POLICY NOTE

THE SCOTTISH PUBS CODE REGULATIONS 2024

SSI 2024/XXX

The above instrument was made in exercise of the powers conferred by sections 1, 7 and 23 and Schedule 1 of the Tied Pubs (Scotland) Act 2021. The instrument is subject to the affirmative procedure.

Summary Box

This instrument will create a Scottish Pubs Code for tied pubs. It creates rights and protections for tied pub tenants and places requirements on pub-owning businesses (the tied pub landlords). It is the main instrument to implement the Tied Pubs (Scotland) Act 2021[1]. It has been prepared consistently with the three regulatory principles set out in the Act. These are:

a)the principle of fair and lawful dealing by pub-owning businesses in relation to their tied-pub tenants,
(b)the principle that tied-pub tenants should not be worse off than they would be if they were subject to neither a product tie nor a service tie,
(c)the principle that any agreement between a pub-owning business and a tied-pub tenant should fairly share the risks and rewards amongst the parties.

Policy Objectives of the Act

The Tied Pubs (Scotland) Act 2021 received Royal Assent in May 2021. The purpose of the Act is to regulate the relationship between tied pub landlords and tenants through the introduction of a statutory Scottish Pubs Code and the appointment of a Scottish Pubs Code Adjudicator. The role of the Adjudicator is to oversee and enforce the code.

Tied pubs are pubs which are owned by a pub-owning business and leased to a tenant. Tenants must buy some or all of their products and services ("the tie") from the pub-owning business (their landlord) or someone nominated by the pub-owning business. Ties can include, for example, beer and these products and services are often charged at a higher cost than on the open market. In return, tenants sometimes pay lower rent and receive other support from the pub-owning business.

Policy Objectives of the SSI

The aim of the Scottish Pubs Code is to improve the position of tied pub tenants through creating a statutory framework to govern the relationship between pub-owning businesses and their tied pub tenants. The Scottish Government supports the principle of fair and equitable treatment within tied pub leases and has a desire to see a vibrant tenanted pub sector in Scotland. As of May 2023, it is estimated there were just under 700 tied pubs in Scotland.

[1] https://www.legislation.gov.uk/asp/2021/17/contents/enacted

Concerns about fairness in the relationship between tied pub tenants and pub-owning businesses led to the UK Government creating a statutory Pubs Code and a Pubs Code Adjudicator in England and Wales in 2016, to regulate the largest tied pub-owning businesses who own 500 or more tied pubs. In 2020 Neil Bibby MSP introduced a Members Bill to deliver protections for tied pub tenants in Scotland. The Scottish Government agreed to support the Tied Pubs (Scotland) Bill in December 2020. This was in response to the evidence put forward at Stage 1 of the Bill, the response to the UK Government's review of the Pubs Code and Pubs Code Adjudicator in England and Wales, and the likelihood that legislation would be required at some point to implement the Economy, Jobs and Fair Work Committee's recommendations on the Bill. The Tied Pubs (Scotland) Act 2021 was passed unanimously by the Scottish Parliament on 23 March 2021.

Much of what the code must contain is already pre-determined by the Act and some of the key things the code will do include:

Market Rent Only

The code will require pub-owning businesses to offer Market Rent Only (MRO) leases in certain circumstances when requested by tenants. An MRO lease is a lease which is free of ties and does not contain any unreasonable terms.

The MRO lease element is one of the main ways that a tenant can check that they are not worse off than they would be if they didn't have any ties, and thus contributes towards the second regulatory principle.

The Scottish Government recognises that to fulfil the third regulatory principle, there needs to a fair share of risk and reward in agreements between tenants and pub-owning businesses. The Scottish Government has sought to develop a balanced approach: giving tenants their rights to request Market Rent Only (MRO) whilst giving pub-owning businesses some certainty of return under their current agreement. This has resulted in the code allowing pub-owning businesses to not provide MRO leases in the following circumstances:

- For short-term leases (less than one year, unless this is a renewed lease);
- If tenants are in the first half of their lease e.g. in year two of a five year lease;
- Where the tenant has previously requested an MRO lease in the past two years;
- Where either the tenant or the pub-owning business have submitted a valid notice to bring the lease to an end; or
- Where there is an investment agreement in place for the pub between the pub-owning business and the tenants (the investment must be at least 1.5x annual rent or £35,000 whichever is greatest) there is a five-year exemption from offering MRO. This exemption is to provide certainty to pub-owning businesses to recoup substantial investment in a pub.

