

# Service Charge Operating Report

## Retail Parks

**SCOR 2022**

Compliance

 **bellrock**  
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# 1. Introduction

## Welcome to the first edition of the new Service Charge Operating Report (SCOR) for Retail Parks.

Our first edition focuses on assessing whether year end service charge accounting documents prepared at 50 of the UK top 100 retail parks comply with the increased presentation and disclosure requirements of the RICS Professional Statement, Service Charges in Commercial Property (RICS, 2018). Academic oversight for SCOR for Retail Parks is provided by Metropolitan State University of Denver, and we hope that you find this new publication useful for assessing the current levels of accounting presentation, transparency, and disclosure within the service charge documents prepared for UK retail parks.

Before we discuss the dataset used and the research findings, it is important to reiterate that occupiers must be vigilant in reviewing and understanding the specific lease provisions that govern the service charge, along with the service charge budgets and annual year end accounts prepared by the managing agent. While this “review” process may help to ensure that the occupier pays a “fair” service charge towards reimbursing the landlord for expenditure incurred in supplying services in accordance with the lease, the recent case of *Sara and Hossein Asset Holdings Ltd v Blacks Outdoor Retail Ltd* (2020) is a timely warning of how the legal interpretation of a lease provision may prevent an occupier from challenging the expenditure incorporated within an annual service charge reconciliation statement.

In this case, the Court of Appeal ruled that, where a lease states that an annual statement of service charge expenditure is “conclusive”, it is conclusive as to the amount due from the tenant, whether or not the certified expenditure was properly incurred in accordance with the terms of the lease. As a result, in situations where such a lease term applies, the occupier is prevented from challenging the certified accounting statement, except where there is evidence of a manifest accounting error or fraud. As a number of existing retail leases commonly include “conclusive” provisions similar to those within *Blacks’* lease, UK retail occupiers need to be aware that even “best practice” levels of accounting transparency or disclosure may not prevent them from paying service charge bills that include amounts outside the terms of the lease. As a result, it is important occupiers carefully scrutinise leases for provisions related to whether the certificate is final and binding, and also quickly challenge any seemingly “non-lease” compliant expenditure included within the service charge budget.

While the outcome of the *S&H v Blacks* case potentially calls into question the actual benefits derived from the increased accounting presentation and disclosure requirements of the 2018 RICS Professional Statement, compliance with these provisions should improve the relevance and faithful representation of service charge accounting information for occupiers. As a result, SCOR for Retail Parks 2022 assesses whether current accounting practices meet these ‘best practice’ requirements.

## 2. Dataset and Methodology

The data for SCOR's compliance analysis was obtained from analysis of the annual statements of service charge expenditure prepared at 50 of the UK's 100 largest retail parks ranked by Gross Lettable Area (GLA).

The characteristics of the compliance dataset used for SCOR for Retail Parks 2022 is provided in Table 1.

Years	No. of Retail Parks	Type of Document	Total Area (GLA)	Total Service Charge Cost
2019-2020	50	Annual statements of service charge expenditure	3,003,670 sq.ft.	£32,758,140

Table 1. Characteristics of the compliance dataset for SCOR for Retail Parks 2022

SCOR's data was drawn from an unbiased and representative dataset, as it included data for any location that Bellrock Real Estate deals with, where a complete statement of annual service charge expenditure was available for a fiscal year that commenced on or after 1 April 2019 (the effective date for the new accounting presentation and disclosure requirements of the 2018 RICS Professional Statement). As a result, no self-selection or bias was used in establishing the dataset, and a unique population of properties was used for the compliance analysis.

While having a representative dataset is crucial, it is also vital that information is collected and analysed in a neutral manner, free from researcher bias and inaccuracy. In terms of data collection, all of SCOR's compliance data was obtained from analysis of the primary accounting documents provided to commercial occupiers. Supplementary information, such as data contained within covering letters and additional attachments (i.e. "service charge packs" and "appendices"), was also reviewed where relevant.

