



# THE UNIVERSITY *of* EDINBURGH

## Edinburgh Research Explorer

### Mutuality for football clubs? Lessons from the financial sector

**Citation for published version:**

Adams, A & Armitage, SE 2004, 'Mutuality for football clubs? Lessons from the financial sector' *Studies in Economics and Finance*, vol 22, no. 1, pp. 26-41., 10.1108/eb043381

**Digital Object Identifier (DOI):**

[10.1108/eb043381](https://doi.org/10.1108/eb043381)

**Link:**

[Link to publication record in Edinburgh Research Explorer](#)

**Document Version:**

Author final version (often known as postprint)

**Published In:**

*Studies in Economics and Finance*

**Publisher Rights Statement:**

© Mutuality for football clubs? Lessons from the financial sector. / Adams, Andrew; Armitage, S. E.  
In: *Studies in Economics and Finance*, Vol. 22, 2004, p. 26-41.

**General rights**

Copyright for the publications made accessible via the Edinburgh Research Explorer is retained by the author(s) and / or other copyright owners and it is a condition of accessing these publications that users recognise and abide by the legal requirements associated with these rights.

**Take down policy**

The University of Edinburgh has made every reasonable effort to ensure that Edinburgh Research Explorer content complies with UK legislation. If you believe that the public display of this file breaches copyright please contact [openaccess@ed.ac.uk](mailto:openaccess@ed.ac.uk) providing details, and we will remove access to the work immediately and investigate your claim.



**MUTUALITY FOR FOOTBALL CLUBS?  
LESSONS FROM THE FINANCIAL SECTOR**

**Andrew Adams\* and Seth Armitage\*\***

Published in  
*Studies in Economics and Finance* 22, Spring 2004, pp. 26-41

\*School of Management, University of Edinburgh,  
email [andy.adams@ed.ac.uk](mailto:andy.adams@ed.ac.uk)

\*\* Department of Accountancy and Finance, Heriot-Watt University,  
email [s.e.armitage@hw.ac.uk](mailto:s.e.armitage@hw.ac.uk)

# **MUTUALITY FOR FOOTBALL CLUBS? LESSONS FROM THE FINANCIAL SECTOR**

## **Abstract**

The mutualisation of two English third division football clubs in 2001 and the creation of a large number of supporters' trusts make it timely to consider whether there is a case for mutualisation of football clubs. This paper assesses whether mutuality would be of economic benefit for clubs, drawing heavily on the experience of mutuals in the financial sector. Our conclusions are mixed. The economic case rests on the distinctive feature of customer loyalty to a club, presuming this to be much stronger than loyalty to a financial institution. However, club members in a mutual must expect to be called upon to provide financial support.

## **1. Introduction**

Most British football clubs are constituted as companies, and several of the largest have been floated on the Stock Exchange, the first to do so being Tottenham Hotspur in 1983. The main objective of a company, at least in theory, is the maximisation of shareholders' wealth, and one would expect this objective to be emphasised after a company is quoted on the Stock Exchange. Unfortunately, pursuit of wealth maximisation by a football club does not coincide with the interests of its customers (supporters) and tends to erode the emotional bond between the club and its supporters. Football supporters are particularly vulnerable to exploitation due to the loyalty and commitment they show to their club, and it is common for boards and supporters to be in open conflict over matters such as ticket prices and the price of replica kit.

Many commentators argue for greater democratisation of club ownership and the government's Football Task Force 'majority report' (1999) recommended that supporters should be given more say in how their clubs are run. Michie & Ramalingam (1999) go further and suggest that full mutualisation 'would suit the culture, ethos and objectives of football clubs and should be encouraged to promote a diverse and modern economic system', though the authors stress that it may be difficult to raise the capital to buy out the shareholders.

Ownership of a football club by its supporters has obvious constitutional attractions. Through the principle of one member, one vote, members would have an equal say in important decisions, and could propose resolutions at general meetings of the club. The involvement of supporters would therefore be reflected in and reinforced through a mutual constitution, with no conflict of interest between owners and supporters. But would the mutualisation of a football club be in the supporters' interests? Given that only a very few clubs are currently flourishing in financial terms, with the majority operating on the edge of viability, this would seem to be an issue worth considering.<sup>1</sup>

In February 2001, Lincoln City Football Club changed its ownership structure to an industrial & provident society<sup>2</sup> and was purchased for £400,000 by a mutual consortium consisting of supporters, local businesses and the Co-operative Society. This followed many years of financial blight at the club. Then in May 2001, Chesterfield Football Club followed suit and turned itself into a mutual after the Chesterfield Football Supporters Society acquired a majority shareholding of the club. The club had run into serious debt and had been penalised by the English Football League for financial irregularities. After mutualisation, the club attracted financial support from many interested parties including the Borough Council.

