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FOOTBALL'S SUMMER 2020 TRANSFER WINDOW – A RETURN OF THE SWAP DEAL?

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'Swap Shop'

In the late seventies and early eighties, Saturday mornings were all about the TV programme, Swap Shop, which involved children swapping their belongings with others. During the week, school playgrounds would reverberate with the same sounds - 'got, got, need, got' - as Panini stickers would be swapped endlessly, albeit perhaps with less thought for the intrinsic value of the sticker (i.e. its rarity) than the perceived value of the player (which itself was often distorted by tribal loyalties).

Professional football itself has come a long way since the dark days of the 1980s, but might the innocent childish pursuits of those times be about to find a greater echo in reality? Given the significant impact of COVID-19 on the economy, football finances and, potentially, football regulation, could we see the player swap becoming more and more prevalent in the modern day?

The return of the English Premier League

In our earlier briefing dated 30 April 2020 (available here), we explored some of the key considerations around the return of professional football and other sports in England. Since, momentum behind 'Project Restart' has grown, a huge amount of work and detailed planning has been done and the Premier League has restarted this week.

In part, this has a social purpose, recognised by Government – the importance sport can play in society's emergence from lockdown and a return, at some point, to some sense of 'normality'. Football itself and some of its players are embracing this heightened sense of social purpose, most recently shown by Marcus Rashford's successful free school meals campaign, but also in the actions of various clubs and players around the country supporting their local communities in the response to COVID-19. Alongside such social consideration, however, clearly there is also a significant financial imperative to the return of football.

'It's the economy, stupid'

As football in the Premier League and other top European leagues restarts, clubs, players, agents, fans and commentators have also been thinking about what lies ahead in the summer transfer window. Some, perhaps with a self-interest to say so, have suggested that it will be 'business as usual'. However, that seems highly unlikely in the context of COVID-19 when you consider the significant impact it has had already on club finances, its likely enduring effect on those finances for an as-yet-unknown period, and the state of the wider economy as we enter a global economic downturn. For football is part of the wider economy. A very successful part through the life of the Premier League, but a part of the wider economy nonetheless.

In some respects, such 'business as usual' thinking is understandable: the top end of football, the Premier League, emerged pretty much unscathed from the Global Financial Crisis. That was predominantly, and at least initially, a banking crisis and football, and its transfer market, with its various sources of revenue, private funding and deferred payment structures, was able to maintain liquidity and largely carry on regardless.

COVID-19, on the other hand, is different: it is sector agnostic. Many industries face rapid and significant changes at the same time. Professional football is no different. Club income from broadcasters, through which Premier League clubs receive a significant proportion of their revenue, is likely to be materially impacted, and there will also be a loss of the usual match-day, and reduction in other commercial, revenues. At the same time, clubs' principal expenditure – the largely fixed-cost of player salaries – has, in the main, remained the same (some reported deferrals aside). This is not sustainable and it is not yet known how long these adverse financial impacts will last (in some form).

Regulation will also play its part: existing financial fair play (FFP) rules will feel even more restrictive for all but the very biggest clubs, but even a relaxation of FFP will only really help transfers involving clubs with cash to spend (i.e. those operating at the top of the market). Looking forward and as a response to the stresses of COVID-19, there is also the possibility of salary caps across some leagues (as seen in Premiership Rugby Union and in US sport such as the NBA). All of which must have an impact on how clubs (are able to) transact in the upcoming transfer window.

Deal activity

A football transfer is, at its heart, like any other M&A transaction, requiring a willing buyer and willing seller, both able to settle on an acceptable value of the target asset (the player). In addition, and unlike most deals in other sectors, it requires a willing 'target'. In circumstances where the buyer is cash constrained and/or faces real uncertainty over its revenues in at least the short and medium term, and the seller is liquidity constrained or facing similar difficulties on a parallel deal where it is the buyer, it is more difficult to reach agreement on 'value'. Put simply, there is downward pressure on values, the likelihood of greater divergence of views and, as a result, deals get more difficult to do.

