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‘*Not quite as expected?*’:
An Investigation of the Regulation of Insolvency as applied to English Professional Football Clubs.

A dissertation submitted for the degree of LL.M. by Research

By Frederick Thomson

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‘*Not quite as expected?’*:
An Investigation of the Regulation of Insolvency as applied to English Professional Football Clubs.

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Abstract

This dissertation reviews the theory and practice of Regulation and its application to professional football. The exploration uses the legal pivot of the 1986 Insolvency Act with subsequent amendments and consolidations to analyse the activities of regulatory agents (Insolvency Practitioners), industry bodies (the Football League) and directors (owners of football clubs) in the context and conduct of affairs relating to Corporate Insolvency. The operation of *The Football Creditors' Rule* receives specific scrutiny. At the heart of this investigation lies '*The Puzzle'* in that, historically, firms in this industry seem exceptionally likely to suffer an insolvency event yet appear exceptionally unlikely to be wound-up. The causes and consequences of this paradox are probed via a journey from theory to practice in the development of the study.

Whilst '*unexpected consequences*' attend many human activities, this thesis is novel in its examination of phenomena in which many taken for granted assumptions are not wholly delivered as expected. The ideas driving the review are obtained from extensive reading of published material and the data are obtained from on-line published sources and are often couched in systems terms. In the main, the data refer to the period 1986-2016 and relate to the full-time English Football industry. The discussion and analysis of data within the thesis are categorised in the manner of Merton's Law of Unintended Consequences. The results of the enquiry pay special heed to issues relating to the accountability of key actors for both the manner and the outcome of their actions; to the need for greater energy to be devoted to how understanding of the complexities surrounding insolvency might be achieved by more effective communication styles/ methods; and to the suggestion that regulation of insolvency and the practice of insolvency law may be better accomplished via an approach which is both fine-tuned and industry-specific.

Prologue

'*Ye don't know what you're doing, Referee!*'[1] This abusive yet plaintive cry hurled by a spectator was the author's introduction, as a young boy watching his first 'big' football match with his grandfather, to an adult world. This was a world in which the spectacle was conditioned by 'rulers' controlling the behaviour of the 'ruled' via the device of 'rules'. That the application of these rules was inconsistent and not wholly understood by those to whom they applied merely added to the delicious unpredictability of the occasion for the author.

In the best Proustian[2] sense, this recollection sowed the seed from which this dissertation has developed into an academic examination of *Regulation* as applied to the world of football.

[1] Motherwell v Rangers : Fir Park Stadium, Motherwell October 1952.

[2] Marcel Proust's '*A la recherche du temps perdu*' .. but with Scotch Pies substituting for the madeleines !

Chapter 1: An Introduction

This dissertation can be seen to be about *THE* law and about *A* law. Although primarily socio-legal in perspective, it freely borrows concepts from other intellectual fields in order to provide a cross-disciplinary view and examines an area harking back to Roman times … that of *'panem et circenses*' ... the games designed for mass popular appeal, in this instance, professional football. The work is constructed in a style not unlike the tartan design on a Scottish kilt. There are dominant colourways such as Regulatory theory, Regulatory practice and the Insolvency Act 1986 which interweave with subdominant themes such as the profession of Insolvency Practitioners and the world of English professional football. In the kilt, these combine in a complex, yet ultimately logical manner, to determine the end product. The discussion produced here follows this kilt design style in its development.

What follows explores a relatively obscure area of organised human behaviour; the activities of financially distressed football clubs. What is of interest is the way in which matters are not entirely as they may seem at casual glance ... nor do they quite conform to openly declared rules of intention and causation. In short, the exploration is of a Wonderland in which Alice might have been comfortable.

The Puzzle:

Central to our discussions is the Puzzle which initiates the enquiry. Baldly stated, this is "Why do so few English football clubs '*go bust'* ?" The pursuit of an answer to this question leads the discussion in unexpected ways.

Scoping of the Topic:

It is usual in commentaries such as this to offer some words on framing the field but even at this early stage, a little of the out of focus character of the ensuing investigation begins to become apparent.

Here, one might easily set a temporal scope; events from 1986 till the present day. The enactment of the Insolvency Act in 1986 provides one convenient bookend to this

dimension ... but the placing of the other bookend is less felicitous. Most of the empirical work in the literature in this area runs till around 2012-13 as do the observations on European Law[3] However, that admirable source of football economic and legal data, Deloittes,[4] continues to be published annually and underpins general thinking throughout.

A working geographical scope has been established in the title as being England. But even allowing for the ellipsis into England and Wales, some celebrated cases[5] from Scotland have been mentioned in reports relating to cases involving English football clubs. The law on corporate insolvency in Scotland is not materially different from that in English Law. Additionally, top-level football clubs who compete in international competition render themselves subject to European legislation.

The study will, naturally, concern itself with the quest for success of professional football clubs. The notion of 'success' (or being successful) might therefore be put forward as a scoping criterion ... but closer consideration leads to the observation that this might be a fruitless avenue to follow. It seems clear that economic success is neither sought nor achieved[6] by football clubs ... strategically, survival may be the principal economic objective in most instances. Other dimensions of success may be, at least in part, be more significant. There is, quite probably, significant personal status (hence social success) to be gained by owning a football club which has achieved/is achieving competitive superiority against its rivals ... one notes the (increasing ?) numbers of club owners who have difficulties with the footballing authorities in regard of meeting the 'Fit and Proper Persons'[7] test before acquiring the club. In passing, it might also be appreciated that even the idea of 'ownership' is not without controversy ... owners may

[3] Possibly the moves towards Brexit have dulled an enthusiasm to publish in this field .. or perhaps there has just been little of interest to report?

[4] Deloitte's Annual Review of Football Finance: Deloitte UK.

[5] Perhaps that involving Glasgow Rangers is the most recent (2012) .. and certainly the most prominent; others include Heart of Midlothian (2012) and Gretna (2008).

[6] Notwithstanding this point football clubs in this study rarely make much money on a year by year basis such is the competitive intensity which provokes extraordinary expenditure in acquiring superior playing talent.

[7] See Chapter 7 later.

have economic and legal title to the club[8] but fans may feel they have an enduring ownership of a social type; a communal right akin to '*the Commons*'.

The descriptor *'professional'* football club is, thankfully, lucid and used as a shorthand for teams in the top four leagues in England ... where all players receive taxable payment. In contradistinction, teams in lower leagues who may well have players signed as amateurs (no taxable payment). [9] [10]

However imprecise these frames seem, they do have a fair degree of functionality in that they help both reader and writer make sense of the chosen topic. So, the investigation will go forward to review matters which mainly took place over the 30 years from 1986, which mainly involve the top 90 or so English professional football clubs and which relate to situations in which some of these clubs have found themselves in 'financial distress'. The level of English football studied here is organised into four divisions. The top division which includes the elite clubs has a membership of 20 clubs whereas the remaining three (Championship, Leagues 1 and 2) each have 24 participating clubs. The practice of promotion and relegation between all four leagues gives a substantial spur to playing performance with exceedingly large economic consequences for both success and failure on the pitch.

Regulation clarified:

'Regulation' is also a term which encourages unpacking with its implications for clarity as to regulator/ruler as compared with regulatee/rule-follower. Immediately, there arise questions as to who fills what role ... and what 'qualification' is needed for the role. Consequential questions as to why regulation is required at all, what the purpose of the regulation may be perceived to be and what style/mode the regulation might best exhibit do need to be addressed. Regulations are seen as being 'rules of order having the force

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[8] Although not always to the club's ground and other facilities.

[9] Such players, of course, no longer receive banknotes in their football boots for travel expenses as did the author as an undergraduate.

[10] This matter is highly significant and was a major feature in the HMRC's action against Glasgow Rangers ... and, presumably, was the principal motive force in the landmark Football Creditors' Case (see Chapter 6 later.)

of law, prescribed by a superior or competent authority, relating to the actions of those under the authority's control.' [11] These would be issued to carry out the intent of the regulator. Conventionally, the regulator would be the state but an expanded view of regulation will be taken in what follows. The treatment of regulation for the purposes of this dissertation will lean towards the conceptualisation in the sociological and/or business fields.

In the wake of such consequential questions lie deeper considerations of the part to be played by communication as an aid to rule-conformance, by sanctions as encouragement by actors to conform, by agents who may act as delegated/proxy regulators on behalf of rule-makers or by adjudicators /facilitators who bring enlightenment and/or realistic solution-building to complex situations.

Systems terms in precis:

This exploration will often use a systems approach as an analytical device. This approach is commonly used in Engineering and in Medicine and it has an across-discipline perspective which will be useful in this study. It will allow legal ideas to be framed and fruitfully developed in relation to an environment which is evolving and in which resources available to interacting actors cannot be taken as given. Whilst no deep understanding of systems theory is utilised, some key ideas are used to marshal the discussion. Accordingly, a very brief outline of terms is now offered. Systems are collections of elements (sub-systems) which are inter-connected and which often are designed to deliver some objective. These elements are inter-related and inter-dependent; if such relationships fail, then the original objective will not be reached … which is not at all to say that no outcome results. They may work together (coupled) or, for a variety of reasons, may not.

Systems theory frequently asserts that the aims of the overall system ought to have priority over that of any element. The word *ought* carries significance ... connoting a duty. In what follows, this will be seen to be problematic. There is the assumption that systems are ordered which in some way delivers the (larger) system's aim and that the

[11] Taken from legal-dictionary.thefreedictionary.com / regulation

elements are able to interact one with another. We will examine whether ability to interact equates to capacity to interact during our discussion. The concept of interdependence[12] implies a degree of co-ordination between elements/subsystems for the effective delivery of an aim (or, indeed, of multiple aims) and raises the question of the degree of integration/ cohesiveness of the overall system. The aims may be real or stated … the reality is that social systems (the type we discuss) may frequently overtly aver one aim and covertly pursue another ... a result which we will note later.

From this can be derived four potential assessment measures for the operation of such a system as will be examined in later discussion …

- ➢ System purpose[13] … what is the desired aim and what benefits are expected (and to whom)?
- ➢ Accountability[14] … who is responsible for achieving the aim(s) (stated or otherwise) of the system … and how might success be measured?
- ➢ Clarity [15]… how understandable is the functioning of the system … to what extent is misinterpretation of written material/legal instruments a handicap to delivering aims?
- ➢ Repeatability[16] … how consistent (and predictable) is the operation of the system?

These will all be used to estimate the way in which the Corporate Insolvency system operates.

Also of relevance are the thoughts that systems have boundaries which may or not be permeable to pressures (inputs) from the outside environment. These inputs may/may not be deliberate (ie. intentional) and so their results (outputs) may/ may not be as planned. The extent of permeability is often, simplistically, labelled as *open* or *closed* in relation to the amount of external influence on the system. Here we see such matters as

[12] Here understood as a relationship implying some mutuality which need not be symmetric.

[13] Who gets to articulate this can be of especial interest.

[14] Accountability to whom ... and what sanctions come with failure?

[15] Questions of different ‘languages’ spoken by different actors become relevant.

[16] Chaos ensues when the system delivers different outcomes to a series of similar inputs.

being on a continuum[17] rather than being polar extremes. Finally, and crucially, regard needs to be paid to the constraints to which actors in the sub-systems are subject … being always aware that these constraints will vary over time for multiple reasons.

Unintended Consequences introduced:

The analysis of material brought forward in each of the main chapters will, inter alia, employ a somewhat crude usage of the eponymous Law of Unintended Consequences. Principally[18] associated with work of Robert Merton,[19] this ’Law’ suggests that there are three main possible outcomes which may be caused by one or other of five main causes.[20] These outcomes are, in turn, ‘An Unexpected Benefit’;[21] ‘An Unexpected Drawback’[22] and ‘A Perverse Result’.[23] The causes are listed below ...

1. Ignorance, making it impossible to anticipate everything, thereby leading to incomplete analysis.
2. Errors in analysis of the problem or following habits that worked in the past but may not apply to the current situation.
3. Immediate interests overriding long-term interests.
4. Basic values which may require or prohibit certain actions even if the long-term result might be unfavourable (these long-term consequences may eventually cause changes in basic values).

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[17] Which provokes consideration of “to what extent?” type questions.

[18] Although economist Adam Smith with his ‘*invisible hand’* quite possibly has an earlier input to the notion. He (and much later, Bastiat in ‘What is Seen and What is not Seen’) analyse events in a manner redolent of systems theory.

[19] In "The Unanticipated Consequences of Purposive Social Action" (1936).

[20] Merton’s ‘causes’ will be returned to the concluding chapter (Chapter 8).

[21] A positive yet unanticipated benefit is made available to one or more of the principal actors in the system.

[22] An unanticipated detriment which accompanies the wished-for effect of the regulation.

[23] An outcome quite contrary to the original aim of the regulation.

5. Self-defeating prophecy, being the fear of some consequence which drives people to find solutions before the problem occurs, thus the non-occurrence of the problem is not anticipated.[24]

The discussion of each chapter analysis will then be synthesised into the overall conclusions in Chapter 8.

Reader signposts:

This thesis develops beyond a scene-setting introductory chapter[25] by engaging firstly with the central concern of the thesis, that of regulation. In this chapter[26] a bewildering variety of perspectives along with multiple approaches are articulated and a tentative chapter summary is offered. It is no real surprise to note that the literature in this field is extensive yet consensus as to the most effective approach(es) is/are not easy to find. The next chapter[27] attends to 'the real world' of regulation by exploring regulatory strategy and examines causes of regulatory failure, considers some aspects of regulatory weakness and comments upon areas of regulatory deficit. This leads naturally to probing concerns held by some as to the nature, style and extent of communication between the regulator (and agent) and the regulatee before deriving further reflections.

The ensuing chapter[28] presents a provisional look at the notion of 'accountability' ... after all, if matters do not go entirely to plan, then someone may/should be held to account? It returns to the issue of accountability raised in the second chapter and examines both accountability principles in addition to a review of accountability issues before yielding a further short set of conclusions.

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[24] This list is acknowledged as being from Wikipedia.

[25] Chapter 1: Introduction.

[26] Chapter 2: Regulation ... as an Idea.

[27] Chapter 3: Regulation ... in Practice.

[28] Chapter 4: Accountability.

Given that a continuing theme throughout the piece is one of uncertainty in many aspects, it was felt that the metaphor of *The Casino,*[29] where rules, actions and outcomes are affected to some extent by chance or ambiguity, might be a suitable device by which to unroll the basic legal platform of this discussion. In turn, the roots of the key legislation, the principal 'players' in the Casino, the major 'set-plays' or choreographed legal manoeuvres and those instances which may be difficult to deal with for cross-cultural or for moral reasons also receive attention. Some fundamental ideas in respect of the English law on Corporate Insolvency are established as are outlines of the enforcement strategies associated with corporate insolvency.

The transit in the discussion from theory to practice moves further in the real world to a contemplation of the practical detail surrounding insolvency in English professional football. This review[30] commences by looking at the landmark case in which HMRC sought[31] to overturn the effects of the notorious 'Football Creditors' Rule.' Related material on Financial Fair Play and on the notion of '*The Sporting Interest*' is also surveyed;[32] the latter being a notion that Alice's Queen of Hearts would have certainly warmed to ... briefly, '*the law does not apply to me!'* Finally, a Concluding Discussion[33] is offered.

Method:

This thesis was developed around a methodical review of current and significant literature. In the first instance, the original research puzzle[34] was the starting point for the construction of a series of mind maps. A consolidated version of the map was then used as a basis for Google Scholar 'anchor points' … which, in turn, allowed a search for suitable books and articles. Notes taken from these sources form the basis of the

[29] Chapter 5: The Insolvency Casino.

[30] Chapter 6: The Football Creditors' Rule.

[31] HMRC v The Football League and FA/Premier League [2012] EWHC 1372 (Ch)

[32] In Chapter 7: Pan European Developments in the Sporting Field.

[33] Chapter 8: Concluding Discussion.

[34] Subsequently amended in the light of developments.

thesis. These notes were supplemented by electronic material obtained from more popular sources such as major consultancies,[35] reputable newspapers[36] and sector-specific magazines.[37] This latter material, although not peer-reviewed, was deemed essential to flesh out the academic literature and to provide some topicality. The approach is, in turn descriptive, interpretive and analytical with insertions of critique both in the body of the development of the various sections and as crucial components of the chapter conclusions and the concluding synthesis.[38]

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[35] Such as Deloittes.

[36] Such as The Guardian.

[37] Such as *Recovery*, the monthly magazine of R3, the group representing Insolvency Professionals.

[38] Whilst the core writing was carried out in 2016-17, the remarks are believed to be up-to-date as at August 2018.

Chapter 2: Regulation

2.1 <u>Preliminary Thoughts</u>:

As a re-iteration of The Puzzle at the heart of the thesis, it is useful to highlight the domain of interest (corporate insolvency in professional football); to note some unexpected recent outcomes; and to raise the question of whether key actors regard these outcomes as being 'satisfactory.'

That there are likely to be a variety of causes for the existence of The Puzzle is taken as given; some speculation as where these causes might lie are explored in the discussion to follow.

There are factors in play in this discussion which may be uncommon. There exist two levels of regulatory authority between the legislature and those whose behaviour is to be regulated. These 'meta-regulatory' regulators are firstly, the football authorities (whose Football Creditors' Rule stands in defiant and continuing opposition to stated law) and secondly, the various Recognised Professional Bodies (RPBs) who regulate the professional conduct of such groups as the Insolvency Practitioners.

The system of regulation being scrutinised is complex and comprises different actors each in their own sub-system which interacts with other sub-systems in unpredictable and in unproductive ways. These actors include Football Clubs and their owner-directors; the football authorities and the RPBs; the Insolvency Professionals whose job it is both to help financially distressed clubs and, potentially, to investigate the conduct of directors of clubs; the Insolvency Service and at, one remove, the Courts and the Secretary of State. There also exist diffuse interest groups such as football supporters; TV companies; and local authorities (who in some instances are also the Landlords of the football clubs). These actor-groups have connections, one with another, which are at times defined by the law ... and at times governed by relations of a different nature. In what follows, mention will frequently made of "The Football Authorities." In England, these comprise of The Premier League (PL), The Football League (FL) and The Football Association (FA) .. all of which adds to complexity! The FA have oversight of

"the rules of the game" (ie soccer); the PL is the principal beneficiary of TV broadcast money and is the top tier in the sport. The FL collectively looks after the other three tiers in the English game.

Perhaps the most obvious tension between the Insolvency Act and the private rules of football is revealed[39] by The Football Creditors' Rule which inserts a form of super-creditor above the claims of preferential, secured and unsecured creditors. In the event of a professional football club entering administration, by the private rules of the football authorities such a club may only continue as a member of the appropriate league if it exits Administration [40]via a CVA[41] and by paying football debts[42] in full. Thus, on exiting Administration, the club's 'old' debts to non-football actors are not a responsibility of the new club and its owners: to continue participation in league football all that is required is payment of football debts.

It is unsurprising that the differing 'worlds' constituting these interacting sub-systems experience communications difficulties; language, meaning and motives for communication are candidates for the cause of confusion. Additionally, there are differences in perspective; differences in cultural history; and differences in arena and focus. Taken together, these factors point to abnormal communication challenges.

The football world is one experiencing substantial change owing to the increasing financial rewards available to successful clubs and the attendant social esteem which concomitantly falls upon the increasingly foreign owners of such clubs. The penalties for failure on the pitch are severe ... financially, socially ... and if the worst happens and the club is insolvent, legally also. The extent to which a resource-poor set of regulators

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[39] eg Ward 2002 … *The State of the Game: The corporate governance of football clubs* (pp53-56) Football Governance Research Centre.

[40] But also note the update at Chapter 5 section 3

[41] Needs approval of 75% creditors voting and is binding on all.

[42] See Chapter 6 for detail .. players, clubs and footballing bodies but NOT others even ticket sellers or HMRC. (the landmark case involved HMRC vs Wimbledon FC *IRC v Wimbledon Football Club Ltd* [2004] EWCA Civ 655)

(of any description) can hope to regulate activity in such a sector will inevitably evolve in response to new environmental conditions ... but how quickly and how?

The thesis discussion on regulation will follow two distinct lines of exploration. One line will be plainly legal in approach ... and will focus on the instruments used in regulation, whereas the other will be rather more abstract dealing, as in does, with principles. We start with the latter line and move to the former in the next chapter.

Hamil et al (2004),[43] articulated concerns that football club boards typically had no internal audit committee nor did they commonly undertake regular reviews of risk assessment reports. These comments were made in the wake of a collapsed agreement with a TV company[44] which had significantly reduced revenue for clubs and the entry of some into Administration; the response[45] then by clubs was that "*they would find advice on Company Law useful*".

Dimitropoulos (2014),[46] focusing on the slightly different field of European football, found evidence that efficient mechanisms of corporate governance, such as the increased board size and independence of directors, result in a reduction in the level of leverage and debt, thus lessening the risk of financial instability. This study provides an additional insight for the importance of establishing sound governance principles in European soccer so as to enhance the effectiveness of the 'Financial Fair Play'[47] regulations as well as to improve the financial status of the clubs and sustain their future viability.

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[43] Hamil S. ; M. Holt ; J. Michie ; C. Oughton ; L. Shailer . The corporate governance of professional football clubs *Corporate Governance*, 2004, Vol.4(2), p.44-51

[44] ITV Digital 2002

[45] A figure of 78% of ALL clubs was reported by Hamil!

[46] Dimitropoulos, P. Capital structure and corporate governance of soccer clubs *Management Research Review*, 2014, Vol.37(7), pp.678-658

[47] Discussed in Section 7.1 later.

In a Scottish context, Kolyperas et al (2015)[48] also examine the way in which Corporate Social Responsibility (CSR) develops within professional football clubs, along with its organizational implications, phases, drivers and barriers for corporate governance. They emphasise that professional clubs have become particularly strong socio-political business institutions, home to numerous social and business relationships.

Perhaps the key paper examining corporate governance of English football clubs is that by Michie and Oughton (2005)[49] in which they claim that good corporate governance is essential if such clubs are to be managed effectively and to survive in the difficult economic circumstances surrounding the football sector. They contend that many existing clubs would benefit from following sundry best practice guidelines and make suggestions on information disclosure, the appointment of directors, board composition, induction and training of directors, risk management and consultation with stakeholders. They found that, despite improvement in some areas over the previous three years, standards of corporate governance in football clubs were significantly below those of listed companies as a whole and there thus was considerable need for improvement. Corporate Governance in the UK is regulated by Company Law and by codes of corporate governance such as the Combined Code (CC)[50] and Michie and Oughton urge that a code of corporate governance for professional football clubs be developed.

Whereas compliance with company law is obligatory, compliance with best practice codes of corporate governance, such as the CC, is voluntary. Companies listed on the London Stock Exchange must either comply with the code or else explain any instance of non-compliance in their Annual Report. The rationale for this self-regulatory process is that good corporate governance brings benefits to companies by engendering the trust of investors and improving corporate performance. Firms will therefore find it in their

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[48] Kolyperas, D ; S. Morrow ; L. Sparks, Developing CSR in professional football clubs *Corporate Governance*, 2015, Vol.15(2), pp.177-195.

[49] Michie, J ; C. Oughton, The Corporate Governance of Professional Football Clubs in England ; *Corporate Governance : An International Review*, July 2005, Vol.13(4), pp.517-531.

[50] The Combined Code (CC) sets out principles of good governance and a code of best practice for companies (Committee on Corporate Governance, 1998).

own interests to comply with the code absent a good reason not to … which should then be explained to shareholders in the company's statement of compliance.

However, it is emphasised that this will be reviewed in a chapter different to this one ... which, instead, will look at issues relating to the design and structuring of regulation. Here the attempt is to review an extensive literature on Regulation and it is that to which we now turn.

2.2 Perspectives on Regulation:

We start our exploration of regulatory concerns with the behaviour of professional football clubs by considering what *regulation* connotes and how this varies according to the approach taken. Three different approaches are considered (traditional; modern and self-regulation) and rather different emphases are uncovered.

Traditional Approaches to Regulation:

Here, and in what follows, regulation is used as a portmanteau term encompassing laws, rules, restrictions and, often, codes. The premise that regulation takes place within the confines of the apparatus of the nation-state is not supported in what follows which asserts that regulation occurs in several sub–state levels. Given that regulations may derive from multiple sources, we may have to consider multiple regulators. By extension, it may be unwise to perceive the regulated as being homogeneous. Instead, they comprise a myriad of sub-groups, sometimes all subject to the same regulations, sometimes subject to regulations of a particular nature and applicable to only one or a few of these potential subgroups.[51]

Regulation is thus seen as an activity exhibited within a network of relations between identifiable groups of regulators and regulatees. Later, when Black's (2001) decentred approach[52] is explored, this network relationship will indicate a different perspective to the conventional hierarchical command and control conception of the regulator/

[51] Much in the way that the criminal law applies to all but the rules governing the activity of a golf club apply only to the membership.

[52] Black, J. 2001. 'Decentring regulation; the role of regulation and self-regulation in a "Post Regulatory" world', *Current Legal Problems* 54: 103-146

regulatee relationship. This is the "traditional' perspective of ruling whereby laws/rules proscribing / prescribing behaviour of the ruled are promulgated by rulers and criminal / civil sanctions are applied after due investigation to rule violators. However, the approach taken here develops the communications emphasis of Black by entertaining the possibility of conflict not just between regulator and regulatee but also between groups of the regulators themselves. Conflict can thus be seen as being both horizontally as well as vertically expressed in hierarchical terms. This decentred approach also enables consideration of 'soft law'[53] methods of control of the ruled. Soft control measures may range from inter-group co-operation[54] to the production of codes of behaviour[55] by regulators, (although it is entirely possible that regulatees may participate in the production of codes affecting them[56]), echoing Michie and Oughton above. Although frequently not legally binding in the first instance, these controls still retain much practical value.[57]

Establishing the meaning of 'regulation' is difficult ... and opinions vary. Standard texts[58] see regulation as having a trio of meanings. These are firstly, as a set of focused rules usually exercised by the state; secondly, as social control of behaviour by state and non-state actors alike; and thirdly, as direct intervention by the state in aspects of the economy.[59] However, these meanings may not be shared between sub-system actors.

We start by examining the first of the meanings, the state's use of rules. Selznick (1985)[60] sees Regulation as *a sustained and focused control exercised by a public agency over activities that are valued by a community* . This introduces the concept of

[53] 'Soft law' refers to rules with less than or without legally binding force.

[54] eg Football Association and Football League.

[55] eg Codes produced by IP RPBs.

[56] For instance, between IPs and RPBs … or between clubs and football authorities.

[57] eg The ghost of *The London Agreement* still lingers (involving the leading banks)

[58] For instance, Baldwin, Cave, Hood, Lodge, Morgan and Yeung who have all published various standard texts on Regulation.

[59] This last meaning appears tangential to this thesis and thus will lie in the background.

[60] Selznick, P 'Focusing Operational Research on Regulation', in R.Noll (ed), *Regulatory Policy and the Social Sciences* (Berkeley, C,A, 1985), p363

control by a regulator and the associated idea of regulatee(s). Also notable is the emphasis on time (in *sustained*) which distinguishes from the one-off . The introduction of *focus* however omits to clarify on what such focus might be. This ambiguity extends to *community* (which community is in play?) and to *values* (again, which ones?). Regulatory discussion is a field in which a multiplicity of views and approaches can be found; it is not just ambiguity which leads to argument, it can also be differences in principle. Consequently the regulation field is one which carries a noticeable degree of contestation either in the foreground or in the background ... but inevitably it is there. The emphasis on *public agency* above implies a state-centred perspective on regulation which is not shared by all writers. Significantly, Selznick omits mention of exactly how the promulgated regulation will achieve compliance by regulatees, either directly or indirectly ... a question which certainly gets ample coverage in the literature, nor does he draw attention to any monitoring required in order to establish instances of rule-breaking; again, a question of importance. Nevertheless, it seems accepted that regulation in most forms is an attempt to deal with the relationship between both state and societal actors and between these societal actors.

The second approach to regulation (social control of behaviour), relates regulation to communication[61] or to regulation being a deliberate attempt at state influence which may be based on command and control but which might encompass other methods. Baldwin et al (1998)[62] expand on Selznick to go beyond a state-centred approach and suggest that *all* forms of social and economic influence on behaviour might be seen as being regulatory. Indeed, regulation may be attempted by bodies other than the state.[63] This approach also acknowledges that regulatory outcomes can be deliberate or accidental and can be enabling or restrictive in aim. It can be useful to deconstruct the

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[61] of rules/laws applicable by some duly-established body.

[62] Baldwin, R. Scott, C and Hood, C. '*A Reader on Regulation'*, Oxford University Press 1998 p3.

[63] Such as professions, trade bodies and, even, by self-regulation.

term further to clarify thinking. Thus, ideas like *regulator,*[64] *target,*[65] *command* [66] and *consequences* are all in common usage[67] in the field.

Outcomes of the regulatory action which may be expected or otherwise and desirable or otherwise will be discussed in different terms in Chapter 8 when *The Law of Unintended Consequences* is in view. Interestingly, these terms also reflect usage in marketing circles, yet this author has not as yet come across any explicitly marketing perspectives on Regulation.

Given that the burden of conforming to regulation can be substantial both in economic terms and in attention/energy/time terms for the actors concerned, it is unsurprising that that there have been calls for deregulation … exemplified in the UK Government of 1993 urging a 'bonfire of red tape' and establishing both new laws[68] and new mechanisms[69] to propel the deregulation cause forward. These manoeuvres aimed to give ministers powers to use statutory instruments to deal with the regulatory load on organisations. The success of such initiatives seems difficult to measure practically and the returning of state-owned organisations to private ownership may have had the unintended consequence of increasing rather than decreasing regulatory activity. This may not be pressing on the actors being studied here ... but the 'general mood' may offer some explanation for a reluctance to introduce further regulation in this area.

