TIED PUBS (SCOTLAND) BILL AT STAGE 2

GREENE KING

Thank you for your letter dated 21 December and for giving us the opportunity to respond ahead of the Committee's commencement of Stage 2 for the Tied Pubs (Scotland) Bill.

As we set out in our submission to your Stage 1 inquiry, Greene King's overarching position is that the introduction of a statutory pubs code in Scotland is unnecessary and that this Bill should therefore be rejected. Alongside the fact that there is simply no evidence on the need for this Bill, we have significant concerns about the way the Bill is currently drafted and fear that it could cause irrevocable damage to Scotland's pub sector. Greene King has made the difficult decision to pause investment of £2 million in Scotland in 2021 due to the uncertainty caused by the Bill, which requires significant amendments if we are to reverse this decision and continue investment in our Scottish estate.

We welcome the opportunity to provide our views on key areas of concern within the Bill and to provide further evidence on the areas you outlined in your letter. Our primary concerns cover the following five areas, with details found in our full response included below this letter:

1. The lack of evidence around the need for legislation
2. The unprecedented powers the Bill provides to the Scottish Government to intervene in the pub sector
3. The ability to serve an MRO notice at any time, which will have a significant commercial impact on pub-owning businesses
4. The MRO provision introduces security of tenure by the backdoor
5. The requirement to offer a guest beer agreement, which could see profitable, commercial beers chosen over local, craft products

We are also calling on the Scottish Government to undertake an Economic Impact Assessment of the Bill as there are currently significant areas of the Bill where the financial impact on the sector is unclear. This will be essential evidence for the Committee during the Stage 2 process. This legislation has the potential to substantially alter the sector and must therefore not proceed until a full impact assessment is available.

All of the above mean that we also have grave concerns that the imposition of such statutory regulation is incompatible with our right to the peaceful enjoyment of our property, in breach of the European Convention of Human Rights and Article 1 of the First Protocol. Under the Scotland Act 1998, legislation passed by the Scottish Parliament must be compatible or it will be invalid and can be struck down by the Courts. We understand that the Scottish Parliament has a "margin of appreciation",

however, there is complete lack of evidence (as opposed to argument and campaigning) that there is a compelling need for the legislation in the first place and the Bill is not proportionate in its effects.

The current situation in Scotland, with the nation's pubs once more forced to close their doors as a result of the pandemic, is a deeply concerning time for the sector. We have so far provided around £3 million in rent concessions to our 120 tenanted pubs in Scotland since they closed last March, but with restrictions in some form expected to be in place for several months, even once pubs are reopened, it is essential that the sector is given the support it needs to survive. This Bill, with the added costs and bureaucracy it proposes, will only hinder the sector's recovery and threatens to see many Scottish pubs close for good.

Numerous MSPs, including the Minister for Business, Fair Work and Skills, noted the need for significant amendments during the Stage 1 debate, a view we wholeheartedly agree with. We would urge the Committee to consider the amendments needed to ensure the Bill has as little adverse impact on Scotland's pub sector as possible, which will not be the case if this Bill passes as currently drafted.

Please find below Greene King's response to the issues set out in your letter. Please do not hesitate to contact me if you have any further questions.

Economy, Energy and Fair Work Committee – Tied Pubs (Scotland) Bill
Response from Greene King – Stage 2
January 2021

About Greene King

- In Scotland Greene King is proud to employ over 2,600 people, at our brewery in Dunbar and in pubs across the country. We own just 120 pubs in Scotland which are covered by varying tie agreements - and we enjoy a strong and constructive relationship with our tenants. Since we acquired Belhaven in 2005, we have continually invested in our strong beer brands and developed our Scottish business. In 2018 Belhaven was named 'exporter of the year' at the Scottish Beer Awards and in 2019 celebrated its 300th birthday.

- Greene King also brews quality ale brands from our Dunbar and Bury St. Edmunds breweries, and is the UK's leading cask ale brewer and premium ale brewer with brands such as Belhaven Best, Greene King IPA, Old Speckled Hen and Abbot Ale.

GREENE KING

- Beyond Scotland, Greene King is the UK's leading brewer and pub retailer and has brewed our beer in Bury St. Edmunds, Suffolk and sold it through our pubs for over 200 years. Today we employ 38,000 people and we operate c. 2,700 managed and tenanted pubs, restaurants and hotels across England, Wales and Scotland. Our leading managed brands include Belhaven Pubs, Hungry Horse, Farmhouse Inns and Chef and Brewer.

- We are proud of our Scottish pub estate. That is why we have invested £6 million in the period 2017-20 and we plan to continue investing in Scotland subject to the recovery of our business following the coronavirus pandemic and the implementation of the Tied Pubs (Scotland Bill). The scale of our investment to date has been transformational for our tied pubs.

- In England and Wales Greene King is one of the six pub-owning businesses covered by the Statutory Pubs Code and Adjudicator due to the size of our tenanted estate. As of 31 March 2020, Greene King (through its various group companies) owned 828 tenanted pubs in England and Wales which are let out on a range of leases and tenancies. This represents approximately 10% of the tenanted tied pubs in England and Wales.

- Today, Greene King is recognised for the quality of its pub estate and the strong partnerships we have with our tied pub tenants. A key part of establishing this reputation has been our continued, significant level of investment in our tied estate and the value provided to tied pub tenants through the SCORFA[1] benefits. The type of support provided to Greene King tenants includes transformational investments, building repairs and decoration.

Summary

It is Greene King's strong belief that the Tied Pubs (Scotland) Bill is unnecessary and a flawed piece of legislation. As the Economy, Energy and Fair Work Committee concluded in its Stage 1 report, there is very little evidence to suggest that there is a wide-scale problem in Scotland regarding the relationship between tenants and landlords which would warrant legislation. As the Committee is aware, Scotland's tied pubs sector is already governed by a voluntary Code of Practice which offers tenants the same protections as English tenants of pub companies with fewer than 500 pubs.

As the Bill has now passed Stage 1, we have identified five key areas of concern with the Bill which we urge the Committee to consider during Stage 2:

[1] Special Commercial or Financial Advantages

1. **The lack of evidence around the need for legislation:** Greene King believes that there is simply no evidence on the need for this Bill and that efforts instead should be focused on encouraging all pub-owning businesses in Scotland to sign up to the voluntary Code. However, should the Bill proceed, it is essential that it is thoroughly amended to ensure its adverse impact on the pubs sector is as limited as possible.

2. **The unprecedented powers the Bill provides to the Scottish Government to intervene in the pub sector:** Clause 23 of the Bill appears to allow the Government to make substantial changes to the primary legislation of the Bill without going through the usual processes and scrutiny. We urge the Committee to carefully consider the extent of power accorded to the Government and to limit this based on common practice in Scottish legislation.

3. **The ability to serve an MRO notice at any time, which will have a significant commercial impact on pub-owning businesses:** We believe that the MRO provision should be removed from the Bill due to the uncertainty it causes, which will be a disincentive to investment in Scotland. Should an MRO provision be required, we believe it should be introduced at a later date once there has been a full and proper consultation on the details, a full Economic Impact Assessment, and time for the Scottish Pubs Code Adjudicator (SPCA)'s office to establish itself. It is also our strong view that an MRO provision should be restricted so there are specific events where a notice could be served, as in England and Wales.