As data was hand collected by the research team from actual service charge documents, there is no potential for third-party bias in terms of manipulation or selective exclusion of documents. Furthermore, all available service charge data for a given period is included, unless underlying source documents are deemed to be incomplete. As this is the first edition of SCOR for Retail Parks, and the effective date of the 2018 RICS Professional Statement was for fiscal periods that commenced on or after 1 April 2019, the research team analysed the first set of annual statements of service charge expenditure prepared in accordance with the new accounting requirements of the RICS Professional Statement. While all UK retail parks within SCOR's dataset have now completed two fiscal years since 1 April 2019, the most recent accounts for a number of properties were not published at the time the research was conducted. As a result, the compliance analysis had to focus on the older accounting documents (i.e. the first accounts whose fiscal year commenced on or after 1 April 2019) in order to provide a more representative population of UK retail park data.

In terms of analysis, content analysis was used to obtain the compliance data, which often requires some degree of subjective interpretation on behalf of the research team. In practice, the potential for bias in this type of work is remote as it requires limited interpretation by the researcher. The data codification required for the compliance analysis is primarily binary in nature and unproblematic, especially when a document provides explanatory information. Judging the efficacy of such information might be contentious in theory, but in practice the nature of the service charge renders the analysis relatively straightforward. Hence, most of the data could be utilised directly, and the resulting compliance analysis provides a valid examination of current service charge accounting and certification practices.

While a major part of SCOR's data collection and analysis is performed by a research team at Bellrock, the work is closely monitored by an independent academic supervisor. This position has been held by Dr Andrew Holt (Professor of Accounting at Metropolitan State University, Denver) since the inception of the various SCOR reports, and has helped to establish the compliance methodology and verify the neutrality and independence of the reported results.

# 3. Compliance with the 2018 RICS Professional Statement

## 3.1 New Compliance Metrics

Based upon a review of 50 annual service statements of service charge expenditure whose fiscal year commenced on or after 1 April 2019, this section presents compliance analysis investigating whether select accounting presentation and disclosure requirements of the 2018 RICS Professional Statement Code have been adopted by managing parties at UK retail parks.

After evaluating the Professional Statement, the researchers identified a series of 17 “must”, “should” and “other” compliance metrics that both captured the main accounting and administrative requirements of the Professional Statement and could be identified via an unbiased, “binary” review (i.e. “yes” it is included, or “no” it is absent) of the content within the annual service charge accounts. As the leases for many properties do not require the creation of a sinking or reserve fund, no metrics were included to measure the accounting requirements in this area. Each of the 17 metrics are explained in more detail in Table 2.

The metrics include 4 “musts”, 12 “shoulds”, and 1 “other” requirement as per the language used within the Professional Statement. As the 1 “other” requirement included within the Professional Statement (“Openness and transparency can be further enhanced by the inclusion of a balance sheet or cash reconciliation”) is neither a “must” nor a “should”, each property’s annual service charge accounts were ranked out of a total compliance score of 16 (i.e. the 4 “musts” and 12 “shoulds”), with separate reporting of compliance with the 1 “other” requirement.

