

SCSI/RICS Code of Practice

# Service charges in commercial property

Professional Statement – 1st edition



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1st edition

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# SCSI / RICS professional standards and guidance

## Definition and scope

SCSI / RICS professional statements set out the requirements of practice for SCSI / RICS members and for firms that are regulated by SCSI / RICS. A professional statement is a professional or personal standard for the purposes of SCSI / RICS Rules of Conduct.

## Mandatory vs good practice provisions

Sections within professional statements that use the word 'must' set mandatory professional, behavioural, competence and/or technical requirements, from which members must not depart.

Sections within professional statements that use the word 'should' constitute areas of good practice. SCSI / RICS recognizes that there may be exceptional circumstances in which it is appropriate for a member to depart from these provisions – in such situations SCSI / RICS may require the member to justify their decisions and actions.

## Application of these provisions in legal or disciplinary proceedings

In regulatory or disciplinary proceedings, SCSI / RICS will take into account relevant professional statements in deciding whether a member acted professionally, appropriately and with reasonable competence. It is also likely that during any legal proceedings a judge, adjudicator or equivalent will take SCSI / RICS professional requirements into account.

SCSI / RICS recognizes that there may be legislative requirements or regional, national or international standards that have precedence over an SCSI / RICS professional statement.

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# Document status defined

The following table shows the categories of SCSi / RICS professional content and their definitions.

| Publications status   |   |
|---|---|
| Type of document  | Definition  |
| SCSi / RICS Rules of Conduct for Members and SCSi / RICS Rules of Conduct for Firms | These Rules set out the standards of professional conduct and practice expected of members of SCSi / RICS.  |
| International standard  | High-level standard developed in collaboration with other relevant bodies.  |
| SCSi / RICS professional statement (PS)   | Mandatory requirements for SCSi / RICS members and regulated firms.   |
| SCSi / RICS guidance note (GN)  | A document that provides users with recommendations or an approach for accepted good practice as followed by competent and conscientious practitioners.       |
| SCSi / RICS code of practice (CoP)  | A document developed in collaboration with other professional bodies and stakeholders that will have the status of a professional statement or guidance note. |



# Glossary

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| <b>Accrual accounting</b>                   | Considered to be the standard accounting practice for most service charges, with the exception of very small operations. This requires that costs be recognised in the accounts when incurred, not when the invoice is actually paid. This is the opposite of cash accounting, which recognises transactions only when there is an exchange of cash.   |
| <b>Accruals</b>                             | Expenses incurred in a period for which no invoice has been received at the period end. As the cost relates to the period, it is to be charged to the service charge account for that period.  |
| <b>Adjudication</b>                         | A simple and efficient method of settling disputes. An adjudicator uses their own knowledge and investigations while weighing the evidence presented by the opposing parties. This helps them to reach a decision that is legally binding until the original dispute is referred to arbitration or the courts, or is settled between the parties themselves.   |
| <b>Administration charges</b>               | The manager's costs in procuring services directly (in other words, not through a contractor) where the actual cost of the service (e.g. the site-management team) is recovered through the service charge. The administration charge is intended to reimburse the manager's indirect costs (e.g. payroll, staffing, etc.) and is recorded to the cost category where they are incurred, as would apply if the service(s) were contracted. |
| <b>Alternative dispute resolution (ADR)</b> | The collective description of methods used to resolve disputes other than through the normal judicial process.   |
| <b>Allocation</b>                           | The splitting of the costs of a service to assign them to a specific schedule or cost category.  |
| <b>Amenities and facilities</b>             | Desirable or useful features, services or resources that are provided to make a place more pleasant and convenient, e.g. information desk, way finding, mobility services, children's play areas and clubs, free Wi- Fi, Click and Collect services, free phone charging, customer lounges or seating areas, etc.  |
| <b>Apportionment</b>                        | The spreading of costs within schedules between occupiers who benefit from the services in that schedule, based on the availability, benefit and use of the services.  |
| <b>Arbitration</b>                          | A procedure whereby two parties in a dispute agree to be bound by the decision of an independent third party (the arbitrator). The role of an arbitrator is similar to that of a judge, although the procedures are often less formal. An arbitrator is usually an expert in their own right.  |

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| <b>Arrears statement</b>                | A transaction list of all unpaid charges demanded by the landlord from the tenants, collated on a tenant by tenant basis.  |
| <b>Balancing service charge</b>         | The resulting difference between an individual tenant's apportionment of expenditure and the on-account service charges demanded from that tenant for any specific service charge accounting period, also having regard to any service charge concessions that may have been granted.  |
| <b>Buyer</b>                            | The buyer is the new/prospective owner of the property.  |
| <b>Commercial property</b>              | All property that is not residential or agricultural and includes retail, office, industrial and leisure properties  |
| <b>Completion date</b>                  | The date of the sale of a property.  |
| <b>Customer services</b>                | The services provided to help and assist visitors to a property.   |
| <b>Depreciation charge</b>              | The 'cost' to the owner representing the measure of the wearing out, consumption or other reduction in life of an asset.   |
| <b>Direct charges</b>                   | Any expenditure that is charged directly to individual occupiers and not funded via the on-account service charges.  |
| <b>Early Neutral Evaluation (ENE)</b>   | ENE is an ADR technique. ENE is voluntary, confidential and conducted on a 'without prejudice' basis. The evaluation is non-binding, and aims to help clarify and define legal and factual issues in the dispute, identifying risks and likely outcomes before further significant resources are spent on the matter.  |
| <b>ICAEW</b>                            | The Institute of Chartered Accountants in England and Wales.   |
| <b>Independent expert determination</b> | This is a process where an independent third party, acting as an expert rather than as a judge or arbitrator, is appointed to decide a dispute (as an independent expert or 'expert determiner' – not to be confused with an 'expert witness').  |
| <b>In trust</b>                         | Money or monies kept in a separately named account that is held in trust within the bank account of its owner.   |
| <b>Landlord</b>                         | The term used in landlord and tenant legislation to denote the person or company who owns and rents or leases premises. The person or company may own the freehold or may have a superior leasehold interest in the property themselves. To avoid confusion, this term is only used in this professional statement where the context makes this necessary. In all other cases the reference is to 'owner'. |

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| <b>Manager</b>                      | The person or team that budgets, forecasts, procures, manages and accounts for the services that comprise the service charge, whether they are the owner, an in-house team, management company or a managing agent (including any wholly or partly owned related companies).  |
| <b>Management charge</b>            | The management charge is the reasonable price for the total cost of managing the provision of the services at the location, and relates only to work carried out in managing and operating the services and administering the service charge.   |
| <b>Management fees</b>              | <p>The remuneration of the manager and related entities including any profit element, for managing the services comprised in the service charge. Typically, this includes the supervision of the site team, overseeing the site contractors and the accounts work necessary to budget, forecast, manage, disperse, balance and apportion the service charge. Specifically, these fees are not to include property management work separate from the service charge, such as owner approvals, income generation or rent collection.</p> <p>Where the subject property/site-management team is not sufficiently large enough to justify specific service managers (for example, a health and safety manager or building surveyor) additional specialist fees may be charged to the relevant cost category for the 'manager provided' service.</p> |
| <b>Management handover date</b>     | The date on which the responsibility to manage the property transfers from one property manager to another.   |
| <b>Marketing and promotions</b>     | Advertising and other forms of promotion intended to bring additional custom / benefit to the scheme (as distinct from attractions and entertainments of a general amenity, benefit, service or attraction).  |
| <b>Matrix</b>                       | An array of costs set out in rows and columns, which is used as a system of methods and principles in the allocation and apportionment of costs between occupiers.  |
| <b>Mediation</b>                    | The generally accepted description of commercial mediation is a voluntary, non-binding, private dispute resolution process in which a neutral person helps the parties to reach a negotiated settlement. A core principle of mediation is that the parties 'control' the outcome, rather than it being imposed on them.   |
| <b>Not for profit, not for loss</b> | Descriptions of the service charge costs, which are not inflated for profit (although the individual services within the costs may contain a profit element for the individual supplier); but also, there is no residual loss (assuming a fully let property with no concessions on service costs to specific occupiers) left for the owner to pay.   |

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| <b>Occupier</b>                               | A person in possession or occupation of premises and usually responsible for payment of the service charge to the owner.  |
| <b>On-account service charge</b>              | An estimated charge raised in advance and anticipation of the final service charge liability, calculated from the service charge budget.  |
| <b>Owner</b>                                  | The person who receives or is entitled to receive the rent. This person is usually responsible for the provision, management, and administration of the services and the service charge. In practice the owner may appoint a manager to discharge the owner's obligations under the terms of the lease.   |
| <b>Planned Preventative Maintenance (PPM)</b> | PPM is maintenance that is performed purposely and regularly to keep the fabric, facilities, plant and equipment of a building in satisfactory operating condition by providing for systematic inspection, detection and correction of failures, either before they occur or before they develop into major defects. PPM also helps to identify the point at which such items can reasonably be deemed to have reached the end of their economic life, such that replacement or renewal may be necessary. PPM programmes are usually prepared in periods of between 5–10 years in advance, and is to be regularly reviewed and updated at frequent intervals. |
| <b>Prepayments</b>                            | Expenses paid in a given period that relate to the following period in whole or part.   |
| <b>Rateable value</b>                         | An official estimate of the value of a property used as a basis of local taxation.  |
| <b>Rebranding</b>                             | The upgrading of house or corporate style, logos, names badges, etc.  |
| <b>Refurbishment</b>                          | The renovation of fabric or equipment to bring it to a workable or better condition. It is often a different concept to repair or improvement, and usually includes elements of both. Where a refurbishment project includes improvements or enhancements beyond normal repair or maintenance, this element of the cost would usually be met by the owner.  |
| <b>Re-launching</b>                           | Marketing to change the perception in the eyes of its target audience. This may be for letting purposes (an owner's cost), or may benefit both owner and occupier – for example, a shopping centre following refurbishment – in which case, an agreement is to be reached as to how the relaunch costs are split between the parties.   |
| <b>Reserve fund</b>                           | A fund formed to meet anticipated future costs of maintenance and upkeep in order to avoid fluctuations in the amount of service charge payable each year (for example, for external cleaning and redecoration).  |

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| <b>Retail Price Index (RPI)&amp; Consumer Price Index (CPI)</b> | A measure of inflation published monthly, or such other comparable national statistics published from time to time.   |
| <b>Sale contract</b>  | The contract setting out the terms on which the property is to be sold and transferred between the seller and buyer.  |
| <b>SCSI Dispute Resolution Service (DRS)</b>                    | SCSI DRS can provide a simple, fast and cost-effective approach to resolving disputes.  |
| <b>Seller</b>   | The previous/current owner of the property.   |
| <b>Services</b>   | Where the word 'services' is used, the reference includes works, such as maintenance and repair of the fabric and structure, and core services, such as the provision of heating, lighting, cleaning and security, etc.   |
| <b>Service charge account</b>                                   | The service charge funds held for a specific property.  |
| <b>Service charge apportionment</b>                             | The method and details of apportioning liability between tenants for contributing to a service charge.  |
| <b>Service charge apportionment matrix</b>                      | Schedules containing as a minimum the information shown in Appendix C (CD and CE).<br>Any on-account service charge or balancing service charge owed by a tenant to the landlord.   |
| <b>Service charge arrears</b>                                   | The expenditure estimated by the landlord or its manager that will be incurred in a given service charge accounting period.   |
| <b>Service charge budget</b>                                    | A comprehensive comparison of all service charge income demanded against all service charge expenditure (including accruals and prepayments) for a given service charge accounting period. This enables the calculation of any balancing charges and credits due from tenants and/or landlords. |
| <b>Service charge reconciliation</b>                            | The allocation of service charge costs into separate parts to reflect the provision, usage, benefit or availability of services between individuals or groups of occupiers.   |
| <b>Schedules</b>  | A fund formed by periodically setting aside money for the replacement of a wasting asset (for example, heating and air-conditioning plant and equipment, lifts, etc.).  |
| <b>Sinking fund</b>   | The account of service charge expenditure/costs and related notes. Commercial leases usually provide for an annual statement of service charge expenditure to be issued to occupiers following the end of each service charge period.   |

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| <b>Statement of service charge expenditure</b> | The term used in landlord and tenant legislation to describe any person (physical or legal) who owns the leasehold interest in property and is liable to pay the service charge under the terms of the lease.   |
| <b>Tenant</b>                                  | As with 'landlord', this term is only used when the context requires; references in the context of commercial property and service charges are to 'occupier'.   |
| <b>Value for money</b>                         | Good value for money is the optimal use of resources to achieve the intended outcomes. 'Optimal' means 'the most desirable possible given expressed or implied restrictions or constraints'. Value for money is not about achieving the lowest initial price.       |
| <b>Virtual bank account</b>                    | A subsidiary or sub-account of a physical bank account that allows segregation of funds, e.g. in respect of individual properties, from other funds in the same account or alternatively where funds can be clearly identified through the use of separate ledgers. |
| <b>Void liabilities</b>                        | The share of the agreed service charge expenditure for any service charge accounting period that is attributable to vacant lettable accommodation   |



# 1. Introduction

Industry collaborative guidance for the management and administration of service charges in commercial property was first published by the RICS in 1996. This iteration of what has become known as the Service Charge Code and is now published as a 1st edition SCSi professional statement.

In the 23 years since its inception, the code has had a profound and positive impact on the commercial property sector and has facilitated major improvements in standards of delivery and accountability for service charges.

The move to formalising the code as an SCSi professional statement is a further significant step forward. This step not only underlines the importance of managing service charges consistently and effectively but also represents a continued evolution of best practice processes and procedures in an increasingly complex and challenging area of commercial property management, which requires practitioners to have a particular and demanding skill set.

This professional statement sets out best practice in the management and administration of service charges in commercial property and provides mandatory obligations that SCSi members and regulated firms engaged in this area must comply with.

For clarity, please be aware that this entire document is an SCSi / RICS professional statement and SCSi / RICS expects that members engaged in activity relating to service charges will be familiar with and comply with the whole document.

If members depart from the best practice requirements set out in the document, they should only do so for justifiable reasons. It is not acceptable to simply comply with the mandatory obligations contained in this document.

**This professional statement is effective for all service charge periods commencing from 1 April 2020 and supersedes the SCSi code of practice 'Service charges in commercial property, 3rd edition'.**

## 1.1 Limitations of the professional statement

This professional statement cannot override the lease but, if read in conjunction with it, can enable users to identify the best way forward in interpreting that lease to ensure effective management of services.

This professional statement sets out specific mandatory requirements for SCSi / RICS members and there may be legal and/or disciplinary consequences for members in departing from professional statements, which may lead to a finding of negligence against a surveyor. However, subject always to the terms of the lease, a failure to meet the standards set out in the professional statement will not of itself be sufficient to negate or limit an occupier's liability to pay a service charge in accordance with the terms of the lease.

As business practice constantly evolves, so it is with service charges. Negotiating a new lease, or the renewal of an existing lease, provides an ideal opportunity to ensure that modern and flexible best practice service charge clauses are incorporated within the lease contract to facilitate effective management of the property and aid the relationships between the parties.

An Alternative Dispute Resolution (ADR) clause will enable any difficulties during the term of the lease to be resolved efficiently and with reduced cost. All parties should carefully consider the principles and requirements of this professional statement prior to entering into a new or renewal lease.

## 1.2 Proportionality

The extent to which owners and managers should seek to comply with the recommended best practice processes and procedures set out in this professional statement will often depend on a variety of issues, such as the size, nature and type of property, the aggregate of the total service charge costs and the amounts payable by individual occupiers, and this should be consistent with best-value principles.

Nevertheless, owners, managers and occupiers should seek to comply with the mandatory requirements and core principles set out in this professional statement at all times.

### 1.3 The service charge arrangement

Service charges deal with the costs of servicing and operating a property, to comply with the use, the services and facilities provided.

The service charge arrangement is set down in the lease(s) and the aim is to entitle the owner to recover their charges and any associated administrative costs incurred in the operational management of the property. This will include reasonable costs of maintenance, repair and replacement (usually where beyond economic repair) of the fabric, plant, equipment and materials necessary for the property's operation, plus any other works and services the parties agree are to be provided by the owner, but subject to reimbursement by the occupier.

If the property is fully let, the owner will normally be able to recover all expenditure on services through the service charge, except any concessionary discounts the owner may have given.

Usually, there will be a manager who administers those services, for which they will receive a fee.

### 1.4 New service charge lease provisions

The City of London Law Society and Practical Law Company have both drawn up service charge lease provisions that have been specifically designed to comply with the principles and provisions of this professional statement. These can be accessed from the following websites:

*City of London Law Society:*  
[www.citysolicitors.org.uk/index.php?option=com\\_content&view=category&id=161&Itemid=471](http://www.citysolicitors.org.uk/index.php?option=com_content&view=category&id=161&Itemid=471)

*Practical Law Company:* <http://uk.practicallaw.com/3-339-5002?q=service+charge+clauses>

Please note that these provisions **relate to UK practice** and should be used only with legal advice.

### 1.5 Using this code

This code sets down best practice in the management and administration of service charges in commercial property.

Section 2 of this document outlines the aims and objectives of this professional statement, along with stating its mandatory requirements.

Section 3 sets out the core principles.

Section 4 gives recommendations and guidance on how the professional statement can be followed.

The Appendices contain additional information and resources to support an understanding of the professional statement and assist with its implementation.

This code is freely available at [www.scsi.ie](http://www.scsi.ie)

## 2. Mandatory Requirements for professionals

### 2.1 Aims and objectives

- To improve general standards and promote best practice, uniformity, fairness and transparency in the management and administration of services charges in commercial property.
- To ensure timely issue of budgets and year-end certificates.
- To reduce the causes of disputes, and to provide guidance on the resolution of disputes if these arise
- To provide guidance to solicitors, their clients (whether owners or occupiers) and managers of service charges in the negotiation, drafting, interpretation and operation of leases, in accordance with best practice.

**Professionals involved in the management of service charge accounts must act in accordance with the following Mandatory principles:**

1. All expenditure that the owner and manager seek to recover must be in accordance with the terms of the lease.
2. Subject to section 5.7, owners and managers must seek to recover no more than 100% of the proper and actual costs of the provision or supply of the services.
3. Owners and managers must ensure that service charge budgets, including appropriate explanatory commentary, are issued annually to all tenants.
4. Owners and managers must ensure that an approved set of service charge accounts showing a true and accurate record of the actual expenditure constituting the service charge are provided annually to all tenants.
5. Owners and managers must ensure that a service charge apportionment matrix is provided annually to all tenants.
6. Service charge monies (including reserve and sinking funds) must be held in one or more discrete (or virtual) bank accounts.
7. Interest earned on service charge accounts, or where separate accounts per property are not operated, a proper and reasonable amount of interest calculated on normal commercial rates, must be credited to the service charge account after appropriate deductions have been made.
8. Where acting on behalf of a tenant, practitioners must advise their clients that if a dispute exists any service charge payment withheld by the tenant should reflect only the actual sums in dispute.
9. When acting on behalf of a landlord, practitioners must advise their clients that following resolution of a dispute, any service charge that has been raised incorrectly should be adjusted to reflect the error without undue delay.

The above mandatory requirements represent what is considered an acceptable standard of performance for SCSI qualified professionals and regulated firms. To provide a service which represents best practice in the management of service charges, practitioners should also have regard to the core principles.

“Tenants who agree to service charge clauses under which they contract to pay against a surveyor’s estimate or an accountant’s certificate rely upon the professional people involved performing their roles with professional scrupulousness, diligence, integrity and independence and not in a partisan spirit, supposing their only task to be to recover as much money as they can for the landlord.”

Jonathan Gaunt QC sitting as a Deputy High Court Judge  
Princes House Ltd v Distinctive Clubs Ltd [2006] All ER (D) 117 (sep). [2007] 14 EG 104 (CS)

### 3. The core principles

These core principles underpin and support the mandatory requirements listed in section 2 of this professional statement. It is acknowledged that some of the following principles may be difficult to quantify, and in rare circumstances strict compliance may not always be possible. The appropriate level of compliance may be based on the professional judgment of all parties as to what is appropriate and reasonable considering all the circumstances.

#### *The service costs*

1. All costs should be transparent so that all parties, owners, occupiers and managers, are aware of how the costs are made up. Management fees should be on a fixed-price basis with no hidden mark-ups.
2. Best practice recommends that services are procured on an appropriate value-for-money basis, and that competitive quotations are obtained, or the costs benchmarked.
3. Owners should not profit from the provision or supply of services. Save for a reasonable commercial management fee that reflects the actual costs of managing the services, the amount an owner may recover is limited only to the proper and actual cost incurred in the provision or supply of services.

#### *Allocation and apportionments*

4. Costs should be allocated to the relevant expenditure category. Where reasonable and appropriate, costs should be allocated to separate schedules and the costs apportioned to those who benefit from those services.
5. The basis and method of apportionment should be demonstrably fair and reasonable to ensure that individual occupiers bear an appropriate proportion of the total service charge expenditure that clearly reflects the availability, benefit and use of services.

#### *Communication and consultation*

6. While the owner has the right to set the standards by which his or her investment will be managed and has a duty to manage, managers should consult with occupiers with regard to the standard and quality of service charge provision required.
7. Managers should communicate with occupiers to ensure services are delivered effectively for the benefit of all, and to ensure that occupiers understand what they can expect to receive and how much they are required to pay.
8. Managers claiming compliance with the principles of this professional statement should be transparent in demonstrating how they comply with it.

#### *Duty of care*

9. Certified accounts of expenditure are to represent a true and accurate record of expenditure incurred. Those certifying service charge accounts should recognise that they have a duty of care to both owners and occupiers to act with professional care, diligence, integrity and objectivity.
10. The owner and/or manager has a duty to manage the property, as well as a duty of care to both the occupiers, who entrust the spending of their own business overhead and cash flow by funding the services, and to the owner whose investment they are servicing.

#### *Financial competence*

11. When incurring costs in the provision of services, the manager is spending the occupiers' money. Managers are therefore expected to demonstrate a high degree of competence, professionalism, integrity, diligence, objectivity and transparency in dealing with the service charge accounts.

12. When issuing statements of accounts and/or certifying expenditure, managers should do so in a non-partisan spirit, acting as experts. The manager will therefore endeavour to ensure that all costs have been incurred and are properly recoverable in accordance with the leases.
13. Service charge monies for each property must be held in one or more separate and discrete bank accounts in recognition of the fact that the monies are being held to provide for the procurement and delivery of the services.
14. All interest earned on service charge accounts must be credited to the service charge account after appropriate deductions have been made (e.g. bank charges, tax, etc.)
15. Annual statement of service charge expenditure should be supported by an independent accountant's review in line with the ICAEW Technical Release (Tech 09/14).
16. The industry standard cost classifications should be used in reporting budget and actual expenditure.

### **Occupier responsibilities**

17. Occupiers should ensure prompt payment of all legitimate service charge on-account and balancing charges. Where a legitimate dispute exists, any payment properly withheld should reflect only the actual sums in dispute – both parties are expected to proactively engage to resolve the dispute.
18. Occupiers should recognise that the service charge provision of any lease has legal effect, and should ensure that any representatives involved in discussions, meetings, etc. have an appropriate level of responsibility and authority to make decisions concerning service charge matters.
19. In recognition that value for money and maintenance of quality standards will be enhanced through partnership, occupiers should be proactive in assisting owners in the operation and utilisation of services and service systems – for example, by separating waste to facilitate appropriate and cost-effective recycling, adopting energy-saving measures, etc.

### **Right to challenge / Alternative Dispute Resolution (ADR)**

20. All new leases (including renewals) should make provision for either party to require the resolution of disagreements through the use of ADR as a cost-effective alternative to court action.

21. If the parties cannot agree a mediator, or an independent expert to determine the dispute, the President of the SCSI should (on request) nominate a suitable person. Where leases do not allow for ADR, parties are reminded that there is nothing to stop them agreeing to use ADR to resolve a dispute.

### **Timeliness**

22. Communication and consultation between managers and occupiers should be timely and regular to encourage and promote good working relationships and understanding with regard to the provision, relevance, cost and quality of services. Timely and regular communication and consultation will help avoid disputes and resolve them quickly should they arise.
23. Managers should issue budgets to occupiers, including an explanatory commentary at least one month prior to the start of the service charge year. Detailed statements of actual expenditure, together with accounting policies and explanatory text, should be issued within four months of the service charge year-end.

### **Transparency**

24. Transparency is essential to achieving good communication. By being transparent in the accounts, the explanatory notes, policies and day-to-day management, the manager will help prevent disputes. Prompt notification of material variances to plans or forecasts ensures better working relationships between owner, manager and occupier.

### **Value for money**

25. Service quality should be appropriate to the location, use and character of the property. The manager should procure quality service standards to ensure that value for money is achieved at all times. The aim is to achieve effective, value-for-money service rather than merely the lowest price.

### **Exclusions**

26. Service charge costs should not include any of the following:



- a) Any initial costs (including the cost of leasing of equipment) incurred in relation to the original design and construction of the fabric, plant or equipment.
- b) Any setting up costs, including costs of fitting out and equipping the on-site management offices that are reasonably considered part of the original development cost of the property.
- c) Any improvement costs above the costs of normal maintenance, repair or replacement. Service charge costs may include enhancement of the fabric, plant or equipment, where such expenditure can be justified following an analysis of reasonable options and alternatives, and with regard to a cost-benefit analysis over the term of the occupiers' leases. Managers should provide the facts and figures to support and vindicate such a decision.
- d) Future redevelopment costs.
- e) Costs and fees relating to the owner's investment interest, for instance, asset management and rent collection, cost of letting units and matters between the owner and an individual occupier. This last category may include activities such as enforcement of lease covenants, dealing with landlord consents for assignments, sub-letting, alterations, rent reviews, additional opening hours, etc. unless demonstrably for the overall benefit of the property
- f) Costs attributable to void premises and the owner's own use of the property.
- g) Any costs arising out of the failure/negligence of the manager or owner.



## 4. Recommended best practice to support the core principles

### 4.1 Standard and quality of service provision

The aim of service provision is to ensure that services are beneficial and relevant to the needs of the property, its owner, its occupiers and their customers.

Managers and occupiers should consider the nature, type and complexity of each property, as the levels and standards of service provided will differ according to these factors. In providing these services, the aim is to achieve effective, value for money service rather than the lowest price.

The manager is responsible for ensuring that the standards of services provided are monitored, that the quality and cost of the services provided are regularly reviewed, and, where possible, to demonstrate that service standards are being delivered and that value for money is being achieved.

It is recommended that management policies and procedures be established to define the procurement, administration and management of services, and to ensure the respective obligations of owner and occupier are discharged and services are provided efficiently, economically, cost-effectively and safely.

Where there are sound reasons for implementing alternative procedures to those set out in the professional statement, the manager should explain and justify these in advance.

Effective communication is key to achieving best practice. The aim is to provide transparency between manager and occupier in the way services are provided and managed, and in how the costs of these services are recovered.

On occasion, additional services will be provided outside the service charge. Occupiers are entitled to expect similar transparency, accountability, etc. in these services. The professional statement applies to these as well.