4. **The MRO provision introduces security of tenure by the backdoor:** The Bill seems to introduce a form of security of tenure that does not currently exist in Scotland due to the ability of the SPCA to determine tied lease terms and for a pub tenant to extend his or her tenancy beyond the existing expiry date. This would give tied pubs a distinct advantage over free of tied pubs, the rest of the pubs industry and other hospitality businesses such as cafes, hotels and restaurants. It has wider implications for the commercial property sector in Scotland where there is no security of tenure and indeed the direction of travel is towards less regulation of business landlord and tenant relationships. This could well be seen as the start of the introduction of security of tenure in Scotland which would be a significant disincentive to investment in the country's commercial property sector.

5. **The requirement to offer a guest beer agreement, which could see profitable, commercial beers chosen over local, craft products:** We believe the provision requiring a guest beer agreement is unnecessary given most tied agreements already enable tenants to have a guest beer option that permits the sale of local draught beer. As currently drafted, the provision also risks tenants simply stocking their most profitable beer and so actually operate in a way which blocks an important existing route to market for small and local breweries in Scotland and reduces consumer choice. As currently drafted that beer would not even need to be a cask beer; it could be a keg beer or lager already supplied by the pub owning business and stocked by the

tenant. The report published by the Scottish Government in 2016 provides evidence that, given the choice, tenants will shop around and may simply use the option as a means of purchasing the same product elsewhere more cheaply and thus increasing their margin.[2]

Points 3-5 have also been raised by the Committee and therefore further detail can be found in response to the Committee's specific questions below. Points 3-4 are discussed under *Areas for further consideration as identified by the Committee's Stage 1 report: 4 – MRO Option* (p.10-13) while point 5 is discussed under *Areas for further consideration as identified by the Committee's Stage 1 report: 3 – Guest beer agreement* (p.9-10).

However, we also welcome this opportunity to share our views on points 1-2 which are set out below.

1. The lack of evidence around the need for legislation

While the Bill aims to promote a fair relationship between tenant and landlord, and ensure tied tenants are no worse off than if they were free of tie, there is simply a lack of evidence to suggest that these are issues in Scotland that require the intervention of legislation. The report commissioned by the Scottish Government's and published in 2016 on the sector stated that the evidence collected "did not suggest that any part of the pub sector in Scotland was unfairly disadvantaged".

The Bill attempts to tackle a problem that does not exist through legislation, a process that will only add further costs and red tape for pubs at a time when the sector is suffering severely from the impact of Covid-19 and associated restrictions. Indeed, the Economy, Energy and Fair Work Committee concluded in its Stage 1 report that there was insufficient evidence to suggest that there were adequate grounds to warrant legislative interference in contractual agreements.

Scotland's tied pub sector is already governed by a voluntary Code of Practice which has been in place since 2016 and which was strengthened in 2019. This Code contains the same protections for Scottish tied tenants as English tied tenants of pub companies with fewer than 500 pubs and successfully fosters good relationships between pub companies and tenants. Since the voluntary Code was introduced, there have been no complaints by tenants against Greene King through the PICA-Service, which is testimony to our positive relationship with our tenants.
We believe that the Bill has not been thoroughly thought through, nor its impact properly assessed. The Scottish Government must undertake a proper economic impact assessment – as is the norm for primary legislation at Westminster – before this Bill proceeds, given the significant areas of the Bill where the impact is unclear. This will be critical evidence for the Committee to consider during the Stage 2 process.

[2] The Scottish Government, Research on the Pub Sector in Scotland – Phase 1 'Scoping Study', 2016

Instead reliance is placed on the fact that there is legislation in England and Wales. We would refer the Committee to the documents provided with this submission which set out the history of the Pubs Code in England and Wales and how MRO came to form part of the legislation. Contrary to what has been indicated in the Policy Memorandum, there never was a clear and compelling evidence-based case for MRO in England and Wales. Rather it was the result of a dramatic U-turn by the then Business Secretary, Vince Cable.

This Bill has the potential to fundamentally change the Scottish pubs market and it is critical that all possible analysis and assessment is undertaken before it proceeds. This requires a full economic impact assessment to be undertaken and a proper assessment of its effect on human rights, including any potential contravention of Convention rights if we are to avoid causing irrevocable damage to the sector.

All of the above mean that we also have grave concerns that the imposition of such statutory regulation is incompatible with our right to the peaceful enjoyment of our property, in breach of the European Convention of Human Rights and Article 1 of the First Protocol. Under the Scotland Act 1998, legislation passed by the Scottish Parliament must be compatible or it will be invalid and can be struck down by the Courts. We understand that the Scottish Parliament has a "margin of appreciation", however, there is complete lack of evidence (as opposed to argument and campaigning) that there is a compelling need for the legislation in the first place and the Bill is not proportionate in its effects.

2. The unprecedented powers the Bill provides to the Scottish Government to intervene in the pub sector

Despite seeking to mirror the Tied Pubs Code in England and Wales, the Tied Pubs (Scotland) Bill gives the Scottish Government far more power to intervene in the sector. Clause 23 (Ancillary provision) of the Bill gives the Scottish Government the power by regulations to *"make any incidental, supplementary, consequential, transitional, transitory or saving provision they consider appropriate for the purposes of, or in connection with, or for giving full effect to this Act of any provision made under it."* It adds that *"regulations under this section may modify any enactment (including this Act)."* This clause (known as an "Henry VIII clause") would allow the Government to make substantial changes to the primary legislation, without going through the same process and scrutiny of passing primary legislation. It would also enable the Government to amend other legislation that might be affected by the Bill.

It is our strong view that the Economy, Energy and Fair Work Committee must carefully consider the extent of power accorded to the Government through this provision and to limit this based on common practice in Scottish legislation.

This has been highlighted by the Delegated Powers and Law Reform Committee in its Stage 1 report as an area of concern.
While the Bill's Delegated Powers Memorandum justifies Clause 23 due to the *"possible requirement to make further provision over time as the new legislation establishes itself"* or where *"other unexpected circumstances arise which require a legislative solution"*, this does not justify giving the Scottish Government carte blanche to introduce significant changes through secondary legislation and to amend primary legislation. The extent of the powers provided to the Government are unprecedented and the lack of scrutiny must not go unchallenged.

Potential areas of amendment as identified by the Minister for Business, Fair Work and Skills

1. **Lengthening the implementation and review the timescales for the Scottish Pubs Code**

We agree with the Minister that if a statutory code were to be implemented, it must be transparent, fair and properly consulted on. This Bill has the potential to change the Scottish pubs market fundamentally and it must not be implemented without a full economic impact assessment having been undertaken. There are also significant areas within the Bill that require consultation, including the implementation of a statutory code, and the MRO provision.

As the Minister also stated, the industry is still dealing with Covid-19, with all our pubs once again closed across Scotland. Even once we begin to reopen, it is likely that some level of restrictions will be in place for several months. With the pubs sector on its knees and time and energies devoted entirely to the survival of our industry, now is the worst possible time to be introducing new, costly and bureaucratic legislation. It will also only serve to undermine investment in the sector, when investment will be needed more than ever to fuel the recovery and ensure local communities do not lose the pubs they love. Greene King has made the difficult decision to pause investment of £2 million in Scotland in 2021 due to the uncertainty caused by the Bill, which requires significant amendments if we are to reverse this decision and continue investment in our Scottish estate.

As such, we agree with the Minister's assertion that – if this Bill were to be passed – more time would be needed to consult fully on the secondary legislation before it comes into effect. This will require more than the one year proposed in the Bill between the legislation passing and a Pubs Code being laid before Parliament.

