



Pubs Code
Adjudicator

RESPONSE 20





Pubs Code
Adjudicator

Guidance: Accounting for duty paid on alcohol and volumes of unsaleable draught products in Pubs Code forecast profit and loss statements

Consultation under section 61(4) of the Small Business, Enterprise and Employment Act 2015

Response Form



Annex C: Response Form

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Please tick the box below which best describes you as a respondent to this consultation:

Pub-owning business with 500 or more tied pubs	<input checked="" type="checkbox"/>
Tied pub tenant	<input type="checkbox"/>
Interest group, trade body or other organisation	<input type="checkbox"/>
Other (please describe)	

Introduction to Punch

It is important to stress that at the heart of the tied business model is an aligned interest of both the Landlord and Tenant to achieve the maximum potential for the pub business, the entrepreneurs running the pub, and the consumers using the pub. Punch operates a mixed estate of circa 1,300 high quality leased, tenanted and retail pubs. Our years of experience have enabled us to develop a leading proposition for those wishing to work with us and run a pub business of their own. Established in 1999, we became one of the largest pub companies in the UK and have played a pivotal part in the tied pub industry evolving. We believe we are ideally placed to provide comment on this consultation.

- We continue to invest substantially to develop fabulous pub businesses. Under the ownership of Patron Capital and May Capital, we have plans to invest over £80 million developing our pubs during the next three years.
- Our market-leading Training Academy and Punch Progress training package provide some of the sector's best induction training and continuing professional development. We have just launched a mobile-friendly training console and app with CPL Training. We have also been recognised with a National Innovation and Training Award (NITA) for our Art of the Possible Training programme.
- We were the first pub company to launch an online ordering and information portal for our Publicans in 2011. We currently have 90% of our estate registered for online ordering via our award-winning Punch Buying Club which has just taken its 100,000th order and sold our 100 millionth pint of beer.
- We operate a mixed estate of leased, tenanted and retail businesses, enabling us to share learnings and best practice across all.
- We have successfully launched and continue to develop a range of innovative retail concepts, including our Champs Sports Bars.

- Our dedicated in-house food team use their expertise and our Academy Training Kitchen to develop innovative and on-trend dishes, perfectly suited to our various retail concepts. The tried and tested results are then brought to our leased and tenanted pubs.
- We provide a market-leading product range to our Publicans, including one of the broadest and most established cask beer ranges in the industry with 72 rotational cask ales a year.
- Our marketing support remains unparalleled including the world's largest pub teams dart competition (The Punch Darts Classic) and the biggest national pub quiz.

The Punch estate contains more than 500 pubs being operated under tied leases or tenancies. Punch are therefore a regulated Pub Owning Business (POB) by the passing of the Small Business Enterprise & Employment Act 2015 and the subsequent introduction of The Pubs Code etc Regulations 2016 (the Code) and The Pubs Code Adjudicator (PCA).

Background: The Code

The consultation document is focused on how a POB can meet their duties under paragraph 5(c) and 5(d) of Schedule 2 of the Code. Schedule 2 of the Code concerns itself with the provision of information for the purposes of a rent proposal or a rent assessment proposal, ensuring a Tied Pub Tenant (TPT) has all of the information they need to make a fully informed decision regarding the rent which is being proposed.

Schedule 2 paragraph 5(c) provides that a forecast profit and loss statement (for the purposes of assessing a rent proposal) should include detail on the volume of alcohol in respect of which duty is paid. This is due to some beer containers having sediment contained within them, sometimes referred to as unsaleable liquid. This provision looks to ensure that when assessing a rent for a tied pub, consideration is given to the volume of beer than a TPT would not be able to sell from the containers they have purchased.

Schedule 2 paragraph 5(d) provides that a forecast profit and loss statement (for the purposes of assessing a rent proposal) should provide a breakdown of sales and gross profit margins achievable by the differing drink categories (draught ales, draught lagers, packaged beers etc). This provision looks to ensure that a TPT can understand how the total assessed sales within the rent proposal have been arrived at and the assumptions made in regard to the sales mix adopted.