No.	Requirement	Must/Should	Measurement
1	The Professional Statement requires that fees be set on a fixed-price basis (Section 4.1.3.2, page 14)	Must	Binary coding – yes/no
2	Ensure that a service charge apportionment matrix for the property is provided annually to all tenants. Clearly shows the basis and method of calculation, and the total apportionment per schedule for each unit within the property. (Section 4.2.4, page 18)	Must	Binary coding – yes/no
3	Service charge monies must be held in one or more discrete [or virtual] bank accounts (Section 4.5, page 22)	Must	Clear statement – yes/no
4	Interest earned on service charge accounts must be credited to the service charge account after appropriate deductions have been made (Section 4.5.10, page 27)	Must	Binary coding based upon evidence – yes/no
5	Timeliness - Detailed statements of actual expenditure, together with accounting policies and explanatory text, should be issued within four months of the service charge year end (Section 4.5.12, page 27-28)	Should	Binary coding – yes/no
6	Industry Standard Cost Classifications should be used in reporting budget and actual expenditure. As a minimum acceptable level of reporting, service charge budgets and statements of actual expenditure should be prepared at cost class level (Section 4.5.5, page 25)	Should	Cost classes Binary coding – yes/no
7	and cost category level (Section 4.5.5, page 25)	Should	Cost categories Binary coding -yes/no
8	Service charge accounts should include a comprehensive list of accounting policies and principles including: whether the accounts are prepared on an accruals or where permitted, the cash basis (Section 4.5.1, page 23)	Should	Clear statement of whether accounts are prepared on an accrual or cash basis yes/no
9	Where the accounts are prepared on an accruals basis, they should be accompanied by a schedule of opening and closing prepayments and accrued expenses (Section 4.5.6, page 26)	Should	Binary coding – yes/no
10	An analysis of any material variances between budget and actual expenditure, with a detailed commentary to explain trends and variances where significant (section 4.5.2, page 23)	Should	Binary coding – yes/no
11	Other information includes: A statement detailing how insurance claims are accounted for (Section 4.5.2, page 23)	Should	Clear statement on insurance claims – yes/no
12	Other information: Whether the owner has waived the exemption to charge VAT (opted to tax) (Section 4.5.1, page 23)	Should	Statement of whether owner has waived exemption to charge VAT yes/no
13	The accounts should be approved by or on behalf of the landlord as complying with the following statements: the accounts produced represent the actual expenditure incurred by the owner in supplying the services to the building (section 4.5.3.2, page 23) and	Should	Clear statement – yes/no
14	That the expenditure the owner is seeking to recover is in accordance with the terms of the leases and where practicable, the provisions of the professional statement (section 4.5.3.2, page 24)	Should	Clear statement – yes/no
15	The approver should be an appropriately qualified and competent person with experience in dealing with service charges. The status of the person and the capacity in which they are acting should be made clear (section 4.5.3.2, p. 24)	Should	Clear statement of status and capacity – yes/no
16	Annual statements of service charge expenditure should be supported by an independent review of service charge accounts, such as specified with the ICAEW Technical Release (Section 3, principle 13, page 11)	Should	Includes an Independent Accountants’ report – yes/no
17	Openness and transparency can be further enhanced by the inclusion of a balance sheet or cash reconciliation (Section 4.5.4, page 24)	Other	Binary coding – yes/no

Table 2: Metrics for assessing service charge accounting compliance with the RICS Professional Statement

### 3. Compliance with the 2018 RICS Professional Statement

#### 3.2 Compliance Results for Retail Parks 2022

Table 3 provides the compliance results for each of the 16 “must” and “should” metrics for the 50 retail parks analysed.

When assessing the results in Table 3, it is disappointing to note that compliance with two of the four “must” requirements (Metrics 1-4 in Table 2) of the Professional Statement failed to exceed 72%, with the “crediting of interest earned” and clearly disclosing that management “fees [were] set on a fixed-price basis” achieving the highest results at 88% and 84% compliance, respectively. While three of these “must” metrics are specifically listed under the Professional Statement’s list of “mandatory” requirements (RICS, 2018, p.9), the statement also “requires that [management] fees be set on a fixed-price basis” (RICS, 2018, p.14) so this metric is also classified as a “must” rather than merely a “should”.

In terms of compliance with the 12 “should” requirements, the overall results appear to demonstrate a commitment to abiding by the recommendations of the RICS Professional Statement, with compliance for 8 of the 12 metrics either meeting or exceeding 78%. However, these results were obtained from a limited sample of 50 UK retail parks, and more detailed work is required before compliance trends can be clearly established for the industry.

While compliance with all 12 of the “should” metrics is important, there are some that are more critical than others, and any compliance rate of less than 100% potentially harms the information content and quality of the resulting accounting document. Furthermore, poor compliance in any area suggests a departure from “best practice”, something the RICS is attempting to prevent in order to improve the overall relevance, reliability, and comparability of UK service charge accounts.

The “relatively” low level of compliance in certain critical areas, such as “Statement that accrual accounting used” (No. 8: 78%) and to certify that the accounts represent actual expenditure incurred in supplying services in accordance with the lease (No. 13: 88% and No. 14: 54%), are concerning, since this information is essential for determining whether the accounts provide “true and fair” and faithfully representative information for occupiers. In terms of metric 14, that the accounts should include a “statement that the amounts seeking to be recovered are in accordance with the lease and where practicable the PS”, it was surprising that a number of the “non-compliant” certification statements highlighted compliance with the RICS Professional Statement, but then failed to specifically mention that the amounts seeking to be recovered were in accordance with the lease. As the lease is the contractual document that governs the service charge agreement between the parties, it is vital that the certification statement primarily refers to it, and additionally, where practicable, compliance with the RICS Professional Statement.

Finally, compliance with certain other accounting requirements, such as providing the financial statements within four months of the year end (No. 5: 52%), that the person approving the accounts should be appropriately qualified and their status made clear (No. 15: 74%), and stating how insurance claims are accounted for (No.11: 20%), should not be too onerous for professional managing parties to abide by, and it is surprising that we still see compliance fall short in these areas.

