Dons Trust

Background paper

Debt, equity & club ownership structure

1.0 Introduction

As you will be aware, The Dons Trust Board (DTB) has been consulting members on the management of debt that we hold.

Part of this has concerned the possibility of altering the club's ownership structure in a way that could allow further equity investment whilst retaining fan ownership.

Retaining ownership is something that is critical to both the functioning and the identity of our football club. It has been the reason that we have managed to achieve what we have collectively.

However, to properly manage the debt that we have as a result of building Plough Lane, particularly through the two Plough Lane Bonds that raised around £10.5m of finance that we lent to the club, we have taken the view that we must consider the possibility of reducing our shareholding to below the current 75%+1 of the shares we own.

We want to be very clear with you as a member: Doing this will not change the fundamental fact that our club is fan-owned. The Football Supporters Association (FSA), which advises and supports clubs like ours, provides a helpful definition of fan/supporter/community ownership:

- *A minimum of 50% +1 of the voting rights of the club to be controlled collectively by a democratic entity which has an open and inclusive membership based on one member, one vote with no substantial barriers to participation as a voting member.*
- *Profits are reinvested back into the club as opposed to being distributed to shareholders.*
- *The club is committed to running as a sustainable business.*

A club owned by its community has the potential to develop deeper longer-term partnerships, particularly local authorities who historically favour this model, and can attract a different type of investment and utilise a different type of finance (source: 'The Football Supporters Association: Supporter Ownership')

This document provides the financial background to this consultation, based on the club's current position and future plans. The DTB want to ensure members are fully informed so they can participate in the consultation process. Please read this information before completing the Survey.

2.0 Back to Plough Lane - the background

Since the club reformed in 2002, it has achieved its two primary initial objectives - namely regaining a place in the Football League and returning to the club to a new stadium in the Borough of Merton.

The Club moved into Plough Lane (PL) in 2020, with its first game on 3 November 2020. COVID had a significant impact on our plans, but despite relegation in 2022 we have managed to maintain strong match-day attendance figures and have already sold more season tickets this season than last.

Financially, the Club continues to make progress after sustaining losses during the Covid-affected period. In the 12 months to June 22, the Club had revenues of £8m (a 60% increase on 2021). Relegation resulted in a drop in income of approximately £500k from central funding as well as lower away attendances - this has to date been offset through player sales, however this is not money that we can rely on as an income stream.

Our accounts for the 12 months to June 23 have not yet been audited, but based on figures compiled to date, the Club generated revenues of £9m (including player sales) and profit before interest of £0.8m, with a closing cash position of £1.9m. This is an improvement versus the previous season owing to improvements in the commercial performance of the Club, and some significant income from player sales. The Boards have taken the decision to invest an amount of this into supporting the player budget, as well as targeting £500k each year towards debt repayment.

Currently, League Two clubs are losing on average £1.5m a year. We cannot do that. We are trying to keep costs down, but it remains extremely challenging to maintain a competitive budget while servicing debt. At this preliminary stage in autumn 2023 before all data is known for the current season we think that despite the additional money allocated, our playing budget is currently only 16th highest in League Two.

3.0 The Club's current sources of finance

Our achievements in funding our new stadium have been possible almost entirely down to our members, our fans, other supporters & investors (via the bonds & Seedrs) and our community. Not only for your attendance and spending on tickets, club merchandise and commercial offerings, but also through your support of crowdfunding initiatives and your investment. Most significantly, when a funding gap threatened the viability of the stadium construction project, more than £10m was lent to the club through the Plough Lane Bonds. As those bonds fall due for redemption - the club now needs to update its financial plans for the new set of challenges ahead.

Currently the club is financed as follows

- 80% of the equity is owned by the DT
- 20% is owned by minority investors who have invested £6m in the Club
- £10m of debt finance has been provided through Bonds, with £3.4m falling due for repayment in Spring 2025, £3.3m due in Spring 2027 and £1.6m due 2030, with the balance spread in much smaller amounts across several years up to 2044.
- The 'composite interest rate' on the bonds is approximately 4%. That is to say the club spends £400k a year servicing its debt currently (not including making any provision against redemption).

4.0 The Club's Business Plan for the next 3 years - increasing revenue and cashflow

The DTB/AFCW PLC have approved a three-year plan which was prepared and compiled by the club's senior executives. This is a critical document: it lays out the club's ambitions, its future profits and cashflows, and its financing needs going forward. The implementation of this plan will be seen through by the club's senior executive team, supported and challenged monthly by the AFCW PLC Board.

