

Pubs Consultation
Consumer and Competition Policy
Department for Business, Innovation and Skills
3rd Floor, Orchard 2
1 Victoria Street
Westminster
SW1H 0ET

13 June 2013

Dear Sirs

PUB COMPANIES & TENANTS: A GOVERNMENT CONSULTATION

Introduction

... welcomes the opportunity to respond to this consultation. We operate ... tenanted pubs ... and believe we fall in the category of **Small-medium sized company**.

We are totally committed to fair, transparent and lawful dealing with tenants and lessees and all other business partners and against any abuse of the tied pub model. We are committed to self-regulation and an independent complaints panel for rents or any other aspect of the Industry Framework or individual company codes. We are also convinced that the tied pub model provides a material and significant net benefit to tenants/lessees, with a low cost entry to running your own business and commitment and investment from companies supporting a vibrant pub sector through an unprecedented and difficult economic climate.

The tie offers entrepreneurs a low-cost, low-risk way of running their own pub with a wide range of support services. The model ensures both the pub company and the licensee have a mutual interest in the ongoing success of the business.

We believe that self-regulation remains the appropriate way to ensure that all parties are protected from any potential abuse of the tied model and that the business potential, level of support and respective obligations are fully transparent and offer a fair deal for all parties.

We do not believe that a Statutory Code underpinned by a newly formed regulator is a necessary or appropriate way forward. The impact assessment is wholly unsatisfactory. The additional regulatory burden adds very significant costs to the pub sector and potentially has hugely damaging consequences in terms of additional pub closures, business failure and reduced consumer choice.

The current rate of pub closures stands at 26 per week. Historically the trend shows that free of tie pubs are more likely to close than tied pubs, as recognised by the impact assessment which highlights a 5% closure rate for free of tie pubs between 2010 and 2012, compared to a 3.4% rate for tied pubs. The recent duty reduction on beer was a hugely welcome step for which the Chancellor was rightly applauded. However, failure to recognise the resilience and advantages of the tied pub model in difficult economic times such as these and the consequences of many of the proposals in relation to the Statutory Code is in danger of undermining this boost and are clearly counter to the Government's own deregulatory and growth agenda.

Before answering the individual questions there are some key points, inaccuracies and assertions from the evidence-base and impact assessment we would like to highlight:

- The number of 'complaints' to BII highlighted in the consultation (400 in three years) were in fact calls to a helpline. Other complaints noted are anecdotal. (companies to be asked to provide numbers of complaints they receive and this will be expanded on with potential access to BII data)
- We would disagree that there has been no culture change, the industry has moved a long way in the last two years in terms of self regulation and the latest Code was supported by ALMR representing multiple licensee interests.
- "The tie gives an additional route of abuse" and being "tougher for tenants to know if they are getting a good deal" are simply assertions with no foundation as is "tied tenants are more likely to face serious hardship". This is simply not true as the tied model protects tenants/lessees when trade falls and this is reflected by a greater proportion of free-trade pub closures as tied pubs. The same section states "The fair working of the beer tie is particularly important because of the hardship many publicans face including the possibility of losing their home" again is no different from the rest of the pub trade (or indeed anybody with a mortgage who loses their job).
- The language of this whole section is emotive, with little if any substance for the Government action then proposed. None of the above suggests the "proportionate regulation" which is the stated intention.
- There is no estimate of what will be a significant increase in costs of self-regulation for those companies below the 500 pub threshold proposed, if

larger companies are no longer part of this (since 2010, self regulation has been funded by BBPA members at a cost of £4million).