It is also worth noting that Schedule 2 paragraph 5(f) also deals with how unsaleable beer that is lost through operational waste (via line cleaning etc) is accounted for, in that a POB should ensure an estimated figure for the volume of this is provided unless there is an allowance made when calculating the gross profit margin – adjusting the achievable profit margins by deducting an allowance for such waste.

Background: Origins of Sediment Allowance/Duty Paid Liquid

Prior to 1990 Brewers would calculate duty of cask ale by assessing sediment content during the brewing process (known as 'at dip'). This process changed to be more in line with European practice and subsequently the UK adopted a 'duty at the gate' approach where brewers would calculate the sediment and duty to be paid once the beer was ready to leave the brewery (when the beer had matured and sediment fully formed). This resulted in the dutiable liquid being

measured once in cask and prior to distribution. HMRC test and agree with the individual brewer the sediment allowance (amount of unsaleable liquid) to be deducted from the duty paid.

The sediment allowance is reflected in the duty paid, which is then reflected in the cost price the Publican pays. Punch, as a POB accept changes to duty from the Suppliers/Brewers we deal with, in line with government changes. These changes in sediment allowances/duty paid are then factored into the Publicans price per container purchased via Punch. Punch will usually pass on both increases and decreases on duty regardless of if they originate from Government changing the duty rate or from brewers altering their brewing techniques which in turn impacts the sediment.

It is also important to note that sediment is unique to Cask products and does not apply to Keg products. Therefore, the requirement to detail the Duty paid volume if this differs from the purchased volume is unique to Cask products (given that in Keg products all volume will have duty paid).

Background: Tied Pub Industry Rent Valuation

It is important to remember that the forecast profit and loss statement is provided for the purposes of proposing a rent assessment as part of commercial negotiations around the tied pub rent. The leading authority for guidance with regards to rental valuation is the RICS Guidance note GN 67/2010 'The capital and rental valuation of public houses, bars, restaurants and nightclubs in England and Wales'. Punch fully understand the requirement for the information to be accessible and welcome the ability for TPT's to make fully informed decision on such matters. It should be noted that the rent proposal forms one side of a commercial negotiation which very often is agreed between the POB and TPT via negotiated settlement.

In addition, it must also be noted that in regard to rental valuation the profits method for which this consultation concerns itself with is effectively a secondary stage of valuation. The first consideration being an analysis of comparable market transactions, of which the considerations such as those proposed in this consultation rarely arise. It is important that this context is retained when considering the overarching purpose of the material covered under this consultation.

Accounting for Duty Paid

Question 1: Do you believe that these proposals will ensure that tied pub tenants are fully informed of the duty that has been paid on the alcohol supplied to them under their tied agreement?

The proposals, as with the Regulations as existing, ensure that information in regard to the volume of alcohol on which duty has been paid is readily accessible and available should a TPT wish to access this. However, the proposals appear to extend beyond the scope of the Pubs Code in that Schedule 2 requires POB's to provide details on the volume of alcohol on which duty has been paid whereas the proposals seemingly seek to require POB's to provide detail on the actual level of duty paid (see paragraph 6.3).

The proposals will therefore not ensure that a TPT is fully informed of the duty that has been paid as this extends beyond the scope of the Regulations. The proposals should concern themselves

with ensuring that a TPT is fully informed on the volume of alcohol on which duty has been paid which we believe the existing Regulations already cater for.

Question 2: If not, please explain what additional or different approaches you think would ensure compliance with Pubs Code requirements.

We would encourage the pursuit of simplicity. What has been perceived as an issue regarding sediment has been given a lot of importance, but in reality it does not have a material impact to many tenants when proper cellar management is carried out.

Given that the information which the TPT should have access to relates to individual beers/products rather than being specific to which POB a TPT engages with, it may be better placed for an industry body such as the BBPA to hold a central list/source of such information and for each POB to provide access to this via their own website.

This will ensure a consistent approach to displaying and communicating such information as well as a consistency in regard to refreshing and reviewing such lists.

Question 3: Can you foresee any unintended ways in which these proposals might have a detrimental effect on tied pub tenants? If so, how might such effects be mitigated?

If POB's display the required information in differing manners (i.e. container sizes, volume of which duty paid/not paid for example) the information could become confusing for a TPT engaging across differing POB's. If information is displayed in a consistent and clear manner there should not be any detrimental effect on the TPT.