'Modern' Approaches to Regulation:

Black offers a useful fine-grained analysis of Regulation and these are taken forward in amended fashion here. After defining Regulation[70] as …

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[64] The person or body who creates, promulgates and enforces the regulation.

[65] The person or group whose behaviour requires influencing and from compliance is expected.

[66] The instruction with which compliance is wished; it can be either means or ends.

[67] eg Coglianese, C. in 'Engaging Business in the Regulation of Nanotechnology' in C.Busso (ed) *Environmental Regulation in the Shadow of Technology* John Hopkins University, Baltimore 2009

[68] The Deregulation and Contracting Out Act 1993

[69] The Enterprise and Deregulation Unit.

[70] Black, J. … see Fn 51 above

"the sustained and focused attempt to alter the behaviour of others according to defined standards or purposes with the intention of producing a broadly identified outcome or outcomes, which may involve mechanisms of standard-setting, information-gathering and behaviour-modification"… she proceeds by way of four questions which help structure our following discussion :

- *Who regulates ?* ... In this thesis, regulators are variously the state; non-state actors such as the football authorities and the RPBs. Economic forces and social forces might also be seen as a form of regulator as both forces influence behaviour in diffuse ways such as the sales of assets in distressed clubs and in the social esteem which accrues to owners of successful teams whereas non-state actors have committees and review bodies.
- *What is the form of the regulation?* ... Here, the State uses the courts and the agency of The Insolvency Service. The market is the principal economic form of regulation and social forces take form in culture, systems and language.
- *What is being regulated?* ... The state is interested in regulating the behaviour of directors of football clubs especially at times immediately proximate to an insolvency event. It is also interested in regulating the behaviour of IPs but has delegated this to the relevant professional bodies and, ultimately, to the courts. The football authorities wish to control actions and responses within the football system in order to ensure the ongoing health of this professional sport in England. Both economic and social forces are 'blind' as to intention and both interact both with each other and with other systems.
- *What techniques are principally used?* **…** Both state and non-state actors use a compendium of techniques which are broadly similar eg rules, information gathered, monitoring and sanctioning. The state has its monopoly on the use of legitimate force whereas non-state actors may use trust. The market is an arena laying stress on rationality and often on repeated interactions whilst social forces use framing, enabling and self-referential reproduction as some of their techniques.

This view of regulation explicitly removes the state from being the focus of regulatory initiatives, being described as '*decentred*' ie not state-centred. This conception of regulation points to five main and distinct strands within the approach. Each is regarded as being significant in its own right yet having an effect on each of the others. These five strands are complexity, fragmentation, ungovernability, interdependency and an acceptance of a diffuse boundary between public and private spheres. The multiple interactions between the actors mentioned above lead to *complexity* with regard to causality ... some factors are known and some are not; some factors change and some do not; some consequences are predictable and some are not.[71] Complexity may be noted in the interactions between actors[72] and Black quotes Koimann[73] ...*"These interactions are themselves complex and intricate and actors are diverse in their goals, intentions, purposes, norms and powers"*
Such a view sets up consideration of regulation in systems terms.

A second key strand is what Black calls fragmentation and is applicable both to power and control as well as to knowledge. The fragmentation of power and control takes analysis away from more traditional state-centred approaches in that, whilst not refuting the state's monopoly on the legitimate use of coercion as a force implementing a command and control approach to regulation, it does however accept that power (and the ability to control) is diffused between the state and the various social actors which are to be the target of regulatory influence. Thus are outlined potential fault lines between the legal system with its state-induced formal ordering and the social system(s) in which other actors exist which perhaps pay more heed to their own social ordering. For instance, IPs may have regard to their seniority within the profession as a whole and owners may value the reflected glory from a successful football team.

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[71] Again, see musings on *Unintended Consequences* in Chapter 8.

[72] For instance, at one point the football club owner may see the IP as 'friend' when a solution to pressing financial problems are being sought (eg at 'Pre-pack' stage) but may later regard the IP as 'enemy' if the IP investigates the owner's conduct.

[73] Kooiman. J (ed), *Modern Governance: New Government-Society Interactions* (Sage, London, 1993)

So, "*Regulation occurs in many locations, in many fora: there is "regulation in many rooms*."[74] The fragmentation of knowledge is portrayed as being more than the traditional acceptance of asymmetric knowledge distribution;[75] it is rather that no one actor possesses the knowledge required to deal with the complexity involved. This paucity of information available to regulators has implications for their power to sanction. If the regulator is not completely aware of the facts, it will be difficult to bring forward sanctions ... owners may have experience in making information hard to obtain.[76] Arguably, knowledge is socially constructed with the consequence that different social groups are likely to construct knowledge in their own terms ... which may differ from that constructed by those in different groups. This line of thought is most prominently developed in writings on autopoeisis which take up the theme of interacting systems (or not) touched upon above. Perhaps the key insight from this type of analysis is that each interacting subsystem constructs its view of the other systems in its own language and terms with each system having its own way of engaging with and making sense of the environment. Understanding by interacting groups of the act, communication or influence attempt of one group towards another can thus not be taken for granted. The idea of sub-systems being reflexively open yet epistemically closed with reference to inter-sub-system connections[77] is significant.

The third decentring strand is *ungovernability.*[78] The actor-systems are both self-regulating and in constant movement resulting in regulation of a system's behaviour producing both intended and unintended results. These unintended consequences need not always be harmful to the regulatory initiative. The restrictions on the knowledge available to any one actor may also combine with the actors' autonomies to substantially

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[74] Nader, L. and Nader, (1985) C.'A Wide Angle on Regulation: An Anthropological Perspective' in R.G. Noll (ed), '*Regulatory Policy and the Social Sciences*'
University of California Press, Berkeley, US

[75] in the form of regulatees having the information that government needs in order to effectively regulate.

[76] Owners may have experience in making information hard to obtain ... vide the FA's "Fit and Proper Test" for owners. (see later at Section 7.1)

[77] See Teubner quoted in Morgan and Yeung ? p 70-72

[78] In Black's occasionally strained lexicon, this means autonomy, not quite in the limited sense of freedom from state engagement but rather that actor-systems will develop along their own path in the absence of intervention.

deny the opportunity either to the state or to any alliance of actor-systems to impose their will on the others. In short, each actor-system may have the capacity to regulate itself but is unlikely to be able to successfully influence the behaviour of any other actor-system in a direct way, a point articulated in some detail in Teubner's[79] conception of '*the Regulatory Trilemma*.' Recall that a trilemma implies a choice being made between three equally undesirable outcomes. In this instance, Teubner foresees three somewhat undesirable potential consequences of regulatory activity ... firstly, that regulatory initiatives will be ignored; or secondly, that the continued existence of the sub-system being regulated will be threatened; or finally, that the integrity and autonomy of the legal system itself will be seriously compromised.

The fourth strand, interdependency, points up the notion that regulation may be co-produced in the sense that all actor-systems have problems and solutions, needs and capacities. Thus each actor needs one or more of the others if matters are to be resolved ... eg the contractual nature of relations between football clubs and the football authorities.

The final aspect of decentring is the dissolution of any boundary between public and private in terms of the social and political realms. This has substantial implications for the way in which regulation can be conceived and allows regulation to become seen as the outcome of the interactions between networks of actors and not just as the desired product of governing hierarchies nor of the blind operation of the market. As Black[80] puts it,"*In a decentred understanding of regulation, therefore, formal* de lege *authority plays an ambiguous role, and regulation is not so much an activity as a product of activity*".

The consequences of such an approach imply that any analysis of regulatory failure[81] which is even partly based on decentring should look closely at the configurations of interaction between actor-systems to assess the extent to which they enable or hinder

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[79] Teubner, G. (Ed) *Dilemmas of Law in the Welfare State* (de Gruyter Inc, Berlin, 1986);

[80] Black, J. (2002) 'Regulation' *Australian Journal of Legal Philosophy* 27 p8.

[81] See later ... section 3.2 *Regulatory Failure*

regulatory objectives. How these patterns of interaction may be adjusted and/or exploited is considered later.

***Self-regulation*:**

Another important aspect of the control function in regulation lies with *self-regulation* ... here, not seen as the ability of an individual to rein in behaviour deemed unhelpful or injurious but more as actor-systems regulating their own affairs. The person doing the 'deeming' can, of course, be the self or some significant other. Potentially, there are benefits to be gained by all parties involved in such arrangements. The state may be able to displace the costs of rule determination, compliance monitoring and sanctioning to others. It may also believe that actor-systems are better placed[82] than it to understand both the complexity of the environment in which that actor-system exists and the inducements required to ensure adequate compliance by actor-elements within that sub-system. Similarly, the actor-system may be more inclined to sense a self-regulated regime as being somewhat more legitimate than an externally imposed one and certainly to calculate that such a regime would be much more susceptible to capture by the regulated actor-system. Thus, the interests of the sub-system would perhaps be likely to be put ahead of that of others, including that of the state. The internal view of legitimacy, however, is liable to be contested by external actor-systems.

That self-regulation occurs at all can be a consequence of a rational state decision delegating some bundle of powers[83] to regulate intra-group behaviour ... or it may transpire because the interest group seizes the initiative and takes on the mantle of self-regulator. The state may connive at this or have other more pressing issues requiring attention. After all, the State can always legislate such regulation away, should it wish to. The way in which activities of Insolvency Practitioners are regulated by their set of Recognised Professional Bodies exemplifies the former (state-delegated self-regulation) whereas the regulations established by the

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[82] This remark links to the more extensive discussion of the point in *The Sporting Interest* (section 7.2) in later discussion.

[83] Often with some oversight powers and with some form of backstop in extremis.

set of football authorities represent the latter (interest group initiated self-regulation.) Commentators on historical professional practice[84] see self-regulation as the hallmark of organised professional activity over the years allowing as it does here, the authority of RPBs[85] to establish entry qualifications, to impose rules of conduct and perhaps most importantly, to mark out a specific area of expertise as their own ... thereby establishing the boundaries of their actor-system.[86] This boundary may shield against unwanted external influences; it also provides a space within which specialised expertise coupled with discretion can flourish. This specialism leads to the development of culture and communications particular to that actor-system and may be, in part or in whole, unintelligible to those rooted in a different sub-system. Specialism, discretion and oblique communications coupled with predominantly internal accountability may well be seen as being a recipe for an actor-system with an external PR problem[87] at best and a focus for accusations of self-serving[88] at worst.

Coglianese and Mendelson[89] make a distinction between meta-regulation and self-regulation where they stress intentionality as the essence of *meta*-regulation. In this sense the State, with prior consideration, attempts to influence targets to establish their own internal responses to what are perceived to be pressing public issues. Thus, Coglianese and Mendelson would characterise the Insolvency Practitioner example above as being meta-regulation. Their central point about *self*-regulation, however, is that the target of the influence attempt is the regulator of that attempt. In other words, the target issues commands which apply only to itself. This more closely describes the activities of the football authorities which issue rules which apply only to the members

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[84]such as Rostain : Rostain, T. " Self-regulatory authority, markets and the ideology of professionalism" in *The Oxford Handbook of Regulation* eds Baldwin, R. Cave, M and Lodge M. Oxford Univ. Press 2012 p169-171

[85] Recognised Professional Bodies.

[86] There is the suggestion that the State was pushing on an open-door in the case of IPs. See .. Rescuing business**:** *The making of corporate bankruptcy law in England and the United States* Carruthers, B.G and T.C. Halliday - 1998 - Oxford University Press

[87] For dubious external legitimacy.

[88] Criminal charges against IPs are not unknown ... see the Collyer, Bristow case of 2012 which was a consequence of Glasgow Rangers' financial difficulties.

[89] Coglianese, C. and Mendelson, E. "Meta-Regulation and Self-Regulation" in *The Oxford Handbook* ibid p146-151

of these authorities and which rules have no particular nor explicitly discernible root in the state's perception of the public good.[90]

2.3 Regulatory Systems, Regulatory Outlooks and Regulatory Arenas:

Aside from contemplation of networks of regulators and an acknowledgement of the existence of multiple perspectives, a further fundamental issue requires examination; that of ...
"what aims and purposes are expected to be furthered when regulators make their regulations?".
The best start to analysis is to contrast regulations which have at heart some conception of public interest to be achieved with those which may be understood as attempts to serve the private interests of one or more groups of regulators.

Public Interest Approaches:

Public interest approaches attempt to put first the interests of specific or all members of a community as a goal of any regulation; a general welfare aim. Sub-varieties may emphasise an economic, market-oriented perspective ... or may focus on different aspects of a more social type.[91] In the economic variation, the regulator responds to some perceived weakness in the operation of the market. Any resultant correction of so-called '*market failures'* is then an increase in general welfare ... and hence in the public interest. The advocacy of the European football authorities (UEFA) in 2009 of measures such as the Financial Fair Play Regulations[92] exemplifies this approach. The aim was to prevent professional football teams over-extending themselves by purchasing players who were expensive to buy and to pay; a type of prophylactic against insolvency.

Ogus (2004)[93] sees this as …

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[90] Which is EXACTLY the situation to be analysed later re The Football Creditors' Rule or The Fit and Proper Persons rule.

[91] eg. enabling the fans of a particular football club to have cross-generational continuation of their interest over time; grandfather, father and son united in their support for a (once-) local team.

[92] Similar measures were instituted in England.

[93] Ogus. A. 2004. *Regulation: Legal Form and Economic Theory*, Oxford: Hart Publishing

"*the necessary exercise of collective power in order to cure 'market failures' to* ***protect the public*** *from such evils as monopoly behaviour, 'destructive competition',* ***the abuse of private economic power****, or the effects of externalities*."[94]

Ogus proceeds to add a cautionary note urging a reluctance to disturb a satisfactorily functioning relationship between regulator and regulatee(s) before conceding, almost dissonantly, that what constitutes the public interest is likely to change over time and place.

However, this may be seen as a narrow economic approach. Other opinions as to the public interest stress matters with a social and/or political nature. These opinions might include, in turn, a need to redistribute asymmetrically held powers;[95] an aspiration to move towards some socially just end (in a sense, supporters of football clubs '*own*' their club yet they rarely have an input into the club's affairs ... especially in times of financial distress); or even forward-looking to serve some purpose[96] in respect of future generations.[97] This public interest focused approach may progress relations between regulator and regulatee in a more participative and dialogue exchanging mode than the command and control approach mentioned above … perhaps heralding the possibility of negotiations between regulator and regulatee ? Arguably, the activities performed by The Insolvency Service conform to this approach.

Private Interest Approaches:

A contra-distinction to public interest theories of regulation, are *private interest* theories. These assume that the aims/purposes of regulations derive from the actions of those eager to maximise their own interests via the following of the regulation by the regulated. Such actions may arise directly from the regulators themselves or

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[94] Author's emphasis ... to establish links elsewhere in this discussion.

[95] Most obviously in expertise? eg Insolvency Practitioners compared with Directors of distressed football clubs.

[96] For instance, see the notion of Football Trusts as explained in "In Football We Trust", Kelly. K, Lewis. R, and Mortimer. T *International Journal of Business and Social Science Vol. 3 No. 8 [Special Issue - April 2012]*

[97] The question of "*to what extent is the social fabric of a locality rendered the poorer if its local traditions in sport in general (or football in particular) are not preserved?",* although of considerable background interest, is not developed further here.

potentially, from indirect influence by others upon the regulators[98] at the stage of formation of any specific regulation. Consequently, any connection between the effect of the regulation and the serving of a public interest is accidental.[99]

Discussion of private interest approaches may reveal possibilities not just of market failure but of *regulatory* failure. Regulatory failure can result from '*regulatory capture* ' whereby officials whose job is directed towards the increase of collective welfare develop such close relations with groups within the ruled so that it is the interests of those groups[100] rather than the generality of the community that are promoted.[101]

Variants on the private interest perspective can, as before, be seen in economic and in socio-political terms. The well-known concerns about the Principal and Agent relationship exemplify the economic strand of private interest thinking viz. In circumstances where the Principal delegates to the Agent the power to take decisions on the Principal's behalf. Here, where the Principal creates the rule and the Agent is expected to apply that rule, either to the Agent's own behaviour or to that of others. Some suggest that Agents may fail to follow the rules as determined by the ruler and seek to manipulate context and interpretation of the rule to the advantage of the Agent establishing the concepts of *conflicts of interest* and of *moral hazard*. That there is likely to be an asymmetrical access to relevant information accentuates possible difficulties.

Conversely, the political strand points to a view of competition between interest groups for influence and power in relation to the ruled often found in accounts of a pluralist society. Pluralism is seen as a state of diversity (in groups) where there is a degree of tolerance for the holding of different views or beliefs and the pursuit of differing agendas. There is no requirement for the groups to have equivalent power ... this would be somewhat of the exception.

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[98]eg, the Committee of the Football Association is extensively lobbied by informal groups of their membership eg "the London Cabal" .. directors of London-located clubs.

[99] Although entirely possible.

[100] One might see the relationship between IP and regular corporate insolvency players such as Banks being explainable by this approach ?

[101] See Croley, for a MUCH more extensive treatment of this. Croley, S. 1998 'Theories of regulation ; Incorporating the administrative process' *Columbia Law Review*' 1: 56-65

Accordingly, it might be said that public interest approaches to regulation are prone to focus on the propensities of *markets* to fail ... and thus are sensitised to the capability of regulation to redeem these failures. In contrast, private interest approaches focus on *regulatory* failure and the probability that special interests of competitively successful or favoured groups may be promoted ahead of any conception of collective welfare.

Institutional Dynamics Approaches:

Aside from the bi-polar constructs of public and private interest perspectives on the regulator-regulatee relationship is a group of theories about regulation labelled the "institutional dynamics" approach. This stresses the '*life of its own'* nature of the various actor groups in the sundry relationships between regulators and regulatees.[102] The institutional dynamics approach stresses firstly that regulatory outcomes may be difficult to predict as these outcomes reflect the interplay[103] of interests and manoeuvres by participants and, secondly, sees little of importance in the public / private actor typology.

Ayres and Braithwaite (1992)[104] take a view blending the public/private duality in an approach which sees relations between actors in terms of gaming by the groups concerned of the rational calculation of cost-benefit 'pay-offs'. Thus, Ayers and Braithwaite move the analysis onwards from mere inter-group competition and allow the actors to consider the consequences of cooperative behaviour. In turn, this permits contemplation of corrupt practices[105] between actors and introduces the notion of the evolution of '*regulatory capture*'.[106] The enduring issue of '*Quis custodiet ipsos*

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[102] As outlined in brief in The Prologue

[103] Consistent with the moving relationships between sub-systems discussed elsewhere in this chapter.

[104] Ayres, I and Braithwaite, J. 1992 *Responsive Regulation : Transcending the regulation debate*, New York : Oxford University Press, 19-53

[105] Hancher, L and Moran. M. 1989. 'Organising regulatory space' cited in Morgan, B and Yeung, K. 2007 *An Introduction to Law and Regulation*, Cambridge. CUP p61

[106] bid p63

custodes?'[107] is addressed in their theory of *Tripartism* in which Public Interest Groups are charged with overseeing[108] '*the guards*' in their monitoring and investigatory roles.

A different approach even more firmly grounded in institutional dynamics is offered by Hancher and Moran (1989)[109] as '*Regulatory space'* ... a concept which emphasizes the arena in which behaviour takes place and which influences the practices that occur therein. According to Hancher and Moran,[110] a regulatory space is composed of a range of regulatory issues subject to public decision. Three main consequences follow from this definition ... which this author shows below.

Aspects of Hancher and Moran	*Consequences*
Occupiable space	a space which can be rationally allocated among several actors but is also available for occupation.
Relative nature of space	regulatory space may be general in relation to the general economic regulation or may be specific, referring to specific sectors of regulation.
The character of space	the concept of regulatory space can be expressed using other metaphors. This accommodates this author's suggestion that both intra- and inter- regulatory space may be the scene for negotiation, for co-operation and for conflict.

Table A : Consequences of Hancher and Moran's thinking on Regulatory Space

Such a space might allow for interactions between actors in a more subtle and dynamic nature manner than other rather static or linear views of regulation would allow. This

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[107] Attributed to Juvenal and often mis-translated as "Who guards the guards ?"

[108] A check and balance of the 'Jeffersonian democracy' type associated with the US approach to rule-making .

[109] Hancher and Moran op cit. p59

[110] In Zanettini, L. in 'The Regulatory Space of Public Procurement'.(n.d.).

idea might be deepened in a related but different way by extending the consideration of interactal space to include the idea of *Ba.*[111]

It is worth noting the complexity of the relations taking place between the interactants in the regulatory space and, unsurprisingly, Hansher and Moran's scepticism regarding the predictability of the expected behaviour of the regulated. Additionally, their perspective gives substantial attention to the contingencies of history; of institutional development;[112] and of the changing balance of power between actor groups.[113] All of these elements appear germane in the context of the historical development of football clubs, their development into elite and non-elite but professional leagues and the nuanced power changes actuated by the unexpectedly high sums of 'TV money' now available to successful clubs.

2.4 <u>In summary</u>:

Much of the discussion above revolves around the establishing of ideal types ... but, as management theorist Henry Mintzberg correctly observed, '*we don't live in an ideal world*!'. Thus, reality may consist of a mixture of types ... and there seems little reason why one type may not morph into another over time or as the context changes. One could conceive of a cycle of change eg. from wholly public interest, through partly public interest/partly private interest, to wholly private interest ... and even a return journey back to public interest as a consequence of changing contextual pressure.

Review of the foregoing discussion indicates that little prominence has been given there to the notions of values and beliefs. Arguably, these are to the fore in public interest accounts ... and also arguably in the background when considering the regulations of professionals ... but what values might spur the regulation of football clubs by the football authorities (*solidarity?)* or what might motivate the actions of a director of a

[111] 'Ba' (Japanese) can loosely be conceived of as a shared space (real or virtual) in which interactants feels safe and consequently exchange insights; often associated with Nonaka in the mid 1990s; the concept also resonates with Bourdieu's *habitus* (or field).

[112] With quite a focus on organisational size and structure.

[113] These groups might equally be the regulator; the regulatee(s); or the agents of the regulator.

football club (*civic pride? self-importance? profit?).* And, after all, the idea of private interest (and capture) also raises similar questions of ethics and values.

The thread of sub-system difference may also be important. Teubner seems to suggest that autopoietic systems are epistemically closed ... which is consistent with each system having different values and languages. But does this necessarily result in boundary closure in epistemic terms ... after all contiguous countries may speak differing languages but be perfectly capable of understanding each other.[114] May there be some form of permeability between some 'neighbouring' sub-systems such as those populated by Insolvency Professionals and their counter-parts at The Insolvency Service ? That interactive understanding between directors and professionals may be difficult to achieve is, however, acknowledged.

The theme of contestation is likewise subdued in the above treatment. Perhaps it might be prudent to bring this more centre-stage in that suggestions, initiatives and sanctions in this field are all very likely to induce a Newtonian opposite and equal effect[115] with the result that regulation and conflict are frequently inhabitants of '*the same room'* outlined[116] earlier. The forms of these contestations and conflicts, perhaps, might require deeper study ?
Thus, we may see the simple distinction of 'regulator and regulated' as one which merely introduces a much more complex regulatory landscape than at first imagined. Perhaps the adage[117] "*People*[118] *obey rules when it is more in their interest to obey than to disobey*" is a useful concluding dictum?

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[114] eg, The Netherlands and Germany; Spain and Portugal;

[115] Notwithstanding the state's alleged monopoly of legal coercion ... which may not be q the case in reality.

[116] See Fn73 above.

[117] Perhaps from Weber? (nd)

[118] In our context, we might substitute the term 'actors' in order to encompass organisational entities also.

Chapter 3 : Regulation in Practice

3.1 Regulatory Enforcement Strategies:

A continuing theme in our discussion has been the clear tension between deterrence and persuasion in relation to enforcement. Thus, some form of plan as to how behaviour is to be influenced requires to be implicitly or explicitly developed and a need for some form of regulatory strategy seems clear.

The Responsive Regulation School:

Taking thinking on regulatory strategies beyond '*either/or*'[119] is an approach characterised by '*both*'. Leading in this perspective are Ayres and Braithwaite who introduce 'Responsive Regulation' as ...

'rejecting punitive regulation is naïve, to be totally committed to it is to lead a charge of the light brigade. The trick of successful regulation is to establish a synergy between punishment and regulation.'[120]

This is enduringly associated with the notion of enforcement pyramids. The pyramids represent an escalating series of regulatory actions which usually commence at the bottom and advance in severity of regulatory response up the pyramid as appropriate.[121] In this way, a more punitive response is offered when persuasion has failed to induce compliance.This attempts to introduce an explicit Tit-for-Tat[122] approach to regulatory strategy and they envisage its utility as much in the regulation of industries as in the regulation of specific firms.[123]

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[119] That is ... *either* deterrence *or* persuasion.

[120] Ayres, I. and Braithwaite, J. *Responsive Regulation* (Oxford,1992)

[121] Appendix 1 is an example of a developed pyramid.

[122] Tit for tat; Robert Axelrod, a rational strategy where each participant in a series of interactions follows a course of action consistent with the other party's previous turn ... and thus, each influences the other's behaviour.

[123] Ibid 38-39.

Like many novel approaches, 'Responsive Regulation' has become both the basis from which other proposals[124] are developed and the target of detailed criticism and objection.[125] The first comment is the most obvious one ... there will surely be instances where a measured (slow?) escalation will be 'too little, too late'. Events in an insolvency context may take place extremely quickly; the idea of '*Pre-pack'* (see later) is often justified by saying 'speed is of the essence'. This is also especially relevant if non-compliance in a high-risk context[126] is suspected. Secondly, an issue for any stages concept, is the difficulty in reversing back one or more stages.[127] The third objection is trenchant; there is a supposition that regulatees will respond to the regulatory action. This may not be well-founded. Surely regulatees, as actors, will '*march to their own drum* '? Consequently, some regulatees will attend to other pressures[128] than those of the responsive pyramid.[129] So, Responsive Regulation is vulnerable to suggestions that it is poorly targeting those on which certain regulatory measures are pressed.

A fourth caveat is a subtle one; there is a presumption that the regulator has the ability/ freedom to escalate enforcement as required. This may not obtain. Resource and/or competence gaps will possibly exist and information on non-compliance may be unreliable/unavailable A feature of recent economic times has been the mandatory reduction in resource made available by the state for regulatory purposes and action. This results in a reduction in proceeding with small scale infractions of regulations ... such as those involved in corporate insolvency. Crucial, in some circumstances, the will of the regulator's political masters may be subject to rapid change in the face of a new '*cause celebre'* with the necessary support for enforcement escalation evaporating.

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124 Later we look in turn at *Smart Regulation*; *Regulatory Craft*; and at *Really Responsive Regulation.*

125 Many of these critiques apply to the further theory developments also but for clarity of exposition are dealt with here.

126 eg The Nuclear Power generation industry.

127 eg escalation up a level may engender an experience or psychological response in the regulatee which may damage the relationships between regulator and regulatee on which success at a lower level rests**.**

128 Competition, history and cold-blooded calculation are all potential pressures in this regard?

129 Intuitively, this "*marching to their own drums*" seems credible vis-à-vis the owners of football clubs.

Finally, the discretionary actions implemented by individual regulators[130] may be labelled as non-transparent and it may be difficult to hold the regulator to account for their decision-making. So, suspicions of regulatory capture whereby the regulator may be perceived to be in some way '*controlled*' by the firm/industry concerned, may not be far behind? It is acknowledged that the pyramid enforcement approach is suggestive rather than conclusive ... thus signalling the consideration of other regulatory tools and strategies. Perhaps there are several routes to successfully climbing this pyramid?

Building on the central ideas of Responsive Regulation is the notion of '*Smart Regulation*'. Again, there is escalation up a pyramid but here the scope is broadened[131] by introducing a third dimension[132]... regulation by businesses themselves or by quasi-regulators.[133] Thus, the regulatory pyramid in Smart Regulation becomes triple-sided and opens up the possibility for the regulator of moving sideways as well as upwards[134] in determining response. Whilst offering a wider range of potential responses which may be rather more creatively applied than in the Ayres and Braithwaite approach, many of the criticisms expressed above in respect of Responsive Regulation still obtain but the approach potentially may be more successful in influencing regulatees compared with more traditional methods.

Conceivably, owners of football clubs are accustomed to examining the rules of which they know in order to exploit these rules; so 'command and control' might not be the most productive path in their instance. This might encourage their would-be regulators to consider the alternative, Responsive Regulation approach. The additional complexities may heighten the burden on individual regulators. However, proponents of the Smart Regulation approach are quick to assert that it may be less costly and easier to apply in many contexts.

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[130] eg The tailored response to an individual firm's non-compliance.

[131] from the consideration of just two actors (state and organisation/ industry)

[132] See Appendix 1.

[133] eg industry associations or professional bodies.

[134] See earlier caveats re backward movement.

The Crafting of Regulatory Strategy School **:**

A somewhat different approach to the regulatory puzzle is offered by Sparrow. His *Regulatory Craft*[135] approach[136] puts the solving of problems at the heart of devising effective regulatory strategies. For Sparrow,' *... the need is to pick the most important tasks and then decide on the important tools ... rather than decide on the important tools and pick the tasks to fit'*.[137]

This alerts regulators to the need to prioritise the tasks (problem areas) needing attention in relation to the performance AND the evaluation of regulatory activity. In turn, this drives the focus on dealing with key[138] regulatory challenges and, even more tellingly, obliges attention to be given to the way in which these challenges evolve over time.

The Regulatory Craft approach has its links to Risk-based Regulation[139]... and endures similar drawbacks in that there is an uncritical assumption that issues CAN be packaged/problematized ... and that there is no direct consideration given to the possibility of the solution to one problem having a knock-on effect on another problem or its 'solution'. However, it does have the immense appeal of being an action-driven/ solutions-oriented way of engaging with regulatory strategy. This will likely win approval from those whose disposition is avowedly pro-active and practical.