- The consultation also proposes that this transfer of value would lead to *increased* investment in the sector. This would appear contrary to the reality today where the asset owners (the pub companies) commit very significant amounts of CAPEX on their estates each year. It is very unlikely that banks will step in to replace the pub companies investment. The more likely scenario is increased pub closures.
- There is no assessment of the impact on pub companies of the proposed guest beer provision, or loss of the machine tie. This would have a very material impact on companies and create a significant distortion of competition above and below the proposed 500 pub threshold. The loss of the machine tie is likely also to lead to a growth in criminal activity for gaming machines.
- This would be completely unwarranted and disastrous statutory intervention into a market which the OFT has repeatedly concluded works well for consumers

The responses to the questions below are predicated on the basis that we do not believe that the evidence supports the need for a Statutory Code and adjudicator and are answered on the basis that if a Statutory Code is implemented it should be light-touch, cost effective and not materially distort competition

Q.1 Should there be a Statutory Code?

As outlined above we do not accept there is a need for a Statutory Code.

Our company firmly believes that self regulation is working and should be given more time. The structure of PIRRS (rent) and PICA-Service (breaches of the IFC) is in place to ensure any claims relating to abuse of the tied model are properly and swiftly dealt with, at least cost to all parties. Self regulation also now ensures that potential licensees have to undertake suitable pre-entry training, financial and legal advice before taking on a pub.

Version 6 of the Industry Framework Code is now in place. Our trade body BBPA spent almost a year in discussion with representatives of multiple lessees agreeing commercially sensitive changes to the Code.

A Statutory Code would also result in a two-tier resolution system with significant cost implications for all companies. This would put an inevitable strain on the voluntary system.

Q2. Do you agree that the Code should be binding on all companies that own more than 500 pubs? If you think this is not the correct threshold, please suggest an alternative, with supporting evidence.

Do not agree.

We support a 500 leased/tenanted pub threshold, but on the basis that this **does not** lead to a material distortion in competition above and below this threshold. The current proposals to abolish the machine tie and offer a guest beer (which could be the pub's best selling lager) would materially distort competition.

A threshold of 500 pubs has other unintended consequences. Managed pub companies will be liable to pay for the Adjudicator under this proposal, despite the fact that they have none, or very few leased pubs.

Q.3 Do you agree that, for companies on which the Code is binding, all of that company's non-managed pubs should be covered by the Code?

As stated above we support a leased/tenanted pub threshold (subject to the caveats surrounding distortion of competition above). The Code should only be binding on those leased/tenanted pubs owned by the company.

Q.4 How do you consider that franchises should be treated under the Code?

Business models termed as franchises do exist within the pub sector, and a number of companies have had these accredited by the British Franchise Association. If franchises are regulated under the British Franchise Association they should not be covered by any Statutory Code.

Q.5 What is your assessment of the likely costs and benefits of these proposals on pubs and the pubs sector? Please include supporting evidence.

We do not agree with the costs and benefits stated in the consultation document regarding the impact the proposals will have on the pub sector. As outlined in the introduction to this consultation response, we have a number of concerns with the evidence base for the proposals, and the assumptions made by the Government in the Impact Assessment.

The primary 'benefit' to the pub sector of the proposals is the transfer of (best estimate) £102 million from the pub owning companies covered by a Code to their licensees, working out at around £4,000 per pub. This is not justifiable or realistic in any way.

In reality there may be little, if any transfer of value if SCORFA benefits are greater than the difference in wet rent and indeed other considerations are properly taken into account. In which case there would be absolutely no justification at all for these proposals.

Therefore we do not believe the proposed calculation of "no worse off" under a Statutory Code and consequent transfer of value is an acceptable or indeed practicable proposition.

There will be costs to those companies under 500 pubs operating under the self-regulatory system, as the larger companies will no longer be part of this system. Therefore, the cost of self regulation (PIRRS/PICA-Service etc.) will go up for the smaller companies, as their share of the costs will increase with the removal of the larger players.

- **Current CAPEX investment on our 50 tenanted pubs will be £650,000 this year, and our expenditure in future years would have to be reduced if the proposals went forward.**
- **We have had one major refurbished project this year and have also spent between £8,000 and £23,000 on toilet refurbishments, porches, and smaller refurbishments on top of our decorating, lighting and signs schedule.**

Q.6 What are your views on the future of self-regulation within the industry?