Where a POB is not a brewer it will be solely reliant on suppliers for the provision of the information. This requirement could lead to some very small brewers, who are unable to easily comply with the proposed prescribed requirements, not being able to supply into the larger POB's covered under the Code. There is therefore a potential significant financial detriment to such smaller suppliers due to perceived over-complication of a matter which has been working in practice for decades.

Accounting for Waste

Question 4: Please indicate whether you agree with the proposal to account for sediment and operational waste separately.

We agree with the proposal to account for sediment and operational waste separately. We already currently display allowances for each of these elements in our existing forecasted profit and loss statements/rent assessment proposals. An example of how this is currently presented is shown below:

Income	Tie	Price Band	Barrels/ Litres	Discounted Price	Unit Price (incl VAT)	Retail Unit	Turnover	% of Total T/O	GP%	Gross Profit
Wet Trade										
Premium Ales - > 4.2% Abv (Barrels)	Y	PPP	30	£462.73	£3.80	Pint	£27,360	3.0%	49.3%	£13,488
Standard Ales - <4.2%Abv (Barrels)	Y	PPP	75	£454.46	£3.50	Pint	£63,000	6.8%	45.9%	£28,917
Ales - Packaged (Barrels)	Y	PPP	1	£716.09	£3.20	275ml	£1,587	0.2%	54.9%	£871
Beer - Guest (Barrels)	Y	PPP	0	£0.00		Pint	£0	0.0%	0.0%	£0
Premium Lager - > 4.2%Abv (Barrels)	Y	PPP	75	£613.39	£4.50	Pint	£81,000	8.8%	43.2%	£34,992
Standard Lager - <4.2%Abv (Barrels)	Y	PPP	75	£480.77	£3.75	Pint	£67,500	7.3%	46.6%	£31,455
Lager - Packaged (Barrels)	Y	PPP	4	£609.16	£3.40	275ml	£6,744	0.7%	63.9%	£4,309
Cider - Draught (Barrels)	Y	PSP	15	£519.99	£4.00	Pint	£14,400	1.6%	45.8%	£6,595
Cider - Packaged (Barrels)	Y	PSP	5	£667.11	£2.25	275ml	£5,578	0.6%	40.2%	£2,242
Specialities (Litres)	FOT	STD	300	£3.14	£3.30	275ml	£3,000	0.3%	68.6%	£2,058
Wines (Litres)	FOT	STD	2,500	£6.40	£3.95	175ml	£47,024	5.1%	66.0%	£31,036
Spirits (Litres)	FOT	STD	500	£17.10	£2.75	25ml	£45,833	5.0%	81.3%	£37,262
Minerals - Bulk (Diluted Litres)	Y	3Z	8,000	£0.86	£1.95	285ml	£45,614	5.0%	84.9%	£38,726
Minerals - Cased (Litres)	Y	3Z	3,000	£1.80	£2.40	275ml	£21,818	2.4%	75.3%	£16,429
Wastage (Barrels)			(7)	£545.98	£3.91	Barrels	£6,100	-0.7%	100.0%	£6,100
Sediment (Barrels)			(3)	£545.98	£3.91	Barrels	£2,609	-0.3%	100.0%	£2,609
Total Wet Trade							£421,749	45.8%	56.8%	£239,671

Although methods over the years may have evolved, the industry has always historically considered the impact of wastage covering both sediment and operational waste in regard to assessing rental values.

Question 5: If not, please explain your objections.

N/A

Sediment Waste

Question 6: Do you believe that these proposals will ensure that tied pub tenants have a clear and consistent approach to information about the volume of cask ales supplied under their agreement that will be unsaleable for reasons of sediment waste?

We believe that the proposals set out in 7.7 – 7.10 in the consultation document are at risk of introducing unnecessary complications into the regulations and relationship between a POB and the TPT. Specifically, the latter proposal in 7.7 regarding specific sediment by Product, would be overly complex in two ways:

- Prospective tenants would find a myriad of information which would be difficult to analyse;
- At present it is not possible for the POB to provide timely product specific information on direct deliveries via the Society of Independent Brewers (SIBA).

