



**Pub Companies & Tenants: A government consultation**  
**Response by HEINEKEN UK and Star Pubs & Bars**

**14<sup>th</sup> June 2013**

## **Executive Summary**

**The Government's proposals for pub company reform are about managing the continued decline of the great British Pub, not about growth.**

- The proposals represent a worrying lack of ambition for British pubs from the Government. They are simply an attempt to manage decline in the industry.
- They stand in stark contrast to recent Treasury policy to support investment in the sector by ending the Beer Duty Escalator and cutting the price of a pint.
- They are at odds with HEINEKEN's vision to work in partnership with our tenants to improve their offering to customers and reverse the trend of more and more people spending less time and money in pubs.

## **There will be a number of unintended consequences**

- There are three very significant unintended consequences if the proposals go ahead:
  1. It will restrict the lifeblood for pubs – investment– leading to closures for some pubs in the short term and continued decline in the medium and long term for others.
  2. Tenants who are already operating at the higher end of the income scale will benefit most while those on low incomes, whom the Government wishes to help, will receive less support.
  3. More pub companies will be forced to adopt a purely commercial property relationship which will remove the partnership approach and be detrimental to many pubs.

## **The proposals fail to address the real challenges facing the sector**

- The proposals fail to recognise or tackle the various challenges which must be addressed if we are to reverse the trend of declining pub visits and sales, including: fiscal pressures (e.g. high duty, business rates and VAT); reduced consumption away from home in favour of at home drinking; increased competition for leisure and household expenditure; legislative changes (e.g. smoking ban); social changes (e.g. rise in mixed-sex drinking and dining occasions); and historic lack of investment in research to understand and address changing customer demands.

- The proposals aim artificially to allocate tenants a slightly larger slice of a shrinking cake. Our vision for Star Pubs & Bars is not about managing decline. It is about increasing the size of the cake by focusing on the things that will attract more customers back to the pub. This will ensure that tenants enjoy higher and more sustainable incomes.

### **Our approach**

- HEINEKEN is the UK's leading cider and beer producer. We directly employ around 2,400 people in our UK business and we operate offices in Edinburgh, Livingston and London; breweries in Edinburgh, Tadcaster and Manchester; and cider production in Hereford and Ledbury.
- HEINEKEN has invested £600 million in purchasing and improving our pub estate since 2010. We continue to invest heavily to improve our pubs with £13m investment in improvements in 2013 – over and above the money we spend on general maintenance.
- We own 1,300 pubs, the majority of which operate on traditional brewery tenancy agreements. We operate a tie on beer and cider but not on wines and spirits.
- We offer low risk low cost opportunities to enter the pub market starting at as little as £10k investment; we have introduced new business start up agreements; and we are improving our support to our tenants through support for Sky TV packages, support to improve their food and coffee offering, mystery shopper customer support, better training, product and marketing expertise, and a range of other SCORFA benefits.
- We believe that we will succeed where we invest in the right pubs, in the right place, with the right tenants. We believe that investment, innovation and insight, coupled with motivated, skilled and entrepreneurial tenants is the key to success.

### **The case for intervention has not been made**

- We recognise that there have been concerns in the past about how the market has operated. As relatively new entrants, HEINEKEN and Star Pubs & Bars are on a journey to make the sector more sustainable. While we recognise that there is more to do to, we believe that the Government has failed to understand the significant improvements that have already been made without the need for legislation.

- The evidence presented by the Government for action is weak and misleading and simply does not justify the extent of the proposed intervention in our business model, particularly when the Government recognises that “many pub companies treat their tenants well”.
- The evidence presented by the Government relating to ‘complaints’ has been shown to be wrong as it relates to enquiries on a wide range of issues.
- At the heart of the debate is the issue of whether or not pub companies are charging too much for beer (wet rent) and also charging above market rent rates (dry rent). We do not believe that the Government has provided any evidence that this is the case.
- We recognise that there is a high profile campaign for pub company reform, however we believe that this is driven by a vocal minority of tenants and former tenants and does not reflect the positive relationship that we have with the majority of our tenants.

#### **Case for the statutory code**

- We believe that self regulation is working and offers a fast, low cost and effective way of resolving disputes between us and our tenants.
- Self regulation has been successful and we are happy to discuss further improvements to the current IFC 6. We therefore do not believe there is a requirement for a Statutory Code.
- The Code should not apply to free of tie agreements.

#### **500 pub threshold**

- Setting a 500 pub threshold would be a significant restriction of competition and we do not support it. As brewer and cider maker we cannot support a system which regulates our pubs in a different way to pubs owned by our competitors.
- The Government offers no evidence that our tenants are worse off than those of companies with fewer than 500 pubs.
- By setting a threshold the Government would establish a two tier system where some tenants have less protection than others. We believe that companies of all sizes which operate fairly should have nothing to fear from being included.
- We have heard concerns from some groups that while in principle they do not oppose the Code covering all companies, they are concerned at the cost

burden on smaller companies. We believe this could be resolved by a funding arrangement where large companies pay the bulk of the cost.

- If a threshold is set, it must apply to the number of tied leased and tenanted pubs owned by a company. It should not cover non tied, managed or franchised pubs.

### **Mandatory 'free of tie' option**

- We fundamentally oppose this proposal as selling our beers and ciders is the reason that we have invested £600 million since 2010 purchasing and then improving the pubs we own.
- It would reduce our ability and the incentive to invest in our pub estate. In fact there would be no incentive to support a pub that was selling beer produced by one of our competitors.
- Adding a third party in to the relationship (e.g. a wholesaler) would also reduce investment as more of the profit is taken by a party without a direct interest in the pub.
- It would reduce the relationship with our tenants to a pure commercial property transaction.
- As it became uneconomic to continue to offer SCORFA benefits this would most affect tenants at the lower end of the market who get the greatest benefit from these services.

### **Principle of fair and lawful dealing**

- We support this principle which we believe already operates through IFC 6.

### **Principle of 'no worse off'**

- We have significant concerns about this proposal. What may appear at first to be an attractive, simple principle to help tenants at the lower end of the market is actually significantly more complicated.
- Many people confuse 'free of tie' with a 'freehold' yet with the exception of being free to purchase beer and cider from any source, the business models are completely different.
- The 'free of tie' model described by the Government only applies to a small number of pubs. Groups such as Wellington operate on a pure property

lease basis which means higher fixed costs (dry rent), no business support services and less flexibility on payment terms.