Indeed, in England and Wales we found that the lack of transition period presented huge difficulties for the pub-owning businesses and the Pubs Code Adjudicator, particularly following the way in which the original legislation was passed, via an amendment to the Bill through the House of Commons, which generated challenges. I would refer you to the briefing paper attached which provides more detail on this. The first version of the Pubs Code was flawed as it failed to take account of landlord and tenant law and security of tenure issues and the final version was only produced

late in the day. It meant that by the time that the Pubs Code came into effect, neither pub-owning businesses, tied tenants nor their advisers had proper time to prepare and to understand what it actually provided for. This was demonstrated in the high number of MRO-related referrals made to the PCA early on which then took many months (and in some cases years) to resolve.

There is no doubt that a transition period to support pub-owning businesses, tied tenants and the PCA would have supported a more successful start in understanding the requirements of a complex piece of legislation and enabled time for the development of pub-owning businesses' back-office processes and systems, staff-

> If this Bill is passed, much more time is needed than is currently proposed to fully consult on the statutory code before it is implemented. This is essential to avoid the problems we saw in England and Wales and to ensure pub companies have sufficient time to recover from the Covid-19 crisis. A rushed implementation of ill-thought through legislation will cause potentially irrevocable damage to the sector.

training and documentation.

Finally, any implementation date must also consider the sector's recovery from Covid-19. Otherwise, there is a very real risk that it could cause irrevocable damage to the industry.

2. The removal of elements of retrospection

The Bill's definition of a tied tenant includes *"a person who has been the tenant under the lease of a tied pub"*. This would give former tenants, including those who have had only a short-term agreement, the ability to require the SPCA to investigate an old contract. It is unclear why the Bill seeks to intervene in a relationship that no longer exists between tenant and landlord and raises the possibility that cases will be brought before the SPCA by former tenants who have potentially had no agreement with the pub-owning business for several years.

This will only cause even greater uncertainty for pub companies in Scotland, with the prospect of costly and time-consuming cases acting as a further disincentive to investment in Scottish pubs.

> We agree with the Minister that any elements of retrospection must be removed from the Bill. Only once a statutory code is implemented should it be applicable to current and new agreements, not those that have already ended.

3. Measures to ensure that levies on pub companies are proportionate

As outlined above, this is a critical time for the pubs industry, with Covid-19 draining resources and investment essential to the sector's recovery. The creation of the Bill will only divert pub company money from capital investment budgets into a levy that

is entirely unnecessary at a time when continued investment is needed to ensure a healthy vibrant pub sector in Scotland in the wake of the pandemic.

To ensure levies are proportionate and do not become an unmanageable burden for pub companies, we believe that there should be a cap on levy payments, which should be set by Scottish Ministers. This would also avoid scenarios were the levy increases year on year due to an underestimation of the costs of the SPCA. In England and Wales, we have seen the levy increase year-on-year with very little information as to the rationale of these increases. The levy methodology in England and Wales has also changed over time. The first year of the levy was based on the number of pubs operated by the pub-owning business. It then changed to the number of pubs operated plus the number of referrals that had been made. It is now based on the number of pubs operated and the amount of time the PCA spends on individual pub-owning business matters. These continual changes cause uncertainty for pub-owning businesses, who risk being faced with burdensome and disproportionate costs – a situation we would want to avoid in Scotland.

There is a risk that levy payments will be disproportionate and will be an additional burden for a sector that will still be recovering from Covid-19. To avoid this, and any potential year-on-year changes, we believe that there should be a cap on levy payments, which should be set by Scottish Ministers.

Areas for further consideration as identified by the Committee's Stage 1 report

1. **Thresholds:** *The Bill proposes that the Scottish Pubs Code will apply to all pub-owning businesses; in England and Wales the Pubs Code applies to pub-owning companies who have more than 500 pubs. The Committee heard differing views at Stage 1 on whether a threshold should be applied in Scotland*

It is our view that no de minimis requirement has been included in this Bill because to do so would shrink the market regulated by the Bill even further than the c. 750 tied pubs currently operating in Scotland. It is therefore clearly questionable whether any legislation at all is necessary for such a small proportion of the sector.

The tied pub market in Scotland is far smaller than that in England and Wales. Any introduction of a de minimis requirement would mean only a small proportion of the tied pubs market would be regulated by the Bill, making it questionable whether legislation is needed.

2. **Court appeal process:** *Stage 1 evidence from the Scottish Courts and Tribunal Service noted problems with the appeal process; the member in charge indicated that this could be revisited during Stage 2*

Greene King has no comment to make on this point.

3. **Guest beer agreement:** *consideration of whether any restrictions should be placed on the guest beer agreement to help small local producers access the market*

The guest beer requirement included within the Tied Pubs (Scotland) Bill goes further than the Pubs Code in England and Wales, where no such provision is included. The financial impact of this proposal is unclear.

Typically, a guest beer concession would only allow a draught 'craft' beer that would increase customer choice; this has generally been used to allow small brewers a route to market under arrangements with the Society of Independent Brewers (SIBA). As currently drafted, the provision risks tenants simply stocking their most profitable beer and so actually operate in a way which blocks this important route to market and reduces consumer choice. As currently drafted that beer would not even need to be a cask beer; it could be a keg beer or lager already supplied by the pub owning business and stocked by the tenant. The report published by the Scottish Government in 2016 referred to above provides evidence that, given the choice, tenants will shop around and may simply use this option as a means of purchasing the same product elsewhere more cheaply and thus increasing their margin.[3] This would have no benefit at all for small and local breweries in Scotland and would also reduce customer choice, instead of increasing it as is clearly the intention behind this provision.

It is Greene King's view that this provision has not been fully thought through. We believe that it is in fact unnecessary as it is difficult to understand how the requirement will make a substantial improvement to the choice our tenants already enjoy:

- Specifically, on beer, Greene King offers a wide range of guest beer products that tenants can choose from. Currently 10% of our estate in Scotland have free-of-tie guest beer lines.
- 80% of Greene King tenants rate the current range available as very good or good. This suggests that, at present, there are no major concerns regarding the product range available through Greene King for tenants.[4]
- In addition, we are signatories to the voluntary Scottish Code of Practice which allows tenants greater flexibility over the choice of local beers and ales that they wish to stock.
- This proposal also fails to acknowledge the huge variety of tied agreements in Scotland (again, only one of our 120 pubs in Scotland is fully tied). The majority of tied pubs already have the flexibility to introduce guest beers.
- All our pubs in Scotland also have the option to use SIBA's services to stock guest beers, giving our Scottish pubs greater flexibility than many in England.

[3] The Scottish Government, Research on the Pub Sector in Scotland – Phase 1 'Scoping Study', 2016 at Section 4.4

[4] Independent research by Kam-Media

However, should this provision remain in the Bill, we believe that the requirement to offer a guest beer agreement should be based on the number of existing lines sold by the tenant and on evidence from the tenant that customers are disadvantaged by the lack of a guest beer or that the tenant has lost sales due to no guest beer being on offer. We would also prefer to see the requirement amended to offer only one draught line that is not stocked by the landlord, and to include local parameters such as the guest beer being brewed within five miles of the tied pub, unless specific approval is granted by the pub company.

This would ensure that tenants do not simply look to stock well-known and widely available beers from large brewers but would support the local economy by stocking beers from small or local breweries, in turn giving customers more choice.

With most tied tenants already having the option to stock guest beer products, we believe the guest beer requirement is unnecessary. If the provision remains in the Bill, it must be amended to ensure small and craft breweries do not lose out to commercial lagers.