Requirement	Must/ Should	Compliance out of 50	
		No.	%
1. Fixed Management Fee	M	42	84.0%
2. Apportionment matrix is provided for each unit in the property	M	31	62.0%
3. Statement that service charge monies are held in one or more discrete bank accounts	M	36	72.0%
4. Interest earned credited to the service charge account	M	44	88.0%
5. Timeliness Compliant (date) - annual accounts produced within four months of year end	S	26	52.0%
6. Cost Classes Used	S	45	90.0%
7. Cost Categories Used	S	48	96.0%
8. Statement that accrual accounting or cash basis used	S	39	78.0%
9. Schedule of accruals and prepayments.	S	39	78.0%
10. Description of Variances	S	45	90.0%
11. Statement about how insurance claims are accounted for	S	10	20.0%
12. Statement about whether owner has waived exemption to charge VAT	S	40	80.0%
13. Statement that accounts represent the actual expenditure incurred in supplying services	S	44	88.0%
14. Statement that amounts seeking to be recovered are in accordance with the lease and where practicable the PS	S	27	54.0%
15. Approver should be an appropriately qualified and qualified person. Status of person should be made clear	S	37	74.0%
16. Accounts should be supported by an independent review in line with ICAEW Technical Release	S	39	78.0%

Table 3: Compliance against 16 “must and “should” accounting requirements of the Professional Statement

In terms of the 17th metric, the inclusion of a balance sheet, none of the 50 documents analysed included this type of accounting statement, which is disappointing as a balance sheet provides transparency as to the magnitude of end-of-period assets, liabilities, and reserves. In addition, the provision of a balance sheet helps keep track of the changes between opening and closing accrued and prepaid amounts (and sinking fund balances), benefits the auditing process, and assists during the handover of the service charge accounts to a new agent.

Figure 1 provides the overall compliance rankings for each of the 50 certificates against the 16 “must” and “should” metrics of the 2018 Professional Statement.

While it is difficult to generalise from such a small sample of only 50 retail parks, it is clear that compliance levels vary, although the majority of documents scored on the higher end of the ranking scale. No document fully complied with all 16 requirements or failed to comply in any way. 39 documents (78%) complied with 10 or more metrics, 82% complied with 8 or more metrics, and only 12% complied with 4 or fewer of the RICS requirements.

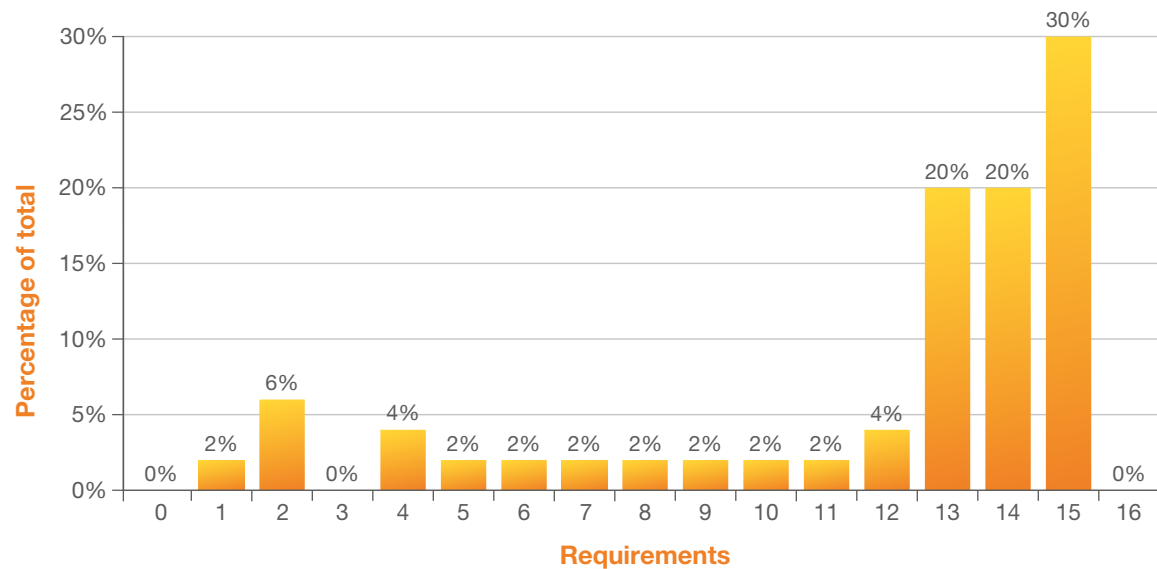


Figure 1: Compliance rankings against 16 accounting requirements of the 2018 Professional Statement

