

Punch Confidential Submission Version for BIS: Contains Business Secrets

Punch Taverns plc (Punch)

response to

The Department for Business, Innovation and Skills:

'The Proposed Statutory Code: Draft Pubs Code of Practice' (the Code)

14<sup>th</sup> June 2013

## **Executive Summary**

1. The tied business model provides significant benefits to tenants – low capital requirements, reduced risk and less exposure to any downturn, lifestyle benefits and substantial support from tied pub companies. This was recognised by the Office of Fair Trading (OFT). See, 1.2 on page 5 below.
2. The interests of pub companies and their tenants are aligned. Tied pub companies are incentivised to ensure their tied agreements are attractive to new tenant partners and provide a sound platform for those partners to compete effectively. Again, this was recognised by the OFT. See, 1.3 on page 7 below.
3. There is already an effective system of self-regulation. Every member of the British Beer and Pub Association (BBPA) is committed to implementing an industry Code that addresses all of the issues raised by earlier select committee reports. Each company code is already legally binding, because it is included in new pub leases. See, 1.4 on page 7 below.
4. There is no reliable evidence to support the Government's objectives. In particular, the Government provides no evidence either that self-regulation is not working, or that there is an imbalance in risks and rewards between the pub companies and their tenants. In determining the level of rewards, the Government seeks to rely on:
  - (i) Data from the British Institute of Innkeeping (BII) helpline – which the Government accepts has since been discredited.
  - (ii) 'Evidence' of apparent hardship from a survey carried out in 2011 by the Institute for Public Policy Research (IPPR) – which the Government recognises as 'unreliable'.
  - (iii) Evidence on pub closures – which the Government accepts does not support a finding of imbalance.
  - (iv) 'Evidence' of tenants' poor literacy and numeracy – which is wrong and misleading.
  - (v) Unsubstantiated allegations and hearsay.See, 1.5 on page 8 below.
5. Government intervention would result in serious adverse consequences – for consumers, business and employment. Research by Compass Lexecon for the BBPA shows that a mandatory free-of-tie option for tenants would lead to around :       pubs becoming unviable and closing. Directly and indirectly, this loss in these pubs accounts to       in value to the economy and a loss of jobs. The proposals would also put at risk:       of annual investment in pubs and prejudice sales of cask ales. See, 1.6 on page 10 below.

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## Section 1 – Overview

### 1.1 Introduction

Very few sectors of the economy have suffered intervention from successive Governments on a scale to match that of the brewing and licensed trade. Decades of Government intervention have left a trail of unintended consequences in their wake – with a large number of pubs changing ownership and business models evolving. As an example, the ill-fated Supply of Beer (Tied Estate) Order of 1989, which was finally repealed in 2002, created unforeseen, long-lasting and far-reaching distortions in the market. The pub and brewing sector have been subject to unprecedented Government intervention, with 42 regulatory reviews since 1969.

In recent years, the pub market and the landlord and tenant relationship have been freer from Government interference. As a result, we have seen the sector mature into a well-informed, healthy and self-regulated market. The Government's current proposals, as set out in the consultation document, would have unintended and far-reaching consequences. They would be bad for jobs and bad for business.

The traditional pub sector has come under considerable pressure over the past few decades. The recession, the smoking ban, regulatory changes, transforming social habits and discounted alcohol pricing by the supermarkets have all played a part. A recent survey shows that 26 pubs are closing every week.

Behind the current proposals is an assumption that the tied business model is to blame for this decline. In the foreword to the consultation document, the Secretary of State states, "the activities of the major pub companies, with their highly leveraged business model, have intensified the crisis". However, this is unsubstantiated and not true. It is also not consistent with the Government's own impact assessment which states:

*"The decline [in pub numbers] 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.*

*"Some campaigners argue the tie plays a factor, but pub numbers do not support this."*

### 1.2 The tied business model provides significant benefits to tenants

The tied business model provides a unique opportunity for entrepreneurs interested in running a small business.

#### Low capital repayments

A tied tenant needs only a low level of capital to start their business. A typical tied tenant can begin with as little as £15,000 in capital, whereas for a typical franchise the required capital would be around £100,000 or more.

On-going capital costs are also low, which aids cash flow. For example: rent deposits can be built up; rent is paid weekly or two-weekly, not quarterly in advance; and repair liabilities can sit with the pub company.

### Lower risk

The business model also allows for a lower fixed property rent, in return for the tied 'wet rent'. The effect is to make a higher proportion of the total 'rent' paid variable – it decreases if beer sales decrease. As a result, a tied tenant has a lower level of risk compared to a free-of-tie occupier, whose rent would be based entirely on a fixed cost. This is of particular benefit to tenants in economic conditions where beer sales are declining – in effect, the risk of lower sales is shared between the pub company and the tenant partner.

### Lifestyle benefits

Tied pubs also provide a lifestyle and standard of living that is rarely offered by other businesses. The tenant is given a large property to live and work in – often at the heart of the community.

### Other benefits

The Office of Fair Trading (OFT) concluded in its 2010 report into the market that: “ as per prior analyses in this sector, the higher beer prices charged by tied lessees are offset by lower dry rent and business benefits”.

In fact, free-of-tie tenants are usually worse off than tied tenants, because tied tenants receive significant support from their pub company. Punch Taverns' tenant partners benefit from:

- Business support and professional advice, for example:
  - Partnership Development Managers provide tailored business advice
  - Catering Development Managers provide bespoke menus and a huge amount of expertise in food retailing.
  - Territory Dispense Managers deliver specialist beer and dispense guidance
  - Regional Launch Managers offer new businesses the best start for long-term success
  - Property Managers provide specialist property repair and investment solutions
  - RICS qualified Regional Valuation Surveyors provide fair, honest and open negotiations with partners.
- Mystery customer visits – 6,000 are carried out every year.
- Licensing support, which includes safe, legal and compliant working, health and safety issues, fire and environmental health legislation. The tied business model is more likely to ensure that the pub is run in a legal and compliant manner.
- Award-winning training and development, both bespoke and online – including investment training. Some 605 delegates attend Punch Taverns' Ready for Business Foundation week.
- A discounted business rating service.
- Marketing and promotional support across drinks, food and all aspects of running a pub. Punch Taverns has spent £            on this in the past 12 months.
- A contact centre, telesales and web-based services.
- Discounted rates on supplies that are not for re-sale.
- Support to develop machine income.
- Free Wi-Fi. With 2,309 installations to date and more every day, 50% of the Punch estate is already covered.
- Repairs and property support. Every year, for the past three years, Punch Taverns has invested £40m. Over a similar period, we have spent £            on repairs.

- Tremendous Product Choice including 31 keg ales, 115 cask ales, 23 draught lagers, and 25 bottled ales, as well as access to the SIBA DDS scheme which provides over 3,000 cask ales from 495 small and medium sized brewers. This is a far greater range which is delivered directly than would be available to a free-of-tie operator sourcing their own products locally.

Other crucial support that is not available in the market for a free-of-tie tenant includes:

- Credit terms and flexibility of payment terms to improve cash-flow.
- Reduced rent and in-goings with flexible payment plans.
- Code of Practice commitments, for example, the provision of a guaranteed lease surrender.

The benefit of these services (not including the low rent, deposit build-ups or low-cost finance) has been conservatively estimated at £3,000 for one-off costs and circa £3,700 per annum for the additional services such as Wi-Fi, rating and legal and compliance services. However, this is a minimum, and doesn't include multiple site visits and refurbishment costs. A more realistic estimate would be in the region of £10-12,000.

Only a pub company, through its economies of scale, can provide this level of benefits to tenants.

### **1.3 The interests of pub companies and their tenants are aligned**

The Government claims that there is an imbalance in risk and reward between pub companies and tied tenants. No evidence is provided for this (see further below).

It is not in any pub company's interest to have such an imbalance. Put simply, successful tenants provide success for the pub companies. Each pub company has to compete to attract tenants – not only against other companies, but against free-of-tie leases, freehold pubs and alternative business ventures such as franchises. A company like Punch Taverns also has to make sure its tenant partners can compete effectively – driving higher sales in the pubs through beer and food sales. The risks and rewards are therefore shared. If there is a downturn, the pub company gets a reduced return, as well as the tenant.

This was also the view taken by the OFT, in its 2010 report. The OFT concluded that tied tenants were able to compete effectively and that the commercial interests of pub companies and their tenants were aligned so that:

*"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"*

There is clear evidence of this with the significant support Punch's partners have provided about their relationship with Punch in the testimonials given at Appendix 15. Some of the testimonials have been sent directly to the Department of Business, Innovation & Skills as part of this consultation process.

### **1.4 There is already an effective system of self-regulation**

#### **Self-regulation is working**

The British Beer & Pub Association (BBPA) has now published version six of the Industry Framework Code of Practice for Tied Tenanted and Leased Pubs (known as IFC).

All BBPA members are committed to implementing the Industry Framework Code by revising their own company codes and submitting them to the BII accreditation body. Punch's Code of Practice was the first to be accredited under version 6 of the IFC, on 3 June 2013.

Each company code is already legally binding on new agreements, because it is included in pub leases.

The industry Code addresses all of the issues raised by earlier select committee reports, and the latest version of the Code goes still further in holding pub companies to account for their behaviours and actions. It provides even greater transparency for tenants and lessees, and tackles a range of more commercially sensitive issues.

The industry Code includes both (i) a cost-effective rent review scheme (PIRRS<sup>1</sup>) to which tenants/lessees can appeal in circumstances where there is an unresolved dispute in a rent review; and (ii) an accessible, independent, low-cost dispute resolution service (PICA-Service<sup>2</sup>)

More than 300 enquiries have been made through PIRRS and PICA-Service. Of these 300 enquiries, a small number of cases have gone through to the respective decision panels. The dispute resolution services are inexpensive and have well-respected panel members. Both services have been well-publicised by the pub companies and the trade press, so that tenants are aware of their options.

The cost to access this high quality service is exceptionally low for tenants. They pay £200 for a behavioural adjudication, or £1,000-£2,000 for a rent resolution. By contrast, the average cost for a commercial property dispute would usually be between £10,000 and £25,000.

### **1.5 There is no reliable evidence to support the Government's objectives**

Contrary to the above, the Government appears already to have concluded both:

- (a) that self-regulation is not working and that a statutory code and adjudicator is necessary; and
- (b) that there is an imbalance in risk and reward requiring a transfer of value (£102m) from pub company to tenant.

The Consultation is only concerned with how best to implement these objectives – and not (as it should be) to establish whether or not there is reliable evidence to support the need for such intervention.

It is clear from a review of the consultation documents that the Government was biased in reaching these conclusions, since it did so on the basis of no reliable evidence.

#### **No need for a statutory code or adjudicator**

As set out above, there is already effective self-regulation.

In its response to the last Select Committee report, the Government stated in November 2011 that the industry Code “will directly address the concerns identified by the Committee”. The Government also stated that:

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<sup>1</sup> Pub Independent Rent Review Service.

<sup>2</sup> Pubs Independent Conciliation and Arbitration Service.

*“Government should not intervene in setting the terms of commercial, contractual relationships, where these are fully justified by law and have been found by the OFT to be raising no competition issues that significantly affect consumers. Fundamentally, whether or not a lease or tenancy includes a tie is a commercial decision on the part of both parties.*

The Government provides no evidence to show how the position has now changed and why there is now the need for a Statutory Code or an Adjudicator.

The Government appears to be relying on either or both of the following:

(i) A suggestion that tenants are not informed of their rights. This is misleading. All Punch partners are provided with a hard copy of the code of practice. It is available on the Buying Club website and is now incorporated into all new leases. Indeed, in its press release announcing the consultation, BIS states that “the independent arbitration service appears to be working well”. In any event, if the concern is that tenants are poorly informed, it is not clear how that is addressed by way of a Statutory Code and Adjudicator.

(ii) The allegation that tenants continue to be treated unfairly and suffer significant hardship. There is no reliable evidence to support this. See below.

#### No imbalance in risk and reward

The Government seeks to rely in the consultation on the following:

(i) **Data from the British Institute of Innkeeping (BII) helpline – which the Government accepts has since been discredited.** The Government places significant reliance in the consultation on the BII helpline having received 400 “complaints” over the past three years; the “vast majority” of which being about large pub-owning companies (see page 18 and Figure 1). On 29 April 2013, BII and BIS issued a press statement clarifying that these were in fact calls to the helpline and not necessarily complaints – the calls would have included technical queries from tenants.

(ii) **‘Evidence’ of apparent hardship from a survey carried out in 2011 by the Institute for Public Policy Research (IPPR) – which the Government recognises as “unreliable”.** The Government seeks to rely solely on a survey of 500 licensees carried out in 2011 by the IPPR, which found that 46% of tied publicans earn less than £15,000 per year, compared to 23% for tenants who are free-of-tie. There are a number of problems with this survey – including the following:

- It was funded by CAMRA and Fair Pint (both campaigners against the tie).
- It is based on too small a sample size.
- It does not compare like with like. Of the pubs surveyed by IPPR, the proportion with a turnover > £300k is higher for non-tied pubs than tied pubs (so that it is not surprising that it results in higher earnings for non-tied pubs).

The Government’s Impact Assessment therefore clearly states that the results are “not very reliable”. And yet it is cited as a key piece of evidence by the Government in the consultation.

(iii) **Evidence on pub closures – which the Government accepts does not support a finding of imbalance.** In his foreword, the Secretary of State suggests “it is undoubtedly the case that the

activities of the major pub companies, with their highly leveraged business model, have [led to higher pub closures] (emphasis added)". In fact, far from being "undoubtedly the case" there is no support for this at all. On the contrary, the evidence, if anything, suggests the reverse. This is also specifically recognised in the Government's Impact Assessment (see [1.1] above).

(iv) **'Evidence' of tenant literacy and numeracy – which is wrong and misleading.** The consultation document suggests that there are "concerns regarding... low levels of literacy and numeracy amongst Tenants" and seems to imply that pub companies exploit this situation. This suggestion is wholly wrong and misleading. It relies on an article in the *Publican's Morning Advertiser* from 22 June 2009. However, this was written about managed houses and the plans put in place for apprenticeships. It was not concerned with tied pubs at all who provide support and training (see 4.6 on page 32)

(v) **Unsubstantiated allegations and hearsay.** The only 'evidence' presented for a Statutory Code is from the hearsay of self-appointed representatives.

#### **1.6 Government intervention would result in serious unintended consequences**

The impact of the proposed transfer of value of £102m from the pub companies to tenants under the Government's proposals would have a dramatic negative effect on the pub sector and the wider economy. In particular, it would result in:

(i) **Significant pub closures.** Research by Compass Lexecon for the British Beer and Pub Association shows that a mandatory free-of-tie option for tenants would lead to . . . pubs becoming unviable and closing. Directly and indirectly, this loss in these pubs accounts to . . . in value to the economy and a loss of . . . jobs.