4. **MRO option:** *there are differences between the MRO option in England and Wales and the proposals for Scotland; consideration of whether the changes proposed are proportionate and whether they will address the issues reported with the 2015 legislation*

We strongly believe that the MRO provision should be removed from the Bill. The uncertainty it causes will be a significant disincentive to investment in Scotland and it is entirely possible that this would see the beginning of the end of the Scottish tenanted market, with pubs simply closed or brought back under management to remove any threat to lose out on any return on investment. This has been evident in England and Wales where there has been a sharp increase in the number of managed premises across the industry. Greene King has already made the difficult decision to pause investment of £2 million in Scotland in 2021 due to the uncertainty caused by this legislation until there is further clarity about what the future looks like.

We also refer the Committee to the attached report from Mr Fraser Clearie. Mr Clearie (a Partner at Riddell Thoms & Company) is a senior and respected member of the RICS in Scotland and a senior authority on the Scottish commercial property market. In his report he expresses concern the Bill may undermine investment in:

(a) the Scottish tied pub sector by i) removal of certainty of rental income for guaranteed period; ii) removal of certainty of income for a guaranteed period; iii) possible disincentives to investment and redevelopment of pubs. If the attractiveness of the tied pub model in Scotland declines, pub companies and brewers may turn their investment instead towards non-tied pub tenancies,

choose to bring pubs into their managed estate or pull out of the tied sector in Scotland altogether.[5]

(b) The wider commercial property market. The absence of regulation of commercial leases and tenancies in Scotland (compared to the rest of the UK) is perceived to be an advantage by investors. Introducing this type of statutory protection for a relatively small element of the hospitality sector would be of concern to investors as to what it might herald. As the work of the Scottish Law Commission[6] shows, greater regulation of such a small element is out of kilter with the direction of travel of the remainder of the commercial property market which is in the opposite direction, namely even less regulation of commercial landlord and tenant law (such as through the abolition of the Tenancy of Shops (Scotland) Act 1949 and the freedom to contract out of tacit relocation)

If an MRO provision is required, it must be introduced at a later date once there has been a full and proper consultation on the details, a full economic impact assessment undertaken, and time for the SPCA's office to establish itself. Such a fundamental change to the Scottish pubs sector must not be rushed through and its impact must be fully assessed before any legislation is brought forward.
As outlined previously is this document, we are also concerned that the imposition of such statutory regulation is incompatible with our right to the peaceful enjoyment of our property, in breach of the European Convention of Human Rights and Article 1 of the First Protocol. There must be a proper assessment of its effect on human rights, including any potential contravention of Convention rights if we are to avoid causing irrevocable damage to the sector.

Delaying the introduction of an MRO provision would also prevent a repeat of the situation in England and Wales, which saw a large number of MRO-related referrals soon after the introduction of the PCA, which overloaded the system and resulted in the slow production of arbitration awards. It absorbed a large amount of time and overshadowed all the other positive elements of the Code, such as provision of information, Business Development Manager (BDM) discussion notes, streamlined procedures for rent reviews and agreement renewals. It was only when the PCA appointed a deputy that progress was made to clear the backlog. Out of 420 referrals accepted by the PCA between July 2016 and June 2020, 369 (88%) were related to MRO. Disputes about the reasonableness of the MRO terms offered by pub-owning businesses dominated the PCA's arbitration caseload throughout the statutory review period. Indeed, the PCA's statutory review submission made in July 2019 had eight pages of a 13-page document taken up with MRO matters, further demonstrating the MRO issues and difficulties experienced in England and Wales.

[5] Fraser W. Clearie, Report on the Tied Pubs (Scotland) Bill & the issue of security of tenure, 2021
[6] Scottish Law Commission's *"Discussion Paper on Aspects of Leases: Termination"* dated May 2018

The ability to serve an MRO notice at any time

We are particularly concerned with the provision that would enable a tenant to apply for an MRO contract at any time. This goes much further than the statutory code in England and Wales, where there are a limited number of occasions where a tied tenant can serve an MRO notice, for example, when a tenant is notified of a significant increase in the price at which a tied product or tied service is supplied. This ability to serve an MRO notice at any time will be a substantial disincentive to investment in the Scottish sector by pub companies, with many likely to decide simply to turn tied pubs into managed pubs or to sell some of their estate. This would have a significant impact on the sector, particularly on small and large breweries which often rely on tied pubs as a route to market. Indeed pub companies and brewers such as ourselves have already put on hold any investment pending the outcome of this legislative process.

If an MRO provision is to be brought forward (once a full and proper consultation has taken place), it is our belief that it should mirror the provisions in the English Code, in so far as setting a limited number of events where an MRO notice could be served. It is our belief that the right to serve an MRO notice at any time has been included in the draft of the Bill as linking an MRO request to a specific event is likely to mean the number will be very small – as we have seen in England and Wales. Indeed, in England and Wales since July 2016, Greene King has received only 126 valid MRO requests, the majority of which were received in the first year of the commencement of the Code, of which 9 MRO agreements were granted. To date there are only 7 'live' MRO agreements currently in our estate, and only 16 valid MRO requests received in the last reporting year (01 April 2019 to 31 March 2020). With the number of tied pubs in Scotland significantly smaller, this only further demonstrates how unnecessary this Bill is, and particularly this specific provision.

We would also point the Committee to the outcomes of the MRO requests that have been put forward in England and Wales since July 2016. Out of 126 MRO notices accepted by Greene King, 83 tenants remain in-situ on improved tied agreements, rather than choosing to go free of tie. This is reflected across the industry, where 62% of tenants have remained tied, left, or another outcome has been achieved (such as withdrawn from the process). Only 13% have chosen to go MRO. This brings in to question the need for the MRO at all, when in our experience the majority of tenants have simply used the process to secure a better tied deal.

The introduction of security of tenure by the back door

Under the Bill's third principle of the fair share of risk and reward between the landlord and tenant, we could also see the SPCA given the power to determine both tied lease terms. This would usher in a form of statutory protection for tenants that does not currently exist in Scotland.

Unlike in England under the 1954 Landlord and Tenant Act, there is no security of tenure in Scotland for business tenants. MRO creates this if Scotland adopts the same approach to terms (lease lengths) as in England, because a pub-owning business would be required to offer a term that is both reasonable and common. This would potentially mean that if a tenant served an MRO notice on the last day of its term, the pub company would have to offer a term of years that would extend beyond the lease term. This would unintentionally give tied tenants security of tenure because a pub-owning business would have to be able to justify why it refused to grant a new agreement to the tenant if challenged. This could look very like the grounds of opposition under Section 30(1) of the 1954 Act. Should the SPCA be given the power to determine tied lease terms, this would be a form of security of tenure that is not available to any other type of business tenant, whether in the hospitality sector or beyond, in Scotland.

As noted by Mr Clearie in his report, the consequence for the pub sector would be that tied tenants are put in a substantially better position than their free-of-tie counterparts or those who own a pub on a freehold basis.[7] Tied tenants would also be given an advantage over the entire rest of the hospitality sector. It has wider implications for the commercial property sector in Scotland where there is no security of tenure. It is unclear what the policy rationale is for introducing statutory protection for certain types of business tenants and not others, and for introducing through the 'back door'. It would also appear to go against the views of the Scottish Government and investors, who believe that the lack of statutory regulation governing landlord and tenant relationships in Scotland has encouraged investment in the country's commercial leasing sector, investment that could be significantly reduced if this Bill passes as it is currently drafted.[8]

This could well be viewed as the start of security of tenure being introduced for all commercial tenants in Scotland, acting as a major disincentive to investment in Scotland's commercial property market. With the statutory Pubs Code in England and Wales so inextricably linked to the 1954 Act, any attempt to simply replicate this in Scotland where there is no equivalent legislation will be extremely difficult.