### 3. Compliance with the 2018 RICS Professional Statement

#### 3.3 Comparative Compliance Results – Retail Parks v Shopping Centres and Offices

Although this is the first year of analysing retail park compliance, it is important to draw comparisons with compliance data obtained from UK shopping centres and multi-let office buildings. SCOR for Shopping Centres 2021 and SCOR for Offices 2021 included compliance results for the same time period and metrics as SCOR for Retail Parks, and these comparative results are shown in Table 4.

In terms of drawing inferences from the comparative compliance analysis, care must be taken, as the properties used for the UK shopping centre analysis were all within the UK's top 60 UK shopping centres by GLA, but the 62 UK offices merely represented the properties whose complete accounting documents were available for scrutiny by the researchers. As a result, the population of UK office buildings included accounting documents prepared by a wider range of providers, including a number of smaller operators and managing parties. In contrast, the retail park and shopping centre accounting documents were prepared by a narrower range of larger commercial managing agents, who should have greater resources to comply with the RICS's increased accounting requirements. Across the 16 metrics reported in Table 4, there are clear differences between the overall level of compliance between the commercial retail and office sectors. In addition, the results for retail parks closely mirror those for shopping centres across most metrics. What is clear is that improvement is needed in many areas of accounting presentation and transparency, across all three sectors.

Requirement	Must/ Should	Compliance for 50 Retail Parks		Compliance for 42 Shopping Centres		Compliance for 62 Offices	
		No.	%	No.	%	No.	%
1. Fixed Management Fee	M	42	84.0%	37	88.1%	32	51.6%
2. Apportionment matrix is provided for each unit in the property	M	31	62.0%	27	64.3%	27	43.5%
3. Statement that service charge monies are held in one or more discrete bank accounts	M	36	72.0%	25	59.5%	24	38.7%
4. Interest earned credited to the service charge account	M	44	88.0%	33	78.6%	39	62.9%
5. Timeliness Compliant (date) - annual accounts produced within four months of year end	S	26	52.0%	18	42.9%	28	45.2%
6. Cost Classes Used	S	45	90.0%	37	88.1%	34	54.8%
7. Cost Categories Used	S	48	96.0%	35	83.3%	39	62.9%
8. Statement that accrual accounting or cash basis used	S	39	78.0%	33	78.6%	29	46.8%
9. Schedule of accruals and prepayments.	S	39	78.0%	33	78.6%	25	40.3%
10. Description of Variances	S	45	90.0%	40	95.2%	43	69.4%
11. Statement about how insurance claims are accounted for	S	10	20.0%	16	38.1%	14	22.6%
12. Statement about whether owner has waived exemption to charge VAT	S	40	80.0%	34	81.0%	36	58.1%
13. Statement that accounts represent the actual expenditure incurred in supplying services	S	44	88.0%	31	73.8%	32	51.6%
14. Statement that amounts seeking to be recovered are in accordance with the lease and where practicable the PS	S	27	54.0%	20	47.6%	19	30.6%
15. Approver should be an appropriately qualified and qualified person. Status of person should be made clear	S	37	74.0%	29	69.0%	26	41.9%
16. Accounts should be supported by an independent review in line with ICAEW Technical Release	S	39	78.0%	30	71.4%	33	53.2%

Table 4: Comparative Compliance against 16 “must and “should” accounting requirements of the Professional Statement

While it is useful to compare overall compliance results for each of the 16 metrics across the three sectors, Figure 2 illustrates the comparative compliance rankings per certificate expressed as a percentage of total documents included with the retail park, shopping centre, and office compliance datasets during 2019-2020.

As with the comparative analysis of each compliance metric, the results for the retail parks and shopping centres show similarities in the relatively higher number of certificates scoring towards the high end of the 16-metric ranking. By way of contrast, the rankings for the accounting documents prepared for office buildings are much more varied, with a wider disparity in overall rankings, and a greater number of documents at the lower end of the compliance rankings.