### 4.2 Staffing and personnel

On-site management staff are required to have a sound knowledge of appropriate modern business practices and to be adequately skilled in order to provide the best and agreed performance standards. As they will need appropriate skills in general management, employment and health and safety

matters, any necessary training costs may also be covered by the service charge.

To ensure the services are provided efficiently and cost-effectively, appropriately sufficient staffing of the right type and calibre is to be provided. In keeping with the goal of transparency, it is best to declare the total costs for such additional staff.

Site-management teams and managers should perform according to defined standards. It is also advisable to measure and review performance regularly against these performance standards.

Where reviews of staffing levels are undertaken, it is reasonable that costs associated with achieving beneficial changes – such as the termination of employment contracts – will be recovered under the service charge. This is provided that such costs can be justified following the analysis of reasonable options, and that the purpose is proven to achieve greater cost-effectiveness and value for money.

### 4.3 Management Costs

#### 4.3.1 Total cost of management

The total cost of management is the reasonable price for managing the provision of the services at the location, and relates only to work carried out in managing and operating the services and administering the service charge.

The total cost of management might comprise two elements:

- the fee charged by the manager for managing and supervising the services at a site (the management fee); and
- the cost of the site-specific management staff, whether based on-site in a full- or part-time capacity (the site-management costs).

No two buildings are identical in the way they need to be run to meet the requirements of all parties with an interest in the property. Management fees and site-management costs will need to be set at the appropriate level. It is not for this professional statement to prescribe the operating business model of the manager.

Where, for instance, a regional facilities manager is employed to oversee a number of properties, managers should be aware of the additional costs in creating a tiered management structure and should be prepared to demonstrate that the total cost of management is fair and reasonable in the circumstances and consistent with the value for money principles set out in this professional statement.

Best practice requires transparency and a management structure where costs are clearly identified and explained. It is therefore recommended that this information be contained within the explanatory notes included in the budget, along with a clear statement of the actual expenditure to occupiers.

#### 4.3.2 Management fees

The management fees charged shall comprise only the reasonable costs and overheads borne in the process of operating and managing the services. These would also reflect the actual work necessary to fulfil the principles of this professional statement. It is recognised that whoever is providing the service is entitled to cover their costs and overheads, including a reasonable profit element.

Management fees should relate only to the actual work carried out in managing the service charge. Other costs – for instance, asset management and rent collection should be excluded from the service charge management fee, which would be stated in the service charge report.

The professional statement requires that fees be set on a fixed-price basis rather than being calculated as a percentage of expenditure. Fees based on a percentage of service costs are no longer considered appropriate and are considered to be a disincentive to the delivery of value for money. The management fee should, therefore, be a fixed fee subject to annual review or indexation.

It is recognised that many leases refer to the management fee as a percentage of the total service charge, or contain a percentage cap.

This professional statement cannot override the terms agreed between the parties and recorded in the lease. However, where the lease limits the amount or quantum of the fee recoverable from occupiers it is a matter between the owner and occupier and should not prevent or limit the manager's ability to charge a commercial fee that reflects the requirements of this professional statement. In certain circumstances, this may result in a shortfall in the recovery of service charge costs on behalf of the owner, but the overriding principle should be to achieve best-practice principles for the management and

administration of services charges in commercial property. Managers should confirm in the service charge report:

- the basis of their appointment;
- when they were appointed; and
- the basis of the management fee payable, which is recoverable under the service charge.

Where the owner manages the property 'in-house' they should have due regard to the principles as outlined above, and be able to support the basis of their fees when benchmarked against other comparable service providers.

Where a lease includes a cap on the amount of management fee chargeable it is the general intention that it refers to the fee the manager receives and not the total cost of management as set out in 2.3.1.

Where specialist reports (e.g. fire-risk assessment reports, Disability Access reports, health and safety reports, etc.) are prepared by specialists working for the same organisation as the manager, the costs should be excluded from the management fee.

Fees for these additional services should represent value for money and be clearly and separately stated within the service charge reports issued to tenants and included under a related cost classification.

#### 4.3.3 Other income

There should be transparency with regard to all other sources of income and related income or other benefits to the manager arising out of the management or provision of services, which should be declared in the annual year-end service charge accounts.

On request, owners and managers should declare what additional services are provided and the income received for same. Any additional fees should be in return for a service of value and must be proportionate to the service provided.

#### 4.3.4 Duties of the manager

The owner has the duty to manage or delegate management of the property, and the responsibility to administer and account for the tax properly due on the service charge.

*Best practice requires the manager to recognise a duty of care, both to the occupiers who fund the services being provided, and to the owners whose investment they are servicing.*

The manager will usually perform additional roles and duties relating to investment interests, for instance asset management and rent collection. In such cases, the fees the manager charges in relation to performing such additional duties should be excluded from the service charge management fee.

#### 4.3.5 Site-management costs

Site-management costs are the full employment costs for sufficient staff, as described in section 1.2. The job titles of the staff will vary, however, the total cost of the staff will include wages, PRSI, tax, compliance with statutory requirements, training and other appropriate benefits.

Site-management costs might also include:

- the costs of providing appropriate office accommodation and administrative support where necessary;
- a fee representing the human resources (HR) and payroll costs associated with dealing with staff (often referred to as an administration charge); and
- separate specialist consultancy fees payable, for instance, in connection with the carrying out of health and safety risk assessments, asbestos surveys, etc. and which should be clearly identified in the service charge accounts within a related cost classification and referred to in the expenditure report notes.

One way of ensuring the costs reflect value for money is to compare them to a third party providing similar services. Where such fees are included the basis of calculation and/or quantum of the fees included should be clearly communicated to occupiers to aid transparency.

The total on site management cost should be explicitly shown in the service charge accounts and allocated under the appropriate cost heading. For clarity, staff costs should be split between other account code headings i.e. security, cleaning etc unless there is an appropriate reason for not doing so.

For instance, the cost of an on-site facilities management team and on-site contract managers of the main building services, e.g. security or cleaning managers (either directly employed staff or those employed through third-party agencies etc.) should be included as part of the 'security or cleaning cost classification.

However, where such costs are not included as a 'site management cost' but allocated to a specific cost heading (i.e. cleaning or security) the manager should be clear and explicit as to how these management costs have been treated.

Where additional management or supervisory functions are carried out by non site-based staff, for instance, a regional/area facilities manager, these costs should be clearly identified and included under the 'site management costs' where they are performing site specific tasks.

Where such functions are performed in place of, rather than in support of, the duties usually expected of or performed by the manager and included within the management fee the costs should not comprise or be regarded as a site management cost but as part of the management fee.

Where the cost of non-site based staff is apportioned to more than one property, the calculation and basis of allocation should be clearly and explicitly communicated to occupiers in the budget reports and statements of actual expenditure. Similarly, any additional administrative charges included should be clearly and explicitly identified.

Where on-site staff are responsible for more than one property, their costs (and any appropriate accommodation and administrative support costs) are best distributed accordingly so that each property covers a fair share of their cost. The service charge report should identify clearly whether this is the case and how the costs are split.

Many buildings require management '24/7'. If it is reasonably considered that a property requires out of hours support a manager may consider supporting the function of the on-site staff by providing a customer support help desk to deal with property matters outside of usual business hours, or when the manager cannot be contacted. Where this is reasonably and necessarily provided as an alternative to employing additional on-site staff, the reasonable cost of running this service may be recovered from the service charge.

If the manager is instructed by a tenant to provide facilities services for their demised property e.g. cleaning, security etc. then the manager's charges for providing these services should be directed to the relevant tenant and not included in the service charge.

Additionally, if the site management team (whose costs are recovered from the service charge) are involved in the administration, oversight or contract management etc. of these tenant services then an appropriate apportionment of their costs should be excluded from the service charge, and the basis for this apportionment should be transparent. In other words, 100% of the site management staff costs should not be recovered from the service charge if the team are also involved in providing tenant services.

#### 4.3.6 Notional rent for management accommodation

Many leases contain provisions for the inclusion of a notional rent within the service charge for management accommodation, or for other premises used in connection with the management of the property. In many cases, management accommodation cannot be separately let, and thus has no market value other than as a location for such an operation. However, there are situations where the management premises comprise accommodation (offices) that would otherwise be lettable space; in these cases, there is an element of rent foregone to provide accommodation for the on-site management team.

It is generally not best practice to charge occupiers notional rent in situations where the premises are incapable of beneficial occupation for any other purpose.

### 4.4 Contract procurement

#### 4.4.1 Service standards and provision

It is best practice to ensure that all contractors and suppliers perform according to written performance standards. On the basis that the manager is approving payment of supplier costs, on trust for the tenants, the manager should regularly measure and review performance against these defined performance standards, as well as to regularly review the appropriateness of the standards used.

#### 4.4.2 Procurement of services

It is the responsibility of the manager to identify the procurement strategy most suitable for the property based on an appropriate level of service and value for money.

In 2011, a new standard covering the procurement of facility-related services was published. British Standard (BS) 8572:2011 Procurement of facility-related services provides owners, operators, facility managers and property managers with guidance and recommendations for procuring a broad range of services that are required to support the physical assets that make up a facility, also the needs of users of that facility.

In July 2018 the RICS / IFMA published a professional statement "Procurement of facility management" which discusses facility management procurement routes and processes open to organisations. It provides information and guidance on the various factors that need to be considered throughout a procurement process, including activities and

key decisions during planning, procurement and post-procurement.

The BS takes the form of guidance and recommendations and is not intended to be quoted as if it were a specification.

The manager may use either an in-house or third-party procurement specialist to deliver best-value solutions, as long as the purpose is to achieve greater cost-effectiveness and value for money. The cost of any procurement specialists employed is considered to be recoverable through the service charge, but the costs should be clearly identified in the service charge report, along with details of whether it is a one-off fee or will be spread over the duration of the contract. It is intended that the fee payable will reflect the work undertaken, which may also be performance-related.

Generally it is the responsibility of the manager or the procurement specialist –

- to develop procurement systems;
- to vet and select the most appropriate contractors, based on track record, skill and management experience; and
- to prepare a contract and specification – including Transfer of Undertakings (Protection Employment) Regulations (TUPE) information – where appropriate.

Contract costs are to be transparent and in accordance with the provisions for transparent accounting.

Appropriate legal and Human Resources advice should be sought where TUPE is likely to arise - for further information see the RICS information paper: TUPE: Information for Property Managers, 3rd edition (2014)'.

The manager or procurement specialist is expected to be responsible for the provision of full pre-qualification assessments of suppliers and contractors in terms of their

- financial standing;
- proven compliance with health and safety;
- appropriate indemnity in respect of the services provided, including any undertakings via subcontractors (with provisions for prior approval thereof); and
- proven environmental / sustainability credentials.

Whether or not managers employ procurement specialists their approach to the procurement process outlined in this section should be transparent. Managers should ensure that there is transparency in procurement fees and charges for verifying contractor financial standing, health and safety records, and environmental credentials etc., including cost or fees charged either to their client or the suppliers and contractors.



If any fees are received from suppliers or contractors, the manager should clearly state, in the service charge accounts, what these are and what they are for.

Managers should also be aware that the practice of requesting fees, other than a reasonable administration charge, from contractors for inclusion in approved contractor lists, contract tendering, etc. is contrary to best practice, and is considered to be wholly inappropriate under any circumstances.

On receipt of tenders, a tender report should be prepared containing recommendations on which contractor is most suitable. Copies of all tender documents should be made available for inspection, if requested. If further copies are required, the manager will be entitled to charge for the time, cost of copying and postage of such documents.

Owners and/or managers are often able to achieve substantial savings and other benefits in the provision of services through bulk purchasing or through the placing of group contracts. However, the pricing of services under such contracts can differ in either providing a single-contract sum, a separate cost per property or a schedule of rates for different services.

Where such bulk or group contracts exist, occupiers are not entitled to have access to documents relating to properties other than the one they occupy. However, where the contract/tender includes other properties, transparency in terms of the apportionment and allocation of costs to the subject property is essential.

Where contracts are reviewed, it is reasonable that costs associated with achieving beneficial change – such as termination of contracts – are recovered under the service charge. This is applicable where such costs can be justified following the analysis of reasonable options, and where the purpose is to achieve greater value for money and cost-effectiveness.

## 4.5 Value for money

Service provision and quality is to be appropriate to the location, use, age and character of the property. The manager should procure quality service standards to ensure that value for money is achieved at all times. The aim is to achieve effective, value for money service rather than the lowest price.

‘Value for money’ can be simply defined as paying no more than is necessary for no less than is required.

Occupiers are to be proactive in assisting managers with operating and using services that are consistent with the aim

of achieving value for money – for example, separating waste to facilitate appropriate and cost-effective recycling.

The manager is to keep all costs under review, and where appropriate (generally every three years), require contractors and suppliers to submit competitive tenders or provide competing quotations. However, where it is considered that formal re-tendering would not be cost-effective or practical, the manager should regularly benchmark the service standards and pricing to confirm that value for money is still being achieved.

In this context ‘regular’ is subject to interpretation as to what is reasonable in the circumstances. Annual review may, in certain circumstances, be considered excessive and not cost effective whereas 3 yearly might be reasonable but 10 yearly would not.

Managers should require major service providers to demonstrate that their services, methods and processes are continually reviewed to ensure value and efficiency.

## 4.6 Direct recoveries

Service charges usually include the cost of utilities for any common parts and services. Traditionally, buildings and/or rent insurance is apportioned to occupiers outside of the service charge arrangement as a directly recoverable cost, with occupiers often being responsible for payment of electricity/gas consumption supplied to the occupied premises direct to the utilities provider. In some circumstances, however, the lease may provide for the cost of buildings insurance and demised electricity to be recovered within the service charge.

Where owners are seeking to recover the cost of insurance and utilities outside of the service charge arrangement, occupiers are entitled to expect the same level of transparency, accountability, etc. in these services, since this professional statement is also applicable to these.

### 4.6.1 Insurance

#### a) Value for money

Where owners are responsible for insuring the property the insurance policy terms should be fair and reasonable and represent value for money and be placed with reputable insurers.

#### b) Commission

The principle of commission retention is now long established. In its base form, the use of commission to cover administrative

costs – including broker fees – is to be recognised, also the owner's ability to benefit from the economies of scale generated by the pooling of risks into a common programme.

Owners, managers and related entities should at all times disclose any remuneration, commission and other sources of income and related income or other benefits received in connection with placing or managing insurance and details of any arrangements that impact on the level of commission e.g. captive entities.

### c) Service

Owners are obliged to provide full insurance details on request, and to be able to explain the process by which occupiers can make claims under the policy. Owners should also provide details of the basis of apportionment of the insurance premiums.

Policies are expected to include an ability to note the interest of occupiers either generically or individually, as well as any subrogation waivers and non-invalidation provisions for the benefit of the occupier. Again, these are to be in line with lease obligations.

Members should refer to the SCSi Guidance Note – 'Insurance for Property Managers 1st Edition'.

### 4.6.2 Utilities

Where a service is provided directly to an occupier or to the occupied premises – such as mains water or electricity supply as distinct from common works and services – it is important that the manager and occupier understand the basis on which the service is provided, and whether the costs are intended to be included within the service charge account, or will be issued as a separate charge.

Separate metering, or full sub-metering of utility supplies, is considered essential to ensure an apportionment of cost between occupiers that reflects actual consumption and usage.

Costs should be recovered in accordance with the terms of the leases, if an administration charge is levied by the manager it should be transparent and clearly communicated to occupiers, and should comprise only the reasonable costs and overheads reflecting the actual work necessary to facilitate the recovery. The recovery should include copies of the original utility invoices, in order to comply with the requirements for transparency set out in this professional statement.

To avoid ambiguity, and to ensure that accurate consumption and billing is recorded for occupiers, it is recommended best practice that the cost of reading meters, where carried out by a third party, is included, subject to legal advice, as an acceptable cost under the service charge as part of the on-site management costs.

Occupiers should be aware of the ever-increasing pressure placed on owners by utility providers for prompt payment and should therefore ensure that all invoices are paid promptly. Where the annual utility charge can be reliably estimated, a regular charge on account subject to periodic adjustment to actual costs may be appropriate.

It is becoming increasingly common for utility companies to request that owners either pay large security deposits or higher energy rates.

Where a lease makes specific provision for the inclusion of a security deposit as a service charge cost, both owners and occupiers are urged to ensure that the lease allows for the occupier's proportion of the deposit to be reimbursed on expiry, or alternatively on sooner determination of the lease, in the event of a change of owner/manager, or if the deposit is otherwise reimbursed by the utility company.

Where a lease makes no such provision, it is considered appropriate for the owners to open a dialogue with occupiers in order to seek to agree to pay a security deposit in return for contract supply rates, as opposed to default supply rates.

The payment of a deposit can be included in on-account payments for the relevant service charge period, credited at year-end and then re-budgeted for the following period. Therefore, if a lease expires in any given period, the occupier will receive an appropriate credit in their final service charge balance.



## 5. Allocation and apportionment

### 5.1 Schedules

Costs should be allocated to the relevant expenditure category. Where reasonable and appropriate, costs should be allocated to separate schedules and the costs apportioned to those who benefit from those services.

The basis and method of allocating and apportioning the service charge expenditure is to be transparent and clearly communicated to all. Any inducements or concessions to attract occupiers to a property should be borne by the owner, and not spread among other occupiers. The rationale for the apportionment between occupiers should be set down in writing, and re-examined annually to see whether there is a need for a new apportionment matrix or new apportionment method to be applied. Where reasonable and appropriate, costs should be allocated to separate schedules, and the costs apportioned to those who benefit from those services.

In many cases, particularly regarding buildings with a variety of users, not all of the occupiers will benefit from the services to the same extent. In such circumstances, it may be necessary to divide the service charges into separate parts (schedules) to reflect the availability, benefit and use of services, with each part being individually apportioned between occupiers according to the core principles. The allocation of costs to separate schedules is essential in achieving a fair and proper apportionment of costs between those occupiers that benefit from specific services. Occupiers will therefore often pay different percentage apportionments under different schedules.

### 5.2 Flexibility

It is worth considering that the availability, benefit and use of the services within a building, and the demand for those services by individual users, could vary over time therefore leases would benefit from being drafted to include flexibility and variation.

For example, additional units may be created or the use of a property may change, thus causing different demands for services and necessitating a change to the costs/payments structure. Even with the grant of shorter-term leases, the ability to change allocation and apportionment methods, where necessary and appropriate, could be made available during the term to ensure service charges are spread fairly and reasonably between beneficiaries and users.

### 5.3 Void and unlet premises

Property owners should meet all costs attributed to unlet premises, as well as any special or personal concessions given to individual occupiers. Owners are also responsible for bearing a fair proportion of costs attributable to their own use of the property – for example, where an on-site management premises is also used for other purposes unconnected with the day-to-day management of the building and services.

### 5.4 The apportionment matrix

Managers are to provide a full apportionment matrix to all occupiers that clearly shows the basis and method of calculation, and the total apportionment per schedule for each unit within the property/complex.

To avoid doubt and to preserve confidentiality this should exclude details of any individual concessions or other arrangements between individual owners and occupiers; these are costs that are normally to be borne by the owner. An individual occupier should be able to clearly verify the basis and method of calculation used in arriving at his or her particular percentage apportionment.

### 5.5 Floor-area apportionment

Apportionment based on floor area is the most common, and often the simplest, method of apportionment. The standard floor-area apportionment is the ratio the premises bear to the total lettable parts of the building.

The 'SCSI Measuring Practice Guidance Notes 2016' sets out definitions of the measurement of buildings and their recommended applications this will include IPMS 1, IPMS 2 and IPMS 3 for office buildings and Gross External Area (GEA), Gross Internal Area (GIA) and Net Internal Area (NIA) for other property types.

Where the service charge is apportioned based on floor area, managers should ensure that the method and basis of measurement used is consistent. In certain situations, it may be appropriate to apportion costs allocated to separate schedule using different methods of measurement, but different measuring methods should not be used in the same schedule.

The basis of measurement used (e.g. GIA, NIA) should be clearly communicated to tenants together with confirmation of

how the floor areas have been established, for example, from computer-generated drawings, other drawings or by laser or tape measurement.

## 5.6 Rateable value apportionments

Rateable values are no longer recommended as an appropriate method for calculating service charge apportionments.

Rateable values take account of a variety of factors relating to value, such as location, etc., and do not generally reflect a reasonable assessment of the benefit and use of common services.

While many leases require service charges to be apportioned based on rateable value, with no provision for any alternative basis to be used and notwithstanding that this professional statement cannot override the contractual terms of any lease, it is nevertheless the view of the SCSi Service Charge Professional Group that rateable value apportionments should be changed to such other recognised methods of apportionment consistent with the aims and aspirations as set out in this professional statement.

Where the use of rateable value apportionments is unavoidable, owners and managers should be aware that rateable values may change over time as occupiers have the right to appeal against assessments by the Valuation Office. In such circumstances, it is considered best practice to use the values in the rating list at the service charge year end date. The date of the rating list and rateable values used should be clearly communicated to occupiers.

## 5.7 Fixed percentage or fixed amount

In some instances, the amount or percentage of the overall service charge costs the occupier pays may be fixed at the time the lease is granted. The fixed percentage or amount offers certainty and simplicity but is inflexible. However, it may be advantageous for short leases where the property or the costs, standard and level of services provided, are unlikely to vary significantly. Provision is often included to review the fixed percentage if the property is altered or extended.

Fixed amounts or fixed service charge percentages can give rise to situations where the total service charge recoverable can be less than or greater than 100% of the actual cost of providing the services. In such circumstances, and notwithstanding the principle that owners must seek to recover no more than 100% of the proper and actual costs of the provision or supply of the services, the terms of the lease remain paramount and this professional statement cannot override the lease.

When dealing with the renewal of leases containing fixed amounts or percentages all parties are encouraged to take reasonable steps to ensure that the terms of the lease reflects the best practice principles set down in this professional statement.

## 5.8 Weighted-floor area apportionment

In addition to the usual recommended methods for the apportionment of service charges, many shopping centre developments often feature a 'weighted-floor area' basis of apportionment that seeks to reflect the different costs involved in servicing different-sized units.

A weighted-floor area apportionment discounts the percentage the occupier will pay over a certain size to reflect the benefit of the services provided. The floor area is divided into bands with a progressive discount, and is a similar concept to the zoning of shops for rental purposes.

For example, a 5,000m<sup>2</sup> unit may not cost five times that of a 1,000m<sup>2</sup> unit, but a 500m<sup>2</sup> unit may cost twice that of a 250m<sup>2</sup> unit.

**There is no such thing as a standard weighting formula. Where the use of a weighted formula is considered to be appropriate, this is to be formulated to reflect the particular circumstances, size of units, layout and use of the scheme being serviced (see below).**

The following is included for illustrative purposes only:

|                                  |   |      |
|----------------------------------|---|------|
| The first 500 m <sup>2</sup>     | @ | 100% |
| The next 500 m <sup>2</sup>      | @ | 80%  |
| The next 2,000 m <sup>2</sup>    | @ | 70%  |
| The next 2,000 m <sup>2</sup>    | @ | 60%  |
| Excess over 5,000 m <sup>2</sup> | @ | 50%  |

In this example, a 1,000 m<sup>2</sup> unit has a weighted floor area of 900 m<sup>2</sup> [i.e. (500 x 100%) + (500 x 80%)] whereas a 10,000 m<sup>2</sup> unit will have a weighted area of 6,000 m<sup>2</sup>. Although 10 times larger in floor area, the 10,000 m<sup>2</sup> unit pays approximately six and a half times the service charge of the smaller unit.

Similarly, the floor area of external units, ancillary basement and upper-floor / mezzanine accommodation, or of remote storage, might be discounted to reflect the reduced benefit derived from certain services as distinct from the internal ground-floor retail space or main offices.

For the avoidance of doubt, a reasonable and fairly administered weighting formula for apportionment of the service charge cannot usually be considered a concession.

## 5.9 Owner's profit centres

Where there is a separate cost or profit centre within a property complex that generates income for the owner that is not credited to the service charge account, the costs associated with maintaining and running that cost centre should not be allocated to the service charge account (for example, car parks, mobile phone masts, advertising, radio aerials, etc.).

If the separate cost / profit centre derives benefit from buildings, equipment staff or services that form part of the service charge, the cost/profit centre will be incorporated into the service charge matrix (for example, the car park, management office, etc.). Alternatively, owners can estimate and declare a contribution to the service charge that reflects the benefit and use of the common services enjoyed.

## 5.10 Tenant alterations

Alterations carried out by tenants may have an impact on or affect the calculation of the apportionment of occupier service charge liabilities.

Tenant alterations that change any factor on which the apportionment calculation is based (such as, but not limited to; floor area, rateable value, or the extent of use and benefit of the services derived) might determine whether adjustments to tenant service charge apportionments would be appropriate.

In the case of a warehouse/distribution centre, the introduction of an additional mezzanine floor, in preference to full eaves-height racking, may not affect or increase the utilisation of the premises, and, therefore, the use and benefit of the common services.

However, a mezzanine floor installed in a unit on a retail park might generate additional sales and customer footfall, with a corresponding increase in goods deliveries, etc. and an increase in the enjoyment, use and benefit of common services such as parking, security, cleaning, etc.

While this situation can often present a dilemma for the landlord, the answer may often be found in the precise wording of the lease. If the lease makes specific reference to the basis on which the service charge apportionment is to be calculated; for instance, for the floor area, the landlord would be obliged to factor in the additional floor area of the demised premises to the apportionment matrix.

Where the lease does not make specific reference to the basis of apportionment and refers, for instance, to a 'fair and reasonable proportion as determined by the landlord's surveyor', the landlord's surveyor, acting as an expert, will be

required to adopt a basis of calculation that conforms with the basic principles of service charge apportionment. This would need to be demonstrably fair and reasonable to ensure that individual tenants bear an appropriate, fair and reasonable proportion of the total service charge expenditure that reflects the benefit of the services enjoyed.

When dealing with alterations to premises, particularly where these require the prior consent or approval of the landlord, it is always desirable that careful consideration be given to the potential impact on the calculation of the service charge, to ensure that the apportionment continues to be fair and reasonable. This is in view of the underlying principles set out in this professional statement.

Landlords are also advised to consider including appropriate wording within any licence for alterations to clarify the position and basis of calculation of the service charge for the future.

## 6. Communication and consultation

### 6.1 Communication

As poor communication often gives rise to disputes, effective communication is key to achieving best practice. Here the aim is to provide transparency between manager and occupier in the way services are provided and managed, and in how the costs of these services are recovered. Communication needs to be timely and continuous, and works best when managers and occupiers deal with each other's reasonable enquiries and reciprocal obligations promptly and efficiently.

Managers are advised to seek feedback from occupiers on the performance management standards and service delivery, and take any action on this feedback as appropriate.

*It is also important to have a clear communication structure. Best practice requires managers to hold regular meetings with occupiers, and occupiers have a duty of care to participate in these meetings and to be proactive in informing managers of the key contacts who deal with service charges.*

Managers are also obliged to make key contact information available to occupiers, for instance, the management surveyor, credit controller, accounts clerk, etc., as well as the names of any on-site staff, along with their roles and responsibilities.

Managers should inform occupiers of any future plans for the property, particularly if these are likely to have an impact on the service charge.