The code also sets out a process to request MRO leases. Drawing upon the experience in England and Wales, the Scottish Government has sought to create an MRO lease process which is more straightforward, flexible and easy to use.

The code sets out terms that would be unreasonable to include in an MRO lease. Most of these are terms which are more onerous than the terms contained in a tenant's existing lease, such as a lease period which is shorter than the remaining period of the current lease.

Guest Beer Agreements

The code will require businesses to offer a guest beer agreement in certain circumstances when requested by tenants. A guest beer agreement allows a tenant to sell to their customers at least one beer that the tenant has chosen, at a price of the tenant's choice. The beer can be changed as often as the tenant wishes.

The code sets out that guest beer agreements should be restricted to brands of beer with a small production capacity of up to 5,000hL. Using sales data as a proxy for production, we estimate this will give tenants access to 96% of beer brands. This approach best meets the regulatory principle around a fair share or risk and rewards, as it is less likely (than if there were no production restriction) to result in sales of guest beer substantially replacing sales of beer supplied by the pub-owning business through the tie.

The Scottish Government is seeking to keep guest beer arrangements straightforward and simple for tenants and pub-owning businesses, therefore there is only one exemption where the pub-owning business is not required to offer a guest beer agreement when a tenant requests one. The exemption provides that pub-owning businesses need not offer a guest beer agreement when tenants have already agreed a guest beer agreement that matches the set criteria for guest beers under the Act.

Information and advice to prospective tenants

Before a tenant enters into a new or renewed lease, or develops a business plan, we are requiring the pub-owning business to make certain information available to existing and prospective tied pub tenants, to ensure fair and lawful dealing and also to enable tied pub tenants to make an assessment in relation to the second and third regulatory principles (not worse off than if they weren't subject to a tie; and a fair share of risk and rewards between the parties). Pub-owning businesses will also be required to advise certain tenants to undertake pre-entry training and to advise tenants to prepare a business plan based on independent advice and provide information on sources of independent advice. The pub-owning business is required to have due regard to the business plan when negotiating a new or renewed lease.

Rent review

A pub-owning business is required to give the tenant a rent assessment statement as part of a rent review process either as provided for within their contract or as part of a rent review under the code. A rent assessment statement should also be provided to prospective tenants. The code sets out what information must be provided and what must be included in a rent assessment statement.

The code provides for a tenant to request a rent review under the code: where a rent review is not already included in a lease, the lease is longer than 12 months and if a rent review or a rent assessment has not occurred within the past 5 years.

Rent reviews are a key part of the ongoing relationship between landlord and tenant and represent an opportunity to support the third regulatory principle “that any agreement between a pub-owning business and a tied-pub tenant should fairly share the risks and rewards amongst the parties.”

Other

The code also sets out arrangements, processes and information requests for other aspects of the tied tenant-landlord relationship. Many of these requirements must be included in the code because of the Act.

The code sets out how disputes are to be resolved and what cannot be taken to the Adjudicator for arbitration.

The code requires pub-owning businesses to provide information to the Adjudicator so that the Adjudicator knows which pub-owning businesses are operating in the Scottish market and fall under the regulatory regime.

The code prevents pub-owning businesses from requiring a tenant to purchase, or rent, gaming machines. It also prevents a pub-owning business from subjecting a tenant to a detriment or imposing a liability on a tenant because of a reading from a flow monitoring device unless a specific condition is satisfied.

EU Alignment Consideration

This instrument is not relevant to the Scottish Government's policy to maintain alignment with the EU.

Consultation

Substantial formal and informal consultation has taken place on the implementation of the Act more generally, specifically on the development of the Scottish Pubs Code.

Ahead of formal consultation, in summer 2021 four workshops were run with key stakeholders. This included the Scottish Licensed Trade Association (representing tenants' views), the Scottish Beer and Pub Association (SBPA) (representing most pub-owning businesses) together with some pub-owning business representatives. In addition, further consultation meetings also took place with the Royal Institute of Chartered Surveyors (RICS), individual pub-owning businesses who are not members of SBPA, Pubs Advisory Service, SIBA (the Society of Independent Brewers) and CAMRA (the Campaign for Real Ale).

Two workshops[2] were also run with five tied pub tenants.

