



LIQUIDATED DAMAGES, PENALTY CLAUSES AND BUY-OUTS IN FOOTBALL-RELATED EMPLOYMENT CONTRACTS UNDER THE FIFA REGULATIONS

This contribution analyzes the differences and similarities between penalty clauses, liquidated damages provisions and buy-out clauses, exclusively under the light of the FIFA RSTP. The author's position is that pure penalty clauses, that grant the player no right and no limitation as to the determination of the damages shall not be accepted and only forfeit clauses (buy-out clauses) or liquidated damages provisions shall be admitted as compliant with the FIFA RSTP.

INTRODUCTION

The inclusion of premature termination clauses in employment contracts has become commonplace in professional football. In the aftermath of "Matuzalem" the football industry perceived these clauses as an oasis of certainty and security in opposition to the calculation based on the criteria of art.17 of the FIFA RSTP that is uncertain by nature. Therefore, within the limits provided by national laws, more and more clubs started to adopt these clauses in their employment contracts.

This proliferation eroded however the image of certainty the clauses initially offered. The majority of discussions related to the topic have as starting point the nature of the clause in each particular case and therefore the consequences following a premature termination.

In some countries, particularly –but not exclusively- those from the common law legal system, the nature of the clause can even determine whether it is valid or void¹.



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¹ For France see Moyersoén Patricia. Buy-out clauses in French Sports Law. Football Legal 9 pg.113.





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It is also important to highlight that there is an international trend towards upholding clauses independent of their classification while granting adjudicators the power to reduce the sum fixed where it is excessive.²

In a recent article, Shervine Nafissi Azar³ summarized the three types of possible clauses that can be found in football-related employment contracts: a) a liquidated damages provision b) a penalty clause or c) a forfeit clause.

A penalty clause is a provision whereby the debtor is obliged to pay the creditor a specified amount if he does not execute his main obligation. The clause serves as a guarantee to reinforce and strengthen the main obligation. It operates *in terrorem* and no damage must be proven to enforce it, simply the breach of the secured obligation⁴.

A liquidated damages provision constitutes a clause in the contract stipulating a predetermined sum of money payable in the event of breach. This makes liquidated damages clauses quite practical in that *they stipulate the amount to be paid and save a party having to sue for general damages, which are quantified by the courts by reference to a number of variables and are, therefore, speculative in nature*⁵. The amount must represent a genuine pre-estimate of the loss generated by the breach.

Finally, a forfeit clause gives the debtor the right to withdraw from the contract at any time subject to the payment of a predefined amount⁶.

In this contribution I will analyze these clauses in employment agreements exclusively under the light of the FIFA RSTP. My position is that pure penalty clauses that grant the player no right and are neither a genuine estimation of the damage in case of breach shall not be accepted and only forfeit clauses (buy-out clauses) or liquidated damages provision shall be admitted as compliant with the FIFA RSTP.

² Pascal Hachem "Agreed sums payable upon breach of an obligation" International Commerce and Arbitration. Volume 7, Eleven International publishing

³ Shervine Nafissi Azar. Contractual Aspects of the buy-out clause: The Neymar Jr case. Football Legal 8 pg.23.

⁴ Pascal Hachem.

⁵ Mark Giancaspro "Buyout clauses in professional football player contracts: question of legality and integrity". International Sports Law Journal 2016 16:22-36

⁶ Nafissi Azar, with reference to Couchepin for the notion of "Consensual forfeit clause" in Swiss Law.





THE FIFA REGULATIONS

Starting point of the analysis is the relevant rule: Art.17 (par.1 and 2) of the FIFA RSTP that provide: “In all cases, the party in breach shall pay compensation. Subject to the provisions of article 20 and Annexe 4 in relation to training compensation, and unless otherwise provided for in the contract, compensation for the breach shall be calculated with due consideration for the law of the country concerned, the specificity of sport, and any other objective criteria. These criteria shall include, in particular, the remuneration and other benefits due to the player under the existing contract and/or the new contract, the time remaining on the existing contract up to a maximum of five years, the fees and expenses paid or incurred by the former club (amortized over the term of the contract) and whether the contractual breach falls within a protected period.”

“Entitlement to compensation cannot be assigned to a third party. If a professional is required to pay compensation, the professional and his new club shall be jointly and severally liable for its payment. The amount may be stipulated in the contract or agreed between the parties.”

