

SCSI/RICS Code of Practice

# Service charges in commercial property

3rd edition



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# Summary of changes since the 2nd edition

The 3rd edition of the SCSI/RICS Code of Practice *Service charges in commercial property* (the Code) follows the same format as the previous edition and is split into 3 sections:

- 1 The Code
- 2 Recommended best practice to support the core principles
- 3 Appendices

The document has been thoroughly reviewed and numerous minor amendments have been made to correct grammatical errors, improve consistency of wording throughout the document and to bring the document in line with SCSI/RICS editorial guidelines.

## Section 1: The Code

The aims and objectives of the Code and the core principles remain broadly unchanged with the exception of minor grammatical amendments.

## Section 2: Recommended best practice

The opportunity has been taken to tidy up some wording but would highlight the following changes:

### 1 Administration

#### 1.3.1 Total cost of management

Reference to the employment of regional facilities managers is now included.

#### 1.3.4 Site management costs

The Code now requires that managers should be clear and explicit where staff costs are allocated to a specific cost heading (e.g. cleaning or security) and where any additional administrative charges are included.

#### 1.4.2 Procurement of services

Reference is now made to BS 8572:2011, Procurement of facility-related services.

#### 1.5.8 Tenant alterations

The RICS information paper *Service charges and tenant alterations* has been summarised and now incorporated as formal guidance.

### 4 Financial controls and competencies

#### 4.2.5 Recommended best practice

Reference is now included to the new ICAEW technical release providing guidance on accounting for commercial service charges. In conjunction with the ICAEW, RICS has issued a sample report on service charge accounting (see appendix C of the Code) 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 the service charges, and for subsequent communication to tenants.

### 7 Provision for anticipated future expenditure

The RICS information paper *Sinking funds, reserve funds and depreciation charges* has been summarised and now incorporated as formal guidance including refined definitions of a sinking fund and a reserve fund.

### 8 Environmental sustainability

Additional guidance is now provided in respect of green leases and Building Energy Rating Certificates.

## Section 3: Appendices

### Appendix B: Standard industry cost classifications

The overriding principles have been substantially amended to focus on facilitation of transparency and clarity with regard to expenditure incurred. Certain wording that duplicates the core principles set out in the Code has been removed.

'Refurbishment' as a cost description has been removed as this is a catch-all for works which may involve repair, replacement and/or improvement of fabric, plant and equipment and where the remaining cost descriptions should be sufficient to facilitate transparency and clarity.

### Appendix C: Service charge accounting sample report

The previous example report has been substantially revised in line with the proposed new ICAEW technical release providing guidance on accounting for commercial service charges and recommended best practice for the disclosures and information that managers should provide to the accountants appointed to carry out an independent review of the service charges, and which should also be communicated to tenants.

It is not for the Code to prescribe the operating business model for 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 certain key elements as set out.

In particular, the example report provides clearer guidance on the proper treatment of accruals and clarifies the distinction between these and the provision for future anticipated expenditure.

### Appendix D: Glossary and terminology

The 3rd edition of the Code provides clearer guidance and definitions on various matters including accruals accounting and planned preventative maintenance.

No responsibility for loss or damage caused to any person acting or refraining from actions as a result of the material included in this publication can be accepted by the authors or SCSi & RICS.

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## SCSI / RICS guidance note

This Code has the status of a guidance note. It provides advice to practitioners. Where procedures are recommended for specific professional tasks, these are intended to embody 'best practice'.

Practitioners are not required to follow the advice and recommendations contained in the Code. They should however note the following points.

When an allegation of professional negligence is made against a practitioner, the court is likely to take account of the contents of any relevant guidance notes in deciding whether or not the practitioner had acted with reasonable competence.

A practitioner conforming to the practices recommended in this Code is unlikely to be adjudged negligent on account of having followed these practices. However, practitioners have the responsibility of deciding when it is appropriate to follow the guidance. If it is followed in an appropriate case, the practitioner will not be exonerated merely because the recommendations were found in a guidance note.

On the other hand, it does not follow that a practitioner will be adjudged negligent if he or she has not followed the practices

recommended in this Code. It is for each individual practitioner to decide on the appropriate procedure to follow in any professional task. However, where practitioners depart from the practice recommended in this Code, they should do so only for good reason. In the event of litigation, the court may require them to explain why they decided not to adopt the recommended practice.

The Code has been prepared to promote best practice in terms of service charges for commercial properties in new leases or renewed leases. Circumstances can arise where the suggested best practice in this Code cannot be applied. This Code therefore should not compel owners, occupiers or managers to an inappropriate course of action. Transparency simply requires that in the event the Code is inappropriate the reasons for this are shared with all relevant parties and a record kept.

In addition, guidance notes are relevant to professional competence in that each practitioner should be up to date and should have informed him or herself of guidance notes within a reasonable time of their promulgation. In the opinion of the approving professional bodies, this Code represents best practice.

# Document status defined

RICS / SCSI produces a range of professional guidance and standards products. These have been defined in the table below. This document is a Code of Practice.

Document status defined		
Type of document	Definition	Status
<b>Standard</b>		
International Standard	An international high level principle based standard developed in collaboration with other relevant bodies	Mandatory
<b>Practice Statement</b>		
RICS / SCSI Practice Statement	Document that provides members with mandatory requirements under the Rules of Conduct for members	Mandatory
RICS / SCSI Guidance Note (GN)	Document that provides users with recommendations for accepted good practice as followed by competent and conscientious practitioners	Recommended good practice
RICS / SCSI Information Paper (IP)	Practice based information that provides users with the latest information and/or research	Information and/or explanatory commentary

# Introduction

This Code of Practice is a best practice document and the industry as a whole is expected to aspire to follow its recommendations.

This document is based on the UK edition and where it varies for the Irish edition, it does so to reflect regulatory or market conditions specific to Ireland.

## The service charge arrangement

Service charges enable an owner to recover the costs of servicing and operating a property from the occupiers, as well as any others who benefit from and 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 his or her 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 these services, for which he or she will receive a fee.

Service charge costs will not generally include the following:

- 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, 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
- 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 are expected to provide the facts and figures to support and vindicate such a decision

- future redevelopment costs
- such costs that are matters between the owner and an individual occupier, for instance,
  - enforcement of covenants and collection of rents
  - costs of letting units
  - consents for assignments
  - subletting
  - alterations
  - rent reviews or
  - additional opening hours, etc.
- any costs arising out of the failure or negligence of the manager or owner.

## New service charge lease provisions

The City of London Law Society ([www.citysolicitors.org.uk](http://www.citysolicitors.org.uk)) and Practical Law Company ([uk.practicallaw.com](http://uk.practicallaw.com)) have both drawn up service charge lease provisions that have been specifically designed to comply with the principles and provisions of this Code. These can be downloaded from their websites. Please note that these provisions relate to UK practice and should be used only with legal advice

## Using this Code

This Code sets down best practice in the management and administration of service charges in commercial property. Section 1 of this document outlines the aims and objectives of this Code, along with stating its core principles. Section 2 then gives recommendations and guidance on how the Code can be followed. The appendices contain additional information and resources to support an understanding of the Code and to assist with its implementation.

