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**ADAPTATION OF BEST VALUE SERVICE ON RATIONALISATION OF SERVICE
CHARGE FOR PURPOSE BUILT OFFICE (PBO) IN MALAYSIA**

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Abstract:

As certain types of property has become more complex and both customer and occupier expectations have changed; the services provided by the owners have increased in scope. A modern service charge may therefore include provision for the recovery of a multiplicity of services. In Malaysian scenario, the calculation of service charge for PBOs is therefore deceived since service charge is embedded in the rental charge to tenants. In addition, the existing practice of rental rate for PBO is not transparency enough to educate the tenants in knowing what they could get from the portion of service charge that they are paying. This paper represents an outline on issues in regards to service charge generally and to the commercial property specifically. A comparative overview between Malaysia and the UK perspective involving relevant codes, best practices and legislative standpoint in governing service charge are the core elements of discussion.

Keywords search: service charge; office lease; office rental; building types; facilities management; services; maintenance charges; lease valuation; management fund; sinking fund; outgoings; commercial real estate; landlord and tenants.

1.0 INTRODUCTION

The modern office building is a more than a “place for transacting business”. It is an “information factory’ where value is added to information for the benefit of customers or client. Office building therefore represents a vital part of our nation’s economic prosperity, providing a significant tax base, an important source of foreign funds and one of the principle investment mediums for our financial institutions. Office building also plays an important role in our cultural and social existence. Their contributions to the architecture of our cities and the economic viability of associated activities including retailing, leisure and support services are immense. Furthermore, they provide an essential setting for personal relationships to be formed and for social interaction to take place. Without office buildings, the lives of many would be barren and lifeless (Markland, 1995).

Service charge for purpose built office (PBO) may include provision of a multiplicity of services and sinking fund. The calculation of service charge is therefore unclear since it is embedded in the rental rate of the lettable space of the purpose built office. In addition, the existing practice of chargeable rental rate for PBO is not transparent enough to educate the tenants in knowing the equivalent value of services that they are entitled to from the payment of the rent. Many property managers has defined service charge as:

“The amount of contribution levied by the owner or developer of a complex on an occupier for providing services, common facilities and the maintenance and upkeep of common property”.

And they go further to say:

“Generally in practice ‘service charges’ is a term used loosely to cover for both items of service charge and maintenance charges”.

According to some , service charge is defined as sum of money payable by a tenant on account of services provided by the landlord and is often collected quarterly in advance at the same time as the rent. The service charge is the means by which an owner is able to recover from the occupiers the cost of providing the services for the benefit of those premises (Singh, 1993). The service charge costs may also include enhancement of the building features and services. Tenants of PBO are hit by surprise when the building owner or the property manager of respective PBO transfers the cost to the tenants proportionately to the occupied space that they rent. It is

important for the owners to provide facts and figures to justify the breakdown of charges and the needs of such improvements. This will allow tenant to understand the basis of what are they paying for and in return, benefits them in term of improvement of quality of facilities and services rendered by the building owner.

It is fundamental that landlord and tenant understands each roles and responsibilities in order to minimise the perception and expectation gap in regards to payment rental and service charges imposed by the building owner to the equivalent best value and quality of services received by the tenant. A justifiable service charge apportionment mechanism should rest on the principle of 'what you pay is what you get'. As a result, a valid and sound equation that explains the quality of facilities related services rendered by the landlord to the charges paid by the tenant of PBOs is served.

As certain types of PBOs has become more complex and both customer and tenants expectations have changed; the office building owners are challenged to provide quality facilities related services (Calvert, 2005). Describing a service is "one of the most difficult aspects of dealing with a service" (Shostack, 1992). The service charge element that is imposed to tenant as part of the chargeable rental rate composition should explicitly justify the value and quality of services rendered to at least meet the expectation of the tenants and building occupiers of the premise.