The 'Ultimate' in Regulatory Strategy?:

Baldwin and Black's Really Responsive Regulation paper[140] takes the debate even further. Their comprehensive approach suggests that successful

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[135] Sparrow, M.K *The Regulatory Craft* (Washington DC 2000) ch 10

[136] Said by some to be a broader approach than Responsive or Smart Regulation but, in actuality, rather more focused than either.

[137] Sparrow, M.K. *The Character of Harms* (Cambridge 2008) ch 1

[138] As compared with 'mere' compliance?

[139] As in Black, J. "The Emergence of Risk-based Regulation" (2005) *Public Law* 512

[140] Baldwin, R. and Black, J. 'Really Responsive Regulation' (2008) 71 *MLR* 59-94 from which many of the ideas in this section were taken.

regulatory systems need to advert to five key elements ... which they offer as being *attitudes* (and culture and behaviour) shaping the regulatee's disposition to the regulatory activity;[141] *institutional setting*, especially matters of formal and informal control of the regulator in regard of actions and resources; *interactivity* of the logics of regulatory tools and strategies;[142] the *performance* of the regulatory regime over time;[143] and the way in which each element *changes* through time.[144] Responsiveness to the interplay of these five factors is said to lie at the heart of the regulator's challenge. They, somewhat exotically, outline the core tasks of regulation for the regulator in *The Dream Sequence* outlined below.

Detection of undesired behaviour:	Key here is the difference between ensuring compliance (a la Tit -for-Tat based schemes) and gaining an insight into the real level of compliant behaviour. The latter focuses upon the real performance of the enforcement system and may encourages consideration of uncontrolled, non-compliant behaviour.
Response by the development of more appropriate regulatory tools:	An assumption made by advocates of responsive based regulatory frameworks is that regulators will have access to and the skills to use the 'full regulatory toolkit.' As this is unlikely it becomes important to have the capacity to develop more focused tools and to augment deficient skills.

[141] These may change over time and are contextually dependent.

[142] Essentially this is about coherence; it is an attempt to consider the extent to which various regulatory rules or tools harmonise or conflict in their operation.

[143] This element focuses on task achievement; the performance of the regulator in achieving the regulatory objectives **over time.**

[144] This links to change and to novelty; the appearance of new challenges for the regulator in the face of some shift in the systemic environment.

Enforcement by application of coherent regulatory strategies:	The use of tools delivering a regulatory strategy forces deliberation of their interaction. Adverse consequences hinder and unexpected benefits help the achievement of objectives. Establishing fit between tools is desirable.
Assessment processes:	Attention is needed to making clear statements of essential actions for removing possible sources of tension. This will also help with performance assessment.
Modification:	This activity builds on the previous four points to possible adjustments to existing regulations; much easier than embarking on new proposals!

There may be significant issues in making the Really Responsive Regulation suggestions workable in real life. As ever, resource deficiencies may render the collection of necessary information problematic. The exercise of regulator discretion may hinder accountability and transparency and prove politically embarrassing. The development of new tools may well be constrained by the institutional context in which the regulator must operate.

There may be significant difficulties for the Really Responsive approach when regulatory power is fragmented ... as in de-centred systems.[145] There are complexities involved in gaining relevant information. There are communication nuances involved in moving that information back and forward to system elements which will hold different values and have different capacities and motivations for dealing with such communication. Above all, there are extraordinary resource demands[146] involved on all sides.

145 As explored in this study.

146 Appendix 2 gives a good idea of the complexity involved!

3.2 Regulatory Failure:

We turn now to instances where the regulatory regime is thought NOT to be delivering its original objectives … 'Regulatory Failure'. We look at a continuum from Regulatory Success to Regulatory Failure rather than simplistically looking at the polar extremes. Instances of Regulatory Failure are commonplace[147] ... but what constitutes a failure needs consideration as do the causes of these failures.

Some causes of Regulatory Failure:

Failure may be foreseeable for some and come as a shock to others; it may result in undesired outcomes or may not follow recommended processes. As examples of outcome failure, three issues are observed.

The first underlines the importance of detection of inappropriate behaviour.[148] Detection difficulties may arise from under-regulation owing to insufficient relevant information being gathered. This raises issues of under or overinclusivity of the rule to be followed. Under-inclusivity gives rise to conduct which ought to be controlled being overlooked … whereas over-inclusivity generates excessively strict controls on behaviour which ought not to be controlled (by that rule). Over-regulation may also lead to over-zealously punitive approaches from regulators and, consequently, to withdrawal of cooperation and communication by regulatees.

The second difficulty relates to regulatory failings due to enforcement problems. Arguably, most pervasive difficulty facing regulatory enforcers 'creative compliance' wherein the regulatee goes through the motions of conforming[149] in order to evade detection. A more subtle difficulty connected with enforcement may surround an over-emphasis on information transparency provoking risk-averse actors to reduce information given to that regulatory process. Reputational inadequacy can have damage

[147] The BHS Pension Fund affair being a topical example.

[148] However defined.

[149] The practice known as tick-boxing relates to this side stepping of the spirit of the regulation and leads to regulation becoming a sham.

successful enforcement. Regulators lacking in credibility[150] are poorly placed to take enforcement activity forward. This credibility shortfall could be perceived or real; could be as a consequence of direct or indirect experience .. and could be a consequence of past or present circumstance. That the credibility gap could be based on for all kinds of criteria ... eg. *capacity/inclination/knowledge-expertise* … serves to highlight the nature and magnitude of the enforcer's challenge.

The final difficulty centres on the regulator's inability to assess and then modify the operation of the regulatory regime. Without relevant data and effective feedback systems it is difficult for regulators to assess their actions and, hence, may find adjustment of their regulatory strategies difficult. It is noteworthy that regulatory failure becomes even more complex as the responsibility for success or failure may be difficult to allocate ... thus driving the thought that regulatory failure may be linked with organisational failure. Indeed, the lines between the various systems in our analysis may be blurred in reality. This will be so both at the "higher" level of legal vs economic vs social systems or at the "actor" level of Insolvency Practitioner vs Director vs Insolvency Service.

Failure may also be a consequence of procedural shortcomings. Commentworthy in this regard would be the manner in which the Leeds Utd administration of 2007 struggled with issues relating to mysterious loans from off-shore entities enabled the then directors of the club to use the votes from the providers of these loans to push through a CVA accepting a payment of 2p/£ at the appropriate Creditors' Meeting. The affair of Glasgow Rangers administration in 2012 also faced procedural difficulty when the IP's favoured buyer[151] turned out himself to be insolvent.

The multi-faceted approach advocated by the decentred view implies that different actors will have different assumptions as to how regulatory procedures ought to be conducted. Whether these expectations are to do with transparency, accountability or consistency matters little; what does matter is that different constituencies may have

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[150] As current (Aug 2018) events in relation to the regulator's (FCA) inability to act against RBS Bank's GRG for several corporate insolvency misdemeanours.

[151] Mr Craig Whyte

really quite different views as to what constitutes regulatory success or regulatory failure.

Further Causes of Failure?:

Explanations of regulatory failures point to matters such as the disinclination of regulatees to conform or to the lack of resource accessible to regulatory agents. However, a different perspective is offered by Hirschman[152] who sees failure as ensuing from one or other of a set of resistor strategies by sceptics of regulatory intervention. These are the futility, jeopardy and perversity positions which may be used to dispute the effectiveness of current or proposed regulations. The *futility* proposition suggests that people do not change their behaviour just because of a regulation ... and that is even more likely where complexities of problems or systems exist. The *jeopardy* position indicates that whilst any single regulatory manoeuvre may be well-intended and useful, the implementation of that measure would prejudice successes already achieved elsewhere or yield side-effects of an unwanted type; narrow 'wins' being outweighed by broader 'losses'. The '*perversity*' view claims that actions often have outcomes which are quite the reverse of their original intentions. Hirschman is, in his way, prefiguring the use of Merton's Unexpected Consequences ideas which we will turn to in later discussion.

Following earlier commentary here, other potential causes of regulatory failure might be conceived, to wit: public interest perspectives on regulation stress the notion of the *public interest* ... but different groups may hold different views of what this term connotes ... and how the public interest is best obtained may also be disputed. This position, much advanced by advocates of Public Interest regulation, is inherently challengeable ... and thus 'success/failure' will be a function of individual stance as much as of objective review. Contrastingly, commentaries based on interest group theories emphasise the self-interested behaviour of groups in the regulation arena. That this self-interest may be economic, political or even symbolic in nature has already been discussed and such groups will be inclined to assess failure in a predictable way.

[152] Hirschman. A. *The Rhetoric of Reaction* (Cambridge 1991)

However, that the consequences of regulatory failure may be perceived in terms of financial loss, of risk avoidance or of blame shifting is worth re-stating here.[153]

Recalling the systems perspective on regulation prompts comment on the Teubnerian[154] notion of the self-referential system closing itself off from external influence thus failing to adapt to new contexts and/or rejecting information which appears to threaten its existence ... accordingly condemning attempts to regulate that (sub)system to failure. Baldwin et al[155] point to a further aspect of regulatory failure by asserting that the inevitable informational asymmetries[156] between key system actors generate drift. Drift is defined to be "*a tendency of a regulatory system to lose focus and direction*" ... ie. a tendency to fail. They conceive drift to be due to governments changing their regulation preferences over time;[157] to regulatory agents being unable (for multiple reasons) to deliver on their regulatory objectives;[158] and to regulated industries not conforming to their regulatory obligations.[159]

***Regulatory Weaknesses*:**

One regulatory weakness in a variety of areas may not cause a regulatory strategy to fail of its own accord ... but may well combine with other weaknesses to irretrievably damage the strategy. These weaknesses may involve one or more of the following ... *ineffective co-ordination*; *poor organisational learning*; and *simplistic thinking*. Examples from the world of football are easy to find; Wimbledon (2003-4) contrived to lose their ground because of co-ordination issues between their landlord (the council) and a developer. They survived only by moving to Milton Keynes.[160] Arguably, Portsmouth demonstrated poor organisational learning by entering administration

[153] Freud, Jung and Klein all have commentary on blameshifting .. aka 'projection'.

[154] See earlier.

[155] Ibid p250

[156] See section on *systems in precis* in Chapter 1

[157] Coalitional drift.

[158] Agency drift.

[159] Industry drift.

[160] Hence their current name of MK Dons.

twice.[161]. Bradford City are celebrated for their 'six weeks of madness' (profligate spending on expensive new players) which took them into administration in 2004 … simplistic thinking at its most striking wherein it was believed that sporting success would inevitably follow this expenditure.

Co-ordination weaknesses have already been highlighted in the discussion of over/under-regulation. This may occur in contexts in which different regulators have an interest in the same field and even in the same activities. Problems occur when methods, sanctions and even time-scales differ. Baldwin et al[162] note the vulnerability of complex organisations to the 'normalisation of deviance' whereby small deviations from the rule at one stage, perhaps at the exercise of discretion, can be compounded by similarly small and acceptable deviations at subsequent stages and eventually result in regulatory failure. Contrary to intention (echoing the *perversity* point above), attempts to improve co-ordination via the 'more regulation' route may increase cost and delay action due to time-lagging or may reduce regular endeavours, so achieving the perverse result.

That poor organisational learning may be a cause of regulatory failure may not surprise. Like humans, organisations endure bounded rationality which propels the search for solutions which satisfice[163] and the acceptance of results which are sub-optimal. The notion of bounded rationality is often attributed to Simon; it suggests that decisions made by humans are limited by the information available, the individual's thinking ability ... and the time available to make the decision. Notably, no mention is made of motivation!

The complexity of the dimensions of decision-making on non-trivial matters is recognised, at least implicitly, and so exhaustive efforts are not always attendant on taking decisions ... even those in relation to the implementation of regulations.

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[161] In 1998-89 and again in 2010.

[162] Baldwin (ibid) p248

[163] I define 'satisfice' as being equivalent to 'good enough to get an acceptable result in the prevailing circumstances'.

A related aspect of organisational learning is rooted in the notion of the organisational paradigm.[164] The consequence of the paradigm is both information-filtering and direction-setting. Thus, the organisation may attend only to whom it trusts and to what it wishes ... thus discarding perturbing information. The organisation may also have a propensity to conduct its affairs in a manner which has given comfort to the organisation (and its directors) hitherto ... thus driving the organisation along a familiar and supposedly safe route. The consequence of ignoring environmental signals and the refusing to update behaviour patterns can lead to regulatory failure.

The final item of regulatory weakness to be explored here may attract a description 'simplistic'. It is acknowledged that such positions may not be frequently encountered in pure form and are included here as ideal types only. Within this set are the notions that '*one straightforward rule is best'*; that '*rules can last for ever'*; and that '*rule-makers have a monopoly on wisdom'*. Taking these in order, the *one rule is best* notion invites failure because its inherent susceptibility to regulatee exploitation by gaming and is thus subject to an array of unexpected side-effects. The *last for ever* point implies that social change does not occur. When it does occur, often bewilderingly quickly, ... the regulation fails. The *monopoly of wisdom* position relates to the propensity of rulers to believe that their dominant view of appropriateness is unchallengeable[165] ... an affliction which in yesteryear was said to offer employment to Court Jesters. That groupthink has led to regulatory failure in military circles has been well documented elsewhere.[166]

Regulatory Deficits:

The idea of regulatory failure has a historical tang to the term as compared to regulatory condition ... which focuses more on the present. Contemporary regulatory efforts have

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[164] An organizational paradigm is a collective mindset/mental model held by the strategic elite driving their strategic decision-making.

[165] See Janis on invulnerability and groupthink eg Janis, I.L. (1982) *Groupthink: psychological studies of policy decisions and fiascoes*. Boston: Houghton Mifflin.

[166] Bay of Pigs, Cuba 1961

to guard against failure in four areas, suggest Lodge and Wegrich (2012).[167] The language here uses 'deficit' as an umbrella term interpreted as implying a shortfall of some kind. The thrust of their discussion is suggestive and draws attention to a series of areas in which regulation might be deliberated.

The first potential deficit is *oversight*. A lack of oversight may be held to be responsible for inconsistent decision making, especially in conformance activity. It may also lead to insufficient resource allocation for investigation and data collection … and for initiatives aimed at the modification of regulatee behaviour. Black[168] also engages with this point suggesting that centralised oversight mechanisms might be appropriate to combat inconsistency. She speculates that a better resourced regulatory infrastructure might require deeper consideration of issues relating to the recruitment and development of regulators with enhanced and relevant expertise to achieve this oversight. Both Black and Lodge and Wegrich are alive to the possibility of regulators becoming too close to the parties whom they oversee, the '*revolving door'* problem whereby senior civil servants, when they retire, regularly move into senior positions within the industry which they recently regulated. In general, such centralising tendencies may be expected to engender any of the types of resistance suggested above.

Another different, potential deficit is that of *participation*. Here the fear is some regulatory relations are conducted too directly between the regulator and regulatee and may eliminate interaction with interested third parties.[169] This exclusionary process may damage both efficiency and social acceptability outcomes unnecessarily. The obvious remedy is to construct a participatory apparatus which enables others who are not directly in the 'line of regulation' to play their part according to their abilities and inclinations. The proposals made by Ayers and Braithwaite[170] and others of the Smart/ Responsive Regulation schools clearly address this point. Participation deficits may also be encountered when self-regulation is a feature and thus some external validation of

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[167] Lodge, M. and Wegrich, K. 2012 *Managing Regulation : Regulatory Analysis, Politics and Policy* Palgrave MacMillan, London p246-251

[168] Black, J. (2007) 'Tensions in the regulatory state, *Public Law*, 58-73

[169] As may happen in a Pre-pack.

[170] See the idea of 'Public Interest Groups' in *Responsive Regulation* (ibid) ch 2

the self-regulation may be required. A similar planned intrusion into decision-making habits may also help to minimise[171] the blinkering effects of strongly held organisational paradigms.[172]

A further regulatory shortfall relates to over-predictability; an *adaptability* deficit occurs. In this, regulators lack the imagination to see potential types of failure and their causes and begin to exhibit 'comfortable' [173] action plans revolving around 'going by the book' and consequently protecting themselves against allegations of arbitrariness. The regulators' views are thus dulled as to potential problems ahead ... particularly regarding threats to the system itself. Haldane and May (2011) note the slightly counter-intuitive point that diversity in regulatory activity may lead to stability in the regulatory system. Thus, regulators who insert some method of challenge vis-a-vis their regulatory arrangements and who act in an unpredictable way with regard to regulatees may be consuming an antidote to over-routinisation.

The final deficit strikes a substantial chord; the concern here is that those involved in a regulatory system may gain insufficient reward for their participation and thus they deliver performance which is sub-optimal. Thus, there may exist an *incentive* deficit. The notion of the benchmarking of regulator performance is powerful although the criteria for this remain unexplored in much detail, as does consideration of who would benchmark the regulators. The idea of incentivising regulatees is consistent with the tenets of behavioural economics[174] and the practice of 'nudging' has been widely reported elsewhere. In the context of exploring regulation, it is of interest to note that there is little in the literature which explicitly looks at how intra-organisational behaviour in respect of regulation-following might be encouraged/rewarded/nudged.

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[171] eg The Court Jester mentioned above.

[172] Where strongly held views are not necessarily correct and might benefit from being contested.

[173] For the regulator concerned.

[174] See, for example, Thaler and Sunstein's many writings … such as '*Nudge*'.

3.3 Communication Concerns:

Communication underpins many aspects of regulation. Concerns abound in areas such as the cost of gaining information and of promulgating regulations. Drafting problems beset the content of regulation and the language in the regulatory instrument may be obscure. Views differ as to who should take action to ensure that understanding IS achieved. Acquiring data on mischief perpetration involves non-negligible expense for a resource-poor regulator. The difficulties here are exacerbated by the hiding of non-compliance by individuals and firms and there may be over-reliance on informal/ unreliable data collection.[175]

Causes of Communication Concerns:

Rule promulgation is no guarantee that that the associated regulatory objective will be achieved. Hence it is useful to outline potential causes of possible failure to achieve. These lie under three heads viz. *creative compliance, inclusivity problems and communication failures*.

Creative compliance is the hall-mark of a regulatee who adheres to the letter of the law but contrives to subvert the spirit of the law.[176] This may occur as a by-product of cries for more precise law[177] and thus the removal of uncertainty in application ... the greater the rule precision, the greater the potential for creative side-stepping of that rule ; particularly so, if the rule has not been updated in the face of environmental shifts.

The inclusivity problems lie with inadequate drafting of regulatory instruments. These may be over or under-inclusive in effect and may discourage behaviour which is consistent with the rule in question.[178] Bardach and Kagan (1982)[179] assert that

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[175] eg.'whistle-blowing' .. the 'telling of internal and prejudicial tales' to external sources.

[176] The tax-avoidance industry exemplifies this.

[177] eg. McBarnet, D. 'Law, Policy and Legal Avoidance' (1988) *Journal of Law and Society* p113.

[178] Or, conversely, may encourage undesirable behaviour.

[179] Bardach, E. and Kagan, R. (1982) 'Going by the Book' Philadelphia, pp66-77

regulators tend to over-regulate with over-inclusive rules because rules can frequently be made in haste; or because regulators are uneasy about displaying discretion; or because regulators wish to avoid the high cost of information–gathering associated with administering well-targeted regulations. Under-inclusiveness will occur if the regulator is unable to accurately establish the cause of the presenting mischief ... with some non-compliers being over-looked. However, Diver (1998)[180] contends that under/over-inclusiveness may indicate other problems equally caused by informational difficulties which are difficult to apply without costly expert assistance.[181] It can be recalled that transparent and accessible rules surface substantial inclusivity problems whereas detailed, precise and up-to-date rules do score well on inclusivity. The question of over/ under-inclusiveness obliges consideration of which inclusiveness approach is the more desirable for a regulator to follow? ... leading to the review of Shrader-Frechette's (1991)[182] Type 1/ Type 2 risks. Shrader-Frachette suggests that although regulators are more inclined to avoid Type 1(producer) risk than they are to avoid Type 2 (consumer) risk, The Type 1 risk is a rule prohibiting the use of technology (and by extension behaviour) which is falsely seen too be dangerous but is in fact safe whereas a Type 2 rule is one which allows the use of technology which is falsely seen as being safe but is in fact risky. In situations of uncertainty, the suggestion is that regulators ought to err in the opposite direction.

Blume (1990)[183] asserts that the situation is further complicated by a series of indirect communication mechanisms whereby the targets of one message receive the message, perhaps in one code via one medium, and then, in their turn, relay this message onwards towards the ultimate target of the regulation using a different code and medium

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[180] Diver, C.S. (1998) ' The Optimal Precision of Administrative Rules', cited in a Reader on Regulation eds Baldwin, R., Scott,C. and Hood C.

[181] A simplified example of Diver's thinking is whether a rule might be passed prohibiting the use of electric hedge-clippers by anyone over 65 years (clear, accessible .. and easy to enforce assuming birth certificate availability). But there are many over 65s able to cut hedges on their own. However, setting a rule in reliance on a set of variables such as levels of experience, eyesight, upper-body strength and participation in an accredited training course may effectively target those able to use the cutter ... but at a hugely inconvenient cost; an open invitation to those tempted to be creative compliers ??

[182] Shrader-Frechette, K.S.(1991) *Risk and Rationality*, Berkeley, 1991.

[183] Blume, P. (1990) The Communication of Legal Rules 11 *Statute Law Review*. 189

combination and possibly with an altered degree of formality. Professional advisors[184] commonly play a significant part in such indirect communication lines ... but the observation is made that the more extended the communication chain becomes, the more likely it is that problems and issues may arise relating to desired regulatee behaviour.

One reason for the use of indirect communication chains is the probability that encoders of original rules may, in reality, speak a rather different language from those whose behaviour is in question. This is not about intelligence nor of literacy in the conventional sense, it is a matter of *functional illiteracy* whereby the ruled do not understand the terms of the rule ... and thus are unlikely to conform adequately to the expected behavioural requirements. This is often wrongly termed '*mis-understanding'* whereas '*non-understanding*' would be more accurate. Translation is required; hence the existence[185] of the intermediary professional advisor acting to remove the drawback of this type of problem. This problem will be particularly in the foreground when the rule in question is legal in origin and when that law is complex and multi-faceted (as is the case in this inquiry).

Some reasons for Regulatory Communication Misunderstanding :

The promulgation of rules and the expectation that these rules will be understood is problematic. The reasons driving rule promulgation are several and mixed. Communication aims might be *to inform*; *to educate; to influence* ... or even *to protect* the ruler against potential adverse circumstances.[186] Consideration of both communications outcomes and how these might be reached follows briefly …

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[184] Possibly but not exclusively IPs?

[185] Perhaps this is a major justification for the existence of company doctors/turn-round specialists?

[186] In popular parlance, '*the protect your backside*' approach.

The lack of understanding of rules by the ruled:

The much-quoted maxim '*Ignorantia leges non excusat*' is used to prevent[187] rule-breakers in all legal systems from offering a '*I didn't know I was breaking the law* ' defence. There is a resultant tension in the rule-communication process; regulatees are expected to obey rules devised by regulators[188] but which they may not always be aware of, far less be able to comprehend.[189] A further, practical, tension ensues when rules, especially legal rules, are changed moderately frequently over the life of a regulatee.[190] Rule obsolescence, whether a consequence of political or environmental change, thus carries the capacity for confusion in the mind of the ruled which the advice of advisors may not eliminate. Unlearning[191] is difficult ... and the potential for ill-informed behaviour is significant when the field covered by the rule is unfamiliar to the regulate. Arguably, the suggestion that regulatees have the right to be cognizant of rules does not always imply[192] a duty to be cognizant of these rules.

The presence or absence of Positive Action to achieve understanding:

The distinction between making rules known in contrast to taking positive action to influence behaviour is a troubling one. The Hansard Society was sufficiently concerned in 2008 to make a series of recommendations[193] on how the UK Parliament might improve its ability to promulgate legal rules as follows ...

"*In order to enhance Parliament's ability to communicate with members of the public, the Hansard Society recommends that:*

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[187] However, this principle has its roots in 2,000 year old Roman law and in a context then of many fewer and simpler laws being promulgated by rulers in a rather different manner to relatively few members of the ruled class

[188] eg.foreign owners of English football clubs ?

[189] The European Convention on Human Rights Art 7.1 is relevant?

[190] Arguably the case in this thesis.

[191] The activity of dispensing with 'old' knowledge.

[192] In today's different circumstances (from ancient Rome) ... see Introduction (Chap.1) above.

[193] Hansard Society Briefing "*Enhancing Parliament's Ability to Communicate with Members of the Public*". House of Lords Debate , Thursday 18 December 2008

A Communications Service should be established for Parliament;
Parliament's communications strategy should be subject to regular consultation, review and evaluation in relation to optimum principles of accessibility and transparency, participation and responsiveness, accountability and inclusiveness; ... " (further detail re drafting practice followed)

Note this advice was offered a generation after the modern laws governing corporate insolvency[194] were passed and that the Hansard Society was sufficiently concerned to further comment (*as excerpted*) ...

"The language, terminology and rules that govern how Parliament works are often complex and anachronistic ...
Parliament as an institution is often too risk averse in relation to both the concept of change and to communicating ...
The lessons learnt from previous initiatives are yet to be applied consistently
Parliament has to compete with other changing patterns of cultural consumption, an ever-expanding media base, particularly online, and with other institutions that people look to first as exercising more influence on their lives ...
People will only switch on to those issues that interest them
Democracy does not come cheap. But ... the public (do) not think that initiatives to improve communication would be a waste of public money."

As a consequence of the above, Blume's[195] comments appear apposite ..

"*Today many legal rules are in reality hidden and such rules are oppressive. The legal system should not be an exclusive domain for jurists. The gap between 'know and know-nots' is not acceptable in a democratic society."*

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[194] The backdrop to this thesis.

[195] Blume, P. 1990. Op. cit.

This state of affairs possibly helps the cause of the professional[196] with the aptitude and inclination to acquire the knowledge/expertise connected with these rules?

Legitimacy and Regulatory Obedience:

If regulated actors are to obey the regulations communicated to them by regulators, then some acceptance of the regulator's right to regulate seems required. This acceptance may be as a calculation of coercive power ... or rather it's imbalance. But the acceptance may also be brought by a belief that the regulator ***should*** be able to develop rules requiring obedience: it is legitimate to expect compliance. So, there exists the possibility of a normative foundation for legitimacy in that regulator and regulatee share certain values. Whilst Scott[197] typifies values of three sorts .. *economic, social/ procedural* and *security/continuity,* he indicates these types may mix together and the ensuing blends may characteristic of particular sub-sets (social groups) within society. This echoes the earlier discussion re Teubner[198] and re Black.[199]

Regulators may be pro-active in developing their claims to obedience and Baldwin[200] suggests five possible ways in which they might so do. The more each claim is accepted individually and collectively, the more the regulator's claim to legitimacy is increased. The entire list of ways is relevant to our discussion here although some claims are more relevant[201] to one or other of the sub-systems being explored, for instance, football creditors may well perceive the due process claim to be fair in their context and IPs will equally deem the expertise claim to be fair in their context.

[196]Again ... the Insolvency Practitioner ?

[197] Scott, C. in Handbook of Regulation (op. cit) p104-118

[198] Teubner (op.cit.)

[199] Black (op.cit.)

[200] Baldwin (p238 , Morgan & Yeung *Introduction to Law and Regulation*. op.cit)

[201] eg. 'Football creditors' may well perceive the due process claim to be fair in their context and IPs will equally deem the expertise claim to be fair in their context.

Baldwin's list is ...

Claim for Regulator Obedience	Basis for Development of Regulator's claim
The *legislative mandate* claim	.. where the rule is based on a clear order by the state.
The *accountability or control* claim	.. where the operation of the rule has unequivocal lines of accountability.
The *due process* claim	.. where the rule is perceived to be fair by those to whom it refers.
The *expertise* claim	.. where the rule is developed and operated by those with appropriate technical expertise.
The *efficiency* claim	.. where the rule produces results at acceptable economic and social cost.

Whilst retaining the focus on values in legitimation in rule-following, Mashaw[202] emphasises the requirement for rules to be administered justly to retain their legitimacy. He offers a three-fold set of perspectives or "dimensions" for such administrative justice which all add something to Scott's analysis above. His dimension of '*Moral Judgement*' reflects the due process claim to fairness; the '*Professional Treatment*' dimension is clearly linked to the expertise claim; and the '*Bureaucratic Rationality*' is another way of looking at the efficiency claim. But Mashaw is going beyond a typology in his thinking ... for him, the key point is that each dimension has a fundamental goal which differs between the dimensions in a way consistent again with the Teubnerian approach. For instance, the moral judgement perspective attempts to deliver conflict resolution and will thus be appropriate when sub-systems of roughly equal power are in disagreement; the bureaucratic rationality perspective will deliver results where

[202] Mashaw, J.L.1983 cited on p252 of Morgan and Yeung, *An introduction to Law and Regulation* (op. cit.)

programme delivery of rules is of prime importance and the professional treatment view will become paramount when client satisfaction is required.

3.4 <u>Concluding Thoughts</u>:

In a thesis populated by sundry acronyms, the author offers his own acronym to finish the chapter. So, we organise the 'concluding thoughts' with the aid of **MURDER**.[203]

M, here, calls attention to the centrality of *Movement* in enforcing regulation. The context changes, yet the rule may not; the tool may change, but the behaviour may not; the mischief maker may change but the mischief may not. Any analysis of regulatory enforcement which does not account for movement will be inadequate.

U points to *Understanding* ... specifically to understanding the causes of non-compliant behaviour. There seems more to gaining compliance than mere rule promulgation. Thoughtful targeting of potential non-compliers, nuanced matching of message to mischief and awareness of how to negate[204] potential harms resulting from disinclination to comply all appear to be areas which need scrutiny if enforcement is to be meaningful.

