EXPLANATORY MEMORANDUM TO

THE SMALL BUSINESS, ENTERPRISE AND EMPLOYMENT ACT 2015 AND PUBS CODE ETC. (AMENDMENT) REGULATIONS 2021

2021 No. XXXX

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Business, Energy and Industrial Strategy and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 The instrument amends the Small Business, Enterprise and Employment Act 2015 (the "2015 Act") and the Pubs Code etc. Regulations 2016 (the "Pubs Code") to improve the practical operation of the Pubs Code, as set out in sub-sections 7.9 - 7.15, as well as to make some drafting changes for clarification and to make two minor corrections.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 The JSCI reported the Pubs Code on 29 June 2016. A copy of that report can be found here: https://publications.parliament.uk/pa/jt201617/jtselect/jtstatin/16/1602.htm. These Regulations do not amend the underlying provisions that were reported on but do make a small technical change to these provisions.

4. Extent and Territorial Application

4.1 The territorial extent of this instrument is England and Wales.

4.2 The territorial application of this instrument is England and Wales.

5. European Convention on Human Rights

5.1 The Parliamentary Under Secretary of State (Minister for Small Business, Consumers and Labour Markets), Paul Scully, has made the following statement regarding Human Rights:

"In my view the provisions of the Small Business, Enterprise and Employment Act 2015 and Pubs Code etc. (Amendment) Regulations 2021 are compatible with the Convention rights."

6. Legislative Context

6.1 Section 46 of the 2015 Act requires the Secretary of State to review the Pubs Code and as part of that review the report must set out any revisions of the Pubs Code which, in the Secretary of State's opinion, would enable the Pubs Code to reflect more fully the principles of behind the Code (further explained at sub-section 7.2 below). The Pubs Code itself also requires further review (see regulation 68). The review of the period from 21 July 2016 to 31 March 2019 was reported on in November 2020.

These Regulations make amendments to Pubs Code to reflect the findings of that review, following consultation.

6.2 The instrument also amends the 2015 Act using the power in s69(9) of the 2015 Act. It is the first time this power has been used.

7. Policy background

What is being done and why?

7.1 The Pubs Code regulates the relationship between "pub-owning businesses", which are primarily businesses with estates of 500 or more tied pubs in England and Wales, and their tied pub tenants. In entering into a tied tenancy, the pub tenant agrees to buy all or some of the alcohol to be sold at the premises from their landlord, usually above market rates but in return for paying a lower rent and other benefits. A pub-owning business might be a brewing business, for whom the tied pub is a route to market, or a business supplying products it has bought through negotiating deals with brewers and other producers to its tenants at a profit.

7.2 The nature of the tied agreement, whereby tenants are unable to access the open market to purchase beer and other stock, exposes the tenant to risks if, for example, sales and margins on tied products are not as envisaged. Following evidence, the Government introduced measures in the 2015 Act to address the failures in the tied pub sector. The 2015 Act required the establishment of a Pubs Code consistent with the principles of fair and lawful dealing by pub-owning businesses in relation to their tied pub tenants and that tied tenants should not be worse off than they would be if they were not subject to any product or service tie. There are six large pub-owning businesses who between them own 8,567 tied pubs in England and Wales (end June 2021).

Explanations

What did any law do before the changes to be made by this instrument?

7.3 The Pubs Code requires pub-owning businesses, prior to agreeing a tied tenancy, to advise the prospective tenant to complete appropriate training, to provide certain information in relation to the maintenance of the tied pub premises and the tied tenancy and to ensure that the prospective tenant has a sustainable business plan. It places obligations on the pub-owning business in respect of gaming machines, insurance, flow-monitoring devices and their Business Development Managers. It further requires the pub-owning business to appoint a Code Compliance Officer who must submit an annual compliance report to the regulator of the Pubs Code, the Pubs Code Adjudicator ("PCA"). Pub-owning businesses must provide rent proposals or rent assessments to their tied tenants in certain circumstances.

7.4 The Pubs Code creates a right for a tied pub tenant, under specific circumstances, to change the nature of their contract from a tied tenancy to a free-of-tie tenancy where the tenant pays only the 'market rent' and is no longer required to buy products from the pub-owning business. The market rent only option is the mechanism that enables the tied tenant to obtain an MRO-compliant proposal (as defined in the 2015 Act and Pubs Code) from their pub-owning business setting out a free-of-tie offer and allows them to remain on their current terms, opt for the free-of-tie offer or negotiate a better deal.

7.5 The Pubs Code is enforced by the PCA which arbitrates disputes in respect of compliance with the Pubs Code. The PCA also has regulatory functions, including the provision of advice, consulting on and issuing guidance and the investigation of suspected non-compliance with the Pubs Code. In respect of the market rent only option the PCA can arbitrate on the MRO-compliance of the terms proposed by a pub-owning business. Where there is a dispute about the proposed rent, an Independent Assessor can be appointed to determine the market rent. Prior to this instrument, the Pubs Code only allowed a 14-day window for referrals to be made to the PCA if the tenant considered that the proposed terms were not MRO-compliant.

