TIED PUBS (SCOTLAND) BILL AT STAGE 2

PUBS ADVISORY SERVICE

A further comment on “investment” in pubs.

We asked the Financial Conduct Authority to look at the kinds of investments offered and advertised by Pub Companies.

These deals were typically that a significant sum of money would be invested in the premises by the owner, a lot of the published materials speak of shared partnership, co-investment, backing their publicans’ business etc.

The return for the pub company (on the money they allocate) is added to the rent and paid back over the remainder of the lease by the tenant operating the business, notably it is not added to any extra beer that might be sold.

The tenant is told that the uplift in rent is based on all the extra trade the pub will get and so will be more than covered by the uplift in customer sales (also give an increased reward for the tenant etc).
The tenant has a personal guarantee in place so any failure to get enough sales to meet the new higher rent will fall to the tenant 100%. The risk is not shared, any uplift is covered by the tenant, the pub company share of the uplift is baked into the rent as a fixed cost. It is notable that the pub company could have shared the return say by marking up the costs of any extra sales of beer, but that comes with a risk, so the pub companies do not attach the payback to the beer as it might be variable so instead they guarantee their share and bake it into the fixed cost / rent.

The FCA informed us that these deals did not meet their definition of an investment and were basically commercial loans, therefore despite the use of the wording investment it was unregulated and outside of their remit, the FCA could offer no redress to any tenant when any returns on the so-called investment fails to materialise. Or as sometimes happens, the sales rise but there is no extra profit and the tenant is now a “busy fool” earning just as much as they were when doing less trade. Further the regulators did not consider them loans either as they were being added to a lease/property agreement and not a standalone lending agreement.

I think the committee needs to be fully aware that these are unregulated investments creating a higher fixed cost but avoid being a loan too, there is no shared risk, it might be misunderstood by members which is understandable given the use of the word “investment” by the pub companies and their lobbyists.

So, the question, or rather the fear, expressed by some committee members is will investments be pulled from tenants if there is a Scottish code?

The answer is: a) they are not regulated investments b) they are not regulated loans c) the tenant bares all the risk d) there are far better commercial loan products at lower fixed cost from a wide group of providers who are covered by financial regulations unlike the pub companies acting as landlords to lend money with zero risk.

On the issue of regulation worth noting several pub companies hold a valid FCA registration for credit lending but do not wish to be under any regulation it when offering “investments” to tied pub tenants – it’s quite a loophole but it will cease to be an issue if tenants have a choice, whilst they remain tied they have no choice.