- We do not believe that it is possible or sensible to compare our model – with its lower fixed costs, lower risk, business support services, investment profile, access to affordable capital, and shared interest in growing beer and cider sales – to a ‘free of tie’ model which is purely a property transaction relationship. It is like comparing apples with oranges.
- We note that the Government has not provided any evidence to suggest that tenants in this small ‘free of tie’ sector are performing better than our tenants. We believe that our tenants and lessees are already in a stronger position than the ‘free of tie’ model suggested by the Government.
- It is difficult to provide an objective valuation of SCORFA benefits in a comparison formula as by definition the value of these is subjective and varies by tenant.

#### **Open market rent review**

- We support the Government’s proposals for Open Market Rent Reviews which we think reflect current good practice, make good business sense, and are in keeping with the spirit of the relationship we have with our tenants.

#### **Gaming machine tie**

- We oppose the proposal to abolish the gaming machine tie.
- We believe that there has been a significant misunderstanding of the role of the gaming machine tie and of the major changes that we have already made to ensure it operates to the benefit of our tenants, Star Pubs & Bars and to the Government through better regulation of a sector which is vulnerable to criminal activity.
- It is vitally important that if the Government removes the tie, that we retain the ability to enter in to binding contracts with our tenants to provide the latest and best managed machines to help grow their income and ours. Poorly managed machines will simply lead to reduced income for tenants.

#### **Guest beer option**

- This proposal fundamentally undermines the principle of the tie by allowing tenants to choose alternative brands which would mean forcing HEINEKEN

and Star Pubs & Bars to allow the sale of major competitor brands in our own pubs.

- Of greatest concern is the fact that the Guest Beer Option could be used for any product. The logic of this is that tenants would not choose to exercise this option to introduce relatively low sales lines. There would be a much greater incentive to use it to circumvent the tie and replace the highest selling tied product with a competitor. This would reduce the tenant's 'wet rent'.
- It also undermines the major progress made by pub companies in providing a low cost route to market for many small and microbreweries through our estate. There is already significant competition and choice for consumers with greater availability of cask ales in tied estates than managed and freehold.

#### **Flow monitoring equipment**

- We oppose this proposal. There is no evidence presented in the consultation as to why flow monitoring equipment should not be used as part of the process of determining if a tenant is not complying with purchasing obligations. IFC 6 already requires additional evidence before a tenant could be found to be in breach.

#### **Role of the adjudicator**

- If introduced, the Adjudicator should:
  - apply to all tied leased and tenanted pub companies
  - be funded predominantly by the largest businesses, with a higher contribution made by companies where the Adjudicator has found against them in referred cases
  - operate alongside a continued PIRRS and PICAS service that would operate as a low cost mechanism which could also consider a wide range including smaller issues that would clog up the Adjudicator
  - become an appeal mechanism for tenants unhappy with the outcome of PIRRS and PICAS
  - be freed up to investigate the most serious allegations of abuse.

### **Other unintended consequences**

- There is a significant risk that the proposals will lead to a large number of pubs being disposed of by pub companies. With little available capital and the banks tightening their lending criteria, there is a risk that there would be insufficient willing and able buyers to match this increase in supply. A large number of disposals would therefore impact negatively on the market by reducing the value of existing estates and would also reduce the value of individual freehold properties.
- It is already difficult for pub companies and freeholders to sell pubs due to the lack of buyers in the market. In recent years there has been an increase in purchases from supermarkets as they seek to expand their convenience store networks. Large numbers of disposals is likely to mean the loss of more pubs to alternative uses.
- Pub companies and their national distribution networks offer a low cost route to market for many cask ale producers and small and micro brewers. Market data from CGA Strategy shows that the leased and tenanted sector stocks more cask ale brands than freehold and managed pubs. Mandatory 'free of tie' options and the proposed Guest Beer would reduce the ability of pub companies to continue to support this sector.

### **Alternative approaches**

- In addition to working with the industry to improve self regulation, we believe that there are a number of additional measures the Government could take as part of a plan for growth:
  - Put pressure on major lenders to increase availability of lending to tenants for investment
  - Encourage greater investment in the pub estate through improving capital allowances
  - Review business rates and consider a business rates holiday for the first year of a new pub tenancy
  - Support a reduction in VAT for food served in pubs to match the rate for supermarkets
  - Support skills and training in the sector to identify the next generation of innovative and entrepreneurial landlords.



## **Introduction**

**The Government's proposals for pub company reform are about managing the continued decline of the great British Pub, not about growth.**

The proposals represents a worrying lack of ambition for British pubs from the Government. They are simply an attempt to manage decline in the industry.

They lack the vision necessary to turn around the fortunes of the pub sector and stands in stark contrast to recent Treasury policy to support investment in the sector by ending the Beer Duty Escalator and cutting the price of a pint.

To tackle the challenges facing the pub sector, we need to work together on a plan for growth that gets more people back in to the pub, spending more money. Without that plan, no amount of rules, regulations and formulas will convince ordinary people to open their wallets and spend more of their hard earned cash in their local. Rather than proposals which simply seek to divide up a shrinking cake, we need a plan to grow the cake so everyone benefits.

## **There will be a number of unintended consequences**

We share the Government's desire to create a more sustainable pub sector and to improve incomes for those pub landlords who are struggling most, particularly in the current economic climate. However, we believe that there are three very significant unintended consequences of the Government's proposals.

The first and the most significant is that it will result in less investment for pubs. This will lead to some pubs closing in the short term. For others, there may be a very short term increase in income, but by restricting the lifeblood of investment, the proposals will lead to inevitable medium to long term decline. If pubs do not invest and change to meet the needs of today's and tomorrow's customers, they will continue to decline.

The second significant unintended consequence is that the very tenants who the Government wishes to support – those with the lowest incomes – would be most likely to be disadvantaged by these proposals. Those tenants operating at the higher end of the income scale tend to rely less on the support services provided by pub companies (known as SCORFA benefits) and will suffer least from their withdrawal. Meanwhile those potential tenants with the least access to capital will struggle to access a pub on terms they can afford.

The third significant unintended consequence is that it will turn more pub companies into purely commercial property companies. The proposals will reduce the partnership approach and shared interest currently in our model and reduce it to a simple tenant / landlord relationship that would be no different to that for

shops, offices and other commercial property. We believe that would be a fundamental mistake for the great British pub.

