likely to follow which could include expulsion from the relevant Champions League or Europa League competition[12]. The reason this has significance is because transfer fees (accounted for by amortisation charges in a club's accounts) and player wages are the largest costs for clubs.

It is likely that non-PL clubs will have a competitive advantage over PL clubs wishing to participate in UEFA competition. This is because their transfer expenditure may be reduced as they can share their outlay with companies willing to contribute to the fee. The basic point is that PL clubs will have to account for the whole of the transfer fee paid when submitting their accounts to UEFA. Non-PL clubs will presumably only have to account for the amount spent in taking - for example - a 50% stake in a player.

Non-PL clubs will have a competitive advantage over PL clubs wishing to participate in UEFA competition

A working example

Player A is available for transfer for €20 million. PL club Arsenal agrees to pay €20 million for the player but in order to register him, the club must to ensure that all third party economic rights are extinguished prior to registration. The club will therefore have a €20 million liability. Porto, if buying the same player, does not have to ensure that any third party rights are extinguished. Porto may even agree to pay the club for its stake in the player, e.g. €10 million with a third party company retaining their stake in a player. As discussed above, there may be additional options for the buying club to buy further stakes from the third party owner at designated times for set amounts[13]. Porto's liability is half the amount that Arsenal would be paying for the same player.

When factoring in such a situation for FFPR compliance, clubs usually value their players in their accounts as intangible assets through an amortisation cost. This means that when a player is purchased, his transfer cost is usually capitalised on the club's balance sheet and is written-down (amortised) over the contract length. Thus in the example above, if the €20 million player was bought on a five-year deal, Arsenal's amortisation cost for each year in its accounts would be €4 million (€20 million divided by five years). Porto's amortisation costs would be €2 million per season (€10 million divided by five years). Therefore, if both teams are participating in the Champions League and require a UEFA licence, which from the 2013-14 season includes adhering to the FFPR, then teams like Porto have an advantage. The flip side in taking less of a risk in purchasing a player is that the transfer revenues are split. Thus, transfer fees may not be as lucrative as if the club owned all of the player's economic rights. This can be avoided if a club puts in place options to acquire or reacquire further percentages at a given price.

PL clubs will be anxious that they are not put at a severe disadvantage when competing in European competition. This is no doubt one of the unintended side effects of the stand the PL initially took to ensure aspects of the 'integrity of the game' argument could be upheld. It may be, however, that clubs that are either in European competition or are aspiring to participate in European competition could decide that the PL restriction goes too far. The additional problem is that any PL or FL decision to change its rules would still require the FA to change its rules too.

Indeed, clubs such as Everton who are believed to have little transfer money available, may argue that they are being unfairly prohibited from sourcing additional capital investment from companies willing to enter into transfer financing agreements. This could lead to the PL or FL voting to change their regulations accordingly. An interesting alliance could develop within the PL, for example, when clubs that want to compete with other European clubs may see this as a large competitive disadvantage whilst other clubs that do not have the transfer resources to pay large sums may feel they are being stifled from finding additional finance. Both types of clubs would have incentives to see such a rule struck out or watered down.

Issues to do with FFPR related party transactions

There are no provisions expressly covering third party ownership of economic rights in the FFPR. Many commentators have tried to pick holes in the FFPR and assess how clubs can take advantage of loopholes and transitional provisions. Much has been written about the standard deviation provisions and Annex XI

exceptions[14]. More recently, much newspaper headline space has been taken up with Manchester City's reported 10-year, £400 million Etihad partnership and whether the deal falls within the related party transaction (RPT) provisions of the FFPR. By analogy, certain third party ownership transactions may need to be looked at by UEFA through its RPT provisions because there may be potential avenues available to circumvent the FFPR.

The basics of the RPT rule in the FFPR is that if an entity which is entering into a transaction with a football club has the ability to control or materially influence the club, then UEFA, after the initial licence application has been submitted, can investigate to see whether the transaction has been conducted at 'fair value' (there is some dispute about whether UEFA has a mandate to investigate unless the club itself flags the transaction as a RPT[15]). If not, UEFA has the ability - for FFPR application purposes - to amend the value of the transaction accordingly.