The MRO provision as currently drafted is not fit for purpose. It is already causing uncertainty for the industry, with Greene King pausing investment in Scotland in 2021. The ability to serve an MRO notice at any time, and the potential introduction of security of tenure, are severe disincentives to investment in the Scottish pubs market and could have far-reaching consequences for Scotland's wider commercial property market.

Any MRO provision must be introduced at a later date once there has been a full consultation on the details and a full economic impact assessment. It is critical that such a fundamental change to the Scottish pubs sector is not to be rushed through.

[7] Fraser W. Clearie, Report on the Tied Pubs (Scotland) Bill & the issue of security of tenure, 2021

[8] Scottish Law Commission Annual Report 2019

The report from Mr Clearie additionally notes that conferring any special concessions – such as security of tenure and MRO at any time – on one category of business may lead to calls for similar treatment by other hospitality and retail businesses. This would potentially dramatically change Scots Law in way that is unlikely to have been intended by this Bill.[9]

Further areas identified by the members of the Committee

1. Clarity on the exact income that tied pub tenants receive

We believe that the tied model is fair and works well for both tenant and landlord. The tied system continues to provide the best opportunity for prospective tenants across Scotland to be able to enter the industry and be supported to run a successful pub. The tied partnership model is designed to be an effective and attractive option for new entrants, providing a low-cost entry into the pub sector, allowing entrepreneurs to grow and flourish.

At Greene King we view our pub tenants very much as entrepreneurs – with their success inextricably linked to our own. And we pride ourselves in providing business development support to help them thrive, including management advice, brand and outlet promotion support and marketing as well as business rates advice, licensing and legal support.

In contrast to misleading allegations made during the Stage 1 consideration of the Bill around low incomes faced by tied tenants, the average income for Greene King's tenants in Scotland exceeds the industry average of £44,240, as estimated by the SBPA. This is based on pre-pandemic levels of income, with the closure of pubs and significant restrictions on our ability to serve customers having a profound impact, as has been the case for all hospitality businesses.

We are proud of the relationship we have with our pub partners and believe that the tied model is fair for both tenant and landlord. We do not believe that there are significant issues with the level of income for the vast majority of tenants in Scotland, in contrast to some allegations raised by proponents of the Bill during Stage 1.

2. Reasons for the divergence of views of tied pub tenants on the need for the bill

Differences of opinion and divergence of views must be expected in any market. However, we are proud of the positive relationships Greene King has with its tenants. For pub companies like Greene King, the tied model is an essential part of

[9] Fraser W. Clearie, Report on the Tied Pubs (Scotland) Bill & the issue of security of tenure, 2021

being a successful business and has adapted over the years to offer flexible, transparent, and competitive agreements to our tenants.

Integral to the success of the tied pub system at Greene King is the key role played by our Business Development Managers (BDMs). The BDM acts as a personal business consultant, undertaking business development reviews, looking at different ways to advise the tenant in their business to build both sales and profit, and to improve the overall business performance. They would typically discuss areas including product range, margin management, marketing support, social media, training opportunities for them and their team and potential investment opportunities. It is important that the BDM is aware of the local trading markets and so they will often be reviewing competitor venues and sharing their findings with the tied tenants. They will also meet with new prospective tenants, as recruiting the right type and calibre of tenant is vitally important. They are the lifeblood of our business and it is important to ensure any new prospective tenant understands what it means to run their own pub business. In addition, the BDM will provide ongoing day-to-day support with matters such as general marketing and promotional support, rent review and agreements renewal information, as well as supporting newly appointed tenants and those who may be exiting.
A free-of-tie lease provides none of these benefits. In England and Wales, tenants recognise this value and that is why so few have decided to take up the opportunity to remove themselves from the tied partnership model, despite being aware of the opportunity to do so at the point of their rent review and agreement renewal. At present, in Scotland, 78% of Greene King tenants describe their current relationship with their BDM as very good or good, underpinning the value of the support that they receive.

It is also important to note that since the inception of the Code in 2016, there have been no complaints by tenants against Greene King through the PICA-Service, which is testimony to our positive relationship with our tenants.

While there will be differing views in any market, it is our belief that the tied model is fair and works well for both tenant and landlord. This has been demonstrated by our experience in England and Wales where the vast majority of tenants choose to remain a tied partner rather than going free of tie when this option is available to them.

3. The level of investment put on hold due to the pandemic

Greene King invested £6 million in our Scottish pub estate in the period 2017-20. This is a total investment equivalent to more than £66,000 in each of our 120 pubs. While we had planned to invest further depending on the recovery from the pandemic, we have been forced to make the difficult decision to pause investment of £2 million in Scotland in 2021 due to the uncertainty caused by this legislation until there is further clarity about what the future looks like.

However, we continue to support our tenants throughout the pandemic. Since pubs closed on 20th March last year, we have provided around £3 million in rent concessions to our 120 leased and tenanted pubs in Scotland – including a 90% rent concession for our pubs in Level 2, 3 or 4 areas (and a 45% rent credit for pubs in Level 0 or 1 areas). This 90% rent support has continued during the current period of lockdown, imposed on 4 January 2021, and will remain in place until these measures are lifted.

This support, which will help our tenants' businesses survive and recover from the global pandemic, would otherwise be unavailable if they were not part of the tied model. In advance of pubs reopening last summer, we provided tenants with an estimated £50,000 of product support, including the replacement of kegs and casks for unopened barrels that would have been out of date when pubs reopened and discounts for tied tenants on kegs/casks purchased for the first eight weeks of reopening. In addition, we provided £30,000 of PPE starter kits to all tenanted pubs and £14,400 of Covid-19 safety signage for pubs.

The support Greene King has provided to its tenants is almost entirely unique to the tied pub model and is in stark contrast to the lack of support provided by many commercial landlords to hospitality businesses throughout the pandemic. We had intended to recommence investment in Scotland subject to the recovery from the Covid-19, but have made the difficult decision to pause this for 2021 while uncertainty around this legislation remains.

4. Support received by non-tied pub tenants from their landlords during the pandemic

The tied and non-tied model operate differently with different benefits, and this is also the case in terms of support received by tenants. A non-tied tenancy is an arms-length relationship that does not have the same SCORFA benefits as a tied relationship. This means that non-tied tenants do not benefit from the same financial support as tied tenants as there is no direct interest by the pub company in the trading of the business.

However, during the pandemic, we have put in place deferred and affordable rent payment plans for those non-tied tenants most in need of support. As outlined in our answer above, we have provided substantial support to our tied tenants during the pandemic, including 90% rent concessions. This level of support simply would not be available to those pubs who may choose to go free-of-tie under this Bill if a similar situation to the Covid-19 pandemic happens in the future.

The tied and non-tied model operate differently and with different benefits. While we have put in place deferred and affordable rent payment plans for those non-tied tenants most in need of support during the Covid-19 pandemic, we have provided substantial support to our tied tenants. This level of support simply would not be available to those pubs who may choose to go free-of-tie under this Bill should a similar situation happen in the future.

The support we have offered to all our tenants, tied and non-tied, is in stark contrast to other commercial landlords. As a tenant ourselves with over 500 landlords across the UK, we have not received rent concessions to the same extent of those we are offering to our tenants.

5. Whether an MRO option is applicable in other sectors, and if so, what impact has it had

Greene King is not aware of any other sector where one party to a commercial contract has the ability to radically alter the terms of the contract with the other party in the way this Bill would provide through the MRO provision.

