Department
for Business
Innovation & Skills

PUB COMPANIES AND TENANTS:

Impact assessment

APRIL 2013

Contents

Title: # Pubs Statutory Code and Adjudicator **IA No:** BIS0395 **Lead department or agency:** Department for Business, Innovation and Skills **Other departments or agencies:**	Impact Assessment (IA) **Date:** 15/02/2013 **Stage:** Consultation **Source of intervention:** Domestic **Type of measure:** Primary legislation **Contact for enquiries: James Ravenscroft, 0207 2152171, james.ravenscroft@bis.gsi.gov.uk**

Summary: Intervention and Options

RPC Opinion: RPC Opinion Status

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year** (EANCB on 2009 prices)	**In scope of One-In, One-Out?**	**Measure qualifies as**
-£17.01m	-£16.03m	£1.86m	Yes/No	IN

What is the problem under consideration? Why is government intervention necessary?

For many years serious concerns and numerous complaints have been raised about the relationship between large pub owning companies and their licensees. The focus has been on tied pubs and the share of reward gained by pub owning companies, for example through large unjustified rent increases. Such behaviour is possible due to pub owning companies' better access to information and resources. The tie gives an additional route of abuse and complicates the relationship. Tied licensees are also more likely to face serious hardship. A self-regulatory approach has been tried since at least 2004, with a last chance given in 2011, but this did not work. As such a stronger intervention may now be needed.

What are the policy objectives and the intended effects?

The aim of this policy is to reduce exploitation of pub owning companies' licensees and increase the share of profits going to the licensees.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

Option 1 - continue with self-regulation
Option 2 - a strengthened statutory code and adjudicator
Option 3 - a mandatory free of tie option

Will the policy be reviewed? It will/will not be reviewed. **If applicable, set review date:** Month/Year

Does implementation go beyond minimum EU requirements?			Yes		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	**Micro** **No**	**< 20** Yes	**Small** **Yes**	**Mediu** **mYes**	**Large** **Yes**

What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)	**Traded:**	**Non-traded:**

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible SELECT SIGNATORY: Date:

Summary: Analysis & Evidence

Policy Option 1

Description: Continue with the self-regulatory approach. (Do nothing option)

FULL ECONOMIC ASSESSMENT

Price Base Year	PV Base Year	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
			Low: Optional	**High:** Optional	**Best Estimate:** 0

COSTS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Cost** (Present Value)
Low	Optional		Optional	**Optional**
High	Optional		Optional	**Optional**
Best Estimate				

Description and scale of key monetised costs by 'main affected groups'

N/A

Other key non-monetised costs by 'main affected groups'

N/A

BENEFITS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Benefit** (Present Value)
Low	Optional		Optional	**Optional**
High	Optional		Optional	**Optional**
Best Estimate				

Description and scale of key monetised benefits by 'main affected groups'

N/A

Other key non-monetised benefits by 'main affected groups'

N/A

Key assumptions/sensitivities/risks **Discount rate (%)**

N/A

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			**In scope of OIOO?**	**Measure qualifies as**
Costs:	**Benefits:**	**Net:** 0	No	Zero net cost

Summary: Analysis & Evidence

Policy Option 2

Description: Establish an Industry Framework Code on a statutory basis and an independent Adjudicator to enforce the Code. (Preferred option)

FULL ECONOMIC ASSESSMENT

Price Base Year	PV Base Year	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
			Low: -29.0	**High:** -9.1	**Best Estimate:** -17.0

COSTS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Cost** (Present Value)
Low	0.7		1.0	**9.1**
High	7.2		2.6	**29.0**
Best Estimate	1.2		1.9	**17.0**

Description and scale of key monetised costs by 'main affected groups'

The total one-off costs to the seven affected pub companies of complying with the code are estimated to be £1m. The annual ongoing costs of compliance are estimated as £168k per pub company totalling £1.2m per year. The adjudicator is estimated to cost £220k to set up and £900k per year to run. These costs are based on those for the Groceries Code Adjudicator.

Other key non-monetised costs by 'main affected groups'

N/A

BENEFITS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Benefit** (Present Value)
Low	Optional		Optional	**Optional**
High	Optional		Optional	**Optional**
Best Estimate	0		0	**0**

Description and scale of key monetised benefits by 'main affected groups'

The main benefit and aim of the policy is the estimated transfer from pub owning companies to licensees that is estimated to be £102m per year. This isn't included in the NPV figures as it is a transfer between businesses.

Other key non-monetised benefits by 'main affected groups'

Increasing licensee's share of profits is likely to have a small positive impact on investment and the long term health of the pubs industry. Licensees will have a greater incentive to invest and this is likely to more than offset the reduction in pub owning companies' incentive to invest investment . This is because licensees are better placed to invest and are less likely to be short-termist.

Key assumptions/sensitivities/risks **Discount rate (%)**

The size of the transfer from pub owning companies to their licensees is highly uncertain and we will explore this further in the consultation.
There is a risk that this results in a major disruption to the industry with unintended consequences, such as a pub owning company getting into financial difficulty or selling, closing or managing more pubs.

BUSINESS ASSESSMENT (Option 2)

Direct impact on business (Equivalent Annual) £m:			**In scope of OIOO?**	**Measure qualifies as**
Costs: 1.9	**Benefits:** 0	**Net:** -1.9	Yes	IN

Summary: Analysis & Evidence
Policy Option 3

Description: Mandatory free of tie option with open market rent review

FULL ECONOMIC ASSESSMENT

Price Base Year	PV Base Year	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
			Low: -28.6	**High:** -8.8	**Best Estimate:** -16.6

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	0.7		1.0	**8.8**
High	7.2		2.5	**28.6**
Best Estimate	1.2		1.8	**16.6**

Description and scale of key monetised costs by 'main affected groups'

The total one-off costs to the seven affected pub companies of complying with the code are estimated to be £1m. The annual ongoing costs of compliance are estimated as £168k per pub company totalling £1.2m per year. The adjudicator is estimated to cost £220k to set up and £850k per year to run. These costs are based on those for the Groceries Code Adjudicator.

Other key non-monetised costs by 'main affected groups'

In the short term, the pub owning companies will have higher costs due to a loss of economies of scale. These costs are likely to fall more heavily on smaller pubs (although they may still benefit overall from the policy) because larger volume pubs and multiple operators are more likely to go free of tie. Without the surety of the tie, pub owning companies are likely to invest less in pubs. The loss of scale for UK brewers may result in brewery closures with resulting losses of jobs and exports.