We believe that there are a range of other unintended consequences from the proposals in the consultation:

- There is a significant risk that the proposals will lead to a large number of pubs being disposed of by pub companies. With little available capital and the banks tightening their lending criteria, there is a risk that there would be insufficient willing and able buyers to match this increase in supply. A large number of disposals would therefore impact negatively on the market by reducing the value of existing estates and would also reduce the value of individual freehold properties thereby having a negative impact on the Independent Free Trade sector.
- It is already difficult for pub companies and freeholders to sell pubs due to the lack of buyers in the market. In recent years there has been an increase in purchases from supermarkets as they seek to expand their convenience store networks. Large numbers of disposals is likely to mean the loss of more pubs to alternative uses.
- The main motivation for pure commercial property companies is to maximise rent, not to retain the use of the property as a pub. Pushing more companies to adopt this business model is likely to lead to more conversions to other uses such as restaurants or betting shops.
- Rather than disposals, some pubs may transfer to the managed sector. While this would retain pub use, it is important to remember that it would still mean the end for the small businesses running them who would be replaced by salaried staff.
- The proposals will create a two tier system of regulation that affords some pub company tenants less protection than others and would leave the smaller pub companies unaffected by the new Statutory Code to bear the cost of the old voluntary system without the support of the largest pub companies.
- Pub companies and their national distribution networks offer a low cost route to market for many cask ale producers and small and micro brewers. Market data from CGA Strategy shows that the leased and tenanted sector stocks more cask ale brands than freehold and managed pubs. Mandatory 'free of tie' options and the proposed Guest Beer would reduce the ability of pub companies to continue to support this sector.

## The proposals fail to address the real challenges facing the sector

British pubs need a positive vision for growth. To succeed in the twenty first century, pubs must improve their offering to customers if they are to reverse the trend of more and more people spending less time and money in pubs.

Pubs face a series of challenges:

- **Consumption** – alcohol consumption is down 16% since 2004 with a greater decline in the on trade than off trade.
- **Fiscal** – high duty, VAT, and business rates have increased the cost to operate and put pubs under pressure.
- **Competitive** – where before there was a pub on every high street, today there may be several coffee shops which reflects the growing competition for leisure expenditure; meanwhile there has been major growth in off trade sales at significantly lower prices than the pub including increasingly attractive ‘Dine At Home’ meal deals.
- **Legislative** – for example the ban on smoking in public places has impacted some pubs while others changes such as rises in the cost of licensing and new measures such as the Late Night Levy have been introduced.
- **Social** – customers have higher expectations of pubs; the way people socialise has changed with more mixed-sex drinking and dining occasions; the shift towards more drinking at home is about much more than prices with people investing more in their homes and with much improved digital home entertainment and social media replacing traditional networks.

The failure of the consultation to give sufficient weight to these issues and interrogate the challenges they pose to pubs is disappointing. Without addressing these challenges, any reform of pub companies will fail to reverse these trends.

## A plan for growth

We believe that it is possible to reverse the decline by investing in the right pubs, in the right places with the right tenants. The changes that we have made to Star Pubs & Bars are geared towards delivering real growth for our pubs.

To achieve this requires much greater focus on:

- **Investment, innovation and insight** – too many pubs have declined because they failed to change and invest to keep up with changing circumstances. Investment is the lifeblood of the pub. The old ways of doing things will not reverse the decline in pub goers. There needs to be more focus on innovation to reduce the cost of operating pubs and find new ways, products

and services to attract customers. The largest and most successful retailers in the country invest heavily in research to understand their customers' needs and tailor their offer to meet these. Too few pubs have done this. The days of opening the pub doors and expecting customers to pour through are gone and more time and effort must be spent on understanding what motivates customers to spend their hard earned money and precious leisure time in the pub.

- **Motivated and skilled entrepreneurs** – in the past too many pub landlords have seen running a pub as a lifestyle choice rather than a business opportunity. There has also historically been too little scrutiny of applicants and their suitability. In the current economic climate and with all the challenges that pubs face, running a successful pub requires people with drive, enthusiasm, strong business skills and entrepreneurial spirit. There is now a stronger process to ensure we get the right people into our pubs. The hurdles are set higher to ensure prospective tenants fully understand the business they are entering. Running a pub is not for everyone. We know that a good tenant can transform a pub by bringing the right attitude, vision, standards, atmosphere and customer service to the pub.

Already we have many examples of where this combination of our investment, innovation and insight alongside tenants who are motivated and skilled entrepreneurs has resulted in significant increases in income for tenants and Star Pubs & Bars. The Partnership that brings together the enthusiasm of our tenants with the expertise of the UK's largest cider and beer company works. We have provided more information on our model later in this submission and appended a series of case studies of how it works to increase tenant income.

case studies  
not published  
- already in  
public domain

### The Government's case for intervention

We recognise that there have been concerns in the past about how the market has operated. As relatively new entrants, HEINEKEN and Star Pubs & Bars are on a journey to make the sector more sustainable.

The reality is that the sector has already made significant changes and with the recent implementation of a new self regulatory code, we are doing more than ever to support tenants and lessees. We do not believe that the Government has paid sufficient regard to these improvements.

We also believe that the evidence cited by the Government is weak and misleading and does not justify the extent of Government intervention in our business model particularly when the Government recognises that "many pub companies treat their tenants well".

In making the case for intervention the parallel has been drawn with the grocery retail sector and the creation of a new Grocery Adjudicator. The two markets could not be more different. Major multiple retailers have enjoyed long term year on year growth, with new stores opening, increasing sales and growing market share. Meanwhile the pub sector has been in year on year decline with pubs closing, reducing sales and loss of market share to supermarkets and other leisure options.

It is also important to remember that there can be no guarantee of success for tenants. There will always be businesses that fail. That is true in every sector as many high street shops and small businesses can attest. Many business start ups fail and it cannot and is not the case that every pub company tenant that fails has been mistreated or abused. The best tenants are able to turn around the business of a pub on the same terms as those given to previous tenants who have failed.

We believe that the lack of evidence put forward by the Government reflects a situation where the campaign for reform is being driven by a vocal minority of tenants and former tenants backed by strong campaign groups, rather than by widespread tenant or consumer dissatisfaction with our business.

#### Concerns raised by Government

The Office of Fair Trading and the Government have been clear that the market does not operate to the detriment of consumers and there is no compelling consumer argument for intervention.

Therefore the case for intervention has been argued by the Government on the basis of:

- ‘a lack of necessary culture change within the industry, with no concerted, long-term effort made to inform tenants of their rights...’
- ‘....discussions on future progress deadlocked on numerous issues.’
- ‘The British Institute of Innkeepers has received over four hundred complaints on its hotline over the past three years’.
- Examples of unfair behaviour including ‘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’ which ‘is possibly due to imbalance in the relationship’ between pub companies and tenants.
- ‘Tied tenants are also more likely to face serious hardship’.
- ‘Increasing tenants’ share of profits is likely to have a small positive impact on investment and the long term health of the pubs industry’.

