Pub companies, pub tenants & pub closures: background history (up to 2014)

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Authors: Melvyn Helsey & Antony Seely
Business & Transport Section

Over the last twenty years the number of pubs across the country has fallen significantly, an issue that has aroused considerable popular interest as well as much activity within the House and its Committees. The trend has been associated with an overall decline in beer sales and the growth in the off-licence trade, particularly in the sales of alcohol by supermarkets. For many commentators the most striking aspect of the pubs sector has been the continued market strength of the pubcos – the small number of companies which lease out their pubs – despite consistent complaints that the system for regulating the legal relationship between the pubcos and their tenants is not fit for purpose.

After a series of inquiries by the BIS Committee, in January 2013 the Coalition Government announced it would consult on introducing a statutory Code of Practice and an Adjudicator, based on the model of the Groceries Code Adjudicator, to arbitrate disputes, carry out investigations and impose sanctions where a pubco had breached the Code.[1] A consultation document was published in April 2013.[2] The Government had anticipated publishing its response by the end of 2013, but this was subject to considerable delay. On 3 June 2014 the Government finally announced that it would proceed with the establishment of a Pubs Adjudicator.[3] Provision for the introduction of a statutory Pubs Code for England & Wales, and an independent Pubs Code Adjudicator to enforce it, were included in the *Small Business, Enterprise and Employment Bill* published later that month.

The Bill did not provide for a 'market rent only option': provision to give all tenants the automatic right to choose a free-of-tie agreement. At the Report stage of the Bill on 18 November 2014, the Commons agreed an amendment, tabled by Greg Mulholland, to make the 'market rent only' option a feature of the new regulatory regime.[4] Subsequently in the House of Lords the Government introduced a series of amendments to the Bill to retain this principle, amendments considered, and agreed, by the Commons on 24 March 2015.[5]

This note traces the historical development of policy towards a statutory system of regulation. A second note looks at the passage of the primary legislation to provide for the new Code.[6]

1 The Secretary of State wrote to the BIS Committee setting out his plans at this time (see, *Fourth Report of Session 2013–14: Consultation on a Statutory Code for Pub Companies*, HC314, 22 July 2013 pp25-6). The background to the establishment of this office is discussed in another Library note: *Supermarkets : The Groceries Code Adjudicator*, SN6124, 17 April 2015.

2 Details are collated on the BIS Gov.uk site

3 Department for Business, Innovation & Skills press notice, *Publicans to get a fairer deal*, 3 June 2014

4 HC Deb 18 November 2014 c196, c238

5 HC Deb 24 March 2015 cc1341-56. The *Small Business, Enterprise and Employment Act 2015* received Royal Assent on 26 March 2015.

6 *Pub companies, pub tenants & pub closures: introducing statutory regulation (2014-15)*, SN7074, 6 May 2015.

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1 Introduction: pub closures, beer sales, market shares

The sight of local pubs up for sale, or simply being turned into housing or supermarket convenience stores is a familiar one up and down the country. Anyone living in the same location for over ten years, with the possible exception of some inner city locations, can hardly fail to notice the extent of de-pubbing in their neighbourhood.

The British Beer and Pub Association estimate that the total number of pubs in the UK has fallen by 19% since 2000: from 60,800 to 49,433 in 2012. The split in ownership of pubs is roughly: one fifth owned by brewers and two-fifths owned by pub companies, while the remaining two-fifths are independent.[7] There are no official figures on pub closures published by BIS.[8]

In their industry briefing, the Campaign for Real Ale (CAMRA) confirm this general trend, although they note that determining the number of pubs in the country "depends firstly on how you define a pub". Can one distinguish easily between a pub and a restaurant, or a night club – particularly if the pub has extended its food menu or dance floor, in response to the competition?[9] The Campaign's Pub Watch Survey suggests that the severity of pub closures has eased in recent years, so that, "18 pubs per week closed permanently in 2012 – significantly down from the 52 per week of early 2009 but still a horrible rate of attrition. In recent years." The survey found that "losses have been heaviest in urban areas, particularly amongst pubs outside city/town centres", many of which were "traditional, drinks-led community locals." By contrast active efforts by local planning authorities to ensure communities were served by at least one local had "helped stem losses in villages."[10]

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7 BBPA, *Statistical Handbook 2013 ed*, September 2013 p68 (Table E5). The BBPA publish statistics on its site at: http://www.beerandpub.com/statistics

8 As noted in answer to a PQ, "the Government does not compile statistics on pub closures and has made no estimate of the number of pubs that have closed in the last two years" (HC Deb 18 November 2013 c665W).

9 This definitional issue is also flagged up in, "Are pubs faring well, or are they bidding farewell?", *FullFact*, 2 November 2012. The author focuses on the separate, if related, question of whether the trend in pub closures can be attributed to the level of excise duty on beer. A second Library note looks at this issue: *Beer taxation and the pub trade*, SN1373, 12 June 2014.

10 CAMRA, *Pubs – Facts and Figures*, undated (ret'd 11/11/2013)

The trend in pub closures has been mirrored by a continued decline in beer sales. The BBPA estimated that UK beer volumes have fallen by 35% since 1979 – though over this period, off-trade sales have grown consistently – from just over 12% of UK beer sales in 1980 to just over 47% in 2012.[11]

While it is clear that the number of pubs, and the amount of beer sold in them, has declined, there is little consensus as to the primary causes of these trends, and, whether they are reversible. For some critics, one distinguishing feature of this sector has been the *continued* market strength of those pub companies which lease out many of their pubs - implying that the difficulties the sector has had to respond to wider social changes have been compounded by the approach taken by pubcos to their tenants. The BBPA estimate that pubco-owned leased pubs accounted for 35% of UK pubs in 2000, and this share has fallen slightly to 29% in 2012.[12] The number of pubco-tenant pubs have fallen quite sharply since 2009 – as CAMRA have noted, this is as a consequence of the four of the six biggest pubcos selling pubs to reduce their debts.[13]

2 Pub companies and pub tenants

2.1 The emergence of the pubcos

The pattern of pubs ownership changed fundamentally over the five years following an investigation in 1989 by the competition authorities – the Office of Fair Trading & the Monopolies & Mergers Commission – into the supply of beer.[14]

At this time the market for beer in the UK was dominated by six national brewers: together, they accounted for 75 percent of UK beer production, controlled just over half of all public houses, and a substantial proportion of off-licence sales. Brewer-owned public houses fell into two categories—managed houses, where the publicans and their staff were employed by the brewer, and tenancies where independent publicans rented the public house from the brewer. Under an exclusive supply deal, the 'beer tie', these tenants were required to buy their brewers' products, guaranteeing the brewer an outlet for their product. The remainder of public houses were owned by regional and smaller brewers, such as the Boddington Group, or by individuals whose public houses were described as 'free houses', many of whom were still tied for their beer supplies to national brewers by means of 'brewer loans', loans made at a favourable interest rate in return for a tie.

In their report the Monopolies and Mergers Commission found that a complex monopoly existed in favour of brewers who owned tied houses or who had tying agreements with free houses.[15] The main recommendation of the MMC was that a ceiling be introduced restricting any one brewing company, or group, from owning more than 2,000 on-licensed outlets (the

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11 BBPA, *Statistical Handbook 2013 ed*, September 2013 p9 (Table A1), p14 (Table A6). In 2011 and 2012 the share of off-trade sales fell slightly, but the BBPA still predict that off-trade sales will overtake on-trade sales in volume terms in the coming years.

12 BBPA, *Statistical Handbook 2013 ed*, September 2013 p68 (Table E5). In 2000 pubcos managed 9,100 pubs and leased another 21,300. In 2012 these numbers were 5,400 and 14,400 respectively.

13 CAMRA website, retrieved 3/12/2013

14 The following paragraphs draw largely on, Trade and Industry Committee, *Pub Companies – Second Report of Session 2004–05*, HC 128, 21 December 2004; in particular, "chapter 2: Development of the UK market for beer, 1989-2004."

15 In turn the MMC was replaced by the Competition Commission, which is to be merged with the OFT to form a new single authority charged with enforcing competition law: the Competition & Markets Authority. For more details see, *The UK competition regime*, Library standard note SN4814, 16 January 2015.

majority of which were public houses), thereby increasing competition in brewing, wholesaling and retailing.

The Beer Orders modified the recommendations of the MMC report by requiring all brewers who owned more than 2,000 on-licensed premises to dispose of their breweries or release from their ties one half of on-licensed premises above the 2,000 threshold by November 1992.[16] They also allowed for landlords of premises which remained tied to purchase one brand of draught cask-conditioned beer and one brand of bottle-conditioned beer[17] from any supplier, the so-called 'guest beer provision'. They also forbade ties on non-alcoholic beers, low-alcoholic beers and non-beer drinks.[18] In 2000 the OFT completed a follow-up report on the industry, in which it recommended that most of the Articles of the Beer Orders could be rescinded, as none of the big six brewers had kept estates that were anywhere near the 2,000 ceiling. The Orders were revoked in 2003 on the grounds that the restructuring of the pub trade left no-one to whom the Orders were relevant.[19][20]

The sell-off by the national brewers of their pub house estates saw the emergence of a new business model in this sector: the pub company, or 'pubco'. In this model, a company controls a series of pubs, which it either manages itself, or leases to tenants. Many, although not all, pubco pubs are tied — obliged to buy products, usually beer, supplied by the pubco itself (some pubcos are also breweries and include their own products as part of the tie). Like the brewery pub ownership model, the pubco model and the pubco tie has generated a great deal of criticism – that pubcos are distorting the market, and that the combined cost of tied beer and the rent is too much to provide a sustainable business for pub landlords. At the same time pubcos have argued that these higher prices are justified because lessees pay lower rents and benefit from business support services.

In December 2004 the Trade and Industry Committee published a report on pubcos and the beer trade. The Committee took the view that the sector was competitive, with no single pubco holding a dominant position:

> Under any of the market definitions we have chosen, no one company, be it pubco, brewer or retail pub chain, holds a dominant position in the total market for beer. The largest brewer, Scottish Courage, has a market share of beer supply to the onlicensed trade of 26 percent but does not own a public house estate. The largest company in terms of public house ownership, Enterprise, owns just 15 percent of public houses, all tenanted, to whom it acts as wholesaler, and has no brewing or retail operations. There are sufficient different types of public houses: pubco managed, pubco tenanted, and free houses, for us to agree with the Office of Fair Trading (OFT) when they say "there seems to be a reasonable amount of competition between on-trade outlets".[21]

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16 The *Supply of Beer (Tied Estate) Order* SI 1989/2390

17 Following an amendment in 1997: The *Supply of Beer (Tied Estate) (Amendment) Order* SI 1997/1740

18 The Beer Orders also included The *Supply of Beer (Loan Ties, Licensed Premises and Wholesale Prices) Order* SI 1989/2258, which prohibited brewers from imposing a prohibition on the use of the premises as licensed premises when they disposed of them, required brewers to publish wholesale price lists for beer and not charge higher prices and prohibited them from withholding wholesale beer supplies without reasonable cause.