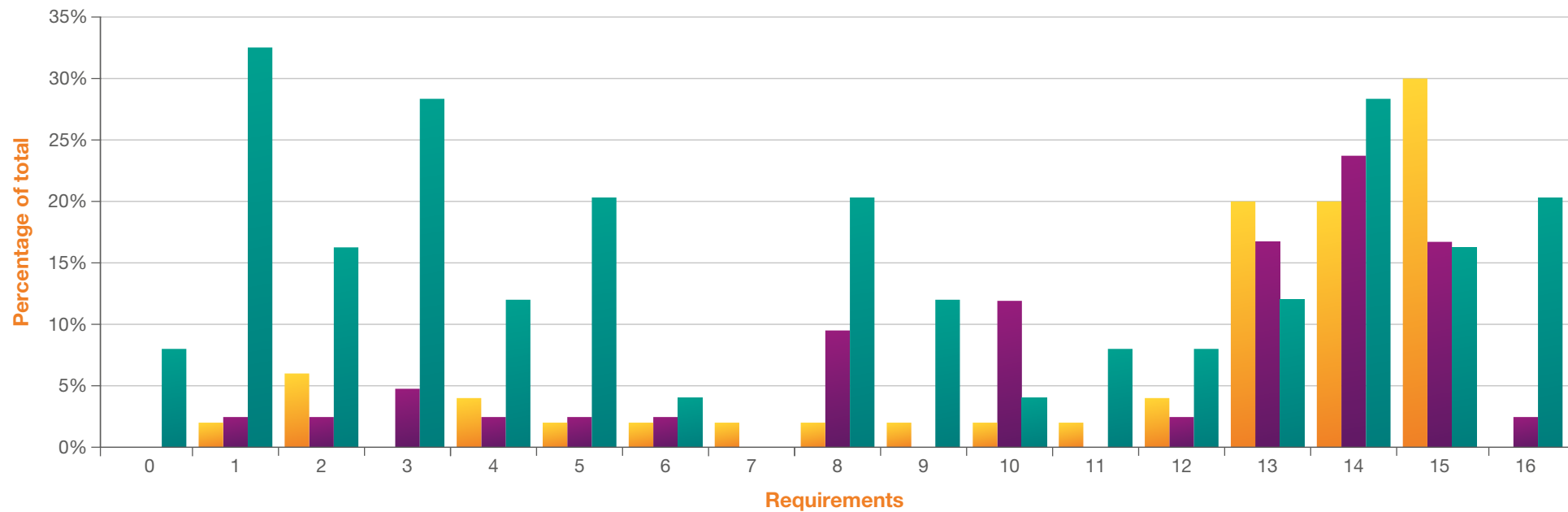


Figure 2: Compliance rankings against 16 accounting requirements of the 2018 Professional Statement

## 4. Conclusions on the Compliance Results for UK Retail Parks

From both the individual and comparative compliance analysis, it is clear that some managing parties at UK retail parks are trying hard to improve the relevance, representational faithfulness, and comparability of the information contained within service charge accounts. However, for some, further work is needed to meet both the mandatory and “best practice” requirements contained in the Professional Statement. The average annual statement of service charge expenditure for a UK retail park is certainly getting longer in length, but often includes repeated accounting information that uses different formats and layout and often includes pages of “boiler plate” disclosures and information about a property that is largely irrelevant to most occupiers. Excessive length and repetition are clear deficiencies but are secondary concerns when compared to the failure to comply with some of the more important accounting requirements of the RICS Professional Statements.

All year-end accounting annual statements of service charge expenditure should provide a clearly prepared and organised document that provides a certified and comparable account of the costs incurred, together with a complete list of accounting policies and accompanying notes, using a “RICS compliant” approach that embodies best practice. However, even in situations where “high quality” service charge accounting documents are provided, the case of *S&H v Blacks* serves to remind occupiers of the importance of negotiating an appropriately worded lease provision that determines both how, and when, the expenditure included within the annual accounts becomes “conclusive”, final, and binding.

Future editions of SCOR for Retail Parks will continue to monitor compliance with key accounting aspects of the 2018 Professional Statement. As with other SCOR publications, the plan is to include additional longitudinal compliance analysis and cost analysis in future editions.

# SCOR reports also available for **Offices** and **Shopping Centres**



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