The type of 'community mutual' at Lincoln City and Chesterfield Football Club has not been created simply to serve the economic interests of its members. The key relationship is between the club and the local community. As Jaquiss (2001) puts it: 'The community is served by the mutual and owns it (through open membership) and controls it (through the elected and co-opted members of the Board).' In many ways this is a return to the community-run, non-profit organisations that football clubs were when they were first established.

The mutual consortia at Lincoln City and Chesterfield were helped by the Supporters Direct organisation, which became operational in September 2000. Supporters Direct was set

---

<sup>1</sup> Aggregate operating losses amounted to £59m for the ninety-two English professional football clubs in the 1999/2000 season. Operating losses of £112m for the seventy-two Football League clubs exceeded operating profits of £53m for the twenty Premiership clubs. Pre-tax losses amounted to £145m overall. (Deloitte & Touche, 2001).

<sup>2</sup> The constitution of an industrial and provident society requires that: the trust must operate for the benefit of the community that it serves; the members and officers will not profit from the trust; and all changes to the rules are monitored by the Registrar of Friendly Societies (Hamil *et al.*, 2001).

up with funding from the Department of Culture, Media & Sport as a response to the recommendation of the Football Task Force that supporters be given more say in how their clubs are run. It provides legal and practical advice to help football supporters form trusts and thereby become more actively involved in the management of their clubs.<sup>3</sup> Ideally, this involves electing representatives of the trust to serve as directors on the board of the club. By December 2001, Supporters Direct had helped in the setting up of forty-two supporter trusts, around half of which have elected supporters' representatives on their boards (Supporters Direct, December 2001).<sup>4</sup> Similarly, in 2000 Celtic supporters formed an industrial and provident society known as the Celtic Trust.<sup>5</sup> By the middle of 2001 there were nearly 200 members of the trust, holding in aggregate shares worth around 1% of Celtic PLC, although there is currently no representation for the trust on the board, which is causing some disquiet among the members.

Some argue that the long-term aim of a supporters' trust should be to expand to the point where it gains control of the club and then to turn the club into a mutual organisation. This seems to be the view of David Burns, Chief Executive of the English Football League, who argues that 'mutuality is not a thing of the past. Instead, as the establishment of Supporters' Direct has shown, it is very much part of the future for many football clubs in this country' (Supporters Direct, September 2001). But whether the supporters' trusts springing up all over the country can be regarded as an intermediate step to full mutualisation depends very much on the economic benefits of such a change in status.

Having established that there is serious interest in mutuality for football clubs, we now assess whether mutual clubs would be viable in the long term. We do this by drawing comparisons with the two types of business in which mutuals have been most prominent in the UK, namely mortgage banking and life assurance. We do not seek to make a case for or

---

<sup>3</sup> The first democratically run supporters trust was created at Northampton Town FC in 1992. The trust managed to obtain representation on the Board through the efforts of the local council who were in a position to exert pressure on the club because the club needed local council support for its ground development (Michie & Verma, 1999).

<sup>4</sup> Under the terms of its initial Department of Culture, Media & Sport funding, Supporters Direct could only provide direct financial assistance to supporters' trusts in England and Wales. However, with additional funding from the Scottish executive it has, since April 2002, also been offering a semi-autonomous service in Scotland.

<sup>5</sup> The origins of the Celtic Trust can be traced back to 1997 when the Heriot-Watt and Edinburgh University Celtic Supporters Club resolved to push for a more proactive role for supporters in the running of their club (Carr *et al.*, 2001).

against mutuality in football, but to assess whether mutuality is a serious proposition in the light of the disappearance of most of the larger financial mutuals.

## **2. Mutuals in the financial sector**

Mutual institutions have been prominent in retail financial services in the UK and in many other countries. In the late 1980s, building societies had a market share of about 70% of mortgages and just over 50% of retail deposits (Drake, 1989), and the market share of mutual life offices was about 38% (Armitage, 1997). But many building societies and mutual life offices have since converted to joint-stock status in the UK, to the point where there is only one large building society and one large life office remaining. There is a real possibility that mutuality will disappear almost completely from the UK financial sector in the next decade. There was a similar wave of demutualisations in the 1990s in the USA, Australia, South Africa and Ireland, although not in continental Europe. Several stock exchanges, including the London Stock Exchange, have also converted in recent years. In this section we consider explanations for the existence of financial mutuals, and whether the recent conversions imply that there is something inherently wrong with the mutual constitution.