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

# Section 1: The Code

## 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.

## 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)

## The service costs

- 1 Best practice recommends that services are procured on an appropriate value-for-money basis, and that competitive quotations are obtained or the costs benchmarked.
- 2 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.
- 3 All costs are to be transparent so that all parties, owners, occupiers and managers, are aware of how the costs are made up. Management fees are to be on a fixed price basis with no hidden markups.

## 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.
- 6 Managers are expected to make available to all occupiers a full apportionment matrix that clearly shows the basis of calculation and the total apportionment per schedule for each unit within the property/complex.

## Certification

- 7 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.

## Communication and consultation

- 8 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 are advised to consult with occupiers with regard to the standard and quality of service charge provision required.
- 9 Managers are expected to 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.
- 10 Managers claiming compliance with the principles of this Code will be transparent in demonstrating how they comply with it.

## Duty of care

- 11 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.
- 12 There will be clear policies as to how the service charge will be managed.

### Financial competence

- 13 In 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.
- 14 When issuing statements of accounts and/or certifying expenditure, managers are urged to 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.
- 15 Service charge monies will be held in one or more discrete bank accounts in recognition of the fact the monies are being held to provide for the procurement and delivery of the services.
- 16 All interest earned on service charge accounts will be credited to the service charge account after appropriate deductions have been made. This applies, for instance, to bank charges, tax, etc.
- 17 The recommended Industry Standard Cost Headings should be used in reporting budget and actual expenditure.

### Occupier responsibilities

- 18 Occupiers are obliged to ensure prompt payment of all 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.
- 19 Occupiers will 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.
- 20 In recognition that value-for-money and maintenance of quality standards will be enhanced through partnership, occupiers are urged to be proactive in assisting owners and managers 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)

- 21 All new leases (including renewals) should make provision for either party to require the resolution of disagreements through the use of alternative dispute resolution (ADR) as a cost effective alternative to court action.
- 22 If the parties cannot agree a mediator or 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

- 23 Communication and consultation between managers and occupiers is to be timely and regular to encourage and promote good working relationships and understanding with regard to the provision, relevance, cost and quality of services.
- 24 Managers will 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, will be issued within four months of the service charge year-end.

### Transparency

- 25 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

- 26 Service quality is to be appropriate to the location, use and character of the property. The manager is urged to 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.

## Limitations of the Code

### Existing lease terms

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

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 ADR clause will enable any difficulties during the term of the lease to be resolved efficiently.

All parties should carefully consider the principles and requirements of this Code prior to entering into a new or renewal lease

### *Proportionality*

The extent to which owners and managers should seek to comply with the recommended best practice processes and procedures set down in this Code 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, which are likely to be consistent with best-value principles.

Nevertheless, owners, managers and occupiers should at all times seek to comply with the core principles set down in this Code.

# Section 2: Recommended best practice to support the core principles of the Code

## 1 Administration

### 1.1 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 the standards of services provided are monitored
- ensuring that the quality and cost of the services provided are regularly reviewed and
- where possible, demonstrating 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 Code, the manager is expected to be able to 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 Code applies to these as well.

### 1.2 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, 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 are advised to 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.

### 1.3 Management charges

#### 1.3.1 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 Code 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 Code.

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.

### 1.3.2 Management fees

The management fees charged should 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 Code. It is recognised that whoever is providing the service is entitled to cover their costs and overheads, including a reasonable profit element.

The manager should ensure that the management fee relates 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 Code requires that fees be set on a fixed-price basis rather than being calculated as a percentage of expenditure. Percentage is no longer appropriate, and is 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 guide 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 Code. 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 must be to achieve best-practice principles for the management and administration of service 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 owners manage 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.

It is advisable for the costs of reports (e.g. fire-risk assessment reports, Disability Discrimination Act (DDA) reports, health and safety reports, etc.) undertaken by specialists working for the same organisation as the manager to be excluded from the management fee, and for any fees for these additional services to be stated clearly and to represent value for money. If other costs of providing the management service are being included as separate items, the management fee is to reflect this separate 'accounting' as part of the management service.

Further detailed information and guidance is available in the RICS information paper, Limiting liability in commercial property management contracts(2009).

### 1.3.3 Duties of the manager

Items 11 and 12 of the core principles outline the duty- of-care responsibilities relating to service charges. 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 will be excluded from the service charge management fee.

### 1.3.4 Site-management costs

Site-management costs are the full employment costs for sufficient staff, as described in 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)
- 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.

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. 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.

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 hours a day, 7 days a week. 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 provided as an alternative to employing additional on-site staff, the reasonable cost of running this service may be recovered from the service charge.

### 1.3.5 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 / off site used in connection with the management of the property.

Notional rents were originally included to provide developers with a return on otherwise unlettable space and to cover the initial provision costs for management accommodation.

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 advisable to charge occupiers notional rent in situations where the premises are incapable of beneficial occupation for any other purpose.

There is also an argument that if notional rents are applied, it may discourage an efficient use of space, or a consideration of alternative uses for areas currently occupied by centre or facilities management.

## 1.4 Contract procurement

### 1.4.1 Service standards and provision

It is advisable to ensure that all contractors and suppliers perform according to written performance standards and statutory regulation. It can prove valuable to regularly measure and review performance against these defined performance standards, as well as to regularly review the appropriateness of the standards used.

### 1.4.2 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. 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 a 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 are to be clearly identified in the 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.

It is generally the responsibility of the manager or the procurement specialist to:

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

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

Further information can be obtained from the RICS information paper, *TUPE: Information for property managers (2013)*.

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

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 to owners. If any fees are received from contractors, managers should clearly state 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 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.

## 1.5 Allocation and apportionment

### 1.5.1 Schedules

Costs are to be apportioned to each occupier in accordance with items 4 and 5 of the core principles.

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 are to 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 subsequently re-examined periodically to see whether there is a need for a new apportionment matrix or new apportionment method to be applied. Where reasonable and appropriate, costs can 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.

### 1.5.2 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.

### 1.5.3 Void and unlet premises

Occupiers are not expected to be liable for the costs attributed to unlet premises; the owner is to meet the cost of these, 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.

### 1.5.4 The apportionment matrix

Managers are to make a full apportionment matrix available to occupiers that clearly shows the basis and method of calculation. 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.

For the avoidance of 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.

### 1.5.5 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.

*RICS Code of Measuring Practice* sets out definitions of the measurement of buildings and their recommended applications, e.g. Gross External Area (GEA), Gross Internal Area (GIA), Net Internal Area (NIA), etc.

Where the service charge is apportioned based on floor area, managers should ensure that the method of measurement used is consistent. Do not mix different measuring methods in the same schedule.

### 1.5.6 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 Code cannot override the contractual terms of any lease, it is nevertheless the view of the steering group that rateable value apportionments should be changed to such other recognised methods of apportionment consistent with the aims and aspirations as set down in this Code.

### 1.5.7 Owner's cost/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 will 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 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.

### 1.5.8 Tenant alterations

Alterations carried out by tenants may have an impact on 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 use 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 this makes specific reference to the basis on which the service charge apportionment is to be calculated, for instance, to 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 Code of Practice.