### Informing tenants

We have been working closely with the British Beer and Pub Association to deliver the improvements in self regulation agreed by the Department for Business Innovation & Skills in December 2011. We translated the revised Industry Framework Code into our own code, which was in turn independently verified by BIIBAS. We have also worked with the BBPA to introduce better training for would-be licensees and a low cost independent complaints system through the Pub Independent Conciliation and Arbitration Service (PICAS).

We believe that these changes are significant, but for them to be fully effective, tenants and lessees need to be aware of them. Therefore, over the last eighteen months Star Pubs & Bars has communicated these changes to our lessees in a number of ways. We have:

- Written to all of our tenants and lessees, outlining the Industry Framework Code 5 improvements in training and the creation of PICAS (the new low cost complaints system).
- Briefed our Business Development Managers (BDMs) to speak to our tenants and lessees about the changes,
- Included a module on the Industry Framework Code in the training programme for all our new tenants and lessees, and
- Outlined the new Industry Framework Code and information on our internal and PICAS complaints procedures on our website.

### Progress on further self regulation

Contrary to the assertion that further progress has not been made, in January 2013 the new IFC 6 was published. Since then we have integrated it in to our own company Code of Conduct and notified and consulted our tenants on the changes involved. We are now operating to the new Code across our estate and will attend the BIIBAS accreditation committee at the end of June 2013.

### Complaints

The evidence presented by the Government relating to 'complaints' made to the BII has been shown to be wrong as it relates to enquiries on a wide range of issues and not to complaints. We understand that the Government accepts these figures have been wrongly used. We are also concerned that the tenant survey launched by the

Government uses emotive and leading language and does not meet the criteria used by the Market Research Society.

It is normal in any commercial relationship for issues and disagreements to occur. These are not always evidence of unfair behaviour or abuse by a pub company. As with most commercial relationships, most 'complaints' are resolved through discussion and negotiation.

Star Pubs & Bars owns around 1,300 pubs and yet our annual complaints are low. In the past 18 months we received 19 complaints<sup>1</sup> which relate to allegations of a breach of our Code of Practice or due to a tenant being unhappy with our response to an issue. Most of these issues were relatively minor disputes and agreements were reached to resolve the matters raised. Five required more detailed investigation. We have had only two formal complaints to PICAS which are currently being heard. In 2011 we had three minor complaints upheld by BIIBAS for technical/clerical breaches of the Code with no material damage to the tenants.

#### Dry rent

It has been argued that 'dry' rents are too high, however we do not believe that the Government or others have provided evidence that this is the case.

The tied pub model offers a lower rent (dry rent), compared to the commercial property rents that are paid on 'free of tie' pubs. In return, higher prices are charged for beer and cider purchased under the tie (wet rent). The benefit of this is that the tenant has lower fixed costs – which is particularly helpful to tenants during quieter trading periods.

As a result, our income is highly dependent on the tenant's success, and we are therefore highly motivated to support our them to be more successful.

The Government appears to misunderstand how rent is calculated. Rent is determined by market conditions (as are all commercial and domestic rents), and are freely negotiated by prospective tenants and pub companies at the start of a new agreement.

We supply detailed rental assessments to prospective tenants as part of the negotiation process and these assessment all have to comply with rules and guidance issued by the Royal Institution of Chartered Surveyors (RICS). The reality is that we have the same control over rental values as an individual has the power to influence the value of their house.

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<sup>1</sup> Letters, emails, BII referrals or escalations to senior management

We recognise that we have a responsibility to ensure that our tenants have the necessary information to make informed decisions. Trust and transparency are the cornerstones of a mutually beneficial and successful partnership.

During the course of an agreement the rent of the pub will be reviewed to prevailing market rates (typically every 3 or 5 years). All market rental valuations and assessments comply with RICS rules and are prepared and approved by RICS qualified Chartered Surveyors. Valuations are prepared by comparing the rents of similar pubs, in similar locations and let on similar commercial terms including the purchase price of beer.

**The tied pub sector is unique in that it allows rent to be reviewed downwards if market rents have fallen. This is the only commercial property sector where this is standard practice.**

If we are unable to agree the market rent with a tenant at rent review an Alternative Dispute Resolution (ADR) scheme called PIRRS exists to allow a for a low cost independent valuer to assess the rent. Again, this is the only property sector where there is an ADR process as routine.

The vast majority of rents are freely negotiated between tenants and pub companies; very few rents are determined through dispute resolution.

#### Tenant hardship

The Government consultation refers to survey evidence of tenant income levels. More recently CAMRA released 'survey evidence' which suggested many tenants earn less than the national minimum wage. We do not recognise these figures from our business. We note that following publication CAMRA admitted to an error in calculation and reissued the figures.

Among the challenges in this area is the different definition of 'income' and 'profit' used by different groups and surveys. Tenants are not salaried by the pub company and many will operate their businesses in different ways. A direct comparison with salaried staff is not straightforward and does not always take into account factors such as free accommodation. We believe there would be benefit in a better understanding of how different tenant income and profitability figures are measured and compared across the pub industry.

#### Tenant investment

The consultation argues that by transferring value to tenants, this will lead to a positive improvement in investment in pubs. Given that the majority of our pubs



operate on a traditional brewery tenancy model of three to five years, it is difficult to see how tenants would have an incentive to make major investments in their pubs if the return on that investment was unlikely to be repaid before the end of their tenancy period.

Furthermore, the levels of value transfer envisaged by the consultation would not lend themselves to significant additional investment by tenants. The £102m value transfer envisaged by the consultation should be considered in the context of the £13m of capital investment that Star Pubs & Bars is making in 2013 to improve our pubs estate, in addition to general maintenance. As it has become increasingly difficult for tenants to access capital through banks, it is highly unlikely that the levels of value transfer envisaged would allow many to embark on the major capital investment that many pubs need to grow their business. Even during more positive economic conditions, those on 3–5 year traditional brewery tenancies or short term agreements can find it difficult to raise capital as lenders are concerned about their ability to repay within the tenancy period.

## Specific proposals and consultation questions

### Statutory Code

*Q.1 Should there be a Statutory Code?*

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

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

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

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

We believe that self regulation is working and offers a fast, low cost and effective way of resolving disputes between us and our tenants. Significant progress has been made in the past few years and the implementation of the new IFC 6 provides additional protection and transparency for tenants. This Code of Conduct forms part of the contract between us and our tenants and is therefore legally binding.

### PIRRS & PICAS

To ensure that tenants are charged a fair market rent, since 2009 the industry has provided funding for an independent body (PIRRS) which allows for a low cost resolution of rental disputes. It provides a real safety net for tenants to ensure that a pub company is unable to use its position to seek rent above market value.