### **2.1 Agency issues**

The accepted explanation for why financial mutuals exist is Fama & Jensen's (1983) application of the agency perspective. They argue that, in the long run, the form of organisation that will survive is the one in which agency costs are minimised. Agency costs in this context are the extent to which managers fail to maximise the welfare of shareholders, or the welfare of members of a mutual, together with the costs of 'monitoring' and 'bonding' mechanisms designed to promote welfare maximisation. In general, the opportunities for agency costs to arise are reduced as the intensity of competition faced by the organisation increases.

The agency perspective might appear to leave no room for mutuals, as some have argued (for example, Rasmusen, 1988). The major advantage of joint-stock companies is that the owners (shareholders) are better able to 'discipline' managers than are the owners (members) of a mutual. A quoted company is under scrutiny by investment analysts and professional investors, and if there is no 'friendly' shareholder owning a large block of the shares, it is vulnerable to a hostile takeover bid. Alternatively, a single owner can acquire a

large stake, or own all of the shares, and can exercise direct control of the company. Thus, the managers can be steered towards maximisation of shareholder wealth either through stock market pressures or through direct intervention by a large shareholder. The aim of a mutual is to maximise the benefits of the organisation to its members. But the absence of stock market pressures, and the one member, one vote principle, mean that a mutual's managers are arguably less accountable to its members than are the managers of a company to its shareholders. Also, it has been difficult in practice to take over a building society or mutual life office without the agreement of its management or the intervention of a regulatory body. The result is that agency costs, manifested in relatively undynamic management, or in unnecessary expenditure, are expected to be greater in a mutual.

To account for mutuals in the agency framework, Fama & Jensen argue that there must be special features of a particular business that give the mutual form an advantage to set against the lack of shareholders. In the case of mortgage banking, the nature of the product means that there is a direct link between member satisfaction and the size of the business. The size of a building society depends primarily on its success in attracting deposits and using them to make mortgage loans (these operations were all a society was allowed to do until the Building Societies Act 1986). Because deposit accounts and mortgages are products which endure over time, customers have an ongoing interest in the health of the product provider, but if they are dissatisfied, they can take their deposit or mortgage business elsewhere, and the mutual shrinks. Fama & Jensen also argue that monitoring by customer-members works best for simple organisations, whose business is easy to understand; a criterion which applies in the case of building societies is not complex. Given these points, the benefits of further 'disciplining' by shareholders may not be worth the costs of having an extra group of stakeholders with a claim on the business.

Life offices are similar to building societies in that they collect savings and invest them to provide a return, but it is, or has been, notoriously costly to withdraw from a with-profits endowment policy once entered into. It is also very difficult for policyholders to assess how competitive their policies are in relation to others available. Arguably, therefore, product market discipline is weaker in the life sector than in mortgage banking, and there is more scope for managers to exploit policyholders in their own or shareholders' interests. Mayers & Smith (1981, 1988) and Hansmann (1985) argue that the main benefit of the mutual form in

the life assurance business is that it avoids costs arising from the conflict of interest between policyholders (customers) and shareholders. The conflict of interest is clear: shareholders wish to maximise the profits allocated to them, which are paid out as dividends or retained as shareholders' funds. Policyholders do not normally receive any of these profits. There is also an argument that it is in shareholders' interests to take what may be viewed as excessive risks with policyholders' funds. If the risks pay off, the shareholders will receive most of the profit; if they fail, profit will be lower but most of the loss will be borne via lower bonuses for policyholders. Mayers & Smith (1981 and 1988) argue that control of this conflict of interest can impose extra costs on the business in the form of regulatory limits to dividend payments and investment policies, which protect policyholders from excessive payments to shareholders and from imprudent investment of their funds. The current authors are not aware of any such limits applying to proprietary offices in the UK. However, to the extent that customers are aware of the differences between mutual and proprietary offices, and know which office is of which type, it may be more difficult for proprietaries to attract new business.

If agency problems are, in fact, no worse in mutuals than in their joint-stock competitors, the two types of organisation should display similar efficiency. The mutual will then be able to provide better-value products for its customers, assuming that over time a proprietary mortgage bank or life office pays out more in dividends than it receives through share issues. This is certainly a reasonable assumption in the long run. Even Microsoft will return cash to its shareholders one day. Thus, assuming that agency costs are no higher in mutuals than in joint-stock companies, the advantage of a mutual is that it does not have to provide a return to shareholders.