(ii) **Further loss of investment (with further knock-on effects for the wider economy).** As set out above.

(iii) **Punch Taverns currently invests around £40m a year in its pub estate.** Across the six pub companies likely to be affected by the Government's proposals, the total is around £175m. None of the companies would be in a position to continue such high levels of investment and it is naïve for Government to assume tenants would make up the shortfall (especially where the tenant has a short term remaining on their agreement).

(iv) **Reduced sales of cask ales.** Allowing tenants to source their own guest beer is likely to result in them choosing a high-volume lager – not the product of a small or medium-sized brewery. A mandatory 'free-of-tie' option is also likely to reduce sales for these breweries. Only 11% of the wet product sold by free-of-tie tenants is cask ale, compared to 18% for Punch tied tenants. Punch provides a direct route to market for 495 small to medium-sized cask ale brewing companies through SIBA (The Society of Independent Brewers). SIBA supports the retention of the beer tie and the pub company model.

(v) **Abolishing the gaming machine tie.** Removing the gaming machine tie is likely to result in a deregulated sector, where pub tenants and lessees are incentivised to source machines from disreputable companies, paying less tax and less attention to legal compliance.

### 1.7 Concluding remarks

Punch is absolutely opposed to the proposed Code. As explained, we have a number of concerns about cost, unintended consequences and the way the consultation has been delivered. In our view, in its consultation, The Department of Business, Innovation & Skills should focus on two overarching principles.

- It should ensure that the behaviour of pub companies is assessed and challenged. Punch believes this is already happening through the existing self-regulation system.
- It should not assess the economic 'business model' of the pub company. If nothing else, history shows that this is fraught with perverse unintended consequences.

Self-regulation has been successful to date, but it needs a longer time period for a full assessment to be made. In view of that, Punch fails to understand why the Government is now considering further intervention.

At a time when the industry is readjusting to major changes in its operating environment, the Code as set out in the consultation document would add additional cost, risk and bureaucracy to a system that is working well so far. This would be bad for consumers, employment and business within the UK.

As drafted, the Code would also constitute unjustified interference by Government over Punch's possessions, in breach of Article 1, Protocol 1 of the European Convention of Human Rights. Punch clearly reserves its right to challenge any legislation in due course.

In conclusion, the proposed legislation is not proportionate to the 'mischief' it claims to resolve. Across the industry there has been significant cultural change over the past few years. This has resulted in a much-strengthened relationship between landlord and tenant. The support Punch offers its pub partners has never been greater, as evidenced by the 277 partners being moved sufficiently to get involved in the consultation in our defence.

## Section 2 – List of Facts

Punch Taverns facts	
400	Employees of Punch Taverns
1200	The number of small businesses set up with Punch Taverns in last three years
£28,700	Average expected earnings for a Punch pub in 2012, not including benefit of accommodation
	The reduction in rental levels in Punch Taverns pubs in the last three years
660	The number of Punch Taverns rent reviews, carried out by qualified RICS surveyors, which resulted in reduced rents in last three years
300	The number of Punch Taverns pubs that benefited from permanent, mid-term, non-contractual rent reductions in last three years
	The amount spent on permanent, mid-term, non-contractual rent reductions by Punch Taverns Pubs in the last three years
per annum	The amount spent on financial support for Punch Taverns pubs during the recession, by way of rent concessions and reduced beer prices
189	Calls to BII hotline by Punch Partners in last four years
3	Number of calls by Punch Partners to BII hotline recorded as “grievances” in last four years
£123,000	Funding provided for Pub is the Hub, Licensed Trade Charity Volunteers and other charitable organisations
18%	18% of beer sold in the Punch Estate was cask ale, compared to 11% in the free-of-tie market
1,100	Number of pubs taking part in Punch Darts Classic – the biggest darts competition in the world
3,300	Number of Punch partners using the Punch Buying Club online buying and advice service
3000	Cask Ales available through the Direct Distribution Scheme via The Society of Independent Brewers.
233	The number of different beer and lager products available for Punch partners.
277	Punch partners being moved sufficiently to get involved in the consultation in our defence

<b>Punch Taverns investment in our partners, pubs and people</b>	
£120m	Punch Taverns investment in pubs in the last three years
12,000	Jobs created through Punch Taverns pub letting in last three years
6,000	Number of mystery shopper visits funded by Punch to support partners in developing business
!	Amount spent on bespoke marketing materials for Punch partners in last 12 months
2,309	Number of Punch Pubs utilising free Wi-Fi service sourced by Punch Taverns
	Amount spent on Punch contractual repairs in last three years
	Amount spent on Punch non-contractual repairs in last three years
605	Number of delegates attending the Punch Taverns Ready for Business Foundation week in 2012
2,339	Number of partners attending the Punch Taverns Roadshows in 2012
72	Members of staff completing level 2 & 3 NVQ apprenticeships

<b>Pub sector facts</b>	
42	Number of UK & Europe regulatory reviews into pub and brewing industry since 1969
£200	The cost of independent arbitration at the Pub Independent Conciliation and Arbitration service, compared to circa £10,000 for a commercial lease dispute resolution
48%	Uplift in Beer Duty taxation since 2006
	Pubs that will close, if government proposals go ahead
	Jobs at risk if government proposals go ahead

## Section 3 – Punch’s Overall Position in Respect of the Code

### 3.1 The changing face of the pub sector

The pub sector has been under considerable threat over the past few decades. A number of structural economic and social factors have led to a reduction in the number of pubs, and the viability of others has been brought into question.

The decline in the manufacturing base of England and Wales has had a detrimental effect. Traditionally, the core consumer for a traditional ‘wet-led’ pub used to be employed in manufacturing sectors such as mining, steel works, engineering and ship building. The decline in these sectors has led to a large number of once-viable pubs, in now socially deprived areas, having to close.

The smoking ban in 2007 added further substantial pressure, as the traditional wet-led pubs relied on the tradition of a ‘cigarette and a pint’ for a large part of their revenue. Smokers stayed at home and investment in external smoking areas failed to stem the decline in trade. Campaigners have made concerted efforts to amend the smoking ban,<sup>3</sup> but little or no change is expected from Government.

Consumer habits have changed considerably over the past few decades. An increase in stay-at-home activities, including digital media and the internet, mean there is no longer a need to leave the confines of home. The quality of ‘take home’ alcohol products has improved significantly, with cask-conditioned bottled beer and ‘draught’ canned beer. Reasons for leaving home for an evening out are now greatly reduced.

The old publican’s adage that ‘You just need to make the environment more comfortable than the customer’s home and they’ll come through the door’ is no longer true. Pubs need a ‘unique selling point’ (USP) to bring customers to their bar. USPs include entertainment through team events, quizzes, live music and open microphone evenings, as well as food offers, unique drink products like cask ale, and promotions and events such as beer festivals. The cost of providing these, together with the cost of supporting hard-working licensees, is ever-increasing. However, the tied pub company model has a unique ability to service these consumer requirements.

In more recent years, the massive and sometimes loss-leading discounting of alcohol by the large supermarket chains has led to a significant change in drinking habits. ‘Pre-loading’ (drinking cheap alcohol at home) before entering licensed premises has never been more prevalent. The subsequent reduction in alcohol spend in pubs – where alcohol is more expensive because overheads include the costs of property, staff, utilities and tax – has further hit hard-working licensees.

All of the factors affecting the pub sector are recognised by the CGA data quoted in the impact assessment as part of the BIS consultation. It states:

*“Some campaigners argue the tie plays a factor, but pub numbers do not support this. The decline [in pub numbers] is widely recognised to be due to a range of factors, including*

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<sup>3</sup> <http://www.amendthesmokingban.com/>

*changing cultural habits, increased taxation, the rise of low cost selling at supermarkets and the smoking ban.*

*“Figures from the latest CGA Study commissioned by CAMRA show that between March 2010 and September 2012 the closure rate was lower in tied pubs, 4.3%, than in free of tie pubs, 4.5%.”*

### **3.2 The history of Government intervention**

Market intervention by Government into the brewing and licensed trade sector has a long and chequered history.<sup>4</sup> Punch is concerned that another legislative initiative would have significant unforeseen consequences. ‘The Supply of Beer (Tied Estate) Order 1989’, and its subsequent repeal, show that legislative distortions in the market have consequences that are long lasting. However, Punch believes that the market in the leased and tenanted pub sector has moved on significantly, maturing into an efficient market, where information is readily available. The very nature of a healthy commercial market will mean that the healthiest will survive. Pub companies that have out-dated practices and that treat tenants poorly will inevitably need to change to attract good quality operator tenants. Information about poor practices is readily available via the internet and deters would-be tenants. This has led to a positive cultural change in behaviour, which has been further enhanced through self-regulation and the Industry Framework Code, promoting the best commercial practice. A new Punch partner is well informed, advised and trained. A poor ‘landlord and tenant’ relationship works for neither party. Successful Punch partners provide a successful business model. In hindsight, a similar if not identical position was commented on in ‘The Supply of Beer (Tied Estate) Order 1989’:

#### ***“The perverse results of interference in the market***

*“Most of the former brewery executives with whom the authors have spoken have expressed the view – with which, unsurprisingly, none has disagreed – that if the industry had been left to evolve naturally, a weakening of vertical integration, together with consolidation in brewing, would have taken place anyway.*

*“When interference in the market takes place, as here, on a scale scarcely – if ever – seen in the UK since the great post-War nationalisation programme, at least some of the consequences are likely to be perverse. In fact, virtually all of them were.”<sup>5</sup>*

It is unnecessary to intervene further into a market that is known to be competitive, and where self-regulation is working. The market is adjusting to take account of any perceived imbalances. The industry finds itself in the same position now as post-1989; where the market is adjusting itself to the correct place, but Government intervention will stop it in its tracks, causing a damaging lack of investment and a large-scale movement of excellent people out of the sector.

Following Government intervention, the tenants of brewery or pub company leases were granted protection under the Landlord and Tenant Act.<sup>6</sup> This was after lobbying from tenant representatives

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<sup>4</sup> The pubs and brewing industry have been subject to regulatory review in the UK and Europe 42 times since 1969 – see Appendix 1.

<sup>5</sup> *Government Intervention in the Brewing Industry*, Spicer, Thurman, Walters and Ward, published by Palgrave MacMillan, 2012. Fifty executives and Members of Parliament contributed to this publication.

who, at the time, complained that breweries were removing tenants when their unprotected leases came to an end and replacing them with tenants paying a higher rent, or converting their pubs to managed houses.

A protected lease offers tenants the opportunity to invest with security and in the knowledge that a premium can be sought for the leasehold at some point in the future. However, the sale of these leases, at the height of the market in most cases, has added to the problems faced by the tied pub sector today. After purchasing the lease, the in-going tenant not only has to pay rent, they also have to pay back capital for the lease premium. This is one of a number of unintended consequences of Government legislation into a market that has seen too much regulation and market interference by successive Governments.

### 3.3 The tied business model

The business model of tied leases provides a low-capital, low-risk way for Punch’s partners to enter into their own business. The average start-up cost for a Punch partner is approximately £15,000, which gives access to a property asset of circa £600,000. The on-going capital costs are also low, which aids cash flow. For example, rent deposits can be built up, rent is paid weekly or two-weekly, not quarterly in advance, and repair liabilities can sit with Punch. Terms are flexible and partners receive on-going support through business advice, marketing and promotional help, and training. The business model also allows for a lower fixed property rent, in return for the tied ‘wet rent’ – so the risk is shared between Punch and the partner.

The £15,000 start-up cost is very low compared to other business start-up opportunities. This is a significant small business enabler and supports enterprise, entrepreneurial opportunity and business initiative. A comparison with this business model would be franchising. A typical catering franchisee will require a significant capital investment. As Table 1 shows, the costs vary significantly from £100,000 to £325,000 – and these figures do not usually include franchise fees.

**Table 1**

Catering franchisor	Franchisee investment required – quotes taken from websites
McDonalds	“As a guide, the cost of a restaurant typically ranges from £125,000 to £325,000.” <sup>7</sup>
Subway	“In fact, in some cases, traditional SUBWAY® outlets can be opened for as little as c. £100,000.” <sup>8</sup>
Dominos	“The full approximate cost of a store is £280,000 – exclusive of VAT of which £150,000 must be liquid funds. The price is based on the average cost of a new store build in 2010.” <sup>9</sup>
Baguette Express (Smaller-style franchise)	“Approximate total investment £81,000 to £130,000. “All figures are exclusive of VAT. In addition to the initial licence fee, a management charge of 7% of gross income is payable.” <sup>10</sup>

<sup>6</sup> The Landlord and Tenant (Licensed Premises) Act 1990.

<sup>7</sup> <http://www.mcdonalds.co.uk/ukhome/Aboutus/Franchising/the-finance-bit.html>

<sup>8</sup> [http://www.subway.co.uk/business/franchise/financial\\_information.aspx](http://www.subway.co.uk/business/franchise/financial_information.aspx)

<sup>9</sup> [http://www.dominos.uk.com/franchising/franchising\\_FAQs.aspx](http://www.dominos.uk.com/franchising/franchising_FAQs.aspx)

The incentives for both Punch and its partners are aligned. It is not in Punch's or any pub company's interest for there to be an imbalance in the risk or reward between the landlord and tenant. Put simply – successful partners provide success for Punch. Pub companies with a tied model need to compete to attract tenants – not only against each other, but also against free-of-tie leases, freehold pubs and indeed alternative business ventures such as franchises. Punch also needs to ensure partners compete effectively, to achieve higher beer and food sales in their pubs. The risks and rewards are shared. In a downturn, Punch sees a reduction in income, as does the partner.

Punch provided 458 new business opportunities in 2012, adding significant value to the UK economy. Each of these opportunities adds a further 10 jobs and £80,000 to the local economy.<sup>11</sup>

### 3.4 Support to partners from Punch – SCORFA

Punch is one of the UK's largest leased pub companies, with a portfolio of approximately 4,200 pubs nationwide.

Punch's business model is based on offering enterprising individuals who run pubs a flexible way to run their businesses with support, investment, training and the right trading terms to make them as profitable as possible. The Punch business model is based on Punch's aim to deliver the best standards of service to partners – working closely with them to earn their trust and to help them build quality pub businesses.

Punch's vision is:

***“To become the UK's highest quality, most trusted and best value leased pub company.”***

This vision is at the heart of the Punch business.