To address wider concerns from tenants about the conduct of their pub company, the industry also established an independent service (PICAS) to investigate complaints by tenants with the ability to compensate tenants if it finds in their favour. PICAS is in its first full year of operation.

It has been suggested that the relatively small number of cases resolved by PICAS and PIRRS represents failure. We believe it is a mark of success because it suggests that there has been an improvement in pub company and tenant relationships and where disputes arise there is greater focus on settling to the satisfaction of both parties without recourse to PICAS or PIRRS. Given that there are always commercial negotiations in any business relationship we believe that this is good practice.

The Statutory Code and Adjudicator proposed by the Government have significant cost implications. We believe that this money would be better used to invest and

innovate to grow sales in our pubs than to fund a new bureaucracy when there are existing low cost dispute resolution options.

We believe that self regulation has been successful and would be happy to discuss further improvements to the current IFC 6. We therefore do not believe that there is a requirement for a Statutory Code. If the Government does proceed, it should be based on the current IFC 6 as we do not support all of the proposals in the consultation.

#### Alterations required to the statutory code

Part 8 of the Code on Compliance should be reviewed to remove the need to appoint a single person as a Compliance Officer. Individual businesses should be free to put in place a corporate governance structure that suits them in order to meet the requirements of the Code.

The Rent Assessment section of the Code does not comply with RICS Guidance.

The Code should exclude tenancy agreements of less than a year. These short term agreements are used to temporarily keep pubs open for the benefit of the community and continuity of the business while a permanent tenant is recruited. If the Code were to apply to these agreements, it would force some pubs to close. This in turn would disadvantage the new tenant as they would be forced to rebuild the trade from scratch.

The Code should not apply to free of tie agreements.

#### Review of the statutory code

We believe that it is sensible to review the Code periodically, perhaps every two to three years to ensure it is operating effectively.

## 500 pub threshold for the Code

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

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

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

### Threshold is unfair and restricts competition

We believe that setting a 500 pub threshold would be a significant restriction of competition and we do not support it. As a brewer and cider maker we cannot support a system which regulates our pubs in a different way to pubs owned by our competitors.

Given that the Government has stated that “the main benefit and aim of the policy is the estimated transfer from pub owning companies to tenants of £102m per year”, it is proposing to legislate to reduce the profits of some businesses but not others and without evidence that tenants of companies with fewer than 500 pubs are better off than our tenants. It is clear that other brewers that own pubs would not be affected and would not therefore have to bear the cost of the adjudicator or transfer value to their tenants, irrespective of whether their tenants are better or worse off than ours. This is unfair and a significant and unjustified restriction of competition.

### Lack of evidence for 500 threshold

The Government offers no evidence that tenants of pub companies with fewer than 500 pubs have any more income than those of larger pub companies. Meanwhile the BII has made clear that the figures used by the Government to justify intervention on the basis of calls made to its helpline is flawed and do not represent actual complaints.

By setting a threshold, the Government would establish a two tier system where some tenants have less protection than others. We believe that companies of all sizes which operate fairly should have nothing to fear from being included.

We have heard concerns from some groups that while in principle they do not oppose the Code covering all companies, they are concerned at the cost burden on smaller companies. We believe this could be resolved by a funding arrangement where large companies pay the bulk of the cost.

### Applicability of any threshold

If a threshold is set, it must apply to the number of tied leased and tenanted pubs owned by a company. It should not cover non tied, managed or franchised pubs.

We understand that the regulation of pub companies is considered by BIS and the Scottish Government to be devolved. This raises the question of a different approach north and south of the border. In this scenario, leased and tenanted pubs in Scotland should not be counted towards any threshold set for the rest of the UK.

We do not believe that companies operating a 'free of tie' model should be covered by the Code as it is a purely commercial property relationship. The Government has suggested that even if the tie is removed and the transaction becomes solely about property, the Adjudicator and the Code would continue to apply allowing the dry rent to be dictated despite the pub no longer being tied. It is not clear to us the legal basis that the Government would have to regulate rents in such a relationship when it does not do so in any other commercial property sector. We believe there would be no justification for this kind of intervention in such a commercial relationship.

Finally it is important to recognise that we have a number of agreements in place to lease pubs to other large companies including in some cases other brewers and competitors. As large businesses in their own right, they are well able to conduct commercial negotiations with us and we do not think they should be subject to the same provisions the Government wishes to introduce to protect smaller tenants on lower incomes.

### **Mandatory 'free of tie' option**

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

We fundamentally oppose this proposal as selling our beers and cider is the reason that we have invested £600m since 2010 in purchasing and then improving the pubs we own. They are the shop window for our products.

In a tough trading environment the pubs that will succeed are those that invest to make the customer experience more attractive. We believe this proposal will reduce our ability and the incentive to reinvest in our pub estate. In fact there would be no incentive to support a pub that was selling beer produced by one of our competitors.

This proposal would do little to grow the size of most pubs' turnover or profit. By adding a third party in to the relationship (e.g. a wholesaler), more of the profit

from the sale of beer and cider will be taken by businesses without a direct interest in the future of those pubs, thereby reducing the ability to reinvest.

As it became uneconomic to continue to offer SCORFA benefits this would most affect tenants at the lower end of the market who get greatest benefit from these services. There would be a tipping point where we could no longer provide these services and sustain a mixed model of tied and 'free of tie' leases.

A mandatory 'free of tie' option would encourage a position where the relationship between pub companies and tenants is reduced to a property only transaction where there is less shared risk and reward and where the pub company has little shared incentive in the performance of the pub.

There is a significant risk that rather than helping struggling landlords, the unintended consequences of the proposals would be the closure of more pubs, a reduction in investment and less support for tenants and lessees.

We are concerned that there is little understanding of how existing 'free of tie' models operate. While tenants may wish to see lower beer prices, it is not clear that moving to a pure commercial property arrangement with higher rent, lower investment, and no knowledge or expertise in increasing beer and cider sales would be in their best interests. Some may take a short term view that proves to be damaging to their business in the longer term.

It has been suggested that removing or loosening the tie would provide more opportunity for a large brewer such as HEINEKEN to sell our products to more pubs. While there could be a short term commercial advantage, we are concerned that the overall impact will be an accelerated structural decline leading to further pub closures, less investment and less innovation which would limit the market opportunity. We would also lose certainty within our supply chain that our UK breweries and cider mills would benefit from with a guaranteed and low cost route to market.