Riddell Thoms Company
Chartered Surveyors and Property Consultants

21st January 2021

Alan McNeil BSC MRICS
Acquisitions & Estate Manager
Greene King Limited

By email:

Dear Sir

Tied Pubs (Scotland) Bill: Issue of security of tenure

You have explained that your organisation intends to make representations to Scottish Government concerning the above matter.

As part of that process, your company has significant concerns as to the impact of the Bill in the Scottish commercial property market.

You have requested my opinion on three property market related concerns that arise from the Bill:

- A brief reminder of the contractual relationship between landlords and tenants of commercial property in Scotland, focussing on security of tenure for tenants. Related comment on the ongoing work of the Scottish Law Commission and observations on the possible implications of the Tied Pubs (Scotland) Bill.

- The potential impact of the Bill on the attractiveness of investing in Tied Pubs.

- Implications for non-Tied Pubs and cafes, restaurants, and possibly shops.

INTRODUCTION

1. The opinions that follow are based on my professional qualifications and 40 years of experience working in the Scottish commercial property market.

2. I am a Fellow of the Royal Institution of Chartered Surveyors and Member of the Chartered Institute of Arbitrators.

3. I am widely recognised within the profession as a specialist in Scottish commercial property landlord and tenant matters, in particular, rent reviews, lease advisory and renewals.

4. In the last 20 years I have been appointed arbitrator, or as an independent expert, and resolved in excess of 60, rental or capital value, disputes that have ranged from multi-million pound claims to modest value cases involving neighbourhood shops.

5. Past and present clients include, [redaction].

LANDLORD AND TENANT RELATIONSHIPS IN SCOTLAND

6. There are important practical differences between the statutes which govern commercial property Landlord and Tenant relationships in England and leasehold law in Scotland. These differences ought to be appreciated when contemplating changes to security of tenure for one class of business.

7. Tenants of commercial property in Scotland depend upon the terms of the contractual arrangement (lease) which prescribes, amongst other terms, the duration, the rent, and basis for any reviews. With limited exceptions, which I will mention shortly, a tenant in Scotland has no security of tenure beyond the contractual period of the lease.

8. The position in England is fundamentally different. Commercial property tenants there have the option of benefiting from statutory protection at the end of the lease period to address (a) continued security of tenure and (b) independently assessed market rents. This is achieved by virtue of the Landlord & Tenant Acts (in particular, the Landlord and Tenant Act 1954), which do not apply in Scotland.

9. Companies based in England with business premises throughout the UK often presume that the law will be the same in Scotland and they are shocked to find no security of tenure beyond the lease expiry date.

10. Furthermore, unlike in England where a tenant may apply (upon expiry) to the Courts to determine a market rent for a continuation of the tenancy, the law in Scotland offers no such protection.

11. In Scotland, tenants and landlords are generally left to negotiate their own terms. In theory, lease renewal negotiations ought to reflect the prevailing market dynamics of supply and demand. It should mean that, if there is excess demand for tenancy, a landlord might press for more rent and greater commitment from a tenant. Conversely, if demand was weaker, rent and terms should be 'softer'.

12. However, market regulation of lease renewal negotiations is frequently 'tainted' by another consideration. Sitting tenants generally make significant investments in their leaseholds (fitting out works, goodwill, licence, etc) and there is no compensation on the expiry of a lease. Tenants seeking to protect their investment by renewing their tenancy, have negligible statutory protection. For this reason, lease expiry/renewal negotiations in Scotland typically disadvantage tenants and benefit landlords.

13. In England, the Landlord & Tenant Acts help to shield tenants' investment in fittings, goodwill, etc, by assuring a continued period of tenure at a rent based on recent market lettings of vacant property – excluding over-bids to protect investment.

14. These critical differences in security of tenure, between Scotland and England, need to be properly understood when contemplating this Bill.

15. There are two limited exceptions to the absence of 'security of tenure' for commercial tenants in Scotland and these are Tacit Relocation and The Tenancy of Shops (Scotland) Act 1949.

16. Under the principle of Tacit Relocation, notwithstanding the date of expiry of a Scottish lease, it will only be terminated if either party serves a valid Notice to Quit upon the other party. Failing a valid Notice, the lease and all rights and obligations, including rent, continue for another year.

17. The other exception is The Tenancy of Shops (Scotland) Act 1949. It enables a qualifying tenant to apply to the court for protection of their business tenancy for a year after the expiry date. The Court must consider each case on its merits. In recent years, there are few published examples of tenants being successful and managing to continue their occupation by this Act.

18. **It has been recognised that Tacit Relocation and the 1949 Act slightly blur the principle of contractual certainty which is a keystone of law of leases in Scotland.**

19. **The issue clarity was important enough to merit a review by the Scottish Law Commission (SLC) of Scots law on security of tenure. As they state on their website the SLC:**

    "...was established under the Law Commissions Act 1965 to make recommendations to Government to simplify, modernise and improve Scots law. Over the last 50 years the Commission has been at the forefront of major changes to Scots law".

    The documents published by SLC in relation to that review and the responses of consultees are relevant to the Market Only Rent and associated security of tenure elements of the Bill.

20. In May 2018, SLC published a Discussion Paper which was topical to the issue of Termination (security of tenure) for commercial property in Scotland. The report, Aspects of Scottish Leases[10], prompted feedback from multiple-unit business tenants and landlords. The consultation period for the report closed in September 2018 and SLC's website currently indicates that a draft report and bill is being prepared.

21. SLC's recommendations focus on the merits of having clarity on lease terminations in Scotland and this could be achieved by abolishing Tacit Relocation and the 1949 Act.

22. I take from this that SLC, and many who provided feedback, are **content to reinforce the absence of statutory security of tenure protection in Scotland. In summary, tenants of commercial property in Scotland should generally have no rights beyond those specified in the lease.**

23. You are concerned that in its present form, the Bill will introduce a form of security of tenure for a limited class of business tenants, namely the tenants of Tied Pubs. Such a move seems contradictory to the views of the SLC, whose role is to advise the Scottish Government on law reform.

[10] https://www.scotlawcom.gov.uk/files/4215/2699/8107/Discussion_Paper_on_Aspects_of_Leases_-_Termination_DP_No_165.pdf

24. Under the Bill as proposed:

    a. Tied Pub tenants are entitled to call for a new lease on a free of tie rent **at any time**.

    b. The terms of the new lease must be common and they must be reasonable. In England and Wales, the Pubs Code Adjudicator, in interpreting the legislation that applies in that jurisdiction, has made it clear that the term (i.e. the duration of the lease offered) must be reasonable and not simply the unexpired residue of the existing lease term.

    c. The effect is that, in order to comply with the provisions of the legislation, a landlord may have to offer a Tied Pub tenant a free of tie lease that will continue their tenancy beyond the existing expiry date. The prospect of this becomes correspondingly higher where the tenant serves notice towards the end of the existing tenancy.

    d. This therefore creates a form of security of tenure since a landlord is not entitled to relet the property at the end of the existing expiry date on such terms as he thinks fit. Nor is he able to choose whether to relet to the existing tenant or an alternative tenant.

25. No other commercial tenants in Scotland enjoy such privileges. That degree of flexibility would place Tied Pub tenants in a uniquely advantageous position.

IMPACT OF TIED PUBS (SCOTLAND) BILL ON THE ATTRACTIVENESS OF THIS ASSET CLASS

26. In Scotland and elsewhere in the UK, it is generally accepted that a vibrant market for investment in commercial property is an essential component of the economy. The principles common to most property investments are, in no particular order, returns commensurate with limited exposure, scope for growth of income and capital, long term security of capital, and a predictable market for the asset.

