



Long tied leases – an *ALMR* proposal

Context

The relationship between the major, national pub companies and their tenants has come under tremendous strain over the past year. This is because the tied lease model has been insufficiently flexible to adapt quickly to the macro-economic downturn, resulting banking crisis and soaring operating costs.

The *ALMR* believes that the time has now come to rebalance that relationship and reform the way in which the product tie operates.

There is a need to ensure a fairer share of the economic benefits for lessees and the division of profits accruing from the individual outlet. That will require both parties to be more open about the income they gain from all income streams within the business, the true operating costs they incur and the long term investment they make in the outlet.

This can be achieved - not by means of legislation - but through all sides working together to deliver a more equitable business partnership. We believe this is achievable and a pragmatic solution to the current state of impasse.

- The Association does not challenge the legality of the Tie nor indeed is against the Tie itself especially in so far as it relates to brewers who own their own pubs or indeed to the smaller companies with their tenancy agreements.

Policy proposal

- On behalf of its Members who are multiple operators the *ALMR* challenges the usual requirement for compulsory supply agreements on long, fully repairing and insuring leases and seeks the opportunity for prospective lessees to negotiate lease terms that properly reflect the open market - and then to be able to enter into separate supply arrangements.
- The Association proposes that all fully repairing and insuring tied leases must include the list [to be agreed] of '**Standard Compulsory Clauses**' that address the continuing fair distribution of the economic benefit between the landlord and the lessee.
- The SCC list is to be drawn up by a working group of all relevant stakeholders whose involvement will be an expression of their commitment to the principles of this proposal, and the working group, under an independent chairman, should aim to report by the end of this Summer.
- All trade associations having members that issue FRI tied leases and/or members that are lessees of such leases should make it a condition of membership that members adhere to the SCC principle.
- That there be a reasonable timetable [say *one year*] for the Standard Compulsory Clauses to be devised and enshrined within all applicable leases and that if this timetable was not to be achieved then the Association should call publicly for there to be an official investigation into the pub leased model and the contractual supply arrangements within it. [*ALMR* would regard this real sanction as nevertheless being a last resort because of the time and resources it would take to investigate and legislate.]



Post script

Significant as this debate is, however, what unites lessees and landlords in the pub industry is much more important than what divides us. The *ALMR* will not lose sight of the fact that, whatever the nature of lease agreements, it is the government which takes the lion's share of our industry's profits – for an average community pub, the government take is 40% more than the profits available to lessee and landlord.

TS/NB

Ealing

22 April 2009

see below:

Chairman's speech at AGM – 23 April 2009



Chairman's speech at AGM – 23 April 2009

Rather than range across the spectrum of *ALMR* activity I intend to cover one single policy point – the Association's proposal to resolve the continuing standoff between landlords and their tied lessees. But before I consider that I stress that our other main concern is the impact of taxation on our industry. We must never forget that the Government takes 40% more profit out of the average pub than its operator and its landlord combined – calculated at a colossal £85k per pub per year. We have an unanswerable case to put to government and this is well summed up in the Beer Group's Community Pub Report, but ministers will wriggle like mad to get off that hook and we must not allow them to point at internal industry issues as an excuse for inaction. Only by putting our own house in order can we successfully lobby political and other audiences – and that's the focus of this speech.

The 10 years following the last recession – and the launch of the *ALMR* - were characterised by a relatively booming economy, a confident consumer, and the organic expansion of the pub companies – particularly Enterprise Inns and Punch but latterly with S&NPE and Admiral. In very broad terms the multiple lessees were content to share an ever-increasing cake – not necessarily a fair share, but more profits nevertheless.

But by 2004 it was becoming clear that there were business pressures on tied lessees and that these were sufficient for the Trade & Industry Select Committee to investigate the concentration of pub ownership in a few companies and, by extension the Tie itself and the Rents model. The Committee's headline recommendations are well known; it called for an improved Code of Practice, for the abandonment of Upward Only Rent Reviews, and the end of the AWP Tie. Most significantly the Committee said that it was not persuaded that the Tie itself was a problem – but it did reserve judgment on its operation.

In 2006 the Association realigned itself in such a way that the 2 principal pubcos became supplier associates rather than operator members and this gave the Association more authority to represent the interests of multiple lessees. This we did by holding meetings with the principal pubcos at which *ALMR* Members debated face-to-face the key issues that needed resolving – or at least airing. There were modest successes from these meetings but we did at least open an effective channel to exchange views.

But the pressures on lessees did not go away and of course by 2007 the economic boom was not only stalling – it was looking like going bust. So the inequalities of the tied lease model were becoming more stark – the cake was getting smaller and the lessees' slice of it was less and less acceptable.