Two written consultations on parts of the Scottish Pubs Code were run from 8 November 2021 to 17 January 2022[3] and from 17 March 2022 to 12 May 2022[4]. Consultation analyses were produced for the first[5] and the second[6] consultation.

For the first consultation, we received a total of 34 responses to the public consultation, with 14 individuals and 20 organisations responding. 11 responses were from tied pub tenants and 6 responses were from pub-owning businesses.

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[2] https://www.gov.scot/publications/tied-pubs-consultation-scottish-pubs-code-workshops-tenants/
[3] https://www.gov.scot/publications/tied-pubs-consultation-scottish-pubs-code-part-1/
[4] https://www.gov.scot/publications/tied-pubs-scottish-pubs-code-part-2-consultation/pages/1/
[5] https://www.gov.scot/publications/tied-pubs-scottish-pubs-code-part-1-consultation-analysis/
[6] https://www.gov.scot/publications/scottish-pubs-code-consultation-2-analysis-report/

Respondents generally had mixed views on the proposals. Tenants broadly welcomed the proposals around MRO leases and guest beer agreements. However, pub-owning businesses had a number of concerns, especially on the unintended consequences of the proposals.

Respondents had mixed views on the proposal to exempt leases from MRO after investments for 5 years; tied pub tenants tended to disagree whilst pub-owning businesses agreed.

On guest beer agreements, some participants felt that the focus in terms of eligible products should be on the type of brewery rather than on the production level of brands of beer. The Tied Pubs (Scotland) Act 2021 sets out that a guest beer agreement must allow a tenant to sell at least one beer of their own choice, regardless of who produces it. This means we cannot use the code to restrict guest beer agreements to any particular type or category of producer, such as small brewers.

On the partial Business and Regulatory Impact Assessment (BRIA) some pub-owning businesses expressed a number of concerns with the partial BRIA.

As a result of the first consultation, changes to the draft code on MRO leases included:

- extending the negotiation period to 8 weeks;
- having a single investment exemption whereby pub-owning businesses do not need offer a MRO lease;
- continue to exempt short-term leases from MRO but provide that short-term leases cannot be continually renewed as a way of preventing access to MRO.

On guest beer, following the consultation, further work was carried out to refine the appropriate production level and to identify impacts. Cans were added to the draft code as being eligible for a guest beer and most of the exemptions were removed from the draft code to keep arrangements straightforward.

On the second consultation, we received a total of 30 responses, with 14 individuals and 16 organisations responding. 6 responses were from tied pub tenants and 6 responses were from pub-owning businesses. Respondents generally had mixed views on the proposals. There were some differences in views between pub-owning businesses and tied pub tenants.

There was general support for the proposals around providing information and advice to new and renewing tenants.

On rent review, pub-owning businesses had concerns about the proposed triggers for the proposed rent reviews, which they often felt were not well enough defined. As a result, we removed the right to a rent review in response to changing material circumstances in the draft code and focused the rent review arrangements on those tenants in a longer lease who might not otherwise have the opportunity to assess their rent.

Further discussions took place with the SBPA, their pub-owning businesses and the SLTA towards the end of 2022.

A short, focused consultation was carried out on MRO process from 19 July 2023 to 21 August 2023. Four responses were received. There was general agreement on most of the proposals. There were, however, mixed views about whether any process for considering

whether a valid MRO request has been received should be included in guidance rather than legislation, so this has not been included in the code.

The Information Commissioner's Office has also been consulted on the proposed package of secondary legislation to implement the Tied Pubs (Scotland) Act 2021 as required by Article 36(4) of the UK General Data Protection Regulation. They highlighted a few data protection considerations and advised that the Adjudicator and/or the Scottish Pubs Code will want to include some early thinking about:

- retention – how long will personal data be stored;
- the fields of personal data that might be involved to ensure that it is kept to the minimum necessary for the required purpose;

Impact Assessments

The following Impact Assessments have been prepared for the supporting instruments which implement the Act:

- Business and Regulatory Impact Assessment
- Child Rights and Wellbeing Impact Assessment (screening)
- Equalities Impact Assessment
- Data Protection Impact Assessment
- Strategic Environmental Assessment (pre-screening notification)
- Fairer Scotland Duty
- Island Communities Impact Assessment (screening)

These impact assessments will be published on the Scottish Government website.