In a separate briefing last month (available here), we looked more broadly at the subject of M&A activity in the COVID-19 and post COVID-19 world. Every economic crisis impacts M&A activity and we have seen already a significant fall in global M&A in 2020: in the early part of this year, global M&A fell c.30-35% year on year. However, prior economic crises also show us that the market and its participants find a way to adapt and there is usually a recalibration of deal type and terms. The same will be true of transactions in the sports industry and football transfers more specifically.

A related question is when the summer transfer window will take place. Before the suspension of the current season, the English window was scheduled for 10 June 2020 until 1 September 2020. The FA and the Premier League are yet to confirm how the window dates will be revised to take account of the extended 2019/2020 season. At this stage, it looks likely that the window will start when the extended 2019/2020 season ends. However, it is not clear whether it will conclude on its originally scheduled end date of 1 September 2020, or else be pushed back to allow a longer window. However, whatever the specific dates of the summer window, the impacts of COVID-19 will be ongoing and therefore remain the same.

Football, at the top end at least, is also a global market and therefore it is not just the English transfer window that is relevant. FIFA has given national associations some latitude to reconfigure their transfer windows. An interesting issue will therefore be how, if at all, national governing bodies can harmonise transfer windows with each other, especially the other major European leagues such as Spain, Germany, Italy and France. UEFA is urging its member associations to adopt a harmonised closure of this summer's window on 5 October 2020.

But with different countries recovering and relaxing lockdown measures at different rates, and their national leagues having different approaches and timetables to resumption (or curtailment) of their 2019/2020 season and commencement of their 2020/2021 season, and a preference (in normal times) to close the transfer window immediately before, or at least very soon after, the commencement of their domestic season, the interaction between the timing of different countries' transfer windows may well be another key contextual factor impacting international transfer business in summer 2020.

Summer 2020 transfer window

Against this backdrop of strained finances, uncertain revenues (at least in the short and medium term) and ongoing uncertainty over transfer window dates, what will be the impact of COVID-19 on the football transfer market this year?

As noted above, a football transfer is fundamentally like any M&A transaction – it requires a willing seller and a willing buyer (plus, in this case, a willing subject matter in the player itself).

There are likely to be willing sellers – clubs will be open to selling players deemed surplus to requirements to bring in cash flow and reduce their wage bill. Indeed, in the same way we talk about distressed M&A more generally, it would not be surprising to see some clubs having to sell some of their best and/or most expensive talent. This could give well-capitalised, or perhaps more financially risk-taking, clubs opportunities to buy players at discounted prices.

From a footballing perspective, some clubs may have gaps in their squad that they need to fill, others that they would ideally like to fill, and clubs may also want to be 'fully stocked' in case certain players become ill or have to self-isolate in the future.

However, the bottom line is that buying clubs are likely to have less cash, and likely to be more cautious (at least in general) to use available liquidity or 'stretch' themselves financially, than they were prior to the occurrence of COVID-19. And ultimately that is likely to mean a reduction in both the size and number of transfers, and fewer of the big money 'blockbuster' deals of recent windows, though a select few of Europe's wealthiest clubs may still be able to transact outside the constraints felt across the rest of the industry. There is also the question of valuation – how will clubs put a value on players in these circumstances and with ongoing uncertainty from both a financial and footballing perspective?

Player swaps as a means to bridge the liquidity and value gap

In the wider economy, we are expecting to see an increase in share for share transactions as part of global M&A activity. Crucially, these enable parties to preserve cash in the short term, and can also remove the need to agree an absolute value of the target at the time, instead focusing on the relative values of the two parties. While football clubs would not issue their own shares as transfer consideration, the equivalent recalibration in the football transfer market would be player for player exchanges, i.e. player "swap" deals.