This triggered the most recent select committee inquiry to which the Association gave written evidence that the pubco model wasn't working well and especially so in a declining market where it lacked flexibility other than through the sacrifice of lessees' profitability. We noted that, while some companies had abandoned the principle of upwards-only rents, this had actually seldom been confirmed in writing in the lease – other than sometimes by a contractual side letter whose cost had to be borne by the lessee!

This was part of our response to the question on Codes of Practice where we observed that the Bill recognition of pubco codes extended only to their clarity, not to their inherent fairness. We reminded the Committee that the pubcos still continued to tie the fruit machines and we gave evidence about the unequal profit share. We certainly noted that the pubcos were less and less



prepared to share their beer discounts with their lessees. But in spite of all this we still believed that further legislative intervention in the industry would be unhelpful – successive governments not having an unblemished record when trying to adjust how markets operate.

Since December the issue of pubcos and the Tie has rarely been out of the news. Some of this is down to the campaigning of the Fair Pint Group and some to the headlines in the financial press. The Committee has been deliberating and we understand that the Report will be published shortly. We have no means of knowing what the Report will contain but it is noteworthy that Lindsay Hoyle MP, a member of that committee, has put down his own Early Day Motion calling for the Tie to be outlawed. In the meantime *ALMR's* Council, and with most helpful contributions from the wider membership has carried on developing our own policy which is written up as a document to be released to members and the press after this meeting.

The first element of this is that Association does not challenge the legality of the Tie nor indeed is against the Tie itself - especially in so far as it relates to brewers who own their own pubs or indeed to the smaller companies with their tenancy agreements. But we do believe that the time has now come to rebalance the landlord/lessee relationship and reform the way in which the product tie operates.

On this basis the *ALMR* would challenge the pubcos' usual requirement for compulsory supply agreements on long, fully repairing and insuring leases and proposes that lessees should have the opportunity to choose lease terms that properly reflect the open market, and then to be able to enter into separate supply arrangements – a tied lease or a free lease.

There is a vital need to ensure a fairer share of the economic benefits for lessees and the division of profits accruing from the individual outlet. That will require both parties to be more open about the income they gain from all income streams within the business, the true operating costs they incur and the long term investment they make in the outlet.

This can be achieved through all sides working together to deliver a more equitable business partnership. We believe this is achievable and a pragmatic solution to the current state of impasse. We are not describing our suggestion as a Code of Practice. A legally binding Code would require government intervention and there is perhaps a surfeit of codes anyway from the individual companies involved. We would, as I have said, prefer that all long pub leases be offered with either a Tie or free of Tie but that cannot be quickly delivered. In the meantime what *ALMR* is proposing is that all FRI tied leases are required to include a list of '**Standard Compulsory Clauses**' that address the continuing fair distribution of the economic benefit between the landlord and the lessee.

We believe that the list of these Clauses will complement and extend the BII-approved codes which, notwithstanding their kite-marked clarity, will always be open to interpretation and negotiation; the clauses will require the remedies to be binding and legally enforceable forthwith.

These Clauses would pick up and confirm the full removal of Upward Only Rent Review clauses, the automatic RPI increases in rent from existing leases and the removal of the machine tie from the long leases of national pub companies. This list could be pretty extensive and we suggest that a working group, drawn from stakeholders and assisted by professional advisers, under an independent chairman could assemble and publish this list of Standard Compulsory Clauses during this summer.

We do have to wait and see what the BESC Report contains but I am reasonably sure that the pubcos in particular will be ready to welcome any suggestion that averts an official investigation.

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They should therefore be prepared to adopt the SCCs. We would go on to suggest that this could be underpinned by trade associations requiring their members that offer such leases to comply ,and for there to be universal advice to tied lessees not to sign leases without this list of clauses in place

The *ALMR* stands ready and willing to represent retailers and work with others to deliver this solution. We believe that it should be possible to agree and apply the new clauses within 12 months and if the national pub companies are unwilling or unable to join us in this work, then we still stand ready to call for the competition authorities to investigate the pubcos and the Tie. This is not an idle sanction because we may yet have to go there; but an investigation would not necessarily have the outcomes that the most ardent campaigners would seek because the evidence gathering here and the likely legal challenges in the UK and in Europe could take years - far longer than our industry can afford to contemplate.

So, to conclude. The *ALMR* proposes

1. a list of Standard Compulsory Clauses to be devised to remedy present unfairness.
2. The legally binding inclusion of this list in existing and new FRI, tied leases.
3. Structured peer pressure for lessors and lessees to comply
4. The sanction of investigation by competition authorities' investigation if there is inadequate progress to a successful outcome.

Ladies and gentlemen - colleagues - we have a unique opportunity for reform for the benefit of all our industry – *ALMR* is up for it and we urge all sides to grasp it with both hands.

ENDS