We fully support self regulation within the industry, and believes great progress has been made in recent years with strong evidence that the system is working well. We are committed to ensuring that, despite Government intervention, the self regulatory system will continue.

We are committed to the Industry Framework Code and self regulation, and will aim to improve it where possible.

Q.7 Do you agree that the Code should be based on the following two core and overarching principles?

i. Principle of Fair and Lawful Dealing

We are totally committed to fair, transparent and lawful dealing with tenants and lessees and all other business partners and to stamping out any abuse of the tied pub model, as has been proved by take-up of the self regulatory system.

ii. Principle that the Tied Tenant Should be No Worse Off than the Free-of-tie Tenant

To retain and attract effective licensees, pub owners need to demonstrate that tied tenants are no worse off than free-of-tie tenants and we support further transparency in this area. Individual pubs are however unique and the proposed mandating of individual benefits (SCORFA) and linking to rent calculations is likely to be unwieldy, complicated and is not practicable.

It should also be noted that the rent of free-of-tie outlets are often set with a lack of knowledge regarding outlet performance and limited information due to the arms-length relationship between the lessee and the pub company. Free-of-tie rents will also be impacted by the economic climate, availability and cost of finance to purchase freehold premises.

Q.8 Do you agree that the Government should include the following provisions in the Statutory Code?

i. - Provide the tenant the right to request an open market rent review if they have not had one in five years

Agree.

- if the pub company significantly increases drink prices or if an event occurs outside the tenant's control.

We would welcome further definition around what constitutes an event outside of the tenant's control.

ii. Increase transparency, in particular by requiring the pub company to produce parallel 'tied' and 'free-of-tie' rent assessments so that a tenant can ensure that they are no worse off.

We support greater transparency of SCORFA benefits which would highlight the key benefits of the tied model to prospective tenants and lessees at rent assessment time.

iii. Abolish the gaming machine tie and mandate that no products other than drinks may be tied.

Do not agree.

We would support a free-of-tie option on AWP machines, whereby tenants and lessees could choose whether to take up the offer of a machine supply agreement with a company rather than closing this option off completely. Indeed, this is the case already with most major pub companies where tenants do not have to tie for machines, but are given the option of doing so. As noted above, lessees of companies with less than 500 would still be able to take up a tied machine offer if they so wish leading to disparity of competition in the pub machine sector.

There is a real concern that removing the tie would encourage the spread of criminal behaviour by unscrupulous suppliers of gaming machines and potentially a lack of understanding of the regulations regarding the control and taxation of Category C gaming machines in pubs.

A further point to note is that if the tenant went free of tie on machines then the income from the machine would be included as part of the divisible balance and therefore taken into account when the rent levels were assessed – whereas under the current tied model income from machines (IFC v.6) cannot be included in the divisible balance. This could result in licensees being no better off under free of tie proposals as the cashbox would be rentalised.

iv. Provide a 'guest beer' option in all tied pubs.

Do not agree.

The 'guest beer' option is defined as 'the tenant should be allowed to purchase and sell one draught beer from any source'. The consultation document justifies the inclusion of such an option by claiming 'it may be of benefit to both the tenant, consumer and independent breweries'. There is no evidence to support this assumption and it would lead to competition issues where pub companies brew their own beer. We already offer a wide variety of choice for tenants within their existing supply agreements.

v. Provide that flow monitoring equipment may not be used to determine whether a tenant is complying with purchasing obligations, or as evidence in enforcing such obligations

Do not agree. There is no evidence presented in the consultation as to why flow monitoring equipment should not be used as part of the process to determine if a tenant is not complying with purchasing obligations.

Q.9 Are there any areas where you consider the draft Statutory Code (at Annex A) should be altered?

We have dealt with a number of the issues raised by the proposed Code in answer to the questions above. We leave it for the BBPA to comment in more detail.