This instrument is anticipated to have minimal to no impacts on children, the environment and island communities.

In terms of the Fairer Scotland Duty assessment, it was identified that we do not have data on the impact that implementation of the Act is likely to have on the incomes of tied pubs tenants and those that they employ. We cannot know whether changes would be uniformly made in the sector across different areas of deprivation.

There may be a difference in awareness and take-up of information about proposed changes to the Adjudicator and rights (parts of the code) between tied pub tenants with less and those with more socio-economic disadvantage and between those with better and worse IT skills, based on the England and Welsh experience. There may also be an uneven impact amongst tenants of pub-owning businesses moving to other types of business models and selling tied pubs. The assessment identifies some actions to address awareness and take-up of the code.

On equality impacts, it was identified that we do not have data on the demographic make-up of the tied pub tenant population in Scotland. However, in general, successful implementation of the Act would mean that tenant and pub-owning business relationships are fairer and more balanced, which should minimise discrimination on any basis, protected characteristic or otherwise.

On data protection, the main impact was around the establishment of the Adjudicator and making sure they are aware of their obligations. The Scottish Pubs Code may also require

pub-owning businesses to disclose publicly available enforcement action against the pub in the last two years relating to health and safety and planning.

Impacts on business are detailed in the financial effects section below.

Financial Effects

A Business and Regulatory Impact Assessment (BRIA) has been completed for the following SSIs:

- The Scottish Pubs Code Regulations 2024
- The Tied Pubs (Fees and Financial Penalties) (Scotland) Regulations 2024
- The Tied Pubs (Scottish Arbitration Rules) Amendment Order 2024

The BRIA is attached and is also available on the Scottish Government website. The BRIA sets out the cost and benefits of various options for pub-owning businesses and tied pub tenants.

We anticipate that the Scottish Pubs Code will result in a financial transfer largely from pub-owning businesses to tied pub tenants in line with regulatory principle three, concerning a fair share of risk and reward, but this will not be uniform and will likely reduce over time as the market responds to reduce this risk. The BRIA sets out the various options and models considered.

Market Rent Only

The cost of introducing MRO arrangements as set out above (the limited code option in the BRIA) are estimated to benefit an individual tenant between £0-£23,800 and for all tenants result in benefits of £0-£16.7 million per year. Pub-owning businesses are estimated to experience the same level of losses. These are estimates recognising that the costs and benefits are situation specific, and their value can be highly subjective. Tenants would also face costs of independent assessment, where this occurs. It would however also provide greater operational flexibility for tenants. Market Rent Only leases would, for pub-owning businesses, lead to a reduction in risk from market fluctuations due to higher dry rent under a MRO lease. The code may result in a reduction in the number of tied pubs and both pub-owning businesses reducing the benefits in the long-run.

Guest beer

Under the guest beer agreements set out above (the minimal code option in the BRIA). The tenant is expected to have economic benefits between £800 and £5,900 a year with the same level of losses by the pub-owning business per tied pub, where the tenant requests and is eligible for a guest beer. This represented an overall estimated benefit to tenants ranging from £0.1 million to £1.0 million per year, with pub-owning businesses experiencing the same range of costs. However, if the pub-owning business is the provider of the guest beer, then some of this loss will be offset. In the longer-term pub-owning businesses may seek to recover lost revenue by increasing dry-rent therefore the benefits of a guest beer agreement may be partially or fully offset in the long-run.

Rent reviews

The approach to create a rent review right within the code (the limited code option in the BRIA), provides tenants with increased bargaining power in the negotiation of rent and leading to potentially more favourable rent arrangements, as well as greater transparency in

the process. There would be costs in terms of time and resource for tenants to understand the rent assessment statement, negotiating rent or seeking independent advice. Costs to pub-owning businesses are estimated to be at £1,500 to £2,500 per tied pub that requests a rent review and there would be increased uncertainty about rent levels and future revenues for the pub-owning business. However, we have been unable to quantify how many leases it would impact. We understand that the market is moving to shorter leases (i.e. less than 5 years) and many existing leases do already have rent review arrangements within them. The impact is therefore likely to be small for pub-owning businesses, but the options could provide benefits to any eligible individual tenants to check there is a fair share of risk and reward.

The code also creates other requirements on pub-owning businesses which will create further financial impacts.

Scottish Government
Directorate for Agriculture and Rural Economy

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