27. My understanding is that Tied Pubs are generally, although not exclusively, held by large brewers as an investment. These assets provide a solid foundation for raising capital (equity and loans) and have the additional attraction of a broad base of contractually committed customers.

28. Landlords of Tied Pubs rely on the same basic principles for investing as landlords of other commercial properties in Scotland. If these principles are threatened, then it is predictable that the attractiveness of investing in Tied Pubs (or non-Tied) may diminish or be nullified altogether.

29. The Bill risks undermining investment principles on account of; (a) removal of certainty of rental income for a guaranteed period (b) loss of opportunity to gain vacant possession at the end of a lease (c) possible loss of scope to redevelop a property.

30. If investment is affected, then there is a real risk that the market could become unbalanced.

31. For instance, if Market Rent Only (MRO) would prevent or even make it more difficult for a landlord to redevelop his property, or sell with vacant possession, or let to a different tenant, or withhold marketing for any reason, then a key rationale for investing would no longer apply.

32. If attractiveness declines, then investors may switch to alternative non-Tied Pub tenancies or operate with salaried managers. During any transitional period, fresh investment in Tied and non-Tied Pubs could be abruptly curtailed.

33. It is for trade experts to opine if withdrawal of funding (equity and debt) would be detrimental to the sector. Logically, if pub values were expected to fall, then fresh funding would presumably be vulnerable.

34. It is generally advantageous to have market conditions and laws that encourage investment and enhancement of the overall stock and standard of property. Actions that are perceived to be unattractive by investors often lead to disinvestment and can, in the longer term, lead to a decline of the overall stock. These considerations could affect more than Tied Pubs.

IMPLICATIONS FOR NON-TIED PUBS, CAFES, RESTAURANTS, AND SHOPS

35. I understand a key aim of the Bill is to promote fair trading by entitling a tenant of a Tied Pub to call for a free of tie lease at market rent (an MRO-compliant lease) **at any time**. Then, if a tenant and landlord failed to agree a new lease, the issue could be referred to the Adjudicator or for independent assessment. The result of this could be a new rent (which could be lower or higher than the existing Tied rent) and terms (including the duration for the lease) which are less advantageous to the landlord than he would seek if the tenant did not have statutory rights.

36. If the foregoing summary is broadly correct, and the Bill adjusts contractual lease relationships, then it may have unintended consequences for other businesses in the shape of unfair competition. Put simply:

- Statutory protection would benefit a Tied tenant in ways that a non-Tied tenant could not enjoy.
- Cafes, restaurants, and shops do not enjoy these protections.

37. There are many instances where a non-Tied Pub tenant is contractually committed to a lease for a long period of years, often with ‘upward only’ rent reviews. That tenant would not have security of tenure at the end of the lease (which the Bill as proposed would potentially secure for a Tied Pub tenant).

38. Furthermore, a non-Tied tenant would have no facility to (unilaterally) require that the rent be adjusted to the market rate - **at any time**. In a changing market, the non-Tied tenant would still be bound to honour contractual commitments whereas, it seems that a Tied Pub tenant would not. This seems to create a platform for unfair competition between the two categories of pub tenant.

39. The position of a pub owner-occupier might also be competitively disadvantaged by the Bill. Although not paying rent, there would be no scope - if pub values/ prices were to fall - for mortgage payments to be summarily adjusted/reduced. (In general terms, the

amount of mortgage payments corresponds with the capital borrowed, which relates to the market value/price of the pub when the loan was agreed.) If a neighbouring competitor were a 'Tied Pub' and it had the option - **at any time** - to require its rent to be adjusted to reflect the prevailing market conditions, then clearly it would have an unfair advantage over a competitor that could not reduce their property costs.

40. If it transpired that capital values of pubs were adversely affected by the Bill, then presumably the current suitability of Tied Pubs as security for mortgage finance would need to be reappraised, and loan to values ratios (and loans) could reduce on new mortgages.

41. The issue of competition arguably extends beyond pubs because the product range of pubs has widened significantly over recent years and overlaps with items sold from other categories of property. There are a growing number of locations where this overlap occurs, and careful consideration is therefore required in the context of the Bill.

42. Tied and non-Tied Pubs offer soft drinks, tea, coffee, and food. Some have diversified and are virtually indistinguishable from cafes and restaurants. Cafes and restaurants sell alcohol with or without food. The differences between pubs, cafes and restaurants may in some cases not be discernible at all. Yet businesses such as cafes and restaurants that may fall outside of the statutory definition of a pub in the Bill somewhat arbitrarily have no security of tenure or opportunity to call for a Market Only Rent **– at any time**. The implications of this are unclear and unknown.

43. The growing trend, particularly in tourist hotspots for mixing refreshment and retail activities blurs traditional definitions of property categories. Therefore, it is predictable that conferring special concessions – security of tenure and Market Only Rents at any time – on one category of business, may lead to calls for similar treatment. In the interests of fair competition, it may be difficult to resist such calls and the consequences of such a major change in Scots Law would reach well beyond what I expect is envisioned by the Bill.

CONCLUSIONS

44. The Bill raises potentially significant legal and competition issues that may not have been foreseen to date. The impact on 'security of tenure' in Scots leases, as was explored by the SLC, deserves to be properly considered.

45. There is a risk that the Bill could affect capital values and funding, and potentially unbalance the market for investment in pubs. It may also affect related categories of property where business activities overlap.

46. I hope that the foregoing contribution is helpful to consideration of the Bill and I look forward to hearing if there are questions regarding the matters that I have identified.

GREENE KING

Yours faithfully

Fraser. W. Clearie BSc, FRICS, MCIArb, RICS Accredited Mediator
Partner
Riddell Thoms & Company LLP
Chartered Surveyors and Property Consultants

TIED PUBS (SCOTLAND) BILL – THE PUBS CODE AND MRO OPTION IN ENGLAND & WALES

This document outlines the history of the statutory Pubs Code in England and Wales, and particularly the introduction of the MRO provision. It also considers the issues with the MRO option and includes findings from the 2019 report by Europe Economics on the Pubs Code, commissioned by the British Beer & Pub Association (BBPA), and provided as evidence as part of the statutory review into the Code in England and Wales.

Greene King believes that the following detail makes clear that the MRO option, which was not originally intended to form part of the Pubs Code in England and Wales, is unnecessary and if introduced in Scotland will have harmful unintended consequences for Scotland's pubs sector.

The legislative history of the Pubs Code and MRO option in England and Wales

- The traditional model of pub ownership in England changed substantially in the late 1980s and 1990s following an investigation in 1989 by the competition authorities into the supply of beer. The 'Beer Orders' that followed prevented any one brewing company or group from owning more than 2,000 on-licensed outlets. The sell-off that followed saw the emergence of a new business model in this sector: the pub company, or 'pubco'.
- At the time, there were numerous complaints by tenants about the tied model and a 2004 report from the Trade and Industry Committee recommended revision of an existing voluntary code of conduct between pubcos and tenant. It added that if the industry failed to implement an adequate voluntary code, the Government should consider statutory regulation. **There was however no recommendation for the removal of the tie.**
- Following a 2009 report from the Business and Enterprise Committee which pressed for an urgent investigation into the sector, the BBPA published a new Framework Code of Practice (IFC) in January 2010. The Committee published a follow-up report in March which concluded that it would recommend statutory regulation if problems for pub tenants continued.
- The following year, the Business, Innovation and Skills Committee recommended that the voluntary industry code of practice and individual company codes of practice should be replaced by a statutory code. In response, the Coalition Government announced a new 'self-regulatory package' for the industry. This made the IFC legally binding by incorporating it into tenancies.
- At the same time, the Pubs Independent Conciliation and Arbitration Service (PICAS) was created to mediate and arbitrate on any matter relating to the

IFC or company codes. The Pubs Independent Rent Review Scheme (PIRRS) was also created for determining rent reviews.