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	Optional		Optional	**Optional**
High	Optional		Optional	**Optional**
Best Estimate	0		0	**0**

Description and scale of key monetised benefits by 'main affected groups'

The main benefit and aim of the policy is the estimated transfer from pub owning companies to licensees that is estimated to be £102m per year. This isn't included in the NPV figures as it is a transfer between businesses.

Other key non-monetised benefits by 'main affected groups'

Increasing licensees' share of profits is likely to have a small positive impact on investment and the long term health of the pubs industry. Licensee's will have a greater incentive to invest and this is likely to more than offset the reduction in pub owning companies' incentive to invest investment . This is because licensees are better placed to invest and are less short-termist.

Key assumptions/sensitivities/risks **Discount rate (%)**

The key uncertainties are the size of the transfer from pub owning companies to their licensees and the number of tied pubs that choose to go free of tie. Both will be explored in the consultation.
This option would be more disruptive than option 2 as it is likely to mean a changes in business model as well as a transfer of profits. Potential outcomes include higher costs for consumers, the exit of a major pub owning company or brewer and dominance of the market by large international brewers.

BUSINESS ASSESSMENT (Option 3)

Direct impact on business (Equivalent Annual) £m:			In scope of OIOO?	Measure qualifies as
Costs: 1.8	**Benefits:** 0.0	**Net:** -1.8	Yes	IN

Evidence Base (for summary sheets)

Background to the pub industry

1. The pub industry faces a range of pressures including the current economic climate, the impact of the smoking ban, competition from supermarkets, improving home entertainment, increases in duty, social and demographic changes and a trend towards drinking alcohol at home.[1] Beer sales in pubs are declining. There has been a big contraction in the industry over the last three decades: from 70,000 pubs in 1980 to around 50,000 today. Over the last 6 months 18 (net) pubs have been closing every week.[2]

2. Despite falling pub numbers there is still competition in the market. In 2010, the 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.”[3] 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.”

Types of pub

3. For this impact assessment, the main relevant differences between pubs are in terms of ownership, management and who they can buy beer from.

Type of pub	Ownership	Management	Buy beer from …	Proportion of pubs in the UK[4]
Managed pubs	Pub company	Pub company manager	Pub company	17%
Free house	Freeholder	Freeholder	Anyone	36%
Leased/tenanted pubs - Free of tie	Pub company	Licensee	Anyone	
Leased/tenanted pubs - Tied	Pub company	Licensee	Pub company	48%

Table 1: Key differences between pubs

4. Obviously the relationship between pub owner and licensee[5] is not a problem for free house or managed pubs as there is no licensee. Despite the potential for problems between owner and licensee, leased pubs are a useful business model offering a relatively low cost entry to the industry. Most leases are either:

[1] OFT, CAMRA super-complaint - OFT final decision, October 2010

1. [2] Figures from CGA

[3] OFT, CAMRA super-complaint - OFT final decision, October 2010

2. [4] Figures from CGA - no distinction is made between free of tie and free house pubs

3. [5] Licensee has a number of meanings and in this document is used exclusively to refer to the person who has the lease or tenancy for a pub from a pub company.

- short-term tenancies – are typically for three to five years, normally with an opportunity to renew the agreement, where the pub company will generally carry out repairs (or structural repairs at least) and the tenancy will not be assignable but can be easily exited, or;

- longer-term lease agreements – are typically for a duration of 10 to 25 years, during which a lessee would be required to carry out full repairs and decoration of the premises and the lease would generally be assignable. A lease agreement will therefore allow a lessee to build up goodwill in a property. This provides a different exit route for a lessee, who is able to assign (sell) the lease. It also allows a lessee to borrow against the lease.

5. A further distinction is between industry and non-industry leases. For industry leases pub rents and valuations are assessed with regard to their trading potential as a pub. For non-industry leases (or traditional commercial leases) valuations and rents are usually based on location and size of the property. Free-of-tie pubs are more likely to have commercial leases.

6. There are a range of other lease agreements. Tenancy at will is a short term agreement that can be terminated by either party without notice. It is often used as a stop gap agreement while a longer term lease is agreed. There is also increasing use of franchise type arrangements from those accredited by the British Franchise Association to agreements which share some but not all the features of a franchise.

The beer tie[6]

7. The beer tie refers to a condition in a lease which requires a licensee to buy beer through the pub owning company, rather than on the open market. Traditionally this involves a discounted property rent, the ‘dry rent’, and above market prices for the beer, the ‘wet rent’. The pub owning company is also likely to provide other services, known as special commercial or financial advantage (SCORFA) such as business development advice, branding or free Sky TV.

Benefits of the tie

8. For the pub owning company having tied pubs provides a guaranteed market for their beer. This gives the pub company economies of scale**.** The impact of economies of scale is seen in the greater discounts brewers give to larger purchasers such as pub companies and wholesalers.[7] For brewing pub owners this provides them with the minimum scale for their brewing operations. For some of the family brewers having a ‘safe market’ of a few hundred pubs is critical to establishing and maintaining their brand and beer sales. For non-brewing companies the guaranteed large order volumes gives them economies of scale within purchasing and distribution allowing them to negotiate discounts from brewers. There are also economies of scale in the other benefits pub owning company offer such as a website, marketing or free Sky TV.

9. The tie is also a profit and risk-sharing mechanism. If the licensee does well (sells more beer) they will pay more ‘wet rent’ and, conversely, in hard times they will pay less. For the licensee this means running a pub costs less up front and has less downside risk. The pub owning company is also an experienced partner with an incentive to help increase sales. The two parties have a shared incentive to invest in the pub. For the pub owning

---

4. [6] There are other ties in operation but beer accounts for the vast majority of sales
[7] OFT, CAMRA super-complaint - OFT final decision, October 2010

company the risk sharing element of the tie makes getting a licensee easier by reducing the upfront cost while not necessarily reducing their overall rent.

Drawbacks of the beer tie

10. Tied licensees have less choice and flexibility with regard to how they run their pub. This can vary from a limit on which beers they stock[8] to restrictions on décor and branding (usually for shorter term tenancies). This is obviously a real downside for the individual publican but doesn't necessarily reduce choice in the market place (see paragraph 22).

11. Profits for licensees of tied products are lower than they would be giving licensees less incentive to sell them. This can be socially inefficient as licensees will not consider the profit that the pub owning company makes.

12. Pub owning companies lose out if the pub does badly, through reduced wet rent, but may have limited control over how the pub is run. Ensuring they have more control is one reason why many of the most profitable pubs are managed pubs.