### 6.2 Consultation

Managers of residential premises are required to follow statutory consultation procedures, and will be keenly aware that if the proper procedure is not followed, the amount they can recover might be limited.

Managers of commercial property are not generally obliged to 'consult' with occupiers prior to incurring costs that are ultimately to be recovered under the service charge arrangement. However, some commercial leases might set out certain procedures to be followed, perhaps prior to incurring large extraordinary costs, such as major fabric or plant replacements etc.

The courts in the UK have recently ruled in a number of instances that owners are obligated to follow the terms of leases strictly when recovering service charges. Therefore, in order to ensure recovery of the service charge, managers

should take particular care to follow exactly the procedures as set down within the lease.

*Even where the lease is silent it is considered best practice for managers to consult with occupiers with regard to the standard and quality of the service charge provision(s) required.*

While the manager has a duty to manage the property and will not wish to avoid expenditure that might have a detrimental effect on the property, managers should ensure that the standard of service provision (and therefore the cost to occupiers) does not unnecessarily exceed the reasonable requirements and needs of the occupiers.

### 6.3 Budgeting and cost review

It is the manager's duty to keep expenditure under regular review in order to identify any unforeseen variances and to notify occupiers accordingly.

Occupiers are entrusting their business overheads/operating costs to an external manager, and as such are entitled to be notified of any significant or material variances to the forecast as soon as possible.

*When significant variances in actual costs against budget are likely, it is best practice for the manager to notify occupiers promptly and within the current service charge year. When substantial works are planned, summary details of the results of tenders and the process used should be communicated to the occupiers, together with full information on the programme of works, costs and the process to be adopted for keeping occupiers informed.*

Whether a variance against forecast is to be regarded as significant or material will often be a subjective assessment, dependent upon a variety of issues such as the size, nature and type of property and the amounts payable by individual occupiers.

Prompt notification of unforeseen variances in the total annual spend should be made to all occupiers with an explanation as to how this is being mitigated at the earliest opportunity.



## 7. Dealing with existing and new leases

### 7.1 Existing leases

The basis by which service charges are operated and managed is set out in the lease.

Many service charge disputes are caused by the failure of managers and/or occupiers to read and properly understand the respective obligations and liabilities under the contractual arrangement made between them. Therefore, care and attention is required to understand the contractual basis of the service charge arrangements properly.

Existing leases may contain service charge provisions that differ from the recommendations in this professional statement. Where this is the case, this professional statement cannot override the lease, but existing service charge clauses are to be interpreted as far as possible in line with the principles and practices as set out here. This applies unless the lease specifically stipulates a different approach, which, therefore, has legal force.

Where doubt or possible ambiguity exists, it is recommended that specialist professional advice be sought.

### 7.2 New leases

As new leases are granted and older leases renewed, it is essential to bring service charge clauses up to modern standards. If modernisation of the service charge provision of the lease is required, both to meet best practice and in the interests of compatibility with other occupiers, and this results in an increase or decrease in the amount payable by the occupier, this is to be taken into account in any negotiations.

While this professional statement cannot override the lease, it does set out the industry-accepted best practice in the field of service charges. It will help solicitors, their clients (be they owners or occupiers) and the managers of service charges to draft, interpret and operate leases in accordance with best practice.

It is recommended that owners, occupiers and their solicitors ensure the lease they sign reflects this professional statement, which will enable more effective, business-focused service charge management during the course of the lease. Terms should be relevant and appropriate, recognising the length of the lease term, and the scale and type of property concerned. At the time of lease renewal, the service charge clauses will certainly require review and probably modernisation/updating.

It is recommended that new leases be drafted with sufficient flexibility to allow for changes in best practice.

The attention of owners, managers and occupiers is also drawn to the SCSi and Dublin Chamber of Commerce document 'SME Guide to Property'.

This 'SME Guide to Property' provides a comprehensive resource for SME's on all aspects of property that impacts their business. The guide is intended for everyone from budding entrepreneurs starting a new business through to existing business owners keen on expanding.

It is unlikely that all leases within a multi-let property will fall for renewal on the same date. Modernising the service charges on an ad-hoc basis may lead to a 'dual' service charge, where in effect two service charge arrangements would operate in tandem, with one based on the older form of leases, and the other based on the modern form. Interim arrangements may, therefore, be necessary to ensure the practical operation of the services and the recoverability of the service costs during the intervening period until such time as all leases have been modernised.

For example, renewal leases might reflect the ideal service charge regime going forward, as well as the status quo, so that when the tipping point is reached, the owner can swap from the old lease service charge regime to the new.

### 7.3 Sweeper clauses

It is often difficult to predict precisely what services might be provided through the duration of a long lease, and which are to be covered by the service charge. To avoid the risk of incurring costs that might fall outside of the service charge, most leases contain a 'sweeper' provision entitling the owner to charge, not only for the services specifically listed, but also for other miscellaneous services that might be provided in the future.

A sweeper clause cannot, unless otherwise agreed, be used to cover the cost of something that was left out of the lease in error. The intention is to give the owner the ability to provide further services that are not identified or in contemplation at the time the lease was granted, and that, for any reason, are considered necessary or desirable to be provided at a later time.

## 8. Financial controls and competencies

### 8.1 Accounting policies

Annual statements of service charge expenditure should include a comprehensive list of accounting policies and principles on which the statement is prepared as well as other information, including:

- whether the statements are prepared on an accruals or cash basis;
- whether the landlord has applied for, and obtained approval from the Revenue Commissioners, to operate the landlord VAT concession (see Appendix E);
- a description of the intended purpose for any sinking or reserve fund, together with an explanation of the tax treatment of contributions to and interest earned on such funds, and details of the bank account / trust where such monies are held;
- a statement of all contributions to and expenditure from the sinking or reserve fund account, together with the account opening and closing balances, and the amount of interest earned and tax paid in the relevant period;
- an analysis of any material variances between budget and actual expenditure, with a detailed commentary to explain trends and variances where these are significant; and
- sign-off statements by the accountants and/or manager with regards to compliance, financial accuracy and the use of appropriate accounting policies.

where a lease sets down specific requirements and procedures, a failure to comply may adversely prejudice the owner's ability to recover such sums.

*Managers should therefore, as best practice, ensure that annual statements of service charge expenditure are issued strictly in accordance with the procedures and requirements as set out under the terms of the lease.*

There is often confusion, however, as to the intention and purpose of the certification process and the requirement for 'auditing' of service charges. Furthermore, the terminology used in relation to the issuing of annual statements of account, particularly in older leases, may be quite generalised, and may not reflect modern auditing and accounting standards and practice.

Independent accountants who issue a report on a statement of service charge expenditure will often carry out differing levels of work and will each sign a different style of report. Consequently, there is a lack of clarity of the level of assurance that owners and occupiers can take from the report, and potentially confusion regarding the actual work undertaken by independent accountants.

### 8.2 Audit and certification of service charges

#### 8.2.1 The requirements of the lease

It is usual for leases to provide for an annual statement to be issued to occupiers following the end of each service charge period; this would normally include a summary of the costs and expenditure incurred in the provision of the services and a calculation of the service charge.

Many leases will set out the procedures regarding the preparation of the annual statement and will often require that the annual statement be 'certified' by the landlord's surveyor, managing agent and sometimes the landlord's accountant. However, certain leases might also require the statement to be 'audited'.

It is essential that any contractual requirements in the lease be duly followed. Compliance with the requirements and procedures set down in the lease may be a 'condition precedent', and recent UK case law has determined that

#### 8.2.2 Service charge certification

Annual statements of service charge expenditure should be certified by an appropriate person

- as representing a true and accurate record of the expenditure incurred in supplying the services to the building; and
- that the expenditure is in accordance with the terms of the leases and, where practicable, the provisions of this professional statement.

In certifying the annual statement of service charge expenditure the certifier is required to act in a professional, non-partisan manner, and not supposing that the only task is to recover as much money as they can for the owner.

Notwithstanding any specific requirements of the lease, the certifier will need to be an appropriately qualified, competent person with experience in dealing with service charges. The certifier also needs to recognise that in certifying the service charge, they have a duty of care to both owners and



occupiers to act with professional care, diligence, integrity and objectivity.

The lease might also set down the credentials/qualifications required of the person who will certify the service charge statement. In certain circumstances, the lease might specifically allow the surveyor or accountant to be an employee of the landlord.

For transparency, the status of the person issuing the certificate and the capacity in which the certificate is issued should be made clear (i.e. landlord's surveyor, accountant, etc.).

In certain instances, certification may be issued in the name of the manager. Where this is the case, managers should have clear internal procedures in place that control who may sign in the name of the firm, and to ensure that this is an appropriately senior individual.

Where the property manager undertakes the certification, the management fee is to comprise this cost. Where the lease requires certification by a third party, the costs of certification of the service charge, together with the fees of an independent accountant, will be recovered through the service charge.

### 8.2.3 Auditing of the service charge accounts

**Best practice is to carry out an audit of service charge expenditure.**

An audit is an independent external review process that adds to the credibility of an entity's disclosures, be it their annual financial statements, systems of internal control or compliance with contractual or legislative obligations.

An audit involves performing procedures to obtain evidence that a specified process is being followed in order to give occupiers sufficient comfort that there is no material misstatement within the information subject to the audit (or in this case, the service charge accounts).

Where the lease specifically refers to an 'audit', this is to be carried out in accordance with International Auditing Standards (IAS's) (UK and Ireland), and should be performed by a registered auditor.

According to ISA (International Standard on Auditing) 200 the objective of an audit is "to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby

enabling the auditor to express an opinion whether the financial statements are prepared, in all material respects, in accordance with an applicable reporting framework."

In carrying out an audit in accordance with accepted auditing standards, the auditor would normally assess the level of risk involved in the instruction and would also adjust the level of work (and cost) accordingly. For instance, the auditor is likely to require a copy of the lease or leases governing the administration of the property, and summarise the expenses that may be charged to the occupiers. This exercise is likely to be extremely time consuming, and hence costly, particularly for larger properties with many leases in operation. The auditor may need to employ an expert in order to carry out this review on their behalf.

The auditor's reasonable and proper costs and fees will, subject to the terms of the lease, be charged to the service charge account.

Frequently, the work required by a modern auditing framework is not what was anticipated when leases were drawn up; especially where the original lease dates back many years. Where this is the situation, the manager faces a dilemma whereby the lease requires an 'audit', but an audit in accordance with auditing standards may exceed that which was intended. An audit may not, therefore, provide best value for occupiers. In such situations, owners/managers may consider it appropriate, following consultation with occupiers, to engage an independent accountant to examine the service charge accounts of a property, rather than carry out an audit.

If the lease specifies that an audit is to be carried out then this should be undertaken, unless the occupiers confirm in writing that it is not required. In these circumstances, an independent accountants' report should be prepared.

### 8.2.4 Independent accountant's report

In the majority of cases, it is considered appropriate for owners/managers to engage an independent reporting accountant to examine the service charge accounts of a property rather than carry out an audit, as the cost of an audit in accordance with auditing standards is likely to be disproportionate and may not offer value for money.

Even where a lease requires the service charge to be audited, or certified by the landlord's auditors, owners and managers will need to make clear whether an audit under accepted auditing standards has been carried out, or alternatively an independent accountant's report prepared.

The onus and style of an independent accountant's review differs from an audit. The procedures carried out may include:

- checking whether the figures contained in the information were extracted correctly from the accounting records maintained by the manager;
- checking, based on a sample, whether entries in the accounting records were supported by receipts or other documentation, or the evidence was inspected; and
- checking that the expenditure report and notes to the expenditure report have been prepared in accordance with the relevant provisions of this professional statement.

It would be usual for annual statements of service charge expenditure to be prepared, and certified, by the owner or manager. In practice, for many small properties, the reporting accountant may be engaged to prepare the statements from accounting records maintained by the owner or manager, as well as providing the independent accountant's report. In these circumstances, the owner or manager will retain responsibility for the preparation and certification of the statement.

Where the lease is silent or the audit is optional, managers should not use an external audit or independent accountant's report as a means of giving credibility to service charge expenditure at the occupiers' expense, unless this is agreed with the occupiers in advance. In addition, an audit or independent accountant's report should not be used as a substitute for an alternative method of certification specified in the lease, unless this has been agreed with the occupiers in advance.

If an occupier requests an audit (subject to clarification of 'audit' as above) or an independent accountant's report, the manager should agree and the costs thereof should be charged to the occupier.

### 8.2.5 Independence

Independence is freedom from situations and relationships that make it probable that a reasonable and informed third party would conclude that objectivity either is impaired or could be impaired. Independence is related to and underpins objectivity and integrity.

However, whereas objectivity is a personal behavioural characteristic concerning the accountant's state of mind, independence relates to the circumstances surrounding the review, including the financial, employment, business and personal relationships between the accountant and the managing agent/owner and their connected parties. Relationships with parties whose interests may be contrary to

the interests of the managing agent/owner may also be relevant to the appearance of the accountant's independence.

All members of recognised accountancy bodies are required to adhere to strict ethical standards covering independence. Any accountants appointed to carry out an independent review should be members of a recognised accountancy body.

### 8.2.6 Recommended best practice

Annual statements of service charge expenditure should be certified by the manager to confirm that they represent a true and accurate record of the expenditure incurred in supplying the services to the building, and that the expenditure the owner is seeking to recover is in accordance with the terms of the leases.

Annual statements of service charge expenditure should be reviewed by an independent accountant in line with the ICAEW Technical Release (TECH 09/14). As stated in the technical release, the accountant should issue a review report, which gives a conclusion as to whether the service charge accounts have been prepared in accordance with the provisions of this professional statement. However, to be consistent with best-value principles this requirement should be considered as optional for smaller properties and dependent on the quantum and nature of the expenditure.

In certifying the service charge, managers have a duty of care to both owners and occupiers to act with professional care, diligence, integrity and objectivity.

If the lease requires an audit to be carried out, then this should be undertaken, unless the occupiers confirm in writing that this is not required. In these circumstances, an independent accountant's report should be prepared.

Openness and transparency can be enhanced by the inclusion of a balance sheet or cash reconciliation as part of or in addition to the statement of actual expenditure.

For mixed used multi-unit developments, the provisions of the Multi-Unit Development Act, 2011, ("the MUD Act") should also be considered.

The Property Services Regulatory Authority (PSRA) is responsible for service providers dealing with property management services, and includes the licensing of all such services providers, the establishment of a complaints investigation and redress system for consumers, the setting and enforcement of standards in the provision of property services, including the use of standard terms of engagement,

the administration of client accounts and the establishment and maintenance of a compensation fund.

In consultation with the Institute of Chartered Accountants in England and Wales, the RICS has issued a sample report on service charge accounting (see Appendix C) setting out recommended best practice for the disclosures and information that managers should provide to the accountants appointed to carry out an independent review of service charges, and for subsequent communication to tenants as to the nature, type and cost of services provided.

### 8.3 Industry standard cost classifications

Appendix B includes details of industry standard cost classifications that should be used in reporting budget and actual expenditure.

The industry standard cost classifications provide 3 levels of analysis as follows:

- cost class;
- cost category; and
- cost description.

As a **minimum** acceptable level of reporting, service charge budgets and statements of actual expenditure should be prepared at **both cost class and cost category** level showing, for the purposes of clarity, only the relevant cost class and cost category levels being used.

Where there is no expenditure under a specific cost class or cost category, these levels should be omitted from the service charge budget and statements of actual expenditure reports, unless for comparison purposes with a different period.

Adoption of the industry standard cost classifications will reap enormous benefits for the industry, as this will facilitate better cost comparison between properties and the benchmark indices. It will also reduce costs, and assist in the transfer of information between managers and owners when properties are sold, or when there is a change of manager (i.e. from in-house to external, or between managing agents).

However, to achieve transparency in accordance with the principles of this professional statement, it is recommended best practice that budget and actual expenditure analyses are provided at the detailed **cost description** level whenever practicable, and particularly in respect of larger properties, with a summary of the total costs under each cost category.

In accordance with the core principle of proportionality it is acceptable for smaller properties or those with limited service charge expenditure (for example, industrial sites) to report at the higher cost category level, although this is generally

regarded as an exception rather than the norm.

To maintain consistent industry standards and to facilitate benchmark comparison, managers and those responsible for preparation of the accounts are encouraged to use all best endeavours to comply with the cost class and cost category analysis as set out and not permit the creation of new cost categories or cost classes.

However, the detailed cost descriptions set out are not intended to represent an exhaustive list, but are included for illustrative and guidance purposes only. Individual cost descriptions may vary from manager to manager, and the inclusion of additional cost descriptions is encouraged where this will facilitate greater transparency and clarity with regard to the expenditure incurred or proposed.

The use of the standard cost classes and categories in industry-standard format are essential if benchmarking is to be effective. However, for benchmarking purposes, accounts are only required at cost-category and cost-class level. It is not intended that benchmark analysis of expenditure be carried out at cost-description level.

### 8.4 Budgets and actual expenditure accounting

The service charge accounting sample report (see Appendix C) establishes a basic framework for the preparation of service charge accounts, and identifies areas for special consideration by managers and reporting accountants.

Managers are required to provide a budget showing an estimate of likely service charge expenditure to occupiers, accompanied by an appropriate explanatory commentary, together with a breakdown of their proportion of the costs, at least one month prior to the commencement of the service charge year.

Detailed statements of actual expenditure, together with accounting policies and explanatory text, will be issued within four months of the service charge year end.

The accounts are to give an adequately detailed and comprehensive summary of items of expenditure, with full explanations of any material variations (+ or -) against the budget, and in a reasonably consistent format year on year.

It is recommended that the budgets and accounts be issued with a report that provides the following minimum information:

- *a comprehensive level of detail to enable occupiers to compare expenditure against estimated budget;*
- *explanations of significant individual costs and of variances from the previous year's budget / accounts;*



- *a comparison against the previous two year's actual costs, where appropriate;*
- *For transparency, it is recommended that expenditure, net of VAT, is shown as a rate per square foot / per square metre, based on the actual area (i.e. not the weighted area) with insurance charges and sinking fund contribution shown separately;*
- *information on core matters critical to that account (e.g. levels of allocation, apportionment, contracts, report on tendering, etc.);*
- *the achieved and / or targeted measures of improved management performance (e.g. successes in delivering improved quality services and greater value for money);*
- *on-site management team costs, separately identified;*
- *details and results of the most recent previous and forthcoming tendering exercises. Occupiers are to be advised of the contractors who are providing the services;*
- *a full apportionment matrix that clearly shows the basis of calculation and the total apportionment per schedule for each unit within the property / complex; and*
- *the date of issue.*

A set of industry standard cost classifications has been drawn up, and is included in Appendix B (see also section 8.3). As a minimum standard when reporting service charge costs to occupiers these should be used at cost-class and cost-category level.

## 8.5 Right to challenge

This professional statement cannot override an occupier's legal right to challenge incorrect or inappropriate service charges subject to the prevailing statute of limitations.

Managers are expected to deal with reasonable enquiries promptly and efficiently, and to make all relevant paperwork available for inspection. Where copies of the supporting documentation concerning the certified accounts are supplied, it is acceptable that an appropriate fee to be charged.

Occupiers and consultants appointed on their behalf have a duty to respect and conform to the principles of the professional statement. In the interest of promoting a swift and harmonious resolution of service charge queries there should be openness and transparency between the parties.

## 8.6 Change of owner or manager

In the event of a sale or change of manager, it is essential that a definitive timescale within which accounts will be closed and handed over to be agreed.

For further information on the recommended processes and procedures in the event of a property's sale, or other circumstances where the manager changes, see the SCSi guidance note: Commercial property service charge handover procedures, 1st edition (incorporated within this professional statement at Appendix D).

This is particularly relevant to solicitors when drafting and reviewing sale contracts

As soon as practicable – but not later than four months following the date of completion of a sale of a property, or a change of manager – full details of all service charge expenditure, accruals, pre-payments, etc. for all outstanding service charge years should be provided to the new owner/manager, up to the date of sale / transfer.

The new owner or manager should issue any future budget in such a way that it provides sufficient information to enable occupiers to compare it with the most recently issued certified accounts. The occupiers can then convert historical data into a consistent format for comparison where the new owner or manager were not responsible for previous years.

Where a property has had more than one manager in place during the service charge period the compilation of the service charge accounts may need to be reconfigured:

- If the former manager has supplied full supporting documentation to the new manager in a timely manner then the expenditure for the full period should be amalgamated and the service charge accounts prepared as normal.
- If full supporting documentation has not been supplied in a timely manner then the expenditure incurred by the two managers should be disclosed separately within the service charge accounts.

Where the expenditure for each managing agent is disclosed separately then the certification by the new manager should only cover the period under their control.

(Note that under the second approach above there may be a period of the service charge accounts that will not have been certified or reviewed).

## 8.7 On-account payments

Service charges are usually 'reserved as rent' in the lease; in reality, however, the service charge is neutral in income and expenditure terms, after year-end balancing charges/credits.

Service charge monies for each property must be held in one or more separate, physical or virtual, bank accounts in recognition of the fact that the monies are being held to deliver services to the property.

Furthermore, and based on the principle that owners should not profit from the supply of services, all interest earned should be credited to the service charge account (after appropriate deductions have been made, i.e. bank charges, tax etc.).

## 8.8 Interest on service charge accounts

Interest earned and late payment interest should be credited to the service charge account. Bank charges and account operating costs are to be offset against the interest. Owners are required to perform their obligations under the terms of the lease, and to account to occupiers for any balancing charges due/owed at the end of the service charge period.

Modern leases often enable owners to recover the cost of borrowing to fund major non-cyclical expenditure as a cost to the service charge. In older leases, there is a risk of having to fund shortfalls from negative cash flows.

It is the owner's responsibility to fund the contribution in respect of void units, and to make these payments to the account promptly.

When communicating with occupiers through budget and expenditure reports, managers should unambiguously state their policy concerning the crediting of interest to the service charge.

## 8.9 Interest on forward funding of service charge costs

Leases should enable owners to recover the reasonable and proper cost of borrowing to fund major non-cyclical or exceptional unbudgeted expenditure as a cost to the service charge. In older leases there is a risk of having to fund shortfalls from negative cash flows.

Where owners are crediting interest earned to the service charge account, they should be reassured that charging the interest at reasonable and commercial rates on borrowed money to fund major non-cyclical or exceptional unbudgeted expenditure meets best practice requirements. (See also Section 9 – Provision for anticipated future expenditure).

In situations where an agreement has been reached whereby the landlord funds the cost of works in the first instance and then recovers a percentage or all of those costs from the tenants through the service charge at a later date, an appropriate accounting policy should be included within the notes to the service charge expenditure report, along with a note disclosing the full details including the amount of any interest charged, if permissible under financial regulations, on the deferred amounts.

## 8.10 Timeliness

It is the responsibility of the manager to provide the occupiers with budget and reconciled accounts for anticipated and actual service charge expenditure at the appropriate time. This to include appropriate explanatory comments with regard to costs proposed or incurred, together with details of the basis of allocation and apportionment, to enable occupiers to reasonably understand how their liability has been calculated.

**Budgets should be issued at least One Month prior to commencement**

**Reconciled accounts issued within Four Months of the end of the service charge year in question.**

Where an occupier raises queries or seeks further clarification on any matters relating to the budget or actual costs, the manager should deal with such proper enquiries promptly and efficiently.

## 8.11 Benchmarking and cost analysis

Adoption of the standard industry cost classifications (see Section 6.3 and Appendix B) is recommended to facilitate better cost comparison between properties and the benchmark indices. It will also reduce costs and assist in the transfer of information between managers and owners when properties are sold, or if there is a change of manager (e.g. from in-house to external, or between managing agents).

Further, these cost classifications are largely compatible with industry benchmark indices, which will facilitate a benchmark comparison of costs.

However, when using benchmark information to compare operating costs for any building, caution is needed. Industry benchmark indices are not intended as a definitive database of costs for operating service charges in commercial buildings, but do serve to highlight indicative trends in service charge costs. Buildings differ substantially in terms of construction, age, layout, gross-to-net floor-area ratio, staffing and security levels, hours of operation, and standards of maintenance and management.

These analyses take the average of service charges for similar properties, and, therefore, provide a guide to the cost effectiveness of the management service.

However, property is not mass-produced in similar formats (as is a car, for example), and therefore each property will have its own variations from the average; therefore, 'beating the benchmark' is not necessarily proof of service efficiency or value for money. Industry benchmark indices provide an excellent guide, but managers may wish to reflect further on how their specific property is performing from a value for money perspective.



## 9. Dispute resolution

There are times where managers and occupiers can disagree on matters such as which services are chargeable, what benefit the occupiers individually or collectively receive, and/or how much they cost.

Traditionally, leases have not allowed for any form of redress for the occupiers, and therefore expensive court action has often been necessary to query the service charge.

It is usually beneficial to both owners and occupiers to resolve service charge disputes quickly, as going to court can be slow and expensive.

Occupiers must comply with lease terms and as a minimum should not arbitrarily withhold payment of any sums that are properly demanded. Any payment properly withheld is to relate to the actual sums queried or in dispute, and not to the whole of the service charge due.

Alternative Dispute Resolution (ADR) can provide a more cost effective way of resolving service charge disputes than the courts, and it is recommended that this process be used even when leases do not expressly provide for it.

When disputes are resolved, the base-rate interest is to be paid or allowed in respect of the period during which the relevant amount has been underpaid or overpaid. In mediation, the parties will agree what they want to achieve, and an independent expert will then determine what the lease says.

### 9.1 ADR as industry best practice

The Law Reform Commission in their consultation paper in July 2008 entitled 'Alternative Dispute Resolution' defined ADR as: "a broad spectrum of structured processes, which does not include litigation though it may be linked to or integrated with litigation, and which involves the assistance of a neutral party and which encourages parties to resolve their own disputes".

Despite historic resistance, ADR has gained widespread acceptance and popularity and indeed the Irish courts regularly encourage parties to use ADR rather than going to court. The attitude of the courts is that litigation should be a last resort.

The courts can require parties to provide evidence that alternative means of resolving their dispute were properly

considered. Therefore it is strongly recommended that in disputes about service charges ADR should be considered before taking legal action.

All new leases (including renewals) should provide for ADR of service charge disputes, and if the parties cannot agree on the person to provide that service, provision should be made for the President of the SCSi to appoint such a person.

Applications for appointments of mediators, independent experts and arbitrators by the President are managed by the SCSi Dispute Resolution Service ([www.scsi.ie](http://www.scsi.ie)).

Where leases contain no ADR clauses, there is nothing to stop the owner and occupier agreeing to use ADR to help them find a resolution to a dispute. It is possible that a party who declines to use ADR, if it is available, could be penalised in a costs order if the court considers they have refused to engage in ADR without a good reason.

There are issues as to which form of ADR is most appropriate to service charge disputes. The options are varied and include:

- early neutral evaluation;
- mediation (facilitative or evaluative);
- independent expert determination; and
- arbitration.

### 9.2 Early Neutral Evaluation (ENE)

ENE is an ADR process whereby both parties retain a neutral party to provide a non-binding evaluation on the merits of a dispute. As the name suggests, this is usually most effective if attempted early in the life of the process, before positions become entrenched and significant costs have been incurred.

There are no procedural requirements for ENE beyond those agreed between the parties.