19 Office of Fair Trading, *The Supply of Beer OFT 317*, December 2000

20 *The Supply of Beer (Tied Estate)(Revocation) Order 2002*, SI 2002/3204 and *The Supply of Beer (Loan Ties, Licensed Premises and Wholesale Prices)(Revocation) Order 2003*, SI 2003/52. On the Government's case for abolishing the Beer Orders see, *Fouth Standing Committee on Delegated Legislation*, 11 December 2002, c 5, cc10-11

21 *Second report of Session 2004-05, Pub Companies*, HC 128, 21 December 2004 p58

The Committee went on to raise concerns about the relative commercial strength of pubcos in comparison to their individual tenants, although it believed that there was "considerable scope for eliminating the root causes" of disputes between tenants and pubcos, and, in particular, "a tenant should never be forced or choose to enter into an agreement without taking proper independent professional advice about the basis of the pubco's offer and the significance of the commitment they are asked to undertake." In addition, the voluntary code of conduct between pubcos and tenants, agreed by the members of the British Beer & Pub Association, should be revised; if the industry failed to implement an adequate voluntary code, the Government should consider statutory regulation:

> This Inquiry stemmed from complaints about inequalities in the contractual relationship between pubcos and their tenants. On the basis of the evidence presented to us we feel that the immediately quantifiable cost of the [beer tie] is usually balance by the benefits available to tenants. However, this does not mean that for every tenant the costs equal the benefits, leading to some tenants getting into financial difficulties. In such cases pubcos could do more to redress the imbalance ...
>
> It is not clear that removing the beer tie would make tenants better off. In practice, pubcos, as property companies, would offset their loss of income from the wholesale price differential (wet rent) they charge by charging higher rents. The pubcos have the right to do this through clauses in their leases and would undoubtedly do so. Pubcos would maximise the rent for their properties as they would have no interest in expanding tenants' businesses. There is a danger that splitting the wholesaling and property functions of the pubcos would only benefit the international brewers who currently control the national distribution of beer. In the main, distribution companies owned by certain international brewers already deliver to the majority of tenanted public houses for the pubcos. Removing the tie would enable them to supply free from tie tenants with wholesale products directly. The national brewers would then have a virtual monopoly on the wholesaling of beer, as they did in the days before the Beer Orders.
>
> Since the British Beer & Pub Association (BBPA) code of practice was updated in 1997 the industry has changed and we suggest that this code of practice should be revised as a matter of urgency. This should involve consultation with the widest range of interested parties. The areas we believe a code should cover include: rent reviews, the role of BDMs[22]; complaint and dispute procedures; disclosure and the availability of information; and the taking of legal and professional advice by prospective tenants. At this stage we do not think a legally binding code of practice necessary, but if the industry does not show signs of accepting and complying with an adequate voluntary code then the Government should not hesitate to impose a statutory code on it.[23]

In its response the Labour Government concurred with the Committee's view that a voluntary code could "go some way" to resolving tenants' concerns, but it went on to raise several objections as to a statutory alternative:

> The Government agrees that a voluntary Code of Conduct, developed by the participants themselves, could go some way to resolving concerns of tenants about their contractual relationships with pub companies. The Government concurs with the Committee's view that prospective tenants should seek independent financial and legal advice before committing themselves to a lease. The Government hopes that the

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[22] 'Business Development Managers' – a role that pubcos use to offer support functions to tenants. Many tenants found their own BDM to be unduly antagonistic or unhelpful. The Committee noted that their performance varied across the industry "from excellent to dire" (para 172).

[23] HC 128 of 2004-05, 21 December 2004 p3, pp62-3

industry will respond positively and constructively to the Committee's recommendation and engage with interested parties to find a suitable way forward.

However, the Government sees difficulties with imposing a statutory Code of Practice upon the industry which would prescribe the terms and conditions for what are commercial arrangements. The Government does not believe that existing legislation would allow it to impose such a Code of Conduct; and believes that any competition concerns that may arise in relation to the behaviour of pub companies would be a matter for the competition authorities, not the Government, to consider and if necessary investigate and take appropriate action.[24]

2.2 The operation of the voluntary code

In its report in December 2004 the Trade & Industry Committee expressed the hope that its successor Committee in the next Parliament would review the situation in the public house industry, "in particular whether the code of practice is working."[25]

In June 2008 the Business and Enterprise Committee launched what, in its view, would be "a short inquiry to establish whether the conclusions of our predecessor still stood." The Committee's report was not completed until May 2009, far longer than expected, "chiefly because of the lack of agreement among our witnesses on almost every point". In addition the inquiry had coincided with a very marked increase in the closures of every type of pub , so that the Committee had had to "look carefully to establish to what extent the difficulties of pubco lessees were the product of tough trading conditions, and if it was clear whether pub closures were more or less prevalent within pubco estates."[26]

While the pubcos and the BBPA attributed tenants' financial difficulties to the general trading environment – new licensing regulations, the ban on smoking in public premises, the strength of the off-licence trade and social trends reinforcing home consumption – lessees argued that the main causes were the level of rents and beer prices charged them by the pubcos. Similarly pubcos had argued that leased pubs were less likely to close than others, as a consequence of the tied model, where lower beer sales could feed through into lower rental costs. By contrast lessees had argued quite the opposite. The Committee noted that the statistics for pub closures showed leased/tenanted pubs doing relatively well – but that these numbers would not capture the number of failed pubs, when a pubco attracted a new tenant. Either way, the Committee concluded that it could not "be confident that pubco lessees are less likely to fail than other publicans."[27]

The Committee went on to consider various aspects of the pubco-tenant contract: the assessment of rents and their review, the restriction of beers on sale through the beer tie, the share of profits between pubco and lessee, the existing mechanisms for resolving disputes. It acknowledged that, for some, the operation of the free market would punish those pubcos who did not support their lessees, but "on the way bad companies will inflict real damage on their direct customers, the lessees, and on their indirect customers, ordinary drinkers." Moreover "the evidence to the Committee shows that the wholesale prices offered to tied

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24 Trade & Industry Committee, *Fourth special report of 2004-05*, HC 434, 14 March 2005 p1

25 HC 128 of 2004-05, 21 December 2004 para 205. The BBPA published a revised code of practice towards the end of 2005, and the British Institute of Innkeepers formed a new company in 2007 to benchmark company codes of practice (HC 26 of 2008-09, para 23).

26 *Seventh Report of Session 2008–09, Pub Companies*, HC 26, 13 May 2009 paras 3-4. The Committee found that around 39 pubs closed each week in 2008, compared with 8 per week in 2004 (para 28).

27 HC 26 of 2008-09 para 35

lessees by the pubcos have increased at a much faster rate than wholesale prices to the free trade or the off-licence sector with the result that lessees of tied pubs are at a significant competitive disadvantage as compared to free of tie tenants and freeholders." The Committee suggested that "this could be a major factor in the failure rate of tied public houses in recent years."[28] As the Office of Fair Trading had taken the view that "there is no significant competition problem in relation to the beer and pub market",[29] the Government "should now assume responsibility":

> There are strong indications that the existence of the tie pushes up prices not just to lessees but to consumers. However, we are wary of simply recommending that it should be abolished; such a move might simply increase the power of brewers or distributors. The OFT has declined to act in the past; we recommend that the Secretary of State refer the matter to the Competition Commission for urgent investigation by a body which has no vested interest in defending its earlier position. However, our provisional view is that the tie should be severely limited to ensure there is proper competition in the market.
>
> Nonetheless, we note that interventions can have unexpected consequences. The Beer Orders led to the emergence of pubcos. Displacing pubcos without considering the market as a whole may put too much power into the hands of brewers and wholesalers. The position of local brewers operating a small tied estate also needs to be considered; we would not wish to damage regional brewers. For these reasons we recommend an urgent investigation, rather than simply making a policy recommendation.[30]

Over the following year there were a number of developments, which lead to the Committee issued a follow-up report in March 2010:[31] principally, mediation talks between industry bodies, associations and pressure groups, and a new Framework Code of Practice published by the BBPA in January 2010.[32] The Committee concluded that it would recommend statutory regulation if these problems for pub tenants continued:

> The 2004 Report and the 2009 Report demonstrated that proposals for reform mean nothing if they are not carried through. The industry now appears to be willing to change and we welcome that. However, past experience has taught us that this is not enough; we have been here before. The industry must be aware that this is its last opportunity for self-regulated reform. If it cannot deliver this time, then government intervention will be necessary. We do not advocate such intervention at this stage, but remain committed to a resolution to all the problems discussed in this Report and those of the 2004 and 2009 Reports. Should those problems persist beyond June 2011, we will not hesitate to recommend that legislation to provide statutory regulation be introduced.[33]

Following the report the then Labour Government announced a number of measures to support community pubs,[34] and set a deadline for the industry to improve the conditions of lessees:

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28 HC 26 of 2008-09 para 193, para 184

29 HC 26 of 2008-09 para 169. See also, *Memorandum submitted by the OFT*, November 2008

30 HC 26 of 2008-09 p4 (Summary)

31 As the Committee noted at this time, "with our encouragement and agreement the Government did not respond to the 2009 Report to allow us to receive a response from industry first" HC 138 of 2009-10 para 4.

