

Canary Riverside, London E14
Service Charge Apportionment Report

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1. Introduction

Gross Fine was established in 1960 and has a total staff of 60 including 7 directors. The company is a wholly owned subsidiary of Hercules Property Services, a quoted company on the London stock exchange, listed under support services. Gross Fine is responsible for the management of approximately 16,000 units having a total service charge collection for residential management in the region of £40 million and employing some 450 staff on behalf of clients.

We have a wide ranging client base, from residents owned management companies for traditional mansion blocks, to corporate landlords in respect of substantial mixed use schemes. We have a number of LVT appointed manager roles, trusteeships and are advising a number of resident groups in respect of right to manage and the right to enfranchise legislation.

I, Richard Daver, have a BSc Honours degree in Urban Estate Surveying, and am a member of the Chartered Institute of Housing and The Royal Institution of Chartered Surveyors. I am a director of Gross Fine and have in excess of 15 years experience in residential property management and prior experience in dealing with both local authority and housing association stock.

As a director of Gross Fine, I run the new development and new business team and my primary role is to act in a consultancy and advisory capacity to major London developers in respect of schemes ranging from simple residential schemes comprising approximately 50 units to major mixed use schemes, in some cases exceeding 1,000 residential units.

The advice given ranges from pre-planning strategy advice to accompany planning applications, through to detailed strategies for matters such as staffing, security and particularly service charge structure and assessment. I also advise in respect of the impact of design and technical detail on the future management of the building both in terms of practical management as well as cost.

The area for which our client most relies on us, is for advice is in respect of the structure of the service charge and assessment of costs. This is of course essential not only for the marketing of the scheme but also for the ongoing management and as whatever is set at the initial stages is likely to be reflected through the life time of the scheme. It is therefore essential that we provide a service charge structure, which is not only equitable but also reflects what is reasonably affordable, particularly where expectations and aspirations may differ, such as will be found in substantial mixed use schemes where there is not only a commercial element but, more likely in recent years, a substantial element of affordable housing.

My experience in this area is one of the main reasons why I have directorial responsibility for the Canary Riverside scheme.



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2. Terms of Reference

I have been instructed by Canary Riverside Estate Management Limited to prepare a report based firstly on a review of plans and documentation made available to me and secondly on my findings since the commencement of Gross Fine's management on 1st January 2004.

My report is to cover the apportionment of service charges to include a review of the current position as well as the factors which were applied to the original calculations and form a view of the reasonableness of the theory applied when the first service charge structure and estimates were configured. My report is also to review the levels of charges both in terms of comparisons with other estates where either myself, personally, or Gross Fine, generally, have direct knowledge and in terms of the individual service charge provisions for items of expenditure within the Canary Riverside service charge budgets.

Although instructed by the landlord to produce this report it is important to Gross Fine to stress our independence. This report has been produced without bias and is based upon my own experience generally and specifically over the past three months that Gross Fine have been managing Canary Riverside. Canary Riverside is of course a significant instruction for Gross Fine however we have a very strong reputation in the market place and we would not allow that reputation to be jeopardised by not seeking to act independently. To emphasis this position, whilst Canary Riverside produces a substantial fee it does in fact represent only 3% of our annual turnover.

3. Estate Description

Canary Riverside is a mixed use estate forming part of the Canary Wharf development occupying a prominent site adjacent to the River Thames. The site comprises four residential buildings (Hanover House, Berkeley Tower, Belgrave Court and Eaton House) comprising 325 apartments. Some residential buildings have commercial units at ground floor level. Each building is served by a doorman 12 hours a day 7 days a week. Included within the 325 apartments, 45 (Circus Apartments) are operated as serviced apartments in one of the buildings.

There is also a five star Four Seasons hotel which we understand comprises 142 rooms. There is also a Holmes Place health and fitness club with a restaurant above and a separate swimming pool building forming part of the club.

In addition to the commercial units located within the residential buildings there are also restaurants located in the WF1 building to the east of the main element of the estate at Westferry Circus.

There is also a substantial car park comprising in excess of 500 parking spaces which is split into residential use and separate public / hotel use.

The development is built over a 5 ½ acre site and there are therefore shared services forming 'the estate' including an estate management office, security control room, security generally, loading bay, roads, pathways, gardens, plantrooms etc...

