

SERVICE CHARGES THE NEW CODE

Service charges have frequently been a contentious issue between Landlords and Tenants. Tenants tend to suspect that their Landlord is endeavouring to make a profit out of the service charges that are raised. Landlords resent being obliged to pay out substantial sums and then have difficulty in recovering them.

As a result disputes have frequently arisen on the amount of service charge and its collection. In an attempt to meet these difficulties the RICS has published a new code, which comes into force on the 1st April 2007. Its intention is to establish best practice dealing with existing service charges both in existing and in new Leases.

The code has four objectives.

- To create an environment where service charges do not become an area of conflict.
- To ensure that neither Landlord nor Tenant makes a profit or loss on service charges, so the Tenant pays and the Landlord recovers no more or less than their respective obligations under the Lease.
- To ensure that the Landlord properly forecasts service charges so the tenant can budget accordingly.
- To improve the relationships between Landlord and Tenant by ensuring transparency in service charges.

It is important to stress that the code is no more than a code. The obligations on the parties, of course, are contained in the Lease and the code cannot override those contractual obligations.

It is however hoped that the parties to an existing Lease will agree to abide by the code and that new Leases will be prepared to incorporate the requirements of the code.

The code is divided into 7 distinct parts:

1. MANAGEMENT.

It seeks to impose duties on property managers to ensure that they achieve satisfactory performance standards. It seeks to ensure that management staff has sufficient

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qualifications and expertise to achieve these standards and to encourage a management regime where tenants are fully provided with management information and have the opportunity to challenge it reasonably.

2. COMMUNICATION

The code is at pains to stress the importance of communication between parties on a regular basis, particularly where substantial works are planned. Regular communication will assist in ensuring that future problems are more likely to be avoided.

3. TRANSPARENCY

The code stresses that the Landlord should be absolutely transparent in the quantification and calculation of service charges so the Tenant can understand the precise financial implications.

4. STANDARD PERFORMANCE

The code deals with the level of performance of contractors and other service suppliers for services provided to Tenants.

5. ADMINISTRATION COSTS

The code stresses that management costs should fairly reflect work actually carried out by the property manager and are not merely a percentage of overall expenditure.

6. SINKING AND RESERVE FUNDS

These can be a frequent area of dispute where Leases provide for payments of sums into a sinking fund to enable Landlords to budget for future major expenditure. The code of practice sets out procedures for the levying and maintenance of the reserve fund.

7. MARKETING AND PROMOTION

Finally, the code provides machinery for determining how the costs of marketing and promotional activities should be shared between Landlords and Tenants.

This covers expenditure by Landlords for the benefit of a substantial site of which tenants occupy part and where the Tenants will benefit from the Landlord's expenditure and should therefore contribute to it.

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TECHNICAL SECTION

The code contains a technical section, which is intended to provide practical assistance to property managers. This section deals with performance contracts to endeavour to ensure appropriate performance standards for the contractors carrying out the services. This section also deals with initial provision in a new development, and with improvements to existing equipment and also enhancement of facilities by providing by new or improved equipment.

DISPUTES

The code recommends that disputes arising under service charge provisions in leases be dealt with by Alternative Dispute Resolution rather than through the courts. The RICS provides its own dispute resolution service. It also encourages mediation and in the event that mediation fails recommends the referral of a dispute for expert determination.

It remains to be seen whether these recommendations become incorporated in new leases and thereby reduce future conflict between Landlord and Tenant in this area.

Should you have any queries in relation to this article please do not hesitate to contact Ken Sutton or Martin Buckeldee in our Commercial Property Department on 01276 686222.