32 Details of the Code are on the British Beer and Pub Association website ret'd January 2015.

33 *Fifth report of Session 2009-10: Pub companies: follow-up*, HC 138, 4 March 2010 para 158

34 For full details see, *Eighth report of Session 2009-10: Government response to the Committee's Fifth report* , HC 503, 25 March 2010 (Appendix 2). See also, HC Deb 6 April 2010 c1221W

> [The Government's support package] includes business support, industry standards and consumer choice and community and local authority action. The support measures included in the industry standards and consumer choice sections address the recommendations made to Government on Brulines[35] and the effectiveness of the BBPA Framework Code …
>
> In its support package communication the Government gives the industry until June 2011 to improve. If the Business, Innovation and Skills Committee concludes by then that the Code is not working as well as it should we will consult on putting the Code on a statutory basis with effective enforcement. The Code of Practice should also incorporate a beer/non-beer tie option for tenants with a commitment that the Government will act if the industry does not. In addition the industry should introduce voluntary provision for tenants to offer a guest beer outside the traditional beer tie as part of the code with Government action to introduce an order if industry fails to act.[36]

In June 2011 the BIS Committee launched a further inquiry, to determine "whether the problems raised in the Parliamentary inquiries of 2004, 2009 and 2010 have been resolved or whether statutory regulation is required." In its report, which was published in September, the Committee noted that "the evidence we received continues to demonstrate a high level of acrimony within the industry" with "claims and counter-claims from both sides", illustrated by "the poor relationship between the two key players, the BBPA – the trade association for the pub companies and brewers – and the IPC – the umbrella body representing lessees."[37] Overall the Committee found that the process for pubcos revising their codes of practice in line with the BBPA's new Framework Code had proved very slow,[38] and that the accreditation procedure had little effective sanction for those pubcos who refused to comply:

> The BBPA has shown itself to be impotent in enforcing its own timetable for reform and the supposed threat of removing the membership of pub companies who did not deliver was hollow. The voluntary withdrawal from the BBPA by Greene King, which has suffered no reputational loss as a result, clearly demonstrates that fact.
>
> Furthermore, while the British Institute of Innkeeping (BII) [the professional body for the licensed retail sector, charged with accrediting individual pubco's codes of practice as compliant with the BBPA's Framework Code] may be seen to have done an adequate job in accrediting the new codes of practice, it is clear to us that its enforcement role is fundamentally undermined by a lack of meaningful sanctions for non-compliance. Given the high number of breaches allowed before sanctions would be applied we believe that "naming and shaming" and subsequent withdrawal of BII accreditation is insufficient.[39]

Arguably of more concern, the revision of pubcos' codes of practice had not lead to any significant improvement in the pubco-tenant relationship. As an example, the Committee noted that two separate surveys of lessees – one commissioned by the BBPA & the Independent Pub Confederation (IPC), the second undertaken by the Institute of Public

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35 ['Brulines' refers to flow measurement devices provided by a company of this name that seek to ensure the beer tie contract is being observed and that the tenant is not buying beer outside the contract – see HC 503 of 2009-10 para 58-69. In its 'support package' the Government stated that the industry should voluntarily ensure that all such measuring equipment was calibrated by the National Weights and Measurement Laboratory, or be required to do so by law.]

36 HC 503 of 2009-10 pp5-6

37 *Tenth report of Session 2010-12: Pub Companies*, HC 1369, 20 September 2011 para 7,8,10

38 An appendix to this note reproduces a long extract from the Committee's report on the implementation of the Framework Code.

39 HC 1369 of 2010-12 para 155

Policy Research – found that comparatively few lessees were even aware of their own pubco's code of practice:

> The fact that approximately a third of lessees in both surveys had not even seen a copy of their companies' codes is extremely concerning and runs contrary to what we had been told by the BBPA and its members. In addition, the results from the IPPR that only 17% of lessees that had seen their company's code of practice thought that it would benefit them should be of extreme concern to those in the industry that believe updated codes would be the cornerstone to rebuilding trust between pub companies and their lessees.[40]

The IPPR's survey was published in August 2011, and characterised the tied sector as being under considerably greater financial pressure, compared with pubs free of the beer tie:

- 57 per cent of tied publicans say they are struggling financially, compared to 43 per cent of those who are non-tied
- 46 per cent of tied publicans earn less than £15,000 per year, in contrast to only 22 per cent of non-tied publicans
- 88 per cent of tied publicans who claim to be financially struggling identify the beer tie as one of the most significant factors in their financial problems
- One-third of tied publicans have not seen their pubco's revised code of practice, and only 17 per cent of those who have believe it will benefit them.[41]

Similarly the new codes of practice had failed to solve the vexed issue of how pubcos should use flow monitoring equipment, to ensure individual lessees were complying with the restrictions on the beer they sold under the beer tie, or what consideration, if any, should be given, when assessing lessees' rents, to the principle that a tied tenant should be no worse off than a free of tie tenant.[42] The Committee concluded that "this latest attempt at reform has failed and we neither have the time nor the patience to continue along this path":

> The position of the previous Government—endorsed by the current Government—was that if we so recommended, it would consult on how to put the Code on a statutory footing. It is now time for the Government to act on that undertaking. In its response to our Report, the Government has to set out the timetable for that consultation and begin the process as a matter of urgency.
>
> We further recommend that the consultation includes proposals for a statutory Code Adjudicator armed with a full suite of sanctions. Considering the amount of evidence gathered by us and our predecessor Committees this should not be a lengthy process; and given the Government's undertaking to us we do not anticipate any meaningful delay. Furthermore, we caution the Government that offering a compromise of non-statutory intervention would be a departure from its undertaking to us and would not bring about the meaningful reform that is needed.
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> We have not come to this decision lightly and we are firmly of the view that statutory regulation should only be used as a last resort. However, our hand has been forced and we see no other alternative for an industry which has for too long failed to put its own house in order.[43]

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40 HC 1369 of 2010-12 para 34
41 Glenn Gottfried and Rick Muir, *Tied down: The beer tie and its impact on Britain's pubs*, IPPR August 2011 p2
42 HC 1369 of 2010-12 paras 53-55, paras 65-68
43 HC 1369 of 2010-12 paras156-8

In November 2011 the Coalition Government published its response to the Committee's report. Although it had been the Committee's view that the new Government had agreed that it would consult on statutory regulation if the Committee recommended this, the Government announced a new 'self-regulatory package'. In coming to this decision, the Government stated that it had "borne in mind the following principles":

- That the OFT has found no evidence of competition problems that are having a significant adverse impact on consumers and therefore the Government is not minded to intervene in setting the terms of commercial, contractual relationships.
- That legally binding self-regulation can be introduced far more quickly than any statutory solution and can, if devised correctly, be equally effective.[44]

The Government also raised doubts that the beer tie made pubco lessees more vulnerable to closure:

> In its report, the Committee has made a number of criticisms of the beer tie; that is, the practice whereby pubcos oblige a licensee to purchase beer through the pubco rather than on the open market. The Government would note that the beer tie is considered lawful practice and that whether or not a lease or tenancy includes a tie is a commercial decision on the part of both parties. Furthermore, tied pubs are run under widely different types of agreements: in particular the long term lease model and the traditional tenancy model of operating offer very different terms and fulfil different market needs.
>
> Whilst the Government recognises that pubs face a wide range of challenges in the current economic climate, it sees little evidence to indicate that tied pubs are more likely to close, as has been suggested. In addition, 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. Data produced by CGA Strategy clearly shows that between December 2008 and June 2011 more free-of-tie pubs closed than tied pubs, both in absolute figures and as a percentage of the total number of pubs in that category.[45]

The details of a new 'self-regulatory' package were as follows:

> Following intensive discussions … the industry has committed to implement a range of substantive reforms. The key elements of this self-regulatory package are:
>
> - The Industry Framework Code to be made legally binding, by incorporating the Code by reference into new agreements and via a collateral contract for existing lessees.
> - A Pub Independent Conciliation and Arbitration Service (PICAS) to be set up under the umbrella of PIRRS. PICAS would provide mediation and arbitration on any matter relating to the Framework or Company Codes and the results would be binding on both parties.
> - A three-yearly reaccreditation process for Company Codes, administered by BIIBAS through examination of annual compliance reports and spot-checks.
> - A new Pubs Advisory Service (PAS), which would provide an initial offering of free advice to all prospective and current tenants and lessees.

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[44] *Government Response to the House of Commons Business, Innovation and Skills Committee's Tenth Report of Session 2010–2012: Pub Companies*, Cm 8222, November 2011 p3

[45] Cm 8222, November 2011 p3

- A strengthened Framework Code, with a particular focus on FRI leases. This will bring about immediate improvements in particular in areas such as rent, insurance, Business Development Manager (BDM) training, dilapidations and pre-entry training, combined with a commitment to discuss further improvements with industry partners.

… Making the Code legally binding and setting up an independent arbitration service will deliver the same outcomes as the Committee's two principal recommendations – to make the Industry Code statutory and to establish a code Adjudicator.

Making the Code legally binding will have the same outcome as making it statutory, as it will allow the Code to be enforced through the courts. Similarly, the establishment of PICAS and PAS, together with the three-yearly re-accreditation process enforced by spot-checks by an independent body, will have a similar effect as establishing a public Adjudicator.[46]

In coming to this conclusion, the Government noted the final decision by the OFT, published the year before, on CAMRA's application that it undertake a formal investigation of the sector.[47] The OFT had concluded that it had "not found evidence of competition problems that are having a significant impact on consumers":

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 consumers are benefiting from significant competition and a choice between different pubs. We consider that in such a competitive market, any strategy by a pub company which compromises the competitive position of its lessees would not be sustainable, as this would be expected to result in sales and margin losses for the lessee and, in turn, for the pub company. To that extent, pub companies' commercial interests would appear to be aligned with the interests of their lessees.

Further, we do not consider that tied lease agreements prevent pubs offering a wide choice to consumers. The evidence demonstrates that large pub companies which supply beer to their tied pubs are generally sourcing from a considerable range of suppliers and there appear to be significant opportunities for access by brewers to pubs and other on-trade outlets.[48]

Despite many lessees making representation about the behaviour of pubcos, the OFT took the view that these practices were not having a detrimental impact on consumers:

We are aware that some lessees are dissatisfied with the prices and rent levels that they pay to their pub landlord, and/or with the rent assessment process more generally. We received a large number of submissions from individual pub lessees outlining such concerns. 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.

As such, we do not consider that lessees' concerns regarding terms of supply, the conduct of negotiations with their pub company, or issues raised in the super-complaint

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46 *op.cit.* p4

47 This procedure is known as a 'super complaint'. This is defined under section 11(1) of the *Enterprise Act 2002* as a complaint submitted by a designated consumer body that 'any feature, or combination of features, of a market in the UK for goods or services is or appears to be significantly harming the interests of consumers'. CAMRA is one of these designated consumer bodies.

48 OFT, *CAMRA super-complaint – OFT final decision*, OFT1279, October 2010 pp 6-7

> regarding rental valuation methods used in the pub industry, are issues for the OFT to address or investigate further.[49]

For its part the Government argued that "the Committee's report must also be considered in the context of the OFT's second ruling on CAMRA's super complaint, which concluded there are no competition issues which significantly adversely affect consumers":

> In such a situation, for Government to intervene in setting the terms of commercial, contractual relationships could set a dangerous precedent.
>
> There are also pragmatic reasons to prefer a self-regulatory solution over a legislative solution. To consult on and introduce changes by statute would take significant time; certainly months, possibly years, whilst it is clear that the challenges facing the pub industry are ones that must be addressed now. Equally, legislation is inflexible and difficult to alter, should future market conditions change.
>
> Self-regulation, by contrast, can be fast, effective and responsive to the needs of the industry. Provided that the solution is sufficiently binding and enforceable on all parties, there is no reason that it cannot provide the same degree of certainty that would be delivered by legislation. It is, furthermore, a far more appropriate response than legislation in a market where it has been found that there are no competition issues which significantly adversely affect consumers.
>
> Therefore, the Government has decided that a self-regulatory approach, as set out below, is a more appropriate, fast and effective solution than statutory regulation.[50]

2.3 Debate over the merits of statutory regulation

The then Minister for Competition, Ed Davey, appeared appeared before the BIS Committee on 6 December 2011. The evidence shows a rather acrimonious session in which the Committee strongly criticised the Government for failing to pursue statutory regulation.