Q.10 Do you agree that the Statutory Code should be periodically reviewed and, if appropriate amended, if there was evidence that showed that such amendments would deliver more effectively the two overarching principles?

Yes.

Q.11. Should the Government include a mandatory free of tie option in the Statutory Code?

No.

We do not agree that a mandatory free of tie (FOT) option should be included in the Statutory Code. A mandatory FOT option would have serious unintended consequences for the entire pub sector, a number of which are identified in the consultation:

- 'In the short term there will be higher costs as a result of lost economies of scale...these are likely to fall disproportionately on lower volume pubs...this may also lead to some pubs becoming unviable and closing'
- 'Choice is likely to suffer' as market could be foreclosed by large international brewers offering limited brands
- 'Removing the surety of the tie would reduce pub owning companies' incentive to invest'

- 'The impacts could include higher costs for consumers, the exit of one of the major pub owning companies and/or dominance of the market by large international brewers'

We would agree with the Government that the chances of the above happening are high. Consequences of losing the tie on a large scale would also be likely to include:

- Increased pub closures and subsequent impact on employment (both direct and indirect);
- A negative impact on pub sales and property value;
- Less people entering the sector;
- Less choice of brands in those pubs that remain for the consumer;
- Closure of breweries and/or breweries divesting their pub estates,
- Denying small brewers a (currently effective) route to market
- Closure of our distribution depot with the loss of most of our staff.
- Possibly make it unviable for the business to run at all, leading to sale of the business with total loss of jobs.

Q.12 Other than (a) a mandatory free-of-tie option or (b) mandating that higher beer prices must be compensated for by lower rents, do you have any other suggestions as to how the Government could ensure that tied tenants were no worse off than free-of-tie tenants?

We believe that the self regulatory system and SCORFA already delivers this.

Q.13 Should the Government appoint an independent Adjudicator to enforce the new Statutory Code?

Under the IFC, PICA-Service already provides an independent conciliation and arbitration service for complaints around company conduct, and PIRRS for rent reviews.

Q.14 Do you agree that the Adjudicator should be able to:

(i) Arbitrate individual disputes?

We would point out that there are already a number of services that are available to tenants to arbitrate disputes:

- PICA-Service (disputes relating to breaches of the IFC)
- PIRRS (disputes relating to rent reviews)
- Via the court system over contractual disputes
- Other established arbitration bodies (ACAS)

(ii) Carry out investigations into widespread breaches of the code?

Investigations into breaches of the Code would have to be based on sound evidence, and specify where exactly the Code has been breached. Systems should be in place to prevent vexatious and speculative complaints being escalated, with the resultant time and financial cost of unnecessary investigations.

Q.15 Do you agree that the Adjudicator should be able to impose a range of sanctions on pub companies that have breached the Code, including:

(i) Recommendations

(ii) Requirement to publish information ('name and shame')

(iii) Financial penalties

The consultation contains no detail of appeals process for companies, recourse to such a system should be in place to prevent unfair decisions being reached.

Q.16 Do you consider the Government's proposals for reporting and review of the Adjudicator are satisfactory?

We leave it to the BBPA to comment in more detail.

Q. 17 Do you agree that the Adjudicator should be funded by an industry levy, with companies who breach the Code paying a proportionally greater share of the levy? What, in your view, would be the impact of the levy on pub companies, pub tenants, consumers and the overall industry?

The impact on the industry and consumers of setting up such an Adjudicator should be as limited as possible. As stated above, we believe the cost estimates of such a regulator are too low. There is the danger of regulatory creep by such a body, and suggest a cap of the budget of the Adjudicator to minimise the impact on the pub sector.

The Levy as proposed will be paid by pub companies covered by the Code, in proportion to number of pubs owned. In second and subsequent years of the levy, it is suggested that those who breach the Code pay more. However, this still does not address managed companies and FOT companies having, as proposed, to pay into the Adjudicator system despite having no pubs that are actually covered by the provisions.

Thank you for taking the time to read our letter.

Yours Faithfully