13. The tie adds an extra layer of complexity to the landlord-licensee relationship compared to a fixed rent and separate beer supply agreement. This complicates the relationship between pub owning company and licensee making it tougher for licensees to know if they are getting a good deal. Many complain that they pay above market rates for beer and while this is a deliberate part of the beer tie it is hard for licensees to judge the fairness of the prices they are charged. This complexity also gives greater potential for abuse.

14. The inability to change supplier also reduces licensees' ability to drive the pub owning company to provide a good service at a good price. The pub owning company does have a strong incentive to provide a good service in order to get high sales and thus a high wet rent. A more likely problem might be pub owning companies providing a poor service that is inconvenient but doesn't necessarily damage trade, for example awkwardly timed deliveries. Another potential problem is if the pub owning company wants to sell the pub to a developer. The pub owning company may deliberately offer a poor service in order to force the licensee out or seek to extract as much rent as possible knowing that the long term viability of the business is not important

The beer tie and pub numbers

15. Overall pub numbers have been in steady decline since at least 1980. The decline has been fairly steady: neither the Beer Orders in 1989 (which established the current non-brewing pub company beer tie system) nor pub company consolidation in the early '90s have seen a major change in the rate of declines. Closures did accelerate somewhat during the recession but have since returned to the previous trend.

16. The decline is widely recognised to be due to a range of factors, including changing cultural habits, increased taxation, the rise of low-cost selling at supermarkets and the smoking ban.

17. Some campaigners argue the tie plays a factor, but pub numbers do not support this. Figures from the latest CGA Study commissioned by CAMRA[9] show that between March 2010 and September 2012 the closure rate was lower in tied pubs, 4.3%, than in free of

---

5. [8] Some pub owning companies do offer their tied licensees hundreds of beers, but some offer a far more limited range. And of course the open market offers even more.

6. [9] The Campaign for Real Ale

tie pubs, 4.5% (see table below). The ‘net closure’ is the more appropriate statistic to use as it takes into account ‘churn’, where pubs close for a short period then reopen. However, if one uses gross closure figures then proportionately even more free of tie pubs are closing, 3.4% versus 5%.

	Free	Tied
Number at March 2010	21601	28404
Number at Sept. 2012	20516	27448
Net closures	-975	-1215
Transfers in	-110	259
Overall change	-1085	-956
Net closure rate	-4.50%	-4.30%
Percentage change	-5.00%	-3.40%

Table 2: Relative changes in tied and untied pub numbers

18. In 2008 and 2009 large numbers of pubs transferred out of the tied sector into the free of tie sector. This led the overall number of tied pubs to fall by over 3000 and the number of free of tied pubs to remain roughly constant. This does not show that the tie is causing pubs to fail, just as the more recent smaller number of transfers the other way does not show that being a free house is causing pubs to close. The two business models have different benefits and movement between them reflects this.

19. More generally these closure figures don’t show whether the tie (or lack thereof) is having an impact. Tied and non-tied pubs differ in other ways that may be impacting these closure figures. For example the OFT “found that [a] higher proportion of free of tie than tied pubs are located in rural areas”. As such, even though free of tie pubs are closing faster this may be nothing to do with the lack of tie.

The beer tie and competition in the market

20. In its 2010 response to a super-complaint from CAMRA, the OFT found no evidence that the beer tie results in competition issues that cause harm to consumers. The OFT reasoned “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.” If pub companies tried to limit choice of beer or raise prices, then consumers would go elsewhere.

21. Consumers have a wide choice of pubs with most pubs operating in areas that include a high number of rival operators. The OFT looked at the number of different rival operators that pubs competed with in narrow geographic areas. Their analysis considered a one mile radius in urban areas and a five mile radius for rural areas. They found that:[10]

- 99.2 per cent of all UK pubs compete in areas that include two or more pubs owned by different operators
- 97.3 per cent are in areas that include three or pub operators
- 87.4 per cent are in areas with six or more pub operators, and
- 65.4 per cent are in areas with 12 or more pub operators.

7. [10] CAMRA super-complaint - OFT final decision, October 2010 paragraph 5.33

22. The OFT did not support CAMRA's claim that the actions of pub owning companies lead to higher retail prices in tied pubs. While the OFT did find beer prices to be higher in tied pubs, it considered other factors likely to contribute to this such as higher rental costs due to more urban locations. Furthermore they found "Large pub companies' gross profit margins have decreased between 2005 and 2010 and consistent with this, prices charged to lessees have increased at a lower rate than the prices charged to pub companies by brewers, suggesting that pub companies have not passed on the full extent of price increases at the brewing level of the supply chain". Across the wider pub market, the OFT found "in the last 10 years, beer prices in pubs have not increased at a faster rate than service sector inflation". Service sector inflation is the appropriate comparator as it includes pub costs such as wages.

23. The OFT did not consider "that tied lease agreements prevent pubs offering a wide choice to consumers". The report states that 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." The OFT found that large pub companies which own tied pubs purchase a considerable volume of beer from micro and regional brewers.[11]

24. A competition assessment will be completed as part of the final impact assessment.

Legal position of the beer tie

25. The beer tie is considered lawful practice.[12] The practice has been found not to be anti-competitive where pub companies buy drinks from a number of sources and are not large enough to contribute to a cumulative foreclosure effect. However, the tie has been found to hinder market access where a significant number of pubs were tied to companies which acquired their beer largely from one source. In these cases the tie benefited from an exemption to competition law as it was found to lead to an improvement in the distribution of beer and provided countervailing benefits for tied lessees.

Problem under consideration and rationale for intervention

26. For many years serious concerns have been raised about the relationship between large pub owning companies and their licensees, particularly with regard to tied pubs. There are numerous complaints of pub companies exploiting their licensees to gain an unfair share of profits. The OFT received a large number of submissions from individual pub lessees outlining concerns about the prices and rent levels that they pay to their pub landlord, and/or with the rent assessment process more generally. The British Institute of Innkeepers has received over four hundred complaints on its hotline over the past three years. Some of these complaints were on other issues but the vast majority were about the pub owning companies with largest number of tied pubs. There are also several other people (usually current or former tied licensees) who act independently and estimate they receive over 10 cases a week that directly relate to the "PUBCO model". There have also been numerous letters to MPs and representations to BIS Select Committee. Even accounting for some overlap, overstatement and mis-categorisation, there are hundreds of complaints per year and these are just those where mistreatment is actually reported.

8. [11] Direct selling to free of tie pubs is the most common route to market, see http://siba.co.uk/wp-content/uploads/2011/02/industry_report_20111.pdf

9. [12] See CAMRA super-complaint - OFT final decision, October 2010 sections 2.31-2.33 for further detail.