The club aims to operate on a sustainable financial basis, whilst also seeking to continue investing in the player budget, so that we have a competitive team in League Two and can aim at achieving promotion back to League One and then being competitive at that level. To enable this the club is focused as follows:

- Improving commercial performance: including sponsorship, hospitality & merchandise
- Growing season ticket and match-day spend
- Building and growing non-match day revenue for Plough Lane as an events provider
- Developing new revenues, eg the education provision
- Keeping overheads as low as possible

- Making player sales each year

The board believe that if this strategy is successfully executed, the club will achieve or surpass the following targets:

- Revenues expected to grow from £9m in 23/24 to at least £10m by 26/27 (not including any significant growth in income from player sales)
- Profit before interest costs to be targeted at £1m each year
- Operating net cashflow each year to rise to £500k

The board wants members and supporters to be aware that the majority of teams in League One and Two are incurring losses on an annual basis - this makes maintaining a competitive playing budget while remaining profitable *and* making debt repayment provisions especially challenging.

5.0 Managing the club's debt/refinancing £10m debt provision long-term planning

Alongside operational improvements, the PLC Board and Dons Trust Board have been considering all the options available to the club to refinance its existing debt obligations. This is taken on a rolling medium-term view as different tranches of Bonds fall due for repayments at different times, but the overall debt provision and financial structure needs to be considered holistically.

As directors, all members of the AFCW PLC and Dons Trust Boards have personal fiduciary duties under UK law to ensure the club can pay its debts as and when they fall due. In practical terms, this means the club must be able to repay any bondholders who want to redeem their bonds in full when they fall due. This means that the boards therefore have two key twin objectives - reducing the debt or extending the provision of the debt.

The first two major redemption windows are in 2025 and 2027. £3.4m of Plough Lane Bonds fall due for redemption in Spring 2025. Bondholders have been surveyed about their intentions and while a significant number have indicated they will not want their bonds redeemed in full at this date, the board are making provisions to cover redemptions for those who will request it. In 2027, £3.3m of the second tranche of Plough Lane Bonds will fall due for redemption.

Currently interest payments on the debt provision cost the club approximately £400,000 per year. Given that the Plough Lane Bonds were issued in a lower interest rate environment, any extension or replacement for these bonds could be likely to be at a more expensive rate.

Alongside planning for redemption windows, the AFCW PLC board therefore want to reduce the overall debt burden - their aim being to bring the total debt down significantly from £10m in the next three years (so before the 2027 redemption tranche falls due). This would also commensurately lower the annual cost of borrowing and improve the club's cashflow. The club's forecast profits year-on-year over the next three years are not currently sufficient on their own to generate enough cash to redeem the bonds falling due. AFCW PLC and DT therefore need to make some significant and difficult choices about what routes to assist refinancing are acceptable to members.

Options for debt reduction and extension

The options for debt reduction are as follows

- Increase the club's revenue generation targets and use this to pay down the debt
- Ask Bondholders to convert some/all of their debt into equity (see below)
- Use further equity investment to pay off the debt (see below)
- Ask members/others to make larger donations that would go towards paying off the debt
- Sell more players
- Ask Bondholders to write-off their debt, or "gift" their debt to the Club

6.0 The options for debt extension are as follows

- Offer Bondholders at redemption the option to extend some or all of their debt. We believe there is appetite for this for the 2025 tranche (based on the recent survey), but assuming economic conditions remain similar for the next two years this would probably be at a higher interest rate than currently. This would mean the club spending more of its nominal operating profit purely on interest payments. The benefit of all extensions and rollovers would be allowing the club longer to use operating funds or future significant "windfalls" (eg a substantial player sale transfer fee or major capital investment) to contribute further to debt reduction.
- Seek to secure bank or commercial financing to replace the "friendly" debt to bondholders. Currently the boards and finance committee do not believe that this is a viable option, because:
  - External lenders have told us that they require a better track record of financial performance than the club can offer;
  - The interest rates would likely be at least 10-12%

- The debt would be secured against the ground, adding risk to the club and undoing the success of the Plough Lane Bond scheme in removing any secured debt

7.0 Availability of equity: what is currently available & what is this consultation about?

AFCW PLC currently only has a small amount of equity headroom (additional shares it can sell) available - which could be used either to allow Bondholders to convert debt to equity or to bring further equity investment into the club. There is approximately 5% currently still available which could provide up to £1.5-1.7m of headroom for either of these alternatives.

Conversations are ongoing with potential investors. It can also be seen that there is not enough equity currently available for bonds falling due for redemption in 2025 and 2027 to convert to equity.