R is for *Roles* ... which the various parties play. These roles may be formally conditioned ... or informally derived. But roles are executed in different styles, to different levels of ability and with different enthusiasms over time. Consideration of roles guides the analysis in the direction of the standards of performance of rule enforcement and also to the connections between role-actors.

D indicates *Deficits*. Deficits, gaps and failures featured prominently towards the end of the chapter. They seem important not just as shortfalls and thus instances of the inconvenient and uncomfortable knowledge of non-achievement of objectives but also

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[203] A Crime of Intent!

[204] From *The Character of Harms* above. Sparrow, M.K. (2008) *The Character of Harms* Ch1 Cambridge .

areas worthy of investigation as to cause and to consequence. The possibility of differential perception by the various parties to regulation and its enforcement is real and significant.

Moving to **E** ... signifying *Enablers*. There is frequent mention in the previous discussion, obliquely or otherwise, of the difficulties caused by lack of resource.[205] The absence of appropriate resource is held to commonly disable enforcement. However, it could be pertinent to also highlight that the presence of certain competences can enable regulatory enforcement initiatives to be more successful. At times, this is the focus of the "Better Regulation" movement ... examples addressed might be *flexibility*, *experience* and *empathy* as competences which enable a regulator to function more effectively.

Finally, there is **R** standing for *Responsivity* ; thus emphasising the continuing nature of enforcement yet recognising that actions have their consequences. In an area which revolves round continuing attempts by one or more parties to influence the behaviour of others in a particular direction, it surely makes a great deal of sense to model continuing interactions in a nuanced way? Perhaps there is a time and place when deterrence ought to be favoured and another when persuasion will seem a better way forward?

[205] Often financial ... or perhaps also related to time?

Chapter 4 : Accountability

4.1 Accountability Principles

Exploration of regulatory activity is incomplete without considering which actor(s) should be responsible for the success/failure of any particular regulation. This also prompts consideration of how actors might be held responsible ... and of who could/ should do this.

Clarifying the Term:

Accountability has elusive and elastic meaning; dependent on both user and context. A preliminary distinction is between internal and external accountability. Internal (inward?) accountability refers to a moral obligation to one's conscience for the consequences of actions taken. Actors may feel responsible for what they do. Arguably, this is brought on by personal values or societal norms ... or perhaps, if the actor is a professional, driven by some set of internalised professional standards. In either instance, this involves self-evaluation of personal behaviour by the actor concerned. Conversely, accountability can be seen as being external in character and, for Mulgan (2000)[206]...

"it comprises a number of core elements, namely that an actor is called to account and obliged to explain and justify their conduct to a third party who can ask questions and pass judgment."

[206] Mulgan, R.'"Accountability": An Ever Expanding Concept?' (2000) 78 *Public Administration* 555, 556.

The literature[207] points to different shades of accountability such as legal, professional and moral accountability ... to which this author adds accountability to clients and to organizational superiors. All five types of accountability are relevant to this thesis.

Concomitant with the external focus of accountability is the notion that there **may** be delivery of external consequences[208] on actors. Rhode (2001)[209] emphasizes the difficult to predict nature of future consequences as a useful control on actor behaviour. The external interpretation leads naturally to the external setting of 'acceptable' standards of behaviour. This rather begs the question, though, of the norms driving those who set these standards ... and the perceived legitimacy of the standard-setting activity.

Echoing the earlier theme of potential and future aspects of accountability is the idea of accountability having a responsiveness dimension with actors anticipating the needs/ responses of those with whom they interact and then acting accordingly. This encompasses a spectrum of actor-actions from advising clients in Pre-packs[210] to responding to Regulators operating a *Tit-for-Tat* regime.[211]

Attention will mainly be paid below to external features of accountability .. but the existence of differing norms in the various sub-systems in the investigation and the communication difficulties relating to these different norms will inevitably throw up aspects of internal accountability of interest.

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[207] eg Schwartz, M. 'The Professionalism and Accountability of Lawyers' (1978) *California Law Review* 669, 673.

[208] Either desirable or otherwise.

[209] Rhode, D. 'Opening Remarks: Professionalism' (2001) 52 *South Carolina Law Review* 458, 467–470.

[210] Whereby IPs may advise the Banks or other secured creditors on plans ahead of a formal entry to Administration.

[211] As in Ayres and Braithwaite's *Responsive Regulation* approach.

Why Should Actors be held to Account?:

Perhaps the principal reason for holding to account is the deterrent effect of a detected breach of rules. The deterrent effect is likely related to the expectation (or otherwise) of the infarction ... and possibly also to the degree of sanction commonly attendant on discovery of the breach. It is the fear of consequent sanctions which may encourage rule-following. Deterrence and the responsibility felt by an actor for rule observance are intermingled ... rules which are perceived as being illegitimate may not trigger any sense of personal responsibility in the actor for rule-breaking nor might stretching of a rule beyond its accepted compass[212] engender feelings of responsibility for any breach.

A further reason for holding to account is that external commentary is essential to cope with actors' tendencies to rationalise decisions which are self-serving with protestations to the contrary ... accompanied, perhaps, by a disregard of unfavourable information. Without such outside accountability, a risk obtains of actors displaying unethical conduct. [213]

Accountability may be used to deal with inadequate/defective decision-making by actors/firms. This may be the case where the actor/firm operates in a context where regulations have been externally set, yet discretion has been allowed as to how these are to be accomplished.[214] Here, there is opportunity to go through the motions of rule compliance with a preference for minimal disruption to existing practice and a tendency to attend to the actor's own objectives being a likely result.[215] This may be worsened where there exists a "ladder of communication" where information flows up and down through multiple levels ... the reality of not passing on information likely to throw one

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[212] eg a lawyer insisting that their responsibility was to draw up a contract rather than to have cognizance of wider implications.

[213] As in relations between professional and client; and in relations between professional/ client and others, including the state and society in general.

[214] As is certainly the case for IPs undertaking an appointment .. or for directors running a football club.

[215]Bamberger, K. (2006) 'Regulation as Delegation: Private Firms, Decision-making, and Accountability in the Administrative State' 56 *Duke Law Journal* 377, pp427–429.

actor in a poor light to another is substantial and contributory to inadequate decisions being made.

Accountability may be used to establish/maintain the legitimacy of not just the rule and the rule-maker but of those who have the power to use the rule. This is a question of both ensuring that the power to make decisions has been used in a fairly/ openly and then that any abuses of these powers have/will be held to account. The reputational issues deriving from this are non-trivial[216] viz; the 'rotten apples' label as applied to the rogue IPs prosecuted after the insolvency of Glasgow Rangers FC. For some, the suspicion remains that actors of substance and consequence may receive favourable treatment when held to account. In turn, this may need to be addressed. The markets in some senses provide a form of accountability between actors of broadly similar financial or expertise power[217] but are less able to restrain undesirable behaviour between powerful and powerless when the power gradient is steep.[218]

Lastly, accountability can function as a vehicle for the delivery of corrective justice, in that it may be a route to establishing that the harm caused by one actor to another is suitably compensated. Conversely, it may be the spur to retributive justice enabling the punishment of the actor who has done wrong.

Codes of Conduct and Accountability:

In a regulatory context, actors contribute to two main forms of problem. These are Agency problems and Externality problems. Agency problems arise when harm is done to one actor by a second by behaving in a way against the interests of the first whilst purporting be acting on their behalf. In distinction, externality problems arise when both (first and second) actors behave in such a way as to burden third parties (and Society?)

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[216] See, for instance, the 2012 case of Collyer, Bristow solicitors.

[217] eg as when the Banks and IPs regularly interact.

[218] eg as when deep-pocketed secured creditors manipulate IPs to favour their interests against small, inexperienced unsecured creditors in insolvency proceedings.

with unnecessary cost. Loughrey (2011)[219] comments presciently, that large, well-resourced and experienced actors[220] are unlikely to suffer Agency problems at the hands of, say, IPs as they are repeat players with the power of repeat business. On the other hand, she warns that ... *"However, as externalities serve clients' interests, clients may not restrain them."*

Codes of conduct[221] are germane in that their contents are relevant to the actions to be controlled. This dissertation is not the place for detailed study of Corporate Governance; nevertheless some mention of the contents of the work of the Financial Reporting Council [222] may be apposite. The Financial Reporting Council (FRC) published a revised Corporate Governance Code (Code), applicable from October 2014. The selected excerpts from their guidance on Risk Management that follow below have relevance to the discussion in both this and the previous chapter ...

Exercising Responsibilities:

" *… The board should establish the tone for risk management and internal control and put in place appropriate systems to enable it to meet its responsibilities effectively …*

… But in deciding what arrangements are appropriate the board should consider, amongst other things:

- ➢ *How to ensure there is adequate discussion at the board.*
- ➢ *The skills, knowledge and experience of the board and management.*
- ➢ *The flow of information to and from the board, and the quality of that information. …* "

Establishing the Risk Management and Internal Control Systems:

" *... Risks will differ between companies but may include financial, operational, reputational, behavioural, organisational, third party, or external risks, such as market or regulatory risk, over which the board may have little or no direct control …"*

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[219] Loughrey, J. Large law firms, sophisticated clients, and the regulation of conflicts of interest in England and Wales *Legal ethics,* Dec 2011, Vol.14(2), pp.215-238.

[220] Loughrey clearly envisages the Banks as an exemplar here.

[221] Several are relevant to this thesis ... eg the Code governing the Conduct of Insolvency Practitioners.

[222] FRC Guidance on Risk Management, Internal Control and Related Financial and Business Reporting (September 2014)

" *... Training and communication assist in embedding the desired culture and behaviours in the company. To build a company culture that recognises and deals with risk, it is important that the risk management and internal control systems consider how the expectations of the board are to be communicated to staff and what training may be required ..."*

A possible reason for corporate failure may lie with the personality characteristics of the key directors concerned. Despite the well-meaning endeavours of many committees over the years[223], none of the codes to date have explored this prospect. Corporate failure may be due to many causes but a possible origin of inappropriate behaviour as having been brought on by enduring personality characteristics has scarcely been considered.

However, Okoye[224] points out ...

"*Behavioural issues can, therefore, be viewed as risks to the corporate governance process, and these risks are significant because they have the potential to result in corporate failures. Questions then arise as to whether existing corporate governance mechanisms have taken cognisance of the significance of behavioural risks; if there are processes in place to manage such risks, how effective these mechanisms are in relation to these risks."*

Okoye goes on to cite two instances from fairly recent corporate life to illustrate his concern. One instance is that of Robert Maxwell (of Maxwell Publishing fame.) and the other being Fred Goodwin of RBS Group.[225]

On Maxwell, Okoye reports inspectors saying ...

... "We regret having to conclude that notwithstanding Mr Maxwell's acknowledged abilities and energy, he is not in our opinion a person who can be relied on to exercise proper stewardship of a publicly quoted company'. It is disturbing to reflect that Maxwell was still allowed to hold executive and managerial positions after the discovery of these flaws in his

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[223] Greenbury in 1995; Hampel in 1998, Turnbull in 1999 … all following in the footsteps of Cadbury in 1992.

[224] Okoye, N. (2013)'The personality of company directors and behavioural risks in corporate governance: Bridging the unidentified gap' *International Journal of Disclosure and Governance* Vol. 10, 3, 261–286

[225] Very sadly, this author has to confess the doubtful privilege of having performed management consulting contracts for both firms and, having met both men, can concur with the sentiments reported.

personality and behaviour, only for a greater manifestation of his inappropriate behavioural tendencies to occur 20 odd years later in 1991, with far greater implications."...

On Goodwin, Okoye cites the FSA Board as claiming in 2011 that

… "t*he FSA had identified a risk created by the perceived domineering behaviour of the CEO at RBS*" …

Perhaps one might observe that UK Company Law does not make mention of any need to contemplate the management of personality risk ... and that is an issue returned to later in the discussion on the 'fit and proper persons rule' later.[226]

The ideas propounded by Okoye fit fairly well with the soft law/self-regulation notions advanced by Ogus inasmuch as they might be incorporated in codes of governance or similar guidance. This might able the reap the advantage of flexibility whilst acknowledging the risk of failure from non-compliance. A hybrid regulatory approach to personality risk management might insert hard law sanctions in order to improve 'success' rates.[227]

The principles enshrined in codes should be unambiguous in language and in application. There should also be clarity as to which principle has primacy if the two conflict. Distinctions could be made between principles which relate to conduct between actors;[228] to conduct within an actor entity [229] (such as a professional firm or a football club); and to conduct having implications for Society.[230] Often, the issue is not one of principle its absence; the issue is one of interpretation and application. Regulators and regulatees can have different views on the meanings and implications for action linked to any one principle ... and any actor adversely affected may plead special/mitigating circumstances as to why that principle should not apply to them.

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[226] See section 7.2 ... particularly the footnote on Mr Marinakis.

[227] See section 2.2 generally for linkage to these points.

[228] Such as between IP and client.

[229] Such as between IP and an employer who is an accounting firm.

[230] Such as the externalities above-mentioned.

Codes often emphasise giving independent advice **to** the client but the requirement to be independent **of** the client is mysteriously[231] absent.[232]

A Duty for Responsible Administration?:

According to Sabel and Simon (2016), bureaucracy is constructed around the tension between a system of stable, hierarchically promulgated rules and lightly supervised discretion ... but they worry that the balance may no longer suit today's issues in that "*addressing current problems requires more flexibility than rules permit and more transparency than discretion typically affords."* [233]

They write in the context of the policing of Civil Rights but it would seem just as appropriate to the work of IPs. The US notion of a '*duty of responsible administration'* points to an increasing interest in the need to reassess routines in the light of changing circumstances. This might offer an additional yardstick against which the accountability of actors might be measured? It also appears an interesting route to assessing the ways in which discretion has been used.

4.2 Accountability for Actions:

This section turns to examine those areas in which actors may be held accountable. These are developed mainly relating to IPs as this is a well-reported area … but many of the central ideas suggest connections to other areas[234] of our enquiry.

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[231] The ensuing regulatory deficit embedded in Codes is further enlarged when one searches for mention of accountability to Society.

[232] Which may be intriguing when Banks contract with IPs for advice prior to a Pre-pack?

[233] Sabel, C.F. and W.H Simon. (2016) The Duty of Responsible Administration and the Problem of Police Accountability 33 *Yale J on Reg* 165

[234] As for example, Directors on *Running the Business*; the Insolvency Service on *Acting as a go-between*; and the Football Authorities on *Sanctioning* .. all to follow in this section.

Accountability across Tasks:

Finch, in her *Avenues of Accountability* (2012)[235] paper, makes the point that often an across-the-board judgement on an actor's performance may be over-comprehensive in approach; it may make more sense to break an actor's performance into constituent parts[236] with each element being assessed separately.

IPs[237] undertake several elements/functions and various factors impact differently on IP accountability for carrying out these activities. A selection of tasks follows[238] **…**

Advisory work:

The provision of client advice by IPs will be given under contract which indicates the scope[239] of advisory work. Given that the clients will be experienced, knowledgeable and, crucially, well able to communicate in the appropriate language, they will be in a good position to assess the quality of advice given. Other interested parties are unable to benefit from such advice at this stage but may learn of its substance later at creditors meetings. Potentially, IPs can be accountable to their clients via the market mechanisms of repeat business and reputation. IPs are not directly accountable to other creditors[240] for advisory work. Additionally, IPs are adjured to be heedful of duties owed to all creditors to note the possible liability of *"any person who is party to a decision that causes a company to incur credit and who knows that there is no good reason to believeit will be repaid".*[241] In the circumstances of a pre-pack sale, the *Kayley Vending*[242] case established that the applicant should make the same disclosures as

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[235] Finch, V. 'Insolvency Practitioners: The Avenues of Accountability' *The Journal of Business Law*, 2012, Issue 8, p.645

[236] Dependent on the functions carried out.

[237] The line of argument could be extended to cover the Insolvency Service and the football authorities .. but for space reasons this has been avoided.

[238] They are examined singly but overlap in practice.

[239] Which will delineate it from any subsequent role for the IP should an Appointment be forthcoming.

[240] SIP16 looms as a form of background regulation of IPs in the instance of directors obtaining an interest in pre-packed asset sales.

[241] SIP16

[242] *Kayley Vending Ltd, Re* [2009] EWHC 904 (Ch)

outlined in SIP16

Collecting Evidence and Data:

With respect to turnaround[243] IPs need to collect information on entry into administration which needs to be up-to-date, accurate and relevant. Disclosure of information around the area of pre-packs falls within the ambit of the Insolvency Code of Ethics which urges IPs to ensure that decision-making is transparent, understandable and readily identifiable TO ALL affected by the proposed sale. The criterion of relevance expands the information–collection net widely ... in theory to anyone with commentary relating to possible outcomes. SIP16 acknowledges that this may not be practically possible before key decisions are made when it sets out after the event disclosure requirements that the IP should bring forward to unsecured creditors ...

"*A detailed explanation and justification of why a pre-packaged sale was undertaken, so that they can be satisfied that the administrator has acted with due regard for their interests*."

IPs are accountable under the Insolvency Act[244] for their actions and, as an Officer of the Court,[245] must behave rationally and reasonably when exercising discretion. Finch[246] comments that the Office of Fair Trading's 2010 report concludes that IPs were wont to supply information to unsecured creditors which *"does not greatly help their understanding of the process"* and she reports that a majority of respondents considered that the information provided under SIP 16 to justify pre-packs "*is insufficient for [them] to make an informed judgement as to whether the sale is in their interests (or does not unfairly harm their interests)*".

Consequently, it is difficult to argue that IPs are held to account by this device.

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[243] Not everyone agrees with Finch that this is adequately performed.

[244] IA 1986 Sch B para 3.

[245] When acting as an administrator.

[246] *OFT, The Market for Corporate Insolvency Practitioners (2010) paras 1.16, 4.70*. See also *IS, Improving the Transparency (2011), p.12*

Managing the Business:

IPs conduct a variety[247] of operating management activities ... and charge fees for this. As officers of court, they will be responsible to the judiciary for the quality and consequences of their actions. In practice, judges are reluctant to comment on this. Finch suggests that they justify this reticence by observing that they have neither the skill nor the experience needed to make such judgements. Secured creditors are able to exercise oversight as and when IPs make their reports but there appears no substantial mechanism whereby unsecured creditors are '*kept in the loop'* as to ongoing operational activity.

As to the accountability of IPs for the fees[248] charged for managing the business, one notes that this is an area which has received much scrutiny in recent times … thus encouraging comments of the '*no smoke without fire*' type?

Thus, the degree of accountability exhibited by IPs in relation to the task of day-to-day running of the troubled business seems notable only in the case of powerful secured creditors. A similar profile might also obtain in respect of fees charged for this management task.

Acting as Go-Between:

The IP may also be portrayed in *go-between* terms … acting as a 'fixer'. This calls for a high degree of communication and social skills whilst facilitating, manoeuvring and deal making. The display of such attributes in relation to repeat-playing and knowledgeable secured creditors will not encounter many problems as specialist language, norms and susceptibility to the profit motive can be expected to smooth matters. Perhaps IPs are inclined to give substantial weight to the interests of such parties in developing '*solutions*'? The picture differs when communications take place with unsecured creditors whose strengths do not include facility with the relevant

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[247] including HR decisions about staff retention; financial decisions about funds raising and funds usage; and interacting with suppliers and customers.

[248] Fees may be fixed either by Creditors' Committees or by the court. There were moves in 2010 to obtain greater transparency around the calculation of fees and expenses; and to require more detailed reports to creditors .. and in 2012 a new Practice Direction set out **eight** guiding principles to be followed when preparing fee invoices. The Insolvency Service was also sufficiently aroused in 2011 to engage in consultation as to whether IP fees might be challenged after the event by dissatisfied parties.

concepts and whose inclination to engage with the IP is diminished by their fragmented, unorganized and poorly resourced positions. Thus, unsecured creditors have minimal inclination to hold IPs to account for their actions as a fixer ... and secured creditors have minimal need to do this.[249]

IPs are also subject to control by their own regulators (see discussion of SIP 16 above) but this addresses only matters for the Creditors' Meeting and is silent on the exercise of communications skills. In theory,[250] the courts also have a part to play.

Protector of Rights:

IPs are obliged to conduct the affairs of a troubled company with respect to the rights of all affected parties. Absent this, they can be held to account in three ways. Firstly, by provision of law: there is the provision under the Insolvency Act 1986 for aggrieved actors to obtain remedies for misfeasance/unfairness and the courts can remove IPs if they find conflicts of interest. Surprisingly, the courts do not view a breach of the IP's professional bodies guidance as automatic grounds for removing an IP from an appointment. Secondly, by the internal regulations of their professions: the failure of an IP to protect rights may incur action via the relevant regulatory standards mechanisms of their profession. The reputation of professions for such self-regulation is not high. Or, finally, by references to Codes of Conduct: a third aspect where control may be required relates to questions of conflicts of interests ... which can result in one party's rights being downgraded in favour of another's. The Insolvency Code of Ethics offers clear framework as guidance in this regard and there also exists a Code of Conduct promulgated by the Secretary of State.

But in the effort to hold Insolvency Practitioners to account on the task of Protector of Rights, the conclusion is largely similar to that pertaining to the other tasks explored above, in that ... secured creditors do not really need the controlling devices; unsecured creditors have neither the inclination nor the resource to avail themselves of these

[249] They can use informal social power and market power perfectly well to protect their position.

[250] Control of IP's actions might be via the courts where it is open to an aggrieved creditor to bring an action in respect of an IP's failure to discharge the obligation to take all relevant factors into account when arriving at decisions. This seems excessively costly for any likely returns and may be discounted as an everyday source of control.

devices; professional bodies apparently have other priorities; and, as the administration of justice requires very deep pockets, the courts rarely become involved.

Accountability Supports:

To ensure that accountability succeeds, supporting mechanisms are needed. Although three[251] separate support mechanisms are explored below, there is no suggestion that these supports stand on their own. Tripod-like they serve to complement each other[252] in real-life use.

Reports ...

Regulators may call for reports by regulatees on their performance and use these reports to assess any need to hold the regulatee to account. The hope, here, is that the preparation of reports will counteract the self-interest and cognitive biases which may influence any decision-making. The ensuing dialogue may be informal and designed to inform/persuade or to guide behaviour back to the expected standard. Alternatively, the assessment may result in sanction-imposition when the non-compliance is more serious. The IP Code of Practice is an example of a mechanism of this type.[253] Whether this mechanism will support accountability is questionable. Calls to account may be resisted by actors who sense that the attempt to control[254] lacks legitimacy.[255] This could imply ***intra***-systemic[256] control by this method may be more successful than ***inter***-systemic[257]

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[251] To wit: reports; dialogue; and sanctions.

[252] Each is suggested to be able in some way to help in the process of bringing actors to account for their behaviour and actions.

[253] Possibly there may exist an expectation that larger, more sophisticated actors will develop internal systems which encourage self-checking of performance against Code of Practice standards before such reports are provided. This will be so for IPs who work for larger groups of accountants or solicitors who will have further professional codes to consider and with which compliance will be required.

[254] - or the controller - or the mechanism of control?

[255] Naturally if all these elements are perceived to be legitimate then the converse will apply.

[256] As when IPs are invited to report on their performance by their own RPBs.

[257] eg the legal system's attempts to influence the behaviour of company directors.

attempts.[258] Nevertheless, the publicity effects associated with the use of this mechanism may reassure public confidence.

Dialogue ...

Associated with reporting, dialogue[259] may further accountability via the guidance effect. The Insolvency Service is renowned for its "Dear IP" letters[260] which may be prone to regulatory capture [261] (see earlier). A sophisticated, yet real, problem highlighted by Lerner and Tetlock(1999)[262] is whether the views of the regulator are known in advance to the regulatee. If **not**, they suggest regulated actors will be more self-critical and more ready to explore alternative perspectives in anticipation of the regulator's response. If the regulator's views **are** known then the only effort needed may be for crude/ unthinking conformance.[263] Thus, there is every chance that regulated actors will press for indications as to what compliance looks like.[264] If paradigm change[265] featured in the objectives of the regulators, then allowing predictability may not be the best route to adopt.

Effective sanctioning ...

Greater accountability arguably will follow more effective use of sanctions whereby the deterrent effect of being sanctioned will influence actor behaviour. The deterrent stands to legitimate behaviour of actors who behave within bounds and to punish behaviour

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[258] However, this does not discount the possibility that, within an actor-subsystem, there may be disquiet as to differential treatment between large and small actors

[259] Formal or otherwise.

[260] And also from other sources.

[261] At least solicitors (aka The Law Society) are aware of this and have suggested ways of dealing with the issue.

[262] Lerner. J. and P. Tetlock, (1999) 'Accounting for the Effects of Accountability' *Psychological Bulletin* 255, 258–259.

[263] Such as unreflective box-ticking.

[264]Or perhaps exchange 'war stories' amongst fellow actors so that some predictability can be achieved.

[265] Paradigms are organisational 'mind-sets' driving organisational behaviour: if an organisation consistently behaves in a way counter to regulation then a regulator may wish to alter this paradigm.

which is outwith these bounds. It also fulfills a Public Relations function by demonstrating to Society that the regulator has legitimate power over relevant actors

The behaviour of actors will be strongly influenced by the norms held by the actor These norms will have a combination of origins; strongly held norms are deeply internalized, weakly held norms are unlikely to influence behaviour beyond the short term. Thus, sanctions are likely to link only to weakly-held norms as to "appropriate" behaviour. As Jones (2006)[266] and Blair and Stout (2001)[267] note, key factors in deep normalization include whether the regulated actors consider the norm to be fair, whether they understand that compliance is expected and whether they sense that their peers also comply. There exists also concern[268] that over-frequent sanctioning leads to a culture of resistance and/or denial as actors attempt sanction avoidance rather than behaviour modification.

The nature of the sanction may also have effect. '*Let the punishment fit the crime*'[269] oversimplifies matters but the regulating bodies[270] have an arsenal of graded sanctions which are deployable to fit different levels of misdemeanour ... and they have additional reference powers to recommend striking off professionals in the most serious cases.

The above does not dwell on the resource implications for regulators when using sanctions[271] but it is probable that 'the powerful' will defend themselves; and so the regulator may choose to save ammunition for less resourceful targets. The use of

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266 Jones, R. (2006) 'Law, Norms and the Breakdown of the Board: Promoting Accountability in Corporate
Governance' 92 *Iowa Law Review* 105, 129.

267 Blair, M. and L. Stout. 'Trust, Trustworthiness and the Behavioral Foundations of Corporate Law' (2001) 149 *University of Pennsylvania Law Review* 1735, 1796–1798.

268 As expressed in general by Ayres, I. and J. Braithwaite, *Responsive Regulation: Transcending the Deregulation Debate* (Oxford: OUP, 1992) 20.

269 Gilbert, W.S. and A. Sullivan *The Mikado* 1889

270 Those associated with corporate insolvency.

271 Engaging with regulated actors who will defend themselves vigorously in the courts will exhaust the budgets of all but the most well-endowed of regulators.

sanctions may not do much to hold the powerful to account ... but may well be useful when dealing with smaller actors or those whose norms are broadly consistent with those of the rule-setter and of the regulator. Parker (1997) [272] observes that what is missing with holding powerful professional firms[273] to account is some practical "*framework of accountability and responsiveness to dialogue with the community*" in which they might be obliged to justify their actions to the community.[274]

Recent developments for IPs:

There have been recent changes[275] in the structure of the IPs Regulatory Regime. Some are noted here ...

Authorisation [276] to practice as an IP must be received from (now[277]) one of five RPBs, each monitored by The Insolvency Service. An augmented Complaints System for receiving complaints against IPs[278] has also been introduced.[279] For our purposes, the main area of complaint explored is IP's remuneration[280] (and expenses) …

RPBs are now expected to encourage IPs to charge fees that are "fair and reasonable." In addition, new rules (which apply in bankruptcy, administration and most liquidation cases) require IPs to provide upfront estimates of their fees for creditors' approval. They will not be allowed to take extra fees unless agreed by creditors."[281]

Upholding of a complaint means that IPs may face a range of sanctions from their RPB; currently the ultimate sanction being withdrawal of authorisation to practice ... tough on

[272] Parker, C. (1997) 'Competing Images of the Legal Profession: Competing Regulatory Strategies' 25 *International Journal of the Sociology of Law* 385, 401.

[273] and their employees !

[274] Echoing Ayres and Braithwaite's PIGs ? (public interest groups).

[275] Source : Commons Library Briefing 28 September 2016 ; changes effective as from September 2016

[276] As per Small Business, Enterprise and Employment Act 2015

[277] Originally there were eight RPBs regulating IPs.

[278] Note ... not about specific legislation nor public policy

[279] June 2013

[280] Recall that IPs may have a coincidental (!!) interest in prolonging the extent of an Administration if they are being remunerated on a per diem basis or some derivative thereof.

[281] Ibid

the IP concerned as this activity is very well remunerated[282] but of no great help to the complainant? The Insolvency Service reported[283] in September 2016 that ...

*"The RPBs should enter into discussions with the Insolvency Service to consider the feasibility of a mechanism **whereby compensation can be paid to the complainant by the IP** [284]where they have suffered inconvenience, loss or distress as a result of their actions.*

This puts the holding to account of IPs on a commensurate level with that to which directors of financially distressed football clubs may be held to account both by 'public law and by private law'.

4.3 A Coda on Accountability.[285]

As a sizable thrust of this thesis involves the activities of IPs, the analysis continues and briefly attempts to pick up some of the themes touched on in the preceding sketch of the area ... and to travel with these themes just a little further. In a way, this is a coda which points to the changing nature of the work of the IP.

Administrative Accountability:

Ab initio, IP practice might be surmised to have been dominated by small groups of solo or loosely connected practitioners devoid of managerial expertise or oversight.[286] However, this seems to have changed over time (at least in part). The inexorable increase in size of IP assignments and their requirement to be serviced by increased resource quite possibly drove an increase in size in the firms which employed IPs ...