A player swap deal is a simple concept of mutual consideration. Club A transfers Player Y to Club B, and in return Club B transfers Player Z to Club A. Unless the players are deemed by the clubs to be of equal value, there will also be a balancing monetary payment or other consideration, perhaps another player added to the deal. These sorts of swap deals are common enough in other sports competitions, such as the NBA (where, as noted above, there are roster salary caps).

Players swaps are also not a new concept in football: there have been high-profile swap deals over the years, both domestic (Sánchez / Mkhitaryan) and international (Ibrahimovic / Eto'o). However, they remain relatively uncommon. There are a number of reasons for this – not least, the need for players willing to move in opposite directions at the same time. However, perhaps summer 2020 is the right time for a reprisal.

The main appeal for buying clubs is that it allows for a transfer without the need for immediate cash expenditure (there are still player wages to pay over the course of the player's contract) and therefore liquidity. In an 'equal' swap deal, there is no cash payment; if not equal, it is still a lesser, balancing payment. The flipside of course is that the selling club will not receive cash proceeds for the player they are selling, and so it is not an answer for a club in need of immediate liquidity.

However, it may improve the liquidity for a club if the wages of the new player are lower than those of the player being swapped out. This might be a driver for any cash-constrained clubs (especially EFL clubs if they do become subject to salary caps), and could even lead to a different type of market that is more focused on salaries than transfer fees, and where there is real strategy to a club's trades in order to stay within the confines of an aggregate cap (as one sees in the NBA).

Swap-specific considerations

Assuming that a swap deal can be put together (i.e. two clubs and (at least) two players that match their respective needs and are willing to transfer), there are a number of considerations for clubs:

- **Inter-conditionality** - it is of course critical that one transfer only happens if the other transfer also completes. So some additional thinking and co-ordination is required about the legal (relatively straightforward contractual provisions) and practical (medicals, work permit processes, announcements, etc.) implications of the transfer process.
- **Execution risk** - allied to the above, the need for at least two players to agree to the move, to pass relevant medicals, to obtain a work permit (if required) etc.
- **Need for a valuation** - though one benefit of a swap deal is that two clubs do not, in the midst of market uncertainty, necessarily have to agree an absolute valuation of either player being transferred for the purpose of determining a transfer payment – the clubs can just agree that Player Y is the same value as Player Z (whatever that value may be) and therefore there is no balancing payment. Or that the value of Player Y is £5m more than the value of Player Z, so there is a £5m transfer payment. However, a valuation will be needed for insurance purposes and, in due course, accounting reasons.
- **Existing sell-on provision** - if the transferring club agreed a sell-on provision when it bought the player, and that sell-on provision was properly drafted by the then-selling club, a valuation of the player will be required to determine whether any sell-on consideration is triggered and, if so, how much. The parties may determine a valuation for this purpose (see below) though to satisfy the original selling club it will need to be a reasonable, good faith valuation. Even then, subject to the terms of the original sell-on, the valuation may need to be determined by, for example, a third party, independent expert or via arbitration through the relevant football authority channels.
- **New sell-on provision** - if the terms of transfer include a future sell-on provision in respect of either player, and that sell-on is to be calculated by reference to any profit or increase in value of that player received by the transferee club, the clubs will need to agree a base value in order to calculate

that sell-on on the future transfer of the player.

- **Solidarity levy** - there is also a regulatory overlay to this: FIFA Regulations on the Status and Transfer of Players require the buyer to pay a 5% "solidarity levy" to previous clubs who have contributed to the training of a player. This applies to international transfers and, as of 1 July 2020, domestic transfers to the extent that the player's previous clubs are based in a different country.

  The jurisprudence of FIFA's Dispute Resolution Chamber is clear that solidarity levy applies to swap deals even though there is no (or only partial) monetary consideration. As such, if a swap deal has such an international component, the clubs will still need to agree a valuation of the players in order to discharge their respective obligations (each will be a buying club in respect of one player) in respect of solidarity levy. It will be interesting to see whether the game's supra-national or domestic governing bodies provide further practical guidance for the determination of such valuations if swap deals do become more common.