27. Examples of the types of unfair behaviour include licensees at rent review being told of large rent increases without justification, misleading estimates of the sales a pub is capable of and overvaluing additional services provided such as business development advice. Such behaviour is possible due to imbalance in the relationship between the two parties - pub owning companies have access to more information and resources. 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 better afford legal and surveyor fees. This problem can be exacerbated by licensees who go into the pub sector as a 'lifestyle choice' rather than as a commercial business decision. Many publicans do not shop around for pubs[13] 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 licensees.[14]

28. 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 licensees to know if they are getting a good deal.

29. Tied licensees are also more likely to face serious hardship - 46% of tied publicans earn less than £15,000 a year, compared to just 23% for licensees who are free of tie. The tie is not universally bad (see paragraphs 8-9) and the latest independent annual survey – conducted by CGA strategy – showed 7 out of 10 licensees would sign up again with their pub owning company (although this does leave up to 3 out of 10 who would not (i.e. 5,000-10,000 unhappy publicans)). The fair working of the beer tie is particularly important because of the hardship many publicans face including the possibility of losing their home (which is the pub).

30. A self-regulatory approach has been tried since at least 2004[15], but this has not worked.[16] As such a stronger intervention may now be needed. A statutory code of practice and an adjudicator would reduce the imbalance between pub companies and licensees and its impact.

31. Secondary to the main rationale is a concern over the long term impact on the industry of licensees not receiving a fair share of profits. An increased share of profits would help reduce the churn of licensees and increase their incentive to invest and innovate. This will help improve the long term health of the pub industry which is of special importance because pubs contribute substantially to community spirit and cohesion.

---

10. [13] In one CGA survey 73% of respondents only looked at one pub owning company.

11. [14] http://www.morningadvertiser.co.uk/General-News/BII-we-must-raise-literacy-and-numeracy

12. [15] The House of Commons Trade and Industry Committee Pub companies report of 2004-05 recommended that if the industry didn't comply with a voluntary code then the Government should impose a statutory code

13. [16] Continuing with the self-regulatory approach is considered under the do nothing option below.

Option 1: Continue with the self-regulatory approach. (Do nothing option)

32. Under this option the industry would continue to progress its current approach. Self-regulation has been tried for a number of years. The industry was given a last chance to make it work in November 2011

33. Some progress has been made since then, notably:

- The industry has implemented Version 5 of the Industry Framework Code of Practice.
- The pub companies all wrote to their tenants in December 2011 to inform them of this change.
- Negotiations are underway with some parties on a further version of the Industry Framework Code.
- The Pubs Independent Conciliation and Advisory Service (PICAS) has recorded 42 enquiries, had three full panel hearings and has others in the pipeline.[17]
- A new Pubs Advisory Service has been established by an independent tenants group; however, it is not clear how substantive a service this provides to tenants.

34. However, problems remain:

- Some in the industry are not convinced that the code is legally binding, though all large pub companies have said that they will be bound by it.
- There has been no co-ordinated communication to tenants about their rights under the code since December 2011.
- At least one pub company incorporates the code into training and some licensee groups actively promote it to their members; however, some groups who do not support self-regulation either don't mention the Code or talk about the Code negatively.
- Even positive developments like PICAS are divisive with its independence being questioned.[18]
- There is continued lack of engagement between parties and an ongoing entrenchment of views which is clearly a barrier to cooperation and progress.

35. This option is likely to continue to deliver small improvements in the treatment of licensees. However, continued wide spread complaints of abuse and the parties difficulty coming together means improvements will be limited. Both sides have admitted that self regulation can't address the issue of rebalancing risk and reward.

36. This option forms the benchmark for the other options and so costs and benefits have not been assessed.

---

14. [17] As of 9th January 2013 http://www.morningadvertiser.co.uk/General-News/PICA-Service-how-does-it-work

15. [18] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/70223/call-for-evidence-new-proposals-to-stand-up-for-british-pubs-and-prevent-unfair-practices-responses1.pdf and further complaints here: http://www.albenhouse.com/#!news/cx3k

Option 2: Establish a strengthened statutory code and an independent adjudicator to enforce the code. (Preferred option)

The Statutory Code

37. The statutory code would be based on the existing Industry Framework Code (version 6), but strengthened to include the overarching principle that 'the tied licensee should be no worse off than the free of tie licensee' as well as other issues of risk and reward. This principle means that the costs of being tied should be equalled or outweighed by the benefits (see the background section for detail on the tie).

38. The statutory code would apply to all pub companies with more than 500 non-managed pubs.[19]

Nature of the Adjudicator

39. The proposed adjudicator will have the power and function to:

- arbitrate disputes between large pub companies and their licensees;
- carry out investigations based on complaints that have been received,
- have wide-ranging powers to require information from pub companies during an investigation;
- impose sanctions including, in the case of severe breaches, financial penalties where an investigation finds that a pub company has breached the Code;
- 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; and
- recommend changes to the Code.

40. The adjudicator would be funded by an industry levy on those who are covered by the statutory code with those who breach the code more paying a proportionately higher levy.

Impact

41. The overarching principle that 'the tied licensee should be no worse off than the free of tie licensee' will mean the projected post rent balance of a tied licensee must be equal or greater than that licensee would receive under a free of tie arrangement. Both rent calculations should use the guidance from the Royal Institute of Chartered Surveyors. The differences will be that the free of tie basis will have beer costs without the premium (wet rent) to the pub owning company and without the benefits, known as special commercial or financial advantage (SCORFA), provided by the pub owning company. (See paragraphs 67-76 for further calculation).

16. [19] For more details see consultation document

42. While this option does not directly prohibit the tie, it could impact on the number of tied pubs compared to free of tie or managed pubs depending on the response of pub owning companies. For example, a pub owning company could decide to reduce its number of tied pubs because of a reduction in expected profits. However, this is likely to be limited because of the benefits both brewing and non-brewing pub owning companies get from the tie in terms of economies of scale. Indeed those representing both licensee groups and pub owning companies felt that pub owning companies would rather increase the benefit of the tie to the licensee than abandon it.

43. No pubs should become unviable as a result of this policy as it just moves profit from one party to another. If a pub was viable prior to the policy the licensee and pub owning company could reach a negotiation that maintained the pub's viability. It is possible that the policy could have an impact on the viability of pub owning companies, as opposed to individual pubs.