As part of his evidence, the Minister underlined what he saw as the difference between the pub sector, and the groceries sector – where long-running concerns about the dominant position of the supermarkets had resulted in the Government's decision in May 2011 to establish a statutory ombudsman.[51] The Committee Chair, Adrian Bailey, quoted the Minister as saying, "for Government to intervene in setting the terms of commercial, contractual relationships could set a dangerous precedent." Nevertheless "you are proposing to do that in the Groceries Code Adjudicator Bill. Why, if it is so dangerous, is it okay there and not in this context?" Mr Davey responded by saying, "I am very grateful for these questions, because you are helping me elucidate the big difference":

> Because there is the issue of competition in the case of the Groceries Code Adjudicator, as found by the independent competition authorities, we therefore felt that there was a case to act on the grounds of competition and consumer detriment, which is the status and locus of the OFT.
>
> The independent competition authorities did not so find in this case. That is why we put so much weight on these competition reports. That is the right thing to do. The reason why successive Governments have moved over the past 20 to 25 years to having

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49 op.cit. p7
50 Cm 8222, November 2011 p10
51 For details see, *Supermarkets : the Groceries Code Adjudicator*, Library standard note SN6124, 1 March 2013

> independent competition authorities is to ensure that Government intervention is not in any way a knee-jerk or unconsidered or in any way unfair. It needs to be balanced, so I therefore put a lot of weight on independent competition authorities and their reports.[52]

The Minister was also asked how long it might take for the Government to introduce statutory regulation, if it wished to:

> Clearly, we would have had to draw up a consultation paper; we would have had to consult for at least three months; we would have had to review that consultation and responded to it; we would then have had to instruct parliamentary counsel; we would, as we have done with the Groceries Code Adjudicator Bill, have had pre-legislative scrutiny. After that process, which would clearly have taken up to a year, we would then have had to fight for a slot in the legislative sessions.
>
> I do not think it is any secret that it is going to be a real scrabble to get all the Bills the different Departments want in the second Session starting next May. It would have been inconceivable that such a Bill would have got into the second Session, so we would have been looking at the third Session. It is already clear that Departments are manoeuvring to ensure they secure their slot in the third Session, so you might have been looking at a fourth Session Bill, with political will.
>
> [By contrast] the process we are undertaking means that the code of practice will be legally binding on the big pub companies from this Christmas.[53]

In January 2012 the House debated this issue and MPs agreed a debate motion, moved by the BIS Committee Chair, that criticised the Government's decision over regulation, on the grounds that, "only a statutory code of practice which includes a free-of-tie option with an open market rent review and an independent adjudicator will resolve the contractual problems between the pub companies and their lessees."[54] Opening the debate Mr Bailey argued that pubco-tenant relationship was a major driver of the rate of pub closures:

> Even in my local area, where 10 years ago there were four pubs within a mile, only one is left. I know that experience is shared by Members up and down the country. There is obviously something profoundly wrong in the industry. Some of it is about social changes, but, to go to the heart of the problem, a huge volume of evidence now shows that the business model governing the relationship between pub licensees and the pub companies that own the pubs is crucial. The code of practice that governs the relationship between them is heavily weighted in favour of the pub company.[55]

Mr Bailey also argued that any future consultation on statutory regulation would have to be tailored to mitigate the impact of the industry's lobbying efforts:

> The motion does not call for immediate statutory legislation. The original recommendations of the Select Committee were predicated on the assumption that any such statutory intervention would arise from genuine and inclusive consultation, but the overwhelming evidence … is that the process is being driven by the BBPA. It is for that reason that I included in the motion a requirement that an independent panel be set up, with membership approved by the Select Committee, to ensure that any

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52 *Pub companies – Oral & Written Evidence: 6 December 2011*, HC 1690-i, 11 January 2012 Ev4, Q28
53 HC 1690-i of 2010-12 Ev5, Q36
54 HC Deb 12 January 2012 c400
55 HC Deb 12 January 2012 c352

> assessment of the processes that the Government undertake to deliver their proposals is monitored, and that recommendations can subsequently be made.[56]

In his response, the Minister, Mr Davey, addressed the issue of the Government's consultation, and the controversy over the role taken by the BBPA:

> There have been suggestions of collusion, with allegations that in the process the Government listened only to the BBPA and were deaf to the voices of licensees. That is simply not true … During this process, I have read copious reports on and information about the concerns of licensees, and we have taken action to address their concerns when we have felt that action is appropriate. …
>
> The Government have now released more than 90% of the documents requested under the recent FOI request [for material relating to this consultation], and more than 500 pages of documentation can now be found on our website, including discussions and minutes of meetings with the BBPA, the ALMR and CAMRA. They show clearly that we listened to all sides and negotiated hard with the BBPA.[57]

Mr Davey went on to argue that there was no evidence that the beer tie was penalising drinkers, while there were indications that the market was responding to the problems identified in the pubco-tenant relationship:

> I have always been worried by the [beer] tie, primarily because I had assumed that it must be interfering with competition and was therefore against the interests of consumers. That is why, like others, I was keen for our independent competition authorities to consider the matter. The OFT's investigation concluded that consumers are well served by British pubs, that there is choice and that a wide variety of beers is available. To override an independent competition authority would be a serious decision for a Minister to take and would require significant evidence that the authority had failed to deliver. As CAMRA decided not to challenge the OFT further [after their decision regarding the super-complaint in October 2010], presumably it did not have further evidence; we certainly did not …
>
> Secondly, when one examines where the relationships between pubcos and licensees have gone wrong, it quickly becomes clear that the major problem is not with the traditional tied tenancy, but with full repairing and insuring leases, which are mostly, but not exclusively, used by the pubcos. There are problems with pre-entry training, transparency and rent guidance not being followed, but not with the basic question of whether a pub is tied for beer. That is why my solution targets full repairing and insuring leases and leaves alone the traditional tied tenancy model, which is used successfully, and for the most part amicably, by local and regional brewers alike.
>
> Thirdly, the market is driving a solution. The figures show that since December 2008, slightly more free-of-tie pubs closed than tied pubs. That is true whether one uses the gross closure rate or the net closure rate, which CAMRA says is more important as it takes account of churning. Furthermore, big pubcos are selling off hundreds of pubs a year, many of which are being bought by family brewers or converting to being free-of-tie. Since December 2008, three times as many free-of-tie pubs have opened than tied pubs and a further 1,300 pubs have converted from being tied to free-of-tie. Where the market is working, the Government do not need to intervene.[58]

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[56] *op.cit.* c355

[57] *op.cit.* c395-6. Material published following this FOI request is collated on the Gov.uk site.

[58] *op.cit.* cc397-8

In October 2012 the Secretary of State, Vince Cable, gave evidence to the Committee on the department's 2012 annual report, and on this occasion he was asked what progress the industry had made in establishing a legally-enforceable strengthened code of practice. He acknowledged that, to date, the answer was very little:

> There is a code of conduct for the industry that is under negotiation but has not yet appeared. That is the complaint that I have had from people representing pubs: they were waiting to see the impact of this code of conduct and they have not seen the impact of it yet. I keep asking about this, because I am as concerned about it as you are, and I continue to get the same complaints, particularly about enterprise. My understanding is that there has been a lot of to-ing and fro-ing, but that the strengthened code of practice has not been agreed. It is … very disappointing that that is the case.[59]

In December the Secretary of State wrote to the Committee, noting limited progress while confirming that the changes were not "as far reaching as I would have liked." As a consequence he was considering "further options" and would set out the Government's intentions the next month:

> Further to my appearance in front of your committee … I wrote to Rodger Vickers (Chair of the Pubs Independent and Conciliation and Arbitration Service – PICAS) on 7 November, copying the letter to British Beer and Pub Association (BBPA), the British Institute of Innkeeping (BII), the Association of Licensed Multiple Retailers (ALMR), the Federation of Licensed Victuallers Association (FLVA), the Guild of Master Victuallers (GMV) and the Independent Pubs Confederation (IPC). My letter asked for evidence on how the self-regulatory approach announced in December 2011 was working. I received 19 responses to the letter …
>
> Version 5 of the Industry Framework Code was made binding in contracts at Christmas in 2011. Some respondents were not convinced that the code was indeed legally binding, though all large pub companies have said that they will be bound by it … The FLVA, ALMR, GMV and BBPA are negotiating Version 6 of the Code, and see opportunities for further improvements. The IPC was involved in early meetings with the BBPA but this engagement lapsed due to a disagreement as to whether the question of whether or not there should be a free of tie option was open for discussion.
>
> PICAS was launched in March 2012, and became operational in June 2012. It has so far heard two cases (both found against the pub companies), with further cases pending. One of the two successful claimants said "The administration of the PICA service was straightforward and efficiently handled and the communication was clear from the start and up to the panel hearing. The actual hearing [chaired by Rodger Vickers] was and the questioning from the panel afterwards was relevant and fair" …
>
> A new Pubs Advisory Service has been established by an independent tenants' group; however, it is not clear from the consultation how substantive a service this provides to tenants. The BII and FLVA are also exploring setting up their own advice services …
>
> Having considered the evidence, although the industry has implemented Version 5 of the Code and made other improvements, notably on setting up PICAS, the changes are not as far-reaching as I would have liked and do not appear to have engendered the culture change that is needed. Many of the responses I received show clear

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[59] Business, Innovation & Skills Committee, *BIS Annual Report and Accounts 2011-12: Oral & Written Evidence*, HC702-i & ii of 2012-13, 7 May 2013 Ev 17, Qs 118-9

> evidence that significant numbers of individual publicans are continuing to face serious hardship and difficulties in operating in this industry.[60]

In January the Secretary of State wrote to the Committee, confirming that he would launch a formal consultation in spring 2013, on established a statutory Code and Adjudicator, in line with the Committee's recommendations in their 2010 report. Mr Cable set out his reasons for this decision as follows:

> Although many pub companies behave well, the evidence I have received makes it clear that in too many cases licensees 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.[61]

Mr Cable went on to give an outline of how a new statutory framework would work:

> The proposed Code will be based on the existing Industry Framework Code, but it will be strengthened to include both an overarching fair dealing provision and also the fundamental principle that 'a tied licensee should be no worse off than a free-of-tie-licensee.' 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. This will help protect small businesses—the many thousands of publicans across the country—who may currently be disadvantaged.
>
> 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 licensees, including about whether or not a rent review has genuinely been conducted on an 'open market' basis, in accordance with the new statutory Code;
> - 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 licensees on the Code;
> - Report annually on his or her work;
> - Recommend changes to the Code.[62]

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60 *Fourth Report of Session 2013–14: Consultation on a Statutory Code for Pub Companies*, HC314, 22 July 2013 pp23-4

61 HC 314 of 2013-14 p25

62 HC 314 of 2013-14 pp25-6

Initially Mr Cable anticipated that the new regime "should apply to all pub companies with a tied estate of more than 500 tied leases, 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." He also confirmed that he was **not** proposing abolishing the beer tie:

> The evidence strongly suggests that the tie, per se, is not the issue: when operated as envisaged and fairly, it is a valid business model being used responsibly by companies both large and small and, 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 proposals would address abuses of the tie, through enshrining the principle that 'a tied licensee should be no worse off than a free of tie licensee' in the Code, whilst not impinging on the business practices of companies that are using the tie responsibly.[63]

2.4 The Government's consultation

The Government published its consultation document – *Pub companies and tenants* – on 22 April 2013. Responses to the consultation were invited by 14 June. The document argued that "there has been a lack of necessary culture change within the industry … 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":

> 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.
>
> This problem can be exacerbated by tenants who go into the pub sector as a 'lifestyle choice' rather than as a commercial business decision.[64] Many publicans do not shop around for pubs or invest based on business 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 tenants.[65] 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.
>
> 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

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63 HC 314 of 2013-14 p26

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

65 "BII: we must raise literacy and numeracy", *Morning Advertiser*, 22 June 2009

> of the hardship many publicans face including the possibility of losing their home (which is the pub).[66]

The paper went on to underline that the Government was intervening "not on grounds of competition, but on grounds of fairness for tenants":

> 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."*
>
> 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.[67]

As indicated in the Secretary of State's letter to the Committee, the central proposal in the consultation was the creation of an Adjudicator to enforce a Statutory Code of Practice. The paper asked for views on what powers the new office should have, what sanctions it could impose, and how the office should be reviewed and funded. The Government's initial view is that the Code would be binding on pub companies with 500 or more pubs – as the vast majority of complaints are made about the seven largest pubcos, and restricting the Code this way would focus 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."[68]

Respondents were also asked if the Statutory Code should include a mandatory 'free of tie' option,[69] and if there were other ways to ensure how tied tenants could be made no worse off than free-of-tie tenants. On the 'free of tie' issue, the consultation document noted the strong division of opinion about the implications of allowing tenants to leave the beer tie:

> 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

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66 *Pub companies and tenants – a Government Consultation*, April 2013 para 3.3, 3.4-6

67 *op.cit.* paras 3.9-10

68 *op.cit.* para 4.15

69 ie, 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

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.[70]

The paper went on to note that past history would indicate that one needs to approach any confident prediction as to future trends with some caution:

5.32 The Government is very mindful of the dangers of unintended consequences. The last major Government intervention into this market, the Beer Orders, led to the unanticipated rise of the major pub companies and, arguably, contributed to the concerns that the industry faces today. It is 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.[71]

The paper went on to consider the limited evidence there was on the impacts, both positive and negative, that might arise from this reform:

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.

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70 *op.cit.* pp 29-30

71 *op.cit.* pp 30-31

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.[72]

Given these uncertainties, the paper concluded that there was insufficient evidence at present to be at all confident about the implications of the free-of-tie option, so that respondents were invited "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."[73]

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[72] *op.cit.* pp 31-33

[73] *op.cit.* para 5.41. see also, BIS, *Pub companies and tenants: impact assessment*, April 2013 pp23-25

Finally, the paper also asked for views on whether the Statutory Code should address other issues related to the balance of risk and reward between pubcos and tenants: specifically,

- provision for a tenant to request an open market rent review;
- requirements on pubcos to publish information for tenants to improve transparency;
- the 'amusement with prizes' (AWP) tie, which determines the income pubcos may take by leasing gaming machines to their tenants;
- the option for tenants covered by the beer tie to sell a 'guest beer'; and,
- the legitimate use of data from flow monitoring equipment by pubcos.

In July 2013 the BIS Committee published a report on the consultation in which it strongly welcomed the Government's proposal for an Adjudicator and Statutory Code of Practice, though it raised concerns about any further delays in their introduction:

> Now that the legislative route is being proposed, the timetable will need careful consideration. There is little in the proposals which has not been considered at length by this Committee, its predecessors, and the industry. Therefore, the Government's response to the consultation should not be a time-consuming exercise.
>
> We do not consider that pre-legislative scrutiny is necessary on this occasion. As we have said, much of the detail has debated at length … Furthermore, the Government has highlighted the parallels between the proposals and the statutory arrangements for supermarkets … As this is a devolved matter the consultation proposals apply to England and Wales only ... Given that the issues are similar in all parts of the United Kingdom we would urge the Government to seek speedy agreement with the devolved administrations to ensure that any future legislation can cover all parts of the UK.
>
> We believe that with the right level of commitment from Government, a Bill could be introduced in this Session of Parliament. At the very least, the Government must bring one forward at the start of the next Parliamentary Session. We will expect the Department, in its Response, to provide us with a timetable for its introduction. There must be no more delays in resolving this matter.[74]

On the detail of the consultation, the Committee supported the introduction of a free-of-tie option, and the use of a threshold – though in the latter case, it argued that the legislation should allow for the 500 pub limit to be amended easily:

> The mandatory free-of-tie option is seen by many lessee organisations as a key tool to address the imbalance in risk and reward. It is also the option which is resisted most vigorously by the BBPA. It is for the Government to decide, on the balance of evidence, whether this should be included in a Statutory Code. We have not previously recommended the abolition of the tied model but we do support a free-of-tie option. If the tied model is proved to deliver significant benefits to the lessee, then the option would not be taken up, and the tied model would remain …
>
> We understand the rationale for setting a threshold for the Statutory Code. However, we see merit in including a level of flexibility in any Bill to allow the Secretary of State subsequently to alter the threshold in the interests of the industry.[75]

The Committee also raised concerns about the future of the existing arbitration services used by the industry:

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[74] *Fourth Report of Session 2013-14: Consultation on a Statutory Code for Pub Companies*, HC 314, 22 July 2013 paras 51-55

[75] *op.cit.* paras 31, 38

> The Pub Independent Rent Review Scheme (PIRRS) and the Pub Independent Conciliation and Arbitration Service are the two industry bodies which provide resolution and arbitration services to lessees. PIRRS was established following our predecessor Committee's 2009 Report and was specifically designed to provide a low-cost rent dispute system. PICAS was established as part of the Government's self-regulation proposals to provide "mediation and arbitration on any matter relating to the Framework or Company Codes". Bernard Brindley (BII) explained that while both PIRRS and PICAS were administered by the BII, "they are controlled by a separate board completely" …
>
> Both PICAS and PIRRS have been positive developments in the pub industry but we are unclear as to how they will fit into a new statutory landscape. The Government needs to ensure that, whichever route it takes, the role of these two arbitration bodies is not lost as a result of a statutory/non statutory split in the oversight of the industry.[76]

Finally, on the question of the Adjudicator's sanctions, the Committee argued that the new office should have the power to fine individual companies which infringed the Code:

> When we undertook pre-legislative scrutiny of the draft Groceries Code Adjudicator Bill, we recommended that the Adjudicator have the power to fine. The Government accepted this recommendation during the Bill's passage through Parliament. We recommend that the Government provide similar powers to this Adjudicator.[77]

2.5 The Government's response to the consultation

On 13 December 2013 the Government published the responses it had received to the consultation exercise. In an introduction to this material the then Minister for Consumer Affairs, Jo Swinson, noted that the response "has been staggering and demonstrates the depth of feeling on the issue", with 1,120 written response and 7,038 responses to an online questionnaire. Ms Swinson went on to state that the Government would decide on its next steps "very soon":

> While we had intended to publish our response to the consultation before the end of the year, and I understand that those affected by the proposals need clarity from us, it is important that we do not rush into a decision. We promised Government intervention to address the unfairness in the relationship between pub companies and tenants and this remains our commitment. We also said that intervention would be proportionate and targeted and, in taking the time to process, evaluate and assess the excellent response to the consultation, that remains our goal. We will decide on the next steps very soon.[78]

This material, in several volumes, is collated on the Gov.uk site. It includes economic analysis of the impact of potential reforms on pub numbers and employment levels that BIS commissioned from London Economics.[79] In the latter case the authors underline that although, in their view, "the conclusions we draw … present a significant step-forward in the debate in terms of explaining in some depth the market dynamics faced both by pubcos and individual pubs … [they] cannot be taken to provide a 'cast-iron' estimate of potential impacts of policy reform":

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[76] *op.cit.* paras 40, 46

[77] *op.cit.* para 49. Initially when the Government proposed the creation of the Groceries Code Adjudicator, it had opposed giving the new office the power to impose fines from its inception. This proved controversial, and the legislation to establish the Adjudicator was amended during its Parliamentary scrutiny. For details see Library Research paper 12/44, 14 August 2012 pp27-8 & Research paper 13/05, 10 January 2013 p9, p16.

[78] BIS, *Pub companies and tenants: introduction to consultation responses*, December 2013 pp3-4

[79] As noted when the issue was raised at Treasury Questions on 10 December 2013 (HC Deb c118).