Punch offers industry-leading support. Our Pathway to Partnership programme, which began in 2009, has been part of a significant cultural shift in the business towards partners. Pathway to Partnership puts the partner at the heart of the Punch business, and this has continued with the introduction of the sector-leading<sup>12</sup> online services provided via the Punch Buying Club. There are now over 3,300 people trading online with Punch through the Buying Club. The online system provides a full range of services including; exclusive offers, ordering of beers, wines, spirits and soft drinks, partner forum and blog, training, advice and e-learning modules, risk management portal, marketing advice, and 'Creative Hub', which allows for the online ordering of support material.

The concept of SCORFA (Special Commercial or Relevant Financial Advantages) was introduced in 1984 by the European Union in Regulation 1984/83 (the exclusive Block Exemption regulations). In essence, in this context, SCORFA represents the commercial, financial or other advantages that the tenant or lessee receives when taking on a tied agreement. SCORFA as a legal concept was dropped from the successor Block Exemption regulations, however it still remains integral to how the tied

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<sup>10</sup> [http://www.baguette-express.co.uk/franchise-opportunities/franchising\\_financial.php](http://www.baguette-express.co.uk/franchise-opportunities/franchising_financial.php)

<sup>11</sup> ONS Annual Business Survey

<sup>12</sup> Shortlisted for Retail Systems 2011 awards "Best Use of Technology in the Hospitality and Leisure Sector"  
<http://blog.micros-ecommerce.com/2011/08/25/snow-valley-punch-taverns-short-listed-for-award/>  
Shortlisted for eConsultancy Innovation Award 2012: "Innovation in B2B Marketing"  
[http://econsultancy.com/uk/blog/8413-revealed-the-econsultancy-innovation-awards-2012-shortlist?utm\\_medium=twitter&utm\\_source=twitterfeed](http://econsultancy.com/uk/blog/8413-revealed-the-econsultancy-innovation-awards-2012-shortlist?utm_medium=twitter&utm_source=twitterfeed)

model operates. There is no fixed definition of what constitutes SCORFA, as different company operating models and different pub agreements will vary. This is a feature of competition between pub operating companies.

Punch has a significant on-going support programme for both new and existing partners; a number of these would not be available as one-off purchases in the open market. These include:

- Business support – Punch has been recognised as having the best business support in the licensed trade, by the trade<sup>13</sup> and Members of Parliament.<sup>14</sup> This business support is vital to a thriving pub business and all Punch partners get regular visits from the operations team through their dedicated Partnership Development Manager (PDM). These visits identify growth opportunities for the pub through a number of different initiatives (see below).
- Mystery customer visits – Punch partners receive regular mystery shopper visits with two mystery shopper reports per year. The Operations Team visit the pub after the report has been produced and provide feedback to the partner at a business review. There is no direct cost to Punch partners for this service.
- Licensing support – At Punch we hold the premises licence for the majority of the estate. This removes an additional regulatory burden from Punch partners and significantly reduces the cost compared to the open market.

Punch provides a number of significant licensing and responsible retailing resources to partners.<sup>15</sup> The Licensing Team at Punch foster excellent relationships with both local licensing authorities and the Police.

Punch also provides other regulatory information to partners, such as the 'Safe Legal and Compliance Manual', which deals with Health and Safety issues, such as fire safety and environmental health legislation.<sup>16</sup>

- Award-winning<sup>17</sup> training and development, including:
  - Online training – Punch Buying Club partners can access a wide range of training resources under the banner 'Punch Progress'. This includes online videos, details of apprenticeships and information about training workshops.
  - Bespoke training – Punch Catering Development Managers (CDM) offer bespoke training for partners introducing or developing a food offer. The CDM Team help partners devise menus, an order management system or staff training, depending on their requirements. The Punch Territory Dispense Managers (TDM) can provide bespoke training for partners on cellar management, beer quality and dispense.

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<sup>13</sup> Heike Funke of Punch was named Business Development Manager of the Year and Rob Summers of Punch was awarded a Highly Commended prize at the ALMR licensed hospitality 2012 Ops Award – <http://www.almr.org.uk/presspdfs/202.pdf>

<sup>14</sup> See Appendix 2 – Letter from Greg Mulholland dated 30 October 2009.

<sup>15</sup> See Appendix 3 – Contents of the 'White Box', challenge notices, refusal books, training records etc.

<sup>16</sup> See Appendix 4 – Safe legal and compliant manual.

<sup>17</sup> National Industry Training Awards 2008 – Best Development Programme Non Managed Estate; 2009 – Social Responsibilities Award; 2010 – Social Responsibilities Award for Profit though Energy and reducing Carbon footprint.

- Investment training – The Operations Team through the PDM, CDM, TDM, Supplier Relationship Managers (providing gaming machine and entertainment support), suppliers and independent training providers, all form part of a dedicated team working with partners when investments take place. The focus is on making sure that the pub opens and continues with the highest possible retail standards. All of these roles form part of the Regional Launch Manager’s remit – which is to give anyone new to the sector, as well as existing partners, the best service possible.
- Rating service – Through its buying power and economies of scale, Punch provides a low-cost business rates appeal service – currently charged at £50 per annum. This is a direct cost and provides a full rating service from one of three, leading, professional rating service suppliers. Partners benefit from a good quality service that means they are not exposed to rogue rates operators who, for an upfront fee, promise a lot and do not deliver.<sup>18</sup>
- Marketing and promotional support – Punch offers a bespoke design and print service to the entire estate, producing items such as menus, flyers, banners, websites and much more – all at a cost plus postage. Punch produces all the necessary marketing materials to drive sales and new investment launches. PDMs use regularly updated toolkits to provide business building ideas and promotional materials to support beer festivals, finest cask and food offers, sporting events, online marketing, as well as wet products such as wines, spirits and soft drinks. Punch produces over 10,000 bespoke printed items to over 2,000 pubs each year. A newly developed online toolkit has been created to allow pubs to order printed products at a click of a button – reducing the speed to market, so that Punch pubs are maximising every marketing opportunity available to them.
- Technical services and technical support – Punch supports partners by providing a free service to manage drink distribution and cellar to bar issues. The technical service teams, together with TDMs and PDMs, provide support on beer quality, glassware and dispense. Should Punch partners experience technical problems, they can use Punch’s free technical helpline.
- Contact Centre, telesales and web-based services – Partners can contact Punch with their queries on Monday to Friday between 8am to 6pm. The distribution helpdesk is also available from 6am to 6pm. These services are available during bank holidays and close only on Christmas, Boxing and New Year’s Days. The property repairs service is available 24 hours a day, seven days a week, 365 days of the year. Partners can place online orders with the Punch Buying Club at any time. If they prefer, they can place orders over the phone with a dedicated member of the Contact Centre Sales Team.
- Discounted rates on supplies not for re-sale – Goods and services of all types and price are available to help partners in running the pub. The variety of these products is large and varies from microwave ovens to beer line cleaners, credit card processing services to waste recycling providers.

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<sup>18</sup> <http://www.morningadvertiser.co.uk/Property-News/Pubs-warned-over-rogue-business-rates-agents>

- Machine support – The machine team at Punch ensures that the latest and best products are used in Punch pubs to maximise income for partners, whilst continually searching for new income streams.

Through the strict commercial terms of the supply contracts between Punch and the suppliers, Punch partners are protected from rogue traders (see later evidence in this document).

- Free Wi-Fi – The buying power and economies of scale achieved by Punch mean that free commercially compliant Wi-Fi is available to all Punch pubs. Consumers in Punch pubs enjoy this at no cost, allowing partners to attract increased trade.
- Repairs and property support – Punch have a dedicated Property Support Team for repairs. Where the repairs are Punch's responsibility under the partnership agreement, a code of practice clearly sets out repair timescales. The Property Repairs Team deals with approximately £5m worth of repairs annually. The Investment Team has provided £120m of property investment work over the past three years. This is considered further in section 6 on pages 48-49.
- Tremendous range of beer products available – over 3,000 locally brewed cask ales are available through the Direct Distribution Scheme via SIBA (The Society of Independent Brewers). A wide range of core branded beers are also available, including 31 keg ales, 115 cask ales, 23 draught lagers, 39 bottled lagers, and 25 bottled ales. This provides the partners access to a far greater range of supply options than the free-of-tie operator.

Service that would not be available in the market place as one-off purchases include:

- Reduced rent and in-goings – By the very nature of the tied model, the rent is lower than a free-of-tie model. This aids cash flow and keeps fixed costs to a minimum. Punch also offers interest-free and low-interest ways to purchase fixtures and fittings. New entrants can also build up their deposit with Punch, which subsequently provides better credit terms.
- Credit terms – Very few suppliers, stockists or wholesalers to the pub sector provide credit terms. Subject to the terms of a partner's agreement, Punch provides one week's credit.
- Code of Practice – The Punch Code of Practice provides partners with a range of contractual benefits no matter what lease type they have been on historically. The benefits of the Code of Practice include: market rent reviews that can go up or down; lease surrender terms that allow partners to leave the pub on specific terms; clear ways of working and what partners can expect from Punch.

Punch asked an external firm of training providers<sup>19</sup> to indicate the cost to an individual tenant of the services provided as SCORFA benefits to tied tenants. The cost of these services is listed in Appendix 5. In some instances, these services were not available at all in the market for individual tenants.

The benefit of these services (not including the low rent, deposit build-ups, or low-cost finance) has been conservatively estimated at £3,000 on one-off costs and circa £3,700 per annum in additional services such as Wi-Fi, rating, and legal and compliance services. However, this is a minimum, and doesn't include multiple site visits and refurbishment costs. A more realistic estimate would be in the region of £10-12,000.

Only a pub company, through its economies of scale, can provide this benefit to tenants.

### 3.5 Risk and reward is shared

In the explanation of the wider context for the consultation and what it seeks to achieve, the consultation document states:

*"The focus has been on tied pubs and the share of reward gained by pub owning companies, for example through large unjustified rent increases."*

This is not a true statement. Punch's overall income from rent has declined (with property disposals taken out of the equation). At rent review and lease renewals, rental income is in decline because Punch operates an open market valuation policy – rent can go up or down. There has been a significant amount of rebalancing of the estate through Deeds of Variation (DoV) to reduce rents. In addition, rent support has been brought in to provide a sustainable rent for partners' businesses, as the Table 2 below shows.

**Table 2**

Downward rent adjustment	Support/Financial assistance
Like-for- like rental levels in the last three years	Reduced by . despite high levels of capital investment
DoV rebalancing in the last three years	Approximately 100 p.a. – at a cost of £'
Rent review and lease renewal	55% of the 1,200 lease renewals and rent reviews that took place in the last three years saw rents reduced and/or beer prices reduced
Financial support in the last three years	£17m p.a.

As can be seen, Punch has been sharing the risk and reward in a positive way with partners. Punch's Code of Practice clearly sets out the route for support and assistance.

<sup>19</sup> ABV training.

In a recent survey undertaken by an independent company, 91% of partners knew why the Code of Practice existed and 86% knew how to access the Code of Practice.<sup>20</sup> This clearly shows that Punch partners understand how they can seek assistance and that “large unjustified rent increases” are not part of the Punch business model.

Punch’s rental valuations and negotiations are carried out by qualified Chartered Surveyors, who follow strict guidelines of professional conduct and are regulated by the RICS.

Punch’s rent levels are at odds with the benchmarking survey carried out by the Association of Licensed Multiple Retailers (ALMR),<sup>21</sup> which indicates that rent levels for free-of-tie tenants are lower than for tied tenants. We have cross-referenced the members’ list on the ALMR website with our partner list and only five partners are members of the ALMR – representing six pubs.

### 3.6 Self-regulation is working

Self-regulation through PIRRS<sup>22</sup> and the PICA-Service<sup>23</sup> is working, with a significant number of enquiries and a small number of cases actually going through to a fully decided case. In most instances, the PIRRS or PICA-Service application is a catalyst for the parties to agree a settlement. Punch believes the sudden requirement for the consultation and a Statutory Adjudicator seems odd given the Government’s comments in November 2011:

*“These reforms will directly address the concerns identified by the Committee. Making the Code legally binding and setting up an independent arbitration service will deliver the same outcomes as the Committee’s two principal recommendations – to make the Industry Code statutory and to establish a code Adjudicator.”*

The rental assessment is completed by Chartered Surveyors at Punch. Punch would recommend this to any other pub company.

The PIRRS process is transparent and fair, because the partner chooses the independent expert. Over the past two years, 48 of the 214 enquiries to the PIRRS team related to Punch Taverns. Only three of the 48 were ever subject to a formal, independent, expert submission.<sup>24</sup>

Punch also has considerable concerns about regulatory creep. If a regulator were to be appointed, then the investigatory function – rooting out problems that may not exist – will lead to significant cost with for no substantive outcome. A cap on costs should certainly be required, so as not to burden the pub sector.

As part of Punch’s commitment to self-regulation, the Punch Code of Practice<sup>25</sup> was first written and accredited in June 2010. The Code has gone substantially further than was required by the Industry Framework Code version 4, and subsequent versions have continued in this vein. As part of the roll-

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<sup>20</sup> Survey, November-December 2012 by Great with Talent – 345 partners surveyed.

<sup>21</sup> Page 5 of the Association of Licensed Multiple Retailers Benchmarking Survey Phase 6; July 2012.

<sup>22</sup> The Pub Independent Rent Review Service received 285 enquiries over a three-year period, with 13 cases completed via an independent expert.

<sup>23</sup> The Pubs Independent Conciliation and Arbitration Service received 52 enquiries up to 22 March 2013, of which four have been to a panel hearing.

<sup>24</sup> <http://www.pirrscheme.com/images/pirrs%20annual%20report%202010%20-%202011.pdf>

<sup>25</sup> See Appendix 6 for Punch’s Code of Practice.

out, a hard copy document was provided to all partners through 2010, as well as to all staff. Punch also undertook a cultural programme within the business to embed the Code, both in letter and spirit, in all of Punch's relationships with partners and as part of process forming and contractual agreements.

Punch is very proud to be the first company to receive accreditation by BIIBAS<sup>26</sup> of the Code of Practice under version 6 of the Industry Framework Code on the 3 June 2013.

The Punch Code of Practice is provided in hard copy version to all new partners and is available on the internet for viewing by new, existing and prospective partners, as well as the wider public. We ensure all new and existing staff understand the importance of the Code and the need to comply with it. A module of the Code forms part of the industry recognised qualification being undertaken by all of the Partnership Development Managers.

The Punch Code exceeds the requirements set out in Statutory Code proposed by the Government, see Appendix 7. This demonstrates further that self-regulation has been working and continues to be a better option than state intervention.

### **3.7 Punch oppose the abuse of the tie**

There are further points on page 47 in Section 6 of this document.

Complaints to Punch have reduced significantly. Over the past 29 months, we have had 28 letters from constituency Members of Parliament. After significant investigation, only two letters raised issues that were Punch's fault. Other issues included flooding, neighbour disputes and minor licensing issues with local authorities.

