

BIS | Department for Business
Innovation & Skills

**PUB COMPANIES AND TENANTS:
A GOVERNMENT CONSULTATION**

22 APRIL 2013

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Pub Companies and Tenants

Explanation of the wider context for the consultation and what it seeks to achieve

The Government seeks to support a healthy, thriving and diverse pubs sector. One longstanding issue in the sector is that, for many years, serious concerns and numerous complaints have been raised about the relationship between large pub companies and their tenants. The focus has been on tied pubs and the share of reward gained by pub owning companies, for example through large unjustified rent increases.

Such behaviour is possible due to pub companies' better access to information and resources. The tie gives an additional route of abuse and complicates the relationship. Tied tenants are also more likely to face serious hardship. A self-regulatory approach has been tried since at least 2004, with a last chance given in 2011, but this has not worked. As such the Government is now proposing to legislate.

As part of its overall aim to secure a healthy pubs industry, the Government's key objective is to ensure that tenants are treated fairly and that tied tenants are no worse off than free-of-tie tenants. Accordingly, the Government is:

- **Proposing to establish a Statutory Code and an independent Adjudicator to enforce that Code.**
- **Setting out proposals as to how 'a tied tenant should be no worse off than a free-of-tie tenant' should be interpreted in calculating rents.**
- **Asking an open question as to whether the Code should include a mandatory free-of-tie option.**
- **Proposing that the Code should apply to all pub companies with over 500 pubs.**

The Government welcomes views on these proposals.

Issued	22 April 2013
Respond by	14 June 2013
Enquiries to	pubs.consultation@bis.gsi.gov.uk

This consultation is relevant to businesses of all sizes in the pub sector, trade associations in the pub sector, economic bodies, surveyors, consumers and consumer organisations.

Foreword from the Secretary of State

Pubs are a significant part of our national heritage, and the Government is keen to support pubs and the pubs sector. One key industry issue over the last decade has been concerns about the fairness of the relationship between large pub companies and their tenants. It has become clear to me that the self regulatory approach, which was announced by the Government in November 2011, has not been sufficiently far-reaching, with many individual publicans continuing to face significant hardships and difficulties. Therefore, further Government action is required in order to maintain a level playing field in the business environment.

The pub industry faces a wide range of challenges and the number of pubs has declined from 70,000 in 1980 to approximately 50,000 today. At present, 18 pubs (net) are closing every week. Whilst the financial crisis has brought into stark relief the slow process of sectoral decline, it is undoubtedly the case that the activities of the major pub companies, with their highly leveraged business model, have intensified the crisis.



With the banking collapse and subsequent recession, the weakness of companies with high debt-to-equity ratios has been rather brutally exposed. What we have seen in recent years is some pub companies trying to retrieve their financial position at the expense of their tenants. We are all familiar with well managed, popular pubs in our constituencies being driven to the wall by, frankly, exploitative financial practices.

Although some pub companies behave well, the evidence I have received makes it clear that in too many cases tenants are being exploited and squeezed, through a combination of unfair practices, lack of transparency and a focus on short-termism at the expense of the long-term sustainability of the sector. This behaviour, especially alongside the many other challenges facing the sector, risks damaging the British pub industry, which not only consists of small businesses employing hundreds of thousands of people across the country but also contributes substantially to community spirit and cohesion.

After considering the various options, I have therefore decided to consult on establishing a Statutory Code and an independent Adjudicator for the pubs sector to govern the relationship between large pub companies and their tenants. At the heart of this intervention I propose to establish both an overarching fair dealing provision and the core principle that 'a tied tenant should be no worse off than a free-of-tie-tenant', enshrined in statute.

I would like to be clear that I am not proposing to abolish the beer tie. When operated as envisaged and fairly, it is a valid business model being used responsibly by companies both large and small. Were it to be removed, the British brewing industry could be significantly disadvantaged. What is clear is that it is the abuse of the tie, like the abuse of rent calculations and other factors, that is causing problems in certain circumstances.

Accordingly, the Government's goal is simply to ensure that 'the tied tenant should be no worse off than a free-of-tie tenant'. This consultation therefore asks an open question as to how best to achieve this, whether by a mandatory free-of-tie option or alternatively by mandating that higher beer prices must be compensated for by lower rents, or by other means.

The Government is committed to ensuring a fair deal for tenants and I look forward to hearing from all those who have a view on how to achieve this.

1 Executive Summary

The Government is keen to support a thriving and diverse pubs sector. One longstanding issue in the industry are the serious concerns and numerous complaints raised about the relationship between large pub companies and their tenants¹. The focus has been on tied pubs and the share of reward gained by pub owning companies, for example through large unjustified rent increases. Such behaviour is possibly due to pub companies' better access to information and resources. The tie gives an additional potential route of abuse and complicates the relationship. Evidence indicates that tied tenants are also more likely to face serious hardship. A self-regulatory approach has been tried since at least 2004, with a last chance given in 2011, but this did not work. As such the Government is now proposing to legislate to ensure that the pubs sector operates more fairly.

The Government is proposing to establish a Statutory Code and an independent Adjudicator for the pubs sector to govern the relationship between large pub companies and their tenants.

The proposed Code will use the existing Industry Framework Code as a starting point, but it will be strengthened to include both an overarching fair dealing provision and also the principle that 'a tied tenant should be no worse off than a free-of-tie-tenant.' This will have particular significance with regards to rents, as the consultation will propose that guidance issued by the Royal Institute of Chartered Surveyors must be interpreted in the light of that principle.

The Government asks an open question as to how best to achieve these core principles, whether by mandating that higher beer prices must be compensated for by lower rents, by a mandatory free-of-tie option, or by another means. The consultation also asks whether the Code should be strengthened in other areas to help ensure a fair balance of reward between pub companies and tenants and discusses issues including a guest beer option, the gaming machine tie, transparency, flow monitoring equipment, and the right to request rent reviews. We are keen to understand how these proposed changes will affect all elements of the pubs industry, including individual pubs, brewers, distributors and pub companies of all sizes, and would welcome evidence from across the sector. Such evidence will be very valuable in informing the development of policy and potential legislation in this area.

The proposed Adjudicator will be based on the model of the widely-welcomed Groceries Code Adjudicator, and will have the power and function to:

- arbitrate individual disputes between large pub companies and their tenants, including about whether or not a rent review has genuinely been conducted on an 'open market' basis, in accordance with the new statutory Code;

¹ By 'tenant', the Government is referring to any publican who rents their pub from a larger company, whether they are referred to as a tenant, a lessee or by any other term.

- carry out investigations based on complaints that have been received, and have wide-ranging powers to require information from pub companies during an investigation;
- where an investigation finds that a pub company has breached the Code, impose sanctions – including, in the case of severe breaches, financial penalties – on that company;
- Publish guidance on when and how investigations will proceed and how these enforcement powers will be used;
- Advise pub companies and tenants on the Code;
- Report annually on his or her work;
- Recommend changes to the Code.

In order to place the most proportionate burden on business, the Government is proposing that this new regulatory regime should apply to all pub companies with more than 500 pubs. For companies covered by the Code, the Code would then apply to all of their non-managed pubs. This approach would target those companies with the greatest market power and exempt smaller companies, about whom very few complaints have been received.

2 How to respond

The consultation will begin on 22nd April 2013, and will run for eight weeks, closing on 14th June 2013.

When responding please state whether you are responding as an individual or representing the views of an organisation. If you are responding on behalf of an organisation, please make it clear who the organisation represents by selecting the appropriate interest group on the consultation response form and, where applicable, how the views of members were assembled.

A copy of the Consultation Response form is available electronically at <https://www.gov.uk/government/publications> (until the consultation closes). If you decide to respond this way, the form can be submitted by letter or email to:

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

Email: pubs.consultation@bis.gsi.gov.uk

A list of those organisations and individuals consulted is in Annex B. We would welcome suggestions of others who may wish to be involved in this consultation process.

Additional copies

You may make copies of this document without seeking permission. Further printed copies of the consultation document can be obtained from:

BIS Publications Orderline
ADMAIL 528
London SW1W 8YT
Tel: 0845-015 0010
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Minicom: 0845-015 0030
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Other versions of the document in Braille, other languages or audio-cassette are available on request.

Confidentiality & Data Protection

Information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data, that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

Help with queries

If you have questions about the policy issues raised in this document, please use the contact details above.

What happens next?

Following the close of the consultation period, the Government will publish all of the responses received, unless specifically notified otherwise (see data protection section above for full details).

The Government will, within 3 months of the close of the consultation, publish the consultation response. This response will take the form of decisions made in light of the consultation, a summary of the views expressed and reasons given for decisions finally taken. This document will be published on www.gov.uk with paper copies available on request.

Comments or complaints

If you wish to comment on the conduct of this consultation or make a complaint about the way this consultation has been conducted, please write to:

John Conway
BIS Consultation Co-ordinator,
1 Victoria Street,
London
SW1H 0ET

Tel: 020 7215 6402
Email: John.Conway@bis.gsi.gov.uk

3 Why is Government Considering Action?

3.1 Over the past decade, increasing concerns have been raised about the operation of the pub industry, particularly focusing on the relationship between large pub companies and their tenants². Four successive Select Committee Inquiries, in 2004, 2009, 2010 and 2011, have identified significant problems within the industry. Self-regulation has been tried throughout that time and, in November 2011, the Government announced that it was giving the industry one last chance to deliver a self-regulatory approach that would address the problems.

3.2 Following a call for evidence in October 2012, it has become clear that the self-regulatory approach has not been sufficiently far-reaching. There has been a lack of necessary culture change within the industry, with no concerted, long-term effort made to inform tenants of their rights and discussions on future progress deadlocked on numerous issues. Although many pub companies treat their tenants well, in far too many cases it appears that publicans continue to be treated unfairly and suffer significant hardship.

3.3 The British Institute of Innkeepers has received over four hundred complaints on its hotline over the past three years. Some of these complaints were on other issues, but the vast majority were about pub-owning companies with large numbers of tied pubs. There are also several other people (usually current or former tied tenants) who act independently and estimate they receive over 10 cases a week that directly relate to the “Pubco model”. Additionally there have been numerous letters to MPs and representations to BIS Select Committee. Even accounting for some overlap, overstatement and mis-categorisation, there are hundreds of complaints per year and these are just those where mistreatment is actually reported.

3.4 Examples of the types of unfair behaviour that have been reported to the Government include: tenants at rent review being told of large rent increases without justification; misleading estimates of potential sales; and overvaluing additional services provided such as business development advice. Such behaviour is possibly due to imbalance in the relationship between the two parties – pub-owning companies have access to more information and resources than tenants. The large pub-owning companies have a better idea of what is particular to a pub and what is a market wide phenomenon. They can also afford legal and surveyor fees more easily.

3.5 This problem can be exacerbated by tenants who go into the pub sector as a ‘lifestyle choice’ rather than as a commercial business decision³. Many publicans do not shop around for pubs or invest based on business

² By ‘tenant’, the Government is referring to any publican who rents their pub from a larger company, whether they are referred to as a tenant, a lessee or by any other term.