The advantages of ENE are that where parties are engaged in direct discussions, the opinion of a mutually respected neutral person may assist in the negotiations. An evaluative opinion from a neutral surveyor, who understands the practical issues relating to the management and administration of the service charge, or a senior legal professional on a disputed point of contractual construction, can help provide the parties with a realistic appraisal of their cases while avoiding deadlock and/or positional bargaining.

## 9.3 Mediation

Commercial mediation is a voluntary, non-binding, private dispute resolution process facilitated by a neutral person (the mediator), and which enables the parties to reach a negotiated settlement. A core principle of mediation is that the parties 'control' the outcome, rather than it being imposed upon them.

Unless required by contract, parties attend mediation voluntarily. Even where it is a contractual requirement, either party can terminate the mediation at any time. This is usually a powerful first step towards settlement, restoring direct communication where it may have broken down previously.

The role of the mediator is not to resolve the dispute nor advise on parties' legal rights and obligations. Rather, it seeks to assist parties to work out their own settlement, on terms they can both live with, and looking at a broad range of issues (not limited to legal rights of the facts of the case). Mediation is used in a wide variety of contexts, from multi-million pound commercial disputes to employment and workplace disputes, through conflicts in the family and community settings.

Mediation is now increasingly encouraged by the courts whether prior to, or during, the litigation process.

A skilled mediator will have received specific training in all aspects of the mediation process and competencies. They should therefore be able to mediate whatever the background of the dispute, regardless of the mediator's own underlying technical discipline(s). That said, it is the case that many clients will prefer to have a mediator who also has good subject knowledge of a primary technical area that is relevant to the issues in dispute.

A skilled mediator should be able to:

- Reopen communications between parties;
- Engage the parties into taking control of the dispute;
- Bring a fresh, neutral pair of eyes to an old problem;
- Take a broader perspective and help parties explore a creative solution; and
- Help parties move toward a realistic, negotiated settlement, in a cost-effective manner.

### 9.3.1 The advantages of mediation

There is one crucial factor that makes mediation different from most other forms of dispute resolution: no one tells the disputing parties who is right and who is wrong. Parties to a dispute will often interpret the same facts and events differently.

They see and interpret them through the eyes conditioned by education, culture, age, environment and other factors. In

other adjudicative dispute resolution processes (e.g. courts, arbitration, adjudication, expert determination) the third party arbiter imposes their interpretation of right and wrong on the subject matter of the dispute, a potentially limiting way of resolving disputes. In mediation, each side will need to make some concession to meet the needs of the other party (who otherwise would not settle). Not only does this create a 'win win' outcome, it also saves the parties legal fees and wasted resources in reaching this point. This is what can make mediation so effective in achieving solutions that meet the needs of the disputing parties.

In summary, the advantages of mediation can be outlined as follows:

- Mediation is non-binding until the parties sign a settlement agreement (at which point it becomes binding as any contract in law);
- The key to any mediation is the fact that it is private and the process is confidential to the parties, (subject to completion of a non-disclosure agreement) except as they may agree. This enables the parties to talk frankly about the strengths and weaknesses of their arguments, and the other side's 'case', without it prejudicing their position if the case does not settle and goes to court;
- Negotiations and communications within the process are generally, subject to some narrow exceptions, inadmissible in subsequent legal or other proceedings;
- The mediator is neutral and his/her only interest is in providing the parties with their best chance of achieving a settlement to their dispute; and
- One of the key strengths of mediation is that the parties take control of the outcome and negotiate their own settlement, 'owning' the outcome. They can decide to withdraw from the process at any time. Any final settlements may take into account other dispute resolution processes e.g. in an ongoing business relationship, opportunities for further work, or the offer of goods or services at the agreed cost, could be features. It may also take into account things that are totally outside of the dispute.

## 9.4 Independent Expert determination

Expert determination is a process in which an independent third party, acting as an expert rather than a judge or arbitrator, is appointed to decide a dispute (as an independent expert or 'expert determiner', not to be confused with an 'expert witness'). His/her appointment is by contract between the parties, which often provides for a nominated appointment.

The duty of an independent expert is to make proper and reasonable investigation and to arrive at a non-negligent decision, tested by what may be expected from the body of professional opinion they may choose, or be so required by

contract, to receive. In doing so, the independent expert may take into account, evidence and arguments from the parties to a dispute, but, unlike arbitration, cannot usually be bound by them.

The independent expert should be able to:

- Base their determination upon their own knowledge and their investigations to discover the facts and all other information, including principles of law relevant to the issues in dispute; and
- Settle their own contractual terms with the parties, e.g. as to remuneration, extent of inspection, assumptions, and carry out the whole of the determination by themselves.

#### 9.4.1 The advantages of Independent Expert determination

A chartered surveyor acting as an independent expert must have in-depth knowledge of the subject matter of the dispute (otherwise he/she is not an expert) and is free to make their own investigations. As a result, the dispute can be determined quickly and 'expertly' and, usually, once and for all. Expert determination is particularly suited to disputes on discrete technical issues, including disputes relating to service charge or quality of work and / or materials.

The expert's decision is normally final and binding unless indicated to the contrary in the contract. In that context, it is somewhat similar to Arbitration or indeed litigation but the fundamental difference is that the expert normally has much more procedural scope than an arbitrator or a judge. The expert is not normally bound by all the rules of natural justice and so can, and is frequently encouraged to, rely on his own knowledge or investigations without reference to the parties.

While this process can be more formal than mediation, the expert is free to use his own knowledge and investigation to come to a final and binding determination of a dispute. SCSi Dispute Resolution Services (DRS) can provide independent experts from their approved panel who are chartered surveyors experienced in property matters.

## 9.5 Arbitration

Arbitration is a dispute resolution procedure whereby two parties in dispute agree (an arbitration agreement) to be bound by a decision of an independent third party (the arbitrator). The role of an arbitrator is similar to that of a judge save that, on principle of 'party autonomy' (whereby the parties can agree procedural and evidential matters), the procedure can be less formal. An arbitrator is usually an expert in his/her own right.

An arbitrator should be able to:

- Act fairly and impartially using his/her general knowledge of the subject matter;
- Reach a fair decision based on the evidence and arguments submitted by the parties; and
- When appropriate take the initiative in ascertaining the facts and law.

#### 9.5.1 The advantages of arbitration

Arbitration is private and often informal. Many property or construction disputes can be settled quickly and fairly by arbitration. A chartered surveyor arbitrator will be able to understand the disputed issues faced by the parties in a land, property or construction dispute.

#### 9.5.2 Rules governing arbitrators

Arbitration is carried out within a legislative framework with the current act being the Arbitration Act 2010 which has replaced the Arbitration Acts 1954-1998.

The Arbitration Act 2010 governs arbitrations in Ireland and a request may be made to the SCSi DRSC for an arbitrator to be appointed or the parties involved can agree one. The process is more formal. The arbitrator decides on the evidence before him or her and the arbitrator's decision, which is called the 'award' is final and binding. An arbitrator's award has the same status as a judgment or order of the High Court and it is enforceable as such. It is not possible to appeal an arbitrator's award and there are limited grounds for challenge under Article 34 of the UNCITRAL Model Law adopted in the Arbitration Act 2010.

Agreements to refer disputes to arbitration are often made in a lease or contract. If not, a separate agreement can be made by the parties after a dispute has arisen.

For more information, please refer to [www.scsi.ie](http://www.scsi.ie)

# 10. Mixed-use schemes

Recently, there has been a significant increase in mixed-use developments. While the concept is not new, what is different about mixed-use developments today is the increase in the introduction of residential units into commercial buildings. This is being driven not by organic growth, but by public policy and commercial reality.

The mixture of commercial and residential uses, in management terms, presents particular challenges that often require both residential and commercial service charge management skills and expertise.

The extent to which the owner is obliged to provide and carry out works and services, in respect of both commercial and residential leases, will depend on a strict interpretation of the wording of the lease.

For mixed use developments the provisions of the Multi-Unit Development Act, 2011, (**"the MUD Act"**) should also be considered. In general terms the MUD Act provides that in respect of such mixed used developments there must be a fair and equitable apportionment of the costs and expenses attributable to the different classes of units within the development.

Further detailed information and guidance on multi unit developments is available in the SCSI 'Code of Practice Property Management in Multi-Unit Developments'.

This professional statement provides a common platform over and above the statutory requirements currently in place under the Property Service Regulatory Authority (PSRA) legislation and the MUD Act.

Whilst not entirely mandatory in its implementation, it is believed that this professional statement forms the basis for best practice within the industry and, where appropriate, recommend that it be incorporated into leases and other legal documentation.

The area of residential service charges has been a potential source of dispute between owner management companies and their members over the years. Whilst this professional statement cannot override existing leases it does offer clarity and consistency to this complex area by providing a clear set of recommendations, standard definitions and descriptions for the various expenditure elements included in service charges, as well as advice on the basis of computation of residential service charges.

## Apportionment of Service Charges in Mixed Use Developments

### 10.1 Introduction

Mixed use development is increasingly common and no doubt here to stay, yet the objectives of residential and commercial developers are varied in no small part due to diversity of occupier requirements. Residential developers sell their property on long leases with little focus on the ongoing maintenance and management (service charge). Their profit is derived from the price at which the long lease is sold and therefore they seek to maximise that sale price by giving certainty of lease terms but may not allow for the initial service charge percentage to be varied.

The MUD Act provides that the annual service charge is to be calculated on a transparent basis and is to be equitably apportioned between the unit owners meaning that account is taken of "all relevant matters including the respective level of use of any common areas by the owners of different classes of units and their servants, agents and invitees."

Residential leases are rarely individually negotiated and standard documentation with fixed percentage apportionment is more commonly used. Commercial developers have a different relationship with their occupiers - leases granted are now typically shorter and even the more substantial leases (save to anchor tenants) will not exceed 25 years. These will be tailored to each individual deal whilst conforming to a framework. Even if the developer sells his investment he will be conscious of the ongoing closeness of the relationship between owner and occupier and will therefore want to deliver fairness in the service charge and the ability to make it reflect changing circumstances as they happen. There will therefore be greater flexibility in a commercial lease in service charge terms and the ability to change apportionment to reflect current factors. This may cause difficulty in the context of mixed use development if such changes in circumstances adversely affect the contributions of the residential tenants.

Those responsible for the apportionment of service charges should also be aware of scale. What may be appropriate in a large complex multi-use development is unlikely to be appropriate in a small neighbourhood parade of shops and flats. Care must be taken to ensure the methodology applied reflects the size and scale of the property and its occupiers.



## 10.2 New Developments

This professional statement will assist in new developments where the service charge apportionment strategy can be constructed simultaneously with the lease documentation. In addition, the principles it sets out can be used when considering revising the apportionment of existing developments where the existing leases do not allow for apportionment to be amended but consequent complications must be taken into account.

Whatever the circumstances, the resultant apportionment strategy must be clearly and transparently set out. It must enable all parties to understand the basis of apportionment and allow for future modifications in the event that circumstances change making a revised apportionment strategy necessary.

## 10.3 The purpose of a service charge

A service charge exists to recover the costs of operating the services and expenses of a property. Thus, it is the means to spread the cost of those services and expenses between the beneficiaries and users of those services in a fair and reasonable manner - the term "fair and reasonable" requires the owner to ensure no occupier is disadvantaged.

Service charges are '*not for profit, not for loss*' although suppliers of services are expected to make a reasonable profit on the services they provide.

## 10.4 Residential service charges

Service charges in multi unit developments are regulated by the MUD Act and the PSRA legislation, and failure to adhere to the statutory procedures and timescales laid down can result in the manager being limited on how much can be recovered.

Please refer to the SCSi 'Property Management in Multi-Unit Developments Code of Practice' which sets out the basis for best practice in the management of multi-unit developments.

## 10.5 Principles of apportionment

The service charge clauses in the lease will usually set out the principles by which the service charge is to be apportioned. On occasion, the lease may call for the landlord or his surveyor to revise or amend the apportionment methodology as circumstances change and further require that revision shall be fair and reasonable. Here the decision will need several factors to be taken into account, not least of which are the principles of availability, benefit and use of the services.

The primary question must be "does the premises benefit from the service?"

Only once that has been established can one address the issue of use. Here custom and practice in the residential and commercial fields have varied and the landlord or his surveyor will need to consider carefully how these issues of benefit and use might be applied.

***In any event best practice requires that the methodology of how a service charge is apportioned must be set out in a clear and transparent document available to all parties involved in the service charge.***

## 10.6 Availability, benefit and use

Typically in residential schemes, all who have the service available are expected to pay. In commercial and mixed use schemes some commercial tenants may have negotiated an 'opt out' in their lease from some services. The services are therefore available but will not be charged.

Where a limited number of people benefit from or use the services, separate 'schedules' can be employed allowing the cost of these services to be spread amongst only those who benefit from and/or use them.

The principle as to the quantum of the contribution will vary on a case by case basis. A discounted charge may be appropriate in some circumstances and a full charge appropriate in others.

A simple example of this would be 'Estate' and 'Building' service charges, for instance on a business park. The estate charge would comprise the general grounds maintenance of the estate, estate security, street lighting etc and each office building within the park would also have a separate building service charge for the heating, ventilation, security, maintenance and specific building services that just benefit and are used by that individual office block.

An alternative example might be waste disposal where some tenants do not use the communal facility having negotiated their own arrangements to deal with their own waste disposal as part of their lease. In this situation, the cost of waste disposal would be apportioned separately from the general service charge (by using a separate apportionment "schedule" for waste).

Water is particularly relevant in mixed use apportionment as domestic water may be a free service from the local authority whereas commercial water supply will incur a cost which will need to be included in the appropriate service charge schedule.



In addition, within a schedule, whether due to size or for some other reason the benefit or use received by one tenant might be in a different proportion to the size that the premises bear to the aggregate size of all the premises. In the circumstances, a 'weighting' may be applied. This will adjust the apportionment between the tenants thus reflecting the different costs involved in servicing different sized units and the different benefit and use applicable to each unit.

## 10.7 The apportionment matrix

The result of these considerations will be an apportionment matrix which communicates transparently how the cost of each of the services in whichever schedule will be split between the tenants. Accordingly, it is possible to see how much everybody is contributing towards the services provided and the cost of them.

Apportionment usually takes place at unit level. An example of an apportionment matrix is attached in Appendix CD, CE and CF.

A number of traditional methods of apportionment are set out in Section 5.

## 10.8 Fair and reasonable proportion

The lease will often incorporate a provision for the proportion to be determined by the owner's surveyor. This provides flexibility and, for the owner, full recovery.

Unless coupled with a statement about how the occupier's apportionment is to be calculated, the lease can give rise to disputes. The terms 'fair and reasonable' requires the owner to ensure no occupier is disadvantaged. Care must be taken to ensure fairness between all the parties.

## 10.9 Alternative apportionment strategies

The issues raised by apportionment in mixed use property are no different to those which existed before. It is still necessary to apportion costs, initially per the specific lease requirements and if there is discretion then based on the benefit and use of the services received. However, the increase of mixed use development and the clarification that residential law applies means more transparency is advised and that process and timeliness are essential.

Accordingly, below are some alternative strategies as to how one might apportion some or all of a mixed use service charge between the varying elements.

## 10.10 Apportionment of other services

There is an ever-increasing range of new services being provided for the benefit of tenants including gym facilities with shower and storage facilities, shared meeting / function rooms, shower and drying room facilities for bicycle users, bicycle repair services, car valeting service, laundry facilities and many more.

Where these services are for the benefit of all tenants and their staff, the costs should be included within the appropriate service charge schedule to ensure that the costs are allocated to those who benefit from the services. A separate budget and apportionment schedule may be required where the service is not available to all occupants.

## 10.11 Foodcourts

It is common practice in foodcourts which share a communal area, with common services and facilities (common seating and tables, cleaning services, tray removal and cleaning, waste disposal) that the associated service costs are apportioned to the foodcourt operators.

The foodcourt charge is often based on the turnover of the foodcourt operators rather than on a floor area on the basis that the level of servicing required is driven by customer use and consequently the greater the turnover of a food retailer, the greater its use of the common area services.

## 10.12 User matrix

There will be occasions, particularly in large, complex, mixed use developments, where the landlord's surveyor or manager feels it necessary to consider the direct benefit and use of services relevant to different occupier types. This can be useful when considering the relative weighting of charges to different occupiers or groups of occupiers.

The service charge apportionment mechanism will be very site specific and tailored to suit the specific circumstances in each development

Commonly used apportionment mechanisms include

- User weighting;
- Area weighting; and
- In more complex schemes a combination of a user weighting and an area weighting.

**User Weighting** - The Gross Internal Area (GIA) of each user type is weighted based upon its use or its position within the scheme, through the application of a weighting reflecting its direct benefit and use of services.

| Example of a Location & User Weighting |              |        |         |        |                    |               |        |
|--|--------------|--------|---------|--------|--------------------|---------------|--------|
|  | Area<br>Sq M | Retail | Storage | Office | Retail<br>External | Weighted Area |        |
| Weighting >>                           |              | 100%   | 50%     | 80%    | 65%                | sq.m          | %      |
| Retail                                 | 50,000       | 50,000 |         |        |                    | 50,000        | 63.1%  |
| Retail External                        | 15,000       |        |         |        | 15,000             | 9,750         | 12.3%  |
| Storage                                | 7,000        |        | 7,000   |        |                    | 3,500         | 4.4%   |
| Office                                 | 20,000       |        |         | 20,000 |                    | 16,000        | 20.2%  |
| Totals                                 | 92,000       |        |         |        |                    | 79,250        | 100.0% |

**Area Weighting** - Area weighting is typically used in large retail schemes with a large variation in unit sizes from anchor stores, MSU's and standard units to provide a quantum discount to the larger units. Area weighting is also used where appropriate at estate level in larger mixed use schemes.

The GIA of each unit is weighted based upon its size, in tranches, with a lower percentage weighting applied to the larger tranches. The size of each tranche will be site specific and tailored to suit the specific circumstances of the individual scheme.

| Example of a Area Weighting |       |           |          |          |                |           |       |
|-----------------------------|-------|-----------|----------|----------|----------------|-----------|-------|
|                             | Area  | Up to 400 | Next 400 | Next 800 | Above<br>1,600 | Weighting |       |
| Weighting >>                | Sq M  | 100%      | 80%      | 60%      | 40%            | Area      | %     |
| Unit 1                      | 4,000 | 400       | 400      | 800      | 2,400          | 2,160     | 51.3% |
| Unit 2                      | 2,000 | 400       | 400      | 800      | 400            | 1,360     | 32.3% |
| Unit 3                      | 450   | 400       | 50       |          |                | 440       | 10.5% |
| Unit 4                      | 250   | 250       |          |          |                | 250       | 5.9%  |
| Totals                      | 6,700 |           |          |          |                | 4,210     | 100%  |

The service charge percentage contribution for each unit is calculated by dividing the weighted area of each unit by the total weighted area of all units within the scheme / schedule.

In large complex mixed use schemes, the estate service charge budget may be apportioned on a 'two step' discounted and weighted area calculation by combining the user / location weighting and the area weighting.

## 10.13 Summary

Landlords' surveyors or managers will increasingly have to justify their decisions. The principle of the term 'fair and reasonable' when applied to apportionment, requires the apportionment to ensure that no occupier is disadvantaged and that occupiers pay a fair and reasonable contribution towards the cost of the services from which they derive benefit.

The principles set down in this practice statement are intended to help those, who have to make apportionment decisions in their deliberations and to help solicitors in their drafting of new and renewal leases.

# 11. Provision for anticipated future expenditure

## 11.1 The contractual arrangement

An occupier will only be liable for making contributions towards a sinking or reserve fund, or for payment of a depreciation charge, so far as the lease allows.

The property management surveyor should be fully familiar with the provisions and definitions relating to sinking and reserve funds, or depreciation charges set out in the lease.

Where the lease is silent, the owner can seek the agreement of occupiers on including such arrangements within the service charge in the interests of good estate management.

Issues that should be clarified between the owner and occupier include:

- the 'ownership' of the money;
- the purpose for which the fund is being accumulated and its timescale (as per the Planned Preventative Maintenance (PPM) schedule); and
- what will happen to it at the end of the lease.

It may be that the fund will continue to exist after an individual occupier's lease expires, and so the money will remain within the fund until it is needed. What happens to the fund when the subject building is demolished is often not thought about, therefore, any unexpended monies may 'revert' to the owner by default. Whichever arrangement is used, clear communication is vital.

## 11.2 Sinking funds, reserve funds and depreciation charges

Some confusion has arisen as the description and purpose of such funds has become interchangeable. The following definitions set out industry guidance on how these terms are to be used.

*A **sinking fund** is a fund formed by periodically setting aside money for the replacement of a wasting asset, (for example, heating and air-conditioning plant and equipment, lifts, etc.).*

*A **reserve fund** is a fund formed to meet anticipated future costs of maintenance and upkeep in order to avoid fluctuations in the amount of service charge payable each year (for example, for external cleaning and redecorations).*

*A **depreciation charge** is a measure of the wearing out, consumption or other reduction in the life of an asset (for example, heating and air-conditioning plant and equipment, lifts etc.). An amount would be included in the service charge to reflect the 'cost' to the landlord based on the initial cost of an installation, rather than on the future cost of replacement.*

### 11.2.1 Sinking (or replacement) funds

It is recommended that a clear policy is set out as to the purpose for which the monies are being built up, for example, to replace the lifts within the building. This will require the owner to act reasonably in estimating the amount of the contributions due.

The policy should set out the basis used in calculating the charge, and include details of how the monies will be held; to whose order; and how financial matters, including interest and tax, will be accounted for. In the case of more substantial funds, it may be advisable to have a formal trust deed setting out the arrangements, trustees, etc.

A recognized method for calculating the sinking fund amount is to use PPM schedules prepared by specialist consultants / contractors, and reviewed annually, in respect of technical M&E (asset register) and fabric (floors, roof etc) with both combined to achieve a full 'view'.

The ownership of sinking-fund monies is often poorly defined, particularly when the purpose of the fund has been discharged. However, a well-set-up fund will usually clarify what is being paid and by whom, to what purpose, and what will happen once that purpose has been achieved, or in other circumstances (such as demolition), to residual monies, and to whom these monies will be disbursed.

At the same time as other occupiers are making their contributions, the owner should contribute to the fund for any void properties as though he or she was the occupier.

Sinking funds remain part of the service charge, and all payments made out of the fund should be clearly communicated to occupiers, and included as part of the annual reconciliation of the service charge.

The nature of sinking funds means that they are best suited to being collected over the life of the item for which they are intended. Many leases of older buildings might make provision for a sinking fund, but if no fund has commenced, this may create a sense of inequity and unfairness if occupiers who took leases later in the life of the building were asked to contribute towards the full replacement cost.

Where a tenant has negotiated an “opt out” of paying a contribution towards the sinking fund, provision should be made for the tenant to make their full contribution upon the expenditure being discharged from the sinking fund or upon expiry of the lease. Any shortfall should be made up by the landlord.

Where significant works are anticipated in the relatively short term, and it is decided to spread the cost during the period leading up to the point at which the expenditure is to be incurred, this then becomes a **reserve fund** rather than a sinking fund.

#### 11.2.2 Reserve funds

Reserve funds are generally relatively short-term in nature, and are created for a specific purpose; for example, external redecoration of a building or internal redecoration of common parts, the purpose being to minimise fluctuations in the amount of year-on-year service charge payable by an occupier as a result of regularly recurring items.

Based on case law, reserve funds may be regarded as occupiers’ monies, and if the fund has not been expended on expiry or sooner determination of a lease, the occupier may be entitled to repayment of any monies contributed to the fund.

Reserve funds remain part of the service charge, and all payments made out of the fund should be clearly communicated to occupiers, and included as part of the annual reconciliation of the service charge.

#### 11.2.3 Depreciation charges

Depreciation is the measure of the wearing out, consumption or other reduction in the life of an asset; by this definition, it is clearly the owner’s money.

Where an owner wishes to recover depreciation costs from the service charge, the wording on the lease should recognise this and require the owner to carry out replacements to potentially pre-agreed service levels, etc.

#### 11.2.4 Forward funding

Where provision for future expenditure is to be made within the service charge accounts such sums should not be included as accruals but should be considered as contributions towards reserve or sinking funds as above and reported accordingly.

Accruals are expenses for goods and services actually incurred in a period for which no invoice has been received. As the cost relates to the period, it should be charged to the service charge account for that period.

However, in certain instances, owners and/or managers often seek to collect or retain money in anticipation of future expenditure by ‘accruing’ costs within a service charge period prior to any works being committed or any liability for expenditure being incurred.

Often the cost of anticipated major works is included in the service charge budget but for whatever reason, no works were actually commenced during the service charge period in question. In such circumstances, the amount included within the original budget is frequently, and incorrectly, retained as an ‘accrual’ against the anticipated commencement of works in the next or subsequent years.

If no expenditure has been incurred, it follows that costs cannot then be ‘accrued’ into the service charge period. Therefore, where no liability for costs has been incurred, the retention of occupier monies outside of a properly constituted sinking or reserve fund is contrary to best practice, and is considered to be wholly inappropriate under any circumstances.

Where the lease does not make specific provision for the setting-up of a sinking or reserve fund, it can often be beneficial to both owners and occupiers to spread the anticipated future works over a number of service charge periods. Such a voluntary arrangement will require to be separately agreed and the costs should be shown on the expenditure report under a separate heading within forward funding titled, ‘Contributions towards future works’. Further details of the forward funding should also be disclosed within the notes to the expenditure report.

#### 11.2.5 Payment plans

Where a sinking or reserve fund or other basis of forward funding has not been put in place, the incidence of significant or extraordinary one-off expenditure can often represent an onerous burden for tenants. In such circumstances an owner might be agreeable to recovering the costs over more than one service charge period (perhaps as a gesture of goodwill to ease the burden on an occupier’s cash flow).



Where the lease is otherwise silent, this is to be regarded as a concession – which is not to be confused with a reserve or sinking fund, or a depreciation charge.

In granting such a concession, there needs to be a clear agreement, which would often be expressed as ‘personal only’ to each occupier. It would be usual to ensure that the period over which the expenditure is to be recovered is within the term of an individual occupier’s lease. The agreement would also need to set out what will happen with regard to payment of any outstanding balance on the original costs owed, in the event the occupier assigns his or her lease or becomes insolvent, or if the lease is otherwise determined.

Where the occupier is a single individual, such an arrangement could, under certain circumstances, be considered to be a credit agreement under Consumer Protection legislation, and therefore it is recommended that legal advice be sought prior to entering into such an arrangement.