The development has been built to a high specification both in terms of the construction and the services provided. This is significant in respect of the levels of service charge which result (see section 7).

4. Apportionment of Service Charge

In brief the service charge is structured as follows:-

There is an estate charge which deals with the costs relating to the services provided to the development which are shared by all and therefore are contributed towards by each element of the scheme. These costs include elements of staffing, most notably security but also the management office staff (excluding the managing agents' Property Manager) and the current, but shortly to end Handyman / Maintenance Man service. The estate charge also covers items such as cleaning the external areas, the management office costs, utilities, elements of maintenance, health and safety an element of insurance and an element of professional fees attributable to the estate.

In addition there is a landscape charge dealing with the main communal gardens however this is not apportioned as per other estate items but only to those areas which are deemed to derive benefit namely the residential and the hotel.

There is also a residential service charge in which the four residential blocks are treated as one and service charge is not therefore divided up by block. That service charge covers costs relating to staffing – namely the doorman located within each entrance block, but also a proportion of the Handyman's cost, internal common parts cleaning, window cleaning, utilities, mechanical and electrical plant maintenance (most particularly lifts and engineering maintenance), general repairs, a proportion of landscaping, health and safety, insurance costs, a proportion of professional fees and an element of reserve funds.

There is also a service charge estimate produced for the car park, the commercial units located within the residential buildings, the hotel, the health and fitness club and the free-standing commercial units at Westferry 1.



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The Headlease contains a clause stating that the estate service charge should be apportioned on the basis of the comparison of gross internal areas between relevant parts of the scheme.

We are advised by both the landlord and a representative of the architect who was involved in the scheme at the time, that in fact the apportionments were based on gross external areas. The position has not been checked, for the purposes of this report, by way of a new measurement exercise either in whole or in part, however I have met with the architect's representatives, most particularly John Henry, in order to satisfy myself as to the method of measurement adopted giving rise to the area figures used and the apportionment of the estate for service charge purposes.

We are advised that the architects, Koetter Kim Associates (KKA) are no longer trading, however, Mr Henry, a principal of OCA Architecture, was heavily involved with the Canary Riverside scheme and has retained information and drawings relating to the project.

It would appear that rather than using gross internal area (GIA) the scheme was measured on the basis of gross external area (GEA). Both, together with net internal area (NIA) are acceptable methods of apportionment in accordance with The Royal Institution of Chartered Surveyor's code of measuring practice. The issue here is that the use of GEA as opposed to GIA does not comply with the Headlease and we therefore need to consider whether this has any material effect on the apportionment.

I have received, from the Landlord, a set of plans which have been reduced to A3 size and are therefore not to scale. Those plans however detail the gross external areas as generated by the design software package used.

I therefore called for, and received, a random selection of drawings from the architects produced in 1:200 scale and these have been considered in order to determine the likely accuracy of the plans reduced to A3 size provided by the Landlord.

It is my opinion that the plans are accurate and therefore I believe it is reasonable to rely on the gross external areas detailed on the reduced drawings.

Those areas have been scheduled, based on which I have calculated apportionments for estate charge purposes and these compare to the actual apportionments in use as follows: -

	Existing Apportionment	Calculated Apportionment
Residential	56.2%	56.2%
Car Park	18.6%	18.6%
Commercial in Residential	1.01%	1.4%
Hotel	16.8%	16.8%
WF1	1.99%	1.6%
Club	5.4%	5.4%
Total	100%	100%

In addition the landscaping costs are currently apportioned at 77% for the residential and 23% for the hotel and on the basis of my calculations this would appear to be correct.

There is a variation in the commercial in residential and WF1 commercial proportions the former being 0.39% understated and the latter overstated by the same amount. Whilst therefore this needs to be investigated further, the discrepancy does not have material impact on the residential apportionment.

In accordance with the service charge structure, the commercial units located in residential buildings pay a proportion of certain elements of the service charge. That proportion is currently, 1.92%. My comparison of the gross external areas however, gives rise to a proportion of 2.4%. The Landlord had highlighted this discrepancy prior to my investigation and had asked for verification. This discrepancy does have an effect on the amount of service charge payable by the residential element but given that the percentage is applied to only a small number of items and does not apply to some of the substantial items such as staffing, the loss is fairly minimal. We would suggest that this be investigated further and if appropriate for the correct



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apportionment to be reflected in the accounts for the year end March 2004 and going forward thereafter.