³ In one CGA survey 73% of respondents only looked at one pub owning company when deciding which pub to rent.

reasons; rather they choose a pub they like or on the basis of the attached living accommodation. There have also been concerns raised regarding the chronically low levels of literacy and numeracy amongst tenants⁴. The tie gives an additional route of abuse as beer prices are changed more frequently than rents. The tie also complicates the relationship, making it tougher for tenants to know if they are getting a good deal.

3.6 Tied tenants are also more likely to face serious hardship - 46% of tied publicans earn less than £15,000 a year, compared to just 23% for tenants who are free-of-tie. Although the tie is not universally bad – the latest independent annual survey, conducted by CGA strategy, showed 7 out of 10 tenants would sign up again with their pub owning company – the fair working of the beer tie is particularly important because of the hardship many publicans face including the possibility of losing their home (which is the pub).

3.7 It has therefore become clear that further Government action is needed to address this situation and create a level playing field in the business environment.

Aims

3.8 The Government's aim is to ensure fairness for tenants, to ensure that tied tenants are treated no less favourably than free-of-tie tenants and to support the continuation of pubs as valuable community assets. We also want to safeguard the long term stability and sustainability of the industry, through proportionate and targeted interventions where needed.

3.9 The Government would like to be clear that this is not a competition issue. In 2010, the Office of Fair Trading (OFT) found that *“At a national, regional and local level, the evidence indicates that there is a large number of competing pub outlets owned by different operators and that there is competition and a choice between different pubs.”* Importantly they also said *“Given that we have found that consumers are benefiting from a significant degree of competition and choice between pubs, we do not consider that issues relating to the negotiation process between pub companies and lessees can generally be expected to result in consumer detriment.”*

3.10 The Government is therefore intervening not on grounds of competition, but on grounds of fairness for tenants. Although it is clear that the tie can be a good business model when operated responsibly, abuse of the tie can cause serious hardship.

3.11 The Government's aim is to regulate proportionately. We will be careful to ensure that measures taken are proportionate, targeted and fair; to ensure those who are currently being treated unfairly are protected, and not to place an undue burden on the companies who are currently treating their tenants

⁴ <http://www.morningadvertiser.co.uk/General-News/BII-we-must-raise-literacy-and-numeracy>

fairly. A responsibly operated pub industry, the safeguarding of valuable community assets and the support of the British brewing industry will all contribute to the long-term sustainability of the brewing and pub sector.

Proposals

3.12 The Government's proposals are to ensure that tenants are treated fairly and that a tied tenant should be no worse off than a free-of-tie tenant ('the core principles').

3.13 The Government is proposing that this should be achieved by means of a Statutory Code, with the above principles at the heart of it, together with an Adjudicator to enforce that Code. The content of the Code and powers of the Adjudicator are discussed in detail in the relevant chapters of this consultation.

Impact

3.14 The main benefit and aim of the policy is the estimated transfer from pub owning companies to tenants of £102m per year. Increasing tenants' share of profits is likely to have a small positive impact on investment and the long term health of the pubs industry. The total net cost to business is estimated at approximately £2m per year, a cost which would fall on the large pub companies, due to compliance costs and the Adjudicator levy. The impact is set out in greater detail in the Government's Impact Assessment available at <https://www.gov.uk/government/publications>.

3.15 It is our assessment that no pubs should become unviable as a result of this policy, as profit is only moved from one party to another. If a pub had been viable prior to the policy, it is our view that the tenant and pub owning company could reach a commercial negotiation that maintained the pub's viability.

3.16 However, the Government is very keen to understand the likely costs and benefits of these proposals to the pubs industry overall. The aim of this consultation is to gather further views and evidence around these proposals, which will be used in a further iteration of the overall Impact Assessment and to inform the development of policy and possible legislation. In particular, we would welcome evidence from the industry on the likely impact of these proposals on their business, specifically including costs and benefits, and whether they would affect the rate of pub closures.

Wider context

3.17 The pub industry faces a range of pressures including the current economic climate, the impact of the smoking ban, competition from supermarkets, improving home entertainment, social and demographic changes and a trend towards drinking alcohol at home. Beer sales in pubs are declining. There has been a big contraction in the industry over the last three decades: from 70,000 pubs in 1980 to around 50,000 today. Over the last six months 18 (net) pubs have closed every week. The Government recognises

that this consultation will only address one part of the challenging situation facing pubs.

3.18 Equally, this is only one part of a wider range of measures that the Government is taking to support pubs and the pubs sector. In the Budget on 20th March 2013, the Government announced that it would be abolishing the beer duty escalator and cutting beer duty this year, reducing the tax on a typical pint by one penny, a decision that will have a significant impact on the beer industry.

3.19 Furthermore, in December 2012 the Government announced £150k funding for Pub is the Hub, an organisation that works with tenants, pub owners and communities to support, retain and locate local services, where possible, within pubs. The Government has also given communities, through the Community Right to Bid, a fairer chance to take over local assets of value to them, including pubs, whilst the National Planning Policy Framework makes clear that local planning policies and decisions should guard against the unnecessary loss of facilities such as pubs. The Live Music Act 2012 now makes it easier for pubs to host live music events; recent changes in corporation tax, gaming machine regulation, national insurance (making it cheaper to employ people on incomes below £21,000) and the doubling of the level of small business rate relief for a further year will all further benefit the sector.

4 A Statutory Code and Adjudicator

The Government is proposing to establish a Statutory Code and Adjudicator in order to ensure that tenants are treated fairly and that tied tenants are no worse off than free-of-tie tenants.

The Government is seeking views on:

- **Whether to establish a Statutory Code and Adjudicator;**
- **Which pub companies the Code should apply to;**
- **For pub companies that the Code applies to, which pubs the provisions of the Code should apply to;**
- **Whether a distinction should be made between leases and tenancies, and how franchises should be treated;**
- **The future of self-regulation.**

4.1 As discussed in the previous chapter, the key issue is to achieve fairness for tenants, in particular by ensuring that the tied tenant is no worse off than the free-of-tie tenant. The challenge is to do this in a way that is both effective and proportionate.

4.2 The Government recognises that the current self-regulatory approach has delivered some benefits. In particular, the self-regulatory Code has delivered some helpful benefits to tenants, particularly in areas such as transparency and pre-entry training; the Royal Institute of Chartered Surveyors' (RICS) guidance, where it is followed, is a very helpful step forward⁵ and the dispute resolution services of the Pubs Independent Rent Review Scheme (PIRRS) and the Pubs Independent Conciliation and Arbitration Service (PICAS) have provided a means for at least some tenants to cost-effectively resolve disputes and obtain redress.

4.3 However, the current system has not done enough. As the Government has said previously⁶, too many tenants continue to be badly treated and are suffering hardship. There has been a lack of the necessary culture change within the industry, with no concerted, long-term effort made to inform tenants of their rights and discussions on future progress deadlocked on numerous issues.

⁵ The BIS Select Committee, in 2011, described it as “one of the few positive messages to come out of the 2010 report on pub companies”

⁶ Secretary of State Vince Cable's letter to the BIS Select Committee, 8 January 2013

4.4 There are also more fundamental limitations to the self-regulatory approach. Both pub companies and tenants have now accepted that a self-regulatory code cannot address the fundamental issue of the balance of risk and reward between pub companies and tenants. Furthermore, the self-regulatory approach relies too heavily on the ability of individual tenants to know their rights and to be able to take their own case to PIRRS or PICAS.

4.5 Accordingly, the Government therefore considers that a legislative approach, based on a Statutory Code enforced by an Adjudicator, would be more effective in delivering the needed change and ensuring fair treatment for tenants.

A Statutory Code and Adjudicator

The Code

4.6 At the heart of the proposed solution will be a Statutory Code, setting out how pub companies must treat their tenants. Although the current Industry Framework Code (Version 6)⁷ provides a starting place for the Statutory Code, it is clear that any Statutory Code will need to be significantly strengthened in order to address the fundamental issues of risk and reward, and to ensure the core principles of fairness and that the tied tenant must be no worse off than the free-of-tie tenant.

4.7 A draft Statutory Code can be found at Annex A of this consultation document; the proposed content of the Code, including whether or not a mandatory free-of-tie option should be included, is discussed further in the next chapter.

The Adjudicator

4.8 The Code would be enforced by an Adjudicator. The Government proposes that the Adjudicator should be based on the model of the widely welcomed Groceries Code Adjudicator⁸ and, accordingly, would have two main functions.

- a. Arbitration function. The arbitration function would be about delivering redress to individual tenants. Essentially, the Adjudicator would be able to deliver an open market rent review, in accordance with RICS guidance and the Statutory Code, to ensure that the rent had been calculated fairly and not artificially inflated. Any tenant dissatisfied with how their rent had been calculated could take their pub company to the Adjudicator for arbitration.

⁷ <http://s3.amazonaws.com/bbpa-prod/attachments/documents/resources/21811/original/UK%20Pub%20Industry%20Framework%20Code%20Version%20Six.pdf?1360685239>

⁸ <http://services.parliament.uk/bills/2012-13/groceriescodeadjudicator.html>

- b. Investigation function. The Adjudicator would be able to undertake proactive investigations provided they had reasonable grounds to suspect that a pub company was breaching the Code. During an investigation the Adjudicator would have strong powers to require information from pub companies and, if the pub company was found to be in breach, could impose sanctions, including financial penalties. As discussed in Box 1, the Government considers that this proactive investigatory function is absolutely fundamental to the effective enforcement of the Code.

Box 1: Importance of the Investigatory Function

The Adjudicator's power to investigate will allow him or her to tackle systematic breaches of the Code that could not be solved by individual tenants going for arbitration.

Example 1: Pre-entry training

Suppose a pub company was not providing tenants with pre-entry training or telling them of their rights under the Code. The tenants would not know of their rights under the Code so would never go to arbitration – however, the Adjudicator could investigate, detect the problem and impose sanctions.

Example 2: Inflating turnovers

Suppose a pub company was charging unfair rents by systematically inflating the expected turnover of its pubs at rent review. This could be hard to detect for an individual pub as there may be many reasons why a pub's turnover could be less than projected. However, the Adjudicator would be able to require the pub company to provide information from 200 pubs: if 80-90% of them were trading below the projected turnover, it would be very likely that this would constitute a breach of the Code, which would allow sanctions to be imposed.

4.9 The powers of the Adjudicator are discussed in more detail in Chapter 6.

4.10 The overall intention of the Government's proposed approach is that pub companies who are already treating their tenants fairly and are complying with the Code should face minimal impact. Conversely, any companies that are abusing or exploiting their tenants will have to make rapid and substantial improvements.