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[282] Cooper, C. and Y. Joyce. (2013) "Insolvency practice in the field of football " *Accounting, Organisations and Society* 38 108-129

[283] CLB Sept 2016 op. cit.

[284] Author's emphasis.

[285] Much of the thinking in what follows is suggested by the work of Friedson and Dingwall who both principally write in relation to medicine. See later and in references for specific citations.

[286] See Finch. V. (2009) *Company Insolvency Law*, 2nd Ed. (2009) Cambridge University Press … generally 202-221

mainly large accounting practices with some concomitant growth in legal practice too. Inevitably this began to constrain the dominance of the IP as an independent practitioner as manager-administrators exerted control. The ways in which control developed could be examined elsewhere (perhaps under '*developments in practice structure*') but most of these focus on financial outcomes at the possible expense of more value-driven approach (see norms of profession above).

An intriguing second difficulty arises with the notion of '*client resistance*.' Friedson (1983)[287] points to (in the medical context) the apparent readiness of patients to seek alternative advice from unlicenced sources[288] (perhaps the homeopathy movement ?) in preference to "managerialist medicine ". This implies a faceless approach to medicine based on large-population-generalities rather than careful examination of the specifics of a presenting individual. One might speculate that the continuing (and expanding ?) existence of the '*Turnround Consultancy* 'echoes a similar trend in Corporate Insolvency ?

Client Accountability:

The term 'client' sits awkwardly in the current discussion. If there is to be a payment nexus then in very many cases, the unsecured creditor is in fact the payor; if the appointing arrangement is held to be key, then the secured creditor (banker, bond-holder and so on) might be argued to be the real client (especially in the instance of repeat-playing) ; but if some parallel is made to the medical profession, then the distressed company might be inferred to be the client/patient. This might be seen as hair-splitting but is meaningful in the context of accountability.

Arguably, Friedson's early work does not really take account of evolving social and market issues in at least four dimensions …

- ➢ The demise of paternalism: Asymmetrical possession and use of information, knowledge and expertise might have been more acceptable in an era in

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[287] In the '*The Reorganization of the Professions by Regulation'*, Friedson. E (1983**)** Law and Human Behavior, Vol. 7, Nos. 2/3,

[288] Op.cit.

which "the professional knows best" but perhaps this approach is less justifiable when even the novitiate unsecured creditor may expect some sense of meaningful communication and involvement in the insolvency process. It is acknowledged that this factor does not apply in respect of others in the community of practice. That this may drive a superficial attempt by IPs to "onside" unsecured creditors by the formulaic communication of information might possibly be expected?

➢ The rise of negligence litigation:

This has been discussed elsewhere in the literature[289] in relation to other professions; as yet, this may be somewhat insignificant in the UK .. yet, UK practice often appears to evolve slowly but surely behind that in the US. Whether this will constitute a threat to the current professional dominance of the IP is questionable as, presumably, matters in such actions would feature expert testimony by one IP against another IP... but it is a factor worth continuing observation and perhaps some State "wing-clipping" of IPs powers and practices can not be ruled out?

➢ The emergence of competition:

That IPs still control activity within the formal process of corporate insolvency is not held to the main issue here. It is more a question of what transpires "upstream" of that formal process. IPs themselves agree to by-pass much of the formal process when they become involved in "pre-packing" yet there seems evidence of rather more action then heretofore by individuals / firms acting as 'Turnround Specialists.' Such turnaround activity may, of course, come after the IP appointment but the thought persists that they are approached as an alternative to engaging with the formal process. When one adds the comment that the Restructuring Market activity is ten times that of the Corporate Insolvency market,[290] one might speculate that Bond-holders / sophisticated international lenders are perfectly aware of and supportive of alternatives to

[289]eg In Friedson op.cit. but in a variety of other articles also.

[290] Private communication with a family member responsible for business affairs in a very large international law firm.

using the formal legal process ... at least in the context of high-value entities and possibly those with cross-border operations and/or ownership.

➢ The changing nature of 'Gate-keeping'[291]

That professionals control access by others to desired states/resources/processes is almost trite. Nevertheless, the opportunity to misuse this control is probably incontrovertible ... which is not at all to say that all professionals DO become involved in such abuse. However, there has been an abundance of recent examples[292] which highlight the dangers in this regard. It takes only a moment to recall the widespread use and acceptance of 'bribes' in relation to the prescription of pharmaceuticals or the continuing question-marks in relation to UK audit practices. It is hardly likely that the State will not attempt to introduce mechanisms to deal with such abuse.

Reviewing Friedson through Dingwallian[293] spectacles gives rise to the following Endnote ....

"a monopoly such as that enjoyed by IPs is given in response to their manifest expertise AND to their role as societal control agents .. in other words insolvency is something requiring social management. The claims of creditors (particularly of unsecured ones) need to be rationed to accord with the capacity of Society to deal with them; IPs are the main tools in this rationing process. "

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[291] See for instance the Zacharias article "Lawyers as Gatekeepers ". This article makes a simple, and ultimately uncontroversial, point that professionals such as IPs are gatekeepers, and always have been. Whatever one's position on the merits of the specific reforms currently being proposed, it is important to avoid the misconception that IPs have no role to play in preventing client misconduct.
Zacharias, F. C. "Lawyers as gatekeepers", *San Diego Law Review* Sept 2004

[292] Of which, the current criminal proceedings for fraud against three IPs involved in various aspects of the insolvency of Glasgow Rangers FC is possibly merely a current manifestation of an on-going problem within this profession. The fact that no Scottish firm was inclined to accept this case may indicate some locally widespread sense that all was not right at that club? Duff and Phelps, for whom the accused IPs worked, are not Scottish.

[293] As suggested by reading Dingwall R (2008) *Essays on Professions*. Ashgate Classics in Sociology. Aldershot: Ashgate.

Underlying this view lie two factors ... an economic one relating to the scarcity of resource and a moral one in that Society has a responsibility to meet the claims resulting from corporate insolvency.

Notwithstanding the events of 2007-2009, the notion of scarce societal resource may be over-played. But, what may happen if/when Society reviews it's labelling of the corporately insolvent role from that of unmotivated deviance (whereby claims such as discussed above are justifiable) to some other label, like motivated deviance ... still deviant but different. Would Society then expect different actions from creditors (and other parties)?... and would Society continue to require IPs to perform their current function?

In short, would the emphasis move from social control to social protection ... with the policy objective shifting to that of ensuring that people get what they pay for? And how would this be done?

Chapter 5: An Overview of the Context of Corporate Insolvency (via the metaphor of The Insolvency Casino)

Even superficial examinations of corporate life within capitalist economic systems cannot fail to note that the bright side of success is mirrored by the dark side of failure. This is inevitable when competition throws up winners and losers. This chapter looks at what happens to these losers.

Patterns of behaviour can be discerned in those involved in their appetites for risk; their experience/knowledge of both business life in general and of failure in particular; and their dispositions to individual/collective action. The ways in which English law constrains, guides and ameliorates these patterns will be indicated ... and this will take place against an almost hidden backdrop of tensions created by 'new' capitalism; by post 2008 economic turmoil; and by ever-increasing internationalization of social, economic and political structures.

The metaphor of the modern gambling casino is here used to structure the discussion and in turn we look at 'The Players'; at 'The Rules of the Game'; at 'The Set Plays' and, finally, at 'The Awkward Cases'. In each instance, key features are explored before ending with conclusions in an Epilogue with links to other chapters being offered. We start with a short exploration of the back story behind what goes on 'in the casino' … the roots of UK Corporate Insolvency.

5.1 The Roots of UK Corporate Insolvency Legislation.

The oft-considered start to reviewing English Corporate Insolvency Law is the so-called Cork Report of 1982 which laid the founds for the major legislation of the 1986 Insolvency Act. There were actually two Reports by Kenneth Cork-chaired committees; Cork 1 (of 1976) which was established as a consequence of the UK joining the European Community and looked at how English law on bankruptcy / insolvency might sit with other European jurisdictions ... and the more substantial Cork 2 which is the principal focus here. This report pushed the notion of 'rescue' of distressed companies centre-stage and made many proposals aimed at facilitating the saving of businesses and

jobs which under the existing legal regime might well have been lost. For Cork, business rescue needed talent and time. Talent was required to develop and execute plans aiding the ailing firm and time was required for the firm to find its feet and for the rescue plan to run its course. Where providers of capital had been granted a floating charge, there was ample opportunity to insert an experienced receiver to potentially provide the talent to achieve more than might be derived for creditors from a straightforward winding-up. Prior to Cork's proposals a formal[294] moratorium[295] was not available.

In the event, the 1986 legislation did not provide for a moratorium; this had to wait till the Insolvency Act of 2000 wherein such a facility was enacted for small companies. However, the 1986 Act did introduce the new Company Voluntary Arrangement procedure (CVA) which enabled the distressed company to enter into a formal contract of composition with creditors and thus give that company an opportunity for a fresh start. It also created a new Administration process. The first set of Insolvency Rules also grows from Cork 2 and were implemented in 1986.

Both Cork 2 and the following legislation attempted to address the tension between allowing entrepreneurs to do what they do best (developing new ideas for profit) and making those entrepreneurs who behaved recklessly or dishonestly[296] face the consequences of their actions. Since 1986, there have been a number of further amendments to both the law and practice of corporate insolvency; some, specific and narrow (such as legislation relating to banks[297] and to insurance companies[298]) and some with rather wider implications (eg. The Human Rights Act 1998, (HRA)). For instance, there were two Insolvency Acts passed in 1994; the first[299] dealing with the liability of

[294] Notwithstanding the use of *the London Approach* for larger firms whereby an informal stay might be arranged.

[295] Of the type prevalent in US legislation; see later comments re 'Chapter 11.'

[296] Curiously, little attention seems to have been given to incompetent entrepreneurs!

[297] eg. The Banking Act1989

[298] eg. The Financial Services and Markets Act 2000

[299] Insolvency Act 1994

office holders to employees and the second[300] clarifying the position of purchasers of land at an impugned undervalue.

In 2000, a further Insolvency Act[301] provided that small companies could seek a moratorium in the context of voluntary arrangements; that disqualification undertakings might substitute for court hearings/legal proceedings in connection with director disqualifications; that changes to evidence provisions when criminal proceedings were being undertaken ... in order to comply with the HRA; and finally, the 2000 Act conferred power on the Secretary of State to give effect to the Model Law on Cross-Border Insolvency.[302] This international dimension to UK corporate insolvency law was amplified by the coming into force in 2002 of the EC Insolvency Regulation[303] which established a European Union regime for the handling of cross-border insolvency cases.

The period up to 2002 was one of review ... which culminated in the enactment of the Enterprise Act (EA) of that year. Several notable reforms were thus brought forward ...

- the abolition of the floating charge holder's right to appoint an administrative receiver.
- the abolition of the Crown's status as a preferential creditor.
- substantial streamlining of the administration procedure.

Subsequently, the Insolvency Service has engaged in a long-running project attempting to review and simplify both the Insolvency Rules and associated statutory instruments and also to lighten the bureaucratic burden connected with the administration of insolvency procedures. This occasioned the Deregulation Act of 2015 (DA). Moreover, the 'Transparency and Trust' review resulted in the Small Business, Enterprise and Employment Act 2015 (SBEEA) which establishes significant changes linked to ..

- the bringing of wrongful and fraudulent trading claims by administrators.
- the increase of penalties when directors are disqualified.

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[300] Insolvency (No 2) Act 1994

[301] Insolvency Act 2000

[302] Subsequently incorporated into UK law in 2006

[303] The EC Regulation on Insolvency Proceedings 2000

- ➢ changes in sanctions to exercise liquidators' powers. Creditors' meetings and proving of debts.

Certain sectors have somewhat different provisions regarding insolvency, notably Financial Services[304]. This factor will be returned to later, primarily in connection with the development of the Sporting Interest in section 7.3

The UK has historically been open to influence from external sources; and corporate insolvency law is no exception. The most obvious source of influence from the US is 'Chapter 11'.[305] Periodically, both academic commentators and legislators in the UK have contemplated how Chapter 11 might be of benefit in the UK. This procedure has much to offer companies in distress, being both flexible and rescue-aligned and is said to be the usual choice of route for business restructuring. Key elements include the continuation of ownership of its assets by the distressed firm which continues to be operated by the previous managers albeit under court supervision and ostensibly for the benefit of creditors. However, a Trustee may be appointed if the court believes that the existing management is dishonest or ineffective.

Under Chapter 11, the company in question can avail itself of a moratorium during which a Chapter 11 rescue plan/restructuring can be assembled for the approval of the creditors committee.[306] This plan is confirmed only on the affirmative votes of creditors whose votes are both divided into classes and are weighted by the amount owed. In the event of the required majority not been achieved, there lies the possibility[307] of a cram-down to gain approval despite hold-out opposition. UK interest has perhaps focused most on the cram-down, moratorium and emphasis on unsecured creditor involvement technical provisions as well as on the cultural predisposition to offer a '*second chance*'.

That modern commercial life necessitates cross-border trading is clear. Perhaps it thus inevitable that cross-border insolvency may also result. Such events throw up instances

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[304] The Financial Services and Markets Act 2000 (Insolvency) Order 2001

[305] More precisely …. Chapter 11 of the US Bankruptcy Code / (US) Bankruptcy Reform Act 1978

[306] Appointed from non-insider largest 20 unsecured creditors

[307] Certain statutory tests have to be met for this.

of conflict of laws which need to be dealt with in as methodical and predictable way as possible. UK corporate insolvency is not confined to national borders ... and thus influence from outside the English legal regime has to be noted. Here we will the influence of both the United Nations and of the European Community, the latter[308] being considered in a more detail later in this chapter and the former being briefly dealt with here.

The United Nations[309] brought forward a 'model law'[310] in 1997 which subsequently has been included in the domestic legislation of many major trading countries. Like the EC legislation which followed, the model law attempts to establish the idea of "main proceedings" to be commenced in the Centre of Main Interest (COMI) in relation to the corporate debtor's activities; imaginatively, all other proceedings linked to the debtor are termed 'non-main'. The purpose of the model law is to encourage signatory states to co-operate with foreign insolvency officials/practitioners in respect of both main and non-main proceedings; and to attempt to limit preferences for local creditors as against foreign creditors.

5.2 The Players in The Insolvency Casino.

In this section, attention will focus on those main players who dominate the play in The Casino. All three types possess varying degrees of skill, power and motivation. All have access to information which they may use to pursue their separate agendas and, for at least two types of player,[311] they have substantial repeat-playing experience.

Insolvency Practitioners (IPs):

IPs are said, at least by themselves, to constitute a profession. Not everyone will perceive them to conform to early sociological criteria on this claim and this may be of

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[308] This was the impetus for Cork 1 mentioned above.

[309] In full, The United Nations Commission on International Trade Law

[310] UNCITRAL *Model Law on Cross-Border Insolvency 1997*

[311] IPs and lenders.

significance during our investigations. Being more specific, one of Flexner's[312] necessary criteria for a profession is the existence of '*public spiritedness*'; the absence of which disqualifies a group from being truly a profession. Acknowledging some IPs give time without charge to '*professional*' activities and noting that IPs claim that not all of their fees are paid, it still is hard to make a strong case for the existence of this criterion. But, then Flexner wrote three generations ago ... and perhaps the definitional world has moved on?

The examination of the professions in the literature often encompasses issues *of status* (both within and without the profession), *of control* (both of access to the profession and quality of work done) and *of power* (to determine the focus of agendas and the distribution of rewards). Additionally, attention is paid to a profession's propensity *to develop norms and values*. This is central in two ways. Firstly, in the way that this may mesh with the state's usage of IPs as a *Soft Law* mechanism to control the manner in which Capitalism's failures are disposed of; and secondly, as a hidden driver (or motivator) for the way in which IPs conduct business.

IPs practice in corporate insolvency, in personal bankruptcy ... or in both. Some appear to work full-time in their field and others part-time; about two-thirds of IPs accept 'appointments'.[313] Further shadowy areas in connection with IPs link to gender[314] and little seems known about other potential areas of within-tribe power and dominance.

Consequent to Cork and ensuing legislation, IPs gained a monopoly licence from the state to conduct most proceedings relating to corporate insolvency. Following the Cork Report in 1982, the Government enacted legislation (Insolvency Act 1986 and then Enterprise Act 2002) giving a monopoly of most of the activity surrounding corporate insolvency to IPs. That this affected the conduct of proceedings in personal bankruptcy

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[312] Flexner wrote 90 years ago and pioneered the use of attribute theory in the study of professions. Attribute theory has its critics but the idea is helpful here.

[313] About two thirds take "appointments" ie conduct cases. It is not known what the remaining third does .. but surely they cannot all work in The Insolvency Service ?

[314] eg.the female President of R3, Liz Bingham, lamented in 2013 that only 20% of the IP profession were women. (see Recovery Summer 2013)

is not relevant to this thesis. They are few[315] in number and highly qualified. In effect, IPs hold double qualifications; firstly, as an accountant or solicitor and then by examination and experience to become an IP. Much is made of the difficulty of the exam which is consistent with the idea of professional status-building but little is known about the nature of the mandatory five years' experience required.

The handling of substantial/complex cases is likely to be done by IPs working within one of the Big Four accountancy firms and a de facto ranking system for the profession is discernible with personal bankruptcies being handled mainly by small, provincial IP firms. There is also some sector-speciality formation with insolvency events at football clubs being handled by a group of repeat-playing IPs. IPs generally have prior backgrounds, either in accounting or in law. Leaving aside those IPs who are regulated by the Insolvency Practitioners Association (and whose membership rules are ambiguous), a cursory inspection of R3 membership figures points to the accountant to solicitor ratio being about 4 :1. Interestingly, despite being a small group, they will be licensed by one of several professional bodies[316]... who themselves are monitored by The Insolvency Service.
A neo-Marxist view of IPs offers the thought that IPs have several overlapping functions in modern capitalist society with some IPs being better at one function than another. Three main functions appear evident,[317] viz:
a). "*Sclaffie*" (a Glaswegian term for roadsweeper) whereby the IP cleans up the mess relating to Failed Firms created by the workings of Market Forces. This tedious work demands application but not inspiration. Efficiency of clean-up is valued more than speed in this regard. According to Frisby (see her 2007 report to ABRP, the predecessor of R3), many insolvency procedures take above a year to conclude; possibly as IPs are diligent in their job of maximising the insolvent firm's estate, possibly not?

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[315] Perhaps around 1750, according to R3.

[316] At the time of writing there were eight bodies (RPBs) who together regulated the activities of the members of this tiny profession ... there now five RPBs. Despite the obvious cost and inefficiency penalties that this attracts, R3 in a recent consultative response to government declared that no change was necessary; hardly the expected response of a forward-looking profession?

[317] These categories and the ensuing exposition are from the author.

b). “*Para-medic*” whereby the IP attempts, perhaps with expert help, to rescue Failing Firms that may still have a viable life left to lead. Here, speed is of the essence and short-cuts are common. A source of continuing concern, felt most keenly by unsecured creditors, is the practice of ‘pre-packing’ whereby a failing company is sold quickly and without formal advance notice. The suggestion is that speed is of the essence in order to keep key employees and to retain essential supplies; this is countered by unsecured creditors suggesting that such a sale may materially undervalue the firm and thus disadvantage their returns.[318] The difficulty in the valuation of knowledge (see later) merely compounds the complexity on this.
c). “*Cherry-picker*” whereby the IP pursues *la Dolce Vita* and, at a pace congenial to the IP, deals only with such dramas resulting from the market as seem to be substantial yet easily financially beneficial to that IP. Occasionally, the State seems concerned[319] about the exercise of this function.

Lenders (and Lending):

With respect to corporate insolvency, there are many players who could be loosely categorized in the Lender category. Arguably, all voluntary[320] lenders might fall to be considered here but perhaps it is more fruitful to exclude trade suppliers[321] and the tax authorities. Instead, we briefly focus on suppliers of capital and of capital goods.

Historically in the UK, firms raised much of their capital via the debt route[322] and the principal suppliers of funds were the banks. Virtually always, this funding was secured either on a fixed or floating charge basis, sometimes both.

Fixed charges were secured on specific assets such as land and equipment which the firm might not dispose of without the prior approval of the lender. This gave the creditor

[318] But also see *Subsequent Events* section in Chapter 6.

[319] See the OFT Report on “*The market for corporate insolvency practitioners* “which tries to throw light on this and related concerns.

[320] Thereby excluding non-voluntary lenders such as tort claimants and employees.

[321] Because these are possibly small scale, frequent and for short time periods .. and, crucially, are very often unsecured.

[322] As compared with equity.

substantial protection although there was always the risk of the value of the secured asset falling. In contrast the floating charge was able to be used/disposed of in the usual course of business as the firm saw fit. This freedom could be advantageous to the firm. As the charge floated over all the firm's assets it was possible that the sum covered would appreciate in hypothetical value. However, in corporate insolvency the floating charge crystallized but does not enjoy preferential status (unlike the fixed charge) and became unsecured debt.

Other sources of funds for various uses in the business can include hire purchase, lease and invoice factoring. Normally, these would have some form of Retention of Title clause giving substantial security to the lender if corporate insolvency occurs ... these secured assets are removed from the insolvent company's estate before dealing with any distributions to creditors.

When a company fails, its assets fall to be distributed in a legally determined sequence viz: firstly, comes the secured fixed charges and then the fee and expenses of the office holder; then followed by preferential debts such as 'the prescribed part' and certain employee rights[323] and then, secured floating charge holders; these are subsequently followed by amounts owing to unsecured creditors and finally (if at all), the shareholders of the wound-up firm obtain any residue. The 'prescribed part' included above is an amount which must be set aside by the administrator or liquidator for the benefit of unsecured creditors to a maximum of £600,000.

Depending on the nature of the loan, it's size and the relations between bank and firm, frequently there would be conditions attached to such loans.[324] Banks would take a distant interest in the affairs of the firm if these conditions were met. The onset of distress, however, would trigger an increasing series of requests[325] for information and other business-related items with the ultimate step being the transfer of the firm's banking facilities to '*The Intensive Care Department*' whereby the bank would press the

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[323] See later in Section 5.5 for amplification.

[324] Frequently termed 'debentures'.

[325] Some would say 'threats'.

distressed firm to take remedial steps[326] or alternatively the route to receivership and winding–up might be selected without further firm-managerial intervention.

In recent times, the role of the banks has begun to change ... noticeably so, for larger companies. Banks are often content to become debt-originators and sell on such debt in a packaged/securitized way to investors who may have differing appetites for packages of different types of risk. There are two immediate consequences with another potentially following later. The first consequence is that having sold the debt, the banks lose interest in monitoring the performance of their debtor clients with knock-on effects for unsecured creditors who previously had a free ride on monitoring the company performance. The second consequence is that dispersed ownership causes co-ordination difficulties between parties if the firm becomes distressed.

The final development of note is germane for bigger firms approaching financial problems … the advent of the market for distressed debt. Traders in this market use sophisticated techniques in order to spot opportunities to purchase debt of distressed companies in the hope/expectation of being able to either to later sell the debt for a profit ... or even to convert the debt into equity of the distressed firm and with judicious actions return the firm to health and then cash in the acquired equity … a form of informal corporate rescue, if you will. This route seems rather less likely for smaller businesses.

***(Delinquent) Directors**:*

In the UK, any registered company has the privilege of limited liability and the directors of such companies are not personally liable for the debts of that company. This situation can invite unscrupulous conduct by directors and the law seeks to address this.

The current provisions in relation to corporate insolvency vis-a-vis directors stem in no large measure from the Cork 2 Report which was concerned by the need to address such mischiefs as *phoenixisation*. Phoenixisation was the (mal-) practice of directors allowing their company to take on trade debts for both supplies and equipment and then,

[326] See remark elsewhere about RBS and its GRG activities.

possibly whilst extracting substantial sums via remuneration, running the firm down till it was no longer viable. At which, the directors declared the firm insolvent and invited a 'tame' liquidator to deal with the liquidation. The directors then purchased the assets of the old company 'for pennies' and resumed trading under a similar name and using the old company's workers. The creditors of the old company were left to pursue the now-empty shell for satisfaction of its liabilities ... a forlorn pursuit!

The Companies Act (CA) 2006[327] lays out the duties which lie upon a company director and the term director is wide in reach encompassing those who have been formally appointed (de jure); those who assume the role (de facto) and those whose instructions other directors commonly obey (shadow). That these duties lie also to the future as well as the present was confirmed in *Winkworth v Edward Baron.*[328] Thus, lenders engaged in company management like banks, managers deputed from parent companies[329] and turn-round specialists (but NOT IPs) may all be susceptible to challenge for their actions particularly in respect of duties to avoid interest conflicts; to act within powers; and to take care. The *Produce Marketing Consortium*[330] case particularly stressed this last point; one which could well trouble some directors of football clubs. Of particular import in the context of impending company failure is the morphing of the focus of such directors' duties ... away from promoting the company for the benefit of its members to having regard for the interests of creditors as a whole. A position which the decisions in *Gwyer* and in *Whalley* did not entirely resolve.[331]

Breach of CA duties renders the director concerned liable to an action for misfeasance. Any monies recovered from this source are returned to the company and used to pay creditors in the usual order. Such actions are raised in the name of the failed company

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[327] CA 2006 s171-177

[328] *Winkworth v Edward Baron Development Co Ltd* [1986] 1 WLR 1512

[329] In *Hydrodan (Corby)Ltd, Re* {1994] BCC 161 it was held that such managers had to have specific responsibilities in the subsidiary.

[330] *Produce Marketing Consortium (in Liquidation), Re* (*No 1)* [1989] 1 WLR 409

[331] *Gwyer* [2003] 2BCLC 153 and *Whalley* [2004] BPIR 75.

by the liquidator/administrator and, are assignable to third parties ... which allows the liquidator some discretion in terms of the risk/reward calculus in respect of litigation.

In addition to the Companies Act provisions in respect of directors, there are also provisions in the Insolvency Act 1986 which attempt to deal with directorial behaviour. These mainly relate to the notions of '*fraudulent trading*'[332] and '*wrongful trading'*,[333] both criminal offences. The former offence requires that the director in question has knowingly behaved dishonestly by everyday standards.[334] The well-known "Ghosh" standard on (dis)honesty was disapproved by the verdict in *Ivey v Genting.* Being subjective, it is notoriously difficult to prove that this standard has not been achieved. The wrongful trading offence[335] is one which focuses on the idea of director negligence[336] rather than on dishonesty. It is worth noting in this regard that a separate offence of '*fraudulent trading'*[337] under the Companies Act still exists. The *BCCI*[338] case merely underlined that the offence needed to be intentional.

Wrongful trading attempts to catch directors (as above) who continue in business if "*at some time before the commencement of the winding up of the company, that person knew or ought to have concluded that there was no reasonable prospect that the company would avoid going into insolvent liquidation*". Here, the director is assessed on the basis of having the skill needed for their job [339] (or higher if they possess special qualifications).

As the cause of action in regard to possible s213 /s214 offences lies only with the liquidator/administrator it is not currently possible for third party assignment to take

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[332] IA 1986 s213

[333] IA 1986 s214

[334] *R v Ghosh* [1982] EWCA Crim 2 ; *Ivey v Genting Casinos* [2017] UKSC 67

[335] s214 IA 1986

[336] Perhaps easier to prove ?

[337] CA 2006 s993

[338] *Bank of Credit and Commerce International SA, Morris v State Bank of India* [2003] BCC 735

[339] As in *Re Produce Marketing Consortium Ltd (No 2)* which was the first UK case in this area.

place. Thus, there may be reluctance to carry such litigation forward. Awards made on successful proof of offences under the Unlawful Trading provisions are compensatory (thus reflecting company losses in the time period involved) rather than being punitive (as would be under conviction for a CA s993 offence).

The Company Directors Disqualification Act 1986 (CDDA) outlines the procedures used to investigate and disqualify company directors who are suspected of misconduct. The disapproved behaviour included continuing to trade when knowingly insolvent; continuing to take credit when there was no reasonable prospect of the creditor being paid; and misrepresentation of facts about the company. In particular, the Act extended the grounds upon which a court could grant a disqualification order, as well as extending the maximum period of disqualification to 15 years for directors found guilty of wrongful or fraudulent trading.

The CDDA consolidates much legislation related to disqualification orders and implements the new concept of mandatory disqualification. Section 6 states "*that a disqualified director cannot take part in the direction, management, promotion, or formation of a limited liability company in the UK, unless given leave by the court*".

Liquidators or Administrators are required to submit Returns/Reports[340] on the directors of any company entering Insolvent Liquidation or Administration to the Insolvency

[340] A return confirms no misconduct whereas a report sets out evidence of misconduct found.

Service (IS).[341] These documents are prepared following professional rules[342] [343] and are not shown to the director(s) concerned. Should the IS consider it to be in the public interest, they will open proceedings for director disqualification. In which instance, it is open to such a director to choose to give a 'Disqualification Undertaking' having a similar effect to an order but usually resulting in a shortening of the disqualification period and in cost savings. Someone subject to an order or undertaking in this context[344] may not act as a director; nor may they manage, promote nor form a company directly or indirectly.

A director violating the terms of a Disqualification Order is guilty of an offence carrying a sentence of up to 2 years in prison and/or a fine. They may also be held personally liable for some/all of the debts of the failed company.
This act also lays out the standards for assessing unfitness to be used to determine whether a director is fit to serve as the director of another company in the future based on their previous performance and conduct.

Three types of disqualification are covered in the CDDA – *mandatory*, *automatic*, and '*at the Court's discretion'*. It is worth observing that the CDDA only applies when a company has gone into liquidation and that this may incline directors to consider CVAs (where there is no investigation of directorial conduct) rather than liquidation. This is a point of which directors of financially-troubled football clubs are usually acutely aware.

