

Make the “Unknown” known – why early Service Charge budgeting matters

In my consultancy I often see a repeating challenge for sales teams, the known “unknown” of annual service charges. As a result, unsubstantiated figures create a lot of hassle in all project stages and few realise that the solution can be straightforward. What is meant to support the early sales effort does not have the desired effect, can even backfire.

One of the first questions every potential buyer asks about is the level of service charges. The running cost is the biggest “unknown” fact to all the sales agents, marketeers, developers and buyers. Numbers are frequently guesstimated to present a budget early on in support of off-plan transactions. Therefore, those numbers are often quite wrong as their method of validation is inaccurate. Subsequently, as the process is imprecise, the result leads to a lot of unsatisfied buyers and embarrassment all around when the “real” numbers are available.

The Drivers

In this short article I try to shed light onto the “unknown” issue to avoid the above complications. Mainly, it starts literally at the very beginning of your project and your vision. Furthermore, I will demonstrate that arriving at a fairly accurate number is possible in the early stages of your development process.

So, here are the main drivers for your budget: staffing, utility consumption, insurance, facility management, management fee and VAT – the rest is made up of smaller budgeting items, licenses etc.

The Process

You need a clear decision of the operational requirements at the beginning of the planning process. Firstly, you need to establish how you run and manage the building after practical completion. Secondly, how much staffing you require, in what capacity etc. This mandates a thorough understanding from all involved parties what the result will look like, namely designer, architect, developer. Thirdly, this also includes how you manage the project later, i.e. agency staffing, self-management or part of an integrated branded management platform.

The next stage is deciding the utility and operating costs for the building. Although, this is a bit more challenging as the exact numbers are only available in stage 3 and 4

with the start of the technical design and procurement process. However, a lot of the information can be pro-actively obtained from within the planning phase. With this ongoing intelligence, you can estimate a fairly accurate model. At the end, the figures can be substantiated after the actual asset register is available.

Following the operations cost, the next big item is the insurance value of the building. A point often overlooked is the fact that this number is twofold: one part is based on the rebuild-value and the other part is often the terrorism damage cover. Once you are in the last stage of the project, you get the exact values to confirm your initial number. The difference will not have a major impact on the budget if the initial due diligence has been exercised.

Facility management is another difficult number in this process as there are several “unknowns” here. To begin with, knowing what M & E equipment is used allows you to plan. Following that, finding out what amount of work is required to manage the daily operation is crucial. Lastly, visiting the building and seeing the installation allows you to calculate what needs to be done, by whom and at what level of service. Again, you need a high level of due diligence and discipline at this point. Having said that, to estimate the numbers at an early stage of the project requires collaboration across your teams. In the end, a massive swing should not occur at point of completion and a manageable figure is on the table.

Whether you manage the building yourself or outsource the contract, this activity will for sure incur a management fee. However, how to manage the building offers two possibilities: self-management or contract. In the first instance, if you manage the building you can apply a discounted rate or the full rate. In the latter instance, any third-party management company is charging the full amount. Those fees are typically around 8% to 10% of the budget.

Finally, VAT: is your service provision (staffing) VAT-able or are the colleagues employed by the building and therefore their services VAT-free? As before, you must answer this question at the very beginning of the project. Depending on the level of service envisioned, this is adding up very quickly. In case of third-party staffing, your VAT for this runs well over £50K - £100K per year, adding nearly £ 0.50 to £ 0.80 per sqft, depending on the size of your building.

The Outcome

The reason why this early calculation method is advantageous, simply lies in the higher accuracy and confidence of your approach to the market with your figures. On the negative side, a good number of projects in PCL start off-plan with a number that

grows over the course of the project by up to 20% to 27%! Imagine you invest in a couple of units and calculate your yield based on inaccurate information?

If you just copy what your competitor is doing, simply to be aligned with them, you make a big mistake. It is important to realise that each building is unique in its layout, operational management and design. Furthermore, you are wrong to use a “convenience number” to please the sales efforts. Therefore, working your agents and suppliers hard for realistic numbers is a short time pain outweighing the long-term gain of trust and reliability as operator/developer.

It is imperative for your brand reputation that getting those numbers as correct as possible the first time. To help with the outcome, building an 8% to 10% buffer for unanticipated events is good practice. As indicated, this buffer is for “surprises” - such as higher staffing costs due to new Brexit regulations or higher operating costs because COVID-19 mandates new cleaning and sanitation requirements and equipment. In any case, you want a small cash contingency too for last minute purchases.

Conclusion

MORICON supports you in all aspects of the service charge budget and pre-opening works and hospitality set-up. We assist your team throughout the project creating a realistic budget as early as possible and liaise with your suppliers to ensure your success. Hence, your sales team can with confidence do what they are meant to do: selling your dream whilst we make the formally “unknown” known and manageable.



Sebastian has more than 25 years of global luxury hospitality and customer service experience. He worked in senior management roles on three continents with a variety of hotel companies, including Fairmont Hotels and Resorts, Intercontinental, The Hazelton Hotel Toronto and Shangri-La Hotels.

His residential experience covers senior management roles at [One Hyde Park Residences](#) (Mandarin Oriental Group), [Ten Trinity Residences](#) (now Four Seasons Hotels) and [Belgravia Gate](#), before founding MORICON Consultants. He consulted [Lodha Group UK](#) on their three London projects – Lincoln Square, No. 1 Grosvenor Square and Kensington Odeon with a combined sales value of £ 1.6B and provided strategic advice for the [Amaala Project](#) in Saudi Arabia, a new super-prime resort destination at the coast of the Red Sea.

Professionally educated in Switzerland, he holds an MBA from Henley Management College. Sebastian has Member status at IRPM and Assoc. RICS and achieved Level 4 BTR Accreditation from IRPM.

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