The trend of executive complaints has been in decline for a number of years. On average, Punch receives one communication per week. These vary from minor delivery issues, to property issues. Each complaint goes via Punch's Partner Relationship Manager and in front of a member of the Executive Board. Punch has a clear and transparent executive complaints and escalation procedure. It is clearly referenced and easy to find within Punch's Code of Practice (on page 57).

At Punch we take any deviation from the Code of Practice very seriously. Line managers and team leaders understand the need for 100% compliance and it is closely monitored and measured. Disciplinary action is taken against employees for non-compliance with the Code of Practice.

### **3.8 Unintended consequences of Government intervention**

The Code states that it is not an attack on the tie. However there are provisions in the Code – such as a guest beer option and a mandatory free-of-tie option – which would undermine the tie and the benefits it brings.

There are significant unintended consequences of the Code; both with the transfer of value of £102m, and if the Code were also to include a mandatory free-of-tie option.

- Economies of scale – The scale of purchasing by the pub companies is significant and the discounts are in part passed to the tenants. If a mandatory free-of-tie option were to be

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<sup>26</sup> BII Benchmarking and Accreditation Services.

implemented, these discounts would be eroded, as the purchasing power of the pub company reduced. Put simply, the contractual power would move from the pub companies to the international brewers. The market price would therefore rise, as the large international brewers absorbed the value currently passed to the pub companies and tenants.

- Pub disposals – Sites that are marginal for the pub company will become unviable if the transfer of value from pub companies to tenants occurs. Punch has a disposal programme, but this will inevitably accelerate. Whilst 95% of Punch pubs are sold with a licence in place and trading as pubs, after two years only 60% remain as pubs. Without pub company support they fail, and this will lead to further pub closures.
- Reduced investment – It is wrongly assumed in the consultation document that the transfer of value from the pub companies to the tenants of £102m would see the tenant investing in the pub. As most leases are short in length and the pub company retains the repairing obligations, the tenant does not have an incentive to invest. Punch will invest or have invested nearly £40 million per annum in 2011, 2012 and 2013, and Punch is committed to investing £40m annually for the next five years. Of the pubs affected by the Government proposals, it is estimated (see Table 3 on page 49 in Section 6), that £172.7m of investment could be lost across the industry.
- The consequences of both mandatory free-of-tie and the guest beer option for the brewing industry are significant.
  - As the international brewers' presence in the market is likely to rise, there will be a significant reduction in the number of products available to tenants. The cost of producing and distributing a smaller number of large-volume products such as lager will be the most efficient way for the market.
  - A consequence of this guest beer option and a free-of-tie option would be a reduction in the number of small and medium-sized breweries, as the large volume producers squeeze the smaller suppliers out of the market.
  - There will be a catastrophic shift in the market to a few large international brewers, who will dominate the market.
  - If mandatory free-of-tie went ahead, it is more than likely that this will be part of a BIS committee and consultation in three to seven years' time – to break up the dominance of the international brewers, due to their effect on the pub sector.
- Punch through SIBA (The Society of Independent Brewers) provides a direct route to market for 494 small to medium-sized cask ale brewing companies. The proposals, especially with a free-of-tie option, would see a move by tenants to high volume lager-based products at the expense of cask ale. Free-of-tie tenants currently sell 11% of their wet product as cask ale; whereas Punch tied tenants sell 18% of their wet product as cask ale.<sup>27</sup>

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<sup>27</sup> See Appendix 8 – Based on Punch Statistics and CGA Brand Data.

- The consumer would suffer a loss in choice across the range of beer products, as small and medium-sized brewers would be reduced.

SIBA supports the retention of the beer tie and the pub company model. Pub companies provide SIBA members with a cost-effective route to market.

CAMRA promote pubs and real ale, yet the proposal as drafted, with a guest beer right that includes a high-volume internationally owned lager product, would have the effect of changing the brewing landscape of England and Wales. It would lead to the closure of a large number of small and medium-sized breweries.

- The impact on jobs if the transfer of £102m happens as a result of the Code will also be considerable:
  - 400 direct jobs with outside contractors and advisors (without including any supply chain jobs) due to the lost investment.
- The impact on jobs if mandatory free-of-tie, the guest ale provision or other parts of the Code were to be implemented are disastrous:
  - direct jobs lost through pub closures.
  - 270 direct jobs lost due to the loss of flow monitoring contracts with Vianet.
  - 
  - Circa 100 jobs with legal and professional advisors.

The total number of direct jobs with external contractors and suppliers, for Punch alone, has been estimated at 415 (see footnote 57 on page 49)

A further unintended consequence of the Code as drafted would be that tenants at the lower end of the earning spectrum would only be fractionally better off. The winners would be tenants earning at the higher end of the earning levels.

### 3.9 Abolition of the gaming machine tie = unintended deregulation = increase in crime

Previous Governments recognised that there was a concern regarding rogue operators in the gaming machine sector. Removing the tie would encourage the spread of criminal behaviour by unscrupulous suppliers of gaming machines. It might also mean Category C gaming machines being set up in pubs where there is a lack of proper knowledge about the regulations around control and taxation.

The current system, discussed on page 45 in Section 6 of this document, ensures that gaming machines are well regulated through rigorous supply contracts that are properly monitored and

maintained. Abolition of the machine tie would lead to a reduction in revenue to the Exchequer, because it would amount effectively to deregulation.

Tenants of companies with fewer than 500 pubs would still be able to take up a tied machine offer, leading to disparity of competition in the pub machine sector. Companies with fewer than 500 pubs would have better quality machines because they would be tied.

### 3.10 **Bad for jobs and bad for business**

- The Code as suggested would have a severe deregulatory effect, as the commercial contracts provide a framework for good practice. The consequences of a free-of-tie estate would be:
  - an increase in crime from the loss of the machine tie, and
  - a loss in revenue to the Exchequer through non-payment of the duty on wet products – because it is likely that illegally sourced alcohol would be sourced from non-duty paid suppliers.
- The pub company and the tenant are aligned in their goals, to make the consumer and retail experience the best it can be.
- Tied tenants are better off than free-of-tie tenants and have seen less exposure to the recession than other sectors – despite the fact that the smoking ban, supermarket pricing and increasing regulation around licensing, have taken their toll of the sector.
- Punch opposes the abuse of the tie. Successful tied tenants provide successful pub companies.
- A catastrophic reduction in investment within the sector. The Code as proposed by the Government would pass an average of £4,000 to each tenant from the pub company. A tenant cannot complete a large-scale investment with £4,000. The pub company has capacity to target large-scale investments.

All of the above 'Bad for jobs and bad for business' points will be considered in Section 6.

## Section 4 – Structure and tone of the consultation document and questionnaire

### 4.1 Introduction

The consultation should be looking at whether intervention is required, not how it is to be implemented.

Punch is concerned that the consultation document refers to the tie as having a number of positive effects, but then goes on to try and remove it by stealth through the mandatory free-of-tie and guest beer option.

### 4.2 Overall structure and bias

Punch also has a number of concerns with the structure of the consultation.

- There is no basis for intervention, as there is no clear detriment to public interest.
- Yet BIS appears already to have decided that:
  - there is a need for a Code and Adjudicator, and
  - there should be a transfer of value from the pub company to the tenant of £102m.
- Punch has received a number of consistent communications from Members of Parliament indicating that ‘the decision is made’ and, most disturbingly, from the Deputy Prime Minister, who uses the words “unscrupulous pubcos”.<sup>28</sup>
- Furthermore, the Secretary of State’s website specifically states: “I support the Fair Pint Campaign, which is pushing for legislation for leased pubs to be released from their tie.” And “the system of tied pubs goes completely against the idea of competitive markets”.<sup>29</sup> This directly conflicts with the OFT findings.

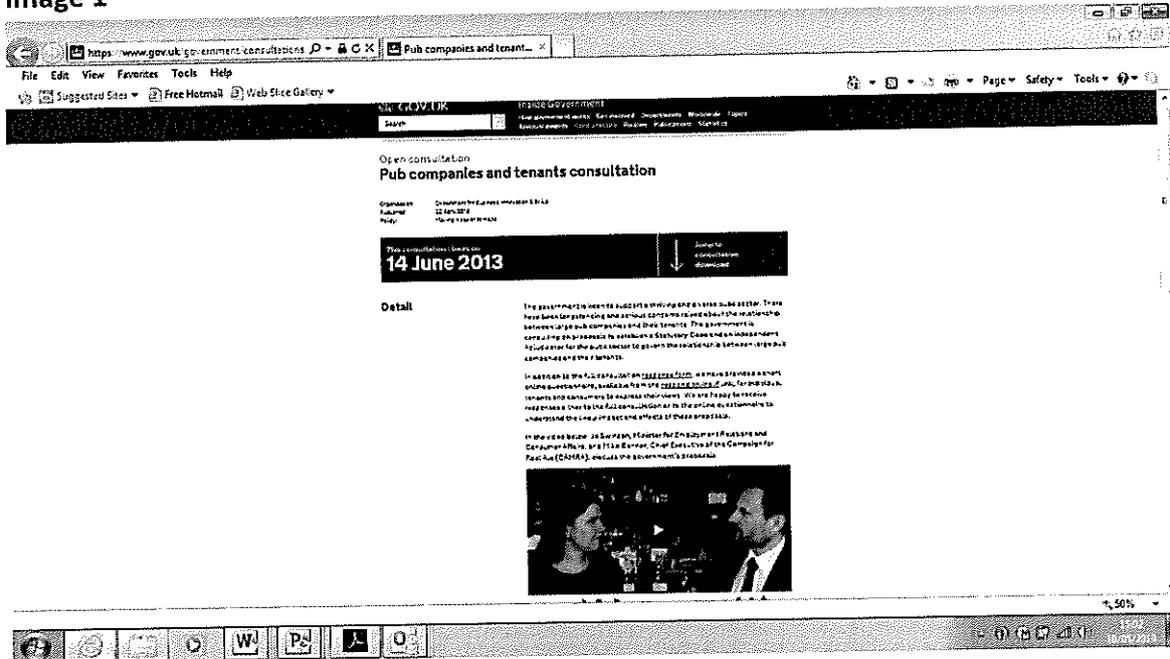
The prejudice of ministers is further evident in a number of communications, which are publicly available as part of the consultation. It is inappropriate to have Jo Swinson the Minister for Employment Relations and Consumer Affairs being interviewed by Mike Benner the Chief Executive of the Campaign for Real Ale on the Government web page for the BIS consultation, where members of the public can answer the questionnaire (see next page):

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<sup>28</sup> See Appendix 9 – Correspondence from Members of Parliament.

<sup>29</sup> <http://vincentcable.org.uk/en/article/2008/082264/vincent-cable-backs-local-pubs-in-fair-pint-campaign>

Image 1



Mike Benner and CAMRA are running a campaign during this consultation and on the CAMRA website it states:

*“CAMRA is campaigning for a rebalance to the current unfair relationship between the giant property companies (pubcos) and their licensees. This rebalance must include an option for lessees to become free of tie, accompanied by an open market rent review, so that they can buy beer on the open market potentially saving each pub business tens of thousands a year. Those who remain tied should be given the opportunity to buy one real ale as a guest beer outside of any beer tie.”*

This leads any respondent, before reading the consultation or answering questions, to an immediately biased view that prejudices any outcome.

#### 4.3 Biased questionnaire

The consultation questionnaire responses are likely to be biased. Punch has a number of concerns with the way this is structured. The preamble is very negative, referring to tenant exploitation. It appears to rely solely on an IPPR survey of just 500 pubs, conducted in August 2011, that is of limited use. This is acknowledged by BIS in the impact assessment, where it states:

*“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. The results suggest that tied licences 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 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.”*

Many of the questions are leading questions.

The Government states its view and then asks those consulted whether they agree. There is no attempt to gauge whether or not self-regulation is working. For example, Question 2 of the online questionnaire simply asserts: "Self-regulation has been tried since 2004, but has not worked – too many tenants are still being treated badly and facing hardship." Those consulted are simply asked whether they support the various proposed initiatives. If you are a tenant being consulted *prima facie* and the result is a transfer of value in your favour, you will simply agree. Who wouldn't?

Punch believes the questions within the consultation document are not balanced in their approach. In a recent edition of *The Publican's Morning Advertiser*, an editorial<sup>30</sup> stated:

*"... in particular the online survey has not been drafted in a neutral manner, and that it asks rather leading questions that prejudice answers." .. and .. "Additionally, nowhere does the survey give satisfied tenants the option to say 'I am happy with my relationship with my current landlord'. The survey's conclusions will be weaker for this apparently partial approach and key omission."*

The questionnaire process is in breach of Para B14<sup>31</sup> of the Market Research Society Code of Conduct, which is designed to reassure the general public and other interested parties that research is carried out in a professional and ethical manner.

B14 reads:

*"Members must take reasonable steps to ensure:*

- That the Data collection process is fit for purpose and clients have been advised accordingly;*
- That respondents are not led towards a particular point of view;*
- That responses are capable of being interpreted in an unambiguous way;*
- That Respondents are able to provide information in a way that reflects the view they want to express, including do not know/prefer not to say where appropriate."*

Some of the consultation questions are Barnum statements.<sup>32</sup> For example:

*"The Government believes the best way of achieving this would be to introduce a Statutory Code, to set down the rules which pub companies would have to obey, and an independent Adjudicator to enforce and referee the Code.*

*Do you agree that a Statutory Code and independent Adjudicator would be an appropriate way of tackling this problem? Yes/No"*

The framing of this question is such that anyone is simply going to say "Yes". It is unlikely ever to illicit a "No". Very little can be done with some of the 'data' gathered, as it consists of little more than platitudes.

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<sup>30</sup>*Publican's Morning Advertiser*, 9 May 2013, p3.

<sup>31</sup> <http://www.mrs.org.uk/pdf/2012-02-23%20Regulations%20for%20Non%20Research%20Purposes.pdf>

<sup>32</sup> The effect of a Barnum statement is that it can provide a partial explanation for the widespread acceptance of some beliefs and practices – or it can give half an explanation in the hope of eliciting a specific, full and misrepresentative answer.

It is also of note that the questionnaire uses the website SurveyMonkey. This seems to indicate that it was produced in a rushed manner, without due diligence.

#### 4.4 Inaccuracies

'Complaints' numbers from the BII Hotline<sup>33</sup> – reported on page 18 and Figure 1 in the consultation document – are or were inaccurate. The whole argument and rationale for consultation seems to be predicated on these numbers – including the 500-pub threshold for application of the Code. However, these were 'calls' not 'complaints'. The numbers were wrong and misrepresented, and whilst BIS has now publicly commented upon them,<sup>34</sup> it failed to make any amendments to the consultation document for over a week, during which responses were still being invited. References to complaints still remained in the consultation document<sup>35</sup> throughout the entire consultation period, and the inference in all of this text was that the complaints are all directed against the big pub companies. The consultation document has clearly stated throughout that: "In choosing the figure of 500 pubs, the Government has been mindful of the fact that significantly fewer complaints have been made about companies below this level" and it further states: "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." Both of these statements are inaccurate and misleading.