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

Further information and guidance can be obtained from the RICS information paper *Service charges and tenant alterations* (2009).

## 1.6 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. Occupiers are often 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 similar transparency, accountability, etc. in these services, since the Code is also applicable to these.

### 1.6.1 Insurance

#### 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.

#### 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 and managers are required at all times to disclose any commission(s) they are receiving.

#### 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.

Policies are expected to include an ability to note the interest of occupiers, 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.

Further information and guidance can be obtained from the RICS guidance note *Insurance for commercial property managers* (2010).

### 1.6.2 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 submetering 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, which ought to allow additionally for the payment of a reasonable administrative charge. The recovery should state unit costs and administration charges and include copies of the original invoice in order to comply with the requirements for transparency set out in the Code.

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 as an acceptable cost under the service charge. Otherwise, such costs would usually comprise 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. In certain circumstances payments in advance may be appropriate.

It is now also 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.

## 2 Communication and consultation

### 2.1 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 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 are to provide occupiers with a copy of the management policy, which should contain standard information about how the property is managed and the aims of the management team (e.g. the manager and the on-site team). Managers should also inform occupiers of any future plans for the property, particularly if these are likely to have an impact on the service charge.

### 2.2 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 incur expenditure that might have a detrimental effect on the owner's investment, 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.

### 2.3 Budgeting and cost review

It is the manager's duty to keep expenditure under constant review in order to identify any unforeseen variances and to notify occupiers accordingly. When significant variances in actual costs against budget are likely, it is good 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.

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.

Whether a variance against forecast is to be regarded as significant or material will often be a subjective assessment, depending on 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.

## 3 Dealing with existing and new leases

### 3.1 Existing leases

The basis by which service charges are operated and managed is set down in the contract between the owner and occupier, otherwise known as 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 Code. Where this is the case, this Code 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, seek specialist professional advice.

### 3.2 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 Code 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 Code, 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 Society of Chartered Surveyors Ireland (SCSI) and Dublin Chamber of Commerce *SME Guide to Property*.

This *SME Guide to Property* provides a comprehensive resource for SMEs 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. Therefore, interim arrangements may 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.

### 3.3 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.

This is not usually a problem for short leases however, as in these cases it is far easier to accurately predict the services that are to be provided. Unless a lease incorporates very clear wording to the contrary, if the owner had in mind the provision of a service, but has not covered the right to include the cost of providing it in the service charge, he or she will not generally be able to use the sweeper clause as authority to recover the cost.

The intention of a sweeper clause 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.

# 4 Financial controls and competencies

## 4.1 Accounting principles

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

- whether the statements are prepared on an accruals or cash basis
- 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 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.

## 4.2 Audit and certification of service charges

### 4.2.1 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 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 ensure that annual statements of service charge expenditure are issued strictly in accordance with the procedures and requirements as set down under the terms of the lease.**

There is currently widespread 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 little understanding 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.

### 4.2.2 Service charge certification

The purpose of certification of the service charge accounts is to provide occupiers with the comfort and certainty that:

- the accounts produced represent a true and accurate record of the expenditure incurred by the owner in supplying the services to the building and
- the expenditure the owner is seeking to recover is in accordance with the terms of the leases and, where practicable, the provisions of this Code.

Annual statements of service charge expenditure should be certified by the manager as complying with the statements above. In certifying the statement the manager 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. In certifying the service charge, the certifier has 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.

In the interest of 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 are advised to have clear internal procedures in place that control who may sign in the name of the firm, and to ensure this is an appropriately senior individual.

Where the manager undertakes the certification or where the lease requires certification by someone other than the manager, the costs of certification of the service charge, together with the fees of an accountant, will be recovered through the service charge.

#### 4.2.3 Auditing of the service charge accounts

- 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 (IASs) (UK and Ireland), and should be performed by a registered auditor.

In carrying out an audit in accordance with accepted auditing standards, it is the auditor who 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 his or her 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 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.

#### 4.2.4 Independent accountants' 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 and
- checking, based on a sample, whether entries in the accounting records were supported by receipts or other documentation, or the evidence was inspected.

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 independent accountants' report, the manager should agree and the costs thereof should be charged to the occupier.

#### 4.2.5 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 by the owner 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. However, to be consistent with best value principles this requirement should be considered as optional for smaller properties and dependent upon 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 accountants' report should be prepared.
- For mixed used multi-unit developments, the provisions of the Multi-Unit Development Act, 2011, ("the Act") should also be considered. In general terms the Act provides that in respect of such mixed use developments there must be a fair and equitable apportionment of the costs and expenses attributable to the different classes of units within the development.
- The Property Services Regulatory Authority, was established by the Minister for Justice and Equality under the Property Services (Regulation) Act 2011, on a statutory basis on 3 April 2012.

The main function of the Authority is to control and regulate Property Services Providers (i.e. Auctioneers/Estate Agents, Letting Agents and management Agents)

The authority 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, the establishment and maintenance of a compensation fund.

Full details of the Authority are available at [www.psr.ie](http://www.psr.ie)

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.

### 4.3 Industry standard cost classifications

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

The industry standard cost classifications provides three levels of analysis:

- cost class
- cost category and
- cost description.

As a minimum acceptable level of reporting, service charge budgets and statements of actual expenditure are to be prepared at cost class and cost category level.

Adoption of the industry standard cost classifications will reap enormous benefits for the industry as a whole, 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 Code, 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.

#### 4.4 Budgets and actual expenditure accounting

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

Core principle 24 requires managers to issue budgets of anticipated service charge expenditure to occupiers, including an explanatory commentary at least one month prior to the commencement of the service-charge year. Budgets should also include a clear explanation of the calculation of the occupier's proportion of the total costs.

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 budgets
- explanations of significant individual costs and of variances from the previous year's budget/ accounts
- a comparison against the previous two years' actual costs, where appropriate
- 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
- the relevant section from the full apportionment matrix that clearly shows the basis of calculation and the total apportionment per schedule for each unit within the property/ complex
- the date of issue

A set of industry standard cost classifications has been drawn up, and is included in appendix B (see also 4.3). It is essential that these be used at cost-class and cost-category level.

#### 4.5 Right to challenge

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

Where the manager has demonstrably complied with the provisions of the lease and this Code of Practice, it is recommended that the manager allow occupiers a reasonable period (e.g. four months from issue) in which to raise enquiries or request further information in respect of the certified accounts. 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 for 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 Code. In the interest of promoting a swift and harmonious resolution of service charge queries, there should be openness and transparency.

## 4.6 Change of owner or manager

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

It is recommended that 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 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 current manager was not responsible for previous years.

Further information on the recommended processes and procedures in the event of a property's sale, or other circumstances where the manager changes, is included in the RICS information paper *Commercial property service charge handover procedures* (2011).

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

## 4.7 On-account payments

Service charges are usually 'reserved as rent' in the lease. However, in reality, the service charge is neutral in income and expenditure terms, after year-end balancing charges/credits. Service charge monies will be held in discrete bank accounts in recognition of the fact that the monies are being held to deliver the service expenditure.

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

## 4.8 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 from void units, and to make these payments to the account as promptly as payments made by occupiers.