Recalibrating deal terms

Of course, swap deals are only one part of the recalibration that may take place in the transfer market. Other areas that may be subject to greater focus include:

- **Transfer compensation structures** - bespoke and complex transfer compensation structures are already the norm, but the circumstances of COVID-19 may see specific changes: for example, the further 'pushing out' of deferred consideration (if the selling club is willing to take the credit risk on the buying club?), a greater dependency on contingent compensation linked to events that generate actual revenue for the buying club and future sell-on clauses.

  The typical contingent compensation triggers could also be used to bridge the cash flow concerns of the buyer with the value expectations of the seller, such as providing for increased payments from buyers later if they satisfy revenue-generating triggers such as European qualification or avoiding relegation. These triggers could become even more bespoke to meet the ongoing nature of the crisis, such as contingent payments that are only due if the following season can be played in full or more explicitly linked to the buying club's future TV or other revenues.

- **Loans** - clubs may increase their use of loans, both in (obtaining a player without a transfer fee) and out (removing a player from the wage bill). Loans can be structured with or without loan fees and with different allocation of player salary between loaning and loanee club for the duration of the loan period, and so offer flexibility for solving shorter term liquidity issues without necessarily involving significant expenditure.

- **Free transfers** - players who will be 'out of contract' this summer and therefore 'free agents' may be more attractive to (immediately) cash-constrained clubs. The most talented and high-profile free agents will undoubtedly be in great demand and may be able to negotiate an increase in overall salary packages (notwithstanding the immediate financial environment), especially over the course of a longer term contract, as a result. Conversely, there may be free agents lower down the football pyramid who struggle to find deals where clubs are struggling to justify paying new wages, whether due to general financial constraints and/or proposed EFL salary caps.

- **Salaries** - as well as its decelerating impact on transfer fees, the crisis is likely to exert downward pressure on player salaries, at least in the short to medium term, as clubs come to terms with a new balance sheet and financial environment. As noted above, this will be felt mostly keenly domestically through the EFL (especially in a world with salary caps), but would impact the Premier League too. Existing salary levels will also be a factor, of course, when considering whether to sell a player, especially where clubs need, or want, to keep all options open for conserving cash and therefore reducing the existing wage bill. Unlike many other businesses, such cost-reduction exercise can only take place, on a controlled basis, during the transfer window.

- **COVID-specific provisions?** – it remains to be seen whether clubs and/or players will look to introduce some wider flexibility or different terms in player contracts to reflect some of the recent experiences arising from COVID-19 and the lockdown: e.g. flexing the term to provide for the extension of a season beyond 30 June?; automatic salary reductions and/or deferrals in the event of football matches not being able to be staged as a result of law or regulation?; fitness, holiday or other behavioural obligations in the event of an enforced mid-season gap where no matches can take place?; a greater link between club revenue and wage levels (aside from an automatic reduction in the event of relegation)?

Clubs, players, agents and indeed football authorities may well wish to consider all or some of the above as and when we proceed to the 'lessons learned' stage of COVID-19.

Concluding remarks

Unlike the Global Financial Crisis, COVID-19 has impacted football, and its finances, at all levels, including the highest. In such circumstances, it seems evident that there will be significant changes to how football's international transfer market will operate in the short to medium term, including the upcoming summer transfer window.

The financial pressures that all clubs will be feeling is likely to translate into fewer of the big cash 'blockbuster' deals of recent years. Regulatory considerations around FFP and salary caps may also have an impact. But football and the transfer market will not stop. Rather there will be a recalibration of deal type and terms as market participants (clubs, players and agents) explore different structures in order to transact, including looking more keenly at player swaps.

If you would like further information about this topic, please contact Andrew Jolly, Paul Mudie or Hemita Sumanasuriya, or speak to your usual Slaughter and May contact.

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