## Overarching principles of 'Fair and Lawful Dealing' and 'No Worse Off'

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

*i. Principle of Fair and Lawful Dealing*

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

### Fair and lawful dealing

HEINEKEN is a major supporter of the great British pub and we want our tenants to have profitable and sustainable businesses. We share the Government's aim to support a healthy, thriving and diverse pubs sector.

We support the principle of fair and lawful dealing which we believe already operates through IFC6.

### No worse off than 'free of tie'

On the question of whether an additional "principle that a tenant should be no worse off than if they were 'free of tie'" should be introduced, we have significant concerns. What may appear at first to be an attractive, simple principle to help tenants at the lower end of the market is actually significantly more complicated.

### 'free of tie' versus Freehold

Before our model can be compared against "free of tie", there needs to be a clearer understanding of what 'free of tie' actually represents.

Many people confuse 'free of tie' with a 'freehold'. The only similarity between 'free of tie' and 'freehold' is that landlords are able to purchase their beer and cider from any source. There the similarity ends as the reality is that the business models are otherwise completely different.

A 'freehold' pub landlord will either own the pub outright or have a loan to cover the balance of the purchase price. The purchase of a freehold is a very large financial undertaking and is a major barrier to entry for very many aspiring publicans particularly as banks are increasingly reluctant to lend or to offer affordable terms.

As with a homeowner, the freehold landlord assumes all the risks and costs associated with owning the property. In return for taking the risk of purchasing the freehold, the landlord may see higher returns. However, there will also be risks of

rising interest rates, falling asset values, defaulting on loans, large maintenance or investment costs etc. The 'freehold' landlord is free to source beer and cider from any source, however the price each landlord obtains will be dictated by factors including volume sales, trading history and credit risk.

#### 'free of tie' model

The 'free of tie' model described by the Government only applies to a small number of pubs. Groups such as Wellington operate on a pure property lease basis which means higher fixed costs (dry rent), no business support services and less flexibility on payment terms. Their model is based on different capital and operating cost structures.

Under the 'free of tie' model tenants enter a contract with the property owner. There is no obligation to purchase beer from the owner. The property company provides no advice or expertise on the operation of the pub market and there are no SCORFA services.

#### Tied and 'free of tie' models are not directly comparable

We do not believe that it is possible or sensible to compare our model – with its lower fixed costs, lower risk, business support services, investment profile, access to affordable capital, and shared interest in growing beer and cider sales – to a 'free of tie' model which is purely a property transaction relationship.

The Government has provided no evidence that this 'free of tie' model offers greater benefits to tenants who would then be contracted to a landlord with no direct interest, information or stake in the operation of the pub business beyond the dry rent, which would be higher leading to larger fixed costs.

We believe that it is misguided of the Government to compare our model with one which removes the incentive for both parties to grow the pub business in partnership and replaces it with a pure property transaction. Investment, innovation and insight are crucial to reversing the fortunes of the sector by improving pubs, finding new ways to deliver what customers want at a lower cost to the tenant, and trialling new approaches. A model which pushes tenants and pub companies in to a purely property relationship would reduce investment and innovation across the sector, sharing of best practice and the ability to drive up standards across the estate.

We believe that our tenants and lessees are already in a stronger position than the 'free of tie' model suggested by the Government. We note that the Government has not provided any evidence to suggest that tenants in this small 'free of tie' sector



are performing better than our tenants. To try to compare the models by way of an artificial formula is like comparing apples and oranges.

Furthermore the comparison between tied and 'free of tie' models is complicated significantly by the difference between traditional brewery tenancies and long leases (often on a FRI basis). The length of the contracts and the obligations on the tenant vary significantly between the two agreements and therefore so does the mix of risk and reward. This is not captured in any way in the example of the formula the Government proposes to measure the difference between tied and 'free of tie' models but is absolutely fundamental to the difference in business models and support we offer. Every tenant will have their own personal view of risk and how much they are prepared to take.

### SCORFA benefits

We also believe that it is difficult to provide an objective valuation of SCORFA benefits to include in a comparison formula as by definition the value of these is subjective and varies by tenant. Often they are of greatest benefit to smaller tenants than to larger ones operating at the top end of the market.

The perceived value of some of these benefits can depend on:

- the individual tenant's available time (e.g. how much longer it might take a tenant to order a service, manage a repair or resolve a licensing issue themselves without support and the opportunity cost of not using that time in the pub).
- their experience and the extent to which they use the insight and expertise offered (e.g. what knowledge they have about the most appropriate levels of insurance cover, best utilities deals or food insight).

## Specific proposals for inclusion in the statutory code

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

- i. Provide the tenant the right to request an open market rent review if they have not had one in five years, if the pub company significantly increases drink prices or if an event occurs outside the tenant's control.*
- ii. Increase transparency, in particular by requiring the pub company to produce parallel 'tied' and 'free-of-tie' rent assessments so that a tenant can ensure that they are no worse off.*
- iii. Abolish the gaming machine tie and mandate that no products other than drinks may be tied.*
- iv. Provide a 'guest beer' option in all tied pubs.*
- v. Provide that flow monitoring equipment may not be used to determine whether a tenant is complying with purchasing obligations, or as evidence in enforcing such obligations*

### Open market rent review

We support the Government's proposals on Open Market Rent Review which we think reflect current good practice, make good business sense, and are in keeping with the spirit of the relationship we have with our tenants.

We support the ability for tenants to request an open market rent review if there has not been one in five years or if there is a significant increase in drinks prices. This is in keeping with our current approach where we only increase our prices once a year for cost of goods rises, supplier increases or duty changes. Significant rises due to duty or tax increases should be excluded as they are outside of our control. Subject to guidance and a sensible definition we would also support a review where an event occurs outside the tenant's control which impacts on the business. Our existing practice in such an event would be to seek to work with the tenant to support them through rent concessions or other measures.

### Transparency

We support measures to improve transparency. However we refer to our concerns about the comparison between our model and 'free of tie' elsewhere in this response for the difficulties in providing parallel rent assessments that are accurate and meaningful.

### Gaming machine tie

We believe that there has been a significant misunderstanding of the role of the gaming machine tie and the major changes that we have already made to ensure it operates to the benefit of our tenants, Star Pubs & Bars and to the Government through better regulation of a sector that is vulnerable to criminal activity.

We have made our offer fair and transparent by removing all royalty payments and administration fees. Tied machine income is not used to calculate dry rent. This ensures that there is a genuine partnership where the profits are shared with our lessees who benefit from the scale and expertise of Star Pubs & Bars and our contractors.