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[341] The IS will act on behalf of the Sec of State for BIS.

[342] SIP 2 (on investigations) and SIP 4 (on reporting misconduct).

[343] Matters which SIP 4 advises should feature in a D Report are:
- *Attempted concealment of assets*
- *Unexplained disappearance of assets*
- *Unexplained deficiencies in the balance sheet*
- *Transferring assets to other companies on terms which are not commercially reasonable*
- *Preferences (giving unfair priority to the repayment of money owed to themselves, their family, other companies that they control or creditors to whom they have given personal guarantees)*
- *Loans made to directors*
- *The occurrence of dishonoured cheques*
- *The use of stalling tactics with the company's creditors*
- *Allowing tax arrears to accrue whilst trading continues and, in particular, failing to account for VAT, PAYE and NI whilst trading continues*
- *Improperly re-starting the business through another company*
- *Abuse of a factoring or invoice discounting facility*
- *Taking deposits from customers and failing to deliver the goods or services for which the deposits were taken and cases resulting in criminal conviction*

[344] Of limited companies.

Further provisions relating to the CDDA were introduced in 2015[345]
The new and amended provisions are intended to tighten up the directors' disqualification rules to ...

"prevent an individual from acting as a director where that individual through their conduct has shown him or herself to be 'unfit'. The measures introduce new grounds for disqualification, create a new way in which creditors may receive financial redress for loss suffered through director misconduct, make the disqualification regime more efficient and update the matters that courts must take into account when considering a director disqualification."

It is also significant that, since the Welfab[346] case, it is clear that directors also have a duty to consider their employees in circumstances surrounding corporate distress.

5.3 <u>The Casino Rules</u>:

<u>Liquidation</u>:

The process of Liquidation brings death to the company, there is no way back. In one form or another, there has been legal provision to wind-up a company's affairs since the mid nineteenth century.[347] The sole aim of liquidation is repay as much as possible to creditors from the sale of such of the wound-up company's assets as can be ascertained and sold. In the unlikely event of there being a surplus after repayment, any outstanding monies are returned to shareholders.

There are several possible routes to company death, each dependent on context

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[345] As part of the Small Business, Enterprise and Employment Act 2015

[346] *Re Welfab Engineers* (1990) BCC 600

[347] Joint Stock Companies Winding-up Act 1844

- ➢ The voluntary route, initiated by directors / shareholders. If the directors can declare that the company is solvent, then they will remain in control of the '*last rites*'. If not, then the creditors are in charge of the procedure.
- ➢ The compulsory route, whereby the court is petitioned for a compulsory winding-up order. This route may be started by one of shareholders/ directors/creditors/the company itself. However, it should be noted that insolvency is only one reason for the petitioning; motives may be mixed as in the *UK-Euro Group*[348] case.

Additionally, if an Administrator has been unsuccessful in achieving some form of rescue (see later), there also exists a route into Liquidation from Administration.

The Liquidator is there to maximize the value of the company's remaining assets. Thus, sales need not be undertaken immediately and there is much discretion exercisable as to the exact conduct of this value-maximising activity. For instance, action may be taken against outgoing directors for 'a contribution' or attempts may be made to avoid some previous transactions contracted by the company. There also exists a moratorium whereby any disposal of the company's property made after the commencement of winding-up shall be void, unless the court decides otherwise.

Distribution of funds realized by these sales is governed strictly by statute with claims being met in the following sequence [349] …

- ➢ Fixed security holders
- ➢ Preference creditors ... such as the liquidator; certain employee claims (see later); the 20% ring-fenced unsecured creditors fund.
- ➢ Holder of a floating charge
- ➢ Unsecured creditors
- ➢ Any deferred debt

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[348] *UK-Euro Group Plc, Re* [2006] EWHC 2102 (Ch)

[349] IA 1986 ss 176ZA (insolvency practitioner expenses), 175 (preferential creditors: employees and pensions) and 175A (ring fence fund)

Any residue goes to shareholders. In the context of professional football, '*football creditors'* are preferred creditors in that they MUST be paid in full if the club concerned is to survive.

The Liquidator owes duty only to the company and thus may be sued only by the company for such as negligence or improper use of powers. Also as a fiduciary, there is the usual requirement against the making of secret profit and acting in conflict of interest.

The process of appointing a Liquidator can take time ... during which assets and/or records may be lost or delinquent directors may still be able to continue with misconduct such as fraud. In this situation, the court can appoint an emergency Provisional Liquidator to take immediate temporary control of the company thus rendering the directors out of office without further notice. Any application for such an order would be expected to demonstrate that the company is without doubt going to be declared insolvent and that there has been misconduct by one or more directors. This procedure may also be followed on application of the Secretary of State for a 'Liquidation in the Public Interest'.

Pari Passu:

On the engagement of the liquidation procedure, individual creditors[350] are no longer able to pursue the company for debt repayment. Instead, creditors become part of a collective regime which has the objective of equitably distributing the estate of the failed company amongst its creditors. This distribution is performed rateably and is called *pari passu*. However, not all the pool of collected assets are distributed in this manner as certain creditors may be paid from the estate before distribution to ordinary creditors (see secured creditors and preferred creditors above). Additionally, other creditors may have utilized rights in rem to except certain assets from the common pool. Consequently, this pool can well be substantially reduced prior to calculation of distributions.

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[350] But see discussion on The Football Creditors' Rule later

Acting to support the *pari passu* distributions, is the common law '*Anti-deprivation*' rule which stipulates that a contract term cannot operate to deprive creditors of an asset which the failed company possessed just before the beginning of insolvency. The landmark case which settled many of the complexities involved in relation to anti-deprivation was *The Perpetual Trustee* [351]case. This case is is also relevant to the High Court hearing in regard of the Football Creditors' Rule which is the subject of section 6.3 later.

The contract terms are usually one or other of two types viz…

- Contracting out of *pari passu* is not permitted (*British Eagle*[352] being the renowned case) as this would promote one creditor ahead of others. However, there is nothing to prevent a term agreeing a relegation behind others.
- Contracting to remove assets from the insolvent estate on insolvency is not permitted if this is for less than fair value consideration. However, exceptions are made if rights/ obligations are made over time ... so leases and licences commonly are terminable upon insolvency.
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Both *pari passu* and the anti-deprivation rule turn out to be central to our Chapter 6 discussion of the Football Creditors' Rule. Interestingly, *pari passu* does not apply to an Administrative Receivership as this is 'not a true collective proceeding'[353] as established by the *HPJ UK* [354]case.

Other Rules:

The period between serving the petition for winding-up and the appointment of the Liquidator is one in which the assets of the failed company may face a risk of

[351] *Perpetual Trustee Co Ltd v BNY Mellon Corporate Trustees Services Ltd* [2009] EWCA Civ 1160

[352] *British Eagle International Limited v Compagnie Nationale Air France* [1975] 1 WLR 758

[353] See Goode, R. (2011) *Principles of Corporate Insolvency Law*, 4th Ed. Sweet and Maxwell. 238

[354] *HPJ UK Ltd (in Administration), Re* [2007] B.C.C. 284, Ch D

dissipation. Thus, there is a general rule that dispositions by the failed company of any property, even if they benefit the company, are void absent approval by the court. Dispositions can be money payments, asset transfers by gift, exchange or sale and granting of mortgages or leases. Transfer of property by prior arranged contract and use by the company of its own assets are not deemed to be dispositions. Avoided dispositions will mean that the property is treated as never having left the company and thus may fall within the scope of an appropriate floating charge. Ward LJ. is cited by Goode[355] as suggesting that avoidance mechanisms under the Insolvency Act …

"*… are integral to and central to the collective nature of bankruptcy and are not merely incidental procedural matters …* "[356]

There also exist five main reviewable transactions in which the incoming Liquidator may take an interest in order to swell the failed company's estate by having such transactions set aside and the Liquidator certainly has a duty to investigate prior transactions of the failed company. In no particular order, these are ...

- *Transactions at an undervalue*;[357] this occurs when the company makes a gift or enters into some transaction wherein the consideration provided by the purchaser is notably less in money value than the provision by the company. Such transactions may be challenged by the Liquidator if they occurred up to two years before the onset of insolvency and the transaction took place when the company was unable to pay its debts.[358] There is a rebuttable presumption, here, that the transaction was made to a 'connected person.[359] There are defences to the claim to void such transactions if the company can show that it entered the transaction in good faith or if the company had reasonable grounds at the time of the transaction for thinking

[355] Goode, R. (2011) *Principles of Corporate Insolvency Law*, 4th Ed. Sweet and Maxwell. 522

[356] *Rubin v Eurofinance SA* [2010] EWCA Civ 895

[357] IA 1986 s238

[358] Where the company fails to pay a statutory demand; or proves to the court that it cannot pay its debts as they fall due; or has assets less in value than its liabilities
(including contingent and prospective).

[359] eg. directors, shadow directors and associates.

that it would benefit the company in some way. It is a matter of doubt that player-transfers are always made at true market value in the context of a financially embarrassed football club seeking to avoid insolvency.

- *Preferences*;[360] these can be seen as the company doing anything or suffering anything to be done to a person (creditor) which has the effect of putting such a person in a better position if the company enters liquidation than would otherwise have been the case. The key test in this instance is not just '*intention*' but '*desire*'... the company must positively wish the result. The relevant times for preferences are two years for a connected person and six months otherwise.
- *Floating charges* ;[361] the avoidance here is to prevent the company granting a floating charge for existing debt where no new consideration is given. If the charge is to a connected party then the two year relevant period applies; if the charge is to an unconnected party then the relevant period is six months with the proviso that the company needs to be insolvent at that time or to become so as a result.
- *Transactions defrauding creditors* ;[362] this catches transactions which attempt to put the company's assets beyond the reach of anyone who might make a claim against the company in the event of insolvency or which otherwise prejudices the interests of creditors. There is no relevant time period in this instance. The popularity in football circles of off-shore accounts to conceal asset ownership and to help avoid tax is oft-reported. Some argue[363] that this defrauds creditors.
- *Extortionate credit transactions* ;[364] the mischief dealt with here is that the company may have entered into a credit arrangement in which the company was required to pay grossly exhorbitant amounts in respect of the risk borne by the credit provider. The relevant review period for this is three years.

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[360] IA 1986 s239g

[361] IA 1986 s245 and IA1986 Sch B1 paras 3, 51 and 56

[362] IA 1986 s423

[363] See media coverage of *The Panama Papers*.

[364] IA 1986 s244

The liquidator also has the power of ‘disclaimer’ which entitles the unilateral repudiation of a prior contract so as to preclude the requirement for future performance of that contract. The disclaiming of unprofitable contracts was an action approved of in the *Nottingham General Cemetery*[365] case.

It should be stressed that the law does not hold a director personally liable solely for any of the above transactions. However, Liquidators do investigate the conduct of directors of insolvent companies and may well cover this in a report under the CDDA.[366]

One notable principle affecting the extent of the insolvent company’s estate is “*Insolvency Set-off*”[367] as contemplated by the Insolvency Rules.[368] Here, set-off acts as a type of netting arrangement in which one of the parties (either the insolvent company or its creditor) applies the sum owed to it by the other to the reduction of any sum owed by the second party to the first. The resultant balance then remains to be paid or claimed as appropriate. The rules for this seem clear …

- The rules are mandatory and the court may not vary them. Authority for this is the *NatWest v Halesowen* case.[369]
- They take immediate effect upon liquidation.
- They cannot be disapplied by the prior agreement of the parties.

Further to these, may be added the requirement that the set-off be in expressed in monetary terms and that the debts are held mutually.
As Lord Hoffman characterized it, … “*Insolvency set-off enables the creditor to use his indebtedness to the insolvent as a form of security*.“[370] Thus, the underlying effect of a set-off is to give a preference to one creditor as against the rest of the creditor class; in effect, this creditor gains an unpublished security.

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[365] *Nottingham General Cemetery Co, Re* [1955] Ch 683

[366] Company Directors’ Disqualification Act 1986

[367] The other types of set-off are known variously as statutory; equitable; contractual and bankers’ set-offs; they will not be pursued further here.

[368] Established in conjunction with IA1986.

[369] *National Westminster Bank Ltd v Halesowen Presswork and Assemblies Ltd* [1972] A.C.785

[370] in *Stein v Blake* [1996] AC 243 at 251

5.4 <u>Set-plays in the Casino</u>:

As a preface to the discussion on 'Set-Plays', we might note that warning signals may exist for those interested in the financial affairs of any particular company. In an effort to facilitate transparency, the UK Government has required[371] a substantial amount of financial information[372] to be lodged with the Registrar of Companies and this is easily available for scrutiny.[373] Of course, these warning signals may not always be heeded[374] by some or all of the key actors.

***Administration**:*

Administration lies at the heart of the post-Cork Report attempts to establish a 'rescue culture' in UK Corporate Insolvency activities. Its ultimate aim is to offer the prospect that financially distressed companies with the capacity to become viable in the future are able to carry on their business. The administration procedure can be started either by application[375] to the court for an Administration Order or by the out of court route which merely requires the filing of papers with the court indicating that an Administrator has been appointed.[376] The current practice for bigger or more complex administrations is to appoint Joint Administrators ... which inevitably helps with the time scales and information processing entailed in this procedure.

Special procedures also exist for financial service companies.[377]
Applications for Administration Orders need to be able to show that the company concerned is currently unable to pay its debts or will so become within a very short

[371] With penalties for defaulting.

[372] eg Annual Report and Accounts; particulars of charges; particulars of all special and extraordinary resolutions.

[373] Although, arguably, only specialists may make complete sense of such material.

[374] Which calls into question issues of motivation and of understanding.

[375] Usually made by
the company's directors or creditors.

[376] May be made by the company or its directors or by a secured creditor who is the holder of a "qualifying floating charge" ("QFC").

[377] eg The Banking Act 2009. For space reasons these will not be followed further here.

period; exception to this rule pertains when the application has been made by the holder of a QFC who is entitled to appoint in the event detailed in the charge document allowing enforcement of that charge.[378] However, the court still retains the discretion not to grant such an application if it sees fit.

Whatever the route followed, the incoming office-holder is required to offer an opinion that the purpose of Administration as set out in the Insolvency Act 1986 is '*reasonably likely to be achieved*'. This purpose is stated in hierarchical form to be, firstly, the rescue of the company as a going concern. If this is not achievable or does not yield the best result for creditors, then the second objective applies viz: the result of gaining a better outcome for creditors as a whole than would be obtained by winding the company up. In the instance of this objective not being practicable, then the third and final objective of realizing property for the benefit of secured and/or preferential creditors obtains.

On the completion of any filing and notice requirements, the distressed company automatically commences the protection of an interim moratorium pending the appointment of the administrator. During this moratorium, the company is protected against being wound up and legal proceedings may not be commenced;[379] security may not be enforced and goods held under hire purchase; leasing or retention of title agreements may not be repossessed. Landlords may not regain entry to premises let. However ... a big however ... a QFC holder has the right to appoint their own Administrator who will take precedence over the preferred appointee of others. In some circumstances, the QFC holder can appoint an Administrative Receiver who may then move to wind the company up.

If the out of court route into Administration is selected and there is no one to whom notice giving notice is a requirement, there is no interim moratorium and the filing of the requisite documents triggers a full moratorium. On this, the holder of a QFC loses

[378] Commonly, a default under a Loan Agreement.

[379] Except on Public Interest grounds.

the power to appoint an Administrative Receiver[380] and any wind-up proceedings are dismissed.

On appointment, an Administrator takes over the complete responsibility for the management of the distressed company including its property. This is accompanied by the assumption of wide powers which potentially may conflict with those of existing Directors who consequently lose their powers unless specifically consented to by the office-holder. This may be the case if the Administrator wishes the company to continue trading for the time being and is satisfied with adequacy of control of and by these Directors. The office-holder acts as the agent of the company and has a duty to act for the benefit of all[381] [382]creditors.

As soon as possible after appointment the Administrator will need to obtain a Statement of Affairs detailing assets and liabilities; and fixed and floating charges from the Directors of the distressed company. This will help both in the assessment of the current financial situation and in the formulation of proposals which the Administrator is required to submit to all known creditors[383] prior to the initial creditors' meeting. It is a requirement that these proposals are sent within eight weeks of appointment and are discussed within ten weeks.

The requirement to hold an initial creditors' meeting is obviated in the instance of the 'pre-pack' sale whereby the sale of some or all of the company's assets is agreed prior to the Administrator's appointment and the sale then proceeds quickly on appointment. This route does not need the approval of creditors and consequently its use is an on-going source of concern and disapproval.[384] Those dealing with Administrators in good

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380 See *Downsview Nominees Ltd v First City Corp. Ltd* [1993] AC 295 for relevant authority.

381 As compared with an Administrative Receiver whose duty lies solely towards the holder of the Qualifying Floating Charge responsible for the appointment. For a charge to be a QFC it must relate to the whole, or substantially the whole, of the company's property.

382 Again, see account of FCR which follows in next chapter.

383 And also to members of the company.

384 See comments elsewhere in this chapter on Pre-packing in general.

faith and providing value in consideration do not need to enquire whether the Administrator is acting within their power.

The administrator also does not need to convene an initial creditors' meeting if there are sufficient funds to pay all creditors in full or, more likely, there are no funds (other than the 'prescribed part'[385]) available at all for a distribution to unsecured creditors. The meeting, however, must be convened in the event of more than 10%[386] of the creditors so wish.

In respect of the Administrator's sundry powers, these may usefully be compared here with those of a Liquidator. Both may seek court orders for the setting aside of transactions at undervalue; for preferences; and for fraudulent activity. Currently,[387] only the Liquidator may seek a court order for a directorial contribution to the company's estate if investigation has uncovered acts of unlawful trading. Both have a duty to provide a report[388] to the Insolvency Service on the conduct of current and previous directors.

After 12 months,[389] the administration of the distressed company ends. The IP concerned may also demit office earlier if it is felt that the purpose of administration has been sufficiently achieved. In the event of sufficient funds having been raised to pay secured creditors in full and there are monies available for a distribution to unsecured creditors, then the administration may be terminated via a Creditors' Voluntary Liquidation.[390] Other possible exit routes from administration are via a CVA; via a Scheme; or via Compulsory Liquidation ... the merits of each approach will be dependent on the prevailing circumstance. In the instance of there being no property or funds available for distribution, the Administrator will usually dissolve the company.

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[385] The proportion of the proceeds of the sale of assets subject to any floating charge, currently up to a maximum of £600,000, which is set aside for their benefit of unsecured creditors).

[386] By value.

[387] About to be changed via the Small Business, Enterprise and Employment Act 2015

[388] See comments elsewhere in this chapter on Directors on general.

[389] Extendable in complex cases by court order or by creditor consent.

[390] See comments elsewhere in this chapter on Liquidation processes and procedures.

Pre-Packs*:*

On entering administration, the Directors of the distressed company lose their executive powers and an IP assumes these on behalf of all the company's creditors. Consequently, the IP will wish to deal with the assets of the company in as efficient a way as possible to achieve the best results possible in line with the EA 2002. One avenue for consideration is disposal of the company via a 'pre-pack'. A pre-packaged insolvency sale (pre-pack) is one which has been set up prior to any insolvency procedure begins and an IP is appointed. The sale will then take place on the agreed terms in very quick order. The procedure to be followed is, most often, administration. That such an arrangement could be concluded absent the prior approval of either court or creditors was confirmed in the *Transbus International*[391] case.

With formal insolvency comes the requirement to give public notice. This may not necessarily be kind to the company's reputation and may thus adversely affect the value of such a business. The 'pre-pack' is a method of dealing with this risk. IPs seek to gain an achieved price for the company which is in excess of that obtainable via other means, thus obtaining a better result for all creditors. This may particularly be so if a purchaser is around who is prepared for strategic or market-share reasons to pay more than the going rate for such a sale IF the reputational damage above has not been severe. However, in many instances, it will be difficult for the IP to adequately market-test for such a sale. Egregious failure in this respect may later render the IP open to challenge and the possibility does exist that the sale may be unravelled.

The decision to pre-pack is a question to be weighed thoughtfully. On the one hand, the benefits of a speedy sale make it difficult for third parties[392] to disrupt matters; make it much easier to maintain harmonious relations with key stakeholders;[393] and it obliges directors to desist from trading when insolvent and so reduces risks of personal liability of their breaching their duty to creditors. On the other hand, downsides do exist.

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[391] *Transbus International Ltd (in Liquidation), Re* [2004] EWHC 932 (Ch)

[392] Such as suppliers and landlords.

[393] eg key employees, customers and suppliers.

Unsecured creditors may feel left out because the speed of events leaves them unconsulted. The commonplace sale to connected parties may also exacerbate fears regarding Phoenixism.[394] Lastly, key contracts held by the insolvent company may be vulnerable to termination by 'insolvency event' clauses being precipitated.

Company Voluntary Arrangements:

For insolvent companies which have been previously profitable and which consider their trading difficulties may be only temporary, there is a 'solution' which offers a route to a quick and efficient restructuring known as a Company Voluntary Arrangement (CVA). This binding agreement addresses unsecured debt only and seeks to replace existing contractual terms with new ones which result in the repayment of some portion of the current debt over time from profits yet to be earned. The rationale to this is that existing creditors may prefer to support the CVA as a better outcome than would be achieved from the low dividends paid in liquidation ... and those creditors might also retain a valuable trading partner on into the future. CVAs are noted for their flexibility in construction and thus are easily adapted to most trading circumstances. However, some have noted[395] that the CA approach has only one class of creditor thereby increasing the chance that the different agendas of different types of creditors are not expressed in the ensuing CVA ... a circumstance which pertained in the insolvency of Leeds Utd in 2007.[396]

The proposed CVA can involve capital restructuring; alteration of the terms of debt; or the disposal of unencumbered assets ... in short, anything which can be agreed with creditors who, naturally, will follow their own separate agendas. The CVA proposal may

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[394] The practice of allowing a new company run by the old directors in the same field to arise having acquired cheap assets and hived off old liabilities.

[395] eg. Goode, R. (2011) *Principles of Corporate Insolvency Law*, 4th Ed. Sweet and Maxwell. 496

[396] See '*Leeds United: the unanswered questions'* in The Guardian of Friday 27 July 2007

be made by directors;[397] by Administrators;[398] or by Liquidators.[399] In practice, IPs are usually retained to draft the initial CVA proposal and to satisfy both directors and themselves that the proposal is realistic. The IP would then file the CVA with the court, communicate with creditors and, as nominee, convene meetings of both creditors and of shareholders. These meetings vote on whether to approve the proposal. If approved,[400] any further legal proceedings against the company are stayed ... unless there is default[401] on the terms of that CVA.

CVAs are attractive to directors of companies not yet in formal insolvency procedures as they remain in control[402] of their company. Significant benefits also accruing to the company include the potential to write off considerable amounts of debt; to quickly adjust costs by terminating onerous supply and employment contracts; and, perhaps, to relieve pressure from the tax authorities. Directors' conduct is also not a subject for investigation. The procedure is particularly effective when the company is unable to transfer critical contracts or certifications on to another company.[403] Up until recently, this was the only route to continued existence open to football clubs which had endured an insolvency event. Notably, the obligation to use this route came not from statute but from the private rules of football's authorities.

If the distressed company is small,[404] it may gain protection in the form of a moratorium of 28 days during which the CVA can be developed and implemented without the threat of proceedings from creditors. Thus, there is no enforcement of security nor appointment of office-holders during this moratorium period.

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[397] Where the company is not in administration or liquidation.

[398] IPs may seek the protection of the administration moratorium for a 'non-small company' while simultaneously proceeding with the CVA.

[399] Where the company is in winding-up and where the liquidator thinks that this would be more beneficial to creditors than liquidation of assets.

[400] The key requirement is to gain approval of 75% of the holders of the existing debt. Failure to achieve this will usually result in voluntary liquidation.

[401] In which case, any creditor may apply for a winding-up order.

[402] Note that the IP supervises the CVA but the directors still run the company.

[403] Thus making the "Phoenix" a less attractive option.

[404] Small companies are those with fewer than 50 employees; less than £6.5M turnover; or less than £3.26M in balance sheet assets.

The cost of a CVA is mainly in respect of IP fees[405] which derive from money otherwise payable to creditors ... and so the creditors need to agree this at the creditors' meeting. Under the terms of CVAs in general, the nominee will receive a single regular monthly amount which is the consolidated agreed payment by the company to its creditors. After deduction of nominee supervision fees, this money is then disbursed under the terms of the CVA to all unsecured creditors.

Perhaps the most significant advantage of this process in many cases is the absence of any requirement to publicise in the press; discreet and shadowy as is much action in The Casino.

Creditors' Schemes of Arrangement (Schemes):

Another tool which may be of use to a distressed company is the Creditors' Scheme of Arrangement (a Scheme). This is an agreement[406] to reschedule debt between the company and any class or classes of creditor and requires to be approved by court. It differs from other procedures relating to the alleviation of company distress by not being a formal insolvency procedure[407] and by not offering a moratorium[408] when used in standalone format. However, the Scheme can also be used in conjunction with formal insolvency if the protection of a moratorium is desired. At root, the Scheme is an arbitrary method for changing the financial structure (including debts) of a company, quite possibly against the wishes of some creditors and is normally used when a much needed reorganization cannot be achieved by other means. Court acceptance of such schemes can not be taken for granted as the *Prudential v PRG Powerhouse*[409]case

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[405] *Real Business Rescue* estimate (Aug 2015) that nominee (IP) fees will be in the region of £10k for formulating / presenting the CVA with a further agreed amount for supervision to be agreed with creditors.

[406] As provided for by the Companies Act 2006, Part 26 (ss.895-901)

[407] Such as administration or liquidation.

[408] As in administration or in Small-company CVAs.

[409] *Prudential Assurance Co Ltd v PRG Powerhouse Ltd* [2007] EWHC 1002

indicates. Here Etherton J. rejected a proposed scheme on the grounds of unfairness and illogicality.

Perhaps the main benefits of Schemes are twofold. The first lies in the ability of Schemes to provide an English law form of 'cram down'[410] whereby the rights of minority but dissentient creditors can be dis-applied if the prescribed class/classes majorities in favour of the proposed Scheme are achieved. This is potentially very useful for distressed borrowing companies who face large and diverse lending syndicates. The *Barclays v HHY Luxembourg*[411] case is helpful in dealing with such complexities. The second advantage results from the use of the Scheme to reorganise foreign debt in circumstances where local law is not able to deliver compromises of the required type. All that is required in this event is 'a sufficient connection' with UK jurisdiction ... no COMI[412] nor establishment in the UK is needed.

A Scheme may be initiated at the behest of the company[413] or any creditor by court application for permission for convening a meeting of creditors. This when the class or classes to whom the scheme proposal is to be put is/are identified. Any creditors not affected[414] by the proposed scheme are left out of these deliberations. If the requisite voting levels are met,[415] the court will then make the appropriate order establishing the Scheme. After receipt by the Companies Registrar, the Scheme becomes binding on all creditors in the classes involved in the proposals. The procedure is held to be expensive and, although versatile inasmuch as there are few limits to what may be included, awkward to set up and is likely only to be used when either of the main benefits mentioned above are significant and crucial. As we will see in the discussion to come,[416] Schemes are not without their uses in some high profile cases.

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[410] Well, closer to 'cram-down lite' in comparison with the US Chapter 11 device.

[411] *Barclays Bank Plc v HHY Luxembourg Sarl* [2010] EWCA Civ 1248

[412] COMI = centre of main interest; see later discussion.

[413] Or the administrator / liquidator of the company if it is formally insolvent .

[414] Because, say, their debts are not affected by the proposals.

[415] A simple majority in number of those voting in person or by proxy and a three-quarters majority in value needs to be obtained.

[416] Regarding Cross-Border Insolvency.

5.5 Awkward Cases.

Cross-Border Insolvency:

As international trade for UK companies continues to grow both in absolute and in percentage terms and a corresponding growth is also noted in foreign companies doing business in the UK, it becomes vital to consider how to efficiently and effectively deal with corporate insolvency in a cross-border context. International insolvency, therefore, considers the treatment of corporate debtors who have assets and/or creditors in multiple countries. The field is concerned with the three areas of choice of law; of jurisdiction; and of enforcement of judgement.

There are several bodies of theory[417] which are relevant here. Firstly, there is the *territorial* approach which does not accept external interference in domestic law; both debtor's assets and creditors within such a country are dealt with domestically. Secondly, the *universalist* approach purports to adopt a single regime whereby all debtor assets would be administered by a single office-holder regardless of the country in which these assets or the debtor's creditors were situated. Lastly, we note the possibility of some *hybrid* approach in which countries co-operate and facilitate proceedings in whichever is agreed to be the most relevant of the possible jurisdictions involved.

There are currently two sets of rules relating to international insolvency which are of interest to this study. These are the UNCITRAL Model Law on Cross-Border Insolvency and the EC Regulation on Insolvency Proceedings 2000 (hereafter ... the Regulation). The starting point for both sets of rules is the finding of the Centre of Main Interest (COMI) of the debtor company.

The COMI is not defined by the Regulation itself but its preamble indicates "'The *"centre of main interests" should correspond to the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties"*. Those companies whose COMIs are extra-EU are not covered by the

[417] See for example, Wessels 2008 (Wessels, B. "Cross-Border Insolvency Law in Europe; Present Status and Future Prospects " PER 2008 Vol 11 no1 pp 68-102)

Regulation. The determination of COMI has proven to a point fraught with contention as exemplified by the more than 20 different factors from decided cases[418]which have helped determine the location of a company's COMI! The controversial 2004 case of *Eurofood* [419](a Parmalat subsidiary) which caused such a furore in both Ireland and in Italy is indicative of the problems which can arise in this area .. and for fear *Eurofood* might be dismissed as a sample of one, other celebrated cases suchas *Daisytek*[420]and *Collins and Aikman*[421] might also be cited as exemplars here.