A mere literal interpretation is not conclusive since no specific types of premature termination clauses are mentioned or excluded. However, the use of the term “compensation” seems to be in contradiction with the notion of penalties that are applicable irrespective of the damage suffered⁷

The rationale of art.17 is explained in the FIFA commentary to the RSTP. A non-binding document issued by FIFA as guideline in 2006⁸. In said commentary FIFA stated: “The parties may, however, stipulate in the contract the amount that the player shall pay to the club as compensation in order to unilaterally terminate the contract (a so-called buyout clause). The advantage of this clause is that the parties mutually agree on the amount at the very beginning and fix this in the contract. By paying this amount to the club, the player is entitled to unilaterally terminate the employment contract.”

With this buyout clause, the parties agree to give the player the opportunity to cancel the contract at any moment and without a valid reason, i.e. also during the protected period, and as such, no sporting sanctions may be imposed on the player as a result of the premature termination” adding on a footnote: The sports legislation of certain countries (e.g. Spain, Real Decreto 1006) provides for a buyout clause to be included

⁷ Pascal Hachm, cited op. See also art. 161.1 of the Swiss CO.

⁸ FIFA Commentary on the Regulations for the Status and Transfer of Players, page.47.





as compulsory in contracts. Other countries cannot include such a clause in their contracts as it is not compatible with mandatory labor law.

Although the commentary is over a decade old and has never been updated, this still seems to be FIFA's position on the matter, as confirmed in a recent publication⁹.

The article clearly explains the difference between a buy-out clause and a liquidated damages provision: *"In other words, if the parties to the contract have agreed beforehand the amount of damages that they will suffer in case of an unjustified termination of the contract by any of them, Article 17 par. 1 of the Regulations will not apply with respect to the calculation of the compensation, and instead the damaged party will receive, as compensation, the amount agreed. In this respect, it is worth pointing out that, in order for a clause to be considered in lieu of the objective criteria listed in Article 17 par. 1 of the Regulations to calculate the payable compensation, its wording needs to clearly reflect that the intention of the parties **is to determine the damages they will suffer and should therefore not be confused with the so-called buyout clauses which do not provide for damages but rather grant to a party or parties, the right to terminate the contract prematurely against full and unconditional payment of the stipulated amount**".*

"Evidently, if a player exercises his/her right as per a buyout clause, the sporting sanctions provided in Article 17 of the Regulations will not apply"

"Another difference is that, evidently, if a player exercises his/ her right as per a buy-out clause, the sporting sanctions provided in Article 17 of the Regulations will not apply. On the contrary, if one of the parties terminated a contract without just cause and triggering a clause in the contract, which provides for the damages that a party will suffer in case of a breach of contract (liquidated damages clause), the party making use of said clause could be subject to sporting sanctions."

Moreover, in my view, a "pure penalty" clause, that gives the player no right and is only a punitive determination of the amount he shall pay in case of breach of contract, would be against the applicable well-settled compensation criterion established by FIFA and CAS for these breaches: the so called *positive interest*. Positive

⁹ Mario Flores Chemor, Maja Kuster Hoffmann and Omar Ongaro: "FIFA's Provisions on the Unilateral Termination of Contracts - Background and their Application".



interest has been defined by CAS case law as basically putting the injured party in the position that it would have had if no contractual breach had occurred.

Another element that points (in my opinion) towards the prohibition of pure penalty clauses is the objective sought by FIFA with the inclusion of these clauses as an alternative to the objective criteria of art.17: to reduce litigation and increase legal certainty.

On the other side, it must be admitted that penalties in employment contracts are not illegal under Swiss law, although some scholars have a diverging opinion. In any event, since Swiss law only applies on a subsidiary basis, the legality of penalties in employment contracts under Swiss law is not conclusive.

Probably the main argument in favor of the validity of penalties in footballer's employment contracts is the amount of CAS case law that deals with (and admits) them. However, this case law shall be read in a context. The "seminal" CAS awards that dealt with the issue of premature termination clauses did not distinguish between penalties, buy-outs and liquidated damages since the objective of these cases was to differentiate between calculation of breach with a provision in the contract and calculation based on the objective criteria.