This is a highly specialist area, and our expertise in delivering insight and innovation in machine management has meant that our pubs have benefited from the best income in the leased/tenanted market. We also provide support to ensure tenants meet their statutory obligations under gaming, licensing and taxation regulations.

By removing the tie the Government opens the door to organised crime, money laundering and reduced gaming receipts as a result.

It is vitally important that if the Government removes the tie, that we retain the ability to enter in to binding contracts with our tenants to provide the latest and best managed machines to help grow their income and ours. Poorly managed machines will simply lead to reduced income for tenants. We already work with tenants to offer differing share splits of gaming machine income to suit their business.

### Guest beer option

This proposal fundamentally undermines the principle of the tie by allowing tenants to choose alternative brands which would mean forcing HEINEKEN and Star Pubs & Bars to allow the sale of major competitor brands in our own pubs.

Of greatest concern is the fact that the Guest Beer Option could be used for any product. The logic of this is that tenants would not choose to exercise this option to introduce relatively low sales lines. There would be a much greater incentive to use it to circumvent the tie and replace the highest selling tied product with a competitor. This would reduce the tenant's 'wet rent'.

It also undermines the major progress made by pub companies in providing a low cost route to market for many small and microbreweries through our estate. There

is already significant competition and choice for consumers with greater availability of cask ales in tied estates than managed and freehold.

Through our Discover Cask programme, Star Pubs & Bars already works with our tenants to bring cask and local beers to our customers where it is clearly in the best interests of the individual business. We have 52 cask brands available through Star Pubs & Bars all year round from 36 regional brewers including the Caledonian Brewery and Theakston's. In addition we offer 16 guest beers each month.

There is limited space on the bar and there is a risk that tenants would use the Guest Beer Option, not to bring new local and regional beers to the pub, but to replace high selling mainstream products. The Government should reject this proposal as it would fundamentally undermine the legitimate operation of the beer tie.

#### Flow Monitoring Equipment

We do not agree with this proposal. There is no evidence presented in the consultation as to why flow monitoring equipment should not be used as part of the process to determine if a tenant is not complying with purchasing obligations. The argument that flow monitoring equipment did not exist in the 18<sup>th</sup> Century and therefore is not required in the 21<sup>st</sup> Century is irrelevant. Tenants that comply with the terms of their contract have nothing to fear from flow monitoring equipment and IFC 6 already requires additional evidence before a tenant could be found to be in breach.

## Role of the Adjudicator

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

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

*i. Arbitrate individual disputes?*

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

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

*i. Recommendations?*

*ii. Requirements to publish information ('name and shame')?*

*iii. Financial penalties?*

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

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

If the Government chooses to proceed with a Statutory Code, it is logical to appoint an Adjudicator to oversee it.

We believe that there is no valid reason why the Adjudicator, if established, should not oversee all pub company / tenant relationships. The Government has not led any reliable evidence to suggest that tenants of companies with 500 or more pubs are at a disadvantage compared to those of fewer than 500 pubs.

We argue that the balance of power between tenant and landlord is no different for an individual operator in a group of 501, or for that matter 1300, than it is in a group of 300. If the Government is intent on proceeding with the Adjudicator then it should apply to all tied leased and tenanted pubs to ensure a level playing field and equal support and protection for tenants of all pub companies.

We recognise that there may be concerns that funding the Adjudicator would be an additional cost on smaller companies. We believe that there is a solution where larger companies could fund the bulk of the cost of the Adjudicator to limit the cost for smaller companies. We would also support the costs of the Adjudicator in subsequent years being met by large companies in proportion to the number of cases where the Adjudicator rules that the pub company has a case to answer. It should not be based on the number of referrals but on the outcome of the cases.

We also believe that changes should be made to how the Adjudicator operates to make it more of an 'appeal mechanism' where tenants are unable to reach agreement through existing effective low cost services such as PIRRS and PICAS. By continuing to use these services, it would reduce the number of complaints to the Adjudicator (thereby limiting the cost), provide quick and cost effective ways to manage minor disputes, and free up time for the Adjudicator to consider only the most serious allegations of abuse.

PIRRS and PICAS are currently funded predominantly by the largest pub companies. There would be no reason to continue funding these if the current proposals were enacted. This would leave those pub companies with fewer than 500 pubs to fund these services in the future.

We believe it makes most sense for the Adjudicator to:

- apply to all tied leased and tenanted pub companies
- be funded predominantly by the largest businesses, with a higher contribution made by companies where the Adjudicator has found against them in referred cases
- operate alongside a continued PIRRS and PICAS service which would operate as a low cost mechanism which can also consider a wide range including smaller issues that would clog up the Adjudicator
- become an appeal mechanism for tenants unhappy with the outcome of PIRRS and PICAS
- be freed up to investigate the most serious allegations of abuse.

Until there is clarity on how the Adjudicator would operate and the content of the Code that it would oversee, it is difficult to comment on what powers of sanction or fines it should have. We believe that the Government should consult on this separately if it goes ahead with the Statutory Code and once its final content is known.

## Alternative approaches

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

As we have stated throughout our response we believe that the consultation is about managing the continued decline of the pub sector as it fails to address the challenges facing the sector in a meaningful way.

To tackle the challenges facing the pub sector, we need to work together on a plan for growth that gets more people back in to the pub, spending more money. Without that plan, no amount of rules, regulations and formulas will convince ordinary people to open their wallets and spend more of their hard earned cash in their local. Rather than proposals which simply seek to divide up a shrinking cake, we need a plan to grow the cake so everyone benefits.

We believe that more can be achieved through self regulation.

We also propose a package of measures that are focussed on helping pubs to reverse the trend of declining visits and sales and help get more people back in to the pub which is crucial to a sustainable increase in tenant incomes.

- In recognition of the difficulty that tenants face in raising capital, the Government should convene a summit with major lenders to discuss the benefits of increased lending to pub tenants and landlords.
- The Government should consider the opportunities to increase capital allowances to encourage greater investment in the pub estate.
- The Government should recognise the significant cost incurred due to business rates which have not been reviewed for many years. It would be wrong to require pub companies to regularly review their rent costs if the Government was unable to ensure regular assessment of business rate liabilities.
- The Government should consider a business rates holiday for the first year of a new pub tenancy to support tenants at a time when cashflow problems tend to be highest.
- To rebalance the market, the Government should support a reduction in VAT for food served in pubs to match the rate for supermarkets.
- The Government should support skills and training in the sector particularly to identify the next generation of innovative and entrepreneurial landlords by working with the industry to raise awareness of the career opportunities in the sector and to provide business advice services.