Best Value arrangements originally exist to secure continuous improvement in the performance of functions by public service organisations. The theory of Best Value is that the results of service reviews feed directly into an action plan that in turn leads to improvements (Entwistle et.al 2003). Best Value is viewed as a useful management tool which has helped to focus on specific service issues, improve the budget process and identify what service users want.

Continuous improvement seeks to balance quality and cost considerations, and is achieved with regard to economy, efficiency, effectiveness and rests on equal opportunities arrangements. While the accountability for service charges, budgetary control and certification of actual costs incurred are all matters that demand considerable attention (RICS, 2006). Therefore, for the purpose of this research, the adaptation of best value towards service charge concept is seen to be appropriate in resolving the dilemma due to its equality in fulfilling the needs and expectations of both owners and tenants in harnessing a sound landlord-tenants relationship.

2.0 RESEARCH BACKGROUND

Kuala Lumpur is known as the soul of Malaysia commercial centre. Hence, there is direct relationship between the growths of Kuala Lumpur to the economic growth of Malaysia. Therefore, for the purpose of this research, PBOs in Kuala Lumpur is selected to represent other cities in Malaysia. In addition, it is evident that Kuala Lumpur commercial property sector is getting into the spotlight again after succumbing to a massive slowdown during the regional financial crisis.

Currently, the overall supply of office space in Kuala Lumpur city centre stands at approximately 66 million sq ft with a total occupancy rate of 82% (NAPIC, 2005). Within the central business district alone, the supply of prime office space totals 17 million sq ft with an average occupancy rate of 90% while in the fringes of Kuala Lumpur, there are some 4.5 million square feet of space with an average occupancy of 84%. In addition, there will be at least 4.5 million square feet of net lettable office space coming on stream from now to year 2009 (Ng, 2006).

This favorable scenario is further supported by the upwards trends of rental rates that reached between RM 5.00 to RM 10.00 per square feet (Ng, 2006) from the previous year rental rate of RM 4.00 to RM 5.50 per square feet. The entire rental quoted is net rental rate which is inclusive of service charges.

In Malaysia and more specifically Kuala Lumpur, where serviced offices have been around for more than 15 years, monthly fees can be as much as RM6,300 (Lim, 2005). There are numerous factors that lead to the upbeat of rental rates in the office sector. Among the attributes that are indicated in the 2006 Global Office Occupancy Costs are excellent infrastructures, exemplary governance and favorable economic climate. Inevitably, one of the main issues faced in the management properties of Malaysian PBOs is the high rate of default in the payment of the service charge (Chan, 2005), There are many reasons, either valid or lame excuses, for non-payment of this charge. The common complaint is that it is too high, or that there is a lack of transparency in the way the charge is calculated.

While landlord and property owners harvesting their return on investment via increased in rental income in the commercial sector, it is also instrumental for them to justify the composition of rental charged to the tenants. Service charge for instance, contributes approximately 20 to 35 percent of the rental rate chargeable to occupier (Chan, 2005).

A service charge usually arises when a property is in multiple occupations. Typical service

charge items cost of maintaining common parts of the building and a proportion of the cost of insuring the premises where the landlord is responsible for insurance (RICS, 2006).

Service charges are levied by landlords to recover the costs they incur in providing services to a dwelling or a commercial space. The way in which the service charge is organized is set out in the tenant's lease or tenancy agreement. In particular, a service charge includes the repair and maintenance of the external or structural parts of a building and normally covers the cost of such matters as general maintenance and repairs, insurance of the building and, where the services are provided, utility charges, lifts, security services, lighting and cleaning of common areas and other related facilities management services together with managing agent's fees and a sinking fund. A service charge payment can be capped in order to limit the amount of a tenant's financial liability (Global Office Search, 2006).

The charges may also include the costs of management by the landlord or by a professional managing agent and for contributions to a reserve fund. Details of what can (and cannot) be charged by the landlord and the proportion of the charge to be paid by the individual leaseholder will all be set out in the lease. The landlord, or, sometimes, a management company that is party to the lease, provides the services, while the leaseholders pay for them. The landlord will generally make no financial contribution, but sometimes has to pay for the services before he can recover their costs (Singh, 1996)

3.0 THE ISSUE WITH SERVICE CHARGES

“Service charges are the costs of the services provided to common parts of a building that are shared by the tenants and paid to the landlord in addition to the rent.” (Calvert, 2005).