A number of researchers have tested detailed predictions from the agency explanation for mutuals. For example, Mayers & Smith (1988) test the hypothesis that relatively weak control of mutual management implies that mutuals 'should be more prevalent in lines of insurance where management exercises little discretion in setting rates' (pp. 357-8). They also hypothesise that mutuals should have more concentrated operations geographically. The idea is that greater managerial discretion and greater geographical diversity will make the organisation harder to monitor and offer more opportunities for risk-taking from which shareholders rather than policyholders will benefit. Controlling for size, they find that mutual operations in the US are more concentrated geographically, measured by the number of states



in which companies are licensed, and that they specialise to some extent in different lines of business. Mayers & Smith (1992) argue that, if chief executives in mutuals have less discretion than in proprietaries, one would expect them to be paid less and, again controlling for size, this is what they find. Adams (1993) investigates whether mutuals and proprietary offices in New Zealand differ in their asset allocation and policy on reserves. The agency prediction is that proprietaries have a riskier profile because this is in shareholders' interests; they should have a riskier portfolio of assets and lower free assets and provisions. But he identifies no differences attributable to the organisation's constitution, which does not square with the findings of Mayers & Smith. Overall, there is patchy empirical support for agency-inspired predictions of difference between mutual and joint-stock business (see Armitage, 1997, and Drake, 1997, for fuller discussions).

A question of obvious interest is whether mutuals are associated with poor performance in relation to their joint-stock competitors. If agency problems are worse in mutuals, this should show up in worse performance. The agency perspective need not in itself lead to such a prediction, however: Fama & Jensen (1983) and Mayers & Smith (1981) are concerned to predict circumstances in which agency costs may be smaller in mutuals. The UK and US evidence suggests that, in fact, mutuality in retail banking and life assurance has not been associated with poor performance or more serious agency problems compared with joint-stock companies in the same business (see Drake, 1997, and Valnek, 1999, for building societies, and Armitage, 1994 and 1997, and Draper & McKenzie, 1998, for life offices). Mutuals in the UK have, if anything, provided a better deal for customers, operated with lower cost ratios, and grown more rapidly.

However, the operations of both building societies and life offices were changing from the mid-1980s onwards, and it can be argued that the changes were undermining the suitability of mutuality. Building societies began to diversify away from the core business of taking deposits and mortgage lending, towards provision of services such as estate agency and investment advice, for which they could charge a fee. A customer would not become a member by virtue of buying such a service. In life assurance, unit-linked products were taking over from with-profits endowment policies as the major vehicle for investment via a life office. The returns of with-profits policyholders approximately reflect the performance of the life office as a whole; if the office's costs increase or the investment performance is poor,

bonuses will suffer. So with-profits policyholders approximately share the risks and rewards of ownership of the office. In contrast, the returns on a unit-linked policy reflect the investment performance of the particular fund to which the policy is linked, rather than the life office's general fund, and unit-linked policies are written with a view to extracting profit from the fees charged for the office's investment management services. Unit-linked policies do not share the risks and rewards of ownership of the office, and so this product does not seem as well suited to the mutual arrangement as the with-profits policy.

In summary, the agency perspective can explain why mutuals are found in some businesses but not in others. The evidence indicates that, in businesses in which mutuals have been prominent, they have been able to compete successfully with joint-stock companies. They have not, as a group, been under pressure to demutualise due to poor performance, although changes in the nature of their businesses have perhaps made mutuality less suitable.

## **2.2 *Access to capital***

Joint-stock companies have an advantage in being able to raise fresh equity capital by issuing shares. Mutuals can only grow through retention of surpluses. This is another possible explanation for why financial mutuals are found in less risky lines of business, such as mortgage lending, but not in lending to companies. Less risk implies less need for capital.

The decision regarding how much surplus to retain is awkward in a mutual. On the one hand, every pound retained is money that could have been paid out to members, for example through declaring higher bonuses on endowment and whole-life policies. On the other hand, retained surplus forms the capital base, which allows growth and absorbs losses. If the base is too small, survival is threatened. Equitable Life was forced to close in 2001 not only because of a House of Lords judgement that it must honour its guaranteed annuity contracts, but also because of its long-standing policy to operate with relatively little capital for its size, which left it unable to honour the contracts.

The capital constraint has been a contributory factor in some decisions to convert, particularly amongst life offices, but was probably not the main immediate explanation in most cases. There was no problem in practice for building societies to grow through retention of surplus, and none of those which have converted were short of capital at the time of

conversion. It is true that many of the life offices which converted were either small or seen as lacking in capital at the time. But these offices were generally taken over by a larger (proprietary) life office or a bank, and the same would almost certainly have happened had they been proprietary offices. So in these cases, demutualisation can be seen as an incidental consequence of the takeover. At the same time, however, it is noteworthy that the larger building societies and mutual life offices have not made large acquisitions, unlike their joint-stock brethren. The inability of the mutuals to issue shares is probably a major reason for their reluctance to make large acquisitions.