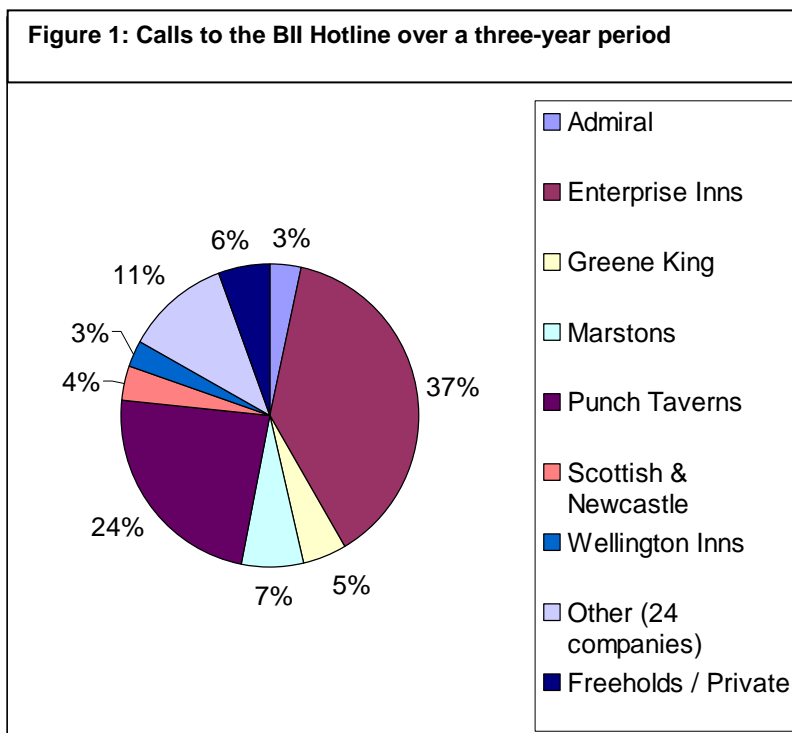
Which companies should the Code apply to?

4.11 In accordance with its wider goals to reduce regulation, the Government wishes to regulate only as much as is necessary to achieve its objectives, as well as to minimise any burden on companies which have acted responsibly. The Government therefore proposes that the Statutory Code should only be binding on pub companies which have 500 or more pubs, thereby targeting the companies with the greatest market power and exempting smaller companies, about whom very few complaints have been received and who, from the evidence received thus far, are widely recognised as behaving responsibly.

4.12 In choosing the figure of 500 pubs, the Government has been mindful of the fact that significantly fewer complaints have been made about companies below this level. Figure 1 shows the number of calls made to the British Institute of Innkeeping (BII) hotline over a three year period.

Although such calls will not, of course, represent the full scale of the problem, it is reasonable to consider that the relative proportion of calls reflects those of the industry as a whole.

4.13 Figure 1 shows clearly that by far the greatest number of calls, either absolutely or proportionately, concerned the largest two companies. Just over 20% of calls concerned the next largest five companies. Only 11% of calls were made about companies with fewer than 500 pubs and no more than five calls were made about any single company in this category over the five year period.



4.14 By setting the threshold at 500 pubs, the Code would therefore be able to address the companies about whom almost 90% of the calls cover.

4.15 A further salient point that has informed the Government’s proposal is that 500 pubs is approximately 1% of the pubs market. Restricting the scope of a Statutory Code to companies with more than 500 pubs focuses it on those businesses who have the greatest market power and who are also better able to bear the compliance costs, without unduly burdening smaller businesses. The Government further notes that a wide range of stakeholders, including the Independent Pubs Confederation (IPC), the Campaign for Real Ale (CAMRA) and the All-Party Parliamentary Save the Pubs Group (APP-STPG) have previously called for a 500 pub threshold to statutory Government intervention.

4.16 The Government considers, therefore, that the 500 pubs threshold is a proportionate response to address the problem, but is very keen to seek views and evidence of the impact and consequences of this threshold on the sector.

4.17 The Government does recognise that, based on the evidence above, some large pub companies appear to be treating their tenants significantly better than others. To recognise this fact, the Government proposes that those companies which are found to have breached the Code more frequently should pay a proportionately higher levy towards the costs of the Adjudicator. This is discussed in more detail in Chapter 6.

A Lease/Tenancy Distinction?

4.18 The Government recognises that there are significant differences between what are commonly known as “leases” and “tenancies” in the pub industry. Leases tend to be for 15-25 years, fully repairing and assignable, whereas tenancies tend to be of much shorter, often under 5 years duration, unassignable but with an easy exit clause and with the repairs met by the pub company.

4.19 The Government further recognises that the traditional tied tenancy model, as operated in particular by the family brewers but also by some larger companies, has a long and honourable history in the British pub industry. This was acknowledged in the Government’s response to the BIS Select Committee in November 2011⁹, as well as by bodies such as the predecessor to that Select Committee in their 2010 report, which stated that “*We have received no evidence to suggest that the tie is a cause of controversy or dispute between smaller family and regional brewers and those who operate their tied estate*”¹⁰ and by CAMRA: “*Without the right to tie pubs, the Family Brewers wouldn’t bring their beers to the bar. Closures amongst the smaller brewers would be inevitable. The tie is a viable way for them to run their pubs.*”¹¹

4.20 That having been said, the Government considers that it would be very difficult to make a distinction in legislation, between a “lease” and a “tenancy”, based on the pub industry definition of those terms; they are not definitions which are currently set out in legislation and they feature a multiplicity of different characteristics. The proliferation of alternative business models, such as franchises and ‘tenancies at will’, adds further complexity to the issue. The risk of drawing a distinction is that pub companies might seek to circumvent the Code, avoiding its provisions, by making small contractual changes to their leases which would not in reality benefit tenants.

4.21 The Government therefore considers that no difference should be made between “leases” and “tenancies”, though acknowledges that the question of franchises is more complex. It considers that, where tenancies are operated fairly, in accordance with the “tenancy” model as genuinely applied, it is likely that these will satisfy the provisions of the proposed Statutory Code and that there will therefore be little impact on the companies that operate such agreements. For the avoidance of doubt, reference to “tenants” in this consultation document should be taken to include “lessees”.

How would the Code be applied?

⁹ Particularly in the case of the traditional tenancy model, the tie may actually play an important role in safeguarding the future of Britain’s smaller breweries

¹⁰ <http://www.publications.parliament.uk/pa/cm200910/cmselect/cmbis/138/138.pdf>

¹¹ Mike Benner, Chief Executive, CAMRA, quoted in ‘What the Tie Means to the Family Brewers’ (January 2011)

4.22 As discussed, the Government proposes that the Code should apply to all companies which own more than 500 pubs. It is clear that this definition should apply at the level of the top company within a group, to avoid pub companies seeking to evade the provisions of the Code by creating a number of smaller companies within a group structure, each containing, for example, 450 pubs.

4.23 For companies with 500 or more pubs, the provisions of the Code would cover all of the company's non-managed pubs. It would not make sense to apply the Code in managed pubs, as these pubs are run by a manager who will be an employee of the pub company, rather than by a tenant leasing the pub from the pub company.

4.24 The provisions of the Code would cover all non-managed pubs, not just all tied pubs, for two reasons:

- a. Firstly, whilst the principle that 'the tied tenant should be no worse off than the free-of-tie tenant' has an impact only on tied pubs, the principle that all tenants should be treated fairly is applicable to all non-managed pubs;
- b. Secondly, were the Code to cover only tied pubs, there would be nothing to stop a pub company from removing the tie and immediately increasing the rent to well beyond market rent values. If the Code only covered tied pubs, such a circumstance would fall outside the scope of the legislation, which is clearly undesirable.

4.25 The Statutory Code would be immediately binding on all pub companies above the statutory threshold and would supersede the terms of any lease or tenancy agreement in cases where the Code and the lease or tenancy agreement were in conflict. Companies would also be required to incorporate the Code into lease and tenancy agreements, to ensure that tenants were aware of their rights.

4.26 As discussed in the next chapter, the Government proposes that it should be possible for the Secretary of State, following a review, to amend the minimum threshold if there is evidence that this is needed.

Q.1 Should there be a statutory Code?

Q. 2 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 any supporting evidence.

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?

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

Future of self-regulation

4.27 As discussed, the Government recognises that self regulation has had some positive impact on the industry. The Government would therefore strongly support it continuing until such time as a statutory solution can be put into place, in particular with regards to the application of the Industry Framework Code and the operation of PIRRS and PICAS.

4.28 Furthermore, the Government considers that it would be strongly beneficial if companies with fewer pubs than the statutory threshold continued to operate a self-regulatory regime, in particular with regards to the creation of company codes and their certification by an appropriate body such as the British Institute of Innkeepers. The Government considers that whether or not smaller companies were willing to operate such a regime is likely to influence its decision of whether to set a statutory threshold for the Code of 500 pubs.

4.29 The Government recognises the positive role that PIRRS and PICAS have played in resolving disputes and would not wish to discourage these bodies from continuing to operate after the proposed Adjudicator had been established. In this way, a tenant would have the option of going either to the Adjudicator or alternative dispute resolution mechanisms, thereby introducing a degree of healthy competition into the dispute resolution market.

4.30 Alternatively, and recognising the cost to the industry of these services, the Government suggests that an alternative might be for companies below the threshold to voluntarily commit, in their contracts with tenants, to use the arbitration function of the Adjudicator to resolve disputes. Such disputes would be arbitrated on the basis of the contractual terms and conditions, including any terms found in the company code, and the companies would not be subject to the wider compliance or investigatory parts of the regime.

4.31 The Government would welcome the views of those within the industry on the possible future of self-regulation.

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

5 Content of the Proposed Statutory Code

The Government considers that the proposed Statutory Code should be based on two overarching principles: that tenants should be treated fairly and lawfully and that tied tenants should be no worse off than free-of-tie tenants. The Code will therefore need to explicitly address issues of risk and reward.

The Government is seeking views on:

- **Whether the overarching principles of the Code are correct;**
- **Whether the Code should include a mandatory free-of-tie option;**
- **Other possible ways of ensuring tied tenants could be made no worse off than free-of-tie tenants;**
- **Whether the Code should address other issues related to risk and reward including:**
 - **The right to request open market rent reviews;**
 - **Transparency;**
 - **The gaming machine tie;**
 - **A guest beer option;**
 - **Flow monitoring equipment.**
- **How the Code could be amended.**

5.1 In order for a statutory Code to effectively ensure that tenants are treated fairly, the contents of the Code must be right. In particular, this means that the Code must explicitly address issues of risk and reward, to ensure that this is shared at an appropriate level between pub companies and tenants, and that tied tenants are no worse off than free-of-tie tenants.

5.2 Although Version 6 of the Industry Framework Code contains a number of valuable provisions that are of use to tenants, in particular in the area of pre-entry training and transparency¹², it does not go far enough in the area of risk and reward. The Government therefore considers that, whilst a statutory Code

¹² "The Association of Licensed Multiple Retailers (ALMR) has endorsed version 6 claiming that it is 'immeasurably better': <http://www.morningadvertiser.co.uk/General-News/BBPA-publishes-Version-6-of-the-Industry-Framework-Code>

may use Version 6 as a starting point, it must be strengthened considerably if it is to achieve the Government's policy aims.

Core Principles (paragraphs 2-4 of the Code)

5.3 The Government proposes that at the heart of the statutory code should be two core and overarching principles. The Code would state that any other provision of the Code must be interpreted in the light of these core principles and that any pub company that acted in a way that contravened one of the core principles would be automatically in breach of the Code. The proposed core principles are:

- i. Principle of Fair and Lawful Dealing;
- ii. Principle that the Tied Tenant Should be No Worse Off than the Free-of-tie Tenant.