Why is it being changed?

7.6 The Secretary of State published a report concluding the first statutory review in November 2020 which found that while the Pubs Code was consistent with the principles set out in the 2015 Act, it was not consistently delivering the outcomes the principles were intended to support. It found that, while there had been improvements since the Pubs Code commenced in 2016, it was not working as well as it should, with some tied pub tenants saying that they had found it hard to exercise their Market Rent Only rights.

7.7 Stakeholders considered the timelines for the Market Rent Only process to be unduly restrictive, in particular the 14-day referral window to the PCA to challenge the MRO-compliance of the terms of the proposed tenancy. While this timeline was introduced to incentivise the parties to complete the Market Rent Only process efficiently, in practice, this short window has led to premature or "protective" referrals being made to the PCA before parties had had an opportunity to discuss the terms.

7.8 The Government committed to consult on a number of options reflecting the areas for improvement identified in the report and invited stakeholders views on possible changes to the Pubs Code between July and September 2021. As a result of that consultation, the Government is making a number of changes to the Pubs Code. As the Pubs Code carefully balances the rights and protections for tied tenants with the property rights of the pub-owning businesses in respect of the pubs they own, these changes have been developed in a way so as to retain that balance.

What will it now do?

7.9 This instrument introduces the following significant changes.

7.10 Schedule 1 amends the 2015 Act by shortening the qualification period for a business coming into scope of the Pubs Code, from owning 500 or more tied pubs for '6 months' in the previous financial year to '3 months'. This may bring certain tied tenants more quickly in the scope of the Pubs Code's rights and protections. It may also result in a pub-owning business which reduces its number of tied pubs to below 500 remaining within the scope of the Pubs Code for longer than it currently would. This would increase the current minimum period of full protection for the remaining tied tenants from 6 to 9 months. The shortened qualification period will take effect from 1 April 2023 to ensure that businesses newly in scope of the Pubs Code (if any) have sufficient preparatory time.

7.11 It introduces an improved procedure to be followed in connection with the market rent only option which:

- creates a longer period of up to 3 months (called the "resolution period") for the parties to negotiate the proposed free-of-tie terms and the offered rent before the

proposal is referred to dispute settlement, where the tenant considers that the proposed terms are not MRO-compliant or disagrees with the proposed rent . This may reduce the number of disputes referred to the PCA for arbitration. The tied tenant can control the process by ending the resolution period at any time after 21 days if the tenant considers that insufficient progress is being made and refer the free-of-tie terms to the PCA or the proposed rent to an Independent Assessor. The resolution period removes the need for the "negotiation period" and "subsequent proposed tenancies" found in the original Pubs Code.

- allows the tenant to refer a "procedural or event dispute" to the PCA within 14 days from receipt of the pub-owning business's proposal (or from the day it should have been received). This retains a similar time frame to the existing process for this type of dispute. A procedural or event dispute includes where the pub-owning business has failed to reply to the tenant's request for a market rent only proposal, or failed to include the proposed rent or where there is a disagreement about the tenant's right to request a market rent only proposal. Once the procedural or event dispute is resolved, the 3-month resolution period would commence.
- gives the pub-owning business the opportunity to update its formal proposal at the end of the resolution period , after which the tenant has 21 days to accept the proposal, or either refer the proposed terms to the PCA or the proposed rent to the Independent Assessor. Where the terms are referred to the PCA, the tenant retains the right to refer the rent to the Independent Assessor within a period of 21 days from when the arbitration process has completed. If the tenant refers the proposed rent to the Independent Assessor, the tenant cannot subsequently refer the terms to the PCA.
- allows referral back to the PCA in relation to a revised response received from the pub-owning business following arbitration where the tenant considers that the proposal is still not MRO-compliant.
- these changes will take effect for events that give rise to the market rent only option that take place after the instrument comes into force.

7.12 It requires the inclusion of the proposed rent, along with the proposed market rent only terms, so that the tenant can consider the market rent only proposal in its entirety during the resolution period. While the proposed rent is often already included in any proposal, expressly making this a requirement in the Pubs Code will enable the tenant to ensure that the proposed rent is known during the resolution period and will aid meaningful negotiation.

7.13 Schedule 2, paragraph 3 adjusts the "comparison period" used to determine whether a significant price increase for a tied product or a tied service has occurred (which allows the tenant to request a market rent only proposal) from the current 56 weeks to 52 weeks. The practical operation of the definition of the comparison period had created a 56-week period, potentially capturing two annual price increases and raise complications for the more traditional 12-month period for business planning. The change ensures that the comparison period does not exceed a 12-month period, thereby reducing complexities in business planning and managing annual price changes.

7.14 The instrument requires a pub-owning business that sells, or otherwise transfers, a tied pub to a person in circumstances that give rise to the tenant having "extended protection" (as defined in s69(4) of the 2015 Act), to inform the PCA of the name,

address, company number of the new owner (where relevant) and anticipated transfer date. The Pubs Code provides the tied tenant whose pub has been transferred, with extended protection for a limited time, during which time the new owner becomes a regulated business under the Pubs Code. The purpose of this provision is to enable the PCA to identify these pub-owning businesses, seek to ensure the new pub-owning business is aware of the Pubs Code's rights and protections for the tenant and to obtain better understanding of how extended protection operates in practice.