Costs

44. The costs of the pubs adjudicator are largely based on the costs of the Groceries Code Adjudicator (GCA).[20] This is because the two bodies will have similar functions including providing guidance, adjudication and carrying out investigations. At this point the pubs adjudicator is expected to have a similar number of staff, although this will become clearer during the consultation. The costs to business are likely to be similar in nature i.e. training, legal costs and dealing with enquiries. The costs are likely to be less in the pubs industry because it is smaller than groceries (see paragraph 61) and codes, albeit voluntary ones, are already a major feature in the industry.

Set up costs

45. The one-off set up costs for the body are likely to be in the region of £140k-£155k (more detail below). However, to take into account that costs are often underestimated, we include an optimism bias of 50%. This leads to a best estimated cost of approximately £220k. Below is the breakdown of the costs based on figures from the Groceries Code Adjudicator impact assessment.

46. *Staff and recruitment*: This will cover the costs of recruitment of the adjudicator, and pay of staff as the body is being set up, before it is receiving cases. We assume that staff would be in place for up to 3 months and the staff mix employed would cost £410k per annum. In total, it is estimated that staff and recruitment set up costs would be in the region of £85k.

47. *Legal*: This will cover the costs for drawing up contracts for sharing premises, back office functions and guidance on procedures and policies including recovering costs on investigations. It is estimated that this would cost between £30k and £40k.

48. *IT*: The IT costs are based on OFT costs as was done for the GCA. Costs for a web presence and set up costs are also included. This is estimated to be approximately £12k

49. *Accommodation:* Accommodation at the OFT for an initial set up period of 3 months is likely to cost in the region of £15k based on the same space requirements as the GCA.

50. *Other:* Other costs incurred could include photocopying and travel. These are likely to be low initially, although set up costs could be up to £1k.

---

17. [20] Groceries Code Adjudicator available here - http://www.parliament.uk/documents/impact-assessments/IA12-019.pdf

	Estimated costs	Estimated costs with 50% optimism bias
	£000's	£000's
Staff and Recruitment	85	128
Legal	35	53
IT	12	18
Accommodation	15	23
Other	1	1
Total	150	220

Table 3: Set up costs of the pubs adjudicator

Operating costs

51. *Investigations*: The cost per investigation would depend on the complaint and the complexity of investigating it. One potential comparison is with the cost of OFT market studies that were estimated to cost £380k each. However, discussions with OFT suggested that the likely cost per investigation for the groceries code adjudicator would be lower than this due to the likely narrower scope of investigations. This is also likely to be the case for a pubs adjudicator. Based on the staff requirements for an investigation and other costs such as consultancy and research, costs could range from £50k to £150k per investigation.

52. The other key variable will be the number of investigations that the pubs adjudicator runs per year. As with the groceries code adjudicator, we estimate the number of investigations to be between 2 and 4 a year.

53. From the figures above, we estimate that investigations will cost between £100k and £600k a year with a central estimate of £300k.

54. *Appeals*: In line with the assumptions for the groceries code adjudicator, we assume appeals will cost £200,000 per appeal. Half of this figure represents cost to Government associated with the appeal court, and the other half legal costs to the parties involved. The number of appeals is unlikely to be above 2 in any year and so we estimate the number to vary between 0 and 2 a year. We estimate that appeals will cost between zero and £400k a year with a central estimate of £200k.

55. *Staff*: Based on the staff composition, total staff costs are estimated to be approximately £400k. However, this includes staff costs that form part of arbitration and investigations whose costs are accounted for elsewhere. The remaining staff requirements, base on those for the GCA, are estimate as between £200k and £400k, with a best estimate of £300k.

56. *IT*: The IT costs are based on OFT costs including for the operation of a web presence. This is estimated to be approximately £11k

57. *Accommodation:* This is based on costs at the OFT and is estimated to cost £62k based on the same space requirements as the GCA.

58. *Other:* Other costs incurred could include photocopying and travel.

	Low estimate	High estimate	Best estimate
	£000's	£000's	£000's

Investigations	100	600	300
Appeals	0	400	200
Staff	200	400	300
IT	11	11	11
Accommodation	62	62	62
Other	30	30	30
Rounded Total	400	1500	900

Table 4: Operating costs of the pubs adjudicator

59. The adjudicator will be required to report on its activity and costs and a post implementation review will seek to establish the actual costs incurred.

60. The pubs adjudicator would be funded by a levy on the pub owning companies covered by the statutory code. As such all the costs would be ultimately borne by business except half the cost of appeals. This gives a best estimate of the cost to business of £800k with a low of £400k and a high of £1.3m.

Costs to pub owning companies

61. There will be a cost to pub owning companies of complying with the code beyond the transfer of profits to licensees. We have based our estimates on those for retailers in the Groceries Code Adjudicator Impact Assessment. The estimated one-off costs were £1m per retailer this comprises staff training and legal costs, redrafting terms and conditions and dealing with code related queries. As it is a smaller industry, the costs in the pubs industry are likely to be lower. Pub owing companies have hundreds of employers rather than hundreds of thousands. A comparison of employment figures is skewed by the inclusion of supermarket workers who do not deal with suppliers so turnover is a better comparison. When the GCA costs were calculated the groceries sector turnover was £146 billion compared to the pubs industry turnover of around £21 billion. Reducing these costs in proportion gives a one-off cost of £1m spread across seven firms, which is our best estimate. The £7m figure is our high estimate and £0.5m (best - 50%) is our low figure.

62. Ongoing costs were estimated to be £168k per retailer. This includes the ongoing training, code compliance management time, internal audit compliance, external legal advice, answering queries and responding to disputes from named complainants. These costs may be overestimated as the pubs industry is smaller than groceries. However, reducing in proportion to turnover gives ongoing costs of just £44k per firm which seems too low, not least because would need to include a compliance officer. As such, our best estimate is £168k per company, with £44k as the low estimate and £252k (best plus 50%) as our high estimate. We will explore this further in the consultation.

63. Our current assumption is that seven companies will be covered by the code and will be explored further during the consultation. This gives a one-off cost of £1m (£7m high, £0.5m low) and an ongoing cost of £1.2m (£1.8m high, £0.3m low) per year.

Benefits

64. The principal benefit will be a transfer from pub owning companies to their tied licensees. Although it is the main benefit and the main intent of the policy, this does not appear in the NPV calculation. This is because the benefit to tied licensees is offset by the cost to the pub owning companies.

The tied licensee no worse off than the free-of-tie licensee

65. Intuitively this should mean that the costs of the tie in terms of wet rent should be offset by other benefits (SCORFA) with any difference compensated by changes in dry rent.