Principle of Fair and Lawful Dealing

5.4 This principle would put an overarching obligation on pub companies to treat their tenants fairly and lawfully. Key aspects of the provision, other than fairness, include the need to cover formal and informal arrangements, the need to avoid duress and the need to provide tenants with clear information. The requirement to treat tenants lawfully means that any unlawful behaviour by a pub company towards a tenant becomes *de facto* a breach of the Code, enforceable by the Adjudicator.

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

5.5 This principle would mean that in all its dealings with tenants, a pub company should ensure that a tied tenant was not disadvantaged compared to a free-of-tie tenant. With respect to rental calculations, the Government considers that the Code would also need to spell out precisely how this was to be interpreted, with respect to the balance between dry rent, wet rent and genuinely quantifiable SCORFA¹³.

5.6 How this would work is set out in detail in paragraph 22 of the Code and is also discussed further below.

5.7 The Government proposes that the Code should be interpreted purposively, in accordance with the spirit and purpose of the core principles (see paragraph 2 of the Code).

¹³ Special Countervailing or Financial Advantage

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

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

Balancing Risk and Reward

5.8 The Government's overarching objective is to achieve the core principles, that tenants are treated fairly and that tied tenants are no worse off than free-of-tie tenants. The Government has an open mind as to the best way of achieving this within the statutory Code and would welcome evidence on this matter.

5.9 There are a number of significant areas where the Government considers it may be helpful to strengthen the Code to ensure a fair balance of risk and reward between pub companies and tenants.

Right to request an Open Market Rent Review (paragraph 16 of the Code)

5.10 The ability to request an open market rent review – and, if necessary, take it to the Adjudicator – is fundamental to ensuring tenants are treated fairly.

5.11 The Government therefore proposes that, regardless of the provisions of their current lease, a tenant should be able to request an open market rent review if:

- a. they have not had one in the last five years; or
- b. the pub company significantly increases the price of tied products; or
- c. there has been an event outside of the tenant's control and unpredicted at the time of the previous Rent Assessment that impacts significantly on the tenant's ability to trade.

Increased Transparency (paragraphs 8-9, 22-24 and Annex A of the Code)

5.12 It is important that tenants have the ability to fairly and openly access information to ensure that they are being treated fairly and to confirm that, if tied, they are no worse off than they would be if they were free-of-tie.

5.13 The Government therefore proposes that the Code should address transparency in a number of ways, but in particular by requiring the pub

company, at rent assessment and rent review, to produce parallel tied and free-of-tie rent assessments (as at Annex A of the Code) so that a tenant can ensure that they are no worse off. These parallel rent assessments would need to explicitly set out the turnover, gross profit, costs and divisible balance, as well as explicitly listing and quantifying any SCORFA, before, if necessary, decreasing the tied rent to ensure the tied tenant was no worse off.

Gaming Machine Tie (paragraph 29 of the Code)

5.14 Four successive Select Committee Inquiries into the pub industry have concluded that the gaming tie serves no good purpose. To quote just two, in 2004, the Committee said:

"In our opinion, pubcos do not add sufficient extra value from their deals to justify their claims to 50% of the takings from AWP [gaming] machines. We remain unconvinced that the benefits of the AWP machine tie outweigh the income tenants forgo and we recommend that the AWP machine tie be removed."

And in 2011, the Committee said:

"The AWP tie is still in existence seven years after our predecessor's initial recommendation to dispose of this tie and despite two follow-up Reports endorsing that recommendation. It is deeply frustrating that the industry has chosen to ignore this as it is a relatively easy area for pub companies to show willing. The industry should have acted on this recommendation. The fact that they did not is another clear illustration of its refusal to engage in meaningful reform."

5.15 The Government agrees with the Select Committee that the gaming machine tie serves no good purpose. As stated by then Minister Edward Davey at the time, the Government was disappointed that the pub companies did not choose to remove the gaming machine tie in the self-regulatory approach trialled in November 2011.

5.16 Furthermore, the lack of willingness by pub companies to act on this matter has led to a concern that even if the gaming machine tie were removed, some companies might respond by tying another product. The Government sees no good reason why any product unconnected to the core business of a pub or brewer – in other words, no produce other than drinks – should be tied and therefore proposes to mandate in the Code that no product other than drinks may be tied.

Guest Beer Option (paragraph 27 of the Code)

5.17 Even in cases where pubs are tied, it may be of benefit to both the tenant, the consumer and independent breweries if the tenant is able to exercise a 'guest beer option', that is that they may buy one beer of their choice from any source. This beer would not have to be one stocked by the

pub company but could be of any source, for example a popular brand demanded by their customers or a local beer produced by a nearby microbrewery, thereby strengthening community links.

5.18 The Government therefore considers that the Code should include a guest beer option.

Flow Monitoring Equipment (paragraph 30 of the Code)

5.19 As acknowledged in the 2010 Select Committee Report, “*the accuracy of data from flow monitoring equipment and the analysis of that data are highly contentious issues.*” It is clear that there is no consensus as to whether the equipment is accurate enough to be used to determine whether a tenant is complying with purchasing obligations. A further difficulty is that, as it appears likely that they are not in use for trade, their accuracy cannot be enforced by Trading Standards.

5.20 Clearly, it is entirely legitimate for one party to a contract to seek to ensure that the other party complies with the terms of that contract. However, the model of the tied public house has been part of the British pub industry since at least the 18th century and for the majority of that time modern flow monitoring equipment has not been available. It is therefore clearly possible to operate a tied estate and to enforce the tie without the use of flow monitoring equipment.

5.21 The Government therefore considers that the simplest and fairest solution is to mandate in the Code that information obtained from flow monitoring equipment may not be used for the purpose of determining whether a tenant is complying with purchasing obligations and that it may not be used or considered as evidence when enforcing purchasing obligations.

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, if the pub company significantly increases drink prices or if an event occurs outside 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.*
- iii. Abolish the gaming machine tie and mandate that no products other than drinks may be tied.*
- iv. Provide a 'guest beer' option in all tied pubs.*
- 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.*

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

Amending the Code

5.22 As with any industry, the pub industry is not static. It is therefore important that any Statutory Code is able to respond to new developments in the industry, whether they be new business practices, new legislation or new technological developments. This will not only prevent 'gaming' of the Code by any pub company that, in the future, may seek to subvert it, but it will ensure that it remains fit for purpose and relevant to both pub companies and tenants.

5.23 The Government therefore considers that it would be appropriate for the Secretary of State to be required to periodically review the Statutory Code and Adjudicator, and to be given the power, by Order, to amend the Statutory Code, if the review showed evidence that such amendment would serve to deliver more effectively the two overarching principles.

5.24 This review would also include the capacity to alter the minimum threshold above which the Code would apply.

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?

A mandatory free of tie option?

5.25 We are interested in views about whether these measures would be a sufficient and proportionate means to address the harm or whether further measures would be merited. A further measure which has been previously mooted by stakeholders is a mandatory free of tie option with enforced open market rent reviews, which may be one possible way of achieving the core principles. For the avoidance of doubt, the Government considers that a ‘free-of-tie option’ means an option in which the tenant is subject to no purchasing obligations of any form and therefore the only sum paid to the pub company is the dry rent.

5.26 Within a mandatory free-of-tie option, one possibility would be that pub companies who were also brewers would be allowed to require their pubs to sell their beers (and only their beers), or that a certain proportion of their beers had to be their own, but that the tenant could buy those beers from whoever they wished. This would potentially preserve those brewers’ route to market, whilst removing the opportunity for the pub company brewer to charge excessive prices and allowing the tenant to buy beer at an open market rate. The Government would be interested in views on this suggestion.

5.27 It is important to emphasise that a mandatory free-of-tie option, in any form, would not by itself solve anything without accompanying enforcement, and would not be a panacea for the wider issues facing the pubs sector. Although rents would be expected to rise to some degree under a free-of-tie option, without enforcement, pub companies, should they so choose, would be free to raise rents to well above the fair values. An Adjudicator, with the power to arbitrate rental disputes, carry out investigations and impose sanctions would be essential to ensure that the free-of-tie rents were fair and open market rents, not artificially exploited.

5.28 The Government recognises that there is a strong feeling amongst some parts of the industry that a mandatory free-of-tie option would be the best way of achieving the core principles. On the other hand, others in the industry, principally pub companies, have argued that a mandatory free-of-tie option would be a disproportionate means of achieving the objective. It has been argued that the beer tie has existed for centuries in Britain and that some companies’ business model is built on being able to tie (or directly manage) their entire pubs estate, something which would not be tenable if some tenants could choose to go free-of-tie. This risks creating undesirable instability in the

industry, if large pub companies restructure, dissolve or sell off pubs in response to the changes.

5.29 The Impact Assessment highlights the uncertainties around the impacts on pub numbers and employment levels of a mandatory free-of-tie option. The Government recognises that these impacts will need to be clarified before any decisions can be made. To help achieve this clarity, the Government will commission independent analysis of the impacts on both gross and net pub closures, and employment levels. This analysis will be based on as much robust evidence as is available.

5.30 An alternative way of achieving the core principles could be for the Code to simply state that higher beer prices due to the tie must be directly compensated for by lower rent and/or other genuine, quantifiable countervailing benefits¹⁴. The exact calculation is expounded upon in more detail in the draft Code, at Annex A, in particular in the hypothetical rent assessment at Annex A to the Code. There would still be a commercial negotiation between pub company and tenant, but the Code would require the tenant to be given all the information required to make an informed, commercial assessment of this – and, ultimately, the matter could be referred to and decided by the Adjudicator.

5.31 Combined with mandatory increased transparency and rigorous enforcement by the Adjudicator, including the imposition of significant fines on companies in breach, this could also achieve the core principles. It would be a less intrusive intervention into the market than a mandatory free-of-tie option, as pub companies would still be able to choose to operate either a tied or free-of-tie model, provided they ensured their tied tenants were no worse off than they would be were they free-of-tie. On the other hand this would be more complex than the mandatory free-of-tie option and tenants might find it difficult to determine whether the rent assessment has been properly calculated by the pub companies without recourse to the Adjudicator.

Unintended consequences

5.32 The Government is very mindful of the dangers of unintended consequences. The last major Government intervention into this market, the Beer Orders¹⁵, led to the unanticipated rise of the major pub companies and, arguably, contributed to the concerns that the industry faces today. It is

¹⁴ “Put simply work out what you would earn FOT take that from the tied net profit before rent (NPBR = divisible balance) and there's your tied rent. Genuine SCORFA's can be incorporated as a cost saving (increasing the tied NPBR) and therefore the rent!” – Simon Clarke, IPC – from the Publican Morning Advertiser Forums, February 2013.

¹⁵ The Supply of Beer (Tied Estate) Order 1989 (SI 1989/2390), the Supply of Beer (Loan Ties, Licensed Premises and Wholesale Prices) Order 1989 (SI 1989/2258) and the Supply of Beer (Tied Estate) (Amendment) Order 1997 (SI 1997/1740)

therefore important that any market intervention is proportionate in achieving the intended outcome, both on individual pubs and the wider pubs sector.