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

## 4.9 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 on borrowed money to fund major non-cyclical or exceptional unbudgeted expenditure meets best practice requirements (see also section 7 Provision for anticipated future expenditure).

## 4.10 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 apportionment, to enable occupiers to reasonably understand how their liability has been calculated.

Budgets will be issued at least one month prior to commencement, and 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 is encouraged to deal with such proper enquiries promptly and efficiently.

### 4.11 Benchmarking and cost analysis

Adoption of the standard industry cost classifications (see 4.3 and appendix B) is considered essential 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 facilitates 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). Each property will have its own variations from the average, therefore 'beating the benchmark' is not necessarily proof of service efficiency and 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.

### 4.12 Value for money

In providing the services, the owner/manager is recommended at all times to endeavour to achieve value for money and effective 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 benchmark the service standards and pricing to confirm that value for money is still being achieved.

It is advisable for managers to require major service providers to demonstrate that their services, methods and processes are continually reviewed to ensure value and efficiency.

## 5 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 (see paragraph 4.5).

It is usually beneficial to both owners and occupiers to resolve service charge disputes quickly, as going to court can be slow and expensive. Many occupiers can become dissatisfied and, believing that disputing a service charge in the courts is not cost-effective, will simply resort to withholding payment instead. Occupiers are advised not to arbitrarily withhold payment of any sums that are properly demanded, rather, where circumstances dictate, any payment 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 (see paragraph 5.1).

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 under or overpaid. In mediation, the parties will agree what they want to achieve, and an independent expert will then determine what the lease says.

### 5.1 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 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 charges. The options are varied and include:

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

### 5.2 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.

## 5.3 Mediation

### The role of the mediator

The generally accepted description of 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. That 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 or 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. He/she 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
- Help parties move toward a realistic, negotiated settlement, in a cost-effective manner

### 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 much, 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.

The advantages of mediation can be outlined as follows:

- Mediation is non-binding until the parties sign a settlement agreement (at which point 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, 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.
- 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 in 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.

## 5.4 Independent expert determination

### The role of an independent expert

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 the 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. He/she may choose, or be so required by contract, to receive, and 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 his/her determination upon his/her own knowledge and his investigations to discover the facts and all other information, including principles of law, relevant to his/her valuation or other issues in dispute;
- Settle his/her own contractual terms with the parties, e.g. as to remuneration, extent of inspection, assumptions; and
- Carry out the whole of the determination by him/herself

### 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 his/her 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 of valuation 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.

## 5.5 Arbitration

### The role of an arbitrator

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.

### 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.

### 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)

## 6 Mixed-use schemes

Recently, there has been a huge 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.

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 used multi-unit developments, the provisions of the Multi-Unit Development Act, 2011, (“the Act”) should also be considered. In general terms the 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.

The Act applies to mixed used multi-unit developments, which is a multi-unit development of which a commercial unit forms part (excluding a childcare facility). For the purposes of the Act, a development will be a multi-unit development where there are not less than five residential units sharing common services, amenities and facilities.

Further detailed information and guidance is available in the *SCSI Code of Practice in relation to property management in multi-unit developments*.

This Code of Practice provides a common platform over and above the statutory requirements currently in place under the *Property Service Regulatory Authority legislation and Multi-Unit Developments Act 2011*.

Whilst not entirely mandatory in its implementation, we believe that this Code 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 Code of Practice 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.

## 7 Provision for anticipated future expenditure

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. It is therefore recommended that proper planned preventative maintenance (PPM) plans are used.

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.

The move towards shorter leases may create 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.

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.

To the extent that these items can be foreseen, it is recommended that the cost of major extraordinary expenditure items to be spread over a number of years (and over a number or 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.

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.

### Sinking fund

A fund formed by periodically setting aside money for the replacement of a wasting asset (for example, major items of plant and equipment, such as heating and air-conditioning plant, lifts, etc.). It is usually intended that a sinking fund will be set up and collected over the whole life of the wasting asset.

### Reserve fund

A fund formed to meet the anticipated future costs of maintenance and upkeep in order to avoid fluctuations, or an anticipated large, one-off increase in the amount of service charge payable in a single year (for example, regularly recurring items such as external cleaning and redecorations).

### Depreciation charge

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 usually be included in the service charge to reflect the 'cost' to the owner of the annual depreciation of plant and equipment, which would be based on the initial cost of an installation rather than on the future cost of replacement.

Where provision is to be made for significant future expenditure such sums should not be included as accruals but should be considered as contributions towards reserve or sinking funds as above and reported accordingly. In managing sinking and reserve funds or depreciation charges, the following is to be considered as best practice.

### Sinking, replacement and reserve funds

- Monies accumulated in a sinking or reserve fund are to be held in one or more separate discrete bank accounts to be maintained in trust for the occupiers.
- The owner or managing agent is expected to act reasonably in estimating the amount of the sinking or reserve fund contributions to be included within the service charge, which will relate to specifically identified expenditure only (for example, repairs or replacement of the roof, boiler plant, lift, etc.) rather than other unidentified future expenditure.
- 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).
- The owner will make all payments into the sinking or reserve fund account for void premises.
- 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.

- On completion of the sale of a property, the vendor will 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.

#### Depreciation charges

- 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.
- A proper and reasonable depreciation charge is to be considered as an annual cost to the owner rather than the initial cost of installation.
- 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.

Further detailed information and guidance is available in the RICS information paper Sinking funds, reserve funds and depreciation charges (2014). Please note that this refers to UK practice but would be a useful guideline provided the reader interprets it with local practice

# 8 Initial provision, replacement and improvement of fabric, plant and equipment

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 (also see below) 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 over the term of the occupiers' leases. Managers should provide the facts and figures to support and justify such a proposal.

Recent UK 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. Current decisions do not give occupiers authority to sustain a proposition that, as a general rule, they cannot be required to pay a higher service charge for works carried out towards the end of the term of their lease. 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.

## 8.1 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.

## 8.2 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.

## 8.3 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.

## 8.4 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 (see also section 9 Environmental sustainability).

## 8.5 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.

## 8.6 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 is also 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.

## 9 Environmental sustainability

### 9.1 Green leases

The sustainability debate has been very much focused on how to develop more sustainable buildings, but it has ignored two key issues: what to do with existing buildings and the role of the occupier in reducing emissions. The recent emergence of green leases in the UK may be one way of addressing these issues. Green leases are standard commercial property leases pertaining to cooperation between landlord and tenants, with the aim of reducing waste production and energy and water consumption.

Owners and occupiers are advised to be aware of the environmental impact of their respective operations. This Code supports and promotes a cooperative and collaborative approach in recognising and managing the environmental impact of the occupation and management of commercial premises.

Leases are binding documents that are not easy to amend. There may be value in owners and occupiers entering 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. This 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 Buildings Partnership's 'Green Building Management Toolkit', which is available at: [www.betterbuildingspartnership.co.uk/download](http://www.betterbuildingspartnership.co.uk/download)

### 9.2 Improving environmental performance

The sharing of data and other related information is essential. It is advisable for owners, managers and occupiers to cooperate on the running of any building management systems and on a range of 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 Code, 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).