7.15 Paragraphs 17 and 18 of Schedule 2 also make two minor cross-referencing corrections to the Pubs Code. The Department does not consider it necessary to provide free replacement copies, given the nature of the corrections and their proportion of the instrument. The Department has complied with the requirement stated in paragraph 4.7.6 of Statutory Instrument Practice to consult with the SI Registrar.

8. European Union Withdrawal and Future Relationship

8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act.

9. Consolidation

9.1 There are no plans to consolidate the legislation amended by this instrument.

10. Consultation outcome

10.1 The first statutory review of the Pubs Code concluded in November 2020 with the publication of the Secretary of State's report on the review https://www.gov.uk/government/publications/pubs-code-and-pubs-code-adjudicator-statutory-review-2016-to-2019. The report summarised the views of a wide range of stakeholders who responded to a public invitation to input into the review considering the effectiveness of the Pubs Code, as well as evidence from surveys and other sources.

10.2 Taking account of the areas for improvement identified in the report, the Government committed to develop proposals and consult on a number of options to improve its practical operation. A consultation paper entitled 'Consultation on proposals to amend the Pubs Code' https://www.gov.uk/government/consultations/options-to-amend-the-pubs-code was published on 12 July 2021 and the period for responses closed on 5 September 2021. Officials held meetings with key stakeholder bodies, including the PCA, to hear their views and clarify any queries about the consultation. A total of 22 responses to the consultation were received, mainly from representative organisations and other bodies with an interest in the Pubs Code.

10.3 Following the helpful responses and insight provided by the respondents to the consultation, the Government determined to amend the Pubs Code in order to improve its practical operation. While views varied, the changes that drew overall support reflect those as set out under paragraphs 7.9 – 7.15 and the Government's response to the consultation is available online at www.gov.uk/government/consultations/options-to-amend-the-pubs-code.

11. Guidance

11.1 The Pubs Code Adjudicator has, amongst others, powers to issue information, advice and guidance on matters relating to the Pubs Code. The changes will not take effect

until 1 April 2022 and the PCA will consider the exercise of those powers to issue guidance or advice as appropriate.

12. Impact

12.1 There is no, or no significant, impact on business, charities or voluntary bodies.

12.2 There is no, or no significant, impact on the public sector.

12.3 A full Impact Assessment has not been prepared for this instrument because assessed costs have been deemed to be below the de-minimis threshold. Pub-owning businesses that sell a tied pub will be required to inform the PCA with details of the new owner, incurring a small administrative cost. Through the amendments to the 2015 Act, a pub-owning business could come into scope of the Pubs Code more quickly and fall out of scope more slowly, incurring annual regulatory costs sooner or for longer than before. Amending the comparison period used to determine whether a significant price increase has occurred for a tied product or service will likely result in a small administrative saving for POBs. The amendments to the market rent only option are not anticipated to impose additional compliance burdens on pub-owning businesses or tenants. On an equivalent annual basis, the expected total direct cost to business of these amendments falls substantially below the De Minimis threshold.

13. Regulating small business

13.1 The legislation applies to activities that are undertaken by small businesses but these will be some of the main beneficiaries of the amendments made. The additional direct costs estimated in this assessment will fall on pub-owning businesses in scope of the Pubs Code, the majority of which will be large businesses due to the requirements of owning at least 500 tied-pubs in order to fall in scope of the Regulations. However, some small businesses may be indirectly affected by the amendments, through potentially more frequent price rises if pub-owning businesses move from a model of adjusting prices every 13 months to every 12 months due to amendments to the comparison period used to determine whether a significant price increase has occurred.

13.2 The impact of the requirements on small businesses (employing up to 50 people) is minimised as the amendments are likely to benefit smaller businesses (tied tenants) more than any indirect costs affecting them. For example, tied tenants may benefit from the additional negotiation time available in the market rent only option following the improvements to the process. This is likely to outweigh any negative impact on tied tenants, the main small businesses affected.

14. Monitoring & review

14.1 The approach to monitoring of this legislation is set out in the 2015 Act and the Pubs Code and requires the Secretary of State to review the effectiveness of the Pubs Code and associated regulations every three years.

14.2 The amendments to the 2015 Act and the Pubs Code being made by this instrument will be subject to the statutory review under those pieces of legislation.

15. Contact

15.1 Stuart Roberts at the Department for Business, Energy and Industrial Strategy email: stuart.roberts@beis.gov.uk can be contacted with any queries regarding the instrument.

15.2 Alesha De-Freitas, Deputy Director for Competition Policy at the Department for Business, Energy and Industrial Strategy can confirm that this Explanatory Memorandum meets the required standard.

15.3 Paul Scully, Parliamentary Under Secretary of State (Minister for Small Business, Consumers and Labour Markets) at the Department for Business, Energy and Industrial Strategy can confirm that this Explanatory Memorandum meets the required standard.