### 11.3 Best Practice

In managing sinking and reserve funds or depreciation charges, the following is to be considered as best practice:

- a) Monies accumulated in a sinking or reserve fund are to be held in one or more separate discrete, interest bearing, bank accounts.
- b) The owner or managing agent should act reasonably in estimating the amount of the sinking or reserve fund contributions to be included within the service charge, which should relate to specifically identified expenditure only (for example, repairs or replacement of the roof, boiler plant, lift, etc.) rather than other unidentified future expenditure.
- c) The owner or manager is to provide a clear explanation of the basis of calculation of the sinking or reserve fund contribution and the items to which it relates, and will apply a realistic assessment of the anticipated life cycle of the item in question and the funds accumulated from previous service charge periods (including any interest).
- d) Owners will make all payments into the sinking or reserve fund to account for void premises. Owners must ensure that any shortfall in the sinking or reserve fund because of a concession, bad debt, or deferment is made up by the occupier concerned or by the owner.
- e) Statements of service charge expenditure will contain a clear statement of any contributions to and expenditure from the sinking fund account, along with the account opening and closing balances, the amount of interest earned and any tax paid in the relevant period.
- f) Where expenditure is required in respect of any item for which a sinking or reserve fund was established, the owner should apply funds from the sinking or reserve fund towards such costs.
- g) On completion of the sale of a property, the vendor should pass all sinking or reserve fund monies held to the purchaser, together with any accrued interest. It is advisable to seek advice to ensure any tax liability on the fund is appropriately mitigated and accounted for. (See SCSI Professional Guidance, ‘Commercial Service Charge Handover Procedures – 1st Edition’)
- h) Charges made in respect of depreciation belong to the owner. Accordingly, where a depreciation charge is made, the responsibility for the cost of replacement moves to the owner. The owner or manager will act reasonably in estimating the amount of the depreciation charge, and will provide a clear explanation of the basis of the charge calculation and the details of the specific items for which the depreciation charge is calculated.
- i) A proper and reasonable depreciation charge is to be considered as an annual cost to the owner rather than recovery of the initial cost of installation.
- j) Depreciation charges and sinking/replacement funds are mutually exclusive. A depreciation charge cannot be made where a sinking or reserve fund is or will be made in respect to a specific item, and vice versa.
- k) The nature of commercial leases and, in particular, the length of these leases has changed substantially over recent years. Many items managed under the service charge will have a life expectancy longer than the lease term being granted. Owners and occupiers need to carefully consider how they will recover (or pay for) these major expenditure items when they are due. It is, therefore, recommended that proper PPM plans are used.
- l) In addition to regular expenditure on services, owners and occupiers may need to make provision for occasional one-off outlays on replacing major items of equipment (such as a heating system). Major expenditure of a regularly recurring nature (such as external redecorations) can also cause significant fluctuations in the amount of service charge payable each year.
- m) The move towards shorter leases creates difficulties in the recovery of the cost of long-term maintenance/repair. An occupier occupying under a lease for a term of, say, five years may only have a ‘transitory’ interest in the replacement of a boiler, for example, which might have a life expectancy far beyond the term of his or her lease. That occupier is, therefore, not likely to be interested in the

replacement of the boiler at an indeterminate date in the future.

- n) Contrast this with the situation of an incoming occupier who has signed a new lease that includes a liability for payment of a proportion of the cost of repair and replacement of the owner's plant, who then finds that the boiler requires replacement within the first year of the term.
- o) To the extent that these items can be foreseen, it may make sense for the cost of major extraordinary expenditure items to be spread over a number of years (and over a number of lease periods) by setting up a sinking or reserve fund, rather than charging the whole cost to the current occupiers in the year in which the equipment is replaced.

# 12. Initial provision, replacement and improvement of fabric, plant and equipment

## 12.1 The principles of replacement and improvement in the context of service charges

The service charge would usually be limited to the recovery of the reasonable costs of maintenance, repair and replacement (usually where beyond economic repair) of the fabric, plant, equipment and materials necessary for the property's operation.

Service charge costs will not include:

- any initial costs (including the cost of leasing of equipment) incurred in relation to the original design and construction of the fabric, plant or equipment;
- any setting-up costs that are reasonably to be considered part of the original development cost of the property;
- improvement costs above the costs of normal maintenance, repair or replacement; and
- future redevelopment costs.

Service charge costs may include improvements or enhancement of the fabric, plant or equipment where such expenditure can be justified following the analysis of reasonable options and alternatives, and with regard to a cost-benefit analysis.

Managers should provide the facts and figures to support and justify such a proposal.

Recent case law has determined that the length of the original or unexpired term of the tenant's lease may be a factor in determining whether costs are recoverable.

If an owner can demonstrate that repairs are necessary to comply with the obligations under the terms of and within the life of the lease, the costs are likely to be recoverable, even from a tenant whose lease is about to end.

## 12.2 Initial provision of fabric, plant and equipment

Service charge costs will not include any initial costs (such as the cost of leasing of equipment) incurred in relation to the original design and construction of the fabric, plant or equipment. The owner is expected to provide these.

This also extends to the cost of fitting-out and equipping any on-site management facilities, as these costs will be indistinguishable from other facilities and equipment such as lifts; heating, ventilating and air-conditioning plant; security systems; toilets; etc. that comprise part of the property. It is expected that these systems will be provided for the management, administration and operation of the property's services from the outset.

In line with best practice, the initial cost of providing such furniture and facilities are not to be included as part of the service charge.

## 12.3 Like-for-like replacement

The service charge should be limited to the costs of replacement and renewal of fabric, plant or equipment only, providing:

- the relevant items being replaced or renewed are beyond economic repair, or efficient or economic operation;
- replacement or renewal of such items is a relatively low cost compared with the much greater cost that could occur due to material postponement of the replacement or renewal; or
- replacement or renewal of such items is a proper requirement of any public or competent authority or legislation, or of the insurers.

Plant and equipment reaches the end of its economic life when it is more economic to replace it than to maintain it. Whether equipment is approaching the end of its economic life or not is determined by an inspection of the plant in operation by an experienced engineer. As equipment approaches the end of its economic life, it is reasonable to anticipate that failures will occur with increasing frequency; therefore, a review of service records, along with records of the occurrence and frequency of failures, will help to establish whether it is necessary to replace it.

## 12.4 Replacement with enhancement

Where plant and equipment that has become dilapidated or worn out is replaced, the replacement will usually include an element of enhancement or upgrade of the previous equipment, due to the fact that the replacement will be of an equivalent modern standard.

Strictly speaking, replacement of plant and equipment by its modern equivalent would generally fall within the definition of repair and not improvements. However, there may well be a tendency towards exceeding the design specification of the original equipment in order to meet modern requirements, or to introduce new products or practices intended to improve the service levels and/or value for money.

If the costs are to be recovered through the service charge, it is important to consider whether the intention is to improve or repair the existing equipment.

If the additional cost of carrying out the improvement can be justified on a cost-benefit basis, for example, a reduction in the ongoing maintenance costs, increased energy efficiency, etc., there is a case for the service charge to be made to cover these. In such circumstances, proper communication, supported by figures to support and justify such a proposal, will help achieve a practical and common-sense solution.

## 12.5 Improvement and enhancement

Service charges would not generally include the cost of improvement above the cost of normal maintenance, repair and replacement as above; but it is likely that circumstances will arise where owners and occupiers would see a direct benefit from the introduction of new innovations or additional improvement or enhancements of the building fabric, plant, or equipment.

The service charge might include such costs where the expenditure can be justified following analysis of reasonable options and alternatives, and having regard to a cost-benefit analysis over the term of the occupiers' leases. Managers should communicate any proposals clearly to occupiers, and provide the facts and figures to support and justify such a proposal.

## 12.6 Refurbishment

Refurbishment is a different concept to improvement. Within the scope of the refurbishment works proposed there may include elements of catching up on accumulated disrepair as well as elements of improvement.

The amount occupiers will contribute towards the cost of refurbishment will depend on the extent and nature of the works proposed, in addition to the wording of the lease.

Owners will seek to protect the value of their investments and to maximise rental levels. Refurbishments are often dictated by market forces, and are generally timed to coincide with rent reviews or lease expiries. Occupiers often object to contributing

towards the cost of refurbishment because not only will they be paying for the cost of refurbishment through the service charge, but also through increased rents as a result of any improvements.

When refurbishments result in higher rental values, the owner is to be responsible for the cost of enhancements or improvements above those of maintenance.

The need to carry out extensive repairs or to replace services is also considered in the decision to refurbish. Prior to a refurbishment, major repairs or replacements may be deferred to benefit from economies of scale through placing one major works contract. The improved efficiency of the new environment and any improved services may produce cost savings in day-to-day services management, resulting in the annual service charge being reduced.

Occupiers may still be liable for the costs of repair or replacement carried out as part of a larger refurbishment contract, as though the works had been started separately from the refurbishment.

## 12.7 Communication

To ensure agreement and avoid dispute, if it is proposed to include the cost of improvements in the service charge, this is to be communicated to occupiers before any expenditure is committed. It would also be advisable to record any agreement in writing.

In the case of refurbishment, the owner's proposals are to be communicated to all occupiers well in advance of commencement of any works to explain which costs the occupiers are responsible for in relation to the service charge.

Best practice also recognises the need to establish regular communication between the manager and the occupiers to monitor the refurbishment and to agree which elements of the works are to be considered service charge costs. This reduces or avoids the potential for dispute over any unexpected costs following completion of the works.



# 13. Social, economic and environmental sustainability – Green Lease Considerations

## 13.1 Cooperative and collaborative approach

Owners and occupiers should be aware of the environmental impact of their respective operations. This professional statement supports and promotes a cooperative and collaborative approach in recognising and managing the environmental impact of the occupation and management of commercial premises.

Green leases are standard commercial property leases with specific provisions pertaining to cooperation between landlord and tenants, with the aim of reducing waste, energy including heating, private car usage and water consumption.

Leases are binding documents that are not easy to amend. Owners and occupiers may therefore enter into a non-legally binding memorandum of understanding (MoU), which provides a roadmap for cooperation between the parties on improving the environmental performance of buildings, and which allows the MoU to be updated to reflect the latest business practice as agreed between the parties during the term of the lease.

Further information can be obtained from the Better Building Partnership's 'Green Building Management Toolkit', which is available at:  
[www.betterbuildingspartnership.co.uk/green-lease-toolkit](http://www.betterbuildingspartnership.co.uk/green-lease-toolkit)

## 13.2 Improving environmental performance

The sharing of data and other related information is essential. For this reason, it is recommended that owners, managers and occupiers cooperate on the running of building management systems and on environmental improvement measures.

There should be a fair and reasonable approach to:

- the apportionment of sustainability costs between owners and occupiers, consistent with the principle that there should be an emphasis on the ethos that the 'polluter should pay';
- the carrying out of works that improve the environmental performance of the building; and
- restrictions on works by either party that adversely affect the environmental performance of the building.

In accordance with the principles set out in this professional statement, improved sustainability and other environmental improvement measures are to be taken into account when considering and assessing whether any particular service or provider offers value for money. These are also to be factors in any cost-benefit analysis carried out to justify improvement costs above the costs of normal maintenance, repair or replacement (for example, the installation of energy-efficient plant).

## 13.3 Building Energy Rating Certificate (BER)

For the avoidance of doubt, the cost of obtaining a BER would not normally be considered a recoverable service charge cost. A BER is only required when a building is sold or rented, and therefore has no relevance to, nor is it a requirement for, the provision and management of common services.

## 13.4 Social initiatives

Communication and involvement with local stakeholders and communities is recognised as being of benefit to all. While the direct benefits of this can be difficult to quantify, this professional statement supports and promotes a cooperative and collaborative approach.

## 13.5 Green Leases

Green leases contain provisions relating to the sustainable operation of a building, which may include measures relating to energy efficiency, waste reduction, waste management, water efficiency and so on, as well as social and ethical issues, designed to protect or enhance the Energy Performance Rating.

Green lease provisions can be found in leases in new or existing buildings, and typically include obligations for both landlords and tenants

Green lease provisions often incorporate specific provisions relating to



### 13.5.1 Sustainability

- to promote the reduction of emissions
- to promote the reduction and recycling of waste
- to ensure the environmental sustainability of resources

### 13.5.2 Building Management Forum (Data Sharing)

- to facilitate amicably agreement and compliance with an Energy Management Plan
- to control the implementation of such property specific sustainability plans in the future,
- to agree and operate initiatives to reduce, re-use and recycle waste
- to share the Environmental Performance Data relating to the demised premises and/or the building.

### 13.5.3 Repairs / Decorations

- Not to carry out any repairs in such manner or using such materials which would adversely affect the Energy Performance of the Building.
- To carry out decorations using energy efficient and sustainable products and materials.
- Not to carry out any such decorations in a manner which would adversely affect the Energy Performance of the Building.

### 13.5.4 Alterations

- fit out or other alterations should not have a negative impact on the energy efficiency of the building.
- replacement plant and machinery to be energy efficient / sustainable.
- prohibition on adverse alterations.

### 13.5.5 Rights of Inspection

- by landlord to review and measure tenant's energy and water use / waste production.

### 13.5.6 Service Charges

- Services to be implemented using sustainable and energy efficient materials, cleaning products, plant and machinery.
- cleaning times programmed to minimise use of lighting, heating and air conditioning

- Identify in service charge schedule the costs and improvements as a result of environmental initiatives

## 13.6 Sustainability Checklist

### 1. Energy

The primary objective for a Managing Agent should be to implement an energy reduction strategy that achieves the combined aspirations of the building owner and occupiers. All businesses, whether they own or occupy buildings, will increasingly feel commercial and regulatory pressures to reduce energy consumption and their carbon footprints.

- Produce an energy policy for the building
- Determine the total energy consumed in the building
- Carry out an energy audit of the building
- Obtain an energy rating for the building
- Determine if there are separate meters for individual floors, units, common parts and on the individual services and consider installing advanced meters
- Create an action plan to ensure future action and improvement
- Involve occupiers in reducing energy consumption
- Consider purchasing energy from renewable sources
- Establish if your building can participate in local and/or communal schemes for energy generation or provision
- Agree an approach with the building owner for the installation of renewable technologies

### 2. Waste

Businesses that generate large amounts of waste can incur significant costs with legislation increasingly penalising waste producers financially. Managing Agents can help building owners and occupiers develop strategies to reduce their waste production and associated costs.

Managing Agents also have legal responsibilities in dealing with waste, which must be fully understood.

- Understand the waste hierarchy
- Produce a waste strategy for a building
- Determine the waste streams and volumes in the building by carrying out a waste audit
- Check your responsibilities under the Duty of Care Regulations
- Control waste during refurbishment and fit-out
- Identify and dispose of hazardous waste
- Identify and dispose of electrical equipment

### 3. Water

A Managing Agent has little control over water use in a building but will be expected to help manage and maintain its

supply. Sustainable water management may be less publicised and regulated than managing a building's energy use but it is a natural resource which can easily be conserved. Together with strong environmental benchmarks and water efficient technology, managing a sustainable supply of water will ensure a reduction in environmental impacts and create financial savings.

- Produce a water use policy for the building including targets
- Determine the baseline water usage and the waste water output of the building
- Agree an approach with the building owner for the installation of high efficiency plumbing fixtures and control technologies/control systems in the building
- Undertake a regular programme of leak inspections at the building
- Where possible, use treated and recycled water, captured rain water and grey water, where potable water is not necessary. Rain water harvesting.
- Determine if there are separate water meters for individual units and the common parts and consider installing advanced meters

#### 4. Alterations & Replacement

This is not an area where Managing Agents are generally able to exert much influence. However, there are important issues to be aware of to ensure compliance with the building owner's objectives and particular building environmental standards.

A Managing Agent's role is to ensure changes to a building either retain or enhance its sustainability performance. A Managing Agent should be able to use their position to ensure best practice wherever possible.

- The role of the Managing Agent during refurbishment and fit-out works
- Identify environmental measurement targets
- Ensure sustainable sourcing is a considered part of the works

#### 5. Transport

Effective travel planning not only helps to reduce an employee's dependency on car travel but can also help reduce global CO2 emissions, maintain a healthy workforce and provide financial savings.

A Managing Agent will have little control over an occupier's travel planning policy but they can help building owners and

occupiers ensure suitable facilities are in place at a building in order to support a Green Travel Plan.

- Agree a 'Green Travel Plan'
- Provide space for bicycle storage and shower and changing facilities for cyclists
- Establish shuttle links where practicable to any local transportation hubs
- Prioritise parking spaces for sustainable transport options

#### 6. Cleaning

The extent to which a Managing Agent has any control over cleaning and procurement will differ from building to building. Cleaning staff can play a role in the success of a sustainability strategy as their day to day activities involve maintaining the building. The Managing Agent's role includes guiding and motivating these contractors and encouraging them to become champions of environmental standards.

- Ensure cleaning contractors support all sustainability measures and follow any sustainable procurement strategy in place
- Provide awareness raising and training to cleaners
- Programme cleaning times to minimise the use of lighting, heating and air-conditioning resources
- Specify appropriate cleaning and maintenance procedures for specialist 'green' plant, equipment, fixtures or fittings
- Elimination of toxic cleaning materials which immediately affect the air quality in the building

#### 7. Sharing Initiatives

A Managing Agent can act as a facilitator for change in a building. Although few occupiers will have the capacity to develop major sustainability initiatives on their own, in collaboration they can achieve much more than they could hope to alone. By establishing Green Building Management Groups (GBMGs) and encouraging the exchange of information, a Managing Agent can help develop a sustainability strategy to meet the needs of both owner and occupiers and assist them in setting collective goals.

- Encourage the building owner and the building occupiers to share and exchange sustainability data and policy target achievements
- Help run sustainability workshops for the building occupiers to demonstrate how reductions and savings to energy, water and waste consumption can be made.
- Provide environmental training and education to employees and communicate their achievements when appropriate.

## 8. Service Charge

A Managing Agent can help a building owner to provide maintenance and other services to a property, the costs for which are generally recovered through a service charge.

Where energy, water use and waste management provision is shared between multiple occupiers, it is best practice to make sure service charges are both transparent and fairly apportioned. Sub-metering of energy (and ideally water) use for both occupier and owner controlled parts of a building will allow for fairer apportionment.

- Where practicable, separately identify the cost of sustainability/environmental initiatives within the service charge account
- Consider service charge adjustments to reflect the metered use of energy and water by individual occupiers
- Monitor the savings achieved to service charges and circulate them to both owners and occupiers through the Building Management Forum or equivalent to encourage buy in

## 9. Tenant Handbook

A tenant handbook is a key source of information for occupiers. The handbook should include all appropriate data and documents relating to sustainability aspects of the building.

- Ensure that occupiers are provided with a handbook or information pack at the commencement of their tenancy.

# 14. Additional best practice guidance for shopping centres, retail and leisure parks and business campuses

## 14.1 Marketing and promotions

The marketing of and promotional activity supporting schemes such as shopping centres, retail and leisure parks and business campuses, are recognised as being of joint benefit to all stakeholders, and are therefore often jointly funded.

The service charge budget and accounts should be transparent and should include the gross marketing and promotional expenditure and the contribution, if any, from the owner. This will clearly show the net contribution due from the occupiers.

It is best practice for marketing plans (including promotions) to be prepared and presented to occupiers in advance of the period to which they relate. It is often useful to agree and regularly review marketing plans with occupier/retailer associations in order to analyse their effectiveness, and to ensure that the stated objectives are achieved.

Where the service charge bears the cost, all pedestrian flow data collected is to be issued to occupiers as a matter of course.

As marketing and promotions are of joint benefit, it is important for owners/managers to encourage occupiers to recognise that they have an obligation to proactively communicate their views on the best approach to marketing and/or promotions.

Items that fall within the definition of marketing and promotions might include, for instance:

- advertising including print, outdoor, radio, TV, etc;
- social media campaigns, production of scheme smart phone or mobile device 'app';
- promotions ;
- public relation initiatives ;
- consumer research;
- performance measurement (e.g. pedestrian flow counting); and
- the element of staff costs related to organising or managing the above activities.

Any costs incurred in relation to the initial promotional launch and/or rebranding of a scheme should be borne by the owner,

and should not to be considered as recoverable service charge costs. It is recommended that any plan to relaunch a scheme be discussed between owner and occupiers so that they can agree to an appropriate split of the expenditure to each party.

The marketing of vacant units is not a service charge item.

## 14.2 Customer services, amenities and facilities

### 14.2.1 Pedestrian flow and car counting

Systems that collate information on the number of customers or cars visiting a site often provide useful data to managers to help schedule resources to match the varying needs and demands of schemes.

Such systems are quasi-management tools and the cost of operating and maintaining such systems should therefore be clearly and explicitly shown as a separate cost heading within budget and actual expenditure reports.

Best practice requires that the information obtained is to be shared with occupiers as a matter of course.

However, pedestrian flow data, combined with sales or turnover statistics, is principally a tool for measuring or monitoring the effectiveness of marketing and promotion expenditure and should be either a shared marketing cost or a landlord cost, depending on the nature of the data collected and the extent to which it is shared.

### 14.2.2 Entertainments and seasonal decorations

The costs of entertainments, attractions, Christmas and other seasonal decorations and events within schemes are not classed as a marketing and promotional cost, but are regarded as amenities or facilities and should be included under the appropriate cost heading (see *Boots UK Ltd v Trafford Centre Ltd* (2008) EWHC 3372 (Ch)).

### 14.2.3 Amenities and facilities

Scheme management has moved beyond just providing clean, safe and secure environments, partly as a response to changing customer needs and expectations.

There are many additional services, facilities and amenities that are often considered as a standard requirement by customers, for example, the provision of free WiFi connectivity.

Where providing such services requires the addition of a new facility, it is recommended that this be discussed between owner and occupiers so that they can agree to an appropriate split of the expenditure to each party. The on-going operating and maintenance cost, subject always to the terms of the lease, would usually be met through the service charge, as is standard practice with other areas of expenditure.

It is considered too prescriptive to attempt to provide a list of potential additional services here, as these might vary considerably from property to property, but the provision of such amenities and facilities should be appropriate to the property and location and be the subject of appropriate consultation and communication with occupiers.

The potential for the requirement to provide additional amenities and facilities will often result from technological innovations and where this is the case the provision of additional services and amenities should be carefully considered, be appropriate to the location and provide benefit to the customer experience.

## 14.3 Commercialisation (non-core income)

Increasingly, owners are finding additional non-core income streams from their investments.

They are entitled to receive this income from the investment they have made; however, if the service charge has provided either the initial capital or ongoing services for the income stream, the income is to be used as a credit against the service costs.

When the owner provides the capital but uses the services to support the operation, an appropriate contribution to the service charge is to be made by the owner to reflect the benefit and use of the services.

Best practice for the owner is to clearly state his or her policy with regard to miscellaneous income within the development.

As well as rents being collected on occupational leases, income is also generated from other sources.

Many properties receive income from vending-machine takings, selling recyclable waste, etc., whilst owners might also

receive income from promotional space (e.g. advertising on displays, and in car parks, etc.) and licences granted for other activities within the common part areas (e.g. children's rides, photo booths, etc.).

Occupiers may also have (chargeable) use of photocopiers in the management offices. How such income is treated varies considerably from property to property, and from owner to owner.

There is to be a clear statement of policy on how and to where costs and income generated from services and activities are allocated. Transparency is required at all times.

Income derived from the provision of a service or activity, where the cost is included in the service charge, is to be treated as a service charge credit, for example, photocopy and fax reimbursements, etc. Income derived from promotional activity is to be credited to the marketing expenditure budget.

Where the owner retains income from common areas, and the space is used on a permanent or semi-permanent basis, e.g. Retail Mobile Units (RMUs) or kiosks, the space is to be included in the service charge apportionment matrix. Alternatively, appropriate equivalent credit is to be given for the costs of that space.

For less substantial or temporary fixtures, a sum is to be credited to the service charge to reflect a contribution towards the benefit of the services enjoyed.

Managers are to clearly state their policy on how costs and income generated from services and activities are allocated. The rules are as follows:

- If the item is not funded by the service charge, nor does it use any services, 100 per cent of the income goes to the owner;
- If the item is funded by the service charge, the income is credited to the service charge (e.g. photocopying for occupiers);
- If the item uses some of the services and/or needs support from the site team who are being paid via the service charge, a contribution is to be made to the service charge in accordance with the policy.

In addition to the minimum information budgets and statements of actual expenditure are also to include a statement detailing how income generated from commercialisation or mall income is dealt with, and how shared services are charged.

The statement is also to clearly set out how this income impacts on the service charge, and what reimbursement has been made to it.



# Appendix A: Compliance checklist

This compliance checklist is a basis to enable owners, managers and occupiers to self-assess their compliance with the core principles set out in this professional statement. However, merely ticking the boxes does not constitute full compliance with the professional statement, which also entails adhering to the further recommended best-practice recommendations as provided to support the core principles.

| Core principle  | Evidence  | Comply |
|---|---|--------|
| <b>Value for money</b><br>Procure an appropriate level of service for the occupiers in the building.<br>Demonstrate that services offer good value for money.               | Competitive tender.<br>Other market testing.<br>Regular cost benchmarking.  |        |
| <b>Transparency</b><br>All costs, apportionments and policies are explicit and open to any scrutiny by occupiers or their agents.   | <ol style="list-style-type: none"> <li>1 A full apportionment matrix for the entire property/estate/complex along with appropriate percentage allocation calculations is published.</li> <li>2 All policies are outlined in budget packs.</li> <li>3 Detailed explanations are provided in year-end statements where the costs have materially varied from the budget.</li> <li>4 The landlord bears the cost of all voids and concessions.</li> <li>5 The manager's fees relating to the property during the year are fully disclosed in the notes to the expenditure report.</li> </ol> |        |
| <b>Timeliness of reporting</b><br>All reports are issued within timeframes recommended by the professional statement.   | <ol style="list-style-type: none"> <li>1 Budgets are issued at least one month prior to the start of the service charge year.</li> <li>2 Year-end statements of actual expenditure are issued within four months of the end of the service charge year.</li> </ol>  |        |
| <b>Approval</b><br>Actual expenditure approved by the manager or an audit or independent review.  | <ol style="list-style-type: none"> <li>1 Certificate issued by manager.</li> <li>2 Audit or independent review undertaken in accordance with the lease and TECH09/14BL.</li> </ol>  |        |
| <b>Management fee</b><br>The management fee reflects a reasonable cost to undertake necessary work to manage and operate the services and to administer the service charge. | <ol style="list-style-type: none"> <li>1 Fixed fee (not per cent of service charge).</li> <li>2 Meets professional statement guidelines on what can and cannot be charged for management.</li> </ol>  |        |

| Core principle   | Evidence   | Comply |
|--|--|--------|
| <b>Duty of care to occupiers – consultation and approval</b><br>All costs are recoverable in accordance with leases.<br>The occupiers are consulted where appropriate for their agreement to the levels of service and services to be offered.   | <b>1</b> All occupiers are given the opportunity to comment on the budget.<br><b>2</b> The occupiers are consulted on the levels of service and/or the introduction of new services.<br><b>3</b> All communication and queries are to be dealt with fully and in a timely fashion. |        |
| <b>Standardised financial reporting</b><br>Budgets and statements of actual expenditure are reported in line with this professional statement's cost categories.<br>Where appropriate, separate schedules are prepared to allocate costs to reflect the availability, benefit and use of different services. | <b>1</b> Standardised cost categories are used.<br><b>2</b> Separate schedules are included as appropriate.<br><b>3</b> Full allocation and apportionment schedules included as standard.  |        |
| <b>Interest income and expenses</b><br>Separate interest-bearing accounts are operated for each building, with all interest income and expenses credited or expensed within the service charge.  | <b>1</b> Bank statement of interest income and expenses.   |        |
| <b>Professional statement – compliant terms in new leases</b><br>New leases have adopted professional statement – compliant terms.   | <b>1</b> Standard lease terms.   |        |
| <b>Support for alternative dispute resolution (ADR)</b><br>ADR is supported and recommended as the basis to resolve service charge disputes.   | <b>1</b> Lease makes provision for ADR in the event of dispute.<br><b>2</b> ADR is proactively pursued to facilitate resolution of disputes.   |        |

# Appendix B: Standard industry cost classifications

## B1 Notes

- The cost descriptions are for illustrative purposes only and not intended to represent an exhaustive list.
- Owners and managing agents are encouraged to include additional cost descriptions where this will facilitate greater transparency and clarity with regard to the expenditure incurred or proposed. However, to maintain industry standards and to facilitate benchmark comparison, the cost class and cost-category structure should not be altered.
- Where reasonable and appropriate cost should be allocated to separate schedules. Separate cost categories are not to be used to describe activities provided across different elements of a subject property, such as the estate, car park, etc. However, where multiple schedules are not used, in order to achieve transparency it may be necessary to repeat certain cost descriptions to make a clear distinction between specific areas where costs have actually been incurred, for example, cleaning costs for estates and car parks.