In particular, in "Matuzalem"¹⁰ the panel ruled: 62. ... *Art. 17 of the FIFA Regulations does not provide the legal basis for a party to freely terminate an existing contract at any time, prematurely, without just cause...*

67. This should not come to a surprise for those that are aware of the history of the provision itself and of the rules that are valid in some countries: Indeed, the rationale of allowing the parties to establish in advance in their contract the amount to be paid by either party in the event of unilateral, premature termination without just cause is to recognize that in some countries players and clubs have not only the right but even the obligation to do so (while, one shall note, in some other countries they may be prohibited to do so).

68 Whether such clauses are called "buy out-clauses", "indemnity" or "penalty clauses" or otherwise, is irrelevant. To meet the requirements of art. 17 para. 1 FIFA Regulations the parties shall have "provided otherwise", i.e. the parties shall have

¹⁰ CAS 2008/A/1519-1520



provided in the contract how compensation for breach or unjustified termination shall be calculated. Legally, such clauses correspond therefore to liquidated damages provisions, at least so far as the real will of the parties to foresee in such clause the amount to be paid by the breaching party in the event of a breach and/or of a unilateral, premature termination of the employment contract is established. Indeed, when FIFA and the relevant stakeholders were drafting the provision, it was recognized that such kind of penalties/liquidated damages may be validly agreed between the parties and, in such a case, it should not be up to the FIFA Regulations to deprive such a clause of its legal effect.

This position was reiterated in several other cases, as in CAS 2009/A/1880 FC Sion v. FIFA & Al-Ahly Sporting Club where the panel stated: 73. *First of all, the Panel observes that Article 17.1 of the FIFA Transfer Regulations sets forth the principle of the primacy of the contractual obligations concluded by a player and a club: “[...] unless otherwise provided for in the contract [...]”. The same principle is reiterated in Article 17.2. Therefore the Panel must preliminarily verify whether there is any provision in the employment contract between the Player and the Second Respondent that does address the consequences of a unilateral termination of the contract by either of the parties. Such kinds of clauses are, from a legal point of view, liquidated damages provisions (see, among others, CAS 2007/A/1358, at para. 87; CAS 2008/A/1519-1520, at para. 68).*

The objective of the panels in those cases was to highlight the difference between a case of contractual breach solved through the application of the objective criteria set out in art.17 RSTP and a case related to a contract that included a premature termination clause. These panels were not dealing with the differences between the various types of premature termination clauses. Some other cases however, did deal with the differences between termination clauses, as I will review in the next paragraph.

PRACTICAL ASPECTS

It is generally admitted by scholars that the differences between a liquidated damages provision, a penalty clause and a forfeit or buy-out clause are very subtle and is hard to differentiate one type of clause from the other. Then, why is the distinction important from a practical perspective? Because the determination of the clause’s nature will define whether sporting sanctions are applicable or not and whether the established amount can be altered.





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In cases where the labor contract was breached by the player or his conduct leads to the termination with just cause and the club is claiming compensation for that unilateral termination the difference between the various type of clauses is of limited relevance: If the clause is a penalty or a liquidated damages provision, its amount will be the main aspect to consider when assessing the compensation: If it is regarded as a penalty, it might be reduced if excessive. If it is considered a liquidated damages provision with a genuine estimation of the damage, it shall be maintained.

Under Swiss law, contrary to common law, the consideration of the clause as a penalty does not automatically lead to its nullification and the amount can be reduced to a genuine estimation of the damages.

As explained above, my position is that pure penalty clauses are against the FIFA RSTP. Therefore, if the player breaches the employment agreement the clause shall not be admitted as a penalty and compensation for breach shall be assessed on the basis of the various parameters established in art.17 of the RSTP. The stipulated amount can certainly be a parameter to take into account, a sort of acknowledgment by the player of the reasonableness of the sums.

Even if the clause is regarded as a forfeit and the player terminates the contract without making the payment or commits a breach that leads to the termination, then the forfeit right would not be properly executed and the termination shall be treated as a simple breach, being the amount of the buy-out clause the main factor on which the former club will probably sustain its claim for compensation.

As explained in CAS 2015/A/4188 AS Monaco v. Sevilla FC¹¹: "8.37 The Player could have simply walked away from the Contract without just cause. However, pursuant to the Regulations, doubtless the Respondent would have pursued the Player under Article 17 of the Regulations. The Respondent would have claimed the EUR 20,000,000 referred to in the Contract, and if the Player had joined the Appellant, then it would be requested to be jointly and severally liable too. Whilst this alternative would most likely not be classed as a transfer, it would raise the risk of disciplinary sanctions. The Player could be sanctioned with a 4 - 6 month playing ban and the Appellant with a two transfer window ban".