### 9.3 Building Energy Rating Certificate (BER)

For the avoidance of doubt, the cost of obtaining an Building Energy Rating Certificate (BER) would not normally be considered to be a recoverable service charge cost. An 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.

However, costs that might subsequently be incurred while improving energy efficiency identified when obtaining an BER might fall to the service charge, subject to the terms of the lease and the principles set out in this Code (see 8.4 and 9.2 above).

Please refer to the Sustainable Energy Authority of Ireland for further information/guidance [www.seai.ie](http://www.seai.ie).

# 10 Additional best practice guidance for shopping centres

## 10.1 Marketing and promotions

The marketing of and promotional activity supporting a retail shopping centre scheme are recognised as being of joint benefit to all stakeholders, and should therefore be jointly funded. This joint funding should cover not just the actual marketing and promotions, but also the costs of providing specialist staff (and accommodation etc.) whether directly or via an agency arrangement.

The service charge budget and accounts should be transparent and should include the gross marketing and promotional expenditure and the contribution 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 occupiers'/retailers' 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 should be made available to occupiers.

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 the marketing of centres.

Any costs incurred in relation to the initial promotional launch of a scheme are to be borne by the owner, and are not to be considered as recoverable service charge costs. It is recommended that any plan to relaunch / rebrand a centre be discussed between manager and occupiers so that they can agree to an appropriate split of the expenditure to each party. The costs of entertainments, attractions, Christmas, and other seasonal decorations and events within the shopping centre are not usually considered to be a marketing and promotional cost, but are to be regarded as amenities or facilities. Where such costs are included within the service charge, they would not be jointly funded as above.

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

## 10.2 Commercialisation (non-core income)

Increasingly, owners are finding additional non-core income streams from their investments. It is clear that they are entitled to receive this income from the investment they have made. However, if the service charge has provided the initial capital for the income stream, the income or a proportion thereof to cover the cost 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., while shopping centres and malls also receive income from promotional space (e.g. advertising on displays and drums and in car parks, etc.) and licences granted for other mall activities (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 in the centre/malls 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, photocopying 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-part areas, and the space is used on a permanent or semi-permanent basis, for example, barrows or kiosks within shopping malls, 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. Owners are to estimate and declare a contribution to the service charge to reflect the benefit and use of the common services enjoyed.

Managers are to clearly state their policy on how costs and income generated from services and activities are allocated. The simple 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 set out in paragraph 4.4, 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.

### 10.3 Apportionment of service charges in shopping centres: 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.

Therefore, 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 ten 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 ancillary basement and upper-floor accommodation, or of remote storage, might be discounted to reflect the reduced benefit derived from certain services as distinct from the 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.

# Appendices

- Appendix A: Best-practice compliance checklist
- Appendix B: Standard industry cost classifications
- Appendix C: Service charge accounting sample report
- Appendix D: Glossary and terminology
- Appendix E: Revenue Commissioners form on VAT Concessions
- Appendix F: Further reading

# Appendix A: Best-practice compliance checklist

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

Core principle	Evidence	Comply
<p><b>Value for money</b></p> <p>Procure an appropriate level of service for the occupiers in the building.</p> <p>Demonstrate that services offer good value for money.</p>	<p>Competitive tender</p> <p>Other market testing</p> <p>Cost benchmarking</p>	
<p><b>Transparency</b></p> <p>All costs, apportionments and policies are explicit and open to any scrutiny by occupiers or their agents.</p>	<p>All apportionment schedules are published</p> <p>All policies are outlined in budget packs</p> <p>Detailed explanations are provided in year-end statements where the costs have materially varied from the budget</p> <p>The landlord bears the cost of all voids and concessions</p>	
<p><b>Timeliness of reporting</b></p> <p>All reports are issued within timeframes required by the Code.</p>	<p>Budgets are issued at least one month prior to the start of the service charge year</p> <p>Year-end statements of actual expenditure are issued within four months of the end of the service charge year</p>	
<p><b>Management fee</b></p> <p>The management fee reflects a reasonable cost to undertake necessary work to manage and operate the services and to administer the service charge.</p>	<p>Fixed fee (not per cent of service charge)</p> <p>Meets Code guidelines on what can and cannot be charged for management</p>	
<p><b>Duty of care to occupiers – consultation and approval</b></p> <p>All costs are recoverable in accordance with leases.</p> <p>The occupiers are consulted where appropriate for their agreement to the levels of service and services to be offered.</p>	<p>All occupiers are given the opportunity to comment on the budget</p> <p>The occupiers are consulted on the levels of service and/or the introduction of new services</p>	
<p><b>Standardised financial reporting</b></p> <p>Budgets and statements of actual expenditure are reported in line with the Code's cost categories.</p> <p>Where appropriate, separate schedules are prepared to allocate costs to reflect the availability, benefit and use of different services.</p>	<p>Standardised cost categories are used</p> <p>Separate schedules are included as appropriate</p>	
<p><b>Interest income and expenses</b></p> <p>Separate interest-bearing accounts are operated for each building, with all interest income and expenses credited or charged within the service charge.</p>	<p>Bank statement of interest income and expenses</p>	
<p><b>Support for alternate dispute resolution (ADR)</b></p> <p>ADR is supported and recommended as the basis to resolve service charge disputes.</p>	<p>Standard lease terms</p> <p>All policies are outlined in budget packs</p>	

# Appendix B: Standard industry cost classifications

The cost descriptions are not intended to represent an exhaustive list, but are used for illustrative purposes only. The narrative is therefore intended to provide guidance for coding only. To facilitate greater transparency and clarity these should not be used as a substitute for a proper and appropriately detailed explanation of the actual expenditure incurred (or proposed).

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, it is suggested that the cost class and cost category structure is not altered.

COST CLASS		Notes
Cost category		
Cost description		
<b>MANAGEMENT</b>		
<b>1 Management fees</b>		
	Management fees	Owner or managing agent fees for managing and administering building services excluding rent collection, asset management etc.
<b>2 Accounting fees</b>		
	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 formal audit of the service charge
<b>3 Site management resources</b>		
	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 site management accommodation
	Office costs (telephones/stationery) Petty cash	Costs of equipping and running site management office Miscellaneous minor expenditure incurred in relation to site management duties
	Help desk/call centre/information centre	Operational costs for providing helpdesk/call centre/information centre facilities
<b>4 Health, safety and environmental management</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