### **2.3 *Windfalls on conversion***

The building societies which demutualised, and at least Norwich Union amongst the life offices, were strong, successful organisations. The primary benefit to the members from conversion, and possibly the only benefit, is windfall in the form of free shares or cash or extra investment in the with-profits fund.<sup>6</sup> It is in the financial interest of most existing members to convert, whether via flotation on the stock market or via take-over by a company. If existing members form the constituency whose financial benefits the mutual seeks to maximise, the mutual is acting in accordance with its objective in converting.

Conversion is in the interest of most members because for most of them the value of the shares and/or cash payment received on conversion is more than the present value of the loss they can expect as customers due to the profit which will henceforth be extracted from them. The reason is as follows. The payment to members on conversion is the market value of the business, which can be viewed as having three components:

1. The present value (PV) of the surpluses which existing members who remain customers would have been expected to generate, had the organisation remained a mutual. This is the PV of cash the members would have contributed to the organisation

---

<sup>6</sup> Although official statements by the boards of financial mutuals which have converted have tended to emphasise advantages to the organisation, rather than the windfall to the members. For example, the chief executive of the then Halifax Building Society wrote that 'the plc form will give us important funding and capital-raising advantages as a bank as well as freeing us from the constraints of an increasingly restrictive piece of legislation [the Building Societies Act 1986]. It will release value for members and will separate the present confused customer/owner relationship into a customer and equity shareholder relationship' (Mike Blackburn, *Banking World*, February 1995, p. 7).

anyway. They are given this PV as part of their windfall on conversion, and would not have received it otherwise.<sup>7</sup> It is therefore a gain from conversion;

2. The PV of net cash flow expected from *new* customers. This is another gain for the existing members;
3. The PV of the extra net cash flow to be extracted from existing members who remain customers, above the surpluses which they would have contributed had the organisation remained a mutual. Extra cash flow is expected because of the change in the organisation's objective. This element in the windfall merely compensates the members as a group who remain as customers for the poorer deal they can expect in future as customers, assuming that joint-stock status does not lead to improved efficiency. It does not represent a gain from conversion for the members as a whole.

Overall, the losers from conversion are mainly future customers of the ex-mutual rather than ex-members. This assumes that conversion does not improve the efficiency of the organisation. If conversion improves efficiency, future customers may not lose, or may benefit.

It appears that the survival of mutuals is threatened whatever they do. Unsuccessful mutuals, or those with insufficient capital, are likely to be taken over or wound up. Successful mutuals will face pressure to convert, in the interests of their own existing members. From a broader perspective, a case can be made for the existence of financial mutuals, to promote diversity and competition (Llewellyn, 1997). But individual institutions have to weigh the benefit of the windfall for their existing members against the possible costs to existing and new customers in the future.<sup>8</sup> Circumstances have forced the managers of remaining mutuals to make a clear commitment of mutuality. For example, most remaining building societies have, in recent years, instituted a policy of 'rewarding' members. The implication is that the society deliberately makes a smaller surplus than the profit it would have made had it been a joint-stock bank. The societies have also changed their rules so that members would not receive the conversion windfall. It remains to be seen whether this amendment, and the

---

<sup>7</sup> Surpluses are retained in practice unless the mutual is wound up or unless it makes losses. Capital can be distributed to members, but we know of no examples of this as yet.

<sup>8</sup> Michie (1999, p. 28) writes that 'demutualisation is ... just one more example of short-termism in the British economy.' But it depends on one's perspective. Demutualisation is clearly in the short- and long-term financial interest of existing members of a mutual as a group. At the same time, a Llewellyn-style argument can be made that future welfare will be diminished if financial mutuals are allowed to disappear completely. If one accepts this

rediscovery that a mutual does not exist to maximise its surpluses, prove enough to secure the survival of societies as mutuals.

### **3. Mutuality for football clubs?**

The basic agency concern about a mutual football club is that the absence of a profit imperative may result in worse performance both on and off the field than if the club were a company. But the experience of financial mutuals suggests that the absence of shareholders is not associated with poor performance, provided that the mutual operates in a competitive market. Football clubs are likely to be similar in this respect; there will always be plenty of competition on the field. And a lack of dynamism on the part of the managers does not seem likely in the football business.

But is there a special feature of the football business that actually gives mutuality an advantage? We suggest that there is one: customer loyalty. This arises partly because of the geographic inconvenience of switching clubs for many fans, but perhaps more importantly because there is a clear sense in which the ‘product’ is unique. The experience of watching your side win is not one which another club can provide and, as with a financial mutual, the product endures over time and involves an ongoing relationship between provider and customer. Loyalty means that a badly managed club will not lose all its customers, while the most successful clubs, with very large loyal followings, can charge near-monopolistic prices for their products. How might supporter loyalty provide a rationale for mutuality?