66. As stated above, the principle that 'the tied licensee should be no worse off than the free of tie licensee' will mean the projected post rent balance of a tied licensee must be equal or greater than that licensee would receive under a free of tie arrangement.[21] The key differences compared to free of tie are the charging of wet rent, the provision of SCORFA and resulting differences in dry rent. The following paragraphs will work through how these differences affect profit.

67. Pub profit is equal to revenue minus cost. As the market is already competitive it is assumed that the price paid by the consumer will not change and so revenues will be the same under both tied and free of tie arrangements. Costs will differ with tied licensees paying wet ret but not for SCORFA provided by the pub owning company. Conversely free of tie pubs will not pay wet rent but the licensee will have to pay for the benefits otherwise provided by the pub owners.[22] The revenue minus these costs and all common costs gives the operating profit. The final difference will be the dry rent that under RICS guidance is calculated as a proportion of the operating profit or divisible balance. The pub owner's share of this divisible balance in most cases will lie within the range of 35 to 65 per cent of the division balance.[23] This analysis will assume the mid point (50%); this is also common practice in the industry. This will mean total profit for the licensee equals half the operating profit. These differences are summarised in the table below.

	Tied	Free of Tie
Revenue	Unaffected	Unaffected
Pay wet rent	Yes	No
Pay for SCORFA	No	Yes
Operating profit	Revenue minus common costs minus wet rent	Revenue minus common costs minus costs to pay for SCORFA
Dry rent	50% of operating profits	50% of operating profits
Profit	50% of operating profits	50% of operating profits

Table 5: Differences affecting profit between tied and untied pub

68. This option only has an impact where tied pubs would be better off under free of tie arrangements. In these cases the change in profit will be the difference between tied pub profits and free of tie profits. In equation form:

Change in profit = Tied pub profit - Free of tie profit

Substituting from the table above gives:

[21] The statutory code states "At a minimum, this should be interpreted as meaning that the projected Post Rent Balance of a Free of Tied Licensee must be equal to or greater than the projected Post Rent Balance that that Licensee would receive, under the same assumptions and all other conditions of the lease or tenancy being equal, under a Free of Tie Agreement. Any genuine and quantifiable Special Countervailing or Financial Advantage (SCORFA) would be reflected by increased costs in the assessment of costs in the Free of Tie model, which would in turn impact upon the divisible balance, rent and Post Rent Balance in that model."

18. [22] We assume that these benefits must be worthwhile or else the pub owning company would not provide them.

19. [23] RICS Practice Standards, UK - The capital and rental valuation of public houses, bars, restaurants and nightclubs in England and Wales

= 50% of tied operating profits - 50% of free of tie operating profits

= 50% of (revenue - common costs - wet rent) - 50% of (revenue - common costs - SCORFA)

Removing the common revenue and costs gives:

= 50% of wet rent - 50% of SCORFA

= 50% of (wet rent - SCORFA)

69. So the transfer is equal to half the difference between wet rent, the premium tied licensees pay for beer, and SCORFA, the benefits the pub owning companies provide. Intuitively this is because paying a premium for beer is justified by the benefit of SCORFA, so if the wet rent is higher than the SCORFA licensees are paying too much. The halving is because any excess wet rent reduces operating profit and thus dry rent too; the licensee already gets half the excess back through reduced dry rent, under this option they get the other half back too.

70. The wet rent and SCORFA will vary between pub owning companies and between pubs within companies. Even with totally transparent information they cannot be perfectly estimated – the standard practice in the industry is to estimate it with respect to the turnover that a reasonably efficient operator could achieve Benefits provided as part of SCORFA include things like marketing and business development that are difficult to value. This is why judgements on whether the tied licensee is at least as well off as a free of tie licensee will need to be made on a case by case basis, by the adjudicator.

Wet rent

71. Looking across the industry it is possible to average out some of the difficulty with assessing a reasonable efficient operator; one cannot assume current turnover is the fair maintainable turnover for any individual pub but it will be across a large number of pubs. While there is not a great deal of transparency in the pubs industry, some estimates of the wet rent have been made.

72. The OFT compared the average sale price of a leading UK drinks wholesaler with the prices charges by the large pub companies. They found the average price differential was 30% which equates to an average difference of around £15.5k per year per pub.[24] This is our best estimate of the average wet rent. The OFT originally used a different method of estimation and arrived at £19-21k. This shows the difficulty and uncertainty involved in estimating the wet rent. We will take the top end of this original estimate, £21k, as our high estimate and take the same difference from our best estimate as our low estimate, £10k.

SCORFA

73. The benefits provided by the pub owning companies are harder to estimate then wet rents. There is even less information on SCORFA partially because it is more commercially sensitive and partially because the values of many of the benefits, such as marketing, are less certain.

74. According to the RICS guidance the dry rent should be a function of the operating profits (see paragraph 67), as such the relevant estimates of SCORFA will exclude reductions in

---

20. [24] CAMRA super-complaint - OFT final decision, October 2010, paragraph 5.147

dry rent. These reductions in rent are a result of increased costs and thus reduced operating profits.

75. Previous estimates of SCORFA provided by some of the smaller brewing pub owning companies suggest a valuation of around £15k per pub.[25] In their submissions to the OFT, pub companies estimated the cost of providing benefits to their licensees as on average £6-8k per pub per year.[26] The OFT later updated its analysis focussing on the provision of operational support which they estimated cost on average £1.5k per pub per year.[27] These three estimates form the basis of our high, best and low estimates of SCORFA.

Transfer

76. The average transfer per pub, half the difference between the wet rent and SCORFA, is shown in the table below. The high (low) estimate of transfer per pub uses the high (low) estimate of wet rent and the low (high) estimate of SCORFA; this ensures the maximum range for the transfer per pub. The low estimate is zero as in this case the statutory code has no effect and so there is no transfer; this represents the case where tied licensees are already better off than free of tie licensees.

	Wet rent per pub (£000s)	SCORFA per pub (£000s)	Average transfer per pub (£000s)	Total transfer (£m)
High	21	1.5	9.75	234
Best	15.5	7	4.25	102
Low	10	15	0	0

Table 6: Summary of transfer from pub owning companies to their licensees

The total transfer is the transfer per pub multiplied by the number of tied pubs covered by the adjudicator - 24,000.

Issues with this estimate

77. These figures may underestimate the impact as pub owning companies below the threshold are also likely to be affected. As large pub owning companies improve the offer to their licensees small companies may have to as well in order to continue attracting high quality licensees.