UTILITIES	
<b>5 Electricity</b>	
Electricity	Electricity supply to common parts and retained areas and central plant, excluding occupier direct consumption
Electricity procurement/consultancy	Consultancy and procurement fees for negotiating electricity supply contract and auditing of energy consumption
Fuel (standby electrical power)	Fuel oil to run any standby electrical power systems
<b>6 Gas</b>	
Gas	Gas supply to owner's central plant, excluding occupier direct consumption
Gas procurement/consultancy	Consultancy and procurement fees for negotiating gas supply contract and auditing of energy consumption
<b>7 Fuel oil</b>	
Fuel Oil	Fuel oil supply to owner's central plant, emergency generators etc excluding occupier direct consumption
Fuel oil procurement/consultancy	Consultancy and procurement fees for negotiating oil supply contract and auditing of energy consumption
<b>8 Water</b>	
Water and sewerage charges	Water supply to central plant, common parts and retained areas excluding occupier direct consumption
Water consultancy	Consultancy fees incurred in reviewing water usage
SOFT SERVICES	
<b>9 Security</b>	
Security guarding	Direct employment or contract costs incurred in providing building security guarding
Security systems	Servicing and maintenance of building security systems (e.g. CCTV, access control, intruder alarm)
<b>10 Cleaning and environmental</b>	
Internal cleaning	Cleaning of internal common parts and retained areas
External cleaning	Cleaning of external common parts and retained areas
Window cleaning	
Hygiene services/toiletries	Cleaning and servicing of common parts' toilet 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
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
Snow clearance/gritting	Costs incurred in snow clearance and supply of snow clearing equipment and gritting salt
Seasonal decorations	Provision and maintenance of seasonal decorations to common part areas

<b>11 Marketing and promotions</b>	
Events	Promotional events
Marketing	Marketing and advertising in accordance with marketing strategy
Research	Research into local market conditions, customer surveys, etc.
Staff costs	Direct employment or contract costs for provision of marketing and promotional activity
Landlord's contribution to marketing	Financial contributions made by landlord towards marketing and promotions
Local authority contribution to marketing	Financial contributions made by local authority towards marketing and promotions
<b>HARD SERVICES</b>	
<b>12 Mechanical and electrical services (M&amp;E)</b>	
M&E maintenance contract	Planned maintenance to the owner's M&E services, including contractor's H&S compliance
M&E repairs	Repair works to the owner's M&E services
M&E inspections and consultancy	Auditing quality of maintenance works, condition of
M&E plant and H&S compliance	Planned maintenance works to the owner's fire protection, emergency lighting and other specialist life safety systems, including contractor's H&S compliance
Life safety systems maintenance	
Life safety systems repairs	Repair works to the owner's fire protection, emergency lighting and other specialist life safety systems
Life safety systems inspections and consultancy	Auditing quality of maintenance works, condition of life safety systems
<b>13 Lifts and escalators</b>	
Lift maintenance contract	Planned maintenance works to lifts in the common part and retained areas, including contractor's H&S compliance
Lift repairs	Repair works to common parts' lifts
Lift inspections and consultancy	Auditing quality of maintenance works, condition of lift plant and H&S compliance
Escalator maintenance contract	Planned maintenance works to escalators in the common part and retained areas, including contractor's H&S compliance
Escalator repairs	Repair works to common parts escalators
Escalator inspections and consultancy	Auditing quality of maintenance works, condition of escalator plant and H&S compliance
<b>14 Suspended access equipment</b>	
	Suspended access equipment includes all forms of high-level access equipment maintenance, i.e. hatchways, eye-bolt, fall address and cradles
Suspended access maintenance contract	Planned maintenance works to the owner's suspended access equipment, including contractor's H&S compliance
Suspended access repairs	Repair works to the owner's suspended access equipment
Suspended access inspections and consultancy	Auditing quality of maintenance works, condition of suspended access equipment and H&S compliance

<b>15 Fabric repairs and maintenance</b>	
Internal repairs and maintenance	Repair and maintenance of internal building fabric, common part and retained areas
External repairs and maintenance	Repair and maintenance of external building fabric, structure, external common part and retained areas
Redecorations	Redecoration and decorative repairs
<b>INCOME</b>	
Distinct activities that yield a true income to the service charge account	
<b>16 Interest</b>	
Interest	Interest received on service charge monies held within owner's or agent's bank account
<b>17 Income from commercialisation</b>	
Car park income	Income yielded from any facilities installed and/or maintained at the occupier's expense
Vending machine income	
Other	
<b>Operational expenses</b>	
Contract charges	Overheads, expenses and operational costs incurred in providing any of the commercialisation facilities
Repairs and maintenance	
Staff costs	
<b>INSURANCE</b>	
<b>18 Engineering Insurance</b>	
Engineering insurance	Landlord's engineering insurances
Engineering inspections	
<b>19 All risks insurance cover</b>	
Building insurance Loss of rent insurance	Landlord's all risk insurance costs
Public and property owner's liability	
Landlord's contents insurance	
<b>20 Terrorism insurance</b>	
Terrorism insurance	Landlord's terrorism insurance cover
<b>EXCEPTIONAL EXPENDITURE</b>	
<b>21 Major works</b>	
Project works	Exceptional and one-off project works, over and above routine operational costs
Plant replacement	
Major repairs	
<b>22 Forward funding</b>	
Sinking funds	Forward funding of specific major replacement projects (e.g. plant and equipment replacements, roof replacements)
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 of major plant and equipment

## Appendix C: Service charge accounting sample report

It is not for the Code to prescribe the operating business model for 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 certain key elements as set out.

Copyright in the Service charge accounting sample report (pp. 43-62), which forms appendix C of this Code of Practice, belongs to the Royal Institution of Chartered Surveyors (RICS).

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# Introduction

In managing the provision of services and 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.

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

*The SCSI Code of Practice Service Charges in Commercial Property* ('the Code') 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 that is being recovered is in accordance with the terms of the occupational leases.

The Code 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) is to issue a technical release to provide guidance on accounting for commercial service charges. This technical release, which will be reviewed by SCSI when published, will provide good practice guidance on technical and practice issues relevant to the work of accountants and other professionals.

This sample report, prepared in consultation with the ICAEW 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 for subsequent communication to tenants as to the nature, type and cost of services provided.

It is not for this Code 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 key elements:

- Service charge certificate (paragraph 3)
- The independent accountant's report
- Service charge expenditure report (paragraph 4 and annexes A and B)
- Notes to the expenditure report (paragraph 5)

- Service charge allocation and apportionment (paragraph 6 and annex D)
- Operational review and variance report (paragraph 7 and annex C).

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 down in the Code as to the nature, type and cost of services provided but would usually be outside of the scope of the independent accountant's review. The basis of apportionment of the service charge would also 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 €**

# 1 Introduction

This report has been produced by [manager's name] on behalf of [owner's name], the landlord 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].

## 2 The management team

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

# 3 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 report and accompanying information on pages [X] to [Y] records the true 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 terms of the lease and, where practicable, the SCSl Code of Practice Service Charges in Commercial Property (current edition).

Signed .....

[Name and qualifications] .....

Position .....

## 4 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 the SCSl Code of Practice Service Charges in Commercial Property. Examples of the summary and detailed expenditure reports are included in this sample report as annex A and annex B respectively.

# 5 Notes to the expenditure report

## 5.1. Accounting principles

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

This section may also be used to provide further details in respect of other accounting principles adopted in preparing the expenditure report. For example, details of landlord contribution to the service charge or information regarding forward funding by the landlord.

## 5.2. VAT

### Example wording

The landlord has elected to avail of the Revenue Commissioners VAT concession on goods and services supplied to property lessees through landlords (See Annex E) . Therefore all service charge expenditure is shown inclusive of VAT. VAT will be charged following completion of the annual audit at the appropriate rate on all service charge payments demanded/invoiced by the landlord.

### Or

Aln line with Revenue Guidelines vat will be charged at each service charge invoice at the marginal rate of vat (currently 23%) .