We noted above that a rationale for mutuality in life assurance is that a proprietary office might have difficulty selling its products due to mistrust on the part of would-be customers. In the life business, it is opacity of the product and of prices, which renders customers vulnerable to exploitation and potentially leads to mistrust. In football, it is supporter loyalty which engenders vulnerability. Thus, mutuality can help a club attract new supporters on the grounds that, were the club to become more successful, price increases for match tickets and other products would be lower than if the club were a company. In addition, the greater involvement with a club implied by mutuality may enhance the experience of being a supporter, thereby enhancing the value of the club’s product. This would be reinforced if the

---

argument, the disappearance of mutuals involves a negative externality. This could form the basis of a public-interest case for preventing current members from ‘cashing in’ via conversion.

club made a deliberate virtue of its mutual status, as the remaining financial mutuals have belatedly done, and as Lincoln City and Chesterfield football clubs appear to be doing. There has been a marked change in the attitude of the remaining financial mutuals, with the development of a less positive approach to making profits.

A central issue is whether football mutuals really would be less inclined to exploit their supporters than football clubs that were companies. There are no shareholders, but the managers could exploit the supporters (members) by increasing their own salaries and by on-the-job consumption. It could be argued that, as institutional investors or other large shareholders are not monitoring a mutual, this agency problem is likely to be more prevalent. Institutional investors have experience in monitoring company managers and have in-house experts in corporate finance and accounting. Nevertheless, members of a football mutual would presumably have collective knowledge of the football business, and loyal football supporters are much closer to a football club than are institutional investors. In many ways they are therefore in a stronger position to monitor managerial performance. Problems such as 'empire building' are unlikely to arise. Members could employ their own financial advisers to help in the monitoring process. There might even be sufficient financial expertise within their own ranks. Supporters are not just in a good position to monitor managerial performance: the emotional bond felt by at least some supporters means that they have a strong *incentive* to monitor. The growth of supporters' trusts mentioned in Section 1 suggests that there is latent enthusiasm for more supporter involvement in club management.

In the case of a badly managed club, the fact that it is a football club makes its position somewhat different from that of most other businesses, including financial mutuals. The normal market mechanism for ensuring that bad management does not persist is decline of the business and, ultimately, closure, or takeover by another management team. However, closure of a football club is, arguably, much more of a last resort than closure of other types of business, because its product is unique. This means that the methods of dealing with poor management should be focused on intervention, for example replacing managers, rather than closure. Again, it could be argued that a mutual constitution is superior to that of a company in the prevention and treatment of poor management. It is the supporters who would employ the paid executives, entrusted with the efficient running of the club.

However, mutuality also has drawbacks. A major issue is the fact that the football business has much more financial risk than mortgage banking or life assurance. Indeed, as most clubs are unprofitable at present (see note 1), the members of mutual football clubs, unlike the members of a financial mutual, would face a serious risk of being called upon to provide extra funds. Mutuals are not found in risky lines of business in the financial sector. We suggested in Section 2 that this is because of the capital constraint implied by the inability to issue shares, because retail customers are not in a good position to monitor and control institutional risk-taking, and because many people wish to avoid risk specific to an institution. We now consider in turn whether these three factors are relevant in the football world.

First, although a mutual football club could not issue shares, its members could still effectively inject funds, for example through donations. Supporters and local communities have in the past often contributed money to bail out failing football clubs, and mutual status arguably makes this more likely. The rewards for such injections of funds would be the survival of the club and the prospect, were its fortunes to improve, of lower prices for tickets and other products, than if it were a company. A change in status to a mutual could, on occasion, actually attract a charitable donation from a wealthy individual, as was the case with Lincoln City. But it is also possible, and perhaps more likely, that the mutualisation of a club would make it harder to attract financial backing from a wealthy individual, since s/he could not be ‘rewarded’ by outright control, or at least by ownership of a large block of shares. There is no easy answer to this. Mutuality offers an alternative to domination of clubs by rich individuals, and to the potential exploitation of supporter loyalty for the purpose of making a profit. But it will not solve the inherent unprofitability of football clubs.<sup>9</sup> Mutuality will only be viable, at least in current circumstances, if the membership accepts a role as potential provider of financial support.