Punch provides membership of the BII to 'new' partners and actively encourages partners to seek independent business advice during their agreements. It comes as no surprise that the number of calls is significant given the size of the Punch estate – this should be actively encouraged. To put these numbers into context, since 2009 the BII Hotline has received over 700 calls, of which 189 were from Punch partners. Only three of these calls have been recorded as a 'grievance' against Punch. This represents 0.4% of all calls, or 1.6% of 'Punch' calls.<sup>36</sup> None of these grievances were referred to Punch from the BII, so it can only be assumed that they were trivial.

In his foreword, the Secretary of State suggests: "At present, 18 pubs (net) are closing every week. Whilst the financial crisis has brought into stark relief the slow process of sectoral decline, it is undoubtedly the case that the activities of the major pub companies, with their highly leveraged business model, have intensified the crisis." Contrast the position in the Impact Assessment:

*"The decline [in pub numbers] 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.*

*"Some campaigners argue the tie plays a factor, but pub numbers do not support this. Figures from the latest CGA Study commissioned by CAMRA show that between March 2010 and September 2012 the closure rate was lower in tied pubs, 4.3%, than in free of tie pubs, 4.5%"*

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<sup>33</sup> BII Hotline refers to the 'Licensee Business Support Helpline' run by the BII.

<sup>34</sup> 'Statutory code: BII clarifies 'misinterpreted data' in consultation paper.  
[http://www.morningadvertiser.co.uk/General-News/Statutory-code-BII-clarifies-misinterpreted-data-in-consultation-paper?utm\\_source=copyright&utm\\_medium=OnSite&utm\\_campaign=copyright](http://www.morningadvertiser.co.uk/General-News/Statutory-code-BII-clarifies-misinterpreted-data-in-consultation-paper?utm_source=copyright&utm_medium=OnSite&utm_campaign=copyright)

<sup>35</sup> See paragraph 3.3, 4.11 and 4.12 in the Consultation Document.

<sup>36</sup> See Appendix 10 – Punch Statistics from the BII.

#### 4.5 Unsubstantiated statements

There are a number of unsubstantiated statements within the consultation document that Punch would disagree with. The language of the document is emotive, with nothing to suggest that this arrives at proportionate regulation.

##### 4.5.1 Evidence of 10 cases per week

The document at 3.3 states:

*“There are also several other people (usually current or former tied tenants) who act independently and estimate they receive over 10 cases a week that directly relate to the ‘Pubco model.’”*

There is no clear evidence to support this claim. It is a biased statement, based on unsubstantiated estimates, from sources that have a vested interest in trying to illicit as much work and fees from tenants as possible. It is also not clear what “relating to the ‘Pubco model’” means, if, as the results of the BII hotline show, queries are about a rent review or wanting business advice.

##### 4.5.2 Potential sales figures are provided by professionals

The document at 3.4 refers to types of unfair behaviour that have been reported to the Government about pub companies and refers to “misleading estimates of potential sales”. Punch use Chartered Surveyors to provide a sales estimate of the Reasonably Efficient Operator as set out in the RICS guidance.<sup>37</sup> At no point is a tenant misled. Some tenants do better than our estimate and in some cases the tenants do not achieve these estimates. This can be for a number of different reasons, including circumstances outside the control of the pub company, such as recession, divorce, death, illness and separation.

##### 4.5.3 Drinks prices increase in line with suppliers

The consultation document also refers to a “significant increase” in drinks prices. This is without any foundation and the OFT response to the CAMRA super-complaint found there was no significant increase in drinks prices. It stated:

*“We consider that in the context of this sector, where an individual pub company generally faces significant competition from other pub operators in the downstream retail market and where the characteristics of the market do not offer conditions in which coordination between the large pub companies is likely to be sustainable, pub companies will not be in a position to sustainably inflate prices charged to lessees above a competitive level.*

*“If pub companies do not ensure that their lessees are well placed to provide a competitive offer to customers, those pubs risk losing custom to other tied, free house and managed pubs in their locality. For these reasons, we do not consider that it would be sustainable for pub*

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<sup>37</sup> Royal Institution of Chartered Surveyors (RICS) Practice Standards UK; *The capital and rental valuation of public houses, bars, restaurants and nightclubs in England and Wales* 1<sup>st</sup> Edition, guidance note. An example of the Punch valuation template can be found in Appendix 11.

*companies to set prices and rents at a level that would compromise the competitive position of pubs within their estate... to that extent, pub companies' commercial interests would appear to be aligned with the interests of their lessees', and it would not appear to be profitable for pub companies to inflate the beer prices and rents charged to their lessees to a level that would undermine their lessees' ability to compete effectively."*

Punch changes its drinks price list annually, in line with suppliers' increases. Table 3 below shows the price increases over the last 4 years, Punch has consistently absorbed some of the costs price rises to help partners profit margins.

**Table 3**

Year	Average Brand Owner WSP Inc. (%)	Average Punch PPP Inc. (%)
2013	3.0%	3.0%
2012	3.7%	3.4%
2011	3.3%	3.3%
2010	2.9%	1.1%

This is dealt with further in the answer to question 8.i on page 37.

#### **4.6 Partners are literate and numerate; and trained**

The consultation document seems to indicate that there are low levels of literacy and numeracy, citing an article in the *Publican's Morning Advertiser* from 22 June 2009. This article has been taken out of context, as it refers to managed houses and the plans put in place for apprenticeships. It does not refer to the leased or tenanted sector. This is misleading.

All new partners produce a business plan prior to making any Punch agreement. The plan is analysed to check whether the partner can make a profit, marketing plans are made, and online platforms are set up for the partner's business. To manage all of this requires a relatively high level of literacy and numeracy. Punch will not provide a new agreement to a partner unless they have demonstrated that they have received advice from both a solicitor and an accountant.

Partners are also required to undertake training to ensure they are ready to begin trading.<sup>38</sup> In 2012, 605 delegates, representing 362<sup>39</sup> pubs, attended Punch's Foundation Week training course. Punch has run 12, yearly, roadshows across the country, where partners can receive advice on a wealth of issues from food preparation and drink dispense through to advice on business rates.

#### **4.7 Application of the Code to those owning 500 or more pubs**

Punch is concerned about the proposal that the Code will only apply to pub companies with 500 or more pubs. This is an arbitrary number, based on a number of biased sources. The rationale from Government for this number is that pub companies with more than 500 pubs can afford the cost of

<sup>38</sup> Ready for Business Foundation Week.

<sup>39</sup> This represents 79% of all new entrants –21% signed a waiver as part of the Industry Framework Code.

compliance. This cost would ultimately be a cost to business; adding to the regulatory burden on this part of the pub sector and undermining competitiveness.

The evidence relied upon by the Government for the 500-pub threshold for application of the Code is the number of enquiries to the BII Hotline. This has already been shown to be misleading and inaccurate. Nevertheless, relying on this evidence that there are fewer complaints made to the BII Hotline about pub companies below the 500 limit, the consultation document concludes that "it is reasonable to consider that the relevant proportion of complaints reflects the industry as a whole". There is no reference to either the validity or quality of complaints or calls. The larger pub companies provide free BII membership for the first year and by virtue of this provides access to quality advice through the BII Hotline. This would explain the larger number of calls.

Punch believes the 500-pub threshold for application of the Code looks like a convenient way for Government to exclude family and smaller regional brewers from the code.

The Groceries Code Adjudicator (GCA) is referenced within the consultation document to support the 500 threshold. The position adopted for the GCA used a turnover threshold. The concern which saw the creation of the GCA was with excessive buyer power and there is a clear link from turnover to buying power. However, there is no such correlation with pub companies and their tenants. Just because a pub company is large does not mean that it treats tenants in a worse manner.

There are also issues regarding boundaries into Scotland, as the Code only applies to England and Wales. So if a pub company owns 430 pubs in England and Wales, and owns 100 in Scotland, does it fall under the Code or not?

#### 4.8 Legality of the Code

As drafted, the proposed Code would be in breach of Article 1, Protocol 1 of the European Convention of Human Rights (A1P1).

By depriving pub companies of future income, the proposals would clearly constitute the exercise by the State of 'control' over Punch's possessions (and those of other pub companies). There are clear and serious adverse consequences for Punch and the other relevant pub companies.

Such interference could only be justified under A1P1, where it is necessary in the public interest.

As set out above, however, there is no real evidence of a detriment to the public interest (either in terms of a failure of self-regulation or an imbalance in the risk and reward between large pub companies and their tenants) requiring intervention. No attempt is made to analyse whether there is in fact an imbalance. If indeed there was ever a mischief, then this has been rectified by both cultural changes and the movement of the market. The consultation document fails to identify actual detriment and seeks to rely largely on anecdotal evidence of a few dissatisfied tenants and self-appointed representative groups.

Punch clearly reserves the right to challenge any legislation in due course.

## Section 5 – Questionnaire answers

### Q1. Should there be a Statutory Code?

No: Punch does not accept the need for one.

BIS has concluded that self-regulation is not working. There is no evidence to support this and it is at odds with the Government's own comments in November 2011:

*"These reforms will directly address the concerns identified by the Committee. Making the Code legally binding and setting up an independent arbitration service will deliver the same outcomes as the Committee's two principal recommendations – to make the Industry Code statutory and to establish a code Adjudicator."*

It is also not clear how a Statutory Code would rectify the current self-regulatory approach. If there is an issue, a solution is to inform tenants of their rights, not to impose a new cost on the industry.

Self-regulation, although slow to come to fruition, has not had the chance to be fully tested. However, there have been 214 enquiries to the PIRRS team over the past two years, of which 48 related to Punch. Only three of the 48 were ever subject to a formal independent expert submission.<sup>40</sup> The PICA-Service received 52 enquiries up to 22 March 2013, of which four have been to a panel hearing. These numbers show that the system is working.

No other sector of the commercial property market provides:

*".. an accessible, independent, low cost dispute resolution service to the licensed industry. Capped fees enable tenants/lessees and Pub Companies/Breweries to resolve disputes in a fair and timely manner."<sup>41</sup>*

The quality and diverse backgrounds of the panels of both PIRRS and the PICA-Service ensure that there are no conflicts of interest. In the case of PICA-Service, they include well-regarded participants from represented trade bodies, as well as Judge Trevor Barber. The self-regulatory system has identified that although tenants are aware of the systems in place to deal with disputes, there has been little take up.

The Punch partner survey in November 2012 showed that 91% of Punch Partners knew the Code of Practice existed, 86% knew how to access the code of practice and 79% believed that Punch complied with the code of practice.

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<sup>40</sup> <http://www.pirrscheme.com/images/pirrs%20annual%20report%202010%20-%202011.pdf>

<sup>41</sup> <http://www.picaservice.com/>

***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 any supporting evidence.***

No: The threshold of 500 pubs is arbitrary. The Code should apply to pub companies that can afford the additional cost of administering this, rather than be targeted against six companies. Inevitably, this distorts the market for those above or below the 500 limit. The best evidence of an arbitrary number within an industry leading to distortions in the market is within the pub trade itself – following The Supply of Beer (Tied Estate) Order 1989 and its subsequent repeal in 2002.

The Groceries Code Adjudicator (GCA) is referenced within the consultation document to support the 500 threshold. The position adopted for the GCA used a turnover threshold. The concern that led to the creation of the GCA was with excessive buyer power – and there is a clear link from turnover to buying power. However, there is no such correlation with pub companies and their tenants. Just because a pub company is larger bears no relation to how it treats its tenants.

***Q3. 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?***

Yes: The Code if implemented should include all leased and tenanted pubs owned by the company.

***Q4. How do you consider that franchises should be treated under the Code?***

Franchises should not be part of the Code.

Licensed trade franchises in most instances do not expose franchisees to stock or property costs and the risk is not with the franchisee but the pub company.

The distinction should be determined by accreditation with the British Franchise Association (BFA). If the BFA is prepared to accept the agreement as a franchise, then the Code should not apply to that agreement.

***Q5. What is your assessment of the likely costs and benefits of those proposals on pubs and the pubs sector? Please include supporting evidence.***

The cost to the pub sector is highlighted and is highlighted throughout the Punch submission.

The cost to the pub sector will be a fundamental shift in the market; away from investment in pubs and into the profits of international brewers. The cost for jobs and business in the UK will be catastrophic.

In Punch's opinion, the cost of the Adjudicator has been severely underestimated. It is indicated within the consultation document that where a pub becomes non-viable for a pub company, a negotiation will occur between the pub company and tenant to ensure it remains viable. This will potentially lead to an influx of cases, let alone the potential of circa 3,000 rent reviews and lease renewals per annum across those pub companies affected.

There are also considerable concerns about regulatory creep. If a regulator were to be appointed, then the investigatory function – checking out problems that may not exist – will lead to significant cost with for no substantive outcome.

**Q6. What are your views on the future of self-regulation within the industry?**

Self-regulation is working and should stay. In the event of a Code being implemented, then it should apply to all. Two systems should not be run in parallel, as this would be a dual cost to the pub sector.

**Q7. Do you agree that the Code should be based on the following two core and overarching principles?**

**i. Principle of Fair and Lawful Dealing**

There is no need for this provision as it is unclear and without a basis in fact.

The inference from this question is that the pub companies have been doing something unlawful. There is no evidence of this in the consultation document, so why is the 'lawful' element included? Can BIS show that pub companies have acted unlawfully?

It is also unclear from the question whether all breaches of agreements are included within the Adjudicator's power; for example, a dispute over dilapidations.

This open-ended principle will lead to additional requirements to those set out in the Code. It will be open for the Adjudicator to find other behaviour that is not 'fair'. There is no clear definition of what 'fair' dealing actually means.

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

This is very difficult to do in practice, based on the tenant's appetite for risk in different business environments.

More in respect of this proposal is set out in the answer to question 8.ii below.

**Q8. 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; Yes: Please see below.**

**if the pub company significantly increases drink prices** No: Please see below.

**or if an event occurs outside the tenant's control.** No: Please see below.

- Punch agrees that a rent review or renewal should happen every five years. The current leases from Punch offer a tenant-only rent review. The tenant can call for a rent review if they believe the rent will go down. However Punch cannot call for the rent review if they believe the rent could go up.
- Punch does not significantly increase drinks prices and only passes on price rises from suppliers. There is therefore no need for a rent review in the case of a drinks price rise. It is also difficult to define 'significant'. If Punch merely passes on price rises and the brewer raises the price, the consequence of a rent review is disproportionate. At Punch there are only annual price increases, and outlined below are the dates of the price increases for the last five years:

30 March 2009, 10 April 2010, 21 February 2011, 20 February 2012 and 18 February 2013.

- Punch disagrees that a tenant should have an opportunity to call a rent review at any time, subject to an 'outside event'. This is similar to the material change in circumstances under which a rating appeal can be made. However a rating appeal can only be made in the event of a 'physical' change and not an 'economic' one. The consultation document does not draw the same distinction.