## B2 Cost classifications

| Cost class                |                                 |  |
|---------------------------|---------------------------------|--|
| Cost category             |                                 |  |
| Cost description          |                                 | Notes  |
| Management                |                                 |  |
| Management fees           |                                 |  |
|                           | Management fees                 | Owner's or manager's fees for managing and administering the services that are permitted to be recovered under the terms of the lease, excluding rent collection, asset management, etc. |
| Accounting fees           |                                 |  |
|                           | Service charge accounting fees  | Fees for preparation of year-end service charge statement and reconciliation.  |
|                           | Independent accountant's fees   | Independent accountant's fees to review the year-end service charge accounts.  |
|                           | Audit fees                      | Auditor's fees for carrying out a formal audit of the service charge.  |
| Site-management resources |                                 |  |
|                           | Staff costs                     | Direct employment or contract costs for provision of staff for management of on-site facilities.   |
|                           | Receptionists/concierge         | Direct employment or contract costs for provision of reception and concierge staff, including associated administrative and training costs.  |
|                           | Site accommodation (rent/rates) | Rent, service charge and rates associated with the site-management accommodation.  |

|                                    |   |  |
|------------------------------------|---|--|
|                                    | Office costs (telephones/stationery)            | Day-to-day running costs of the on-site management office.   |
|                                    | Systems   | Costs of computer licences, etc. and other systems.  |
|                                    | Help desk/call centre/information centre        | Operational costs for providing helpdesk/call centre/information centre facilities.  |
|                                    | Administration fee                              | Fees for HR and payroll costs associated with dealing with on-site staff (where not included as part of the management fee). |
| <b>Professional fees</b>           |   |  |
|                                    | Landlord's risk assessments, audits and reviews | Consultancy fees and other costs associated with provision and review of owner's health and safety (H&S) management systems. |
|                                    | Other professional fees                         | Fees of specialist consultants engaged in respect of the provision of services.  |
|                                    | Legal fees                                      | Legal advice in respect of the placing or termination of contracts for the provision of services.                            |
| <b>Utilities</b>                   |   |  |
| <b>Electricity</b>                 |   |  |
|                                    | Electricity                                     | Electricity supply to common part and retained areas and central plant, excluding the direct consumption of occupier(s).     |
| <b>Gas</b>                         |   |  |
|                                    | Gas   | Gas supply for the owner's central plant, excluding the direct consumption of occupier(s).                                   |
| <b>Fuel oil</b>                    |   |  |
|                                    | Fuel oil  | Fuel-oil supply for the owner's central plant, emergency generators, etc., excluding direct consumption of the occupier(s).  |
| <b>Water</b>                       |   |  |
|                                    | Water and sewerage charges                      | Water supply to central plant, common part and retained areas, excluding direct consumption of the occupier(s).              |
| <b>Utility consultancy</b>         |   |  |
|                                    | Utility procurement and consultancy             | Consultancy and procurement fees incurred for negotiating, reviewing, auditing and reporting on all utilities.               |
| <b>Soft services</b>               |   |  |
| <b>Security</b>                    |   |  |
|                                    | Security guarding                               | Direct employment or contract costs incurred in providing security guarding for the building(s).                             |
|                                    | Security systems                                | Servicing and maintenance of building security systems (e.g. CCTV, access control, intruder alarms, etc.).                   |
| <b>Cleaning and sustainability</b> |   |  |
|                                    | Cleaning  | Cleaning of common-part and retained areas.  |
|                                    | Window cleaning                                 | Cleaning of external windows.  |
|                                    | Hygiene services/toiletries                     | Cleaning and servicing of common-part toilets and toiletry accommodation.  |

|   |   |  |
|---|---|--|
|   | Carpets/mats hire                                   | Provision of dust and rain mats to common-part areas.  |
|   | Waste management                                    | Refuse collection and waste-management services provided for building occupiers.   |
|   | Pest control  | Pest-control services provided to common-part and retained areas.  |
|   | Snow clearance/road gritting                        | Costs incurred in clearing snow and supplying snowclearing equipment and gritting salt.  |
| <b>Landscaping and environment</b>                  |   |  |
|   | Internal floral displays                            | Providing and maintaining floral displays within the common part areas.  |
|   | External landscaping                                | Provision and maintenance of external landscaped areas and special features.   |
|   | Seasonal decorations                                | Provision and maintenance of seasonal decorations to common-part areas.  |
|   | Events and entertainments                           | Events and entertainments within the common parts areas.   |
| <b>Marketing and promotions</b>                     |   |  |
|   | Marketing   | Marketing and advertising in accordance with marketing strategy.   |
|   | Research  | Research into local market conditions, customer surveys, pedestrian flow counting systems, etc.  |
|   | Marketing staff costs                               | Direct employment of staff or staff contract costs for marketing and promotional activity.   |
|   | Landlord's contribution to marketing                | Financial contributions made by landlord towards marketing and promotions.   |
| <b>Hard services</b>                                |   |  |
| <b>Mechanical and electrical services (M&amp;E)</b> |   |  |
|   | M&E maintenance and repair                          | Planned maintenance and repair of the owner's M&E services, including the contractor's H&S compliance.   |
|   | Life safety systems maintenance and repair          | Planned maintenance and repair of the owner's fire protection, emergency lighting and other specialist life safety systems, including the contractor's H&S compliance. |
|   | H&S (mechanical and electrical)                     | Works carried out to M&E plant and equipment in accordance with H&S regulations or recommended best practice.  |
|   | M&E/life safety systems inspections and consultancy | Auditing the quality of maintenance works and the condition of M&E plant and life safety systems to ensure H&S compliance.   |
|   | Car parking M & E maintenance and repairs           | Maintenance and repair of entry systems, payment systems, car counting systems and other specialist car park equipment.  |



| Lifts and escalators           |  |   |
|--------------------------------|--|---|
|                                | Lift maintenance contract and repair           | Maintenance and repair of lifts in the common part and retained areas, including the contractor's H&S compliance.                           |
|                                | Escalator maintenance and repair               | Maintenance and repair of escalators in the common part and retained areas, including contractor's H&S compliance.                          |
|                                | H&S (lifts and escalators)                     | Works carried out to lifts and escalators in accordance with H&S regulations or recommended best practices.                                 |
|                                | Lift and escalator inspections and consultancy | Auditing the quality of maintenance works, the condition of lift plant and H&S compliance.  |
| Suspended-access equipment     |  | Suspended-access equipment includes all forms of high-level access equipment maintenance, e.g. hatchways, eyebolt, fall arrest and cradles. |
|                                | Suspended-access maintenance and repairs       | Maintenance and repairs to the owner's suspended access equipment, including the contractor's H&S compliance.                               |
|                                | Suspended-access inspections and consultancy   | Auditing the quality of maintenance works, the condition of suspended-access equipment and H&S compliance.                                  |
| Fabric repairs and maintenance |  |   |
|                                | Fabric repairs and maintenance                 | Repair and maintenance of the building structure and fabric common parts and retained areas.  |
|                                | Redecoration                                   | Redecoration and decorative repairs.  |
|                                | H&S (Fabric)                                   | Works carried out to building fabric in accordance with H&S regulations or recommended best practice.                                       |
|                                | Building fabric inspections and consultancy    | Auditing the quality of maintenance works, the condition of the building and H&S compliance.  |
|                                | Car park fabric maintenance and repairs        | Maintenance and repair of the car park structure, fabric and road surfaces.   |
| Income                         |  | Distinct activities that yield a true income to the service charge account.   |
| Interest                       |  |   |
|                                | Interest                                       | Interest received on service charge monies held within the owner's or manager's bank account.   |
| Income                         |  | Income yielded from any facilities installed and/or maintained at the occupier's expense.   |
|                                | Car park income                                |   |

|                                  |                                       |  |
|----------------------------------|---------------------------------------|--|
|                                  | Commercialisation income              |  |
|                                  | Vending machine income                |  |
|                                  | Gift card income                      |  |
|                                  | Other income                          |  |
| <b>Income operating expenses</b> |                                       |  |
|                                  | Operating expenses                    | Overheads, expenses and operational costs incurred in providing any of the income streams, including gift cards.         |
|                                  | Bank charges and transaction costs    | Cash collection costs, transaction fees related to income  |
|                                  | Staff costs                           |  |
| <b>Insurance</b>                 |                                       |  |
| <b>Engineering insurance</b>     |                                       | Landlord's engineering insurances.   |
|                                  | Engineering insurance                 |  |
|                                  | Engineering inspections               |  |
| <b>All-risks insurance cover</b> |                                       | Landlord's all-risk insurance costs.   |
|                                  | Building insurance                    |  |
|                                  | Loss of rent insurance                |  |
|                                  | Public and property owner's liability |  |
|                                  | Landlord's contents insurance         |  |
| <b>Terrorism insurance</b>       |                                       | Landlord's terrorism insurance cover.  |
|                                  | Terrorism insurance                   |  |
| <b>Exceptional expenditure</b>   |                                       |  |
| <b>Major works</b>               |                                       |  |
|                                  | Project works                         | Exceptional and one-off project works, over and above routine operational costs.   |
|                                  | Plant replacement                     | Replacement of the whole or major components of plant and equipment (where beyond economic repair).                      |
|                                  | Major repairs                         | Significant one-off repairs or maintenance costs over and above the costs of routine operational maintenance and repair. |

| Forward funding        |                                     |   |
|------------------------|-------------------------------------|---|
|                        | Sinking funds                       | Forward funding of specific major replacement projects (e.g. plant and equipment replacements, roof replacements, etc.).  |
|                        | Reserve funds                       | Forward funding of specific periodic works to even out fluctuations in annual service charge costs (e.g. internal/external redecorations).  |
|                        | Depreciation charge                 | Depreciation charge in lieu of sinking/replacement fund contribution for major plant and equipment costs.   |
|                        | Agreed contribution to future works | Forward funding of major projects but where the lease does not allow for a sinking or reserve fund to be set up. This is a voluntary arrangement and must therefore be agreed in writing between the owners and individual occupiers and full details provided within the notes to the service charge expenditure report. |
| Miscellaneous charges  |                                     |   |
| Irrecoverable VAT      |                                     |   |
|                        | Irrecoverable VAT                   | Cost of any irrecoverable VAT (if not included in headings above).  |
| External contributions |                                     |   |
|                        | Contributions from external parties |   |
|                        | Contributions to external parties   |   |

# Appendix C: Service charge accounting sample report

In managing the provision of services and in certifying the service charge, managers have a duty to both owners and occupiers to act with professional care, diligence, integrity, and objectivity.

Accounting for service charges in the property industry is a specialist area that requires expertise and an understanding of the sector.

*Service charges in commercial property*, RICS professional statement, 1st edition, recommends as best practice that an annual statement of service charge expenditure be certified by the manager to confirm that it represents a true and accurate record of expenditure incurred in supplying the services to the building, and that the expenditure being recovered is in accordance with the terms of the occupational leases.

The professional statement also recommends that annual statements of service charge expenditure should be reviewed by an independent accountant.

The Institute of Chartered Accountants in England and Wales (ICAEW) and RICS have issued a technical release to provide guidance on reporting on commercial service charges. This technical release provides good practice guidance on technical and practice issues relevant to the work of accountants and other professionals.

This sample report sets out recommended best practice for the disclosures and information that managers should provide to the accountants appointed to carry out an independent review of service charges and to tenants.

It is not for this professional statement to prescribe the operating business model of the manager and, therefore, there is no strict layout or order of preference for the statement of service charge expenditure. However, it is recommended best practice that the statement of service charge expenditure should include the following elements:

- the expenditure report (C3 and CA and CB)
- the service charge certificate (C4)
- the independent accountant's report
- notes to the expenditure report and variance report (C5 and CC)
- operational review (C6) and
- the apportionment matrix (CD and CE).

The information referred to in this sample report under 'Operational review' is considered to be best practice to meet the core principles for communication and transparency as set out in the professional statement as to the nature, type and cost of services provided but would usually be outside of the scope of the independent accountant's review.

## Statement of service charge expenditure

OWNER'S NAME]

[PROPERTY NAME AND ADDRESS]

[dd/mm/yyyy] TO [dd/mm/yyyy]

**Total service charge expenditure** €

### C1 Introduction

This report has been produced by [manager's name] on behalf of [owner's name], landlords of [property name] and relates to the reconciled service charge for the period [dd/mm/yyyy] to [dd/mm/yyyy]. This report has been produced having regard to the best practice guidelines for service charges in commercial property that have been published through the collaboration of a number of professional bodies representing a diversity of interests throughout the property industry.

The report is intended to provide further explanation as to actual service charge costs incurred and any material variances against the property budget issued to tenants on [dd/mm/yyyy]. A summary and detailed expenditure report is included at CA with a variance report showing percentage charge year-on-year at CC.

### C2 The management team

[Insert names and contact details of management team, i.e. property managers, building/centre manager, accounts manager, etc.]

### C3 Service charge expenditure report

The summary or detailed expenditure report should be inserted. This should be prepared and presented in accordance with the current edition of RICS professional statement, *Service charges in commercial property*. Examples of the summary and detailed expenditure reports are included as CA and CB respectively, to this sample report.

### C4 Service charge certificate

#### Model landlord surveyor's certificate

**Certification period: [dd/mm/yyyy] to [dd/mm/yyyy]**

Landlord: .....

Managing agent: .....

Building: .....

I hereby certify that, according to the information available to me, the attached statement of service charge expenditure and accompanying information on pages [ X ] to [ Y ] records the actual cost to the landlord of providing the services to the property for the period [dd/mm/yyyy] to [dd/mm/yyyy], in accordance with the current edition of the RICS professional statement, *Service charges in commercial property*.

Signed .....

[Name and qualifications] .....

Position .....

For and on behalf of [manager's name] .....



## C5 Notes to the expenditure report

### C5.1 Accounting policies

#### C5.1.1 Accruals basis

A statement should be made as to whether the accounts are prepared on an accruals basis or cash basis (note: best practice recommends all statements of service charges should be prepared on an accruals basis).

#### C5.1.2 Insurance claims

A statement should be made detailing how insurance claims are accounted for, e.g. it is policy to recognise income in respect of insurance claims in the service charge period in which confirmation has been received from the insurers that the claim will be settled. The associated costs of the claim are charged to the service charge in the period in which the costs are incurred.

#### C5.1.3 Landlord forward funding

A statement should be made detailing how forward funding by the landlord is accounted for, e.g. where the costs of major works expenditure has been borne upfront by the landlord the cost is to be recovered through the service charge in accordance with the terms agreed between the landlord and tenants.

This section may also be used to provide further details in respect of other policies accounting policies adopted in preparing the expenditure report. For example, details of landlord contribution to the service charge.

### C5.2 VAT

#### Example wording

With effect from [dd/mm/yyyy] the landlord elected to waive the exemption from VAT. Therefore, all service charge expenditure is shown exclusive of VAT. VAT will be charged at the appropriate rate on all service charge payments demanded/ invoiced by the landlord.

OR

The landlord has not elected to waive the exemption from VAT and therefore all service charge expenditure is shown inclusive of VAT where applicable.

### C5.3 Sinking fund/reserve fund

This section is to include a description of the intended purpose of any sinking/reserve fund and details of the calculation of the contributions together with an explanation of the tax treatment of contributions to and interest earned on such funds, and details of the bank account where such monies are held.

It is important to recognise and understand the distinction between sinking funds and reserve funds and all contributions thereto should be accounted for separately.

|  |   |
|--|---|
| Balance brought forward as at [dd/mm/yyyy]       | € |
| Contributions during the year excluding interest | € |
| Interest credited                                | € |
| Expenditure during the year excluding tax        | € |
| Tax paid   | € |
| Balance carried forward as at [dd/mm/yyyy]       | € |

## C5.4 Depreciation charges

This section is to include a clear explanation of the basis of the charge calculation and details of the specific items for which the depreciation charge is made.

## C5.5 Agreed contributions to future works

Where the lease does not specifically allow for sinking or reserve funds to be set up, but there is an agreement between the owners and occupiers to include a charge in the service charge in anticipation of future works, then these costs should be shown on the expenditure report under a separate heading within forward funding titled, 'Agreed contributions towards future works'. Details disclosed in this note should include:

- the nature of the works
- the total cost
- the amount being charged to the tenants via the service charge and
- a timetable of when the charges will be made.

## C5.6 Landlord forward funding

Details disclosed should include:

- the nature of the works
- the total cost
- the amount being recharged to the tenants via the service charge and
- a timetable of when the recharges will be made.

If the owner is seeking to include interest on borrowed monies full details are also to be provided.

## C5.7 Banking

A clear statement is to be provided as to whether service charge monies are held in one or more discrete (or virtual) bank accounts and whether interest earned is credited to the service charge account.

## C5.8 Commercialisation

Where income is generated from services and activities in the property include a clear statement of policy on how and to where costs and income generated from such services and activities are allocated.

## C5.9 Marketing and promotions

The service charge accounts should be transparent and should include the gross marketing and promotional expenditure and the contribution from the owner, to clearly show the net contribution due from the occupiers.

|                                       |   |
|---------------------------------------|---|
| Gross marketing/promotion expenditure | € |
| Contribution from the owner           | € |
| Net marketing/promotion expenditure   | € |

## C5.10 Total cost of management

### C5.10.1 Management fees

The manager should provide details of the basis of their appointment and whether this relates only to the subject property or includes other property owned by the same landlord/client.

The manager should confirm the basis of the fee, e.g. a fixed fee subject to annual review/indexation and should include a clear statement as to whether the fee relates only to work carried out in managing the service charge. RICS professional statement *Service charges in commercial property* clearly states that asset management and rent collection costs are excluded from the service charge management fee. Good practice would be to confirm this in the service charge budget and statement of actual expenditure.

### C5.10.2 On-site management

The manager should provide details of all on-site management staff and the total employment costs, which would usually include National Insurance, pension contributions and other direct employment costs. A separate breakdown of any other costs incurred in employing on-site staff, such as the provision office accommodation, etc. should be provided.

If staff are employed on more than one property a clear explanation is to be given of the calculation of the costs charged to the subject property, which should generally only relate to those costs associated with the actual time spent working on that property.

If a separate administration charge is made in relation to human resources and payroll costs associated with dealing with on-site staff, this should be clearly stated together with the amount of the fee and identified as a separate cost heading.

### C5.10.3 Summary of all fees charged by the managing agent

All fees charged by the managing agent should be separately disclosed in the service charge accounts. This can either be done by using separate codes on the face of the expenditure report or by providing additional detail by way of a note. An example note is provided below:

| Expense code             | Total fees | Professional fees | Procurement fees |
|--------------------------|------------|-------------------|------------------|
| Management fees          | €1,000     | €1,000            | -                |
| FM fees                  | €500       | €500              | -                |
| Help desk                | €250       | €250              | -                |
| Staff salaries (on-site) | €250       | €250              | -                |
| Office costs (on-site)   | €50        | €50               | -                |
| Electricity              | €250       | -                 | €250             |

Where there have been multiple managers during the period the relevant fees should be shown in separate columns.

## C5.11 Accruals

These are expenses for goods and services actually incurred in a period for which no invoice has been received. As the cost relates to the period, it should be charged to the service charge account for that period.

A schedule of accruals included in the service charge expenditure should be provided. Where invoices are not received in respect of an accrual brought forward from the previous year, the accrual should be credited back to the service charge unless there is a realistic expectation that an invoice will be received in the future.

Large round sum provisions included to spread the cost of significant works over a period of time are not accruals as they do not represent a liability at the end of the period. Accordingly, they should not be included as accruals but should be considered as contributions towards reserve or sinking funds and disclosed separately (see section C5.3).

## C5.12 Prepayments and security deposits

A schedule of prepayments included in the service charge expenditure for the period should be provided (including utility deposits).

## C5.13 Empty units and concessions granted to tenants

Where appropriate, costs are apportioned on a daily basis and for the avoidance of doubt it is confirmed that the landlord bears an appropriate proportion of the service charge expenditure in respect of voids and vacant premises.

Likewise, if any tenant has any form of concession, whereby their contribution towards the service charge is capped, or is lower than the apportionment due, the landlord pays the difference.

# C6 Operational review

This section should comprise a comparison between the budgets and finalised actual expenditure for each service line for the period in question. The report should be prepared using the same headings as the service charge expenditure report and should include a detailed commentary and an explanation of significant variances.

## C6.1 Service procurement

### C6.1.1 Procurement fees

Where a procurement specialist is used this should be clearly stated together with the amount of the fee and the cost category in which it is included. A clear explanation should also be provided as to the basis of calculation of the fee to demonstrate delivery of best value solutions, greater value for money and cost effectiveness.

## C6.2 Contracts

The manager should provide tenants with a schedule of contracts in force during the service charge period with details of the contractor, a summary of the scope of the contract, the annual contract sum, the date of commencement and length of the contract and dates of any reviews.

Where a contract has been retendered or placed during the service charge period the manager should provide a brief summary of the results of the selection process and a clear explanation of the rationale for the appointment.

Where appropriate and at least every three years, contractors and suppliers should submit competitive tenders or quotations although where this is not considered to be cost effective the manager should benchmark the service standards and pricing to confirm value for money.

For each of the main service lines the manager should provide a summary of when the service line contract was last retendered.

## C6.3 Service charge allocation and apportionment

### C6.3.1 Service charge allocation – schedules

Where costs are allocated into separate schedules, managers should provide a detailed description of the schedules and the basis and rationale for the cost allocation.

**For example:**

#### **Service charge allocation**

Costs are allocated to separate schedules and the costs apportioned to those who benefit from those services as follows:

[Insert list of schedules and description]

Schedule 1 Estate

Schedule 2 Building 1

Schedule 3 Building 2

[Note to managers – add additional schedules as necessary to achieve fair and reasonable allocation of costs].

#### **Schedule 1 – Estate**

[Insert detailed description of schedule and basis of allocation]

#### **Schedule 2 – Building 1**

[Insert detailed description of schedule and basis of allocation]

#### **Schedule 3 – Building 2**

[Insert detailed description of schedule and basis of allocation]

### C6.3.2 Service charge apportionment

Managers are to provide a full apportionment matrix for the property/complex to all occupiers, which clearly shows the basis of calculation and the total apportionment per schedule for each unit within the property/complex. To avoid doubt and to preserve confidentiality this should exclude details of any individual concessions or other arrangements between individual owners and occupiers; these are costs that are normally to be borne by the owner. An individual occupier should be able to clearly verify the basis and method of calculation used in arriving at their particular percentage apportionment.

Managers should also be transparent with regard to the treatment of void and unlet premises, and the cost attributable to the owner's own use of the property (see empty units and concessions granted to tenants in C5.13).

See CD and CE for example apportionment matrices



## C6.4 Notes on expenditure

A full copy of the budget is enclosed in Appendix A in both summary and detail form. The total anticipated expenditure for [property name] is €xxx split across x schedules.

The expenditure comprises the following:

### Note to managers:

Include summary information under each standard industry cost classifications detailing the service provided, the cost and comments on the specification or staffing levels, last tendered, etc. Explanatory notes are to include a detailed explanation of significant individual costs together with an analysis and full explanation of any material variances between budget and actual expenditure.

Service charge budgets and actual expenditure reports should use the standard industry cost classifications. As a minimum acceptable level of reporting, all reports should be detailed at cost class and cost category level as below.

However, to achieve transparency in accordance with the principles of the professional statement it is recommended best practice particularly in respect of larger properties, that budget and actual expenditure reports and analyses should be provided at detailed cost description level whenever practicable, with a summary of the total costs under each cost category.

In accordance with the proportionality statement included under the professional statement's core principles, for smaller properties or those with limited service charge expenditure (e.g. industrial sites) it is considered acceptable to report at the higher cost category level although this should generally be regarded as an exception rather than the usual practice.

## C7 General notes

[Insert any other relevant information].