78. The distribution of this impact is likely to be uneven as some pub owning companies will offer licensees a better deal than others. Those companies that already offer sufficient benefits to justify the wet rent will be unaffected. Even within pub owning companies some pubs are likely to be getting a better deal than others. This uneven distribution of impacts means that using an average to derive the overall transfer, as we have done, will result in an underestimate if some pubs are unaffected. Take the simplified example below that could reflect the best estimate. The median pub, represented by the top of the triangle might have a transfer of about £4k, as in our best estimate. This would also represent the mean if the distribution is symmetrical. However, where the SCORFA exceeds the wet rent, the transfer is negative (the white area of the triangle). In practice

21. [25] Independent Family Brewers of Britain Submission to European Commission Directorate-General for Competition, September 2009

22. [26] CAMRA super-complaint - OFT final decision, October 2010, paragraph 5.152

23. [27] CAMRA super-complaint - OFT final decision, October 2010, paragraph 5.154

the transfer in those cases would be zero rather than negative and so the average would be higher. We will use the consultation to better understand the distribution of the impact and how this affects the overall level of transfer.

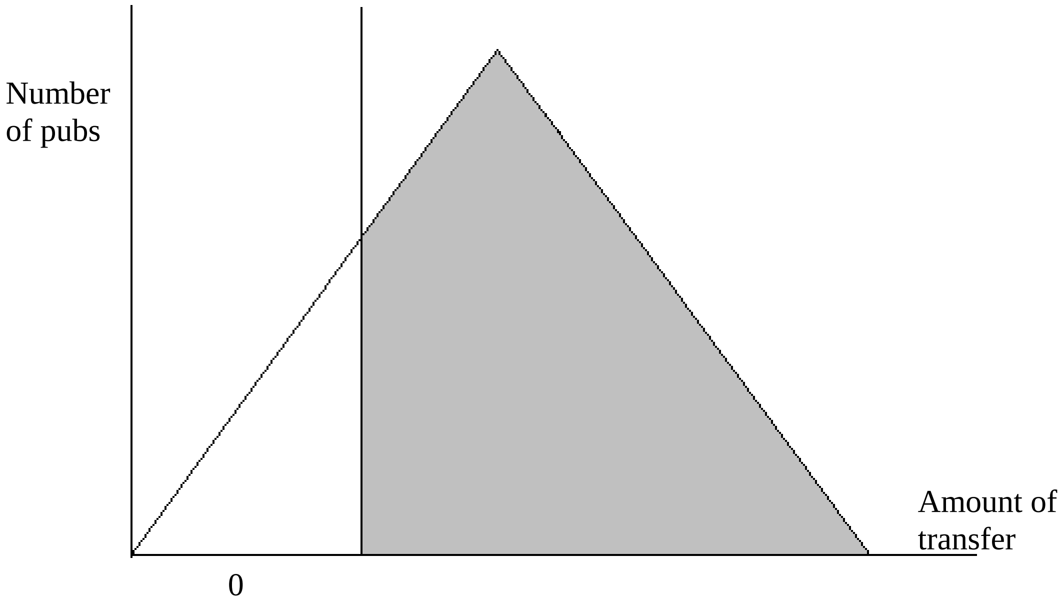

Figure 1: Impact of uneven distribution of transfer on the average

Other possible approaches

79. There are other approaches to estimate the size of the transfer and we will explore these further during the consultation. One estimate submitted to the European Commission by the Independent Family Brewers of Britain (IFBB) [28], a group of the smaller brewing pub owning companies, was based on free of tie tenants buying their pub and paying interest on the loan but no rent. This estimate found that the average tied tenant was £1.3k worse off, but was sensitive to changes in factors such as interest rates and beer volumes - their forecast was for tied pubs to be better off than free of tie pubs by now.

80. Our estimate also depends on the figures for wet rent and SCORFA used and we will use the consultation to test our current figures. We already have some alternative estimates. An estimate by a member of the Independent Pubs Confederation, a licensee umbrella group, assessed the transfer for the average pub of one pub owning company would be £14-22k.[29] Using our methodology and IFBB figures mentioned in the previous paragraph[30], gives an estimate of the transfer £8-13k per pub depending on the type of pub. These estimates are far higher than ours and the main reason is higher estimates of the wet rent. We will explore this difference further during the consultation.

81. One method to check the figures are in the right area is to compare the incomes of those in tied pubs and free of tie pubs. A survey commissioned by the Institute for Public Policy Research asked tied and free of tie licensees what their personal income was.[31] The results suggest that tied licenses are about £6k worse off than free of tied licensees. This is also not a very reliable estimate because there is a small sample size and the answers

24. [28] Independent Family Brewers of Britain Submission to European Commission Directorate-General for Competition, September 2009

25. [29] The lower estimate used some of the publically available figures from the pub company while the higher estimate did not.

26. [30] Independent Family Brewers of Britain Submission to European Commission Directorate-General for Competition, September 2009

27. [31] Tied Down - The Beer Tie and its Impact on Britain's Pubs, IPPR, 2011

were given in bands. Also some of the gap is likely to be accounted for by differences in the pubs, for example turnover at tied pubs is around 10% lower. However, it does suggest that our estimate is in the right area.

Other benefits: improved long term health of the industry

82. Increasing the share of profits that goes to licensees will increase their incentive to invest and make innovations. There will obviously be a corresponding reduction in the incentive for pub owning companies to invest. While we might usually expect these two effects to offset, there are reasons they probably will not here.

83. Firstly, most investments and innovations need a large input from the licensee; they are the ones on the front line. This would not be a problem if the pub owning company could give them an offsetting reward for increasing profits. However, the level of distrust in the industry is such that this will often not be possible. A second reason is that some pub owning companies may be taking a short term view due to pressures servicing debt.

84. This benefit is not likely to be large, given that the OFT did not find evidence that a lack of competition was reducing innovation and did not consider issues regarding the conduct of negotiations between pub companies and lessees can generally be expected to result in consumer detriment.

Risks

85. There is a risk that the transfer from pub owning companies to licensees results in a major disruption in the industry. This could be a result of one or more pub owning companies deciding to manage, sell or close more pubs or getting into financial difficulty. This kind of unexpected disruption would be more likely if the transfer is larger than our estimates.

86. The pub owning companies may find a loop hole in the statutory code that allows them to continue acting as currently. To mitigate this risk the rules will be written in terms that are difficult to game and the potential for gaming of the rules will be explored in the consultation. We will also propose that the code, which is likely to be set out in secondary legislation, will be amendable in certain circumstances which will allow it to reflect new developments in the industry and close any loop holes that are found.

Option 3: Mandatory free of tie option with open market rent review

87. All pub owning companies with over 500 pubs would have to offer a free of tie option with open market rent review. This would apply at the next rent review point for current leases and for all new leases. Each licensee would be able to choose to be either tied or free of tie. This is in addition to the statutory code and adjudicator from option 2.