> The tied pub system is one of the most inter-woven industrial relationships you can identify in the UK, with multiple streams of payments running in both directions, from the pub tenant to the pubco and vice versa, generally negotiated on a pub-by-pub basis.
>
> Unravelling these streams, including 'special commercial or financial advantages' (SCORFA) which, by common (dis)agreement are extremely difficult to quantify, has forced us to develop an approach based on testing key assumptions through running multiple scenarios to produce a range of outputs as we do not feel that any model based on the current state of knowledge could be trusted to deliver a valid 'point-estimate'[80], especially in the light of fundamental underlying re-alignments in drinking behaviour in the UK.[81]

Bearing this in mind, the authors suggest that "the reforms proposed in the consultation will close up to 1,600 pubs, although there is very great uncertainty about the precise value"; furthermore, "the key finding of this study is not the number of pubs which may close as a result of one policy or another, but rather the high number of pubs that currently appear to be at the margin of viability." A longer extract from the report's summary is given below:

> The tied pub model is one of the most complex industrial relationships remaining in UK industry and aims to deliver a system to ensure floor levels of demand for British brewers, sustaining diversity and the traditional family brewery model. In recent times, this has become increasingly necessary, as the consumption of beer in pubs has declined, with the numbers of barrels sold falling dramatically as consumption patterns have changed, both due to lower prices in supermarkets and the emergence of alternatives such as restaurants, clubs, and bars. A number of stakeholders interviewed noted that the UK is probably still operating excess pub supply of approximately 6,000 pubs, suggesting a sustainable number of pubs of approximately 45,000.
>
> This over-supply has led to low profitability, both for many tenants and pubcos, particularly in a climate where servicing debt has become difficult. The key finding of this study is not the number of pubs which may close as a result of one policy or another, but rather the high number of pubs that currently appear to be at the margin of viability. Irrespective of what changes may be proposed or considered, the interlocking nature of a large variety of revenue-streams, and the high level of costs being faced by pubcos, suggest that almost any policy reform may have noticeable and unpredictable effects.
>
> In the estimates we produce of the impact of the consultation proposals, even taking account of second order effects, of the 13,300 pubs we believe will be in scope of the Code, up to 2,400 or 18 percent could become unviable for their pubco owners, on top of those already unviable (c.1,300)[82] within the base case scenario, although we estimate a third of these would re-open under alternative management.
>
> The threat that the number of tied pubs currently operated by the pubcos may diminish by between 25-30% due to closures, even if these pubs subsequently re-open under a different owner, and disregarding any who may wish to take up the free-of-tie option, may be sufficient to eliminate the economies of scale in purchasing that many tied

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[80] A 'point-estimate' is a single number output from a model, such as 'my model predicts a team will score one goal' as opposed to a range-estimate, such as 'my model predicts a team will score between zero and three goals'. A 'point-estimate' reflects far higher certainty in the modelling than we feel we can deploy in this case.

[81] *Modelling the impact of proposed policies on pubs and the pub sector*, December 2013 piii

[82] It must be noted that this figure is driven by our assumptions in the calibration exercise and is therefore entirely an artefact of our modelling process.

tenants in this sector (unknowingly) benefit from. This suggests that there is a real possibility that each of the proposed policy reforms, except possibly the code without permitting guest beer, instead of delivering the policy objective of ensuring tied tenants are treated fairly, i.e, 'no worse off' than free of tie tenants, may lead to the end of a large scale tied pub system.

This, however, may not be as disastrous as it initially sounds. The tied pub model is very similar to more standard franchising arrangement, albeit one where the pubco supplies the sales product and leases the property to the franchisee, and this model is already being attempted by some pubcos and may be worthy of further consideration.

In the short-term, it is also worth noting that the PICAS/PIRRS system, which is the most concrete element of the current voluntary framework, is now becoming an established part of the infrastructure, and appears to be having some effect in starting to address the worst tenant circumstances,[83] although some stakeholders have raised the point with us that some tenants are wary of taking the PICAS/PIRRS route in case the discretion available ends up increasing their rental, even though it is recognised in the BIS Committee report that there are flaws in the current system too.

It is our conclusion that the reforms proposed in the consultation will close up to 1,600 pubs, although there is very great uncertainty about the precise value; In particular, the size of the transfer from pubcos to tenants resulting from the 'no worse off' principle is very hard to estimate, our results reflect the impact of a range of possible transfer values; However, there is clearly surplus pub capacity, in quite a volatile market where, with so many pubs on the margin of viability it is hard to determine which pubs will close. Stakeholders raised with us that that there may be up to 6,000 surplus pubs in the UK forming 12% of the market, and if this policy did deliver several thousand closed pubs it would act as a substantial fraction of this long-term trend which is likely to occur unless major changes to tax policy and social norms take place.

If one assumes, as we have done, 60% of consumers move to another pub that implies that, on average pubs which remain will see footfalls 7.2% higher than present. This would be sufficient to turn a poorly performing pub into a more attractive prospect if it can see the immediate future out. As such it may deliver enough of a boost to other pubs to reduce closure rates in the medium term.[84]

The Government's consultation was the subject of an Opposition Day debate on 21 January 2014. On this occasion Toby Perkins, argued that the response to the consultation had demonstrated the case for the establishment of an independent adjudicator, and that the Opposition took the view that legislative proposals for a statutory code of practice should be published within six months:

> The response to the consultation was overwhelming: over 7,000 people responded, 96% were in favour of regulation, 67% were in favour of a mandatory free-of-tie option, 92% were in favour of open market rent assessment, and there was widespread support for a stronger independent adjudicator …
>
> Our motion calls for three key steps to be taken that will ultimately lead to a better future for Britain's boozers. First, we need a mandatory free-of-tie option. The beer tie, whereby landlords can buy products only from their pubco, works for some licensees, but for many others it means that they can buy only limited products at inflated prices. We want every landlord to have the choice of whether to go free of tie … Secondly, we need independent rent reviews. When a new licensee takes over a pub, or when an

[83] Business, Innovation and Skills Committee (2011). 'Pub companies, tenth report of Session 2010-12'.

[84] *op.cit.* pp vii-viii

> existing rent contract expires and is renegotiated, there should be a fully transparent and independent rent review, completed by a qualified surveyor. That would deal with so many of the horror stories that we have heard in this debate and previously. Finally, there must be a truly independent body to monitor the regulations and adjudicate in disputes between licensees and pubcos.[85]

In response the Secretary of State, Vince Cable, argued that the Government needed more time to fully consider all of the responses it had had to the consultation, and, given the complexities of the issue, he would not give a date for this process to be completed:

> We received about 9,000 responses, more than 1,000 of which were very specific—they were often written communications with nuanced arguments, which we must try to address …
>
> Let us also remember that the industry is a complex one, and it was not a simple "yes or no" issue. The consultation also covered a set of other issues, including flow monitoring, guest beer and the gaming tie, each of which must be examined properly, not to mention its open question, which was about the mandatory free-of-tie option and open market rent review … We want to see action, but first we must provide a thorough and proper response to the consultation … Although I am conscious of the legislative timetable, I will not give a specific date on which this report will be concluded.[86]

In his speech Mr Cable addressed the question of whether tied pubs were more vulnerable to going out of business than independents:

> There is quite a lot of debate about the evidence on the speed of closures and how they operate in the tied sector and the non-tied sector. My understanding is that there has been a fairly steady rate of decline, from some 70,000 pubs in 1980 to 50,000 today. Depressingly, that is something in the order of 18 a week net. That decline has continued even after some of the big changes that have taken place in the industry—from the beer orders to pub company consolidation. I know that there is a debate among campaigners about whether tied pubs are more likely to close than pubs that are free of tie, but the evidence I have seen goes both ways. This is not fundamentally an argument about pub closures; it is essentially about the unfairness of and inequalities in the relationship …
>
> To us, the essential point is best captured in the work done by CAMRA that suggests that 57% of tied tenants earn less than £10,000 a year. If we apply that to 35-hour week, 48 weeks a year, we are talking about less than £6 an hour, which means that people are working for considerably less than the minimum wage. Since many work much longer hours, that means that this is a very low-paid industry. Many publicans are struggling. In contrast, only 25% of those who are free of tie are on at the same income level. There is a striking disparity, which is at the heart of the question.[87]

In his speech the Chair of the BIS Committee, Adrian Bailey, said, "there appears to be no coherent logic as to why [the Government's response] has been delayed for so long":

> This is a debate that I never thought we would need to have again. Last year, we were given assurances that a statutory code would be introduced; a year later, there is still no sign of it … I can think of no reason whatever why they could not have introduced

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85 HC Deb 21 January 2014 c167, cc168-9. The Opposition motion argued that "the Government should by July 2014 bring forward legislative proposals to introduce a statutory code of practice of the kind recommended by the Business, Innovation and Skills Committee."

86 *op.cit.* c170, c172

87 *op.cit.* c174, c175

> legislation soon after the consultation process was concluded. There was nothing dramatically different in the consultation from the evidence unearthed by Select Committees or the points made in debates in the Chamber. The Groceries Code Adjudicator Act 2013 could provide a model for that legislation. Although there might be different opinions on different recommendations in the Select Committee report, it would have been appropriate to put those recommendations in legislation and have a debate on them in the Chamber. The different opinions are not in themselves an excuse for legislation not having been brought forward.[88]

In responding to the debate the Minister for Consumer Affairs, Jenny Willott argued that responses to the consultation showed that views "are often polarised on the degree and the nature of the problem, and what the best solutions would be." The Minister went on to say, "we intend to publish the Government's response … as soon as we can, but we are working to reach a proportionate solution that delivers greater fairness for Britain's publicans."[89] In the event the Opposition's motion was defeated by 311 votes to 244; subsequently Ms Willott set out the Government's position on pub closures in answer to a PQ a few days later:

> **Dan Jarvis**: To ask the Secretary of State for Business, Innovation and Skills what steps he is taking to reduce the number of public houses which are closing down.
>
> **Jenny Willott**: The Government values the pub industry, recognises the important contribution that pubs make to the fabric of local communities, and to jobs and growth in the wider economy.
>
> The Government has introduced a number of measures to help pubs. In Budget 2013 the Government announced the end of the beer duty escalator and cut beer duty, so that the tax on a typical pint of beer is 1p lower. In future, beer duties will rise by inflation only. At autumn statement 2013, we announced a major business rates package which will benefit small businesses, including pubs. They will also benefit from the abolition of employer national insurance contributions for under-21s earning below £813 per week from April 2015.
>
> The National Planning Policy Framework makes clear that local planning policies and decisions should guard against the unnecessary loss of facilities such as pubs. We are also helping pubs to become more sustainable through our funding for Pub is the Hub, which is helping pubs to diversify their services. Our funding for the Plunkett Foundation is supporting communities to take over their local pub as a co-operative, and the Community Right to Bid offers communities a chance to save their local pub from being sold and lost to the community by taking ownership of it.
>
> The Government has also consulted on proposals for a statutory code of practice and an adjudicator to enforce the code, to help tied pub landlords by addressing the imbalance in the relationship between pub companies and their tenants.[90]

However, it was several months before the Government published its response to the consultation exercise. On 3 June 2014 the Government announced that it would legislate "at the earliest opportunity" to establish a Statutory Code and Adjudicator. Under the Government's proposals all tied tenants would be covered by a 'Core Code', while an 'Enhanced Code' would cover tenants who are tied to a pub owning company with 500 or

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88 *op.cit.* c182, cc183-4

89 *op.cit.* c211

90 HC Deb 27 January 2014 cc447-8W. see also, HC Deb 31 March 2014 c509W

more tied pubs.[91] The Government's response document summarised the scope of the two codes of practice as follows:

> The Government is committed to ensuring fairness in the industry, and has therefore concluded that a Core Statutory Code should be introduced to provide all tied tenants with increased transparency, fair treatment, the right to request an open market rent review if they have not had one for five years, and the right to take disputes to an independent Adjudicator. We shall consult further on the precise definition of provisions to enable tenants to request a rent review within the five-year period if the pub owning company significantly increases drink prices or if an event occurs outside the tenant's control.
>
> An Enhanced Code will additionally require pub owning companies with 500 or more tied pubs to offer parallel tied and free-of-tie rent assessments to potential or existing tenants if they request them when they are considering taking on a pub tenancy or at the time of their regular tied rent review. Pub owning companies have long held that 'tied tenants are no worse off than free-of-tie tenants'. For the first time in the history of the tie tenants will now be shown whether that is true through the free-of-tie rent assessment provision. It will strengthen the negotiating position of the tenant and incentivise pub owning companies to ensure they are offering a fair share of risk and reward in their tied agreements.[92]

In the light of responses received, the Government proposed that free of tie assessments would be carried out 'on an individual pub basis':

> A tenant would have the right to request this parallel free-of-tie rent assessment once the parties had been unable to reach agreement on a tied rent offer following a period of negotiation. If the tenant requests a parallel rent assessment, he or she would pay a £200 fee to the Adjudicator – the purpose of which is to ensure that tenants consider carefully if the parallel free-of-tie rent assessment is necessary for the negotiation to be concluded successfully. The new Adjudicator will give tenants confidence that if the parallel rent assessment provision is not properly implemented, then they can seek redress from a truly independent third party.
>
> We have listened to concerns from both sides of the debate that the formulaic free-of-tie parallel rent assessment set out in the consultation was too mechanistic and did not take into account the diversity of pub owning company practice in the sector. To remedy this, the Government now intends that the free-of-tie parallel rent assessment should be carried out on an individual pub basis and in addition will require that they are carried out in line with Royal Institution of Chartered Surveyors (RICS) guidance.[93]

The Government decided that the new code would *not* establish a mandatory free-of-tie option, and should *not* include a guest beer option. Pubcos would be able to use flow monitoring equipment to enforce the beer tie but *only* if used with other evidence:

> The Code will not give tenants the automatic right to choose a free-of-tie agreement. The Government acknowledges that such a mandatory free-of-tie option – also known as the market rent only option – is popular with many tenant groups and might arguably offer the simplest way of ensuring a tied tenant is no worse off than a free-of-tie tenant. It would have required companies with more than a certain number of pubs

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91 *Pub Companies and Tenants : Government Response to the Consultation*, June 2014 p96, p3.
92 *op.cit.* p5
93 *op.cit.* p6

> to give their tenants adequate information to decide whether they would be better off under a tied or free-of-tie agreement and then allowed the tenants to go free-of-tie if they wished. However, it would have been likely to cause a high degree of uncertainty in the industry, with a likely negative impact on investment and the possibility that several pub owning companies would abandon the tied market. It would also have unnecessarily risked leading to higher levels of closures and job losses.
>
> For similar reasons the Government has decided not to include a guest beer option in the Code. This would have given tied tenants the right to purchase one beer of their choice from any source. After considering the evidence received, the Government considers that this proposal also carries too great a potential to undermine the tied model as a whole because of the likelihood that tenants would use the provision to purchase their best selling beer (usually a draught lager) outside of the tie.
>
> The consultation proposed that flow monitoring equipment (FME) should not be used in enforcing the beer tie. There was widespread agreement that FME data should not be the sole evidence used to enforce the tie but some confusion over whether the intention was to rule out any use of FME data for enforcing the tie. The intention was not to prohibit the use of FME altogether but to prevent enforcement of the tie based on FME data and the Government has decided to replicate the existing industry framework code provision so that FME data may be used to enforce the beer tie only if it is supported by other evidence.[94]

Finally, in the light of actions taken by the pubcos, the Government decided not to abolish the amusement with prizes (AWP), or 'gaming machine' tie:[95]

> The consultation responses also showed that many of the concerns about the gaming machine tie have now largely been addressed by pub owning companies and in changes to the industry framework code. The active management which pub owning companies provide for gaming machines can help to maximise income for both tenants and the pub owning company. On the basis of this evidence, the Government has decided not to abolish the gaming machine tie. Instead, the Government intends to stipulate in the Statutory Code that tenants should have the choice whether to be tied or not for gaming machines.[96]

On the establishment of the Adjudicator, the Government proposed that its work will be funded an industry levy and that it *would* have the power to impose financial sanctions:

> A new independent Adjudicator will enforce both the Core and Enhanced provisions of the Code with powers to arbitrate disputes, investigate systemic breaches and provide guidance on interpretation of the Code. The Government also intends that the Adjudicator will have the power to impose sanctions – including financial penalties – if it finds that the Code has been breached
>
> Both the Code and Adjudicator will be subject to review, initially after two years and then every three years thereafter. The Adjudicator will be funded by an industry levy which will be set in proportion to the number of tied pubs that each company owns.

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94 *op.cit.* p6

95 This agreement places an obligation on tenants to source their gaming machines through approved suppliers. Tenants then share the profit from the machines with their pub owning company, usually on a 50:50 basis (*op.cit.* p52).

96 *op.cit.* p95

> Over time, those companies that breach the Code will contribute more, which should provide an additional incentive for compliance with the Code.[97]

The department also published estimates of the cost of setting up the Adjudicator, and the number of possible pub closures from this reform:

> The adjudicator is estimated to cost £540k to set up and then £1.75m a year to run. The annual costs are made up of the cost of arbitration £400k, investigations £300k, staff for other functions £470k, appeals £400k and other costs of £180k. These costs will be paid by a levy on business. The cost of carrying out free of tie rent assessments is estimated at £1.6m per year to pub companies and £0.3m to tenants.
>
> Our best estimate is that eventually the policy will indirectly cause 52 pub closures resulting in an indirect cost to business of £2.2m per year …
>
> There will be a cost to pub companies of treating tenants more fairly. The exact scale of this transfer to tenants depends on the level of unfairness currently in the sector. Based on all tenants currently being treated unfairly, we estimate the upper bound of this transfer to be £140m. This cost is offset by a benefit to tenants of the same size.[98]

The department's estimate of the number of pub closures is much lower than that provided by the London Economics analysis, mentioned above. In coming to this view, the department also drew on work commissioned by the BBPA from Compass Lexecon on the possible impact of a mandatory free of tie option:

> 111. In practice we would expect the number of closures to be towards the bottom of [the range of estimates made by London Economics (LE)] … for two reasons. First, the LE research was based on an across the board transfer [of costs following a parallel rent assessment] from pub companies to tenants. As we do not believe there is unfairness in all pub owning company - tenant relationships, we do not expect an across the board transfer.
>
> Second, even where the parallel rent assessment suggests that the tenant should be getting a better deal, there will not be an automatic adjustment in the contract – it will still be subject to a commercial negotiation between the pubco and the tenant. In practice if the pubco indicated that it would have to sell the pub if the tenant were to demand better terms, the tenant may choose to accept the existing terms …
>
> 112. A proportion of the pubs sold off by pubcos might be expected to close entirely. However, this would only be the case where the tenant does not choose to operate as a free house and the pub is not bought by another operator. Based on studies of what has happened recently LE assumed that two thirds of pubs sold would close. Part of the reason for assuming this was to maintain comparability with previous studies; Compass Lexecon use a similar assumption.
>
> 113. However, these estimates are based on historic evidence of the impact of past pub sales. As such, it is not clear that they offer a good prediction of the impact of implementing the mandatory free of tie policy. Past closures would have been those naturally occurring in the market, presumably because a pub was found not to be financially viable at the operating level. In contrast, in the current impact assessment we are estimating the impact of a policy change which might affect the viability of a

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[97] *op.cit.* pp6-7

[98] Department for Business, Innovation & Skills, *Pubs Statutory Code and Adjudicator – Impact Assessment*, June 2014 p2

> particular pub business model (pubcos and tied houses) but which should not affect the underlying economics of the pubs market.
>
> An analogy is with what would happen if a pub owning company ceased trading and put all its full portfolio of pubs up for sale; one would not expect two thirds to cease being pubs. Therefore, we would expect a significant proportion of any pubs sold off by the pubcos to remain in business – either as free houses or purchased by another operator.[99]

In its response document the Government stated that it would seek to introduce the necessary primary legislation to establish a Statutory Code and Adjudicator "at the earliest opportunity."[100] Subsequently, on 25 June the Government published the *Small Business, Enterprise and Employment Bill*; part 4 of the Bill would introduce a statutory Pubs Code for England & Wales, and an independent Pubs Code Adjudicator to enforce it.

The Government has published its response to the BIS Committee's report on the pubco consultation.[101] In its report the Committee had been strongly critical of the amount of time taken by the Government in deciding on a course of action. The Government acknowledged the Committee's regret but went on to argue, "it was important for the Government to give the industry time to change before proposing a statutory solution, which should always be a last resort":

> As the Government noted in its response to the Committee in November 2011, 'legally binding self-regulation can be introduced far more quickly than any statutory solution and can, if devised correctly, be equally effective.' At that time, the Government supported a self-regulatory approach following the industry's commitment to implement a range of reforms. It was also right that the Government did not rush into a decision following the close of the consultation and that we allowed time to process, evaluate and assess all of the responses to ensure that intervention was proportionate and targeted.[102]

The Committee argued that the Government should ensure the 500 pub threshold could be easily amended, that the role taken by existing arbitration systems should not be lost, and that a Pub Adjudicator should have the power to impose financial penalties. The Government responded to these recommendations as follows:

> The Government intends that the legislation will provide for the Code and Adjudicator to be periodically reviewed by the Secretary of State, initially after two years, as with the Groceries Code Adjudicator Act 2013. This would enable the threshold for the Core and Enhanced provisions in the Code to be kept under review. The Secretary of State will have the power to make amendments to the Code, including to the minimum threshold above which the Code applies, following a review; and any changes to the threshold would be subject to scrutiny and approval by Parliament …
>
> The Government sees the merit in tenants having a choice of arbitration mechanism but whether PIRRS and PICAS do continue is essentially a question for the industry. Given the persuasive evidence from the consultation that self-regulation may lapse after the introduction of a Statutory Code and Adjudicator, the Government intends to ensure statutory protection for all tied tenants through the Core Code and Adjudicator...