In Annex X(E) of the FFPR, reference is made to ' related party transactions and fair value of related party transactions.' The specific provisions of this rule are to ensure that owners and close associates of clubs are not able to:

- artificially inflate a club's revenues; or
- subsidise a clubs cost base in order to bolster the chances of passing the FFPR.

Annex X(E.7) of the FFPR states: 'A related party transaction may, or may not, have taken place at fair value...An arrangement or a transaction is deemed to be 'not transacted on an arm's length basis' if it has been entered into on terms more favourable to either party to the arrangement than would have been obtained if there had been no related party relationship'.

Such an instance could occur if, for example, an owner buying the economic rights of a number of players then sells those rights free of charge or at an undervalue to the club. Such a transaction could fall within the RPT rule.

By way of a practical example, if the owner of football club A owns 90% of the economic rights in player B and player B is bought by club A, such a transaction may be subject to further questions asked by the UEFA Club Finance Control Panel, including whether the deal represents 'fair value'. The underlying reason being that UEFA would not want club A to purchase the player on the cheap (i.e. under value), which would be another way for an owner to provide assistance to the club over and above any acceptable equity injections. How to quantify fair value for a transfer becomes a difficult proposition for UEFA.

Conclusion

Although the English football authorities may have thought they had seen the last of third party ownership, an interesting side effect of the FFPR has potentially brought the prohibitions back into the limelight. There appears little appetite on the continent for any similar prohibition, but the English PL clubs - who originally voted in the restrictions to ensure a Tevez-like scenario could not occur again - may be rethinking their approach at a time when transfer amortisation costs need to be balanced against revenues for FFPR compliance. When certain clubs may need to take radical steps to reduce their cost base to adhere to the FFPR, non-PL clubs participating in UEFA competition are at a particular advantage.

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Ariel N. Reck was the lawyer representing the company that owned the economic rights to Diego Faurlin.

1. Case C-415/93, available at http://eur-lex.europa.eu/smartapi/cgi/sga_doc?smartapi!celexplus!prod!CELEXnumdoc&lg=en&numdoc=61993J0415
2. See http://news.bbc.co.uk/sport1/hi/football/15298353.stm
3. www.reuters.com/finance/stocks/FCPP.MU/key-developments/article/2324935
4. www.reuters.com/finance/stocks/FCPP.MU/key-developments/article/2377227
5. from p62
6. www.fcporto.pt/IncFCP/PDF/Investor_Relations/Ingles/RCConsolidado20092010INGLES.pdf
7. See the Bollati - Falcao agreement on page 63 of the Porto Report.
8. www.vda.pt/en/press-centre/news-and-media/Sporting-Portugal-Fund/7488/ and http://mobile.bloomberg.com/news/2011-09-28/fifa-probes-soccer-investment-fund-run-by-ex-chelsea-ceo-ronaldo-s-agent
9. This transfer is now the subject of a bitter dispute between Palermo and the investors, headed by Pastore´s agent (footnote www.guardian.co.uk/sport/2011/sep/14/chelsea-juan-mata-javier-pastore)
10. See PL Rule L37-38 www.premierleague.com/staticFiles/bc/8a/0,,12306~166588,00.pdf, FL Rule 48 www.football-league.co.uk/regulations/20110629/section-6-players_2293633_2125731#46 and FA Third Party Rule Regulations on www.thefa.com/thefa/rulesandregulations. Even after the QPR Faurlin case, it is clear that the FA will allow a temporary suspension of those rights by its holder. A club must acquire 100% of the economic rights before registration. This represents a disadvantage, as explicitly recognised by the Regulatory Commission Panel in the QPR case in paragraphs 15.2-15.3.
12. For a detailed analysis of the rules see 'Financial Rules: UEFA's Financial Fair Play Regulations: analysis', World Sports Law Report Volume 8 Issue 12, December 2010 or visit www.danielgeey.com/UserFiles/ELSJ-UEFAFinancialFairPlayRules-UPDATED.doc
13. Such payments would have to be accounted for as a cost under the FFPR.
14. This allows for employment contracts entered into prior to June 2010 to be excluded from the break-even calculations.
15. See 'Financial Rules: UEFA FFPR 'related party' rules: Man City's Etihad deal', World Sports Law Report Volume 9 Issue 8, August 2011.

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