It is also a significant departure from a standard institutional lease and risks completely removing public houses from the investment arena. Investors are not going to accept such uncertainty of income. How could a value be placed on interest where the income streams could change at any time?

***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.***

Yes: Subject to the issues below.

In a practical scenario, the overarching principle of comparing a single pub on a free-of-tie basis and on a tied basis, as set out in the example in Annex A of the Code, is at best flawed and at worst impossible for a single property pub valuation. The principle of valuation should be about evidence of comparable market transactions, not a statement taken out of context and developed by a tenant's advisor – i.e. that the tied tenant should be not worse off than the free-of-tie tenant, or that the free-of-tie tenant should be no worse off than the tied tenant.

There is a conflict between the RICS guidance and the Proposed Statutory Code. As can be seen from section 7.21 and 7.22, 'Comparability' between leases on different terms is problematic.

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

No: The regulatory nature of the tie is better from a tenant, machine owner and Exchequer point of view. Machines are controlled. (See pages 44-46 for further supporting information.) Removing the machine would lead to an increase in criminal behaviour as can be seen from the recent case which saw Spelthorne Council successfully prosecuted a criminal offence under the Gambling Act 2005.

Removing the tie would not give the result intended by the 2004 Select Committee, as stated in the consultation document: "pubcos do not add sufficient extra value from their deals to justify their claims to 50% of the takings". At Punch we can justify the support we provide as we promote the best machine options available to our partners.

The machine tie also aligns the share of risk, costs and reward between the pub company and tenant as machine income is shared.

The Government should leave the tie alone. To suggest no other products should be tied is nonsensical and would be at odds with other sectors in the economy, such as franchising. McDonalds ties its franchisees to burgers, bread and every other item. Costa Coffee ties its

franchisees to products other than coffee, for example, to cakes, pastries and paninis. Is this seen as unjust?

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

No: Punch is against the Guest Beer option, and believes this is directed at trying to improve cask ale volumes to appease CAMRA. The unintended consequence would be passing a mass market internationally brewed lager straight through to the consumer. The tenant would remove the cask ale as the 'guest beer' and promote the highest-volume product – that is, lager. This would be detrimental to both small and medium-sized local cask ale brewers. The loss of jobs in UK brewing would be significant.

Punch has a Guest Cask Ale option within some of its new agreements, based on local cask ales. This promotes SIBA products through the Direct Distribution Scheme (DDS). DDS has provided a direct route to market for small brewers and supports a now-vibrant independent UK brewing sector.

The unintended consequences of the Guest Beer option should not be underestimated as anything other than catastrophic.

Potentially there would be an increase in free-of-trade loans from large multi-national brewers. The international brewers will seek exclusivity for their products through pubs and will incentive tenants by offering loans agreements. The loan agreement will be conditional on a supply arrangement.

***v. Provide that flow monitoring equipment may not be used to determine whether a tenant is complying with purchasing obligations, No.***

***or as evidence in enforcing such obligations. No.***

Punch agrees that flow monitoring must not be relied upon as the sole basis for checking for buying out. However, alongside other evidence, it can be relied upon as evidence in enforcing such obligations.

The question shows a lack of knowledge of the legal system in seeking damages for the breach of the contractual position. The equipment in itself does not 'determine' whether the tenant is complying with their contractual agreement. Ultimately, it is the court that 'determines' the outcome, or a negotiated settlement to determine the damages.

A similar system of monitoring is found in other industries and activities such as Tachographs in commercial vehicles. Therefore, this is a proposal that refuses to acknowledge the assistance that can be provided by technological advancement. The system has proved to be reliable and, where the flow monitoring system is challenged, a Punch partner can ask for the system to be calibrated.

The consultation document as drafted (point 30 on page 49) would result in significant job losses in Stockton-on-Tees at Vianet plc (formerly Brulines). Vianet plc is a technology-based company, employing approximately 270 people, that is beginning to export its product.

***Q9. Are there any areas where you consider the draft Statutory Code (at Annex A) should be altered?***

Yes: Punch has dealt with a number of the issues raised by the proposed Code in answer to the questions above.

The provision, language and structure of the Statutory Code do not work in practice.

For example:

Part 1, on page 41 'Objective of the Code', refers to Fair and Lawful dealing as "without distinction between formal or informal arrangements". This will lead to confusion from a pub company and lessee point of view, what is fair under one agreement maybe unfair under another and provides an onerous provision for example on a Tenancy at Will where no notice period is required.

Part 2, on page 42 'Pre-Contractual Negotiations' 6a(ii), refers to the term 'Qualification Curriculum Authority', but there is no definition of this term.

Part 2, on page 42 'Pre-Contractual Negotiations' 6c, refers to advising the tenant to consult RICS guidance. The RICS guidance on page 1 indicates: "This is a guidance note. It provides advice to RICS members on aspects of their profession" and goes on to say at 1.6 on page 2: "The valuer needs to be actively involved in the market for this class of property, as a practical knowledge of the trading aspects of a trade related property is fundamental to the analysis of the property's existing operation and trading potential". Is BIS expecting every new tenant to have the knowledge of a professional and for the pub company to check this?

As indicated above, the Statutory Code as drafted in Annex A is poorly thought-out and leaves a number of areas open to interpretation, which would lead to uncertainty for pub companies and tenants.

As Punch support self-regulation, we would make the following observations in comparison to the current IFC:

- In general there is no distinction made between leases and tenancies in the Statutory Code as compared to the IFC version 6. Tenants of short-term agreements, which in some instances have a very short notice period, will be covered by the Statutory Code and will be subject to the same obligations as long-term lessees which is currently not the case.
- Definitions in the introduction to the Code:
  - 'Tenant' – Tenant is explained here as meaning the person to whom the pub is assigned as either a lease or a tenancy (irrespective of which type of agreement). Yet the Code itself (notably Part 6 – Miscellaneous Provisions) does refer to separate 'lease' and 'tenancy' agreements, which is inconsistent and confusing;
  - 'Pub' – Attempting to define a 'pub' is always a difficult task and defining it within legislation such as this could lead to unintended consequences. The definition set out in the Code could exempt food-led, non-managed pubs, or indeed include premises which

otherwise could be classed as 'restaurants' – if they have a high level of food turnover and no specific licensing conditions relating to consuming food at the premises.

- Part 1 of the Code introduces the two principles that all subsequent provisions should be subject to, namely:
  - Tenants should be treated fairly and lawfully; and
  - Tied Tenants should be no worse off than free-of-tie Tenants.

This is over and beyond any specific principles set out in the IFC. Please see answer to Q7 above.

- Part 3 – rent assessment statements: It is not clear throughout this section as to the difference between an initial rent assessment provided to a tenant going into a new pub and existing tenant rent reviews. This will lead to confusion.
- Part 4 of the Code contains the majority of the new obligations on pub companies. We have commented on these in earlier answers and within this submission:
  - Section 20 – no other products other than drinks may be tied;
  - Sections 22 – 24 regarding calculation of rent in relation to FoT leases and SCORFA;
  - Section 27 – guest beer option;
  - Section 30 – flow monitoring. This is a significant departure from the IFC as it does not allow flow monitoring evidence to be used in any way to determine whether a tenant is complying with purchasing obligations, whereas in the IFC it could be used in conjunction with other evidence.
- Part 5 of the Code contains a number of obligations that are not included in the IFC regarding PDM (BRM) training etc.
- Part 6 – Miscellaneous provisions
  - Section 33: New obligations here include incorporation of the Code by the next rent review. There is inconsistency here regarding the definition of 'rent assessment' to cover both reviews and initial assessments for new tenants;
  - Section 37: More onerous obligations for tenants and pub companies regarding 'keeping' or 'putting' the pub in good order as there are different requirements for leases and tenancies. This will cause problems if they have to be adopted by traditional tenancies. In most instances, there is no Schedule of Condition as assumed in this section. Often the clauses are open to interpretation in the tenant's favour. This section would remove this advantage and pass an onerous obligation to tenants.
- Part 7 – Pub company codes of practice: does not require those subject to the Code to produce a separate IFC compliant code, which will lead to two system requirements for those pub companies involved.

- Parts 8 and 9 deal with the Statutory Adjudicator and related dispute resolution and so are above and beyond anything within IFC version 6.
- Annex A – rent assessment statements – this differs from the IFC as it includes a hypothetical FoT option as comparator. See the answer to question 8.ii above.

***Q10. 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?***

No: The uncertainty of any review of a Statutory Code would cause uncertainty in the pub sector and delay investment decisions by companies that might be affected. The reliability of evidence required to review any Statutory Code would need to be robust. As can be seen from the weak evidence in the consultation document, this would need greater scrutiny. The timing of any review would also be critical, as any changes would need to be given time to work. Again, this is similar to the current position in that self-regulation has not been given adequate time.

***Q11. Should the Government include a mandatory free-of-tie option in the Statutory Code?***

No: This is bad for jobs and bad for business. These points have already been raised in this document.

The effect would be a wholesale shift in the pub market away from pubs and investment. The economies of scale that pub companies gain and then invest in pubs would be lost; the profit would go to the large international brewers. The void created by this loss of investment would not be filled by the banks and other lending institutions with their strict lending criteria.

At a meeting with BIS on Friday 19 April 2013, Punch specifically asked \_\_\_\_\_, Assistant Director in Competition Policy at BIS, ahead of the consultation: “You’re not simply going to ask – Would you prefer to go free of tie?” \_\_\_\_\_ gave the assurance that this would not happen. Question 11 effectively asks this question; although with the caveat of a rent increase in the online survey.

Punch also believes there could be a conflict with the European Convention of Human Rights, please see page 35 of this document.

BBPA instructed Compass Lexicon to undertake an independent study into the potential consequences of the current BIS proposals and particularly the impact of the mandatory free-of-tie option.

Compass Lexecon is one of the world’s leading economic consulting firms. It provides expert economic advice on competition policy, economic and financial regulation, public policy and the assessment of damages in complex disputes.

Compass Lexecon modelled pub-level data from \_\_\_\_\_ pubs provided by BBPA members who would be impacted by the proposals (i.e. who operate over 500 pubs). The findings were then scaled up to cover the total \_\_\_\_\_ pubs covered by BIS proposals. The full report and detailed methodology has been provided to BIS.

The key findings are as follows:

- If all licensees exercised the mandatory free-of-tie option, this would lead to a further  $\pm$  pub closures. From employment numbers provided to the study by tenants this would lead to the loss of  $\pm$  direct jobs. Almost half of these jobs would be among 18-24 year olds.
- The loss of economic value generated by the sector equates to  $\pm$
- A further  $\pm$  indirect jobs in the pub supply chain would also be lost.
- Pub companies invest an average £8-10,000 per pub per annum across the sector. Their incentive to continue with this programme would be greatly reduced.
- Under a commercial lease, payment for fixtures and fittings are paid up front and rent is paid quarterly in advance. These changes would contribute to an increase in licensee in-goings from just £12,500 on average to almost £46,000 on the pubs modelled.
- The net effect of these latter two points is almost certainly to further accelerate pub closures and job losses, as many licensees are likely to be unable to generate additional borrowing and investment required from banks and elsewhere.
- Tenanted/leased pubs stock more cask ales than independent free houses and sell more cask ale as a proportion of their total beer sales. There will be a reduction in cask ales available to consumers and a resultant drop in sales. We have not modelled the impact on British cask ale brewing.

***Q12. Other than (a) a mandatory free-of-tie 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 the tied tenants were no worse off than free-of-tie tenants?***

No: Tenants are already compensated with lower rents for higher beer prices via the profit and loss based rent assessment. There is no need for any change.

The RICS guidance provides a sufficient basis for allowing the tenant to achieve the correct rent, whether that is the 'wet' rent or the 'dry' rent, at any given rent event or letting.

***Q13. Should the Government appoint an independent Adjudicator to enforce the new Statutory Code?***

No: self-regulation is working.

The current case load by both PIRRS and PICA Service is relatively small; why are tenants likely to use an Adjudicator compared to those already in place?

The quality and awareness of the self-regulatory system is high, and the cost is low. There is no need for a further system which could compromise the current system by spreading the case loads even further.

***Q14. Do you agree that the Adjudicator should be able to:***

- ii. Arbitrate individual disputes?***

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

No: There is no need for an Adjudicator to arbitrate individual rent disputes. There are already two systems in place and a third would simply add further complexity. The two systems in place allow for the following:

- low-cost award, with no reasoning (PIRRS)
- higher-cost award, with reasons and potentially costs award (dispute resolution clause within the agreement).

If there is to be an Adjudicator, then they should only be looking at breaches of the Code for behaviour. However, self-regulation is working and investigations into pub company behaviour are already working.

Further, if there is to be an Adjudicator they will need provisions to deal with frivolous or vexatious claims and if the claim is shown to be either then the Adjudicator must impose the cost on the complainant. This is not the case currently envisaged by the consultation.

**Q15. 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?**

No: It is unclear what the financial penalty would be and the Groceries Code provisions brought in recently still remain unclear on this point.

If there is to be an Adjudicator, there is no reference to an appeal process. There should be one.

There should be a cap on the Adjudicator's budget to ensure this is an efficient system.

**Q16. Do you consider the Government's proposals for reporting and review of the Adjudicator are satisfactory?**

Yes, if there is to be a code. However, the answer to Q10 above should be noted regarding uncertainty, reliability of evidence and timing.

**Q17. 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?**

No: Funding would be directed away from current trade bodies. The funding for the BII and the BBPA trade bodies would be reduced and their effectiveness would be diminished.

Punch is also concerned about the regulatory creep of the Adjudicator, with expanding staff numbers and activities beyond its remit.

## Section 6 – Further Information for Submission

### 6.1 Support to the community and behaving responsibly

Punch is aware of its responsibilities on a number of levels. It is active on industry issues to promote responsible drinks retailing and in 2012 generated £1.8m worth of value-in-kind media coverage for ‘Why Let the Good Times Go Bad’.

As well as supporting ‘Pub is the Hub’ through funding and management time, we also financially support The Licensed Trade Charity’s volunteer visitor programme and promote the Punch Community Promise through Head Office in Burton where, as well as financial support to good causes such as the local scanner appeal, every employee has one day a year allocated to work for a local charity.