Landlord is particularly inflexible on new ideas especially on service charge (RICS, 2006).

Landlords are driven by the old adage that *“... if it is not possible for me as the landlord to pass to you the tenants the total responsibility for repairing, maintaining and insuring the building, then I must undertake these functions and you must pay. Therefore I will expect repayment from you and I shall bill you accordingly.”* (Singh, 1996)

Theoretically, the landlord has to buy all the services before he is reimbursed. If the lease allows him to recover interest, then at least he can afford to fund the costs, but if not, it costs the landlord to provide the services, which may make him reluctant to fulfill his obligations. Generally, in return for the ability to levy a service charge, the landlord is under an obligation under the lease

to provide the services.

Originally, any properties do not have service charge budgets. As for the rental charges of PBOs, the costs of services were included in rental payments, but as costs and inflation escalated, landlords would want to make sure they recovered all their costs every year. Some old leases still provide for a fixed charge to be levied. Accordingly, these charges cannot be varied, regardless of the actual costs to the landlord. However, most service charges are based on the actual or estimated cost of the services and thus vary from year to year. These are known as variable service charges.

The lease will dictate the format of the charge. It will usually give the dates of the service charge period. More often than not the period is a year, but sometimes it is a half-year or a quarter. The lease will usually set out the percentage payable by the lessee, but sometimes the lease just stipulates a 'fair' or 'just' proportion. If differing groups of occupiers benefit from different services, there may provision for more than one percentage to be paid. The lease will say whether advance payments are to be made and, if so, whether they are based on the previous year's cost or an estimate of the cost in the year to come. There will always be provision for a final charge at the year end when the actual costs are known. If interim payments have been made, and they exceed expenditure, the final 'charge' will be a credit. If the leases in a block do not provide for interim payments, that can present a real difficulty for all concerned.

There are numerous complications arise from the sole reliance of lease agreements as the determinant to govern the mechanism of service charges. The ignorance of the landlord and tenants in familiarization of the lease agreement contents for instance has made it worse since more than often that both parties blatantly empowered the solicitor in drafting the lease agreement without scrutinizing the contents of the document. This has also led to inconsistency in the charging of service charge since all leases are specific to a building and a landlord thus there is no standard approach to service charges as to what is mode of facilities are suppose to be included.

Calvert (2005) in his research has further indicated that the trouble with service charge in commercial real estate lies in the diverse responsibilities of various parties involved. It is evident that the business elements of service charge mechanisms are not linked up and owned by a single party.

In tandem, Calvert (2005) in his seven years research on service charge for commercial buildings in the UK has also indicated that the country is vitally in need for a national code of practice for service charges instrument. A new established Code of Practice entitled *Service*

Charge in Commercial Property by RICS has been introduced and will be effectively applied by April 2007 emphasizes on agreed service charge apportionment. This new guideline, produced through years of best practice implementation derives the elements for cost classification by managing agents through strict monitoring by the appointed government agency.

4.0 SERVICE CHARGES AND MALAYSIA SCENARIO

Malaysia has a range of policies and regulations also known as the Traditional Regulatory (TR) which is typically characterized in the form of Acts, Ordinance and Building Codes. It generally focuses on development elements including land, building layout, environmental assessment and infrastructure provisions. There are rarely additional requirements and virtually no flexibility for developers or builders to apply innovative solutions to service charge (Zakaria and Yang, 2005).

In the Malaysian context, service charges have not been defined under any existing law. The only statutory instrument that make reference to the term service charge is Section 16 of Schedule H of the *Housing Developers (Control and Licensing) Act 1966, and Regulations 1989 (Amendments)*. However, there is no explicit definition of the term service charge and this statutory instrument has limited application as it only covers residential strata type developments.