5.33 The tie has a long and honourable history in the British pub sector, going back to at least the 18th century. It can be used to very good purpose to benefit both sides: many tenants profess themselves to be very happy with their pub companies. The benefits that the business model offers to small and medium sized brewers, granting them a guaranteed market to sell their beer and build their brands, is significant. Uncertainty created by a mandatory free-of-tie option could undermine this, potentially leading to an increased risk of pub closures.

5.34 The current pub industry landscape is highly beneficial to brewers. During the 21st century there has been a significant real ale revival and, in 2012, the number of British breweries topped 1000, a higher number than has been seen since the 1930s. Brewing is part of Britain's heritage and the cost of undermining this industry, which includes hundreds of micro-brewers, dozens of medium-sized family brewers and a small number of regional brewers such as Greene King and Marston's, would be substantial, in terms of jobs, the economy and consumer choice.

5.35 There have been a number of positive and negative potential impacts that have been presented to the Government that could potentially result from a mandatory free-of-tie option.

Positive

5.36 Tenant groups have suggested some advantages of the free-of-tie option include:

- a. Simplicity. A free-of-tie option would allow every tenant to choose between tied and free of tie, thereby letting the market decide which was best.
- b. Greater opportunity for microbrewers. Despite initiatives to facilitate sales to large pub estates, the majority of microbrewers' sales are to local, free-of-tie pubs. It is therefore possible that an increase in pubs going free-of-tie would benefit the microbrewing industry.
- c. Greater consumer choice within each pub. Although the OFT concluded that the market was operating competitively to produce a high degree of consumer choice, it is possible that more free-of-tie pubs would mean a greater degree of choice within each pub, as each pub could choose its own range of beer. The extent to which this occurred would partially depend on the extent to which tenants chose a wide range of different beers.

Negative

5.37 Pub companies and brewers have suggested some disadvantages of the free-of-tie option include:

- a. Loss of economies of scale. It is likely that, particularly in the short term, a mandatory free-of-tie option could lead to some degree of losses of economy of scale: the pub companies' buying power can drive large discounts from producers and their national distribution networks increase efficiency.
- b. Lack of incentive of companies to invest in pubs. It appears likely that, if a mandatory free-of-tie option were introduced, at least some pub companies and brewers might invest less. Without the surety of being able to tie, there is less incentive to want the tenant to do well and sell more beer – the profit-sharing mechanism is gone. This could lead to the degradation of the pub estate which could harm the long-term future of the industry.
- c. Market becomes dominated by a few small international brewers. It is possible that, in the absence of pub company buying power, large international brewers would offer tempting, discounted offers in exchange for exclusivity, essentially foreclosing the market. If this occurred, it could reduce consumer choice as well as putting pressure on, potentially leading to the closure of, British micro- or family-brewers.
- d. Exit of a major company. It is possible that a mandatory free-of-tie option could cause a major pub company to go into administration, as their business models are highly predicated on the ability to tie. This could also happen without a free-of-tie option due to the effect of the prime principle. If this occurred, hundreds or thousands of pubs might be placed on the market at once. If those pubs were bought by other pub operators there could be a positive, transformative process for the industry; equally though, if there was not enough capital in the industry, it could lead to a significant number of otherwise viable pubs being sold off for alternative use. The uncertainty and disruption would also be likely to discourage investment.
- e. Brewery collapse or downsize of a major brewer. The brewing pub companies sell a significant portion of the beer they brew through their pubs. Under a mandatory free-of-tie option, their guaranteed market would decrease which is likely to cause them to sell less beer. It is possible that this could lead to one or more breweries becoming financially unviable leading to closure; such an eventuality could lead to several hundred direct job losses with up to several thousand more in the supply chain, concentrated within one region. It is possible that this could be mitigated if the breweries were still able to require their pubs to

sell their beer (though allow them to buy it from any source) as described in paragraph 5.26.

5.38 The arguments for and against a mandatory free-of-tie option are finely balanced and the Government does not, as yet, have sufficient evidence to say conclusively which of these positive and negative effects are most likely to occur. The Government would therefore welcome further evidence presented by those responding to the consultation that would inform this decision.

Conclusions

5.39 The Government has put forward both the potential benefits and possible costs of a mandatory free-of-tie option. It has also set out an alternative way that the core principles could be achieved, involving mandating that higher beer prices for a tied tenant must be balanced by a lower rent.

5.40 The Impact Assessment highlights the uncertainties around the impacts on pub numbers and employment levels of a mandatory free-of-tie option. The Government recognises that these impacts will need to be clarified before any decisions can be made. To help achieve this clarity, the Government will commission independent analysis of the impacts on both gross and net pub closures, and employment levels. This analysis will be based on as much robust evidence as is available.

5.41 From the evidence thus far, it is hard to determine accurately the most appropriate method of proceeding. The Government therefore strongly encourages respondents to the consultation to set out, not only which option they favour, but the evidence that supports that option, including the likely consequences, intended or unintended, that might result from that option.

5.42 The Government would also welcome any alternative options that respondents might have for achieving the core principles.

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

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?

6 Powers of the Proposed Adjudicator

The Government is proposing to establish an independent Adjudicator to enforce the proposed Statutory Code. Enforcement by an independent Adjudicator would ensure that the Code was genuinely complied with and provide a means of dispute resolution without tenants being forced to go to court.

The Government is seeking views on:

- The powers and functions of the Adjudicator;
- The sanctions that the Adjudicator should be able to impose;
- How the Adjudicator should be reviewed and funded.

6.1 The Government considers that it will be necessary to have an independent Adjudicator to enforce the statutory Code. Enforcement by an independent Adjudicator would ensure that the Code is genuinely complied with and would provide a statutory dispute resolution mechanism so that tenants have an option other than court. Particularly given that much of the Code relates to issues (such as rent) that will be specific to each pub, the ability for an independent and expert Adjudicator to take a view will be essential. The Government considers this would be the case whether or not the Code included a mandatory free-of-tie option – a Statutory Code without enforcement would be like a sports match with rules but no referee.

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

Powers and Functions

6.2 The Government proposes that the Adjudicator would be based on the model of the widely welcomed Groceries Code Adjudicator¹⁶ and, accordingly, the Adjudicator would have two main functions.

- a. Arbitration function. The arbitration function would be about delivering redress to individual tenants. Essentially, the Adjudicator would be able to deliver an open market rent review, in accordance with RICS guidance and the Statutory Code, to ensure that the rent had been calculated fairly and not artificially inflated. Any tenant dissatisfied with

¹⁶ <http://services.parliament.uk/bills/2012-13/groceriescodeadjudicator.html>

how their rent had been calculated could take their pub company to the Adjudicator for arbitration.

- b. Investigation function. Using his or her investigatory function, the Adjudicator would be able to undertake proactive investigations provided he or she had reasonable grounds to suspect that a pub company was breaching the Code. During an investigation the Adjudicator would have strong powers to require information from pub companies and, if the pub company was found to be in breach, could impose sanctions, including financial penalties. As discussed in Box 1, the Government considers that this proactive investigatory function is absolutely fundamental to the effective enforcement of the Code.

Arbitration function

6.3 The Government proposes that if a dispute arises under the Code and is not resolved to the satisfaction of the tenant within 21 days, they could make an arbitration request to the Adjudicator. Disputes would usually be arbitrated by the Adjudicator, though they could be referred by the Adjudicator to another independent arbitrator in certain circumstances, for example if the Adjudicator had a conflict of interest. This will enable the Adjudicator to gain a greater understanding of how the Code is operating, which will help them carry out their other functions (such as providing advice or carrying out investigations).

6.4 The main advantage of arbitration is that it ensures that pub companies and tenants can deal with overrunning disputes in a short period of time and provide them with redress for any damages they have suffered. The ability of the Adjudicator to be the final arbiter of whether a rent review has genuinely been conducted on 'an open market' basis, in accordance with RICS Guidance and the Code, is central to an effective statutory solution.

6.5 The Government considers that it should be free for a tenant to bring a complaint for arbitration, but recognises that it would be necessary to have some mechanism to prevent frivolous complaints being made to the Adjudicator. The Government considers that this could be best achieved firstly by the 21 day period, during which the pub company would have the opportunity to resolve the dispute, and secondly by providing that the Adjudicator could impose costs on the complainant if the complaint was found to be vexatious or wholly without merit.

Investigatory function

6.6 Although arbitrations are effective at tackling individual disputes, they do little to tackle underlying or systemic issues. Particularly as many tenants may not know their rights, it is possible that a pub company could systematically breach the Code and consider that the cost of the minority of cases that went to arbitration were simply a 'cost of doing business'.

6.7 The Government therefore proposes that, if there are reasonable grounds to suspect that a pub company has broken the Code or failed to follow a recommendation, the Adjudicator may carry out an investigation. In deciding whether to start an investigation the Adjudicator would be able to consider information from any source, including complaints from individuals and information from trade bodies, third parties, whistleblowers or information in the public domain.

6.8 During an investigation, the Adjudicator would have powers to require information from pub companies. The Adjudicator would therefore be able to consider broad patterns of behaviour and consider detailed commercial evidence to determine whether a pub company was in breach of the Code. Whilst in some cases it may be difficult to tell whether a pub company was in breach of the Code when looking at a single pub (as the trading performance of a pub depends on many factors), when looking across several hundred pubs it would be very easy to tell if a company was, for example, consistently not providing pre-entry awareness training, withholding documents or grossly inflating projected turnovers.

6.9 The Government considers that the Adjudicator should require large pub companies to pay some or all of the costs of an investigation if they have breached the Code. However, if an individual has made a complaint that is found out to be vexatious and wholly without merit, then that complainant should pay some or all of the costs of an investigation (a complaint that was simply wrong would not incur costs). This ensures both the large pub companies and the tenants are protected and are not placed under burden without reason.

6.10 Investigations would, therefore, allow the Adjudicator to tackle and publicise any widespread abuses in the industry and ensure that all companies recognised that they needed to comply with the Code.

6.11 The Government considers that the Adjudicator should also be able to provide advice and guidance to pub companies and tenants. This power would be exercised with a view to encouraging compliance with the Code. The advantage of this is that the Adjudicator would be able to help to ensure that pub companies complied with the Code, that tenants knew their rights under the Code. This will encourage compliance by the large pub companies and keep those within the industry well informed overall, helping to prevent disputes occurring in the first place.

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

i. Arbitrate individual disputes?

ii. Carry out investigations into widespread breaches of the Code?

The Adjudicator's Sanctions

6.12 If an Adjudicator's findings from an investigation show that the Code has been breached, the Government considers that the Adjudicator should have the power to impose a range of sanctions. This should include making recommendations, 'naming and shaming' those who breach the Code and, in the severest of breaches, imposing financial penalties upon a company.