The second and third reasons why financial mutuals are not in high-risk businesses are less applicable for a football mutual. In our view, the supporters *are*, at least potentially, in a good position to monitor and control the management of the club. That is part of the attraction

---

<sup>9</sup> However, widespread mutualisation of clubs would lead to reduced losses if it results in a reduction in the ‘subsidy’ for the football business which is currently provided by rich individuals. Clubs would be forced to align costs more closely with the income which the supporter base is actually willing to provide. Some clubs may simply have too small a supporter base to be viable, in which case they must either remain subsidised by their benefactor(s), or close.

of the mutual constitution and part of the reason for the establishment of supporters' trusts. There is, therefore, less concern *a priori* than in a financial mutual about the possibility that managers will take risks which the members do not know about, and would not condone if they did. In addition, the financial risk for a member of a football mutual is likely to be much less, and more 'voluntary', than in the case of a financial mutual. For many people, being asked to pay a higher ticket price (if a football mutual performs poorly) is not in the same league as the loss of one's savings (if a financial mutual performs poorly).

There remains the problem that, were a mutual club to be successful, it might come under pressure to convert, for the same reason that applies to financial mutuals. But here again, supporter loyalty could mitigate against the desire to cash in. This factor was largely absent in the case of financial mutuals. Most customers did not know the difference between a bank and building society before the conversions started. A survey of consumer attitudes to mutuality conducted in 1996, when the conversions were well under way, found that 'amongst the majority of respondents, understanding of it [mutuality] is at a very basic level, or non-existent, and it is devoid of any real meaning for consumers... There is a failure to discern any difference between mutual and non-mutual insurers, and, indeed, substantial ignorance as to which are or are not mutuals' (Janet Levin Associates, 1996). Whilst many customers had a vague attachment to building societies, presumably this would pale into insignificance in comparison with supporter feelings for a mutually owned football club. The form of mutual constitution adopted could also prevent conversion. The 'anti-conversion' measures taken by the remaining building societies have so far been effective.

#### **4. Conclusions**

The consideration of financial mutuals in this paper clarifies both the case for mutuality amongst football clubs and the problems involved. The strongest economic argument for mutuality, we suggest, is that if the club were to be successful, the supporters would not be exploited to make profits for shareholders. This danger arises because a club's product is unique, whereas the product of a building society or life office is not. A mutual constitution may therefore make it easier for clubs to attract and retain supporters. The fact that supporters could be genuine members of their club may also enhance the experience of being a supporter. The evidence from financial mutuals is that mutuality is not associated with inefficiency, and there is no obvious reason to expect mutual football clubs to be less efficient



than proprietary football clubs. The one member, one vote arrangement could even lead to better monitoring and control of club management than the shareholder alternative. So we do not envisage that agency problems would, in general, be any worse in mutual clubs than in joint-stock clubs.

On the negative side, football is a risky business financially and mutuals are not found in risky lines of business in the financial sector. Members would face a high probability of being called upon for more funds, perhaps repeatedly. They would need to be a source of capital if a mutual club is to survive hard times. Furthermore, football fans are generally not experts in monitoring of the management of an organisation, nor are they financial experts, although they could buy in such expertise.

The fundamental reason for the wave of conversions amongst financial mutuals is that the value of the windfall exceeds the costs to customers of the poorer deal they can expect after conversion. For the same reason, there might be pressure to convert if a club were mutual and became more successful. However, the emotional-attachment factor which has already led to the mutualisation of two English third division clubs, combined with anti-conversion provisions, could mean that mutual clubs face much less pressure to convert.

Our conclusion is that there is potential for mutuality to add more value in the football business than it has in financial services, due to the greater loyalty of a club supporter compared with a mortgage-bank or life-office customer. But mutualisation would be unlikely to make the cost of football cheaper for supporters. The nature of mutuality in football, if it develops, will therefore be somewhat different from the nature of mutuality in the financial sector. The advantage of a financial mutual is based squarely upon not having to provide a return to shareholders. Financial mutuals are found in relatively low-risk and simple lines of business, because the agency costs of the mutual constitution should be relatively low in these lines, and because of the mutual's inability to raise new capital. The advantage of football mutuals, if they develop, would be based only partly on not having to provide a return to shareholders. Successful joint-stock clubs can and do exploit their loyal supporters, and this should not occur in a mutual. But most clubs struggle financially, and many depend on the backing of a rich shareholder. For such clubs, the immediate advantage of mutualisation is that it would give the supporters control. The club would have a constitution in which the

supporters had the votes, and in which they could be as involved in the management as they wished. Supporters would probably not benefit financially, at least not until such time as the club started to make healthy surpluses. In fact, supporters would have to accept a role as potential providers of financial support. In our view, the question about whether mutuality catches on in football boils down to this: will supporters be willing to accept the greater financial ‘responsibility’ for their club implied by mutuality, in exchange for greater control? This question may well arise at a number of clubs in the coming years.