Under the Dons Trust Constitution, the Trust's shareholding currently must stay above 75%. The Dons Trust Board would therefore like members to consider the option of making further equity available. This could both enable further money to be invested into the club as equity (which could be used reduce the capital debt and annual interest costs) as well as allow more bondholders to convert their bonds into equity.

The option under consideration would be to confirm the Dons Trust as the majority shareholder which must always own at least 50%+1 of shares and voting rights. This would make up to 25% further equity available. Total equity headroom for investment or conversion would be approximately £9-10m rather than £1.5m.

The DTB has taken external legal advice which is summarised below for you to consider in the context of reducing its shareholding below 75%.

Current Protections for Members at 75% or more

Currently, with 75% the DT enjoys certain additional protections under UK company law as compared to being a majority shareholder (i.e. below 75%), including the following:

- The right to pass special resolutions needed to amend the articles of association (the Club's 'rules'); change the company's name, authorise the company to issue new shares without having to offer them to existing shareholders first and allow the company to buy back its own shares out of capital - all of these actions require 75% of shareholders to vote for approval.

Ongoing Protections for Members at 75% or below

However, the Trust currently has additional protections provided by the “Restricted Actions” list in the articles of AFCW PLC (Schedule 1) which are also included in the rules of the DT (note the word ‘Society’ refers to the DT). These provide that the PLC Board shall not take any action nor pass any resolution without the prior written consent of the DTB (and Members) in any matter that pertains or relates to:

- Any action that results in the Society’s voting capacity in AFCW plc falling below 75% (in the event of changing structure to below 75% this would be updated to reflect this new limit)
- Sale of any freehold interest in Plough Lane
- Any ground relocation from Plough Lane
- Creation of any new leasehold interest in Plough Lane
- Any issue of new shares in AFCW plc, or transfer of existing Society shares in AFCW plc, to 3rd parties
- Any alteration in the ownership or corporate status of any subsidiary company that increases the influence of 3rd parties over any of those companies vis-à-vis the Society
- Setting up any new subsidiary company that is not 100% owned by AFCW plc.
- Creating any agreement in respect of Plough Lane to leave the club having less favourable terms in respect of length of tenure, rights or rents paid
- Name of the Club including nickname, or its status with the FA
- The primary colours of the Club (yellow and blue)
- The Club and associated subsidiary badges and crests
- Borrowing against the security of the freehold at Plough Lane

These protections would remain in the articles of the PLC in the event of the Trust shareholding falling below 75%. The articles of the PLC cannot be changed without 75% of shareholders voting in favour (i.e., if the DT vote was against any such change it could never pass). It would however mean that should the DT want to change the articles it would need some of the other shareholders to vote in accordance with any future changes to pass to reach the 75% threshold. So existing safeguards could not be removed, but it would not be guaranteed any new safeguards could be added.

8.0 What would the DTB be asking for members to vote on?

The exact wording of the resolutions to be voted on would need to be confirmed but the expected questions the DTB would put to members would likely be:

1. Whether they support a motion to allow the DT shareholding and voting rights in AFCW PLC to fall below 75%, but always maintain at least 50%+1 of the voting rights.
2. Whether they believe the existing Restricted Actions contain enough protections.
3. If not, what other protections in the form of Restricted Actions members would like to add to the current list. For example: Do members think there should be a limit on the maximum shareholding a person can have eg 15% or 20%? Should the DT having the first right to buy when someone wants to sell their shares in AFCW PLC? Should new share issues not trigger pre-emption rights for existing shareholders?

A vote on any of these matters would be a restricted action under the Dons Trust constitution. To allow any of the above to happen the DT would need to have a vote in which at least half the membership vote and for two thirds of those voting to be in favour, with some changes requiring two votes within one month of each other.

9.0 Timeline

This survey will be indicative only ahead of any formal vote - and also allows time for members to ask any questions of the boards or about the financial background to this consultation.

In order to enable the DT and club to plan and set the budget for 2024-25 and to manage the first tranche of bond repayments due in early 2025, the DT would intend on bringing a vote to members in January 2024.

Any further vote to add additional Restricted Actions will take place within one month of the first vote.

Once the options available for refinancing have been confirmed by the outcome of the votes, all bondholders will receive further communication of the options available to them at least 12 months before their bonds fall due for redemption.

Should members decide that the Trust should not be allowed to drop its shareholding below 75%, then the boards and finance committee will have to make plans for refinancing without having equity headroom available for debt reduction through conversion to equity or replacement with equity investment. This will be much more challenging and have an impact on the club's financial performance and availability of operating cashflow year-on-year.

10.0 What comes next?

Please consider the information provided in this background carefully before participating in the survey. The results of the survey will be provided once the survey closes. We then expect to hold further discussion in the run up to the AGM.