Neither is the term 'insolvency' defined in the Regulation (cf the two UK tests discussed earlier.[422] However, 'insolvency proceedings' are stated to be *"'collective insolvency proceedings which entail the partial or total divestment of a debtor and the appointment of a liquidator".* These proceedings can either be main proceedings or territorial proceedings. A potential cause of friction between jurisdictions is the omission of any mechanism for dealing with rival jurisdictional claims that their proceedings constitute main proceedings.

The Regulation is, at root, a conflict of laws measure which allows the EU member states to develop their particular approaches to corporate insolvency. Notwithstanding this freedom, it does clearly establish that one jurisdiction will be deemed to be primary and that any others will be secondary.
One would guess that EU interest in harmonizing laws exhibited in other areas falters in the domain of cross-border insolvency given the great difficulties in gaining agreement from individual states with widely divergent approaches to such matters as …

- ➢ the purpose of an insolvency regime; where this might be seen as a choice between rehabilitation/rescue vs liquidation/distribution

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[418] See Wessels op cit pp75/76

[419] *Re Eurofood IFSC Limited* (Irish company, part of the Parmalat group).

[420] *Re Daisytek-ISA Ltd* [2004] BPIR 30.

[421] *Re Collins & Aikman Europe SA* [2005] EWCH 1754 (Ch).

[422] eg As in Fn 57

- ➢ the operation of set-off; where on the one hand, there are jurisdictions where creditors and debtors have mutual debts, the creditor may set-off the claim in its entirety ... whilst on the other hand, some states oblige creditors to pay the debtor in full before then going to make their claim in proceedings
- ➢ the question of whether the commencement of insolvency proceedings automatically stay secured creditors from the exercise of their rights.

A revision of the Regulation was in place by 2017. This will address issues arising thus far and, as Marshall (2015)[423] states, "*help to promote an EU rescue culture* ".

An important change of emphasis will be the expansion of the existing automatic EU-wide recognition of insolvency proceedings whereby a main insolvency proceeding progressed in one member state gains automatic recognition throughout the EU. Currently, this catches only those proceedings in which an office holder has replaced management and thus liquidation is expected. The revisions open up the possibilities that pre-packs and / or other rescue mechanisms may be fall within the regulation ... and also that existing management may, in some instances, become debtors-in-possession.

The new Regulation carries an appendix to clarify the type of proceedings within its scope: evidently the UK does not list 'schemes of arrangement' in this appendix. Schemes are held to be a useful tool in restructuring distressed companies whether they be of UK or non-UK origin. In the latter instance, UK courts will be satisfied by finding a 'sufficient connection' in order to approve such a scheme. Key here is the absence of a requirement that the debtor company has a UK COMI, as would have been necessary if schemes were entered in the appendix.

The Regulation only applies to companies having their COMI in an EU state; and main insolvency proceedings must be opened in the state in which the COMI is located. There exists a rebuttable presumption that the COMI is situated where the Registered Office is to be found. This has enabled companies to move their COMI to a different

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[423] Marshall, J. "*Plus ca Change* " *Recovery* Spring 2015 p8

country where different insolvency arrangements apply; sometimes known as '*forum shopping* '. The UK has perhaps a more developed and flexible insolvency regime than some other EU member states and shifting COMIs to the UK has resulted in several successful restructurings according to R3.[424] This has saved companies from going under, preserved jobs and delivered added values for creditors ... but has still attracted adverse comment from elsewhere in Europe as the lurid, yet memorable tag of the UK being the '*Insolvency Brothel of Europe*' suggests. Amendments to the Regulation will not affect the better outcomes generated by COMI shifts but instead aim to offer more transparency in order to combat 'abusive forum shopping'.

Dealing with group insolvencies in Europe has not always been easy under the Regulation (see *Parmalat* above). Accordingly, attention has been given to this area in the Regulation's revisions; the Commission at first suggesting a flexible, light touch approach to enable better co-ordination of such insolvencies but the European Parliament was more interested in a mandatory framework for co-ordination. Almost inevitably, the solution was a compromise arrangement which will establish a voluntary set-up for co-ordination. This considers appointing a group co-ordinator who may propose a restructuring plan for the distressed group. Individual group companies are able to opt-out of this plan if deemed not in the interests of their particular creditors. Likewise, office holders of participating group companies need only 'consider' recommendations from the group co-ordinator as these recommendations do not bind.

Briefly turning to the UNCITRAL Model Law on Cross-Border Insolvency .. adopted by the United Nations Commission on International Trade Law in 1997. This is an attempt to help states develop a modern framework for dealing with cross-border insolvency proceedings. It makes no attempt to harmonize or unify; instead, it attempts to help build co-operation and co-ordination in the dealings which states have between themselves in relation to corporate insolvency. The Model Law has been a basis for legislation in more than twenty countries such as the UK, the US and Japan. Neither the main EU countries nor the BRICs have, as yet, made moves in this direction. Two aspects of the Model Law are worth highlighting here. Firstly, there is a procedure for a

[424] See R3 website ... https://www.r3.org.uk ... accessed 24 June 2018.

‘foreign representative’ (the representative of a debtor in a foreign proceeding) to have that proceeding recognized and for relief from the domestic court in respect of that proceeding. This can lead to the representative gaining the power to control the disposition of assets located in the domestic location, provided that sufficient safeguards are in place for local creditor protection. This can be also be used co-ordinate sales of debtor’s assets in more than one foreign country. The second aspect of note is the requirement that courts within enacting countries should ‘co-operate to the maximum extent possible’ with foreign courts and office-holders.

The increasing practice of English elite football clubs having part or full ownership of clubs in other European countries makes the above commentary potentially relevant in the future but, as yet, no actions have developed from that source. However, there is also the practice, said only to be nascent, of player-registrations being part-owned by clubs and part-owned by third parties. These third parties are said to non-UK entities and in the West Ham case[425] were thought to be of South American background. How these interests might dealt with in a football club insolvency is not yet known.

Employees in Insolvent Companies:

The rights of employees of a company which is financially distressed emanate from two sources ... employment law and corporate insolvency law. These sources sometimes do not engage too efficiently and the position for individual employees is often complex and thus an additional source of stress for an already vulnerable stakeholder. What follows is the broadest of overviews only.

One way to clarify matters is to start by considering the type of insolvency procedure which pertains to the employee’s company. If the company is in Liquidation, the company closes and the job ends. This, at least, has the virtue of clarity. However, if the company is in administration, then things become less clear-cut.

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[425] *Sheffield United Football Club Limited v West Ham United Football Club Plc* [2008] EWHC 2855 (Comm) aka The Carlos Tevez case

Employees' rights appear under a variety of headings, many of which are hedged around with service period and earnings cap restrictions,[426] some of which are reviewed annually. Those rights generally accruing from Corporate Insolvency legislation bestow preferential creditor status whereas those coming from Employment legislation generally only offer ordinary unsecured status. Dividends payable in the latter case are unlikely to be high. The bundle of rights due to include that they should be paid for work they have done (outstanding wages), receive any accrued Holiday Pay owing; and have their outstanding pension contributions paid. In addition, the usual Employment Protection rights in respect of Statutory Notice; Unfair Dismissal; and Protective Awards may well be place for qualifying employees.

Thus, at first sight, the employee who loses a position due to his company going into Liquidation seems to be somewhat well placed, especially by comparison with other involuntary creditors. However, as indicated above, in Liquidations there is often little left for ordinary creditors and not necessarily too much, either, for preferential creditors. The nature of the cap results in those who have high skill or a managerial position finding only limited protection. The ability of employees to directly apply to the Redundancy Payments Office[427] (RPO) for relatively quick payment of certain monies due albeit on a capped basis is useful. The excess over the cap may be claimed from the company as part of the Liquidation and the NIF then subrogates against the insolvent company for these payments. Employees will be expected to attempt to mitigate their loss in these circumstances by, for instance, claiming such state benefits as they are entitled; additionally, there may well be income tax implications with regard to certain payments.

In the instance of a sale of the distressed company as part of an administration, employees may be transferred to a new business. Here there are protections for such employees under the TUPE regulations.[428]

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[426] eg Unfair Dismissal provisions under the Employment Rights Act 1996 (s184 and elsewhere)

[427] Which deals with claims on behalf of the National Insurance Fund (NIF)

[428] Transfer of Undertaking (Protection from Employment).

We now look briefly at the impact of the Acquired Rights Directive on employees of troubled firms. Specifically, the focus is on situations where all or part of the company is being sold by the office-holder. In such circumstances an employee will either be transferred ... or not. If not, the provisions of employment protection in respect of wrongful dismissal are relevant.[429] It is the position of the transferred employee that we will discuss here.

There is an enduring tension between the purpose of the Acquired Rights Directive[430] which attempts to provide protection for a transferred employee from loss of service and other rights built up over time and the understandable enthusiasm of the purchaser (transferee) of the whole or part of the company to acquire the services of such services at least cost. It should be noted that the cost here is rather more than the existing terms and condition of service of the employee concerned; it also includes transferred liabilities which may be considerable.[431]

Attempts have been made to lessen the burden of transferred cost to the transferee with the aim of improving rescue prospects. Normally, a transferee will normally assume responsibility for all matters under or connected with the employees' contracts but a limited exception is made in relevant insolvency proceedings (see below) so that certain sums outstanding at the date of a relevant transfer [432] will be met from the National Insurance Fund (NIF), rather than by the purchaser. Timing is key here; the NIF will only pay out if proceedings have been 'opened', if not then the purchaser will be held liable for all debts to employees.

Regrettably, the law is less than lucid in this area and decisions taken by IPs and other parties cannot always be precisely calculated. For instance, a distinction has to be made as to which one of two insolvency routes is being followed. If the process is part of a liquidation then employees may be dismissed without liability for Unfair Dismissal

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[429] These claims are unsecured debt (not preferential) and stand little chance of being paid.

[430] Enabled in the UK via TUPE (1981) and then amended by TUPE (2006)

[431] Such as Protective Awards (see below). Transferors/IPs must now give accurate information on these matters prior to transfer (no easy matter!)

[432] DBERR does not deem compulsory liquidation, or creditors' voluntary liquidation as relevant.

accruing.[433] Alternatively, if the process is part of a rescue-oriented sale, then employees gain protection. In the latter instance, dismissal may not necessarily be unfair if for an ETO [434] reason.

IPs are allowed to consider varying employees' contract in an effort make a purchase more attractive; however, any such variations do need to be agreed with all parties including employee representatives.[435] If employees' claims are taken to an employment tribunal, an IP will endure careful scrutiny of their actions in order to establish the "Real Reason" for employee dismissal with the fair/unfair argument being in focus. There are also requirements for the office-holder to consult collectively;[436] failure so to do attracts substantial potential liability.[437] IPs will also find it difficult to plead that insolvency as such is a "special circumstance" making consultation impractical. This is clearly an area of concern ... with the difficulties in interpretation of the law and the calculation of risk to IPs, potential purchasers and, above all, to the employees involved.

One might wonder why the above section is necessary when this thesis is exploring insolvency in football … and football creditors have a form of preferential status? Beyond the trite observation that there is no future guarantee that football clubs will continue to avoid insolvency as they have in the past lies a structural point relating to the way companies organise themselves. Many elite clubs structure themselves into divisions with the footballing operation being only part, albeit a very significant one, of the overall company. These other divisions might exploit merchandising, hospitality and other non-football sporting activities. It is submitted that employees in these divisions would be unlikely to fall under the heading of 'football creditors'. However, if the

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[433] Perhaps the key case here is *Oakland v Wellswood* (a pre-pack case) where the IP concerned admitted that his purpose had not been the rescue of the firm but the maximisation of creditor return

[434] Economic, Technical or Organizational reason ; this has not always been easy to justify in court .. see Frisby "*TUPE or not TUPE?"* (2000) 3 CFILR 259

[435] These will be trade unions representatives if a union(s) are recognized. Matters will necessarily be more problematic if not. The *Information and Consultation of Employees Regulations 2004* may conceivably be of use in such situations.

[436] 20 or more employees at the one establishment over 90days ; key case here is *Woolworths*.

[437] Can be a Protective Award ... up to 90 days UNCAPPED pay per employee affected.

football club failed, these employees might be caught up with events in the way any conventional employee would be.

Chapter 6 : The Football Creditors Rule

6.1 Introduction

The frequent insolvency events[438] in English football clubs have prompted many to call for changes in insolvency legislation. In particular, what has come to be known as the Football Creditors Rule (FCR) has aroused widespread dissatisfaction. This rule has been held to be a highly significant factor in the way in which clubs have mismanaged their finances and thus resulted in insolvency. A major case in the High Court was brought by HMRC[439] in which a declaration was sought that the FCR contravened key tenets of insolvency law – in particular, that FCR offended both the *pari passu* rule and the anti-deprivation principle.

As an indicator of political concern, a report[440] in 2013 by a House of Commons Select Committee indicated their disquiet with the failure of the footballing authorities to deal with the perceived financial ineptitude of professional football clubs and referred to the then recent insolvency case of Glasgow Rangers in 2012 as being " *a powerful example of the excesses of professional clubs competing with one another, and the consequences for their community when mismanagement leads to financial collapse*".

This committee saw the FCR as being immoral and as being simultaneously a symptom and the cause of financial mismanagement. They called for government action to improve governance in football and to overturn the FCR. Indeed, the then Sports Minister stated [441] "*Football is the worst governed sport in this country, without a shadow of doubt*",

[438] Which, of course, need not ultimately lead to the winding up of the club concerned.

[439] *HMRC v The Football League and FA/Premier League* [2012] EWHC 1372 (Ch)

[440] House of Commons Department of Culture, Media and Sport select committee "DCMSSC"

[441] Hugh Robertson, 10 Jan 2011 HoC

In brief, the FCR[442] states that if a club becomes insolvent, then payment must be made firstly and fully to that club's football creditors else that club will be expelled from the Football League (FL). A highly similar provision applies to clubs participating in the English Premier League (EPL) and in the four Scottish Football Leagues. The consequence of this regulation is that players and other clubs get paid in full qua secured creditors ... and other creditors get very little indeed. An oft-quoted example of the imbalance in settlements is the administration of Crystal Palace in 2010 in which football creditors got paid in full (circa £2m) and other creditors (including HMRC) were paid 2p in the £.

6.2 The Football League's Employment of the FCR

All the clubs within the FL[443] have one share; often called the *Golden Share.* On entry to the FL via promotion or exit via demotion, share transfer takes place between the in and out clubs. This Golden Share turns out to be hugely significant in what follows. The FL is a limited liability entity and the individual clubs are its members; governance is via the FL's Articles of Association and by its Regulations. The FL has adopted a clear, written Insolvency Policy which clarifies its position vis-à-vis the insolvency of a member club.

One income stream to football clubs derives from contracts from the televising of football matches. This can be a considerable fraction of total revenue for many teams. The negotiation of television deals and other media rights is done on behalf of clubs by the FL[444] and each club receives it's share from the "*Pool Account*". The right of a club to gain access to its monies is dependent on that club following the rules of the FL mentioned above.

The eventual decision in the HMRC 's case against the FL paid particular attention to five parts of the FL's constitution. These are briefly addressed below ..

[442] Technically, the FCR only applies to clubs in the three Football League divisions but the associated arguments are broadly the same both for Premier League and for Scottish clubs.

[443] At time of writing (July 2018), there were 72 members of the FL

[444] Again, the arrangements are similar for other UK football clubs in the PL and in Scotland.

1. Art.4.7.4 ... which compels a "*club subject to an insolvency* [445]*event*" to transfer its Golden Share.
2. Art. 4.8 ... which permits the FL to waive Art. 4.7.4 in the event of Football Creditors[446] being fully paid.
3. Art. 77.3 ... which indicates that the payment of monies from the Pool Account is conditional on the club in question fulfilling all its fixtures. Although interim payments ARE made these are stipulated to be completely returnable in the event of fixture default.
4. Art 80.2 ... which requires that in the event of a club failing to pay a football creditor as per Art.4.7.4 the any residual amounts due to that club from the Pool Account will be forfeited to those unsatisfied football creditors.
5. Reg. 61 ... which states that if a club leaves the FL as a result of a share transfer under Art. 4.7.4, then the registrations of footballers contracted to that club will be cancelled and then ownership of their contracts will fall to the FL; thus likely depriving the distressed club of its most important assets.

The consequence of the above is a straightforward choice for a financially distressed club ... it either pays up to its footballing creditors or it self-destructs as a commercial being. In either instance, non-football creditors lose out ... and in the instance of HMRC, that loss can be dramatic. As Serby[447] puts it ... the impact of the FCR is to create "*a false market within the world of football; a reason for the spiralling wages of footballers ... which encourages clubs to overreach themselves and ... many*[448] *become insolvent"*.

6.3 The HMCR's position in respect of the FCR

That the HMRC should end up as being a substantial non-football creditor follows from two different aspects of the professional football system. Firstly, professional footballers at the level of FL teams are almost exclusively on fixed term contracts (often of several

[445] See later for a list of these insolvency events.

[446] Defined as being the FA, employees of that club and other clubs in the English professional football system Interestingly, the position of non-UK football creditors is obscure ... but see later.

[447] Serby, T. British Football Clubs: 'Regulatory Reform Inevitable ?' *Int Sports Law J* (2014) 14: 12

[448] From 2002 -2012, 36 clubs in the FL became insolvent.

years duration). The NIC / PAYE sums due on these contracts are due in arrears ... offering an opportunity for a financially distressed club to accrue significant debt. Secondly, the amendments to the Insolvency Act 1986 brought in by the Enterprise Act of 2003, abolished the HMRC's[449] preferential creditor position; it now has to take its chances with other unsecured creditors in any distribution of an insolvent's estate. Consequently, HMRC was eager to remedy the situation which seemingly resulted in an endless loss of funds[450] to the public purse; hence, its[451] 2012 challenge to the FCR.

The High Court Hearing:

The HMRC pleadings labelled the practice by the FL of paying interim monthly amounts to clubs with the proviso that such payments did not belong to the recipient club till fixture-list completion see Art.77 above) as a sham intended to avoid the basic insolvency principle of *pari-passu* which intends that all creditors receive equal treatment. They argued further that Art. 4.7.4 (see above) was effectively a deprivation in that the Golden Share was removed from the club at the commencement of insolvency. The HMRC thus reasoned that such practices be held to be "*void and unenforceable as a matter of public policy*".[452]

Unsurprisingly, the FL offered a detailed response which may be read in five parts ...

a. Clubs need to be prevented from acquiring advantage unfairly by purchasing (new and better ?) players and then not paying the selling club in full.
b. The whole point of competition in a league structure depends crucially on total fixture completion; all clubs NEED to play each other in order to make the competition credible.
c. The risk of domino-defaultation whereby a default in debt by one club leads consequentially to a series of defaults in other clubs has to be minimised.

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[449] Or at least its predecessor bodies.

[450] Serby (op cit) suggests that in the period 2000-2008, some £30 million was lost in unpaid tax from professional football clubs !

[451] The Premier League also became involved in this case.

[452] *HMRC v The Football League and FA/Premier League* [2012] EWHC 1372 (Ch)

d. The payment of interim monies from the Pool Account did NOT change the position of distressed clubs having no legal right to such monies until complete fixture fulfilment (see Art.77) and the payment of football creditors under Art. 80 was perfectly reasonable as the monies in the Pool Account only become property of the club on finishing the fixtures.
e. Finally, the FL pointed to the unreasonableness of asking other clubs to entertain as a fellow member of the League a club still owing funds to one or more of their community. The Stock Exchange case involving MMI Stockbrokers[453] was quoted as precedent for the suggestion that the obligation to transfer the Golden Share was NOT a breach of the anti-deprivation principle.

In the event, the Court judgement did not give HMRC the declaration which it looked for the FCR was not unlawful nor did it break the fundamentals of Insolvency Law.

Having said this, the Court[454] felt able to deliver judgement in such strong terms as to make one wonder why there has been no action some six years later. Some of the more emphatic comments are paraphrased below ...

- ➢ The court accepted that a substantial moral case against the FCR had been made out
- ➢ The court concurred that risky decisions in respect of trading valuable players are stimulated by the knowledge that payment will be forthcoming to the footballing party despite non-payment to 'normal' creditors.
- ➢ The court conceded that the requirement to complete all fixtures before entitlement to money from the Pool Account was a lawful contract term. This opens up discussion of '*The Sporting Exception* ' which is dealt with in more depth later.
- ➢ The court commented that the judgement in this occasion had been made on an abstract basis (on a 'paradigm case ') rather than on one with a factual basis ...

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[453] Money Markets International Stockbrokers Ltd v London Stock Exchange Ltd. [2002] 1 WLR 1150

[454] In the form of Richards, J.

this was felt by Roberts[455] to leave the way clear for a further future challenge based on a particular insolvency. It has to be noted that this has not yet happened despite a specific industry targeted amendment[456] to the 1986 Insolvency Act being passed in respect of utility providers having to continue supplies even if existing debt has not been satisfied.

The court's comments merely extend the puzzle that the study of football insolvency has become. The question of the FCR being a symptom of prevailing financial recklessness or a cause thereof will be further investigated in the next section which looks at 'Financial Fair Play' in the context of (major) football clubs.

Subsequent Events

Accountancy Age reported in 2015[457] that the Football League[458] had amended its regulations in respect of the Football Creditors' Rule from season 2015-16 onwards. For our purposes, the principal change was a new stipulation that in order to exit administration and retain membership of the Football League, the new owners of a financially distressed club would have to pay its unsecured creditors at least 25p in the pound on gaining control.[459] This, however, stands alongside the existing requirement to pay all football creditors in full. Sanctions for failure to comply with these new rules revolve around an increased deduction[460] of League points which will almost automatically result in relegation for the club concerned.

Responding to widespread criticism (from R3 and others), the Football League also instituted a new requirement in that the ailing club be marketed by the IP/Administrator

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[455] Roberts D (2012) HMRC and the Football creditors Rule-An own goal? Olswang

[456] Amendment of s233 Insolvency Act 1986 after *Wellworth Cash & Carry (North Shields) Ltd. v Northeastern Electricity Board* [1986] BCC 99, 265

[457] Richard Crump in *Accountancy Age*, 9 June 2015.

[458] But not the Premier League.

[459] Or 35p in the pound if 'paid up' over three years.

[460] A 12 point deduction in some circumstance and a 15 point deduction in others.

for at least three weeks. During this period, any bid from the appropriate Supporters' Trust should be considered.[461] An additional and highly significant change was the removal of the obligation for the insolvent club to exit administration via a CVA: the League would now be happy to transfer the crucial club share in the League to the Administrator's preferred bidder, providing that all the other appropriate League regulations were fully complied with. It was hoped that these changes would reduce (professional) costs, deliver greater returns to creditors and limit the previous owners' ability to control what happened in a CVA.

The Accountancy Age article also reported, without comment, the somewhat triumphalist remarks made by the Football League's CEO as …
'The League has now gone two full seasons without a club suffering an insolvency event which is an encouraging sign. The use of Financial Fair Play regulations in all three divisions, the requirement for new owners to demonstrate the source and sufficiency of their funding and the ongoing monitoring of club's tax affairs have helped us bring more stability to club finances.'

The omission of any justification for continuing to treat unsecured creditors who likely will get 25% of their debt repaid as third-class citizens as compared with their football counterparts who will get 100% of their debt repaid could be seen by some as being self-serving (or worse). Others might argue that it a step in the right direction and rather better than nothing.

[461] Echoing the 'In Football we Trust' point made at Fn 95 above?

Chapter 7: Pan-European Developments in the Football Field.

7.1 <u>The Financial Fair Play Rules</u>:

The original UEFA FPP rules are outlined here; they also serve as a model for the subsequent English adoption and for ensuing amendments. The key concept is that of 'break-even'.[462] This seen as being *relevant*[463] income less *relevant* expenditure. Here, income is the sum of gate money, broadcasting money, advertising and sponsorship, and any profit from player sales. Interestingly, there seems no mention of prize-money nor of items such as the notion of 'parachute payments' for relegated clubs. Conversely, expenditure is stated to include the expected 'cost of sales' category but also include the writing down of transfer fees for incoming players and the wages paid to all footballing-related staff. Despite being largely discretionary, finance costs and dividends are said to be relevant expenditure. Significantly, expenditure on stadia building are not included in the break-even calculation; nor, indeed, is expenditure on youth development or on women's football. Presumably, these latter elements may serve an apparent Public Interest purpose?

Departures from break-even as losses are permitted only to a stated limit over a stated period[464] but losses to a maximum[465] are allowable subject to the injection of owner funds to cover the loss … clearly, owning elite clubs is for those with deep pockets and possessed of stout heart! In an attempt to control upwardly spiralling player/coach wage costs, these are restricted unless the club concerned can show commensurate revenue increase. This last point conceivably links to the one made earlier about the favourable expense treatment of building larger capacity stadia. In addition to the break-even stipulation, UEFA also instituted a 'Payables' rule which stopped clubs having 'overdue' creditors ... which links strongly to the corporate insolvency context in English law as discussed in this thesis.

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[462] Not defined in precise accounting terms as per the International Accounting Standards Board.

[463] Author's emphasis.

[464] Currently, a total loss of £15M over three years is permitted in the Premier League (PL) in England.

[465] Currently, £105M in the PL.

It is quite likely that under-performance on the football pitch results in reduced revenues from gate-money and from performance payments. Continuing under-performance may well lead to relegation and further lost income. In such conditions, there must be a temptation to attempt to 'buy success' by acquiring better players who, in turn, demand higher wages. Thus, the goal of cost reduction may be undermined by the pursuit a strategy of short-term survival.

To deal with this, the FL has, over time, brought in regulations focused on limiting over-spending. One such rule is the requirement for PAYE reporting called 'HMRC Reporting' which places restrictions on player purchase on those clubs who fail to keep their PAYE situation up to date. An additional development has been the institution of a '*fit and proper person*' hurdle to be jumped by anyone seeking to purchase a football club ... a development which rarely fails to amuse sporting journalists obliged to comment on the football scene who then delightedly point to the insalubrious backgrounds of many recent, would-be purchasers. The footnote[466] below provides a topical and colourful example !

But even more activity in this regard has come from outside the UK ... especially from Europe. At roughly the same time as HMRC was bring its High Court case against the FL, the European football authority, UEFA, brought in clear boundaries as to the amount of loss permissible to individual football clubs in any given season.[467] The FL followed UEFA's lead in 2012 and established its clone, also called by a similar name to that of UEFA, viz Financial Fair Play Rules (FFP). The required boundary to losses in the FL version was a mere £8 million per club per season from 2013-14 onwards.

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[466] The Guardian of 18 May 2017 (Ed Aarons) reported that Mr Evangelos Marinakis, a Greek shipping magnate had purchased 100% of the shares of Nottingham Forest FC for £50M. To do this, Marinakis had passed the Football League's 'Owners' and Directors' Test (formerly The Fit and Proper Person's Test). Marinakis also owns Athens' premier club, Olympiacos, and lurid photos of him entering the pitch packing a hand gun after a disputed match decision in 2016-7 Greek football season circulated widely in the media. At the time of this purchase Marinakis was being investigated by UEFA for match-fixing. These matters, seemingly, had no bearing on the English Football Authority's decision. Nottingham Forest were reported in The Guardian of 29 August 2018 as having spent more than £30M on transfer fees over the summer of 2018. There is no information on the source of Mr Marinakis's funding.

[467] No more than 45 million Euros per season per club in 2011-12 and 2012-13 seasons !!

Failure to adhere to these figures invited punishment via a transfer embargo on player sales or a fine if the loss ensued from player purchase which gained promotion to the Premier League. Given the financial bonanza consequent on any such promotion, such threats might appear inconsequential in the circumstances. Some commentators[468] opined that the FL should get ready to justify these rules as a result of player contestation of the effects of the rule on their earnings. However, the UK Minister for Sport [469] seemed pleased ...

"The implementation of FFP should gradually lead to clubs reducing their spending, and as a result, see fewer incidents of club insolvencies. I hope that the FFP, should, in turn, negate the need for football to rely on the Football Creditors Rule in cases of club insolvencies."

Sanctions levied on clubs vary from competition to competition and sporting regulator to sporting regulator but all include financial penalties, mainly substantial fines, and sporting penalties such as exclusion from the tournament, loss of points or demotion. Thus the sanctions seem severe ... but, in reality, evidence of preparedness to use these sanctions, this far, seems slender.

Gallagher and Quinn (2017)[470] submit that although the FFP regulations have an ultimate and intended goal of nudging clubs to avoid financial distress, this economic aim with an emphasis on finance has an unintended consequence of diminishing sporting achievement. This inevitably will downgrade overall quality within the competitions to which FPP applies and raises the spectre of a further unintended consequence in that the on-going viability of professional soccer competition may not be taken for granted. Arguably the results in this instance may be likely to make the original situation worse rather than to improve it; a perverse outcome. Whether the cause of these unintended consequences can be attributed to difficulties in modelling the interactions between system actors or merely the not-unusual tendency of regulators to attend more to immediate rather than to longer term interests is not entirely clear … quite possibly, both play some part here.

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[468] eg David Conn in The Guardian of 26/02/14

[469] Hugh Robertson, 2013 30/04/2013 cited in Serby op.cit.

[470] Gallagher. R, and Quinn, B. (2017)'*Regulatory Own Goals'* ,unpublished.

The same authors also have concerns that the implementation of FPP rules merely serve to perpetuate the dominance of pre-existing soccer elite clubs.[471] Thus, the perspective of regulation from a Private Interest standpoint seems perfectly well justified here. This mechanism gives this elite group of clubs the ability to extract more than their fair share of monies available to teams engaged in competitions to which FPP meaningfully applies.

7.2 The Sporting Interest in Law

The European Dimension:

The theme of paradox explored elsewhere in this thesis becomes apparent again when consideration is given to an increasingly unusual acceptance of law-breaking in the context of sport in general and English professional football in particular.