## 5.3. Sinking fund/reserve fund

This section is to include a description of the intended purpose of any sinking/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 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. For further information refer to the RICS information paper *Sinking funds, reserve funds and depreciation charges* (2014).

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

## 5.4. Banking

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

## 5.5. Accruals

These are expenses for goods and services actually 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.

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 reported accordingly (see above).

### 5.6. Prepayments and security deposits

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

### 5.7 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	x,xxx
Contribution from the landlord	<u>x,xxx</u>
Net marketing/promotion expenditure	x,xxx

### 5.8 Commercialisation

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

### 5.9 Total cost of management

#### 5.9.1 Management fees

The manager should provide details of the basis of his or her appointment and should confirm the basis of the fee, for example, a fixed fee of €x 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. This code clearly states that asset management and rent collection costs are excluded from the service charge management fee.

If in addition to the management fee a charge is made relating to the cost of providing a help desk, the rationale should be explained and the costs detailed separately.

#### 5.9.2 On-site management

The manager should provide details of all on-site management staff and the total employment costs, which would usually include PRSI, pension contributions and other direct employment costs. A separate breakdown of any other costs incurred in employing on-site staff, such as the provision of 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 the cost category in which it is included.

Where separate specialist consultancy fees are incurred, for instance in relation to the carrying out of health and safety risk assessments, these costs should be shown separately.

# 6 Service charge allocation and apportionment

## 6.1 Empty units and concessions granted to tenants

Managers should confirm the basis on which costs are apportioned for periods less than the full service charge year, for example, on a daily basis.

For the avoidance of doubt, managers should also confirm 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.

## 6.2 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, for example:]**

Schedule 1 Estate

Schedule 2 Building 1

Schedule 3 Building 2

[Note to managers – add additional schedules as necessary in order 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.]

## 6.3 Service charge apportionment

Managers are to make a full apportionment matrix available to occupiers that clearly shows the basis and method of calculation. 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. Managers should also be transparent with regard to the treatment of void and unlet premises, any special concessions given to individual occupiers and the cost attributable to the owner's own use of the property (see empty units and concessions granted to tenants above).

See annex D for an example apportionment schedule.

## 7 Operational review

This section should comprise a comparison between the budget 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.

### 7.1 Service procurement

#### 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.

### 7.2 Contracts

A schedule of contracts in force during the service charge period should be made available upon request with details for each contract 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 in any event, 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 brief summary of when the service line contract was last retendered.

### 7.3 Explanatory notes and variances

#### Note to managers

Include summary information under each standard industry cost classification 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 must use the standard industry cost classifications. As a minimum acceptable level of reporting, all reports must be detailed at cost class and cost category level as set out in appendix B of this code

However, to achieve transparency in accordance with the principles of the Code 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 Code'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.

## 8 General notes

[Insert any other relevant information.]

# Annexes

Annex A: Example service charge summary expenditure report

Annex B: Example service charge detailed expenditure report

Annex C: Example service charge variance report

Annex D: Example service charge apportionment schedule

# Annex A: Example service charge summary expenditure report

## SUMMARY 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>				
1 Management fees	€60,000	€10,000	€25,000	€25,000
2 Accounting fees	€1,600	€1,600		
3 Site management resources	€71,135	€21,135	€26,600	€23,400
4 Health, safety and environmental	€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>				
5 Electricity	€229,900	€5,900	€112,000	€112,000
6 Gas	€11,050	€1,050	€5,000	€5,000
7 Fuel oil (heating)	€0			
8 Water	€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>				
9 Security	€144,100	€137,500	€3,500	€3,100
10 Cleaning and environmental	€185,730	€52,250	€58,300	€75,180
11 Marketing and promotions				
<b>Subtotal</b>	<b>€329,830</b>	<b>€189,750</b>	<b>€61,800</b>	<b>€78,280</b>
<b>HARD SERVICES</b>				
12 Mechanical and electrical services	€187,970	€32,750	€74,750	€80,470
13 Lift and escalators	€24,500		€14,000	€10,500
14 Suspended access equipment	€5,300		€2,800	€2,500
15 Fabric repairs and maintenance	€99,325	€36,850	€40,700	€21,775
<b>Subtotal</b>	<b>€317,095</b>	<b>€69,600</b>	<b>€132,250</b>	<b>€115,245</b>
<b>INCOME</b>				
16 Interest	-€1,068	-€332	-€373	-€363
17 Income from commercialisation				
<b>Subtotal</b>	<b>-€1,068</b>	<b>-€332</b>	<b>-€373</b>	<b>-€363</b>
<b>INSURANCE</b>				
18 Engineering insurance	€900		€500	€400
19 All risks insurance cover				
20 Terrorism insurance				
<b>Subtotal</b>	<b>€900</b>	<b>€0</b>	<b>€500</b>	<b>€400</b>
<b>EXCEPTIONAL EXPENDITURE</b>				
21 Major works	€92,483		€92,483	
22 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>

# Annex B: Example service charge detailed expenditure report

## 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>1 Management fees</b>				
Management fees	€60,000	€10,000	€25,000	€25,000
<b>2 Accounting fees</b>				
S/C audit fees	€1,600	€1,600		
<b>3 Site management resources</b>				
Staff costs	€15,000	€15,000		
Receptionists/concierge	€50,000		€26,600	€23,400
Site accommodation (rent/rates) (telephones/stationery)	€4,335 €1,800	€4,335 €1,800		
<b>4 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>5 Electricity</b>				
Electricity	€224,000		€112,000	€112,000
Electricity procurement consultancy	€5,600	€5,600		
Fuel (standby electrical power)	€300	€300		
<b>6 Gas</b>				
Gas	€10,000		€5,000	€5,000
Gas procurement/consultancy	€1,050	€1,050		
<b>7 Fuel oil (heating)</b>				
<b>8 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>9 Security</b>				
Security guarding	€132,000	€132,000		
Security systems	€12,100	€5,500	€3,500	€3,100
<b>10 Cleaning and environmental</b>				
Internal cleaning	€91,200		€38,400	€52,800
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>11</b>	<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>12</b>	<b>Mechanical and electrical services (M&amp;E)</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>13</b>	<b>Lift and escalators</b>				
	Lift maintenance contract	€21,000		€12,000	€9,000
	Lift repairs	€3,500		€2,000	€1,500
<b>14</b>	<b>Suspended access equipment</b>				
	Maintenance contract	€5,100		€2,700	€2,400
	Repairs	€200		€100	€100
<b>15</b>	<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>16</b>	<b>Interest</b>				
	Interest	-€1,068	-€332	-€373	-€363
<b>17</b>	<b>Income from commercialisation</b>				
	<b>Subtotal</b>	<b>-€1,068</b>	<b>-€332</b>	<b>-€373</b>	<b>-€363</b>
<b>INSURANCE</b>					
<b>18</b>	<b>Engineering insurance</b>				
	Engineering insurance	€900		€500	€400
<b>19</b>	<b>All risks insurance cover</b>				
<b>20</b>	<b>Terrorism insurance</b>				
	<b>Subtotal</b>	<b>€900</b>		<b>€500</b>	<b>€400</b>
<b>EXCEPTIONAL EXPENDITURE</b>					
<b>21</b>	<b>Major works</b>				
	Plant replacement	€92,483		€92,483	
<b>22</b>	<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>

# Annex C: Example service charge variance report

## EXPENDITURE VARIANCE REPORT

Period [dd/mm/yyyy] to [dd/mm/yyyy]

Property address .....