- a. Recommendations: Recommendations would be the lightest-touch of the Adjudicator's recommendations and would be non-binding. They would be likely to be used in cases where a breach had been minor or accidental, or in combination with the more serious sanctions. The Adjudicator would be able to require the pub company to report on how it had complied with a recommendation and failure to follow a recommendation could lead to another investigation and, if a further breach were found, a more serious sanction.
- b. Requirement to publish information: Under this sanction, sometimes referred to as a 'name and shame' power, the Adjudicator could require the pub company to publish information about the breach of the Code. The Adjudicator would be able to require the pub company to publish the information in a suitable place, for example on their website, by sending a letter to all of their tenants or by taking out an advertisement in the Publican's Morning Advertiser or other suitable publication. This information could then be taken into account by those dealing with that pub company in future and would make it very clear to the rest of the industry that a breach of the Code had occurred, and why.
- c. Financial penalties. For the most severe or repeated offences, the Government considers that the Adjudicator should be able to impose financial penalties on the pub company. The ability to impose fines would be a very strong deterrent and send a strong message to the industry that non-compliance was not an option.

6.13 A range of sanctions will allow the Adjudicator to tailor the severity of sanction to the severity of the breach, ensuring that non-compliance is punished according to how serious it is.

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. Requirements to publish information ('name and shame')?*
- iii. Financial penalties?*

Funding and Accountability of the Adjudicator

Accountability

6.14 The Government proposes that the Adjudicator should report annually on his or her work, setting out details of arbitrations conducted, investigations carried out and any breaches of the Code that had been found. This information would be useful to the Secretary of State and to Parliament in reviewing the overall effectiveness of the Adjudicator and useful information to those in the pub industry more widely.

6.15 The Government also proposes that the Secretary of State would be required to review the Adjudicator and his or her effectiveness every three years. This would include a consideration both of how well the Adjudicator was enforcing the Code, whether the Code needed to be amended and whether the Code and Adjudicator were still needed.

Funding

6.16 The Government proposes that the Adjudicator should be funded by an industry levy. Each of the large pub companies covered by the Code would pay a share of the levy: the Government considers that is appropriate, as it is the conduct of pub companies that has led to the need for an Adjudicator. The total annual cost of the Adjudicator is estimated at approximately £820k a year, meaning the contribution from each pub company should be affordable, given that all the companies in scope would have over 500 pubs.

6.17 There may be a risk of these costs being passed to pub tenants, and ultimately to the consumer. The Government considers that as the market is already competitive, the price paid by the consumer is unlikely to change, and thus revenues would be unaffected – however, we would welcome comments on the likely impact of this levy on pub tenants and consumers.

6.18 In the first year of operation, the Government proposes that the levy should be divided amongst the companies in proportion to the number of pubs that each owns. However, the Government believes that it would be fairest if those companies who behave badly have to pay more, whilst those which behave well should have to pay less. The Government therefore considers that in the second and subsequent years of the levy, the levy should be split proportionately so that those companies who breach the Code pay more. As well as being fairer, this will also act as an additional incentive for pub companies to comply with the Code.

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

Q.17 Do you agree that the Adjudicator should be funded by an industry levy, with companies who breach the Code more paying a proportionately 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?

Annex A: The Proposed Statutory Code: Draft Pubs Code Of Practice

INTERPRETATION

1. In this Code:

“Business Development Manager” means those employees of a Pub Company whose role includes from time to time responsibility for interaction with, managing the relationship with or otherwise being responsible for the Pub Company’s interactions with the Tenant.

“Free-of-tie Tenant” means a Tenant who is not bound by any purchasing obligations.

“Tenant” means the person to whom the pub is assigned under a lease or tenancy agreement, and in relation to a prospective lease or tenancy agreement includes the prospective Tenant;

“Pub” means any premises as defined in the Licensing Act 2003 which has a premises license authorising sale by retail of alcohol for consumption on the premises. In addition the premises must be used principally for retail sales of alcohol to members of the public for consumption on the premises, and sales must not be subject to the condition that buyers reside at or consume food on the premises.

“Pub Company” means a company who is designated as a Pub Company in accordance with [the Pubs Adjudicator Act]

“Premises” means the property and structures which are the subject of the tenancy agreement.

“Lease or Tenancy Agreement” means an agreement for the lease or tenancy of premises, created out of the freehold, which are occupied by the Tenant for the purposes of a business that he or she carries on.

“Tied Agreement” means a lease or tenancy agreement which includes purchasing obligations.

“Tied Tenant” means a Tenant who is bound by purchasing obligations.

“Rent Assessment” means the pre-contractual assessment of rent and any reassessment of the rent payable at one or more points during the life of the lease or tenancy.

PART 1

OBJECTIVE OF THE CODE

2. All provisions of the Code should be interpreted purposively in accordance with the objective that:
 - a. Tenants should be treated fairly and lawfully; and
 - b. Tied Tenants should not be worse off than Free-of-tie Tenants.
3. Fair and lawful dealing will be understood as requiring the Pub Company to conduct its relationships with Tenants in good faith, without distinction between formal or informal arrangements and without duress.
4. The Pub Company must keep a written record evidencing compliance with this Code.

PART 2

PRE-CONTRACTUAL NEGOTIATIONS

5. Before a lease or tenancy agreement is made the Pub Company must be satisfied that:
 - a. the Tenant is a suitable and properly qualified person; and
 - b. the Tenant has a sustainable business plan.
6. In order to demonstrate that the requirement at paragraph 5 has been met the Pub Company must:
 - a. ensure that the Tenant:
 - (i) is aware of their obligations under the Licensing Act 2003;
 - (ii) has completed accredited pre-entry training which meets the Qualification Curriculum Authority's standards;
 - (iii) has taken proper independent professional advice, including business, legal, property and rental valuation advice.
 - b. ensure that the Tenant has independently produced a business plan, having received professional advice. The business plan must include:
 - (i) estimations of incomes and related costs;
 - (ii) a sensitivity analysis examining the business performance on an increase/decrease in business income and the effect of those increases/decreases on costs and profitability; and
 - (iii) the impact of indexation if appropriate.
 - c. advise the Tenant to consult RICS guidance and any relevant industry Benchmarking Reports which may assist with market comparisons for the preparation of the business plan;
7. The Pub Company is not required to comply with the obligations at paragraph 6 if the Tenant agrees in writing that the obligations should be waived and the Tenant:
 - a. operates at least one other pub; or
 - b. can demonstrate at least three years relevant business management experience in the sector; or
 - c. has an existing lease or tenancy agreement with the Pub Company.

8. Before a lease or tenancy agreement is made the Pub Company must provide the Tenant with clear information to allow the Tenant to establish the costs and risks of trading.
9. In order to demonstrate that the requirement at paragraph 8 has been met the Pub Company must:
 - a. provide the Tenant with information regarding:
 - (i) the types of lease and tenancy agreements available;
 - (ii) the period of tenure;
 - (iii) any purchase obligations or product ties;
 - (iv) the extent to which the lease or tenancy agreement will place obligations on the Tenant in respect of the requirement to maintain and repair the property and the condition in which the pub should be returned to the company at the end of the lease or tenancy;
 - (v) the procedures which Tenants must follow to assign their lease or tenancy agreement;
 - (vi) how they will deal with any requests for surrender of the lease or tenancy;
 - (vii) the range of support programmes and advice which will be available during the operation of the lease or tenancy, on issues such as –
 - the capabilities and training needs of the Tenant and the Tenant's staff;
 - licences and any relevant training requirements;
 - business management advice;
 - brand promotion and merchandising;
 - provision and maintenance of dispensing equipment;
 - pub promotion and marketing;
 - procurement benefits;
 - rating advice;
 - external decoration, signage, building repairs, car parks and gardens.

- (viii) how their relationship will be conducted during the operation of the lease or tenancy;
 - (ix) their policy for dealing with requests for assistance from Tenants arising from circumstances where they experience business difficulties which are beyond their control.
 - (x) whether they would be willing to consider amendments to their standard terms.
- b. provide the Tenant with a blank template profit and loss account for business planning purposes if requested;
- c. provide the Tenant with a full description of the premises, including:
- (i) details of the premises licence and any licence conditions;
 - (ii) any enforcement action taken during the previous two years, where known;
 - (iii) information about any material changes of commercial conditions likely to appear in the area¹⁷ and how these might influence the business opportunity available.
 - (iv) details of any restrictions on the premises use, such as planning constraints on types of trading, hours of trading and use classes;
 - (v) a schedule of condition identifying the state in which the premises are being provided, drawing attention to any specific problems or features and clarifying what, if any, remedial work is required and expected during the course of the lease.

¹⁷ This should include any developments to nearby premises in the Designated Pub Company's estate.

- d. encourage the Tenant to inspect the premises thoroughly;
- e. advise the Tenant to seek independent professional advice on the structure of the premises;
- f. advise the Tenant to obtain a survey of the premises, ideally carried out by a professional with experience of the pub market;
- g. advise whether fixtures and fittings will be purchased and, if so, provide information about the arrangements for payment;
- h. provide a protocol governing the treatment and procedures to be followed in dealing with dilapidations which will specify:
 - (i) the timetable for the review and updating of the original schedule of condition (not less than 6 months before the end of the lease or tenancy);
 - (ii) that any further dilapidations/determinations can be added to the schedule of condition at a later date in circumstances where there is clear evidence of new material consideration or developments which could not have been taken into account at an earlier date;
 - (iii) the process for agreeing a schedule of wants and repairs in line with the schedule of condition;
 - (iv) The period (not less than 12 months) before the end of the lease or tenancy when a survey will be conducted to determine the extent of dilapidations;
 - (v) the process by which any dispute concerning the extent and amount of repairs and making good is resolved.
- i. clearly set out their policy regarding potential investment opportunities for improvements and refurbishments and any implications for rent;
- j. clarify whether they will maintain and meet the cost of insurances for the premises or whether the cost of such insurance is to be arranged by the company and re-charged to the Tenant.

PART 3

RENT ASSESSMENTS

10. All initial rent assessments must be:
 - (a) accompanied by a Rent Assessment Statement based on a shadow profit and loss account produced by the Pub Company. The Rent Assessment Statement must include the minimum content set out at **Annex A** to this Code.
 - (b) signed by a qualified RICS valuer as being conducted in accordance with the RICS Guidance at **Annex B** of this Code, interpreted in light of the overarching principle that a Tied Tenant should be no worse off than a Free-of-tie Tenant.
11. Rent Assessment Statements are not intended to be nor must they be taken to be projections of profit or turnover. Assumptions within Rent Assessment Statements should be determined by reference to what a Reasonably Efficient Operator (as defined by RICS Guidance) would be expected to be able to achieve: individual Tenants may therefore achieve either higher or lower profits than this. Failure to achieve turnover or profits set out within a Rent Assessment shall not in itself constitute a breach of this Code.
12. Before a Rent Assessment is agreed a Pub Company must advise the Tenant to obtain proper independent professional advice, including rental valuation advice.
13. The Pub Company must ensure that a responsible officer of the company or its agent involved in obtaining and/or evaluating the supporting material provided in preparing the Rent Assessment will have visited the premises in question within at least 3 months prior to the assessment being undertaken.
14. The Pub Company must provide the information specified at paragraph 9 prior to any Rent Assessment.
15. The Pub Company must seek to comply with any reasonable request for further information from the Tenant and/or their professional advisors relevant to the Rent Assessment. Where such information is not available the reason for this must be disclosed.
16. A Tenant may at any time request a Rent Assessment provided that:
 - (a) a Rent Assessment has not been conducted within the previous five years;
 - (b) the Pub Company makes a significant alteration to the price at which it supplies tied products to the Tenant; or

- (c) there has been an event outside of the Tenant's control and unpredicted at the time of the previous Rent Assessment that impacts significantly on the Tenant's ability to trade.
17. If a rent assessment is requested by the Tenant and one of the conditions at paragraph 16 is met the Pub Company must complete a Rent Assessment within six months.
 18. The Pub Company must clearly set out a specific timetable for information, including the Rent Assessment Statement, to be provided in advance of the Rent Assessment. In any event this information should be provided a minimum of six months before the Rent Assessment date or no less than three months after the Tenant has requested a Rent Assessment under paragraph 16 above.
 19. If the lease or tenancy agreement provides that the rent is to be varied by reference to an index the Pub Company must specify:
 - (a) which index will be used;
 - (b) the date on which the rate will be assessed and applied;
 - (c) the frequency of any adjustment;
 - (d) that payments may be adjusted upwards or downwards, according to the movement of the index at the time.
 20. Upwards only Rent Assessments shall be considered invalid and unenforceable.