### **About HEINEKEN and Star Pubs & Bars**

HEINEKEN is the UK's leading cider and beer producer and the name behind drinks brands such as Foster's, Strongbow, Kronenbourg 1664, Bulmers, John Smith's and Heineken®. We directly employ around 2,400 people in our UK business and we operate from sites in London, Edinburgh, Livingston, Manchester, Tadcaster and Herefordshire. More than 90 per cent of our beer sold in the UK is brewed in the UK and we are a major supporter of British agriculture sourcing 100% of our malt and barley for our UK brewed beer from UK farms and maltsters. Around 30% of all UK apples are used to produce our ciders.

HEINEKEN UK is a passionate supporter of the great British pub. Since 2010, HEINEKEN has invested £600m in developing our pub business including purchasing 918 great British pubs from Royal Bank of Scotland. Today, through our Star Pubs & Bars business we own a nationwide estate of 1,300 high quality invested pubs which in turn employ an average of 10 people per pub.

### **How our model works**

- 77% of our pubs are community pubs and the majority of our tenants and lessees are from the local community in which they work.
- Less than a quarter of our pubs operate long term leases of up to 25 years—often known as Fully Repairing and Insuring leases.
- Our remaining pubs operate on a traditional brewery tenancy agreement with the majority being between three and five years.
- We do also operate some shorter term agreements.
- We operate a tie on beer and cider in our pubs. We do not tie our tenants and lessees on wine or spirits.

### **Benefits of our model**

The beer tie works for small businesses and supports the British brewing industry. As a brewer which brews more than 90% of the beer we sell in the UK, the future of our breweries and cider mills in the UK is closely linked to the success of our pubs.

Our model offers hundreds of small businesses and entrepreneurs who want to run a pub but simply cannot afford the high levels of capital investment required to purchase a freehold pub the opportunity to start and build a business in the pub trade.

For a small capital outlay we supply a new pub landlord with a site, alongside training and maintenance. In return our tenants pay rent, and promise to buy their



beer through us. The result is a low cost model that manages the risk for the tenant. Given the current lack of bank lending to small business and the high cost of obtaining a freehold, without our model, entering the pub market would be unachievable for many people. It is possible through our new business start up agreements to enter the market and run your pub for as little as £10k investment with the ability to exit with just three months notice.

Our main interest is in growing our business in partnership with our tenants and lessees and we are working hard to help small businesses through tough economic times. Our sustainability depends on the success of our lessees. It costs HEINEKEN and Star Pubs & Bars an average of £60,000 every time a lessee changes.

We believe that our tenants benefit significantly from our model with low cost and low risk entry to the market; significant investment in our pub estate; and a wide range of additional benefits and support measures that mean that our tenants are enjoying returns ahead of the market and higher beer sales. Because our pubs sell our cider and beer we have a direct interest in working in partnership with our lessees to grow their businesses.

### **Our vision for growth**

HEINEKEN and Star Pubs & Bars have an ambitious agenda to support the great British pub with the investment, expertise and support needed to reverse the trend of declining beer drinkers and pub goers. We are a vertically integrated brewer which is investing in pubs in order to sell our beers and ciders.

Our vision is not based on managing decline, but on returning growth to the pub sector. We believe that we will succeed where we invest in the right pubs, in the right place, with the right tenants. We believe that investment, innovation and insight, coupled with motivated entrepreneurial tenants is the key to success. We have many examples of where our investment has given tenants access to capital that is simply not available through banks, but which can transform the pub, bringing new customers and significantly increased income.

We recognise that there have been concerns in the past about how the market has operated. As relatively new entrants, HEINEKEN and Star Pubs & Bars are on a journey to make the sector more sustainable. We love great British pubs and believe they have a valuable role in society at the heart of their communities. Our leased pub business model supports SMEs, helping them to create businesses that are sustainable in the long term.

### Investment and support

In 2013 our capital expenditure to improve our pubs stands at £13m – equivalent to £10k per pub. This excludes the cost of operating repairs and maintenance. We believe that this investment is critical to the success of our pubs as competition increases and consumers demand higher standards from their local pub. In a tight financial environment access to capital to invest in their businesses is difficult for lessees to secure from banks and therefore our investment is vital to the growth of their businesses.

We're helping our lessees to create more sustainable businesses through support for funding when they start running a new pub and through capital investment for refurbishments. We also provide business advice, industry-leading expertise, training and support initiatives which have resulted in the highest average sales turnovers of any national UK leased pub estate.

Services include support for:

- Training courses and online training packages for tenants and their staff
- Property maintenance
- Compliance
- Ratings and licensing
- Subsidies for Sky TV
- Food and menu support
- Utilities
- Merchandising and promotional activity
- Mystery shopper service with cash bonuses for good results
- Procurement benefits for insurance, equipment and consumables
- Category support for wines, spirits and soft drinks
- Early access to new innovation in beer and cider
- Technical services
- Financial assistance with payment of large bills and additional bonuses for achieving pre agreed volume targets.

Our insight in to what customers want from a pub today and in the future is second to none, meaning that our tenants benefit from the expert support they need to move from running a pub as a vocation, to running a pub as a growing business that meets the needs and expectations of its customers. We also have a strong

focus on innovation, trialling new approaches to bring additional customers to our pubs and increase profitability which we share across our estate.

### Our leases

We have launched new start up agreements providing low cost entry to new lessees. We believe a sure foundation is critical to the long term success of a pub and we invest heavily in first year support programmes and business planning to keep lessees' risk and investment low and enable them to terminate contracts with three months' notice.

Our leases are written in plain English and have distinct differences designed to help potential tenants and lessees to choose the agreement that's right for them. For example:

- ***Business Start Up Agreement (Three Years)*** – designed for first time operators, this lease includes our unique 'walk-away' clause which allows tenants to terminate their contract with us, at any time and for any reason, giving only 3 months' notice. They have to carry out some internal repairs and decorations.
- ***Rolling Tenancy (Three Years)*** – designed for operators with some business experience, this lease offers the protection of the Landlord & Tenant Act and entitles tenants to renew the lease at the end of the tenancy. They have to carry out some internal repairs and decorations.
- ***Fully Repairing and Insuring Lease (By Agreement)*** – designed for experienced operators, our long term lease (10+ years) is fully assignable (i.e. lessees can sell it on) and lessees are responsible for all repairs.

All of the agreements above offer a 'Cooling Off' Period. This lasts for the first three months and means that if a tenant or lessee decides that the pub is not for them, they can leave at any time and without incurring cancellation fees.

[ For further information we have appended a copy of "Is it for me – The plain English guide to running a leased pub with Star Pubs & Bars". ]

*not published – already in public domain*