It might be asserted that Football breaks the both English and European law without compunction and does so continuingly. For instance ... although domiciled in England for most of my adult life, I cannot represent England as I am Scottish[472]**.** If I did pay football at the level discussed in this thesis, I would be unable to move to another employer when I so chose [473]... and quite probably I would have to reveal my whereabouts to the authorities at all times should they institute a random drug-testing regime.[474] Thus, my protection against discrimination on the basis of nationality would be flouted; my rights as to freedom of employment would be ignored; and my entitlement to privacy would be disregarded. Add to these 'aberrations', the practice of football authorities selling media rights on a collective basis, ostensibly so that all participating clubs will share the commercial benefits; many would see this as a cartel ... banned under both English and European anti-trust/fair competition legislation.

The reasons for the evident litany of law-breaking lie with the suggestion that because sport is not a 'normal' area of business, it is not just acceptable but prudent for such

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[471] One can easily reel off the names here ... Real Madrid, Barcelona. PSG, Bayern, Milan, Juventus, Manchester City, Manchester United, Chelsea ... and so on. That the average ten-year old would have little difficulty with this list merely underlines the point being made.

[472] See the Deliege case : Case C-51/96 and C-191/97, *Deliège* [2000] ECR I – 2549

[473] See the Wouters case : Case C-309/99, *Wouters* [2002] ECR I-1577

[474] See the Meca-Medina case in what follows.

apparently illegal practices to be permitted. Thus, the notion of 'sporting specificity'[475] has entered the legal lexicon from EU law sources as an indicator of the special and specific nature of sporting activity. In short, Football (and other sport) is to be treated, at times, in ways quite different to usual business practice. Sadly, the term *'specificity of sport'* enjoys a life of ambiguity which the evolution of the law over the last sixty years or so has merely made worse. As an aid to understanding, this phrase may have little more than '*label value*' to commend it ... as will be shown below.

The Evolution of 'The Specificity of Sport' in Europe:

The position of the European Court of Justice (ECJ) for many years after the Treaty of Rome[476] of 1957 was reasonably clear; its rules were of no standing in relation to bodies which regulated sport on the grounds that EU laws were designed for economic life and thus did not apply in sporting contexts.

Perhaps the genesis of the sporting interest is to be found in the Walrave case of 1974[477] in which the ECJ stated that '*the practice of sport is subject to Community law only insofar as it constitutes an economic activity within Art 2 of the Treaty*.'[478] Hence the Court seemed to be signalling that sport may have different characteristics which set it apart from the norm and which merited different treatment from that norm ... a special case, so to speak. Such an idea, of course, was always likely to be positively received in sporting governance circles such as the football authorities as it seemed to offer the prospect of increased self-regulation and freedom to establish their own rules and to follow their own traditions. Whilst the Court placed heavy emphasis on the detailed knowledge and experience possessed by sporting authorities, it was not clear as to why Sport was singled out as requiring this extraordinary degree of autonomy.

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[475] Often referred to as '*the sporting interest'*

[476] The Treaty on the Functioning of the European Union (TFEU) 1957 and subsequent consolidations .. aka The Treaty of Rome.

[477] Walrave and Koch Case 36/74) [1974] ECR 1405

[478] Treaty on the Functioning of the European Union (1957)

Other commentators[479] have suggested that the ECJ's judgement took into account matters such as ...

- ➢ The development of young and emerging talent in terms of recruitment and training.
- ➢ The requirement for league competitions to be credibly balanced and unpredictable.
- ➢ The mutual dependence of competitors in ensuring that league programmes get completed.

All of the above connect back to the central exploration of this thesis. The first nudges[480] rich clubs away from constantly buying high-priced experienced talented players whose wages might ultimately contribute to financial distress. The second echoes the first and answers a need to maintain audience /crowd interest in the various competitions, without which the vital media funding would be lost ... again jeopardising the financial stability of the participant teams. The final point is arguably even more significant in the context of the Football Creditors Rule alluded to above[481] in that it emphasises the crucial requirement for seasonal fixture lists to be completed in their entirety. This point was made much of in the Football Authorities' arguments, albeit without direct reference to European jurisprudence in relation to the *Sporting Specificity*.

Legislative evolution

Following the *Bosman* case[482] in 1995, there followed a period of development both of legislative interest in the field of sport and of judicial action in attempting to clarify an increasingly complex field. It was felt by some that the absence of any mention of sport in the founding treaty made matters difficult to deal with in a predictable way. Thus,

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[479] Infantino, G. (2006). '*Meca-Medina: a step backwards for the European Sports Model and the Specificity of Sport?*' UEFA Report.

[480] In a way reminiscent of Sunstein and Thaler (see Fn 174).

[481] See discussion re FCR in Chapter 6.

[482] Union Royale Belge des Sociétés de Football Association ASBL v Jean-Marc Bosman (1995) C-415/93.

over time, action was taken in the form of a non-binding annexe[483] to the Amsterdam Treaty in 1997 and the Helsinki Report on Sport of 1999 recommended a 'new approach framework'[484] for the application of EU rules to sport. The Nice Declaration of 2000 saw the first official usage of the '*specificity of sport'* phrase. This seemed to acknowledge the claims of sporting bodies to operate autonomously[485] and was followed by the EU's 2007 White Paper on Sport.[486] This latter document distinguished the *'specificity of sporting activities and rules'* from '*the specificity of sport structure'* ... both ideas relevant to the discussion here. The list of suggested and actual amendments to EU law in this context culminates with the Lisbon Treaty of late 2007[487] which made a substantial attempt to remove the confusions built up over the prior years. This appears endorse the specific nature of sport ... and hence, admittedly at long distance, lend some support for the stance of English footballing authorities in respect of their insolvency policy.

Judicial evolution

The efforts of judicial action during this period as applied to issues relating to football in particular and sport in general also merit some mention here. The case of *Bosman*[488] is often perceived to be the catalyst for subsequent cases. Bosman argued that the then prevailing transfer system placed unreasonable restrictions on a football player's ability to change employers.[489] Whilst the verdict went for Bosman, the court indicated that it was prepared to accept that sporting bodies did have a legitimate right to have rules on

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[483] Which called on the various EU entities to heed the representations of sporting authorities in the context of sporting issues.

[484] Which aimed to maintain sport's traditional values and customs in the face of legal and economic change.

[485] Albeit with provisions as transparency and democracy.

[486] Which examined the themes of the White Paper on the societal role of sport, the economic dimension of sport, and the organisation of sport, and provided an overview of the follow-up actions planned by the Commission.

[487] Which, inter alia, recognises the rights, freedoms and principles set out in the Charter of Fundamental Rights of the European Union of 7 December 2000

[488] Union Royale Belge des Sociétés de Football Association ASBL v Jean-Marc Bosman (1995) EU:C-415/93

[489] And in direct conflict with Article 45 TFEU

restriction of movement as long as these were '*proportionate*,'**[490]** regrettably the court felt no need to clarify the term! A further significant case was that of *Lehtonen*[491] in 2001which also looked at issues of transfer periods as well as restrictions on alternative employment. Here the court stated that …

"a transfer period is characteristic of organized competitive sports and is 'inherent' to the sports organization and thereby, in principle, immune from competition law"

and that transfer deadlines were acceptable as they …

"*ensured the regularity of sporting competitions*"

and so they can be justified on …

"*non-economic grounds concerning only sport as such"*.

Thus, it emerged that the ECJ was comfortable with the notion of the sporting exception if the sports authorities in question developed regulations which were '*justifiable, functional, necessary and proportional* '. Perhaps the final landmark case to be mentioned here is that of *Meca-Medina*,[492] which involved a doping issue. The detail is not in focus here but the judgement is: viz …
"the mere fact that a rule is purely sporting in nature does not have the effect of removing from the scope of the Treaty".

Prior to this case, any sporting specific regulation carrying an economic connection was deemed to be outwith the scope of EU law in the economic and competition areas solely because it was related to sport. The judgement appears to call this into question and, since issues in this area are decided on a case by case basis, this ruling seems to add to

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[490] Although it was conceded that, in the case of Bosman, they were NOT proportionate.

[491] Jyri Lehtonen and Castors Canada Dry Namur-Braine ASBL v Fédération royale belge des sociétés de basket-ball ASBL (FRBSB) EU:C:2000:201

[492] David Meca-Medina and Igor Majcen v Commission of the European Communities EU:C:2006:492

complexity rather than reduce it. It should be noted, however, that if the sporting authorities were able to show that their regulations met the legitimacy and proportionacy requirements referred to above then the *Meca-Medina* ruling might have little effect. Nevertheless, the current situation remains opaque.

Chapter 8 : Concluding Discussion
A Summary, Analysis and Some Conclusions.

One of the key features of modern law is the furnishing of an architecture within which acceptable behaviour is displayed; running a professional football club should be no more exempt from that feature than other businesses. Yet it has been demonstrated in this dissertation that this is not the case. The thought thus occurs that unenforced or unenforceable law may not be worth having.

The issue then turns to questions as to what might be done to enforce that law or to make it more enforceable ... which significant parts of this thesis have addressed. That is why we have examined the balance of power and control between the key actors in the system pertaining to dealing with insolvency in English professional football. We have noted the ways in which the actor relationships in relation to power and control are affected by the ebb and flow of professional knowledge, of moral authority and of managerial expertise.

Chapter 2 concluded with the provocative and somewhat simplistic suggestion that rule-following is likely to be a question of self-interest, with obedience being more probable if it brings advantages which outweigh any disadvantages. However, matters rarely stay still for long and that chapter also drew attention to the flux of the environment which may alter the balance of what is seen to be advantageous and what is not. Exploration of the values and beliefs held by actors permitted an enlargement of the analysis in terms of what might be seen to be an advantage (not to mention consideration of the moral and ethical issues related to using that advantage). Acceptance of the fact that actors within the systems studied differed both within subsystems and across subsystems sensitised readers to avoid over-simple suggestions such as the one mentioned. The chapter closed by indicating the prevalence of contestation and conflict between those different actors.

Thus, applying the Law of Unintended Consequences in the context of the discussion, there might certainly have delivered a series of unexpected drawbacks and which just

possibly may lead to perverse results. Amongst the drawbacks may lie the law's difficulty in keeping its regulations consistent with changing economic and social environments; its awkwardness with dealing with subsystems with wholly different backgrounds in knowledge and expertise; and its struggle when dealing with conflict-inducing topics. The perverse results hinted at above might include having regulations which are out of date; are irrelevant to achieving their original purpose; and which are openly flouted. Whether the causes of these are due to poor or incomplete analysis or to the laziness of following old habits which seem to deliver successful regulation in the past is not easy to say.

When reviewing the relevant literature here, one is struck by the continuing emphasis on resource presence or absence yet there is virtually nothing which examines the presence or absence of a capability to utilise this resource. In the context of professional football this might refer to the presence of sufficient financial resource to purchase (and to pay) expensive footballing talent yet fail to perform successfully on the pitch due to an absence of ability to integrate this expensive resource into the playing style of the team. Or, in a different part of the system, the presence of sufficient resource to advise on insolvency manoeuvres does not guarantee that the advice will be accomplished.

In the third chapter, concerns regarding the translation of theory into real world practice were pointed out. Notable among these disquiets were the assumptions that sufficient resource of the appropriate type would be available; that the exercise of regulatory discretion would not give rise to sundry problems, particularly with respect to accountability; and that the environmental context would present few issues for the regulator. Above all, perhaps, was the realisation that decentred systems of the type we study in this thesis result in fragmentation of the regulator's power to ensure that regulation occurs in the anticipated manner.

This chapter examined some causes of regulatory failure with detection (of inappropriate behaviour) difficulties; with enforcement problems; and with operational assessment issues being prominent. Commentary was also offered on the possibility that the regulatee response to activity by regulators might well be conditioned by their

adoption of one or more of the futility, jeopardy or perversity positions in respect of any particular regulation.

The discussion of regulatory failure then progressed away from a focus on individual actors towards a more pronounced focus on systemic aspects contributing to lack of regulatory success. The notions of ineffective co-ordination between system elements; of inadequate systemic learning; and of a fondness for simplistic thinking (not only by regulators) were put forward as possible cause of regulatory failure, particularly if these mechanisms interacted one with another. The prospect of our complete system becoming progressively closed to external influence could not be entirely discounted; nor could the likelihood of system drift as a consequence of information asymmetry. This examination of informational inadequacy was associated with the very human propensity to filter out unwelcome communication, even to the extent of setting up unconscious but significant group paradigms which ultimately lead to regulatory failure.

Analysing the synthesis of chapter 3 so far in terms of Merton's ideas again is wholly suggestive of regulatory activities in respect of our Central Puzzle which certainly yield unexpected drawbacks aplenty; which quite possibly deliver some perverse results … and, which, in terms of that chapter's discussion, do not seem to result in any unexpected benefits. Perhaps any of the Merton list of causes other than that of *self-defeating prophecy* might be said to be in play here?

Notwithstanding the above, the chapter also engages with the concept of regulatory deficit as a means of investigating regulatory shortfalls. Such deficits allegedly may derive from questionable oversight by regulators (which may well be a factor in relation to the 'revolving doors' between The Insolvency Service and the body of experienced IPs); or from an over-direct participative relationship between regulator and regulatee potentially excluding third party interaction (which almost certainly pertains with that obtaining between RPB and IP in respect of complaints against IPs); or from the intriguingly termed adaptability deficit in which regulators are slow to accommodate to environmental change both within and without the system here being explored. In defence of the regulators here, it might be observed that the terms *fast* and

slow are relative ones: the key point is surely not so much the speed of the change but awareness of the extent and consequences of systemic drift away from the original regulatory purpose. The final deficit, that of a shortfall in incentives for regulatees to conform to regulatory pressure is clearly relevant in our context and will be returned to towards the end of this chapter. Again, all of the above can be considered to a greater or lesser degree to be both unexpected and perverse results.

Finally, Chapter 3 pays attention to aspects of communication. Here, in turn circumstances which result in misunderstanding; which highlight inadequate attempts to achieve understanding; and which survey hidden and indirect communication are each considered. As discussed above in relation to other Chapter 3 ideas, such aspects may be deployed on their own or in conjunction with one another. Examples of these communication issues, in turn, might be the direct conflict between English insolvency law and the rules of the football authorities; the evident disquiet felt by the Hansard Society about how legislation is communicated; and the hidden (and differing) moral stances adopted by the variety of regulators in our observed system, all of whom profess to working in 'the public interest'. Communication activity is of manifest significance when questions of obedience to a rule is expected and thus regulators might be expected to publicise to regulatees one or more of their claims for obedient behaviour and support these with some sensible support for such claims. The Mertonian analysis offered in previous paragraphs is also similarly relevant on these features.

Chapter 3 concludes with this author's MURDER acronym which, in part, points to areas in which Regulation in Practice could profitably improve upon.

Chapter 4 looks at Accountability: who might be held responsible for what … and who should initiate and control motions of account. The discussion accepts that accountability can both be internal and external in character, thus raising questions about norms held by individuals and groups and also about the legitimacy of the regulator, the regulation itself and the mode of regulation. There are many connections to the discussions in previous chapters with the concepts of legitimacy, of inadequate decision-making and of compliance being prominent. The linkage to ideas of corrective or of retributive justice is a fairly easy one to make and can also be related to

appropriate independent codes outlining desired behaviour by key system actors in a variety of circumstances. Such codes may not just suggest the detail of the prescribed action but may also help underline the duty to act in a responsible manner.

The areas in which actors in general and IPs in particular may be held accountable can be usefully distinguished into five areas[493] … those relating to providing advice; to gaining credible data; to managing the insolvent business; to acting in an intermediary role; and to supporting the rights of all parties concerned. In order for any accountabilities to succeed, the need for one or more accountability supports (reports, dialogue and sanctions) was acknowledged. A somewhat different direction was followed later in the chapter when the specific notion of accountability to 'clients' was explored; the difficulty here in establishing which actor constituted the client was noted as was the unusual position of the IP as being a gatekeeper … as well as being a (within-profession) competitor.

The chapter finishes by asking whether regulation might accomplish more by shifting away (at least in part) from a position of social control to one of social protection.

Chapter 5 notes, early on, that IPs may not have too strong a claim to be always acting in the public interest and there exist concerns that their monopoly of insolvency 'appointments' offers the common opportunities for price (fee) exploitation. They also have choices as to their individual modus operandi … the options being nuanced between 'cleaning up' insolvency problems; performing urgent activity aimed at 'saving corporate lives'; and selectively plucking 'low growing fruit' to make a comfortable living.

The chapter proceeds to examine the role of lenders of funds/resources to firms which consequently become financially distressed. The focus here is mainly on banks and a change in role of the lender is noted. In the time period covered by the thesis, banks have moved their focus from being holders of debt to being more interested in being originators of debt which is then sold on. This has implications for the degree of interest

[493] The examples given here apply specifically to IP activity but could be generalised outside this sphere with little difficulty.

which banks, in general, are said to take in the day to day running of the debtor company.

Then the chapter moves to briefly review the regulatory sanctions available against directors who have been involved with offences or undesirable conduct in relation to the insolvency of their company. There has been a recent tightening of the rules relating to director disqualification which supplement the practice of directors giving a Disqualification Undertaking in lieu of being potentially subject to a Disqualification Order. Of particular interest here is that directors conduct is not reviewed if their company exits from administration via the CVA route ... which is commonly the case with financially distressed football clubs.

An exposition of the way in which insolvency is conducted for companies is then offered which starts with the liquidation process and administration, moves through discussions of the *Pari Passu* rule and other rules such as the Anti-deprivation rule and ends with outlines of the methods of exiting administration of which Pre-packs and CVAs are the most relevant to our discussion. The chapter finishes by succinctly discussing the implications for English corporate insolvency of foreign legislation and considering the consequences of insolvency moves for the employees of the distressed company. These open the way for discussion in subsequent chapters relating to the payment of staff and players of football clubs and to the impact of foreign regulators on the financial conduct of English football clubs.

Chapter 6 saw analysis and commentary regarding the unusual instance of the Football Creditors' Rule which seeks to interpose an industry-specific regulation between member clubs of English professional football and the 'law of the land'. The Judge in the High Court hearing left no doubt as to his view in regard of the morality of this regulation but nevertheless his judgement did not alter the FCR in any way. It was left to later self-adjustment by football's authorities to attempt some ameliorisation of the effects of the rule. Even then, that changes could not be viewed as being radical ... and the requirement to pay football creditors in full, with unsecured creditors being paid a small fraction of that, remains the case.

The last of the discussion chapters[494] surveyed attempts, initially from outside English football though eventually imitated within, to address what was perceived to be ***a*** cause if not ***the*** cause of financial distress in professional football ... that of financial profligacy. It was thought that clubs just spent too much in the pursuit of sporting success and paid insufficient heed to financial prudence whilst running their businesses. Thus was launched a series of regulations collectively entitled The Financial Fair Play rules. Arguably, these have been more sound than fury so far … with little evidence of sanctioning to date. Concurrently with the FPP notions, it was mentioned that the concept of *The Sporting Interest* gained traction in legal thinking, based as it was on the premise that sport is not a normal line of business and thus it should not be subject to normal laws, particularly of an economic character. This approach was seen to be fundamentally European at root and, presently, after the Medina case, not easy to predict in application. The UK's expected exit from the EU will render the sporting interest notion even more problematic.

If judged by the Corkian standard of Business Rescue, then the English professional football sector must be rated an outstanding success. Only one club going into liquidation[495] out of more than a hundred over a period of 30 years or so seems to indicate that English Insolvency law has achieved its purpose very well indeed. Compared with the insolvency rate of companies in the High Street Retail sector, one might well wonder why this has been so.
If, however, a more focused view is taken of this success, it is not difficult to discern a different story; one in which the Public Interest approach to regulation seems thwarted both deliberately and accidentally and in which Private Interest forces appear dominant. That Merton's comments regarding unexpected consequences seem apposite in relation to football insolvency regulation is held to be justified.

Despite recent changes to the industry's own private rules, the position of football's unsecured creditors remains weak as compared with creditors from within football's

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[494] Chapter 7 ... Pan-European Developments

[495] Maidstone Utd in 1992

own system. The rescue of clubs and their ability to then survive is mainly a function of their ability to reap a harvest of debt owed to the state (in the guise of HMRC) with further contributions from relatively powerless small, unsecured industry suppliers. That this continues appears to be a considerable anomaly in public policy.

The apparent injustice, here, is compounded firstly, by inadequate communication to and from participant clubs and appointment-holding IPs[496] and secondly, by the difficulties of holding individual IPs to account in any individual insolvency case. Again, as previous discussion has shown, these inadequacies are well enough known but appropriate remedial action has yet to be taken.

Based on the analysis provided above it is hard to forcefully refute the overall assessment of this sector/system as being one in which some of the more significant entities/actors seem to be, if not outside the control of the law then outside the current interest of the state to bring them under the law's control. The proposition that the Sporting Interest is, in practical terms, above the law (at least vis-a-vis Corporate Insolvency) seems a strong case to make.

Put differently ...*"Matters are not quite as expected" !*

[496] Usually acting as Administrators

Epilogue

This piece started with an anecdote about the author's youth in Scotland. It may apt to book-end it with another reference from that youth's schooling.

Robert Burns is often quoted as saying in his poem, "*To a Mouse*",[497]

"*... the best laid schemes o' mice and men gang aft agley ...*"

Here, Burns pithily draws attention to the disconnect between plan and outcome. This dissertation provides evidence that this is true in certain applications of Insolvency Law. But that evidence relates to the *process* of executing the plan and not the overall *result* ... after all, practically no professional football clubs are ever liquidated.

Perhaps it is to the complete verse from that poem which we should refer …

"But Mouse, you are not alone,
In proving foresight may be vain:
The best laid schemes of mice and men
Go often askew,
And leave us nothing but grief and pain,
For promised joy!" [498]

The final two lines are key in the circumstances of Burns' lifelong support for the struggles faced by the underdog. In the context of this thesis these lines highlight the unfortunate exchange … *grief and pain* instead of *promised joy* ... which for football's unsecured creditors, sum up the law's pursuit of a rescue culture driven approach to corporate insolvency in respect of English professional football clubs. Those able to control the content of regulation and those carrying out the regulation do seem to have the joy; those who are powerless to affect the course of the regulation are left with the grief and pain.

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[497] Burns, R. "*To a Mouse, on Turning up her Nest with the Plough*", 1785

[498] This Anglicised version is taken from Wikipedia.

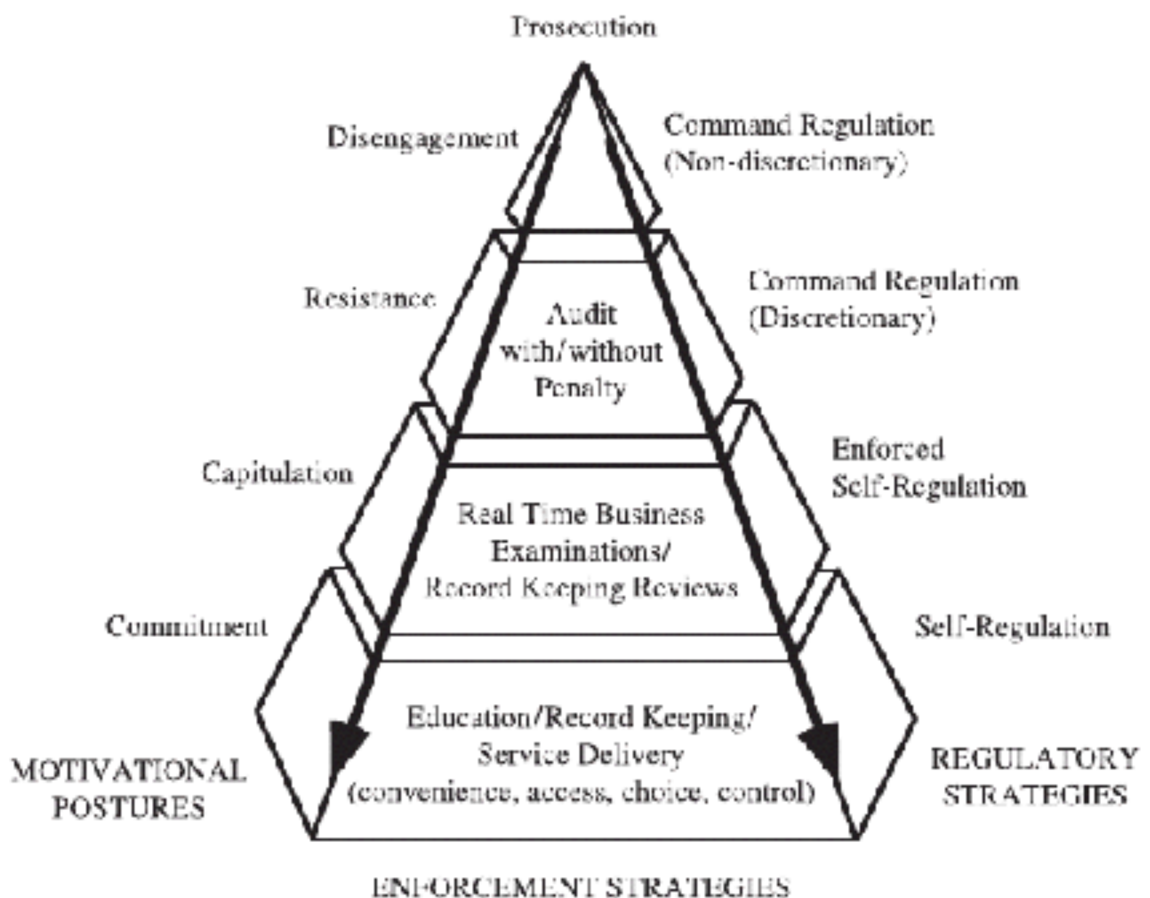
But, as a regulatory agent himself in later life, Burns became perfectly aware that the connection between Regulation and Justice is neither clear nor tidy. And so it is now with this author.

Appendices and References

Appendix 1:

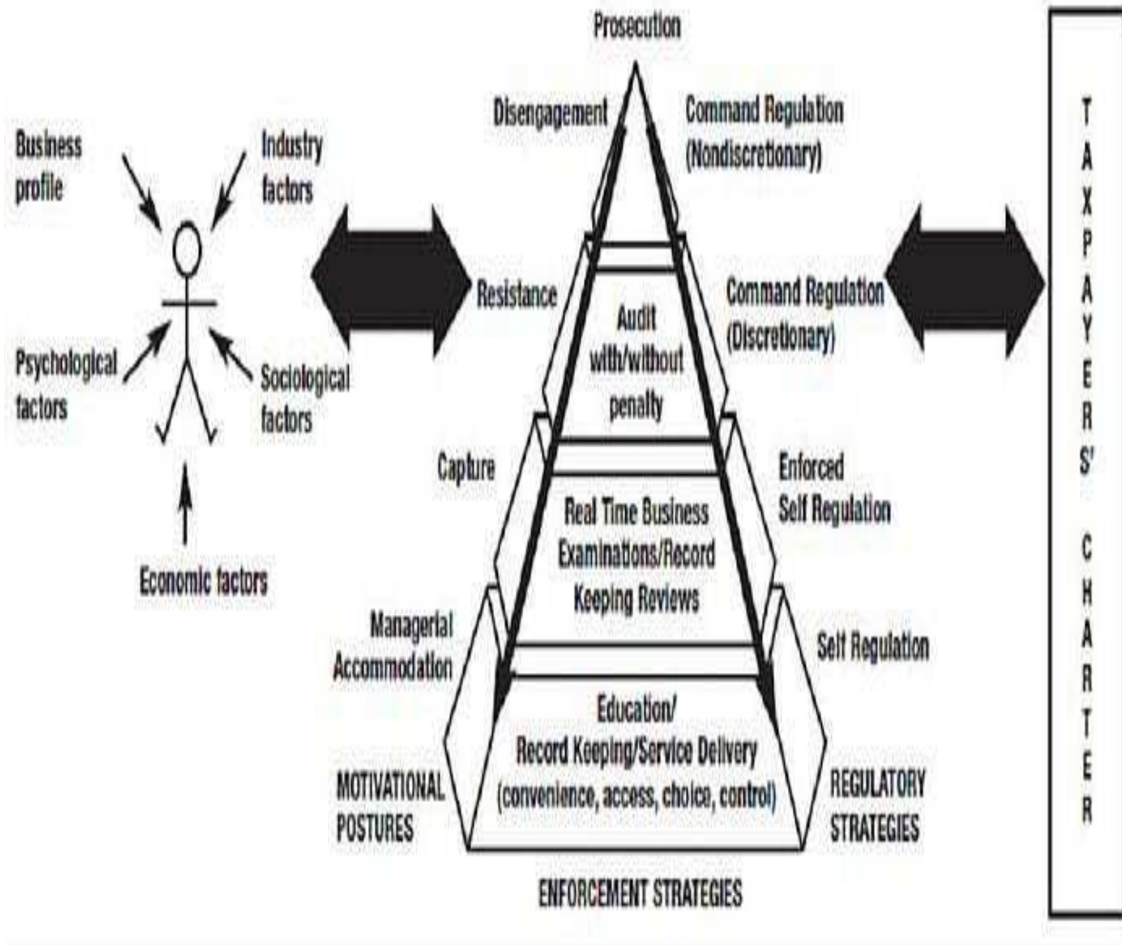
Modified Ayers and Braithwaite 'Responsive Regulation Pyramid' for Risk Differentiation.

Regulatory risk differentiation is the process used by a regulatory authority (the regulator) to systemically treat entities differently based on the regulator's assessment of the risks of the entity's non-compliance.



Appendix 2 :

An Australian exemplification of the connection between enforcement, motivation, regulatory strategies ... and the environmental context.



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Deregulation Act 2015

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The Financial Services and Markets Act 2000 (Insolvency) Order 2001

Insolvency Act 1986 (the Insolvency Act)

Insolvency Act 1994

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Insolvency Act 2000

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