PART 4

TIED AGREEMENTS

21. The provisions in this Part of the Code apply specifically to Tied Agreements. Tied Agreements are also subject to the provisions in the other parts of the Code.

Rent

22. In determining rental calculations, the overarching principle that “a Tied Tenant should be no worse off than a Free-of-tie Tenant” should be interpreted as meaning that the projected Post Rent Balance of a Tied Tenant must be equal to or greater than the projected Post Rent Balance that that Tenant would receive, under the same assumptions and all other conditions of the lease or tenancy being equal, under a Free-of-tie Agreement. Any genuine and quantifiable Special Countervailing or Financial Advantage (SCORFA) would be reflected by increased costs in the assessment of costs in the Free-of-tie model, which would in turn impact upon the divisible balance, rent and Post Rent Balance in that model. The example rental agreement in Annex A provides a demonstration of how this should be applied in practice.
23. A Pub Company which proposes a Tied arrangement must provide the Tenant with a shadow profit and loss account which clearly demonstrates what the equivalent rent assessment would be if the agreement was a Free-of-tie Agreement, and how this has been calculated. The shadow profit and loss account must include the specified minimum content contained in Annex A to this Code. The Pub Company must use the same assumptions and propose the same share of the divisible balance for the preparation of the shadow profit and loss accounts in both tied and free-of-tie equivalents for any given pub.
24. The Pub Company must be able to demonstrate by reference to the rent assessments and the profit and loss accounts that the Tenant would be no worse off in the Tied Agreement than they would be in a Free-of-tie Agreement.

Purchasing Obligations

25. Where drinks are supplied under a tie, details of the range of products available will be provided by the Pub Company to the Tenant, including:
- (a) the national prices charged for these products;
 - (b) qualifications for discount; and
26. The Pub Company must supply the Tenant with its current and relevant price list which will include notification about any imminent changes.
27. Where drinks are supplied under a tied agreement, the Pub Company must provide the Tenant with a ‘guest beer’ option. This is to be interpreted to mean that the Tenant should be allowed to purchase and sell one draught beer from any source without any control or restriction being imposed by the Pub Company.

28. Where drinks other than beer are also supplied under a tied agreement, the terms of the purchase obligations attached to these products will be made clear to the Tenant by the Pub Company. An outline of trading terms will also be provided to the Tenant by the Pub Company.
29. No products other than drinks may be tied.
30. Information obtained from flow monitoring equipment may not be used for the purpose of determining whether a Tenant is complying with purchasing obligations, nor may it be used or considered as evidence when taking enforcement action on purchasing obligations.

PART 5

BUSINESS DEVELOPMENT MANAGERS

31. The Pub Company must:
 - (a) provide Business Development Managers with a copy of this Code;
 - (b) provide training on the requirements of this Code to all Business Development Managers at least once each calendar year;
 - (c) publish their provisions and commitments regarding the competence and future progression of Business Development Managers, including qualifications and on-going training and their commitment to continuous professional development;
 - (d) keep records of the training received by Business Development Managers for inclusion in their Annual Compliance Report.
 - (e) provide information to Tenants about the role of the Business Development Managers and the support and guidance they will provide.

32. The Pub Company must ensure that Business Development Managers:
 - (a) receive training before carrying out a rental negotiation;
 - (b) abide by the overarching principle of this Code

PART 6

MISCELLANEOUS PROVISIONS

Incorporation of Code into Lease and Tenancy Agreements

33. The Pub Company must incorporate the Code into all new lease and tenancy agreements and into all existing lease and tenancy agreements at the next rent review following this Code coming into force.

Assignment of Leases

34. The Pub Company must respond timely to requests for assignment and explain the implications for disposal of the business.
35. Following a request for assignment from the Tenant the Pub Company must provide the Tenant with information regarding:
- (a) professional support and advice that is available;
 - (b) fees;
 - (c) buy back arrangements (if any);
 - (d) any dilapidations.

Insurance

36. Where the Pub Company charges the Tenant for insurance the Pub Company must:
- (a) provide the Tenant with full details of the insurance schedule (to include all aspects of cover provided), a summary of cover, the charges payable and any excess applicable;
 - (b) provide the Tenant with any additional information to enable a comparable quotation to be sought; and
 - (c) price-match any like-for-like policies identified by the Tenant by recompensing the monetary difference or alternatively allow the Tenant to obtain their own insurance;
 - (d) include insurance charges clearly and separately in the shadow profit and loss account.

Premises

37. Unless otherwise specified in the terms of the lease or tenancy agreement it will be assumed that the Tenant is required to “keep” or maintain the building in the condition set out in the schedule of condition.

38. The schedule of condition should be referenced when preparing wants of repair and dilapidations and it will form the basis of agreement on the repair liabilities of the lease or tenancy agreement offered.

PART 7

PUB COMPANY CODES OF PRACTICE

39. Designated Pub Companies may, if they so choose, produce a Company Code of Practice. Company Codes of Practice must be based on the principles within this Code.
40. Nothing in a Company Code of Practice will affect the rights of a Tenant and duties of the Pub Companies set out in this Code.
41. The legal status of the Code must be described and included in the Pub Company Code of Practice.
42. If the Pub Company produces a Company Code of Practice it must be provided to all Tenants.

PART 8

COMPLIANCE

43. The Pub Company must appoint a suitably qualified employee as the Code Compliance Officer.
44. The Pub Company must ensure that the Code Compliance Officer:
 - (a) will be provided with all resources necessary for the fulfilment of their role, including access to all documentation relating to, and availability of the Business Development Managers to discuss issues in connection with, the Pub Company's obligations under this Code;
 - (b) will be available as a point of contact for Tenants and any authority or other body making enquiries in relation to this Code;
 - (c) will be independent of, and must not be managed by, the Business Development Managers; and
 - (d) will be available to discuss with the Tenant the reasons for any decisions made by the Pub Company in relation to this Code.
45. The Pub Company must ensure that, for each complete financial year in which this Order is in force, the Code Compliance Officer delivers an annual compliance report to the Pubs Adjudicator, within four months after the end of the financial year to which the annual compliance report relates.
46. The annual compliance report must have been submitted to, and approved by, the chair of the Pub Company's audit committee and must include a detailed and accurate account, for the financial year to which the annual compliance report relates, of:
 - (a) the Pub Company's compliance with the Code in the preceding year, including instances where a breach or alleged breach of the Code has been identified by a Tenant, and the steps taken to rectify it;
 - (b) steps taken during the preceding year to ensure compliance with the Code, including details of employee training undertaken and guidance issued in relation to the Code; and
 - (c) disputes between the Pub Company and its Tenants regarding the terms of any lease or tenancy agreement, or the application of this Code, and the outcome of any such Dispute.
47. The first annual compliance report required for the purposes of paragraph 45 shall cover the period from the commencement of this Code until the end of the first full financial year in which this Code is in force.
48. The Pub Company must ensure that:

- (a) the Code Compliance Officer provides such other reports as are necessary to ensure that the Pub Company's audit committee retains effective oversight over the Pub Company's compliance with the Code;
 - (b) if the Pub Company does not have an audit committee, the Code Compliance Officer should report directly to the non-executive director of the Pub Company who carries out the functions typically associated with an audit committee, or in the absence of such non-executive director, to the Pub Company's Chief Executive Officer or Managing Director.
49. A summary of the annual compliance report must be included in the Pub Company's annual company report. If the Pub Company does not produce an annual company report, and the summary of the annual compliance report will be published clearly and prominently on the Pub Company's website within four months after the end of the financial year to which the compliance report relates.

PART 9

DISPUTE RESOLUTION

50. The Pub Company must take all reasonable steps to resolve any disputes that arise under this Code swiftly.
51. A Pub Company may not hinder a Tenant from exercising his rights under this Code. Exercising rights under the Code should be interpreted as including making use of any of the dispute resolution functions under the [Pubs Adjudicator Act], including making a complaint to the Adjudicator, referring a matter to the Adjudicator for information or providing information to the Adjudicator, as well as using any other reasonable formal or informal dispute resolution mechanism that the Tenant chooses.
52. Information which may be used in any dispute resolution mechanisms should not be unreasonably withheld and should be shared on request, subject to appropriate confidentiality agreements.
53. Any attempt by a Pub Company to cause a Tenant to suffer detriment as a result of a Tenant exercising or attempting to exercise its rights under this Code shall constitute a breach of the Code.

Annex A: RENT ASSESSMENT STATEMENTS

A Rent Assessment Statement must be provided by the Pub Company to all Tenants prior to a Rent Assessment, in accordance with the provisions contained in Part 3 of this Code.

The information to be included in the Rent Assessment Statement is detailed in Part 3 of the Code and in this Annex. This is to be regarded as the minimum level of detail that must be included but the Pub Company can provide further information if they so wish.

The Rent Assessment Statement must:

- (i) be based on and explain reasonable assumptions;
- (ii) be signed by a properly competent individual;
- (iii) be clear about the basis of the rental assessment and how the market rent for the property has been established;
- (iv) make reasonable allowances for costs and sustainable trade;
- (v) include the past three years trading or volumes purchased direct from the company over the past 3 years where available, including barrelage. If this information is not available then the Pub Company must explain why;
- (vi) include projected sales and gross profit margins, with separate figures for: draught ales; lagers; ciders; wines; spirits and soft drinks;
- (vii) include a waste figure where it is not included in the gross profit margin;
- (viii) include games machines where they are not included within the terms of the lease or tenancy agreement;
- (ix) include the estimated cost of a manager where the effect of such a cost will materially affect the earning potential of the Tenant, for example, where the Tenant is not intending to be the day to day manager;
- (x) express information as a percentage relative to turnover;
- (xi) be net of tax Value Added Tax and Machine Games Tax;
- (xii) reference comparable Benchmarks where appropriate.

A sample Rent Assessment Statement is displayed below.