## CA Example service charge summary expenditure report

| Period [dd/mm/yyyy] to [dd/mm/yyyy] |               |                      |                          |                          |
|-------------------------------------|---------------|----------------------|--------------------------|--------------------------|
| Property address.....               |               |                      |                          |                          |
| Cost category                       | Expense total | Schedule 1<br>Estate | Schedule 2<br>Building 1 | Schedule 3<br>Building 2 |
| <b>Management</b>                   |               |                      |                          |                          |
| Management fees                     | €60,000       | €10,000              | €25,000                  | €25,000                  |
| Accounting fees                     | €1,600        | €1,600               |                          |                          |
| Site management resources           | €71,135       | €21,135              | €26,600                  | €23,400                  |
| Health, safety and environmental    | €10,000       | €10,000              |                          |                          |
| Subtotal                            | €142,735      | €42,735              | €51,600                  | €48,400                  |
| <b>Utilities</b>                    |               |                      |                          |                          |
| Electricity                         | €229,900      | €5,900               | €112,000                 | €112,000                 |
| Gas                                 | €11,050       | €1,050               | €5,000                   | €5,000                   |
| Fuel oil (heating)                  | €0            |                      |                          |                          |
| Water                               | €7,000        |                      | €3,500                   | €3,500                   |
| Subtotal                            | €247,950      | €6,950               | €120,500                 | €120,500                 |
| <b>Soft services</b>                |               |                      |                          |                          |
| Security                            | €144,100      | €137,500             | €3,500                   | €3,100                   |
| Cleaning and environmental          | €185,730      | €52,250              | €58,300                  | €75,180                  |
| Marketing and promotions            |               |                      |                          |                          |
| Subtotal                            | €329,830      | €189,750             | €61,800                  | €78,280                  |
| <b>Hard services</b>                |               |                      |                          |                          |
| Mechanical and electrical services  | €187,970      | €32,750              | €74,750                  | €80,470                  |
| Lift and escalators                 | €24,500       |                      | €14,000                  | €10,500                  |
| Suspended access equipment          | €5,300        |                      | €2,800                   | €2,500                   |
| Fabric repairs and maintenance      | €99,325       | €36,850              | €40,700                  | €21,775                  |
| Subtotal                            | €317,095      | €69,600              | €132,250                 | €115,245                 |
| <b>Income</b>                       |               |                      |                          |                          |
| Interest                            | -€1,068       | -€332                | -€373                    | -€363                    |
| Income from commercialisation       |               |                      |                          |                          |
| Subtotal                            | -€1,068       | -€332                | -€373                    | -€363                    |
| <b>Insurance</b>                    |               |                      |                          |                          |
| Engineering insurance               | €900          |                      | €500                     | €400                     |
| All risks insurance cover           |               |                      |                          |                          |
| Terrorism insurance                 |               |                      |                          |                          |

| Cost category                  | Expense total     | Schedule 1<br>Estate | Schedule 2<br>Building 1 | Schedule 3<br>Building 2 |
|--------------------------------|-------------------|----------------------|--------------------------|--------------------------|
| <b>Subtotal</b>                | <b>€900</b>       | <b>€0</b>            | <b>€500</b>              | <b>€400</b>              |
| <b>Exceptional expenditure</b> |                   |                      |                          |                          |
| Major works                    | €92,483           |                      | €92,483                  |                          |
| Forward funding                | -€90,000          |                      | -€90,000                 |                          |
| <b>Subtotal</b>                | <b>€2,483</b>     | <b>€0</b>            | <b>€2,483</b>            | <b>€0</b>                |
| <b>Grand total</b>             | <b>€1,039,925</b> | <b>€308,703</b>      | <b>€368,760</b>          | <b>€362,462</b>          |

## CB Example service charge detailed expenditure report

| Period [dd/mm/yyyy] to [dd/mm/yyyy]     |                 |                   |                       |                       |
|---|-----------------|-------------------|-----------------------|-----------------------|
| Property address.....                   |                 |                   |                       |                       |
| Cost category                           | Expense total   | Schedule 1 Estate | Schedule 2 Building 1 | Schedule 3 Building 2 |
| <b>Management</b>                       |                 |                   |                       |                       |
| <b>Management fees</b>                  |                 |                   |                       |                       |
| Management fees                         | €60,000         | €10,000           | €25,000               | €25,000               |
| <b>Accounting fees</b>                  |                 |                   |                       |                       |
| S/C audit fees                          | €1,600          | €1,600            |                       |                       |
| <b>Site management resources</b>        |                 |                   |                       |                       |
| Staff costs                             | €15,000         | €15,000           |                       |                       |
| Receptionists/concierge                 | €50,000         |                   | €26,600               | €23,400               |
| Site accommodation (rent/rates)         | €4,335          | €4,335            |                       |                       |
| (telephones/stationery)                 | €1,800          | €1,800            |                       |                       |
| <b>Health, safety and environmental</b> |                 |                   |                       |                       |
| Risk assessments and audits             | €10,000         | €10,000           |                       |                       |
| <b>Subtotal</b>                         | <b>€142,735</b> | <b>€42,735</b>    | <b>€51,600</b>        | <b>€48,400</b>        |
| <b>Utilities</b>                        |                 |                   |                       |                       |
| <b>Electricity</b>                      |                 |                   |                       |                       |
| Electricity                             | €224,000        |                   | €112,000              | €112,000              |
| Electricity procurement consultancy     | €5,600          | €5,600            |                       |                       |
| Fuel (standby electrical power)         | €300            | €300              |                       |                       |
| <b>Gas</b>                              |                 |                   |                       |                       |
| Gas                                     | €10,000         |                   | €5,000                | €5,000                |
| Gas procurement/consultancy             | €1,050          | €1,050            |                       |                       |
| <b>Fuel oil (heating)</b>               |                 |                   |                       |                       |
| <b>Water</b>                            |                 |                   |                       |                       |
| Water and sewerage charges              | €7,000          |                   | €3,500                | €3,500                |
| <b>Subtotal</b>                         | <b>€247,950</b> | <b>€6,950</b>     | <b>€120,500</b>       | <b>€120,500</b>       |
| <b>Soft services</b>                    |                 |                   |                       |                       |
| <b>Security</b>                         |                 |                   |                       |                       |
| Security guarding                       | €132,000        | €132,000          |                       |                       |
| Security systems                        | €12,100         | €5,500            | €3,500                | €3,100                |
| <b>Cleaning and environmental</b>       |                 |                   |                       |                       |
| Internal cleaning                       | €91,200         |                   | €38,400               | €52,800               |

| Cost category                             | Expense total   | Schedule 1 Estate | Schedule 2 Building 1 | Schedule 3 Building 2 |
|---|-----------------|-------------------|-----------------------|-----------------------|
| External cleaning                         | €15,500         | €15,500           |                       |                       |
| Window cleaning                           | €22,800         |                   | €9,600                | €13,200               |
| Hygiene services/toiletries               | €8,180          |                   | €4,500                | €3,680                |
| Waste management                          | €9,050          | €9,050            |                       |                       |
| Pest control                              | €1,600          | €700              | €500                  | €400                  |
| Seasonal decorations                      | €1,000          |                   | €500                  | €500                  |
| Internal floral displays                  | €9,400          |                   | €4,800                | €4,600                |
| Estate cleaning                           | €18,000         | €18,000           |                       |                       |
| External landscaping                      | €9,000          | €9,000            |                       |                       |
| <b>Marketing and promotions</b>           |                 |                   |                       |                       |
| <b>Subtotal</b>                           | <b>€329,830</b> | <b>€189,750</b>   | <b>€61,800</b>        | <b>€78,280</b>        |
| <b>Hard services</b>                      |                 |                   |                       |                       |
| <b>Mechanical and electrical services</b> |                 |                   |                       |                       |
| M&E maintenance contract                  | €151,250        | €20,000           | €63,000               | €68,250               |
| M&E repairs                               | €16,250         | €2,150            | €6,750                | €7,350                |
| M&E inspections and consultancy           | €7,500          | €7,500            |                       |                       |
| Life safety systems maintenance           | €11,350         | €2,350            | €5,000                | €4,000                |
| Life safety systems repairs               | €1,620          | €750              |                       | €870                  |
| <b>Lift and escalators</b>                |                 |                   |                       |                       |
| Lift maintenance contract                 | €21,000         |                   | €12,000               | €9,000                |
| Lift repairs                              | €3,500          |                   | €2,000                | €1,500                |
| <b>Suspended access equipment</b>         |                 |                   |                       |                       |
| Maintenance contract                      | €5,100          |                   | €2,700                | €2,400                |
| Repairs                                   | €200            |                   | €100                  | €100                  |
| <b>Fabric repairs and maintenance</b>     |                 |                   |                       |                       |
| Internal repairs and maintenance          | €50,000         |                   | €35,000               | €15,000               |
| External repairs and maintenance          | €6,775          |                   |                       | €6,775                |
| Redecorations                             | €5,700          |                   | €5,700                |                       |
| Estate repairs and maintenance            | €32,100         | €32,100           |                       |                       |
| Car park repairs and maintenance          | €4,750          | €4,750            |                       |                       |
| <b>Subtotal</b>                           | <b>€317,095</b> | <b>€69,600</b>    | <b>€132,250</b>       | <b>€115,245</b>       |
| <b>Income</b>                             |                 |                   |                       |                       |
| <b>Interest</b>                           |                 |                   |                       |                       |
| Interest                                  | -€1,068         | -€332             | -€373                 | -€363                 |
| <b>Income from commercialisation</b>      |                 |                   |                       |                       |



| Cost category                    | Expense total     | Schedule 1 Estate | Schedule 2 Building 1 | Schedule 3 Building 2 |
|----------------------------------|-------------------|-------------------|-----------------------|-----------------------|
| <b>Subtotal</b>                  | <b>-€1,068</b>    | <b>-€332</b>      | <b>-€373</b>          | <b>-€363</b>          |
| <b>Insurance</b>                 |                   |                   |                       |                       |
| <b>Engineering insurance</b>     |                   |                   |                       |                       |
| Engineering insurance            | €900              |                   | €500                  | €400                  |
| <b>All risks insurance cover</b> |                   |                   |                       |                       |
| <b>Terrorism insurance</b>       |                   |                   |                       |                       |
| <b>Subtotal</b>                  | <b>€900</b>       |                   | <b>€500</b>           | <b>€400</b>           |
| <b>Exceptional expenditure</b>   |                   |                   |                       |                       |
| <b>Major works</b>               |                   |                   |                       |                       |
| Plant replacement                | €92,483           |                   | €92,483               |                       |
| <b>Forward funding</b>           |                   |                   |                       |                       |
| Sinking funds                    | -€90,000          |                   | -€90,000              |                       |
| <b>Subtotal</b>                  | <b>€2,483</b>     | <b>€0</b>         | <b>€2,483</b>         | <b>€0</b>             |
| <b>Grand total</b>               | <b>€1,039,925</b> | <b>€308,703</b>   | <b>€368,760</b>       | <b>€362,462</b>       |

## CC Example service charge variance report

| Period [dd/mm/yyyy] to [dd/mm/yyyy] |                         |                        |                        |                    |                                 |
|-------------------------------------|-------------------------|------------------------|------------------------|--------------------|---------------------------------|
| Property address.....               |                         |                        |                        |                    |                                 |
|                                     | Previous year<br>actual | Current year<br>budget | Current year<br>actual | Actual v<br>budget | Current v<br>previous<br>actual |
| <b>Management</b>                   |                         |                        |                        |                    |                                 |
| Management fees                     | €60,000                 | €60,000                | €60,000                | 0.00%              | 0.00%                           |
| Accounting fees                     | €1,500                  | €1,600                 | €1,600                 | 0.00%              | 6.67%                           |
| Site management resources           | €66,000                 | €70,000                | €71,135                | 1.62%              | 7.78%                           |
| Health, safety and environmental    | €5,000                  | €15,000                | €10,000                | -33.33%            | 100.00%                         |
| <b>Subtotal</b>                     | <b>€132,500</b>         | <b>€146,600</b>        | <b>€142,735</b>        | <b>-2.64%</b>      | <b>7.72%</b>                    |
| <b>Utilities</b>                    |                         |                        |                        |                    |                                 |
| Electricity                         | €218,700                | €236,000               | €229,900               | -2.58%             | 5.12%                           |
| Gas                                 | €9,700                  | €12,500                | €11,050                | -11.60%            | 13.92%                          |
| Fuel oil (heating)                  |                         |                        |                        |                    |                                 |
| Water                               | €6,880                  | €7,500                 | €7,000                 | -6.67%             | 1.74%                           |
| <b>Subtotal</b>                     | <b>€235,280</b>         | <b>€256,000</b>        | <b>€247,950</b>        | <b>-3.14%</b>      | <b>5.39%</b>                    |
| <b>Soft services</b>                |                         |                        |                        |                    |                                 |
| Security                            | €144,100                | €144,100               | €144,100               | 0.00%              | 0.00%                           |
| Cleaning and environmental          | €176,543                | €180,000               | €185,730               | 3.18%              | 5.20%                           |
| Marketing and promotions            |                         |                        |                        |                    |                                 |
| <b>Subtotal</b>                     | <b>€320,643</b>         | <b>€324,100</b>        | <b>€329,830</b>        | <b>1.77%</b>       | <b>2.87%</b>                    |
| <b>Hard services</b>                |                         |                        |                        |                    |                                 |
| Mechanical and electrical services  | €193,750                | €180,000               | €187,970               | 4.43%              | -2.98%                          |
| Lift and escalators                 | €24,500                 | €24,500                | €24,500                | 0.00%              | 0.00%                           |
| Suspended access equipment          | €5,300                  | €53,000                | €5,300                 | -90.00%            | 0.00%                           |
| Fabric repairs and maintenance      | €34,500                 | €50,000                | €99,325                | 98.65%             | 187.90%                         |
| <b>Subtotal</b>                     | <b>€258,050</b>         | <b>€307,500</b>        | <b>€317,095</b>        | <b>3.12%</b>       | <b>22.88%</b>                   |
| <b>Income</b>                       |                         |                        |                        |                    |                                 |
| Interest                            | -€989                   | -€1,000                | -€1,068                | 6.80%              | 7.99%                           |
| Income from commercialisation       |                         |                        |                        |                    |                                 |
| <b>Subtotal</b>                     | <b>-€989</b>            | <b>-€1,000</b>         | <b>-€1,068</b>         | <b>6.80%</b>       | <b>7.99%</b>                    |
| <b>Insurance</b>                    |                         |                        |                        |                    |                                 |
| Engineering insurance               | €800                    | €1,000                 | €900                   | -10.00%            | 12.50%                          |
| All risks insurance cover           |                         |                        |                        |                    |                                 |

|                                | Previous year<br>actual | Current year<br>budget | Current year<br>actual | Actual v<br>budget | Current v<br>previous<br>actual |
|--------------------------------|-------------------------|------------------------|------------------------|--------------------|---------------------------------|
| Terrorism insurance            |                         |                        |                        |                    |                                 |
| <b>Subtotal</b>                | <b>€800</b>             | <b>€1,000</b>          | <b>€900</b>            | <b>-10.00%</b>     | <b>12.50%</b>                   |
| <b>Exceptional expenditure</b> |                         |                        |                        |                    |                                 |
| Major works                    |                         | €90,000                | €92,483                | 2.76%              |                                 |
| Forward funding                | €25,000                 | -€90,000               | -€90,000               | 0.00%              | -460.00%                        |
| <b>Subtotal</b>                | <b>€25,000</b>          | <b>€0</b>              | <b>€2,483</b>          |                    | <b>-90.07%</b>                  |
| <b>Grand total</b>             | <b>€971,284</b>         | <b>€1,034,200</b>      | <b>€1,039,925</b>      | <b>0.55%</b>       | <b>7.07%</b>                    |

## CD Example service charge apportionment schedule %

| Period [dd/mm/yyyy] to [dd/mm/yyyy] |         |                |                      |                          |                          |
|-------------------------------------|---------|----------------|----------------------|--------------------------|--------------------------|
| Property address .....              |         |                |                      |                          |                          |
| Unit/address                        | Tenants | Area           | Schedule 1<br>Estate | Schedule 2<br>Building 1 | Schedule 3<br>Building 2 |
| <b>Building 1 (Tower block)</b>     |         |                |                      |                          |                          |
| Ground floor                        |         | 10,600         | 7.41%                | 10.43%                   |                          |
| 1st floor                           |         | 15,400         | 10.76%               | 15.16%                   |                          |
| 2nd–4th floors                      |         | 46,200         | 32.29%               | 45.47%                   |                          |
| 5th floor                           |         | 4,900          | 3.42%                | 4.82%                    |                          |
| 6th floor                           |         | 4,900          | 3.42%                | 4.82%                    |                          |
| 7th floor                           |         | 4,900          | 3.42%                | 4.82%                    |                          |
| 8th floor                           |         | 4,900          | 3.42%                | 4.82%                    |                          |
| 9th floor                           |         | 4,900          | 3.42%                | 4.82%                    |                          |
| 10th floor                          |         | 4,900          | 3.42%                | 4.82%                    |                          |
| <b>Total building 1</b>             |         | <b>101,600</b> |                      | <b>100.00%</b>           |                          |
| <b>Building 2</b>                   |         |                |                      |                          |                          |
| Ground floor and first floors       |         | 9,750          | 6.81%                |                          | 23.49%                   |
| 1st floor                           |         | 6,500          | 4.54%                |                          | 15.66%                   |
| 2nd floor                           |         | 6,500          | 4.54%                |                          | 15.66%                   |
| 3rd–5th floors                      |         | 18,750         | 13.10%               |                          | 45.18%                   |
| <b>Total building 2</b>             |         | <b>41,500</b>  |                      |                          | <b>100.00%</b>           |
| <b>Grand total</b>                  |         | <b>143,100</b> | <b>100.00%</b>       |                          |                          |

## CE Example service charge apportionment schedule % (weighted floor areas)

| Period [dd/mm/yyyy] to [dd/mm/yyyy] |             |               |        |              |               |             |               |             |                  |           |         |
|-------------------------------------|-------------|---------------|--------|--------------|---------------|-------------|---------------|-------------|------------------|-----------|---------|
| Property address .....              |             |               |        |              |               |             |               |             |                  |           |         |
| Weighting                           |             |               |        |              |               |             |               | Sch 1       | Sch 2            | Sch 3     | Sch 4   |
| Unit no                             | Tenant name | NIA (sq. ft.) | 0–5000 | 5,001–10,000 | 10,001–20,000 | Over 20,000 | Weighted area | All tenants | High street only | Main mall | Offices |
|                                     |             |               | 100%   | 80%          | 70%           | 60%         |               | 147,785     | 14,060           | 126,825   | 6,900   |
| <b>High street</b>                  |             |               |        |              |               |             |               |             |                  |           |         |
| 1                                   |             | 350           | 350    |              |               |             | 350           | 0.24%       | 2.49%            |           |         |
| 2                                   |             | 12,800        | 5,000  | 4,000        | 1,960         |             | 10,960        | 7.42%       | 77.95%           |           |         |
| 3                                   |             | 300           | 300    |              |               |             | 300           | 0.20%       | 2.13%            |           |         |
| 4                                   |             | 1,200         | 1,200  |              |               |             | 1,200         | 0.81%       | 8.53%            |           |         |
| 5                                   |             | 500           | 500    |              |               |             | 500           | 0.34%       | 3.56%            |           |         |
| 6                                   |             | 750           | 750    |              |               |             | 750           | 0.51%       | 5.33%            |           |         |
|                                     |             |               |        |              |               |             | <b>14,060</b> |             |                  |           |         |
| <b>Main mall</b>                    |             |               |        |              |               |             |               |             |                  |           |         |
| 7                                   |             | 1,050         | 1,050  |              |               |             | 1,050         | 0.71%       |                  | 0.83%     |         |
| 8                                   |             | 7,250         | 5,000  | 1,800        |               |             | 6,800         | 4.60%       |                  | 5.36%     |         |
| 9                                   |             | 1,050         | 1,050  |              |               |             | 1,050         | 0.71%       |                  | 0.83%     |         |
| 10                                  |             | 1,780         | 1,780  |              |               |             | 1,780         | 1.20%       |                  | 1.40%     |         |
| LSU 1                               |             | 29,700        | 5,000  | 4,000        | 7,000         | 5,820       | 21,820        | 14.76%      |                  | 17.20%    |         |
| 11                                  |             | 1,500         | 1,500  |              |               |             | 1,500         | 1.01%       |                  | 1.18%     |         |
| 12                                  |             | 1,500         | 1,500  |              |               |             | 1,500         | 1.01%       |                  | 1.18%     |         |
| 13                                  |             | 2,700         | 2,700  |              |               |             | 2,700         | 1.83%       |                  | 2.13%     |         |
| 14                                  |             | 1,800         | 1,800  |              |               |             | 1,800         | 1.22%       |                  | 1.42%     |         |



| Unit no           | Tenant name | NIA (sq. ft.) | Weighting |              |               |             | Weighted area | Sch 1       | Sch 2            | Sch 3     | Sch 4   |
|-------------------|-------------|---------------|-----------|--------------|---------------|-------------|---------------|-------------|------------------|-----------|---------|
|                   |             |               | 0-5000    | 5,001-10,000 | 10,001-20,000 | Over 20,000 |               | All tenants | High street only | Main mall | Offices |
|                   |             |               | 100%      | 80%          | 70%           | 60%         |               | 147,785     | 14,060           | 126,825   | 6,900   |
| <b>Dept store</b> |             | 56,500        | 5,000     | 4,000        | 7,000         | 21,900      | 37,900        | 25.65%      |                  | 29.88%    |         |
| 15                |             | 3,375         | 3,375     |              |               |             | 3,375         | 2.28%       |                  | 2.66%     |         |
| 16                |             | 2,200         | 2,200     |              |               |             | 2,200         | 1.49%       |                  | 1.73%     |         |
| 17                |             | 6,000         | 5,000     | 800          |               |             | 5,800         | 3.92%       |                  | 4.57%     |         |
| 18                |             | 5,500         | 5,000     | 400          |               |             | 5,400         | 3.65%       |                  | 4.26%     |         |
| LSU 2             |             | 25,900        | 5,000     | 4,000        | 7,000         | 3,540       | 19,540        | 13.22%      |                  | 15.41%    |         |
| 19                |             | 270           | 270       |              |               |             | 270           | 0.18%       |                  | 0.21%     |         |
| 20                |             | 12,200        | 5,000     | 4,000        | 1,540         |             | 10,540        | 7.13%       |                  | 8.31%     |         |
| 21                |             | 1,800         | 1,800     |              |               |             | 1,800         | 1.22%       |                  | 1.42%     |         |
|                   |             |               |           |              |               |             | 126,825       |             |                  |           |         |
| <b>Offices</b>    |             |               |           |              |               |             |               |             |                  |           |         |
| 1st floor         |             | 2,450         | 2,450     |              |               |             | 2,450         | 1.66%       |                  |           | 35.51%  |
| 2nd floor         |             | 2,450         | 2,450     |              |               |             | 2,450         | 1.66%       |                  |           | 35.51%  |
| 3rd floor         |             | 2,000         | 2,000     |              |               |             | 2,000         | 1.35%       |                  |           | 28.99%  |
|                   |             |               |           |              |               |             | 6,900         |             |                  |           |         |
|                   |             | 184,875       |           |              |               |             | 147,785       | 100%        | 100%             | 100%      | 100%    |

## CF Example service charge apportionment schedule €

| Period [dd/mm/yyyy] to [dd/mm/yyyy] |             |             |                  |            |            |             |
|-------------------------------------|-------------|-------------|------------------|------------|------------|-------------|
| Property address .....              |             |             |                  |            |            |             |
|                                     |             | Sch 1       | Sch 2            | Sch 3      | Sch 4      |             |
| Unit no                             | Tenant name | All tenants | High Street only | Main mall  | Offices    | Total       |
|                                     |             | €50,000.00  | €25,000.00       | €50,000.00 | €10,000.00 | €135,000.00 |
| <b>High street</b>                  |             |             |                  |            |            |             |
| 1                                   |             | €118.42     | €622.33          |            |            | €740.75     |
| 2                                   |             | €3,708.09   | €19,487.91       |            |            | €23,196.00  |
| 3                                   |             | €101.50     | €533.43          |            |            | €634.93     |
| 4                                   |             | €406.00     | €2,133.71        |            |            | €2,539.71   |
| 5                                   |             | €169.16     | €889.05          |            |            | €1,058.21   |
| 6                                   |             | €253.75     | €1,333.57        |            |            | €1,587.32   |
| <b>Main mall</b>                    |             |             |                  |            |            |             |
| 7                                   |             | €355.25     |                  | €413.96    |            | €769.20     |
| 8                                   |             | €2,300.64   |                  | €2,680.86  |            | €4,981.50   |
| 9                                   |             | €355.25     |                  | €413.96    |            | €769.20     |
| 10                                  |             | €602.23     |                  | €701.75    |            | €1,303.98   |
| LSU 1                               |             | €7,382.35   |                  | €8,602.40  |            | €15,984.75  |
| 11                                  |             | €507.49     |                  | €591.37    |            | €1,098.86   |
| 12                                  |             | €507.49     |                  | €591.37    |            | €1,098.86   |
| 13                                  |             | €913.49     |                  | €1,064.46  |            | €1,977.95   |
| 14                                  |             | €608.99     |                  | €709.64    |            | €1,318.63   |
| <b>Dept Store</b>                   |             | €12,822.68  |                  | €14,941.85 |            | €27,764.53  |
| 15                                  |             | €1,141.86   |                  | €1,330.57  |            | €2,472.44   |
| 16                                  |             | €744.32     |                  | €867.34    |            | €1,611.66   |
| 17                                  |             | €1,962.31   |                  | €2,286.62  |            | €4,248.93   |
| 18                                  |             | €1,826.98   |                  | €2,128.92  |            | €3,955.90   |
| LSU 2                               |             | €6,610.96   |                  | €7,703.53  |            | €14,314.48  |
| 19                                  |             | €91.35      |                  | €106.45    |            | €197.79     |
| 20                                  |             | €3,565.99   |                  | €4,155.33  |            | €7,721.32   |
| 21                                  |             | €608.99     |                  | €709.64    |            | €1,318.63   |
| <b>Offices</b>                      |             |             |                  |            |            |             |
| 1st floor                           |             | €828.91     |                  |            | €3,550.72  | €4,379.63   |
| 2nd floor                           |             | €828.91     |                  |            | €3,550.72  | €4,379.63   |
| 3rd floor                           |             | €676.66     |                  |            | €2,898.55  | €3,575.21   |
|                                     |             | €50,000.00  | €25,000.00       | €50,000.00 | €10,000.00 | €135,000.00 |

# Appendix D: Commercial property service charge handover procedures

## 1. Introduction

Unlike demands for the payment of the principal rent reserved under a lease, which are usually charged as a fixed quarterly amount, interim or on-account service charge demands are usually based either on a budget or historic costs. These may not be a true reflection of a tenant's ultimate liability which is usually calculated based on their proportion of the actual costs incurred in a given year in the provision of services to the property. A balancing charge, or credit, will be issued to the tenant when the annual service charge reconciliation compares the tenant's ultimate liability with the on-account service charge payments received for the same year.

As a result of this requirement for annual service charge reconciliations, it is recommended that those responsible for drafting sale or management contracts recognise service charges as an important area. They should ensure that they provide a mechanism for the service charge to continue to be managed and administered in accordance with industry best practice, through and beyond the date of sale or management transfer. This is consistent with the general duty of care owed to occupiers.

This guidance note is aimed at property owners and managers and their legal advisers. Its intention is to set out a series of procedures which will apply during any handover period in order to improve the quality of service to the industry's customers.

Handovers occur for two main reasons; the sale of a property or a change of manager. A sale of a property may not always involve a change in manager as some properties are managed directly by owners or the buyer may keep the existing manager on after the sale completes. This guidance note is intended to cover all situations.

When a property changes hands or a new manager is appointed, delays in handing over information often lead to delays in the issuing of statements of service charge expenditure and reconciliations. In extreme instances, this can result in statements of service charge expenditure being held up for many years, with the resultant difficulties for owners in recovering all costs and expenses, and occupiers having to carry forward potentially onerous contingent liabilities.

This guidance note aims to improve this situation by outlining practical procedure for the handover of information relating to the service charges. Its recommendations are compatible with sections 4.6 and 4.10 of the SCSi / RICS Service charges in commercial property Code of Practice, (the service charge code). These require (among other things) service charge reconciliations to be completed within four months of the end of the service charge period.

### 1.1 Scope of this guidance note

This guidance note covers commercial multi-let property where there is a service charge. It deals with the handover of financial and supplier information between owners and/ or managers.

The mechanics for the handover of service charge information would generally be specified in the sale contract, or (more rarely), within a manager's contractual agreement. In practice, the timetable and requirements set out in such documents are not always adhered to so this guidance note aims to assist the overall process and ultimately lead to an industry standard, the terms of which can then be incorporated into sale contract or management contract documentation.

## 2. Service charge accounts – handover procedures

### 2.1 Sale of a property

On the sale of a property, the onus should be on the seller (either themselves or via their managing agent) to provide to the buyer (or their managing agent) all the necessary information about the service charge in a timely manner.

Sale contracts and the resulting completion statements may make some provision for service charge monies either in express clauses or using the standard conditions of sale.