### 6.2 Further inaccuracies

A number of the organisations within the document are incorrectly referenced e.g.:

- At page 6 and subsequently, the document refers to the Royal Institute of Chartered Surveyors. It is the Royal ‘Institution’.
- At page 11 and subsequently, the document refers to the British Institute of Innkeepers. It is the ‘British Institute of Innkeeping (BII)’.
- The impact assessment refers, at point 33, to the implementation of Version 5 of the Industry Framework Code of Practice. Version 6 was published on 11 February 2013 and implemented in time for the publication of the Government consultation document.

### 6.3 Abolition of the gaming machine tie = Unintended deregulation = Increase in crime

We do not agree with the assertion that: “The gaming machine tie serves no good purpose”. We feel this comment clearly demonstrates an absence of knowledge and understanding about this important element in the successful operation of a public house. The consultation document shows a similar lack of knowledge about the benefits that accrue to licensees and legitimate machine suppliers as a result of the tie.

Feedback from the manufacturers and suppliers of gaming machines<sup>42</sup> shows how strongly they view the benefits of the tie in the profitability and professional operation of gaming machines in UK tenanted and leased pubs. Industry experts believe that the position would revert to the situation that prevailed before the introduction of the 1968 Gambling Act. The Act was brought into force to stop black market activity – which included illegal machines being put into pubs and a failure to pay the requisite licences, VAT or Machine Gaming Duty (MGD).

In their dealings with suppliers of gaming machines, pub companies set rigorous standards of performance and enshrine these in contracts. These standards ensure that all the pub company’s tenants receive the same level of service and operational support – for example, maintenance calls within two hours of notification. By removing the tie, the tenant would lose this consistent support

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<sup>42</sup> Appendix 12 – Testimonials from Gaming Machine Suppliers.

and there would be an increase in rogue operators, using various tactics to compel tenants into taking machines. Machine security and software updates to protect machines from theft and attack are monitored by the pub companies, ensuring that tenants benefit from secure and protected machines. This would also be lost.

Centralised contracts ensure consistent pricing for the gaming machines – preventing unplanned changes to the cost of machines for both the tenant and the pub company. The machine tie provides substantial benefits to the tenant, to Government, to the Exchequer and to the regulatory and licensing authorities, including the Gambling Commission. Better management and monitoring of machine performance leads to greater returns than in a free-of-tie environment. Tenants maximise their profit, bringing higher returns for the Exchequer.

The tie allows machine suppliers to deal with legally compliant and socially responsible corporate organisations that represent large numbers of tenants. As a large pub company, we operate a specific machines function to ‘approve’ suppliers through a thorough and professional tender process, which establishes the legal and compliance status of suppliers. This ensures that the suppliers are ‘fit and proper’, with the requisite gambling licences, and that they are run by approved and licensed executives. It also means that Punch can ensure the three main principles of the Gambling Act are upheld: namely ‘Keeping gambling crime free’; ‘Protecting the vulnerable’; and ‘Protecting children from gambling’. Removal of the tie would lead to rogue and illegal operators, who will cut corners, operate without the required licences and supply dangerous and poorly maintained equipment, with illegal software or stake and prize controls.

Pub companies and their approved suppliers administer gaming permits and licences, constantly ensuring pubs are able to provide gaming legally. This results in a high level of compliance. Without the tie, tenants would have to sort this out individually. This would inevitably result in high levels of non-compliance, as well as a potential loss of revenue for the licensing authorities and the Exchequer. The introduction of MGD has been strongly supported by the pub companies, with resources, awareness literature and compliance monitoring. The machine tie ensures this takes place.

Without the tie, this support would end. Pub companies are able to work with the manufacturers of gaming machines to support them in understanding how machines are perceived by customers. They can also provide feedback on hardware and software developments, and in testing new concepts. There would be no supervision of the rates at which new machines were supplied by approved operators. As a result, the development and manufacture of product into this market sector would become questionable. Suppliers would sweat their assets longer, leading to a decline in performance, as machines rapidly become dated, generating less income and tax.

The removal of the tie would accelerate the decline in the supply of new machines being manufactured, leading to a reduction in staff employed by suppliers and throughout the supply chain. Individual tenants would not have access to information about the performance of machines across a broad range of outlets, to judge the quality and performance of a particular machine. This would lead to poor decision-making and loss of revenue to all parties. The testing, approval, injection and changeover rates, service standards and customer choice are all essential elements that contribute to the success of gaming machines in pubs. The loss of these controls would have negative repercussions all the way down the supply chain.

There would be a loss of income to the Responsible Gaming Trust<sup>43</sup> (which works to minimise the level of problem gambling and gambling-related harm in Britain), as they are supported by the pub companies at their own expense. This would result in a loss of lobby support to engage with Government to drive change around gaming.

#### **6.4 Tied tenants tend to be insulated from economic factors due to the tie**

There are a number of economic factors referenced within the consultation document. These are not exclusively relevant to the pub sector, but affect different businesses that retail directly from premises rather than online. As such, a direct comparison can be made with the retail sector, where it is estimated that 28 shops a day are closing due to the economic climate.<sup>44</sup> The closure of pubs is wrongly identified and associated with the pub company business model, when the same situation is happening within other sectors of the economy.

The consultation document states that:

*“The pub industry faces a wide range of challenges and the number of pubs has declined from 70,000 in 1980 to approximately 50,000 today”*

There is an inference that this is due to the tied business model. This is not the case. There have been a number of factors, including the habits of consumers, the decline of traditional manufacturing, loss-leading alcohol at the supermarkets and the smoking ban.

There has been little or no help from successive Governments over the years. Increases in beer duty, extending the rating revaluation cycle, and the increase in legislation affecting small businesses have all affected the sector negatively. Pubs and brewing remains one of the most regulated sectors in the economy, with a raft of legislation covering every aspect of the sale of food and alcohol.

The consultation document states that:

*“At present, 18 pubs (net) are closing every week.”*

This has been usurped by a recent survey that shows that 26 are now closing every week. These figures are placed in the context of the pub company business model. However, this does not reflect the November 2011 report from the Government, which states that the free-of-tie tenant is more likely to fail than the tied tenant. This increase has become starker as the tied estates have sold their pubs into the free market. Although the pubs are sold with their licences in place, the free market usually moves them away from pub use.<sup>45</sup>

The consultation document further states that:

*“Whilst the financial crisis has brought into stark relief the slow process of sectoral decline, it is undoubtedly the case that the activities of the major pub companies, with their highly leveraged business model, have intensified the crisis.”*

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<sup>43</sup> <http://www.responsiblegamblingtrust.org.uk/>

<sup>44</sup> 28 February 2013, 'High street closure toll could reach 28 stores a day'  
<http://www.guardian.co.uk/business/2013/feb/28/high-street-store-closures>

<sup>45</sup> Punch sells 96% of its pubs as pubs. Information from Christie & Co (see Appendix 15) and Punch's own in-house survey show that two years after disposal only approximately 60% of these remain as pubs.

This is not the case. As can be seen from the List of Facts on page 12 and 13, the support that tied tenants get is significantly greater than that of free-of-tie tenants.

### 6.5 Punch opposes the abuse of the tie

There are further two statements within the consultation document that are contrary to the evidence of recent Government publications:

*“The tie gives an additional route of abuse and complicates the relationship.”*

This statement directly conflicts with the evidence of the Office of Fair Trading’s (OFT) findings following the Campaign for Real Ale’s (CAMRA)<sup>46</sup> super-complaint. This states:

*“Given that we have found that consumers are benefiting from a significant degree of competition and choice between pubs, we do not consider that issues relating to the negotiation process between pub companies and lessees can generally be expected to result in consumer detriment.”*

The other statement within the consultation document states:

*“Tied tenants are also more likely to face serious hardship.”*

This statement directly conflicts with the Government own evidence of 2011.<sup>47</sup> This states:

*“Whilst the Government recognises that pubs face a wide range of challenges in the current economic climate, it sees little evidence to indicate that tied pubs are more likely to close, as has been suggested. In addition, particularly in the case of the traditional tenancy model, the tie may actually play an important role in safeguarding the future of Britain’s smaller breweries”*

Given the above statement and the amount of financial support evidenced in Table 2 on page 21, Punch would argue the opposite point – that tied tenants are generally less likely to suffer serious hardship than free-of-tie tenants.

### 6.6 Bad for jobs and bad for business

At 3.6, the consultation document states that the tied tenant is “more likely to face serious hardship”. This is not true, as can be seen from the already-quoted response from the Government in November 2011.

*“Data produced by CGA Strategy clearly shows that between December 2008 and June 2011 more free-of-tie pubs closed than tied pubs, both in absolute figures and as a percentage of the total number of pubs in that category”<sup>48</sup>*

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<sup>46</sup> p7 of the OFT report; [http://www.of.gov.uk/shared\\_of/super-complaints/oft1137.pdf](http://www.of.gov.uk/shared_of/super-complaints/oft1137.pdf)

<sup>47</sup> Note in the Government’s Response to the House of Commons Business, Innovation and Skills Committees Tenth Report of Session 2010-2012: Pub Companies dated November 2011, on page 3.

<sup>48</sup> Note in the Government’s Response to the House of Commons Business, Innovation and Skills Committees Tenth Report of Session 2010-2012: Pub Companies, dated November 2011, on page 3.

The evidence that tied tenants are more likely to face serious hardship appears to rely solely on the survey of 500 licensees carried out by the IPPR in 2011, which found that 46% of tied publicans earn less than £15,000 per year, compared to 23% for tenants who are free-of-tie. Punch is seeking to understand the nature of this survey, which was funded by CAMRA and Fair Pint, both opposed to the tie.

Comparisons between pubs are notoriously difficult to make. Punch notes that of the pubs surveyed by IPPR, the proportion with a turnover > £300k is higher for non-tied pubs than tied pubs. If that is right, then it is not surprising that it results in higher earnings for non-tied pubs. Indeed, this appears to be recognised by Government. In the Impact Assessment, BIS states.

*“A survey commissioned by the Institute for Public Policy Research asked tied and free of tie licensees what their personal income was. 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 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.”*

Inevitably, tenants are going to under-assess their earnings within a survey where the end result may be available publicly. It is also more difficult to assess the gross salary in a pub with accommodation, than it is for an employee who pays for accommodation and travel.

However, before renting a pub from Punch, our partners sign an agreed profit and loss account, which we jointly agree is achievable. In the current financial year,<sup>49</sup> we have agreed terms with approximately 370 partners, where the average earnings or net disposable income is estimated at £28,700 per annum. This is income that is additional to the accommodation and living expenses that partners enjoy.

#### **6.7 A dangerous reduction in investment**

Quoted in paragraph 3.14, the consultation documents states:

*“The main benefit and aim of the policy is the estimated transfer from pub owning companies to tenants of £102m per year”*

If there were a transfer of value of this magnitude from the pub company to the tenant across the pub sector, the unintended consequences would be significant and would lead to job losses. Table 3 on the following page shows the levels of investment within the likely affected pub companies in 2012.

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<sup>49</sup> August 2012-April 2013.

**Table 3**

Pub company	Investment spending
Admiral Taverns	£8m <sup>50</sup>
Enterprise Inns	£63m <sup>51</sup>
Greene King	£21.6m <sup>52</sup>
Marston's	£32.1m <sup>53</sup>
Punch	£38m <sup>54</sup>
Star Pubs (formerly Scottish and Newcastle Pub Enterprises)	£10-15m <sup>55</sup>
Total	£172.7m <sup>56</sup>

The reduction of investment due to the reduced level of income available would be one of the inevitable consequences. Punch will have invested on average £40m per annum over the last three years. It is estimated that the contractors and advisors, excluding the supply chain, currently employ 461<sup>57</sup> people, and these jobs would be lost. Across the entire sector, with a £102m reduction in investment, 1,250 jobs would be lost across the construction and design sectors.

The impact assessment produced by BIS at paragraph 82 and 83 states:

*“Increasing the share of profits that goes to licensees will increase their incentive to invest... some pub owning companies may be taking a short term view due to pressures servicing debt (by not investing).”*

This is not true of the business model. Even if some of the companies are highly leveraged, Table 3 speaks for itself – the pub companies are investing. On the other hand, most tenants with a transfer of value from the pub company will not invest in the pub – particularly if they have a short-term agreement. Pub companies usually have a long-term interest in the pub, even if the tenant changes, and therefore look to invest and reinvest in continuous cycles. The only real ability to create growth in the pub sector is through investment.

<sup>50</sup> Admiral Taverns' press release 28 February 2013.

<sup>51</sup> Enterprise Inns plc, Annual Report 2012, p9.

<sup>52</sup> Greene King plc, Annual Report 2012 p64; Financial Statements Capital Expenditure – tangible assets capital expenditure, Pub Partners.

<sup>53</sup> Marston's plc, Annual Report and Accounts 2012 p62; 'Segment Reporting' – Capital Expenditure, Property Plant and equipment (excluding intangible assets).

<sup>54</sup> Punch Taverns plc, Annual Report and Financial Statements 2012 p1.

<sup>55</sup> Not publicly available. Figure taken from verbal enquiry with Star Pubs' Property and Strategy Director, 10 May 2013.

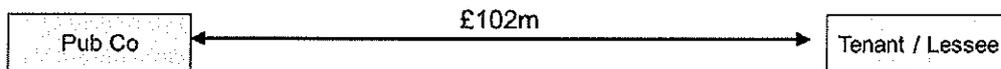
<sup>56</sup> This is the lower figure provided by Star Pubs.

<sup>57</sup> £40m spend equates to c400 projects based on Punch's average spend of £100k per pub. Each 'average' project is on site for three weeks typically and would involve c18 workmen for this time. Each project has c54 man weeks x 400 projects = 21,600 man weeks; divided by 52 = 415 FTEs. In addition, we have 23 external Punch designers/project managers. An estimate would be that they, on average, have two people 'dedicated' to Punch work, so 46 FTEs involved. This excludes the people in the supply chain.

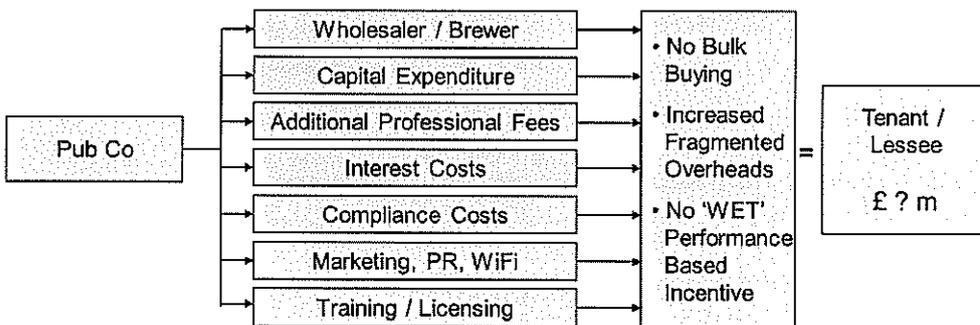
Even assuming tenants want to invest, it is still unlikely that the £102m will be invested if some or all of the proposals set out in the Code are implemented. Image 2 below shows how the loss of economies of scale would be substituted by higher costs to the tenant, as additional costs and fees would increase.