		Previous year actual	Current year budget	Current year actual	Actual v budget	Current v previous actual
<b>MANAGEMENT</b>						
1	Management fees	€60,000	€60,000	€60,000	0.00%	0.00%
2	Accounting fees	€1,500	€1,600	€1,600	0.00%	6.67%
3	Site management resources	€66,000	€70,000	€71,135	1.62%	7.78%
4	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>						
5	Electricity	€218,700	€236,000	€229,900	-2.58%	5.12%
6	Gas	€9,700	€12,500	€11,050	-11.60%	13.92%
7	Fuel oil (heating)					
8	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>						
9	Security	€144,100	€144,100	€144,100	0.00%	0.00%
10	Cleaning and environmental	€176,543	€180,000	€185,730	3.18%	5.20%
11	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>						
12	Mechanical and electrical services	€193,750	€180,000	€187,970	4.43%	-2.98%
13	Lift and escalators	€24,500	€24,500	€24,500	0.00%	0.00%
14	Suspended access equipment	€5,300	€53,000	€5,300	-90.00%	0.00%
15	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>

## Annex C: Example service charge variance report (continued)

<b>INCOME</b>						
16	Interest	-€989	-€1,000	-€1,068	6.80%	7.99%
17	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>						
18	Engineering insurance	€800	€1,000	€900	-10.00%	12.50%
19	All risks insurance cover					
20	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>						
21	Major works		€90,000	€92,483	2.76%	
22	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>

# Annex D: Example service charge apportionment schedule

## APPORTIONMENT SCHEDULE

Period [dd/mm/yyyy] to [dd/mm/yyyy]

Property address .....

Unit/address (SqM)	Tenants	Area	Schedule 1 Estate	Schedule 2 Building 1	Schedule 3 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 1st 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>		

# Appendix D: Glossary and terminology

<b>Accrual accounting</b>	This is 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>	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>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>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>	Arbitration is 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 his/her own right.
<b>Balancing 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>Commercial property</b>	All property that is not residential or agricultural and includes retail, office, industrial and leisure properties.
<b>Depreciation charges</b>	The 'cost' to the owner representing the measure of the wearing out, consumption or other reduction in life of an asset.
<b>Direct recoveries</b>	Any expenditure that is charged directly to individual occupiers and not funded via the on-account service charges
<b>SCSI Dispute Resolution Service (DRS)</b>	SCSI DRS can provide a simple, fast and cost-effective approach to resolving disputes in the complicated world of property and construction, where disputes are bound to arise.
<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>Gross internal area (GIA)</b>	The area of a building measured to the internal face of the perimeter walls at each floor level in accordance with the <i>SCSI Code of Measuring Practice</i> .
<b>Independent expert determination</b>	Independent expert determination is a process in which 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>International total occupancy cost code (ITOCC)</b>	ITOCC from the Investment Property Databank (IPD) Occupiers Property Databank (OPD) was designed to be the standard form of measuring property and facilities costs for all businesses and public sector organisations. It is prepared with the help of IPD occupier and other leading occupiers, consultants, accountants, service providers, developers and academics. As ‘total’ suggests, it takes account of all of the costs of occupancy, not just those in the common part(s).
<b>Landlord</b>	Landlord is the term used in Landlord and Tenant legislation in to denote the person or company which 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 Code where the context makes this necessary. In all other cases the reference is to ‘owner’.
<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>	The remuneration of the manager (including his 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. Where the subject property/site-management team is not sufficiently large 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.
<b>Marketing and promotions</b>	Advertising and other forms of promotion of a shopping centre intended to bring additional custom to the centre (as distinct from attractions and entertainments of a general amenity, benefit, service or attraction within the centre).
<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>Net internal area (NIA)</b>	The usable area within a building measured to the internal face of the perimeter walls at each floor level in accordance with the <i>SCSI Code of Measuring Practice</i> .
<b>Not for profit</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.
<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 in order 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 to 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. Rateable value is said to be the amount equal to the rent at which the property might reasonably be expected to be let from year to year if the occupier undertook to pay all of the usual occupier rates and taxes, and was also to bear the cost of repairs, insurance and other expenses (if any) necessary to maintain the property in a state to command that rent.
<b>Rebranding</b>	The upgrading of house or corporate style, logos, names badges, etc.
<b>Refurbishment</b>	Refurbishment is 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>Relaunching</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 redecorations)
<b>Schedules</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>Services</b>	Where the word 'services' is used, the reference includes works, such as maintenance and repair of the fabric and structure, and true services, such as the provision of heating, lighting, cleaning, 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 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. This 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. 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.
<b>Tenant</b>	The term 'tenant' is 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. 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', see above.
<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.

# 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-imbusement 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

# Appendix F: Further reading

Bannister, E., *Commercial Leases 2009: A Surveyor's Guide* (2nd edition), RICS Books, Coventry, 2008

Forrester, P., *Case in Point: Service Charges* (2nd edition), RICS Books, Coventry, 2008

Forrester, P. and Gibb, G., *Residential & Commercial Service Charges: A Surveyor's Handbook* (1st edition), RICS Books, Coventry, 2008

Freedman, P. et al., *Service Charges: Law and Practice* (3rd edition), Jordan Publishing Ltd, London, 2002

Tanfield Chambers, *Service Charges and Management: Law and Practice* (2nd edition), Sweet & Maxwell, London, 2009

## Marketing and promotions

A Good Practice Guide – *Shopping Centre Marketing and Promotions*, a publication produced for the Property Managers Association (PMA) by James Goodliffe of The Boots Company and Belinda Burnstone of WHSmith PLC, and endorsed by the British Council of Shopping Centres (BCSC), British Retail Consortium (BRC), PMA, the British Property Federation (BPF), The College of Estate Management (CEM) and RICS

BS 8572:2011 *Procurement of facility-related service*, BSI, 2011

*The Code for Leasing Business Premises in England and Wales 2007*, available at: [www.leasingbusinesspremises.co.uk](http://www.leasingbusinesspremises.co.uk)

## SCSI / RICS professional guidance

*Commercial property service charge handover procedures* (1st edition), RICS information paper, 2011

*Insurance for commercial property managers* (1st edition), RICS guidance note, 2010

*Limiting liability in commercial property management contracts* (1st edition), RICS information paper, 2009

*Managing mixed use developments* (1st edition), RICS guidance note, 2012

*RICS Code of Measuring Practice* (6th edition), RICS guidance note, 2007

*Service Charge Residential Management Code* (2nd edition), RICS guidance note, 2009

*Service charges and tenant alterations* (1st edition), RICS information paper, 2009

*Sinking funds, reserve funds and depreciation charges* (2nd edition), RICS information paper, 2014

*TUPE: Information for property managers* (2nd edition), RICS information paper, 2013

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