### **Acknowledgements**

We are grateful to Kenneth Forman, Ian Graham, David Grant, Christopher Pong, Philip White and two referees for many useful comments on earlier drafts of this paper.

## References

- Adams, Mike, 1995, 'Balance Sheet Structure and the Managerial Discretion Hypothesis: An Exploratory Empirical Study of New Zealand Life Insurance Companies', *Accounting and Finance* 35, pp. 21-47.
- Armitage, Seth, 1994, 'The Performance of Proprietary Compared with Mutual Life Offices', *Service Industries Journal* 14, pp. 238-61.
- Armitage, Seth, 1997, 'The Future of Mutual Life Offices', in Hugh Macmillan & Mike Christophers (eds), *Strategic Issues in the Life Assurance Industry*, Butterworth Heinemann, pp. 43-63.
- Carr, Peter, Jeanette Findlay, Sean Hamil, Joe Hill and Stephen Morrow, 2001, 'The Celtic Trust', in Hamil, Sean, Jonathan Michie, Christine Oughton & Steven Warby (eds), *The Changing Face of the Football Business: Supporters Direct*, Frank Cass, pp. 70-87.
- Deloitte & Touche, 2001, *Annual Review of Football Finance*, August, p. 5.
- Drake, Leigh, 1989, *The Building Society Industry in Transition*, Macmillan.
- Drake, Leigh, 1997, 'The Economics of Mutuality', *Loughborough University Banking Centre-Building Societies Association Project Paper 3*, Building Societies Association.
- Draper, Paul & Eddie McKenzie, 1998, 'The Returns to Policyholders from Alternative Organisational Structures: Evidence from the UK Life Assurance Industry', Working Paper 98.6, Centre for Financial Markets Research, University of Edinburgh.
- Fama, Eugene F. & Michael C. Jensen, 1983, 'Separation of Ownership and Control' and 'Agency Problems and Residual Claims', *Journal of Law and Economics* 26, pp. 301-49.
- Football Task Force, 1999, *Investing in the Community*, Stationery Office.
- Hamil, Sean, Jonathan Michie, Christine Oughton and Lee Shailer, 'The State of the Game: The Corporate Governance of Football Clubs 2001', Football Governance Research Centre, Birkbeck College, University of London.
- Hansmann, Henry, 1985, 'The Organization of Insurance Companies: Mutual versus Stock', *Journal of Law, Economics and Organization* 1, pp. 125-53.
- Jaquiss, Kevin, 2001, 'Mutualism Rules: The Community in Football', in Hamil, Sean, Jonathan Michie, Christine Oughton & Steven Warby (eds), *The Changing Face of the Football Business: Supporters Direct*, Frank Cass, pp. 51-56.
- Janet Levin Associates, 1996, *Consumer Attitudes to Mutuality*, Janet Levin Associates, London.

Llewellyn, David T., 1997, 'The Mutuality v. Conversion Debate', *Loughborough University Banking Centre-Building Societies Association Project Paper 2*, Building Societies Association.

Mayers, David & Clifford C. Smith, 1981, 'Contractual Provisions, Organizational Structure, and Conflict Control in Insurance Markets', *Journal of Business* 54, pp. 407-34.

Mayers, David & Clifford C. Smith, 1988, 'Ownership Structure across Lines of Property-Casualty Insurance', *Journal of Law and Economics* 31, pp. 351-78.

Mayers, David & Clifford C. Smith, 1992, 'Executive Compensation in the Life Insurance Industry', *Journal of Business* 65, pp. 51-74.

Michie, Jonathan, 1999, *New Mutualism: A Golden Goal?* The Co-operative Party.

Michie, Jonathan & Shay Ramalingam, 1999, 'Whose Game Is It Anyway? Stakeholders, Mutuals and Trusts', in Hamil, Sean, Jonathan Michie & Christine Oughton (eds), *The Business of Football: A Game of Two Halves?* Mainstream Publishing, pp. 158-67.

Michie, Jonathan & Shraddha Verma, 1999, Corporate Governance and Accounting Issues for Football Clubs, Working Paper 99/05, Department of Management, Birkbeck College, University of London.

Rasmusen, Eric, 1988, 'Mutual Banks and Stock Banks', *Journal of Law and Economics* 31, pp. 395-421.

Supporters Direct, 2001, *Supporters Direct Newsletter No. 4* (September), *No. 5* (December).

Valnek, Tomas, 1999, 'The Comparative Performance of Mutual Building Societies and Stock Retail Banks', *Journal of Banking and Finance* 23, pp. 925-38.