Image 2

**BIS Assumptions**



*Taking into account SCORFA benefits, wholesale margins and other costs*



The further unintended consequences are highlighted within the consultation document at paragraph 3.15, where it states:

*“It is our assessment that no pubs should become unviable as a result of the policy, as profit is only moved from one party to another.”*

This is a naive statement at best. If the pub becomes unviable for the pub company, it will form part of a disposal estate. If the pub is unviable, the tenant and pub owning company are under no obligation to reach a commercial negotiation as is suggested within the BIS consultation and impact assessment. If no agreement can be reached, what are the options? The Adjudicator could well find they are either swamped or have no pubs to deal with, as they will be disposed of by the larger pub companies and will be part of a smaller non-tied estate. This would lead to a further decline in the sector, as no support would be available to the tenant as there is under the tied model.

BBPA instructed Compass Lexicon to undertake an independent study into the potential consequences of the current BIS proposals and particularly the impact of the mandatory free-of-tie option.

Compass Lexicon is one of the world’s leading economic consulting firms. It provides expert economic advice on competition policy, economic and financial regulation, public policy and the assessment of damages in complex disputes.

Compass Lexicon modelled pub-level data from [redacted] pubs provided by BBPA members who would be impacted by the proposals (i.e. who operate over 500 pubs). The findings were then scaled up to cover the total [redacted] pubs covered by BIS proposals. The full report and detailed methodology has been provided to BIS.

### **6.8 Impact on Punch suppliers**

The Government's proposals would inevitably have a significant negative impact on Punch Taverns' suppliers. In the new operating environment, with fewer pubs, reduced investment and the balance of power shifting towards the international breweries, our mainly-British suppliers and contractors would experience loss of business and be forced to make job cuts. The impact on companies such as Vianet, which provides our peak flow monitoring equipment, and the small and medium-sized brewers that supply our guest cask ales, cannot be over-stated.

Testimonials supplied for this consultation by Punch suppliers are shown in Appendix 14 a few extracts are highlighted below:

who run two Punch pubs including the

I have read with interest the recent opposing opinion with regards to the way in which operators such as Punch Taverns work with their tenants and whilst I can appreciate that every case may differ, there is always more than one side to the debate.

There will undoubtedly be tenants that are struggling in the current climate and this is sadly as a result of many factors, and the blame cannot be attributed to one factor namely the operators such as Punch. The reality is that many factors have influenced the demise of the pub trade including the taxation/duty imposed on alcohol, the smoking ban, the downturn in the economy leading to customers having less disposable income etc. and in my experience to date we have enjoyed an amicable relationship with our landlords namely Punch.

We recognise that Punch is a business with its own financial difficulties much the same as other large operators such as Enterprise inns, whom we also have a commercial relationship with. We have found Punch to be supportive to the best of their ability and we have always communicated effectively with our regional manager which has in turn resulted in a positive relationship being able to work with each other in the interests of both parties remaining happy with the agreement.

We have certainly had support in respect of a joint venture investment in our flagship pub in , which as a result of their continued support during difficult initial trading periods has now flourished. We had a relatively low level cost to entry into the trade and were also provided with a platform to showcase our beers. As a micro-brewery in a highly competitive market place this has proved incredibly valuable and a model we wish to recreate in other locations with their support. Our goal is to further strengthen this relationship and hopefully create a portfolio of pubs with Punch and increased listings with their finest cask and product listing nationally. We feel the growth of our business in respect of a portfolio of pubs would not be viable without their support and the reality is they can also help significantly increase our distribution and growth in the brewery so the partnership is a win win for all.

From our experience we certainly wouldn't have any hesitation in recommending Punch to other people interested in entering into the industry.

, Managing Director of

It is my opinion that the majority of the current problems surrounding 'the tie' were caused as a result of the 'Beer Orders' and this subsequently created 'greedy' pub companies. However I have at first hand seen a marked improvement over the last five years in how the senior leadership at Punch Taverns has improved the whole culture of the business from the core outwards. It was clearly true a decade or so ago that pub companies were simply property companies that were enjoying increasing asset values whilst being able to use existing agreements that were in place from the national brewers before them to take much more than their fair share out of the value chain that pubs created. This was to the detriment of the tenant and in most cases the consumer as well.

Much change has already been driven through; Punch Taverns now operates to keep pubs open. The penny has dropped with pub companies with a realisation that they need highly

motivated, innovative and suitably rewarded entrepreneurs to run their pubs. No longer can these pubs be closed in the knowledge that they are making more in daily capital gain than they do as a trading pub. Punch have consolidated their operations and actively seek to engage with their partners, both to understand their needs better and to give them the tools and information they need to assist them in running a successful business. The pub itself as a trading entity is important again. We regularly attend Punch Road Shows where this process can be seen in action and we have the chance to showcase our beers to visiting tenants and get the chance to understand what they want from us, the supplier. I'm sure that Punch Taverns would be more than happy to invite you along to see one of these events for yourself, to experience the support and innovation they offer their partners.

, Director at

Punch have a national network of business relationship managers who help and work closely with their tenants to drive business, support refurbishment programs, discuss and advise with regard to changing cultures in the pub industry and liaise with small brewers such as ourselves to get involved and support community pubs. Indeed we now provide free cask ale cellar training to Punch licensees, lend equipment for small festivals, offer brewery tours and arrange in the pub 'meet the brewer' evenings etc.

From new signage to arranging weekend beer festivals, sponsoring celebrity visits, loaning a marquee, supporting applications for licensing of special events Punch's management team work hard to look after their partners.

We value our partnership with Punch Taverns. We have enjoyed 5 years of honourable trading with them and despite being a small supplier we have at all times been treated fairly, openly and positively. Unlike many of our 'free of tie' freehold customers Punch Taverns also pay us on time every single month. (This is crucial to a small business like )

We regularly attend Punch Roadshows in our region where we can meet up to 300 of their publicans in a single day. I am sure those involved in the government's consultation process will be familiar with the efforts Punch are making to engage their tenants but in case they are not I can honestly say that in the last two years, every tenant to whom we have spoken at a Roadshow has told us that Punch is a changed organisation that listens to and cares about its partners. We have also met senior executives from Punch who attend to listen and understand the feedback from their estate.

### 6.9 Current experience and evidence from Punch partners

The majority of the campaigning and rhetoric regarding the pub companies is from disaffected tenants. They are a loud but very small minority of individuals, many of whom have ulterior motives. The views of the 'silent majority' of tenants are ignored. Why would you respond to a consultation when everything is going well?

The great experience of Punch partners is a sign that the tied pub company works. Punch has received 276 testimonials from partners, which is at Appendix 15, a few highlights from the testimonials given to BIS and Punch Taverns are given below:

[redacted] at the [redacted]

Since the economic downturn, Punch, and many of the major Pubcos, have revisited and remodelled the lease terms, with many of the changes to the benefit of the leaseholder. Punch have recognised their part in a dying industry, and are working hard to provide solutions for their leaseholders, whilst obviously trying to protect their revenue interests at the same time. Last November, [redacted] received a significant refurbishment, funded by Punch, which has lifted my business profile, negated my impending repair issues, and given me an excellent platform to drive my business forward. My rent has remained at it's previous level, and I have a beautifully refurbished pub to attract new business. It is obviously not possible for Punch, or any of the other Pubcos, to refurbish their whole estate, but they are clearly re-investing where suitable, with good effect, even though the responsibility of repair and renovation lies with the leaseholder.

[redacted] a multiple tenant):

Whilst it is true that the lowest gross margin products on sale in any of leasehold pubs are tied lager and ale, this is not a point of great concern. Like many others, [redacted] has concentrated on developing an excellent food offering and extensive wine list ( both of which our customers really want) thus ensuring that average gross margins across all sales can be maintained at an acceptable level. In all other areas of retail, lessees would pay a base rent and a turnover rent as the norm – in tied pub leases the beer supply tie is simply a (part) turnover rent by another name.

It is also worthwhile contemplating that whilst the "holy grail" of free of tie beer supply may be helpful to some, it is far from certain that it will lead to cheaper beer for retailers as the beer manufacturers and distributors will then face dealing with many thousands of new customers all wanting cheaper prices. In all likelihood, the increase in sales and customer service costs and importantly credit risk faced by the beer suppliers are likely to lead to higher prices than many retailers currently envisage.

[redacted] at the [redacted]

Punch have always listened and in 2007 recognised the need for our rent to be reduced significantly. We didn't have to beg or seek arbitration it was just done. We have just renewed our lease and again the rent has gone down no hard negotiations required just an acceptance by both parties that trade ain't what it used to be. We knew what we were getting into when we signed the lease and that we pay significantly more for our beer than if the pub were free of tie. However it is not lost on us that if we had a free of tie lease it is unlikely that our landlord would want to share our pain but merely enforce the collection of the rent. Punch have shared that pain, as our beer volumes have declined they have lost revenue but also that knowledge has enabled them to step in to reduce our rent before our business went under.

[ : at ]

I have run the [ ] now for over nine years and throughout this period have found Punch Pubs to have been very and easy to work with and the rent review process very honest and open. They have always helped and supported us whenever necessary and helped us with a massive investment which enabled us to keep growing the business.

Whilst the beer tie has many detractors it does enable people like myself that would not be able to finance freehold properties an entry point into the industry that would be otherwise denied. Without the Pub Co. Support many leaseholders would suffer by not having the expertise to organise their training, licensing, marketing or legal responsibilities – which are all currently given with the help and support of a Retail Business Manager.

Yes, the beer is more expensive with a tie but would you still get the full help and support from these big organisations if they were just straight forward Landlords? I doubt it.

My final point is this, that although Pub Companies do take a lot of bad press, it is not all their fault. Whilst even they admit that they do not always get it right, many people blame them because it's easier than to look at themselves when their business fails nor can they blame their customers, so who else is there?

[ at the ' ]

Along with my partner I have been a leaseholder of a small community pub since 2004 and since around 2005 the pub has been under the ownership of Punch Taverns PLC, whilst we could never have described ourselves as a thriving business we were able, up until a couple of years ago, to just about keep our heads above water ( through a mixture of hard work and luck!). For the last 2 years or so, however, we, like so many other business's, have found it virtually impossible to survive and I have to say that without the help of Punch Taverns our business would definitely have gone under.

I feel it is only fair that credit is given where it is due and my own experience is that in the last few years Punch Taverns have certainly changed the way they operate. I have a very good open relationship with my Business Development Manager and can honestly say that both he and the company have tried their best to help us, they have invested in my business by funding a refurbishment, have reduced my rent and have given us large discounts on the price we pay for our stock.

[ ... at the ... ]

The first 3 years of trading have been very difficult but with help from Punch's support network we are now having a good year despite the hard economic times. As we speak we are currently having 3-4K spent on the pubs electrics that the pub company is paying for which if we were free of tie we would have to spend ourselves.

Punch have paid £1500 for new stillages in the cellar in order to save wastage which actually means we buy less beer from Punch but improves our profitability.

The support network which we use on a daily basis would also not exist if we were free of tie. The online ordering website which offers deals and new products would also not be available. We have recently encountered some health and safety issues at the pub which have been dealt with efficiently by the Punch risk department.

We have a very good relationship with our local Business Development Manager who comes down for regular on site meetings to let us know about our performance and any new ideas and incentives. This service obviously has to be paid for and if we were free of tie then Punch would not be able to provide these very valuable resources. If it wasn't for all these departments our business probably wouldn't still be succeeding.

[ ... who runs ... ]

During the negotiations of all four agreements the pub companies described the heads of terms in great detail providing us with huge packs of supporting information and various courses to help in areas where we lacked expertise. On top of this we carried out our own market research and analysis of figures and entered into each of the agreements fully understanding the terms and any restrictions imposed on us.

In our opinion there is nothing exploitive about these agreements and the support provided by the pub companies has been incredibly helpful and has allowed us to develop a successful business, which now employs 60 people!

[ . . . ]

The free of tie model does of course have the benefits of lower beer prices that we negotiate through buying direct from the wholesalers however it is important to point out that support is almost non-existent and if available always comes at a price. In effect it can be quite a lonely place to be and I am very fortunate that I can turn to my Punch contacts to discuss ideas, issues and solutions.

On the other hand in my Punch leased and tenanted pubs I have been able to weather the storm of the smoking ban a new licensing regime and the dreadful economic downturn through their support. We have benefited from rent concessions, repayment plans, seasonal rents and all manner of other support including menus and posters etc. Our relationship with the Punch PDM's is excellent it is forward thinking and at times challenging however it has helped to ensure that our business has remained commercially viable.

It is also important to mention that the tie has worked for us in numerous ways allowing us to flex from either being fully tied or part tied thus having a lower or higher rent depending upon the location and style of pub that we are looking to operate.

[ . . . ]

I would like to express my views, having recently taken on a 10 year lease with Punch Taverns

Right from the start of the process, they explained the Pub-co structure outlining investment required, structure and beer pricing. I feel that although I have taken on a very tough business in these times of financial uncertainties, Punch have consistently supported with training, considerable investment into the property to ensure the business trade area looks and feels bespoke for the high expectations of today's public visitor.

Having worked previously for a large hospitality company for 15 years, I can honestly say how refreshing I have found being a business partner with Punch, they have offered far more support, physically, mentally and in a genuine caring way that the business should succeed in the short time that I have been at the [ . . . ] than the last few years with a company that should have had a 100% interest in ensuring their business performed

I look forward to a continual developing partnership with Punch, knowing that I can call upon their Expertise to support the business into the tough times ahead to a successful conclusion

## **Appendices**

- Appendix 1 Reports and inquiries into the public house sector since 1969
- Appendix 2 Letter from Greg Mulholland dated 30 October 2009
- Appendix 3 Contents of the 'White Box', challenge notices, refusal books, training records etc.
- Appendix 4 Safe, legal and compliant manual
- Appendix 5 Likely cost of SCORFA benefits
- Appendix 6 Punch's Code of Practice
- Appendix 7 Where Punch's Code of Practice exceeds the Industry Framework Code
- Appendix 8 Punch Statistics and CGA Brand Data
- Appendix 9 Consistent anti-pub co correspondence from Liberal Democrat MPs
- Appendix 10 Punch statistics from the BII
- Appendix 11 An example of the Punch valuation template
- Appendix 12 Testimonials from gaming machine suppliers
- Appendix 13 Christie & Co report on-going sales
- Appendix 14 Testimonials from Punch suppliers
- Appendix 15 Testimonials from Punch partners