Consideration must however be given to the position whereby GEA figures were used rather than GIA.

It is my opinion, having reviewed the plans, that again there is no material difference between the measuring practice used as long as it has been, as it appears, implemented on a uniform and consistent basis in the calculation process. The main difference between these two methods is the inclusion or exclusion of the external walls. There is nothing in the plans that I have seen that would give rise to a concern as to a substantial variation between GEA and GIA figures which would have an affect on the result of the apportionment. As a matter of principle, taking GEA instead of GIA would virtually make no difference. It is my opinion therefore that whilst not strictly in accordance with the Headlease the method of measurement appears to be fair and reasonable as it has been consistently applied.

There is however one item of apportionment which I believe should be reviewed and that relates to landscaping. It is clear that the Holmes Place club and the restaurant above derive benefit, through the visual enjoyment of the gardens for its guests. In the case of the restaurant its patrons are able to access the club through the gardens. Indeed there is a sign advertising the restaurant (Ubon by Nobu) located within the gardens. It is understood that the original apportionment was undertaken on the basis of those actually being able to utilise the landscaped areas rather than just having a right to pass through them. On this basis only the residential and hotel currently contribute.

It is worth noting however that the club will only contribute a small proportion and it may be that a weighting in favour of the club should be applied as they only pass through the grounds rather than actually having a right to use them. Similarly, by charging the club for this facility this may imply a right to use the landscaped areas which may have a detrimental effect on appearances. Given the small contribution



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and the fact that even that contribution may be reduced further by way of weighting, it may be that it will be more beneficial to maintain the status quo rather than give or imply rights of use.

Each of the residential buildings is served by a cradle which is subject to maintenance and repair costs. The cradles are, in the main, used for the window cleaning operation for the residential but will also be used for repairs to the exterior of the building to which the commercial units, located within the residential buildings, contribute under the terms of their leases. It would be equitable therefore to apportion some of the cradle maintenance and repair costs to those ground floor commercial units and this does not appear to be factored into the current service charge structure. However the commercial units pay currently 1.92% (which, with reference to my previous comments, may need to be increased to 2.4%, of this cost). Bearing in mind that a substantial proportion of the cradle usage is for the residential window cleaning exercise there should be some weighing applied to those costs. We may therefore be looking at a contribution equivalent to say approximately 2% of 25% the cradle maintenance cost which overall, will be relatively insignificant.

If I were to be approaching this development afresh, in its design stages prior to the construction, I would have structured the service charge slightly differently. Firstly I may have had a separate service charge for each residential building with that service charge having two schedules to reflect the commercial element. The first schedule would be for shared services, i.e. costs shared by both the residential and the commercial, such as insurance or the maintenance of the structure and external fabric of the building.

The second schedule would reflect only those costs attributable to the apartments for example, lifts, common parts cleaning, doorman costs, etc...

The four residential buildings at Canary Riverside vary in size. It could be argued therefore that items such as window cleaning for the smaller buildings (e.g. Hanover House) subsidise the larger ones (e.g. Berkeley Tower). However there are other



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costs such as 24 hour staffing where the cost will be the same per building regardless of its size and it could therefore be argued that the larger buildings subsidise the smaller ones.

Therefore whilst the service charge structure is not as I would have produced it, it is not unreasonable to treat the four residential buildings as one and the same for service charge purposes and indeed there are many examples throughout London of similar service charge arrangements.

The estate also contributes towards to the Canary Wharf Estate charge however whilst this is calculated by Canary Wharf on the basis of the development as a whole it appears that, the charge is only apportioned to the commercial units. We are yet to understand whether there are any formal arrangements under the terms of the legal agreements, but if not it would appear that the commercial elements of the scheme heavily subsidise the residential element. Aside from apportionment issues there are a number of queries in respect of the Canary Wharf estate charge which we will be taking up shortly with the managers for Canary Wharf.



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5. Service Charge Comparisons

Gross Fine manage a large number of prestigious properties and substantial estates including mixed use schemes. In addition my work in respect of new developments (both existing and under construction) provides a good insight into the levels of service charge for central London schemes.