The intention of Schedule 2 is to ensure a TPT can make a fully informed decision regarding a proposed tied rent. As you can see from the example profit and loss statement detailed above, a TPT already receives considerably detailed information in order to fully understand how a valuer has arrived at their opinion of rent value. A TPT would also be expected to complete their own assessment of trade and retail selling prices for their business to enable a negotiation regarding rental value to take place.

Further to this, a TPT may not stock the same cask products as the hypothetical 'Reasonably Efficient Operator' (REO) that a valuer assumes. Therefore, an overall assumption of the level of waste or unsaleable cask product should be used. This is identified in the latter part of paragraph 7.7 as a 'consolidated allowance' as part of the rent assessment proposal.

Question 7: If not, please explain what additional or different approaches you think would ensure compliance with Pubs Code requirements.

This has been identified in answer 6 above. The approach of having a 'consolidated allowance' to cover unsaleable cask product is in our view the only practical solution in enabling a TPT to clearly understand the rent assessment proposal whilst aligning to the principles of the hypothetical REO as per the RICS rent valuation guidelines. The consolidated allowance applied should not be disproportionate to the available products and so an average allowance across the range of cask products available should be adopted.

At present Punch adopt an allowance of unsaleable liquid equivalent to 4 pints per 9g container (72 pints) within forecast profit and loss statements for the purpose of providing a rent assessment, however, across our range of available cask products the average unsaleable liquid is currently only equivalent to circa 2.1 pints per 9g (72 pints).

Question 8: Can you foresee any unintended ways in which these proposals might have a detrimental effect on tied pub tenants? If so, how might such effects be mitigated?

It is important to understand that a tied pub tenant will be receiving a large amount of information when taking on a pub or undergoing a rent review. The information identified in this consultation will only form a very small part of the issues and concerns that they will be taking on board as part of becoming a new publican or at a rent review. It is therefore critical that, whilst being completely transparent regarding the impact of the potential unsaleable liquid on the forecast profit and loss statement for the purpose of a rental valuation, the simplest way of expressing this is utilised.

The rent assessment proposal provides a clear assessment of the POB's opinion on rental value. However, a tied tenant may have a very different opinion of what they are likely to achieve through their own business plan. A commercial negotiation will take place between parties with a view to achieving a settlement of any differing opinions. As part of this Punch fully advocate TPT's obtaining their own independent, qualified and professional advice from accredited sources when engaging in negotiations regarding opinions of rental value and how such matters as those identified in these proposals can impact the profitability of their business.

Operational Waste

Question 9: Do you believe that these proposals will ensure that tied pub tenants have clear and consistent information about the volume of draught products supplied under their agreement that will be unsaleable for reasons of operational waste?

The proposals as laid out in paragraphs 7.11-7.16 seem contradictory, in firstly assuming that there is an assumption of the reasonably efficient operator (as per RICS Public House rental valuation guidelines) and then go on to highlight that one should not rely on generic assumptions. It is agreed that the individual characteristics for a property/business should be factored in (such as bar layout, number of beer pumps and line length to the cellar) but there should be no issues with assumptions being made in regard to the actions of the hypothetical reasonably efficient operator (REO) such as line cleaning frequency etc.

Question 10: If not, please explain what additional or different approaches you think would ensure compliance with Pubs Code requirements.

The Code already accounts for making allowances regarding Operational Waste via Schedule 2 paragraph 5(c). The approach of taking account of individual site characteristics such as bar layout, number of beer pumps and line length to the cellar when assessing operational waste more than adequately ensure this is fully considered and accounted for within rent valuations and proposals. The proposed approach seemingly over complicates an assessment without resulting in any benefit or difference to the calculation of rent being proposed.

So long as an allowance for operational wastage is made, considering assumptions of a REO as well as site specifics, the additional breakdown of this figure across the specified drink categories adds little value. This incorrectly assumes that operation waste is aligned to sales mix. The assumption regarding line cleaning is that a beer line would be cleaned (with operational waste) once per week regardless of if that line has dispensed 9g or 99g. The lead brewers, who own and maintain the beer lines expect cleaning to be conducted every 7 days. Punch currently make an allowance for operational waste within rent assessments based on this expectation.