SAMPLE RENT ASSESSMENT STATEMENT

RENT ASSESSMENT: TENANCY AGREEMENTS

ACTUAL RENT ASSESSMENT

		% Turnover	
Sales			
Draught Lager	£86,000	32.5%	
Draught Ale	£50,000	18.9%	
Draught Cider	£14,000	5.3%	
Packaged Beer	£7,500	2.8%	
Packaged Cider	£6,500	2.5%	
Total Draught/Packaged Beer/Cider	£164,000		
Packaged FABs	£1,000	0.4%	
Wines	£25,000	9.4%	
Spirits	£10,000	3.8%	
Soft Drinks	£10,000	3.8%	
Total Drinks Sales	£210,000	79.2%	
Food	£50,000	18.9%	
Accommodation	£0	0.0%	
Other	£5,000	1.9%	
Net Machine Income(1)	£0	0.0%	
Total Sales (Turnover)	£265,000	100.0%	
Wet GP%	51.0%		
Dry GP%	60.0%		
Gross Profit			
Wet	£107,100	107100	
Dry	£30,000	30000	
Accommodation	£0		
Other	£5,000		
Net Machine Income (Free of Tie Only)	£0		
Total Gross Profit Cash	£142,100		
Costs as % of Turnover Benchmark			
Wages, Salaries & Other Staff Costs	£33,920	12.8%	12.8%
Rates	£7,950	3.0%	2.9%
Utilities	£10,600	4.0%	3.6%
Repairs, Maintenance & Renewals	£5,300	3.0%	4.0%
Building Insurance	£1,590	0.6%	0.6%
Marketing & Promotion Costs	£13,250	6.0%	6.5%
Telephone	£530	0.2%	0.2%
Consumables	£1,325	0.5%	0.5%
Waste/Cleaning/Hygiene	£1,855	0.7%	0.7%
Professional Fees	£1,855	0.7%	0.5%
Bank Charges	£530	0.2%	0.2%
Equipment Hire etc	£2,120	0.8%	1.5%
Depreciation/Interest Charges	£3,180	1.2%	1.1%
Miscellaneous Costs	£1,060	0.4%	0.2%
COSTS SUBTOTAL	£85,065	34.1%	35.3%
SCORFA (if tied)			
	Annualised Value		
SCORFA 1	£1,000		
SCORFA 2	£1,500		
...	...		
SCORFA N-1	£4,500		
SCORFA N	£650		
SCORFA TOTAL	£7,650		
Total Operating Costs	£85,065		
Divisible Balance (DV)	A	£57,035	
Rental Bid	B	£28,518	10.8% 50.0%
Post Rent Balance	C = A - B	£28,518	
Rent Adjustment	D = C - C'	-£10,875	
Rent After Adjustment	E = C + D	£17,643	
NET POST RENT BALANCE	F = A - D	£39,393	
Manager's Salary (if appropriate)		£0	

HYPOTHETICAL RENT ASSESSMENT UNDER FREE OF TIE OPTION

£86,000	32.5%		
£50,000	18.9%		
£14,000	5.3%		
£7,500	2.8%		
£6,500	2.5%		
£164,000			
£1,000	0.4%		
£25,000	9.4%		
£10,000	3.8%		
£10,000	3.8%		
£210,000	79.2%		
£50,000	18.9%		
£0	0.0%		
£5,000	1.9%		
£0	0.0%		
£265,000	100.0%		
65.0%			
60.0%			
£136,500	107100		
£30,000	30000		
£0			
£5,000			
£0			
£171,500			
£33,920	12.8%	12.8%	
£7,950	3.0%	2.9%	
£10,600	4.0%	3.6%	
£5,300	3.0%	4.0%	
£1,590	0.6%	0.6%	
£13,250	6.0%	6.5%	
£530	0.2%	0.2%	
£1,325	0.5%	0.5%	
£1,855	0.7%	0.7%	
£1,855	0.7%	0.5%	
£530	0.2%	0.2%	
£2,120	0.8%	1.5%	
£3,180	1.2%	1.1%	
£1,060	0.4%	0.2%	
£85,065	34.1%	35.3%	
Additional costs due to lack of SCORFA			
£1,000			
£1,500			
...			
£4,500			
£650			
£7,650			
£92,715			
A'			
£78,785			
B'			
£39,393	14.9%	50.0%	
C'			
£39,393			
N/A			
N/A			
F' = C'			
£39,393			
£0			

Prior Three Years Beer Volumes			
Barrelage Date	Year 1	Year 2	Year 3
Year commencing..			
No. Barrels	260	250	240

(1) Income from Gaming Machines and other entertainments as specified to be included in the Shadow P&L net of associated costs to be shown here. Associated costs to include machine rentals; gaming duties and any other charges

Notes on Cost Assumptions

Wages, Salaries and other staff costs	This will include staff working in the bar, kitchen, door staff, accommodation and management time where appropriate as well as training, holiday cover, uniforms and contract staff cost. If significant income is derived from food or accommodation, or the outlet is large enough to require dedicated management, this may be shown and accounted for separately. In all other cases, adequate provision for cover should be reflected in staff wages
Rates	Rates will be the rates payable or if not available the estimated rates based on the FMT.
Utilities	This will include gas, electricity, other energy source and water and sewerage charges.
Premises Repairs & Maintenance	Building, fabric, internal, external and garden repairs and redecoration
Equipment repairs & maintenance	Includes bar, kitchen, cellar and security equipment and furniture repairs and renewals.
Insurance – Buildings	Insurance cover required and usually provided by the landlord and re-charged to the lessee
Entertainment	Provision for entertainment - this may include Sky, background or live music, karaoke or jukebox and similar costs.
Marketing and promotion	Cost of social media, website, direct advertising, teams quizzes and prizes, in-house promotion and food and drink marketing and offers and other similar costs.
Telephone	Telephone and Internet access costs.
Consumables	Includes catering equipment, tableware, electrical, glassware, barware and optics.
Waste Cleaning & Hygiene	Waste collection, cleaning materials and specialist contract cleaning but not cleaning staff.
Professional Fees	Costs of on-going professional advice including legal, surveyor, accountancy, specialist rental valuation, business advisor, professional membership subscriptions as appropriate.
Bank Charges	Banking and credit card charges
Equipment Hire etc.	Rental costs e.g. coffee machines and including plant
Trade Insurance	Public and employers liability, contents, loss of business, interruption of trade
Regulatory Compliance Costs	To include such charges as gas and electrical certification and servicing, fire/smoke alarms and emergency lighting, lift hoist and similar costs
Licensing & Social	Premises licence and associated fees, late night levy, where

Responsibility	membership of BID, Best Bar None, Pubwatch or other social responsibility scheme evidenced
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Annex B: RICS Guidance

References within this Code to 'RICS Guidance' shall be taken to refer to the Royal Institute of Chartered Surveyors' document "*The capital and rental valuation of public houses, bars, restaurants and nightclubs in England and Wales*" (GN 67/2010) published in December 2010.

Annex B: List of Individuals/Organisations consulted

Admiral Taverns
Adnams PLC
All-Party Parliamentary Beer Group
All-Party Save the Pubs Group
Anheuser-Busch InBev
Arkell's Brewery Ltd
Association of Licensed Multiple Retailers (ALMR)
Association of Valuers of Licensed Property
Barlow Brewery
BIS Select Committee
Black Sheep Brewery plc
Brakspear Pub Company
Bramwell Pub Company
Brighton & Hove Licensees Association
British Institute of Innkeeping (BII)
British and Beer Pub Association
Budweiser Budvar UK Ltd
C & C Group plc
Camerons Brewing Company
CAMRA
Carlsberg UK
Charles Wells Ltd
Daleside Brewery Ltd
Daniel Batham & Son Ltd
Daniel Thwaites plc
Diageo plc
Donnington Brewery
Elgood & Sons Ltd
Enterprise Inns
Everards Brewery
Fair Pint

Federation of Small Businesses
Federation of Licensed Victuallers Association (FLVA)
Felinfoel Brewery Co Ltd
Frederic Robinson Ltd
Fuller Smith & Turner plc
George Bateman & Son Ltd
GMB Union
Gray & Sons (Chelmsford) Ltd
Greene King
Guild of Master Victuallers (GMV)
Hall & Woodhouse Ltd
Harvey & Son (Lewes) Ltd
Heavitree Brewery plc
Heron and Brearley Ltd
Holden's Brewery Ltd
Hook Norton Brewery Co Ltd
Hydes Brewery Ltd
Independent Family Brewers of Britain (IFBB)
Independent Pub Confederation (IPC)
iNTERTAIN Ltd
JC & RC Palmer Ltd
J D Wetherspoon
J W Lees & Co (Brewers) Ltd
Joseph Holt Ltd
Justice for Licensees
Kurnia Group
Liberation Group
Maclay Group Ltd
Marston's plc
McMullen & Sons Ltd
Mitchell's and Butler's
Mitchell's of Lancaster (Brewers) Ltd
Molson Coors Brewing Company (UK) Ltd

Office of Fair Trading (OFT)
Palmers Brewery
Pubs Advisory Service (PAS)
Pubs Independent Conciliation and Arbitration Service (PICAS)
Pubs Independent Rent Review Scheme (PIRRS)
Punch Taverns plc
R W Randall Ltd
Robert Cain & Co Ltd
Route Organisation Ltd
Royal Institute of Chartered Surveyors (RICS)
S A Brain & Co Ltd
SAB Miller
Shepherd Neame Brewery Ltd
Society of Independent Brewers (SIBA)
Spirit
Star Pubs(Heineken)
St Austell Brewery Co Ltd
T & R Theakston Ltd
Timothy Taylor & Co Ltd
Titanic Brewing Co Ltd
Trust Inns
Unite Union
Wadworth & Co Ltd
Wellington Pub Company
Weston Castle Ltd
Young & Co's Brewery plc

Annex C: List of Questions

- Q.1** Should there be a Statutory Code?
- Q.2.** 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.
- 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?
- Q.4** How do you consider that franchises should be treated under the 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.
- Q.6** What are your views on the future of self-regulation within the industry?
- 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*
 - ii. *Principle that the Tied Tenant Should be No Worse Off than the Free-of-tie Tenant*
- 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, if the pub company significantly increases drink prices or if an event occurs outside 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.*
 - iii. *Abolish the gaming machine tie and mandate that no products other than drinks may be tied.*
 - iv. *Provide a 'guest beer' option in all tied pubs.*
 - 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*
- Q.9** Are there any areas where you consider the draft Statutory Code (at Annex A) should be altered?

- 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?**
- Q.11. Should the Government include a mandatory free of tie option in the Statutory Code?**
- 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?**
- Q.13 Should the Government appoint an independent Adjudicator to enforce the new Statutory Code?**
- Q.14 Do you agree that the Adjudicator should be able to:**
- i. Arbitrate individual disputes?*
 - ii. Carry out investigations into widespread breaches of the Code?*
- 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. Requirements to publish information ('name and shame')*
 - iii. Financial penalties?*
- Q.16 Do you consider the Government's proposals for reporting and review of the Adjudicator are satisfactory?**
- Q.17 Do you agree that the Adjudicator should be funded by an industry levy, with companies who breach the Code more paying a proportionately 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?**

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