

Sharing out service charge

Q&A Jennifer Meech and Edward Williams detail the requirements for managers to achieve value for money and explain how service charge is divided

DO RETAIL TENANTS HAVE CAUSE TO COMPLAIN?

QUESTION

I am the manager of a shopping centre containing 30 commercial units in two buildings. One of the buildings has a lift and two escalators, the other is single-storey. I recently provided the service charge estimate to the tenants for the upcoming service charge year. The estimate set out what percentage of the service charge each unit will be liable for and made provision for "hard services"; this sum includes the cost of a maintenance contract for an old and mechanically unusual lift. It is maintained by the same company we have used for 10 years.

A few of the tenants complained, arguing that the estimate is in the wrong format and that I have not explained why they have to pay the allocated share. Some tenants in the single-storey building have asked why the hard services costs are so high. Is there any reason for the tenants to complain?

ANSWER

The tenants are entitled to complain that you have not explained their allocated share. The RICS Code of Practice for Service Charges in Commercial Property, 3rd edition ("the Code") requires that the manager send with the budget a clear explanation of the calculation of the occupier's proportion of the total costs. You may also want to reconsider whether it is fair to charge the costs of maintaining the lifts and escalators equally across the tenants of both buildings. You will need to ensure that the maintenance company you are using provides value for money.

EXPLANATION

The 3rd edition of the Code, which was published in early 2014, sets out detailed procedures that are best practice for managers of commercial property. Although practitioners are not required to follow the advice and recommendations in the Code, its contents are likely to be taken into account if a professional negligence action were commenced by the landlord.

Of course, the Code cannot override the terms of the leases of the premises and you should check that you are complying with the landlord's legal obligations. For example, a modern lease might contain a requirement for consultation before engaging in large scale works.

In relation to the "estimate" sent, this may well not be enough. The 3rd edition (unlike the 2nd) makes no reference to "estimates" and instead requires the manager to circulate a "budget". The requirement to send, together with the budget, a clear explanation of the calculation of the occupier's proportion of the total costs is a new requirement in the 3rd edition. Previously a matrix had to be available but there was no requirement to send it with the estimate.

It would be sensible for you to look at the example expenditure reports at Annex B to the Code and use these as a guide. These examples are new to the 3rd edition of the Code and should be useful to the industry.

The example reports contain industry-standard cost classifications which comprise three levels of detail: cost class, cost category and cost description. For your budget you need to provide, at a minimum, cost class and cost category. However, it is best practice (if it is proportionate to do so) to provide all three levels of detail, which would mean expanding on "hard services" to explain how much is due to "lifts and escalators", and, within that, how much is due to the "lift maintenance contract".

Fair division?

As for whether it is fair to charge the costs of maintaining the lifts and escalators equally across the tenants of both buildings, the Code provides that, where some occupiers do not benefit from certain services, or benefit to a lesser extent, the total service charge should be divided into separate parts (schedules) to reflect the availability, benefit and use of services.



You mention that the same lift maintenance company has been used for the past 10 years. It is one of the core principles of the Code that value for money should be achieved when commissioning services. The 3rd edition provides a clear definition of value for money: "paying no more than is necessary for no less than is required".

The Code provides that managers should keep costs under review (generally every three years) and require contractors to submit competitive tenders or provide competing quotations. If re-tendering would not be cost-effective or practical, you should benchmark the service standard and price. You say the lift is mechanically unusual, this may mean that maintenance costs are higher than for a newer lift and fewer companies may operate in the field, but you should ensure that you achieve value for money.

Jennifer Meech is a barrister at Enterprise Chambers and Edward Williams is an associate at Charles Russell Speechlys LLP

Questions can be e-mailed to egq@a@charlesrussell.co.uk and egq@a@enterprisechambers.com