88. The rent in the free of tie offer would have to be based on RICS guidance. This would ensure that there was a genuine free of tie option rather than one involving an unrealistically high free of tie rent.

How many would choose free of tie?

89. Even if given a choice, many tied publicans would choose to remain tied. The latest independent annual survey – conducted by CGA strategy – showed 7 out of 10 licensees would sign up again with their pub owning company. This suggests that around 30% of tenants under current arrangements would choose to go free of tie. However, with the improved arrangements for licensees in the statutory code the number going free of tie is likely to be less. As such, our best estimate is that 15% of pubs if offered the choice would go free of tie.

90. This is, nevertheless, subject to a high level of uncertainty due to the fact that it would be fundamentally changing the predominant business model that currently prevails in the industry. For example, it may be that licensees are content with their pub owning company because they see it as offering a fair deal under the current paradigm of the tie, but would still go free of tie if given the option. One pub owning company indicated that they thought very few licensees would go free of tie, as their tied arrangements are so beneficial; conversely, a licensee considered that almost 100% of licensees would choose a free of tie option if given the choice. Reflecting this uncertainty, our high estimate is 50% and our low estimate is 5% (on the basis that at least some would go free of tie).

Which pubs would choose free of tie?

91. As under option two, licensees would be protected by the principle of not being worse off than a free of tie operator. However, higher volume pubs and multiple operators (a single operator running multiple pubs) would benefit more from being free of tie. For these pubs the scale and experience of the pub owning companies would be less valuable. These pubs would be able to negotiate larger discounts than smaller pubs (although not as large as the pub owning companies. Some of the benefits included in the SCORFA will be less valuable to higher volume pubs and multiple operators. For example, costs such as marketing can already be spread over a higher turnover and business support may be less valuable to an experienced multiple operator. This suggests that higher volume pubs and multiple operators are more likely to go free of tie.

92. There will also be cases where the relationship between the pub owning company and licensee has become very bad and the licensee would choose to go free of tie.

Want would pub owning companies do?

93. Pub owning companies could maintain some of the benefits of the tie by converting more of their estate to managed pubs. This would involve a cost to business - shown by the fact they are not currently managed and so the current arrangements are preferable for

business. However, during our engagement with stakeholders we were told this would not be a likely approach taken by pub owning companies. A more likely approach is to emphasize the benefits of the tie.

94. Another alternative is for pub owning companies to sell more pubs. This response may be limited because pub owning companies are already selling large numbers of pubs and will have very limited if any capacity to sell more. Conversely, one brewing pub company have said that they only own pubs in order to sell beer and so under this option one or more pub owning company may decide to sell off all their pubs. Regardless, the net impact is likely to be limited as it would merely be a change of ownership, provided the pubs remained viable and there was the finance available to run them as a pub. The possibility of pubs becoming unviable is considered below in paragraph 102.

Impact

95. As in option two, the main impact will be a transfer from pub owning companies to licensees. This will be the same as in option 2 with a best estimate of £102m and a maximum of £234m and a minimum of zero. As in option 2, these are transfer costs and so do not appear in the net present value figures of costs to business.

96. The large pub owning companies benefit from greater economies of scale than smaller independent wholesalers. In the short term these economies of scale would be reduced if licensees went free of tie. The impact would be higher costs. The size of the loss of economies of scale will depend on the numbers of pubs that go free of tie.

97. As it is higher volume pubs and multiple operators that are more likely to go free of tie (see paragraph 91), it is lower volume pubs that are likely to face higher costs.

98. In the longer term independent wholesalers may grow to replace the large pub owning companies. Alternatively, large international brewers may be able to replicate the distribution economies of scale of pub owning companies and expand their UK sales.

99. This option is likely to be significantly more disruptive than option 2 and so has greater potential for unforeseen consequences. The impacts could include higher costs for consumers, the exit of one of the major pub owning companies, the closure of one or more breweries and/or dominance of the market by large international brewers.

Costs

100. This option would still involve an adjudicator in order to address the problem of pub owning companies taking advantage of their greater information and resources. The cost of the adjudicator would be the same. Costs may be lower due to the reduction in the number of tied pubs, which attract more complaints.. Assuming the number of investigations reduces in line with the number of tied pubs, which probably overestimates the cost saving, reduces investigation costs in the best, low and high estimates by 45k (15% of 300), 30k (30% of 100) and 30k (5% of 600) respectively. This results in total costs in the best, low and high estimates of roughly £850k, £350k and £1450k respectively. The cost to business (removing half the appeal costs as in paragraph 60) gives best, low and high estimates of roughly £750k, £350k and £1250k respectively.

101. The cost to pub owning companies of complying with the code beyond the transfer of profits to licensees will be the same as in option 2 - a one-off cost of £1m and an ongoing cost of £1.2m per year.

102. In the short term there will be higher costs as a result of lost economies of scale (see paragraph 96). These are likely to fall disproportionately on lower volume pubs (see paragraph 97). This is likely to be a particular concern as protecting the most vulnerable licensees is one of the reasons for this policy. This may also lead to some pubs becoming unviable and closing.

103. In the longer term this cost will probably reduce as independent wholesalers or large international brewers are likely to replicate the economies of scale. If it were the large international brewers choice is likely to suffer as international brewers are unlikely to supply alternative brewers' beers.

104. There is a chance that the loss of scale for some brewing pub owning companies leads them to close breweries in the UK. This would result in job and export losses.

105. Removing the surety of the tie would reduce pub owning companies' incentive to invest in even the pubs that remain tied. This would particularly affect pub owning companies that are currently acting responsibly and investing in their pubs.

Benefit

106. As in option two, the main benefit will be a transfer from pub owning companies to licensees. This will be the same as in option 2 with a best estimate of £102m and a maximum of £234m and a minimum of zero. As in option 2, these are transfer costs and so do not appear in the net present value figures of costs to business.

107. As discussed in paragraph 91, higher volume pubs and multiple operators may benefit from being free of tie beyond what would be guaranteed by the statutory code.

Risks

108. This option has similar risks to option 2 but with a significantly greater level of uncertainty as a result of the greater likely level of disruption.

This publication is also available on our website at www.gov.uk/bis

Any enquiries regarding this publication should be sent to:

Department for Business, Innovation and Skills
1 Victoria Street
London SW1H 0ET
Tel: 020 7215 5000

If you require this publication in an alternative format, email enquiries@bis.gsi.gov.uk, or call 020 7215 5000.

BIS/13/738