However, these contract clauses rarely contain sufficient detail. Ideally they should deal with:

- the reconciliation of any outstanding closed service charge years
- the handover of any credit balance on the service charge account
- the recovery of any shortfall or arrears, including specifically which party (buyer or seller) can pursue the arrears and how; and
- the supply to the buyer or its managing agent of adequate records and information to provide continuity in the management and administration of the service charge arrangement for the current service charge year.

Commercial service charges generally fall into two categories:

- i) those where the landlord recovers costs periodically, say quarterly, based on actual expenditure incurred; and
- ii) those where the landlord collects on-account sums in advance, usually quarterly, and reconciles the service charge at the end of the service charge year, comparing actual expenditure against the on-account payments demanded and then producing certificates detailing the resultant credit or debit due on the account.

The correct wording for the sale contract will vary between these two, but the service charge Code states that in both cases reconciliation of the current years' service charge should be achieved within four months of the year-end.

Where appropriate (and/or required), allowance should be made for an audit or review by an independent accountant within this timetable.

The sale of a property can occur at any point during the service charge year. Although some leases permit a change to the service charge year end, it is recommended best practice not to do so save in exceptional circumstances.

So the sale usually occurs part way through (rather than at the end of) a service charge year. The buyer or its manager will be responsible for reconciling the service charge for that year. In order to do so properly and on time it is essential that the seller, or their manager, provides full information within a relatively short time frame of the sale.

Where there are prior service charge years for which the closing accounts have not yet been issued, the seller, or its manager, should be obliged in the sale contract to fully reconcile any outstanding service charge accounts for those prior years within a specified period (certainly no later than two months after completion of the sale).

Often, it is the buyer or the buyer's agent that will actually issue the demands for any balancing charges, credits or certificates (whether to existing or former tenants) once the reconciled accounts are available. Whether the buyer accepts responsibility for pursuing payment will be a matter for negotiation.

In some transactions the buyer is not prepared to deal with previous years. The buyer will insist that the seller reconciles these and issues the accounts before completion.

Where possible, buyers should ensure that sale contracts contain measurable sanctions if information, certification and/or service charge credit balances are not provided within the time frames set. Ideally, the buyer should make a retention from the sale price pending satisfactory receipt of the relevant details. Alternatively, the sale contract could impose liquidated damages, although to be enforceable under contract law the amount of the liquidated damages should reflect a reasonable measurement of the anticipated loss. Otherwise, it may be considered a penalty clause and prove unenforceable.

Where the manager is not being retained by the buyer, it is recommended that the buyer or his agent communicate with the tenants, licencees and occupiers immediately following completion of the sale to advise of the sale and to secure payment of ongoing charges.

## 2.1.1 Property setup information

Information required for the property management set up would usually be requested under standard enquiries before contract. If not, such information, should be passed to the buyer (or their agent) prior to completion, or within five working days of the completion date.

Property Handover Information should include:

- service charge accounting period
- service charge apportionment basis
- details of void areas, landlord's liability and landlord's funding
- details of any tenant direct charges
- current service charge budget
- copies of the last three years' reconciled service charge accounts
- details of commercialisation income and interaction with the service charge accounts
- details of any sinking funds, reserve funds or depreciation charges, as set out in paragraph 2.1.5 below, including current valuation statements, assets, contribution, schedules and expiry dates of funds; and
- a statement of funds currently held in the service charge account along with a list of creditors.
- demand addresses, agency arrangements, trading names and contact details
- tenancy details, including occupancy and vacancy dates, in an up-to-date tenancy schedule
- details of all tenant disputes, payment plans and breaches
- the basis of collection for all direct charges



## 2.1.2 Financial information

Detailed up to date property / tenant financial information should be provided to the buyer (or their agent) at completion, or within five working days of the completion date to include:

- a detailed tenant arrears statement including details of disputes, payment plans and breaches
- details and copies of the last tenant on-account demands both for service charges and direct charges
- for direct charges, including utility recharges, the basis of collection and up-to-date meter readings should be provided; and

an interest summary showing credits to the service charge account.

## 2.1.3 Financial transfer

This is the physical movement of funds between the buyer and seller in the sale process. At completion, the service charge bank account will often contain monies that have not yet been expended. The amount will depend on the level of service charge tenant arrears and the amount owed to suppliers for services rendered. The amount to transfer may be very small.

The sale contract should provide that prior to completion, the seller should supply a full statement of tenant service charge arrears and also within five working days after completion, an updated statement of arrears as at the completion date.

Unless the service charge is being administered by a management company which is being taken over by the buyer, and which will continue to administer the service charge, the buyer will be responsible for collecting from the tenants any outstanding or future on-account payments or balancing charges.

If there are extensive service charge arrears outstanding, the buyer may adjust the purchase price to deduct these to avoid the risk of non-payment.

The seller should ensure, so far as is practicable, that all supplier invoices and credit notes are issued and paid from the service charge account prior to completion.

The buyer may have to fund the service charge account in the period between the completion date and the date when the service charge account is credited with funds from the seller or its manager, or payment by the tenants of on-account sums.

## 2.1.4 Statements of service charge movements

### Current service charge year

As described in section 2.1, as soon as practicable but in any event within four months of the completion date the seller (or their agent) should provide a statement of service charge movements for the period from the start of the current accounting period up to the completion date. The statement should include:

- the income received on account of the service charge, with copy demands
- the statement of service charge expenditure incurred with copies of vouchers/invoices
- an analysis of seller landlord's liabilities and tenant direct charges, marketing and commercialisation accounts. These should be separately identified and where tenant direct charges apply these should be treated separately to the service charge

- a service charge cash reconciliation (calculated as detailed in appendix B)
- an up-to-date arrears statement (if changed from the statement issued within five working days after completion), together with explanatory notes on any disputes; and
- explanatory notes on major variations from the original budget for that service charge accounting period.

Where the closing balance on the service charge cash reconciliation is a positive sum, the seller shall transfer to the buyer within five working days of the issue of the service charge cash reconciliation, the positive balance (after deduction of any interim payment already made on account of such credit balance under paragraph 2.1).

Where the closing balance on the service charge cash reconciliation at the date of transfer is negative (this will occur when the expenditure exceeds the income), the buyer will reimburse such negative balance to the seller within five working days of the issue of the service charge cash reconciliation.

The buyer or its manager will then be responsible for completing the full year service charge reconciliation. This will include certifying the accounts and arranging for their independent review or independent audit, where required, in accordance with the SCSl / RICS Service charges in commercial property Code of Practice, (the service charge code).

The buyer or its manager will then issue the statement of expenditure and any balancing service charges to the tenants at the end of the service charge year in the usual way.

#### **Prior service charge years**

If there are prior service charge years for which the closing accounts have not yet been issued, the contract should set out what is to happen. See section 2.1 for various options.

## **2.1.5 Sinking and reserve funds**

In all instances where the seller operates sinking or reserve funds, the information about these will normally be provided in response to standard preliminary enquiries before contract. If not, the sale contract should provide for the following information to be supplied before the completion date (or at the latest within five working days after completion):

- details of all funds and assets covered
- details of the term of the fund, expiry date and life expectancy of the assets
- a full statement showing fund values / bank balances broken down between each asset and details of landlord and tenant contributions, tax and interest
- a statement of expenditure from each fund, if applicable; and
- details of tax liability and any trust status applicable to each fund.

## **2.1.6 Depreciation charges**

If the service charge included depreciation charges, but details have not been provided in response to standard enquiries before contract, then the sale contract should provide for the following information to be supplied, before the completion date (or at the latest within five working days after completion):

- details of all assets covered by the charges
- details of the period of cover including start date and cost of asset; and
- the final book value of each asset and details of the charges recovered from each service charge year, from each tenant up to the completion date.

## 2.1.7 Security deposits for utilities

There has been a growing trend over recent years for utility companies to request a security deposit from owners as a condition of the supply agreement.

If that utility supply agreement is to be novated to the buyer the seller should obtain confirmation that the supplier recognises the buyer as the beneficial owner of the security deposit, and the security deposit will roll over with it. The sale contract should then provide for the buyer to reimburse the seller an amount equivalent to the deposit. This could be included in the financial transfer procedure set out in section 2.1.3.

If the utility supply agreement is to be terminated on completion (and the buyer will arrange its own in substitution) then the seller can arrange direct for the refund to it of the deposit.

If the original deposit was included as a 'cost' in any previous service charge period, the buyer should account for the return of the deposit as a credit item as part of the service charge reconciliation up to the date of sale.

## Sale of Property

| Timeline   | Information To Be Provided by Old Managing Agent to Buyer / New Managing Agent                    |
|--|---|
| Immediately Prior to Completion of Sale            | <b>Tenants:</b>   |
|  | Detailed service charge arrears statement for each tenant   |
| No Later Than 5 Working Days of Completion of Sale | <b>Service Charges:</b>   |
|  | Confirmation of annual accounting period  |
|  | Basis of apportionment  |
|  | Details of Voids, Landlord liability / funding  |
|  | Details of tenant direct charges / recharges (eg utilities) and basis of calculation              |
|  | Current service charge budget   |
|  | Copies of last 3 years audited service charge accounts  |
|  | Details of commercialisation income and interaction with the service charge accounts              |
|  | Full details of sinking fund / reserve fund accounts held with interest earned                    |
|  | A statement of funds currently held in the service charge account with interest earned            |
|  | A list of creditors.  |
|  | <b>Contractors:</b>   |
|  | List of all 3rd party suppliers / contractors and their contact details                           |
|  | <b>Tenants:</b>   |
|  | List of tenants and their contact details   |
|  | Details of all tenant disputes / payment arrangements   |
|  | Up to date tenancy schedule   |
|  | Detailed arrears statement for each tenant as at sale completion date                             |
|  | Basis of collection for all direct tenant charges   |
|  | Copies of last billing period demands   |
| Within 2 Months of Completion of Sale              | <b>Service Charges:</b>   |
|  | Fully reconciled outstanding historic service charge accounts (if any)                            |
| Within 4 Months of Completion of Sale              | <b>Service Charges:</b>   |
|  | Statement of service charge movements from start of service charge period to sale completion date |
|  | Transfer all remaining service charge funds or seek payment from purchaser (if negative balance)  |

## 2.2 Change of manager

A change of manager will often occur as a result of a sale of property, in which case, the procedures outlined in section 2.1 should be adopted. Where a change in manager occurs for any other reason, the following procedures should apply (and the obligation to comply with them should form part of the management contract).

### 2.2.1 Property set up information

All information required for the property management set up should be provided to the new manager no later than three weeks before the management handover date, to include:

- service charge accounting period
- service charge apportionment basis
- details of void areas, landlord's liability and landlord's funding
- details of any tenant direct charges
- current service charge budget
- copies of the last three years' reconciled service charge accounts
- details of commercialisation income and interaction with the service charge accounts
- details of any sinking funds, reserve funds or depreciation charges, as set out in paragraph 2.1.5 below, including current valuation statements, assets, contribution, schedules and expiry dates of funds
- statement of funds currently held in the service charge account along with a list of creditors.
- demand addresses, agency arrangements, trading names and contact details
- tenancy details, including occupancy and vacancy dates, in an up-to-date tenancy schedule
- details of all tenant disputes, payment plans and breaches the basis of collection for all direct charges

### 2.2.2 Financial information

Detailed up to date property / tenant financial information should be provided to the new manager no later than three weeks before the management handover date to include:

- A detailed tenant arrears statement including details of disputes, payment plans and breaches
- details and copies of the last tenant on-account demands both for service charges and direct charges
- for direct charges, including utility recharges, the basis of calculation collection and up-to-date meter readings, and
- an interest summary showing credits to the service charge account.

On the management handover date, the old manager should provide to the new manager a full service charge arrears list, together with tenant history reports and details of disputes, payment plans and bad debts. It is recommended that the old manager transfers to the new manager, within five working days of the management handover date an amount equal to its reasonable estimate of the credit balance on the service charge account. The old manager should provide to the new manager (within two months of the management handover date) a final service charge cash reconciliation (calculated as detailed in appendix B), together with a transfer of funds equating to the cash balance analysed in the service charge cash reconciliation (less the earlier sum transferred, if any).

## 2.2.3 Statements of service charge movements

A change of manager is likely to be known in good time, unlike completion of sales which can take place at short notice. Consequently, it should be possible for the transfer timetable to be quicker. However, it is recommended that the same timetable as in a sale (as set out in section 2.1.4) is adopted in the management contract as a backstop.

## 2.2.4 Sinking and reserve funds

The same procedures apply as in section 2.1.5, but all statements and transfers should be made to the new manager no later than the management handover date.

## 2.2.5 Depreciation charges

The same procedures apply as in section 2.1.6, but all statements should be issued to the new manager no later than the management handover date.

## Change of Managing Agent

| Timeline  | Information To Be Provided by Old Managing Agent to New Managing Agent                 |
|---|--|
| No Later Than 3 Weeks Prior To Management Handover Date | <b>Service Charges:</b>  |
|   | Confirmation of annual accounting period   |
|   | Basis of apportionment   |
|   | Details of Voids, Landlord liability / funding   |
|   | Details of tenant direct charges / recharges (eg utilities) and basis of calculation   |
|   | Current service charge budget  |
|   | Copies of last 3 years audited service charge accounts                                 |
|   | Details of commercialisation income and interaction with the service charge accounts   |
|   | Full details of sinking fund / reserve fund accounts held with interest earned         |
|   | A statement of funds currently held in the service charge account with interest earned |
|   | A list of creditors.   |
|   | <b>Contractors:</b>  |
|   | List of all 3rd party suppliers / contractors and their contact details                |
|   | <b>Tenants:</b>  |
|   | List of tenants and their contact details  |
|   | Details of all tenant disputes / payment arrangements                                  |
|   | Up to date tenancy schedule  |
|   | Detailed arrears statement for each tenant   |
|   | Copies of last billing period demands  |



## Change of Managing Agent (continued)

| Timeline  | Information To Be Provided by Old Managing Agent to New Managing Agent |
|---|--|
| Management Handover Date                          | <b>Tenants:</b>  |
|   | Details of all tenant disputes / payment arrangements                  |
|   | Up to date tenancy schedule  |
|   | Detailed tenant arrears statement for each tenant                      |
|   | <b>Service Charges:</b>  |
|   | Statement of service charge funds held together with interest earned   |
|   | <b>Contractors:</b>  |
| Within 5 Working Days of Management Handover Date | A schedule of creditors outstanding with copy invoices.                |
|   | Summary of all payments made to 3rd party suppliers / contractors      |
|   | <b>Service Charges:</b>  |
|   | Statement of service charge funds held together with interest earned   |
| Within 2 Months of Management Handover Date       | Transfer of service charge bank account funds                          |
|   | Transfer of sinking fund / reserve fund bank account balances          |
|   | <b>Service Charges:</b>  |
| Within 2 Months of Management Handover Date       | Final service charge cash reconciliation                               |
|   | Transfer of any residual service charge bank account funds             |

### 3. Supplier information

A lack of communication between buyer and seller, or between old and new manager, concerning suppliers can lead to a failure to terminate or novate supplier contracts and result in unauthorised work being carried out and incorrect invoices being issued.

In the course of a sale, a buyer would normally ask for details of the supplier contracts before exchanging the sale contract. In particular, the buyer will be focusing on the novation or termination provisions. The buyer can then decide whether to request novation, assignment or termination of individual contracts, and will provide for this in the sale contract. If the supplier contract is to be terminated, the period of notice may overrun completion which will mean the seller has to pay supplier invoices for the period after completion or handover, so attention must be paid to this early on during the sale process.

Consideration should be made in advance, which supplier contracts are capable of novation or assignment. If the supplier contract cannot be novated or assigned, then the owner/ management must assess what notice should be given to terminate it, and a new contract may need to be established with a new supplier.

It is important to focus on this early to avoid unnecessary duplication of payments to old and new suppliers. The supplier contract will normally be with the owner / management company (the client) so a change of manager will not precipitate a need for novation, assignment or termination.

Where no arrangements are made for novation, assignment or termination of the supplier contract, the seller or previous manager will be responsible for any costs arising under the contract following completion/handover.

If the supplier contract has been novated, assigned or terminated, the old manager should not give instructions or order works from that supplier following completion/ handover.

# Glossary

|                                  |   |
|----------------------------------|---|
| <b>Accruals</b>                  | These are expenses incurred in a period for which no invoice has been received at the period end. As the cost relates to the period, it must be charged to the service charge account for that period.  |
| <b>Arrears statement</b>         | A transaction list of all unpaid charges demanded by the landlord from the tenants, collated on a tenant by tenant basis.   |
| <b>Balancing service charge</b>  | The resulting difference between an individual tenant's apportionment of expenditure and the on-account service charges demanded from that tenant for any specific service charge accounting period, having regard to any service charge concessions that may have been granted.  |
| <b>Buyer</b>                     | The buyer is the new/prospective owner of the property.   |
| <b>Commercial property</b>       | All property that is not residential or agricultural, including retail, office, industrial and leisure properties.  |
| <b>Completion date</b>           | The date of the closing of the sale of a property.  |
| <b>Depreciation charge</b>       | The 'cost' to the owner representing the measure of the wearing-out, consumption or other reduction in the life of an asset.  |
| <b>Direct charges</b>            | Any expenditure that is charged directly to individual occupiers and not funded via the on-account service charges.   |
| <b>Landlord</b>                  | The party that holds the interest in the reversion on the leases granted to the tenants and the party responsible for the provision of common services within the property. (Note: In the context of a sale of the property, the landlord will be the seller prior to the completion date and the buyer after the completion date.) |
| <b>Management handover date</b>  | The date on which the responsibility to manage the property transfers from one property manager to another.   |
| <b>Manager</b>                   | The person or team that budgets, forecasts, procures, manages and accounts for the services that comprise the service charge, whether they are the owner, an in-house team, a management company or a managing agent (including any wholly or partly owned related companies).  |
| <b>On-account service charge</b> | An estimated charge raised in advance and in anticipation of the final service charge liability, calculated from the service charge budget.   |
| <b>Prepayments</b>               | These are expenses paid in one period that relate to the following period in whole or part.   |
| <b>Reserve fund</b>              | A fund formed to meet anticipated future costs of maintenance and upkeep in order to avoid fluctuations in the amount of service charge payable each year (for example, for external cleaning and redecorations).   |

|  |   |
|--|---|
| <b>Sale contract</b>                           | The contract setting out the terms on which the property is to be sold and transferred between the seller and buyer.  |
| <b>Seller</b>                                  | The seller is the previous/current owner of the property.   |
| <b>Service charge account</b>                  | The service charge funds held for the property.   |
| <b>Service charge apportionment</b>            | The method and details of apportioning liability between tenants for contributing to a service charge.  |
| <b>Service charge arrears</b>                  | Any on-account service charge or balancing service charge owed by a tenant to the landlord.   |
| <b>Service charge budget</b>                   | The expenditure estimated by the landlord or its manager that will be incurred in a given service charge accounting period.   |
| <b>Service charge Code</b>                     | The SCSl / RICS Service charges in commercial property Code of Practice   |
| <b>Service charge reconciliation</b>           | A comprehensive comparison of all service charge income demanded against all service charge expenditure (including accruals and prepayments), for a given service charge accounting period that enables the calculation of any balancing charges and credits due from tenants and/or landlords. |
| <b>Sinking fund</b>                            | A fund formed by periodically setting aside money for the replacement of a wasting asset, (for example, heating and air-conditioning plant and equipment, lifts, etc.).   |
| <b>Statement of service charge expenditure</b> | The account of service charge expenditure/costs and related notes.  |
| <b>Tenants</b>                                 | The immediate tenants of the landlord holding leases of lettable accommodation within the property.   |

## Example reconciliation statements

### On completion of sale

|  |               |
|--|---------------|
| Income received from tenants for current open service charge year                          | €             |
| Less: Expenditure incurred/paid for current open service charge year                       | €             |
| Add: Vendor's liability at the date of completion for the current open service charge year | €             |
| Add: Accruals at the date of completion for the current open service charge year           | €             |
| <b>Service charge cash to be handed over on completion</b>                                 | <b>€.....</b> |

### On handover

|   |               |
|---|---------------|
| Service charge demanded from tenants for current open service charge year | €             |
| Less: Expenditure incurred/paid for current open service charge year      | €             |
| Less: Service charge arrears for current open service charge period       | €             |
| Less: Arrears from past service charge years                              | €             |
| <b>Service charge cash to be handed over on transfer</b>                  | <b>€.....</b> |

# Appendix E

## Revenue Commissioners Form On Vat Concession

OFFICE OF THE REVENUE COMMISSIONERS,  
VALUE ADDED TAX BRANCH,  
CASTLE HOUSE,  
SOUTH GREAT GEORGE'S STREET,  
DUBLIN 2.  
(01) 792777 Ext2440\2441

OIFIG NA gCOIMISINEIRI-IONCAIM,  
BRAINSE CHAIN BHREISLUACHA,  
TEACH AN CHAISLEAIN,  
SRAID SAN SEOIRSE THEAS,  
BAILE ATHA CLIATH, 2.

date

### VAT on goods and services supplied to property lessees through landlords ("service charges")

Dear Sir,

I refer to our recent discussion and confirm that, having regard to the special features of the application of VAT to property, the Revenue Commissioners are prepared, as a concession, to agree to the following arrangements for the transmission to VAT-registered lessees of a deduction for VAT charged on these goods and services.

(1) A landlord who is not registered for VAT and who is not obliged to register may seek the agreement of his Inspector of Taxes (VAT) to become registered by concession. The application should be made by letter to the Inspector and should give the address(es) of the property(ies), a list of the registered tenants, the accounting year/s and quote the registered VAT number of the landlord, if already registered. On being satisfied regarding the circumstances of the case the Inspector will register the landlord. A landlord whom an Inspector agrees to register will be allocated a VAT number which will enable the landlord to issue to his registered lessees once a year, directly or through his management agents, invoices bearing this number and showing VAT, where appropriate. Such invoices will enable the registered lessees to take a deduction for the VAT invoiced, subject to the usual conditions.

(2) Landlords who are registered for VAT in accordance with the procedure described above will have the same obligations as persons who are obliged to be registered. They will, therefore, be obliged to keep records in sufficient detail to enable their VAT returns to be checked and validated. In the following instances their obligations will be somewhat modified.

#### (i) Invoices

The landlords will not be obliged to issue invoices showing VAT as they receive payments from their lessees. Only one invoice showing VAT should be issued to the lessee and this at the end of the landlord's accounting year. Any difficulties in this regard (e.g. changes in VAT rates during the year, end of an accounting year not co-inciding with the end of a VAT taxable period) will be settled by the Inspector.

#### (ii) Returns

Unless a landlord has several properties to which different accounting years apply, only one VAT return per year will be required. Although a VAT return form is intended to cover a taxable period of two months only (January/February, March/April and so on) the entry in the return should cover the accounting year of the property in question. This will mean that five "NIL" returns will have to be made each year. If "NIL" returns are not made, computer-operated follow-up procedures will be automatically activated.

If a landlord has several properties and different accounting years apply to different properties, as many "positive" returns as there are accounting years will be required each year. "NIL" returns will also be required as appropriate. The returns should show no net liability or repayment since they will merely represent the appropriate values of liable considerations invoiced to land-lords by suppliers and the same values invoiced by the landlords to their VAT-registered lessees. The returns should show the precise values involved, segregated as between the different tax ratings.



### Conditions

- (3) It is a condition of the concession that it be kept within the strictest bounds and be subject to the following conditions in particular:
- (i) it will operate from accounting years ended March 1985 and later;
  - (ii) it will be subject to regular review;
  - (iii) it will be subject to withdrawal in any particular case at the discretion of the Inspector if he ceases to be satisfied that the conditions of the scheme are met or where he discovers that the limits of the Scheme are exceeded;
  - (iv) it may not result in repayments to participating landlords or in relief for input VAT to which these landlords would not otherwise be entitled.

### Exclusions

- (4) The concession will not extend to the supply of services/goods by landlords using their own labour or other resources. Such supplies are taxable in the ordinary way. This is so whether or not a landlord was liable in respect of the letting of the premises in question.
- (5) The arrangement likewise does not apply to other expenses incurred on a joint basis by lessees, for example, staff employed jointly by a number of lessees subject to re-imbursement by the others.

### VAT-registered landlords

- (6) Landlords who are already registered for VAT may also avail themselves of this concession once they obtain the agreement of their Inspector of Taxes. Such landlords continue to be obliged to make VAT returns in respect of those activities for which they are already registered or obliged to be registered. Details of the transactions covered by the concession should be included, at the appropriate time, in such a landlord's ordinary VAT returns.

### Payments on account

- (7) A VAT deduction may not be taken by VAT-registered lessees in respect of VAT included in demands for payments on account made by a landlord or his management agent and VAT should not be separately shown on such demands for payment since a deduction may only be claimed by lessees in respect of VAT shown on the end of the year final invoices.

Any problems arising out of the operation of the concession should be addressed to the appropriate Inspector of Taxes (VAT). An example of the operation of the concession is attached.

Yours faithfully,  
D. Dempsey.

## Example

A company develops a site as an office/shop complex and creates 35 year leases in favour of 10 lessees. The company undertakes, as landlord, to provide insurance, security and cleaning services and heat and light and the lessees covenant to re-imburse the company for such cost. The complex is managed by a property management agent on behalf of the company. The lessees undertake to re-imburse the company for the agent's fees also. Each lessee makes a quarterly payment on account of €2,500. At the end of the year the landlord or his agent calculates each lessee's liability as €10,175 made up as follows:

|                           | €      | €     | €       | €                               |
|---------------------------|--------|-------|---------|---------------------------------|
| Insurance (exempt)        | 50,000 | -     | 50,000  | 5,000                           |
| Electricity (zero)        | 10,000 | -     | 10,000  | 1,000                           |
| Heating Oil, Gas (10%)    | 10,000 | 1,000 | 11,000  | 1,000 + 100 VAT                 |
| Cleaning Security (23%) } | 20,000 | 4,600 | 24,600  | 2,000 + 460 VAT                 |
| Management (23%)          | 5,000  | 1,150 | 6,150   | 500 + 115 VAT                   |
|                           | 95,000 | 6,750 | 101,750 | 9,500 + 675 VAT (Total €10,175) |

A landlord, or the management agent on the landlord's behalf, who has made the necessary arrangement with his Inspector of Taxes should issue an itemised invoice (see specimen attached) showing the consideration excluding VAT and indicating separately the VAT on each liable charge. This will enable a VAT-registered lessee to take the appropriate deduction in his VAT return.

## Specimen Invoice

From:

A. Landlord

VAT No. 123456 A

To:

A. Lessee Unit 14(b), XYZ Shopping Centre

Date

To "service charges" for year ended 31 March 1985 as follows:

|                               |                                 |
|-------------------------------|---------------------------------|
| Insurance .....               | €5,000 + Nil VAT (exempt)       |
| Electricity .....             | €1,000 + Nil VAT (0%)           |
| Heating Oil, Gas .....        | €1,000 + €100 VAT (10%)         |
| Cleaning and Security .....   | €2,000 + €460 VAT (23%)         |
| Management Agent's Fees ..... | €500 + €115 VAT (23%)           |
| .....                         | €9,500 + €675 VAT Total €10,175 |
| Less:                         |                                 |
| Paid on Account .....         | €10,000                         |
| Balance .....                 | €175                            |

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