In all these situations, irrespective of the nature of the clause, if the contract is breached, sporting sanctions might apply. The importance of the distinction arises in

¹¹ An excellent analysis of the award, especially its procedural aspects can be found at Jordi López Batet "FIFA and the CAS rule on rescission / Buy-out clauses. " World Sports Law report Vol. 14 Issue 08 August 2016





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cases where the player executes the clause, considering it as a forfeit clause and terminates the contract in advance by paying or offering to pay the stipulated sums, but the club objects such termination.

If the clause is considered a liquidated damages provision, then it will only be a pre-estimation of the club's financial losses, giving the player no right to terminate the employment agreement and making him (and eventually his new club) subject to sporting sanctions.

This was the case in CAS 2013/A/3411 Al Gharafa S.c. & Mark Bresciano v. Al Nasr S.C. & FIFA where the panel held that: *As made clear by such definition, which corresponds to standard practice in international football, the parties, while entering into a contract, may agree that at a certain (or at any) moment one of the parties (normally, the player) may terminate the contract, by simple notice and by paying a stipulated amount. In other words, one of the parties (ordinarily, the club) accepts in advance that the contract may be terminated: as a result, when the contract is effectively terminated, such termination can be deemed to be based on the parties' (prior) consent. Therefore, no breach occurs, and the party terminating the contract is not liable for any sporting sanction. It is only bound to pay the stipulated amount – which represents the "consideration" (or "price") for the termination.*

However, the acting Panel (confirming the FIFA DRC decisión) considered that the relevant clause was not a buy-out but rather a "liquidated damages" provision and therefore imposed sporting sanctions to the player and the new club: *"the wording of the clause is rather clear: it does not grant the Player the right to terminate the Contract, but sets the consequences "if" the Contract is terminated; Article 8.1 refers to "damages" caused by the Player's "cancellation of the Contract": the expression "damages" is inconsistent with a "buy-out clause", since any payment to be made by the Player would not be "damages", but the consideration for the exercise of a contractual right".* A controversial aspect of this case is that the DRC and also CAS admitted a higher compensation than the one set up in the liquidated damages clause.

The same conclusion as to the nature of the clause was reached in CAS 2016/A/4550 Darwin Zamir Andrade Marmolejo v. Club Deportivo La Equidad Seguros S.A. & F.I.F.A. In this case, the player did pay the amount stipulated in the clause but his former club sued for sporting sanctions against him and the new club. FIFA granted the request, and CAS confirmed, considering that the clause was not a buy-out clause but a liquidated damages provision.



Here, the fixed amount of compensation was not modified by the panel. However, the decision treats as synonyms the notions of penalty and liquidated damages: “118. The Panel agrees with FIFA’s position, and confirms that the clause contained at Clause 2 par. 2 of the Employment Contract qualifies as a contractual penalty or “liquidated damages” clause (“clause pénale” or “Konventionalstrafe”) under Swiss law (Article 160 of the Swiss Code of Obligations (the “CO”)... In other words, Clause 2 par. 2 of the Employment Contract, which sets the amount of “damages” to be paid in case of “termination [of the Employment Contract] without just cause by the employee before the expiration of the contract”, appears to perform a function (the determination of the amount that a party has to pay to the other as damages in the event of breach of contract) perfectly consistent with Swiss law.

On the other side, if the relevant clause is considered a buy-out clause, either established by mutual agreement or imposed by the law (as in Spain), then the player has a right to terminate the employment contract against the payment of the established amounts and without further consequences. No sporting sanctions shall apply and the sums paid are the final amount the former clubs will obtain for the premature termination of the employment contract.

The negative effects of admitting a pure penalty clause are easier to perceive in these cases in which the player pays or offers to pay the stipulated amount, considering that the contractual clause is a buy-out.

The former club, even after receiving the payment of the “penalty”, would be entitled to claim the application of sporting sanctions against the player and the new club. Also, invoking art. 161.2. Of the Swiss CO, the club will be able to consider the amounts insufficient and sue to obtain additional compensation.

By the same token, the player and/or the new club (that usually bears the financial burden of the buy-out) might pay reserving the right to claim a reduction of the penalty based on art.163.3 of the Swiss CO and request a reimbursement of the amounts paid in excess once the move is completed.