Question 11: Can you foresee any unintended ways in which these proposals might have a detrimental effect on tied pub tenants? If so, how might such effects be mitigated?

The Code already accounts for making allowances regarding Operational Waste via Schedule 2 paragraph 5(c) in relation to assessing fair maintainable operating profit and rental value. Whether operational waste is accounted for by category, in adjusting the fair maintainable volume to reflect saleable volume, or whether an overall allowance is made as a deduction from the overall gross profit margin achievable, the result will be exactly the same.

The difference, however, in adopting a 'by category' approach will result in further complications within a rental assessment. In addition POB's will be faced with time consuming and costly changes to IT systems or Valuation models which have been in existence for many years. The approach for the Pub industry should be looking to remove red tape and complexity where possible.

These proposals seemingly look to further complicate matters in exchange for what seems to be no real benefit towards the overarching purpose for which such information is being provided.

Training and Support

Question 12: Do you have any comments on the proposed approach to access to training for tied pub tenants?

Punch welcome the approach in ensuring TPT's have access to the necessary training on cellar management, saleable volumes and dispensing best practice. Punch have recently opened up an industry leading Training Academy within our head office. This facility features two fully functioning bars and an operational cellar to allow on-site training to take place. Further to this our TPT's can currently also receive dedicated in-pub cellar training as part of their ingoing training package.

Given that such training is applicable across the industry it may be advisable to include such materials in the BII PEAT certification.

In regard to ongoing access to cellar management support in the form of stocktaking, technical and other professional services it is important to stress that the TPT operate their own business and will make commercial decisions regarding this of their own will. The requirement under the Code in Regulation 9 concerns Pre- Entry Training, the Code does not extend itself to prescribing ongoing support. As such, the level of services and support offered by each POB will form part of their individual competitive packages for their TPT's and will align to the commercial interests of each POB.

Question 13: Do you have any comments on the proposed training requirements in respect of BDMs?

Punch welcome the approach to ongoing Continuous Professional Development for our BDM's. Under the Code the definition of BDM can be wide reaching, due to catch all clause of including anyone who deals with current or future business plans. The requirement for training in regard to explaining and understanding the forecast profit and loss statements should therefore only apply to employees classified as BDM's who are directly involved with producing forecast profit and loss statements for the purposes of rental assessment.

Closing Comments

This consultation concerning 'Accounting for duty paid on alcohol and volumes of unsaleable draught products in Pubs Code forecast profit and loss statements' needs to be considered in context with the RICS guidance of rental valuation. Whilst the profits method is often utilised, it is only so as a secondary stage in the absence of comparable market transactions. In regard to the comparable method of valuation, an analysis of rents agreed for comparable property transactions is considered in arriving at a proposed rent, in this case the whole argument around detailed specifics such as the impact of unsaleable product and assessing gross profits disappears. Ultimately a rent is agreed between both the Landlord and the Tenant as a commercial property transaction following commercial negotiations.

Secondary to the above, it must also be remembered that this consultation concerns itself with ensuring, when utilising the profits method, that unsaleable product has been allowed for when a POB is producing a forecast profit and loss statement for the purpose of a rent assessment proposal. So long as this is accounted for in an understandable, fair and lawful manner, the difference in the

methodology currently being used and that proposed by this consultation will be little value. The only impact will be the risk of over-complicating a matter that actually would benefit from further simplicity.

The focus of this consultation only forms one very minor element amongst many pieces used in assessing a forecast profit and loss statement, further to this it must be remembered that this concerns one side of a commercial negotiation which is only decided once both parties reach a form of mutual agreement. Punch are fully supportive of ensuring TPT's can make fully informed decisions, however providing further complication and introducing a level of detail which is of little benefit seems to be counter-productive. Lastly, the proposals provide a risk of unnecessary detriment to smaller brewers by potentially being excluded from dealings due to bureaucracy and instilling a level of cost and changes within POB's ways of working.

In summary there appears to be very limited potential benefit from introducing the proposed changes, with a real risk of unnecessary complexity for all parties through disproportionate regulation.

Thank you for giving us the opportunity to represent our views in this process.

Office of the Pubs Code Adjudicator

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