- However, pubs continued to be the subject of parliamentary scrutiny. In January 2012, the House of Commons debated the issue of whether a statutory ombudsman should be created, during which MPs agreed a debate motion which said that "*only a statutory code of practice which includes a free-of-tie option with an open market rent review and an independent adjudicator will resolve the contractual problems between the pub companies and their lessees*".
- A year later, Business Secretary Vince Cable wrote to the BIS Committee confirming he would launch a consultation on establishing a statutory code and adjudicator. He said the code would be based on the existing IFC but strengthened to include the fundamental principal that 'a tied licensee should be no worse off than a free-of-tie licensee'. **Significantly, Cable confirmed he was not proposing the abolition of the beer tie.**
- In the Government's 2014 response to the consultation, it announced that it would legislate to establish a statutory code and an adjudicator. **It stated that it had decided not to include a mandatory free-of-tie option in the Code**, noting that an MRO option would have been likely to "cause a high degree of uncertainty" in the industry, with a likely negative impact on investment and the possibility that several pub owning companies would abandon the tied market.
- **The Small Business, Enterprise and Employment Bill, introduced in June 2014, did not provide for an MRO option.** However, at the Bill's Report Stage, the Commons agreed an amendment, tabled by Greg Mulholland MP, to make the 'market rent only' option a feature of the new regulatory regime. Subsequently, the Government introduced a series of amendments to retain this principle as the Bill passed through the Lords. These were agreed in 2015.

The MRO option in England & Wales

- The MRO provision in the 2015 Act contains a number of specific situations where an MRO notice can be served:
    - On the renewal of a business tenancy under the 1954 Landlord and Tenant Act
    - The service of a rent assessment where the lease contains a contractual rent review clause
    - A significant increase in the price of tied products
    - A 'trigger event', broadly an event that occurs which was outside the tenant's control, not reasonably foreseeable and which has a significant impact on trade.

- This provision states several ways a tenancy can be MRO-compliant, including if it does not contain any "unreasonable" terms or conditions. However, it does not state what is to be regarded as 'reasonable' or 'unreasonable'. The PCA has issued subsequent guidance in the form of statutory guidance and advice.
- A consequence of this is that there has been a focus on the need for the term of an MRO lease to be reasonable and common. Although Regulation 30(2) provides that the lease must be at least as long as the unexpired residue of the term, this does not mean that granting a lease that will expire on that date will necessarily be reasonable.
- That means that in order to comply a pub-owning business may have to grant a new lease that will extend the tenant's rights beyond the expiry of the existing lease. That may be the case even where the tenant would otherwise have no such right because its lease was contracted out of the security of tenure provisions of the 1954 Act.
- This is akin to a form of security of tenure, as it restricts the ability of the landlord to recover possession and it gives the tenant a right to extend his rights of occupation and business use of the property.

Experience of the MRO option in England & Wales

- Only a relatively small number of tenants have served MRO notices. According to the Europe Economics Report, after "an initial spike, the number of MRO notices each month has dropped considerably and now typically averages 20 responses per month".[11] That is across a total of 9,600 pubs covered by the Pubs Code.
- The lack of transition period provided difficulties for pub-owning businesses and the PCA, particularly following the way in which the original legislation was passed, via an amendment to the Bill. The first version of the Pubs Code was flawed as it failed to take proper account of the 1954 Landlord and Tenant Act (such as the grounds of opposition and the timings) and the final version was only produced late in the day.
- This meant that pub-owning businesses, tied pub tenants and their advisers had insufficient time to prepare and to understand its provisions. This was demonstrated in the high number of MRO-related referrals made to the PCA early on which then took many months (and in some cases years) to resolve. A transition period would have supported a more successful start in understanding the requirements of a complex piece of legislation and enabled time for the development of back-office processes and systems, staff-training and documentation.
- In terms of numbers of referrals accepted by the PCA between July 2016 and June 2020 there were 420, of which 369 (88%) were related to MRO. Disputes about the reasonableness of the MRO terms offered by pub-owning

[11] Europe Economics, Impact Analysis of the Pubs Code, 2019

businesses dominated the PCA's arbitration caseload throughout the statutory review period.

- Out of 1030 total valid MRO notices received to date across the industry, 62% of tenants have remained tied, left or another outcome has been achieved (such as withdrawn from the process). Only 13% have chosen to go MRO. This illustrates the extreme disparity between the number of MRO notices that have been served and the number of tenants that have actually chosen to go free of tie. However, it must bring into question the need for MRO in the first place when most tenants have simply used the process to secure a better **tied** deal, which was not one of the stated objectives of the Code of Parliament when it passed the legislation.

Europe Economics Report

- The BBPA commissioned a report from Europe Economics dated April 2019. This was submitted as evidence as part of the statutory review of the Code in England and Wales.
- The report reviewed the original impact assessment (IA) undertaken by the then Department for Business, Innovation and Skills. The report found that:
    - The IA did not provide a proper quantification of the problems it identified, making it difficult to establish whether these issues were a real economic problem or simply the isolated experience of some tenants.
    - Identification of problems in a market should consider the views of both sides of the market. The consultation that supported the IA only considered the views of the tenants and there was little investigation of any reasons which might explain the alleged behaviours.
    - Any assessment of a tenant being better off under a free-of-tie arrangement should carefully consider whether any potential 'value transfer' is a legitimate one. The authors demonstrated that the risk-sharing mechanism of a tied arrangement involves pubcos recovering their investment in expansionary periods. It adds that it would be 'unfair' that tenants only make use of the scheme in the periods where they are being subsidised by the pubco and break the tie in expansionary periods.
    - Using the MRO as a means of improving a tenant's tied deal might 'carry several dangers', including being an unsustainable strategy in the longer term with possible detrimental indirect effects on the tied market.
    - There is no evidence that tenants face unfavourable/unclear terms that keep them locked into contracts with their pub companies.
- The report also considered the potential unintended consequences of the legislation, including:
    - Taking greater numbers of pubs out of the tenanted and leased market and placing them directly under management. This is already being

evidenced, with 30% of the original 14,000 pubs covered by the Code in England & Wales no longer falling within the Code's jurisdiction.

- Creating barriers to new entrants to the pub sector.
- Reduction in investment by pub companies in their tied estate.

GREENE KING

Yearly breakdown	Total	2016	2017	2018	2019	2020	2021	2022
1. Total number of MRO Notices received								
a. Number of MRO Notices that were accepted	1030	239	237	216	191	147		
b. Number of MRO Notices that were rejected	213	83	52	16	27	35		
c. Number of MRO Notices that were withdrawn	12	1	2	3	3	3		
2. Number of full responses to accepted MRO Notices issued	989	218	220	214	187	150		
3. Number of full responses to rejected MRO Notices issued	205	81	54	16	25	29		
4. In cases where a MRO Notice has been received and accepted								
a. Number of free of tie arrangements agreed by new agreement	130	0	21	39	51	19		
b. Number of new free of tie arrangements agreed by deed of variation	10	0	0	0	8	2		
c. Number of new tied arrangements agreed by new lease	62	0	21	16	13	12		
d. Number of other new tied arrangements agreed (rent or other terms)	455	34	182	112	91	36		
e. Number of tied tenant departures from the pub	86	3	26	21	21	15		
f. Other outcomes	41	0	25	7	6	3		
g. Ongoing – yet to be concluded	244					244		