On the contrary, if the clause is considered a forfeit clause, the former club would not be able to claim sporting sanctions or additional amounts. As to the new club and the player, since consensual forfeit benefits the debtor, the reduction established in art.163.3 does not apply¹².

¹² Nafissi Azar, pg.27





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To my knowledge, there is still no case of a club requesting an additional amount of compensation following the payment of the buy-out / penalty by the player or the application of sporting sanctions (contrary to the referenced cases of liquidated damages) or –on the other side- the reimbursement of the amount paid allegedly in excess.

Still, press usually reports that clubs “suffering” the loss of a player evaluate what legal actions they have against the player and/or the new club even after receiving the payment of the sums set in the contract. With multi-million-dollar clauses flourishing and clubs competing for limited talent and “franchise” players, is not hard to forecast that these claims will be filled sooner than later.

Also, in CAS 2016/A/4585 *SS Lazio SpA v Al Sadd SC*, where the panel rejected a claim for reimbursement of the solidarity mechanism, these potential consequences of a pure penalty were discussed. The acting panel accepted the validity of a pure penalty clause, and in that case not on a general manner but specifically as opposed to a buy-out clause.

For the panel, the clause inserted in a player’s (Mauro Zárate) employment contract was just a penalty foreseen in case of a unilateral breach and therefore could not be interpreted as an anticipated consent with the player’s termination or as a transfer price set in advance.

The subsequent acts of Al Sadd, especially the frustrated negotiations where the Qatari club asked for a higher transfer amount and the claim at FIFA for breach of the loan agreement¹³, confirmed for the panel the club’s lack of consent with the exit of the player and therefore the nature of the clause.

¹³ Claim rejected by FIFA and TAS, award CAS 2012/A/3018





CONCLUSION

Summarizing, if a premature termination clause is inserted in an employment contract governed by the FIFA RSTP, it shall be considered either a liquidated damages provision or a buy-out clause. Pure penalties that give the player no right or no limit as to the compensation in case of breach, and are of a punitive nature shall not be admitted.

If the player breaches the employment contract, the stipulated amount shall be a parameter to assess alongside other criteria. If it constitutes a genuine estimation of the damage, then it must be upheld to the extent agreed and no further. If it exceeds a reasonable anticipation of the losses, then it can be taken at most as an additional parameter to fix the compensation. In both cases, sporting sanctions might be applicable.

If the player terminates the contract offering to pay or paying the stipulated amounts and those exceed a reasonable pre-estimation, then the clause shall be considered a buy-out and the player shall be free of any further claims or sporting sanctions.

CAS panels have been given in my opinion too much weight to the wording of the clause and the use of terms like "damages", in principle incompatible with buy-outs. I believe that is more important to analyze the overall conduct of the parties. A club that puts in an employment contract a termination amount that exceeds a genuine estimation of the losses (even if it is clearly written as a pure penalty and mentions the possibility of applying sanctions) is focusing on getting as much money as possible from the termination, way more than the positive interest.

On the other side, the player that admits the inclusion of such clause in his contract and later pays the money that exceeds a genuine estimation of losses is clearly interpreting the clause as the possibility to terminate the employment contract without further consequences. Why would a player accept the inclusion of a clause that gives him no right to leave and even increases the amounts paid in case of breach beyond the notion of compensation? In such cases it must be interpreted that he is executing a buy-out clause.

The potential consequences of considering a termination clause a pure penalty reveal the negative effects of such qualification and are the main reason for me to sustain they are not valid under the FIFA RSTP.

The objective of the option established in art.17 RSTP is to give the parties legal certainty and to simplify or even reduce litigation. The consideration of a termination clause as a penalty achieves the exact opposite result, it fosters litigation: The former club can claim sporting sanctions and even an additional amount after receiving the stipulated sums. The new club and the player can claim that the clause is excessive and request a reimbursement.





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Therefore, it is my opinion that under the FIFA regulations, any clause contained in an employment contract that establishes an amount to be paid in case of premature termination by the player shall be

considered either a liquidated damages provision or a buy out clause. The determining element to differentiate between both possibilities shall be whether the amount is a genuine pre-estimation of the damages or is in excess of such estimation. Pure penalty clauses shall not be admitted in employment contracts governed by the FIFA RSTP.