There will be a number of factors affecting the levels of service charge in terms of a rate per sq. ft. and in particular, these will be the overall size of the scheme and the services provided. In terms of size and by way of example, to provide a 24 hour porter to a block of 100,000 square feet will cost half the rate per sq. ft. to provide exactly the same service to a block half the size.

With regards to services, Canary Riverside has a substantial number, all of which have an obvious impact on the levels of service charge payable. The scheme has 24 hour security, 12 hour a day 7 days a week doorman service to the residential buildings, external window cleaning via cradle access, a substantial amount of mechanical and electrical plant, an on site estate office, estate and administration staff, a Canary Wharf estate charge, landscaped areas maintained to a high standard, a high voltage / low voltage conversion system for the supply of electricity and a large number of lifts serving both the residential and the estate. Based on the budget figures for YE 31 March 2004, the average service charge for the residential portion of the estate was about £4.45 per square foot. (total residential service charge inc. estate / total residential NIA = £1,834,605 / 412,415 sq ft = £ 4.44)

In my opinion the emphasis should be placed on quality of service and value for money rather than purely cost.

With regards to comparisons from our portfolio we would advise that service charge levels are as follows: -



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The most direct comparison that we have to Canary Riverside is that of Chelsea Harbour. Chelsea Harbour comprises 310 residential units across six blocks. There is also a commercial element and an overall estate charge (termed in this instance the 'village' charge).

There is one main difference in the service charge structure in that at Canary Riverside the residential buildings are treated as one for service charge purposes. However in the case of Chelsea Harbour, each building has its own service charge and makes a contribution to the village charge. The level of service charge therefore varies from block to block and whilst the services are similar, the buildings differ in size. Therefore if you took a building with a portered reception and one lift for example, the cost of those services will be, on a pro rata basis, higher per square foot in the smaller building.

At present based on the service charge year to 30 September 2004, service charges are running between £3.83 (Admiral Court) and £6.00 (Belvedere Tower). The average across the estate would appear to be in the region of £4.50-£4.60 per square foot.

In addition to Chelsea Harbour we also manage two residential blocks which form part of the Paddington Central Estate. The service charge for those blocks is running at £5 per square foot even though only 12 hour per day portorage cover is provided. There is however a large security presence provided through the estate, which we do not manage. We are in fact presently challenging the service charge and insurance contributions for the estate on behalf of our client.

We also are appointed on a consultancy basis in respect of a new build scheme which forms part of the Paddington Basin development. That property will have 24 hour cover and comprises some 170 units. Service charges are projected at £4.20 per square foot including the estate charge contribution.

We are also instructed in respect of the Imperial Wharf development where average service charges per square foot are running at approximately £3.40. These charges



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are however assessed on the basis of the full stage one development which will comprise in excess of 1,100 units and therefore there are substantial economies of scale to be gained.

We also manage Regent on the River in Fulham, which comprises 255 units. Again there is 24 hour cover, with enhanced security overnight, and the building is split into ten blocks which means that there are additional services such as a larger number of lifts than you would expect. Including substantial reserve fund contributions for capital works over a phased 15 year programme, service charges are currently in the region of £5 per square foot.

There are a number of other properties where service charges are in excess of £4 per square foot and I could of course provide details of buildings where they are much lower. However those buildings would not be comparable in terms of either size or services / facilities.

It is important, when producing comparisons to look at the extent of services provided as the levels of service charge will be influenced substantially by matters such as levels of staffing, the extent of mechanical and electrical equipment, the window cleaning strategy (e.g. if cradle or abseil access is required then the service charge cost will be higher) and insurance where location and claims history is as important as the level of cover.

6. Conclusion

In so far as my review of the service charge has taken place to date I am content that the structure and apportionments are fair and reasonable and any adjustments or changes highlighted in this report should be investigated further and implemented as a matter of good management rather than being viewed as a deficiency in the previous arrangements.

With regards to service charge costs it is again in the interests of good management to review costs on a regular basis but I have found no evidence to date of anything substantial that I would class as being unfair or unreasonable.

It is my opinion that whilst every attempt should be made to reduce service charges (but maintaining service and value for money), the levels of service charge on a rate per sq. ft. basis for Canary Riverside are not dissimilar, and in some cases are lower, than similarly serviced buildings and estates where we have management responsibility.

20/23

Appendix A Service Charge Structure