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99 *op.cit.* pp24-5

100 *Pub Companies and Tenants : Government Response to the Consultation*, June 2014 p96

101 *Government Response to the House of Commons Business, Innovation and Skills Committee's Fourth Report of Session 2013-14*, Cm 8867, June 2014

102 *op.cit.* pp5-6

> The Government intends that the legislation to take forward a Pubs Code and Adjudicator will contain a similar power to that contained in the Groceries Code Adjudicator Act 2013, enabling the Adjudicator to impose a financial penalty on a company if, following an investigation, the Adjudicator finds the company has breached the Code and considers that a fine is the most appropriate sanction.[103]

During the debates on the Queen's Speech the Chair of the Committee, Adrian Bailey, noted the Government's decision not to introduce a mandatory free-of-tie option:

> The proposals for a statutory code and an independent regulator are welcome … However, the failure to commit to introducing a mandatory free-of-tie option will leave publicans feeling let down and disillusioned … The fact is that the overwhelming number of tenants support a free-of-tie option and a mandatory rent review. According to the Government's consultation, 92% of tenants saw the beer tie as their biggest challenge. My conversations with tenants on this issue and the proposals in the Government response indicate that one of the key problems is the deep suspicion of the rent revaluations based on Royal Institution of Chartered Surveyors guidelines; their experience has not given them any confidence that this will significantly address issues that have been so long debated.[104]

In its report the Committee had concluded that while, previously, they had not recommended the abolition of the tied model, "we do support a free-of-tie option." In its response, the Government reiterated its view that the market rent only option would pose a risk to the tied market as a whole:

> The Government is concerned at the potential negative consequences the inclusion of such a provision in the Code could cause, including the impact on investment and the economies of scale from which pub owning companies benefit. In particular, it seems clear that this option would cause uncertainty for pub owning companies and this would have an unpredictable impact on the wider pub sector. Faced with a significant number of their tenants going free-of-tie, pub owning companies may take the decision that it makes business sense to leave the tied market.
>
> This is of course less likely for brewers but is a realistic option for the three large companies that are non-brewers. Some tenants may be content to see the tie broken but from the responses to the consultation, we believe that even among the voices in the industry that are most critical of pub owning companies, many support the principle of the tie. While the mandatory free-of-tie option has undoubted attractions, the evidence suggests that the wider impact on the pub industry is difficult to predict and could pose a risk to the tied market as a whole.[105]

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[103] *op.cit.* pp8-10

[104] HC Deb 11 June 2014 c591

[105] Cm 8867, June 2014 p8; see also, HC Deb 1 July 2014 c541W

Appendix 1: Findings by the BIS Committee on the voluntary code

In its report on the pub companies published in September 2011, the BIS Committee discussed the operation of the voluntary code of practice in some detail. An extended extract from the Committee's report is reproduced below:[106]

*

Previous Committee Reports

In 2004 the Trade and Industry Committee recommended:

> At this stage we do not think a legally binding code of practice necessary, but if the industry does not show signs of accepting and complying with an adequate voluntary code then the Government should not hesitate to impose a statutory code on it.

As a result the BBPA updated and expanded its Framework Code of Practice.

The 2009 Business and Enterprise Committee Report recommended:

> The BBPA's Framework Code of Practice and the recommendations of the Trade and Industry Committee have not solved the problems of inequality in bargaining power and inadequate means to resolve disputes identified in 2004: we believe that more is now needed.

And:

> It may be the industry's problems can be solved by a framework ensuring fairness and transparency in dealings between landlord and lessee. It may be necessary to ensure that inequalities in bargaining power are recognised, even when business contracts are involved. It may be that the beer tie should be prohibited.

In response to the 2009 Report the BBPA decided it would again update its Framework Code of Practice as it did in response to the 2004 Committee Report. The 2010 Business, Innovation and Skills Committee Report which assessed the progress of the new BBPA Framework Code of Practice found:

> We do not believe previous BBPA and pub company Codes of Practice have been sufficiently robust. Nor do we believe the pub companies have properly complied with them. This history of evasiveness and the demonstrable consequences for lessees inevitably requires a critical response to the new Framework Code.

That Report was also disappointed in the delay to the Framework Code being published:

> We are disappointed that it took until the end of January 2010 to publish the new BBPA Framework Code of Practice. We were given sight of a draft Code ahead of the evidence session in December 2009 and the difference between the draft and the published Codes appears to be minimal. This delay put back publication of our Report as it was only fair to let other groups respond to it.

Our predecessors concluded:

> The new Framework Code of Practice appears to be a modest step in the right direction. Of necessity it provides a framework for companies of all sizes. We expect

[106] HC 1369-I , 20 September 2011 pp9-13

> the major pub companies to treat it as an absolute de-minimis requirement and to significantly build on it with their own Codes. Only by doing so will pub companies be able to demonstrate that they are committed to reform. We recommend that our successor committee, at an early opportunity in the next Parliament, assess the extent to which pub companies have built on what is a bare minimum of a Framework Code; and evaluate how effective the new Code has been in improving the relationship between lessees and pub companies. Previous codes have been weaker and not fully observed by the pub companies. We will need to see compelling and continuing evidence by June 2011 that the new codes are being observed and enforced if our successor committee is not to recommend statutory intervention.

Deadlines and delays

The Framework Code of Practice is the industry's 'template' for individual pub companies' codes of practice. The Framework Code was drawn up by the BBPA but individual company codes would be accredited by the British Institute of Innkeeping (BII) which is the professional body for the licensed retail sector. In evidence to the 2010 inquiry the BBPA told us that by June 2010 they hoped most pub company codes of practice would be accredited. Our predecessor Committee believed that the BBPA should be held to its deadline and concluded that:

> The Codes of Practice are moving in the right direction, but they are not yet in place. We will hold the BBPA to its timetable for implementation for the larger pub companies. Any delay beyond June 2010 which is not accompanied with a justifiable reason, will not be acceptable. Furthermore, after the assurances it has given to the Committee, the BBPA not individual pub companies will be held responsible if delays and slippages occur.

It also recommended that the industry:

> Produces a project plan for change with key stages at which it can be marked against achievement. This would make it easier for the industry to see how it is progressing and for our Committee, our successor Committee and the Government to be confident that real change is happening. If slippage in the project plan occurs the Committee and Government must be provided with explanations and industry plans for action to get the timetable back on course.

In July 2010, the month after the deadline, the BBPA wrote to us with details of how the accreditation had progressed:

> All major pub companies have now either had their Codes of Practice accredited by BIIBAS (Punch and Enterprise), or are actively engaged in the process of accreditation which is expected before the end of July (Admiral, Mitchells and Butlers, SNPC, Greene King and Marstons). These companies represent more than 20,000, pubs or 90% of the leased and tenanted pub sector.

In October 2010, the BBPA provided an updated submission which stated that:

> The majority of BBPA members who operate leased or tenanted pubs have now either had their Codes of Practice accredited by BIIBAS or are in the final stages of this process. These companies represent over 23,000 pubs or around 98.6% of BBPA members with leased and tenanted pubs.

That submission also stated that the BBPA "took note of the Select Committee's comments and decided that, in the interests of minimising [cost] burdens [on small businesses], very small companies should have more time to complete the accreditation process". The BBPA

concluded that "We expect such companies, representing 324 pubs, to complete and implement their codes by the end of the year".

The following table, provided by the BII, sets out the accreditation timing for each pub company and highlighted the number of companies which did not meet the June 2010 deadline:

Pub Operating Company	Date of Accreditation
Admiral Taverns	10.11.10
Adnams	16.03.11
Batemans	01.04.10
Brakspears	19.08.10
Charles Wells	30.06.10
Daniel Thwaites	08.09.10
Elgood and Son	26.01.11
Enterprise	30.06.10
Everards	03.12.10
Frederic Robinsons	17.01.11
Fullers	03.06.10
Greene King	13.06.10
Hall and Woodhouse	25.10.10
Heavitree	07.03.11
Holdens	02.06.11
Holts	15.12.10
Hook Norton	18.05.11
Hydes	03.12.10
JW Lees	19.08.10
Marstons	15.07.10
McMullens	26.07.10
Mitchells and Butlers	14.12.10
Mitchells of Lancaster	03.05.11
Palmers	14.02.11
Punch	30.06.10
SA Brains	20.08.10
Scottish and Newcastle	22.07.10
Shepherd Neame	06.08.10
St Austell	07.01.11
Timothy Taylor	28.10.10
Wadworth	09.07.10
Young's	30.06.10

When we asked the BII why some of the codes had still to be accredited, Mr Robertson, Chief Executive of the BII, told us:

> You would probably need to ask colleagues in the pub companies that question. My gentle observation would be that this is a significant departure in practice for some of the companies. Some of the small companies have found it particularly difficult to respond to it. There are one or two smaller ones that have still not got there.

Brigid Simmonds, Chief Executive of the BBPA, reiterated that by July 2010, 10 companies, representing 90% of the pubs in the leased and tenanted sector had been accredited and that "all the big companies had their accreditation in before June 2010; not all were accredited by that time". She argued that smaller companies "would want to wait and see

how the larger companies fared and learn from them" but asserted that "all companies have now put forward for accreditation to BII" although "there are five that still have not been finalised through the process".

While we agree with our predecessor Committee that accreditation had the potential to be more onerous for smaller companies, we note that Batemans, a small brewer pub company, was in fact the first company to have its codes accredited.

When questioned on the cause of the accreditation delays, Brigid Simmons argued that that there had been a queue of companies waiting to be accredited. In a follow-up note to the Committee the BBPA also offered the following two reasons:

1. The setting up and iterative processes involved in the accreditation process were more difficult than originally envisaged, leading to delay for some of those companies who were early into the process.

2. BII took their own legal advice about the legal status of Codes and this delayed the accreditation of some already submitted Codes.

Marston's was one of the larger companies which did not make the deadline. Alastair Darby, Managing director, Marston's Pub Company, explained his experience of the accreditation process:

> We went for our first accreditation hearing during June. There was a queue of companies waiting to be accredited or for their codes to be reviewed. We had a long four-hour meeting with the BII, which resulted in some suggested amendments and changes to our code to improve clarification. We submitted those after that meeting, towards the end of June, and got official accreditation in July. The reason for the delay was purely the process, and making sure that the codes were as clear as they possibly could be in the eyes of BIIBAS, the accreditation panel.

The fact that there were delays was unfortunate, but not entirely unexpected, given the nature of the process. However, the BBPA did not give the impression that it was active in trying to speed up the process. Contrary to the 2010 recommendation, the BBPA did not inform the Committee at the time that it had made changes to its timetable. Nor did it alert the Committee, in advance, to delays in its project plan and supply reasons for it. The BBPA should have been more upfront with the fact there had been slippages and written earlier to explain what they were, what had gone wrong and what the plan of action was to get matters back on track.

The BBPA's failure to supply the Committee with information requested by our predecessor Committee on slippages yet again demonstrates the industry's failure to be transparent and to engage in the process. Just simply glossing over major slippages in their own target without providing any information smacks of complacency and demonstrates an inability to deliver meaningful reform.

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