Elsewhere, the Strata Titles Act 1985 makes reference to the term “*management fund*” which is considered to be equivalent to the service charge but not make any reference to the precise term. The *Land (Subsidiary Titles) Enactment No 9 of 1972* of Sabah also refers to the term “*Management Fund*”.

To Singh (1996), tenancy agreements drawn up by solicitors have commonly employed the following definition of service charge:

“Service charge means the amount of money determined from time to time by the landlord and includes the costs of maintenance and upkeep of the lifts and air-conditioning plant, payment for electricity and water supplied and used in the common property of the building including the employment and other expenses incidental to the employment of personnel engaged in and about the provision of service, maintenance, upkeep and security of the common property of the building and insurance of the building”.

It is quite obvious that while there are laws which make reference to service charge, none of them defines the term and the situation is made worse by the fact that the different laws provide different terms. The situation is further exacerbated by the fact that there exist no comprehensive

laws which govern tenancies other than the *National Land Code* to provide an all embracing definition of service charges.

Looking beyond our shores for guidance, the Glossary of Property Terms (*Estates Gazette*) defines service charges as:

“The amount payable by a tenant on account of the services provided by his landlord. In the specific case of residential flats, as defined for the purpose of Sections 18 and 30 of the Landlord and Tenant Act 1985 (applicable only in the United Kingdom), this means an amount payable by a tenant as part of or in addition to rent for the services, repairs, maintenance or insurance or the landlords costs of management, the amount varying with the relevant costs (including overheads)”.

Section 18 of the Landlord and Tenant Act 1985 (UK) defines service charge as follows:

“Service charge means an amount payable by a tenant of a dwelling as part of or in addition to the rent:-

- a. Which is payable, directly or indirectly, for services, repairs, maintenance or insurance or the landlord’s costs of management, and*
- b. The whole or part of which varies or may vary according to the relevant costs.”*

Service charges have been defined as the levy made by a landlord on a tenant for the provision of housekeeping, maintenance and replacement services. Other have defined it as a charge to ensure that the landlord recovers the rent payable under the lease free from the risk that he will have to spend part of it on maintaining or repairing the demised property or otherwise incurring running costs.

Service charge has also been defined as the charge for those items of expenditure the execution of which, under the terms of the lease or tenancy are the responsibility of the owner but the total cost of which is to be met by the tenant and the items included would not only be the shared services but also the insurance and maintenance of the building as a whole. The starting point for calculation of service charge is the day the Certificate of Fitness for Occupation or CF is issued, and where the common areas are clearly defined

In the United Kingdom, in essence the service charges are the means by which the landlord is able to recover from his tenants the cost of services carried out for the benefit of the tenants and

the building.

It is obvious that by virtue of service charges being defined in various codes and best practices, the ensuring interpretations of service charges have been more precise in the United Kingdom and this has ensured uniformity in the provisions of lease agreements. In addition, the leasehold valuation tribunal is established in the UK to resolve any disputes between landlord and tenants which includes service charge disagreements.

(i) Service Charges in Sub-Divided and Non Sub-Divided Buildings

What all of the above mentioned definitions convey is the message that all buildings in multi-occupation have to establish service charges which will pay for the costs of services carried out for benefit of the occupants and the building as a whole. In Malaysia, buildings in multi-occupation can be of three types.

The first type is one where individual units of the building are sold on a strata basis each of which will be given a strata title and these units can either be owner occupied or tenanted out.

The second type is a building that is owned by a single proprietor and is leased out to numerous tenants and the third type is one that has a mixture of the earlier two types. The buildings in multi-occupation referred to comprise of purpose built office complexes, shopping complexes, flatted factories and residential apartments and condominiums.

All types of subdivided buildings be they residential, commercial (office and shopping complexes which have been sold individually on strata basis) or industrial (e.g. flatted factories), are subject to the provisions of the Strata Titles Act 1985 Act 318 (as amended).

Section 39 of the Act states that *“upon the opening of a book of the strata register in respect of a subdivide building, there shall come into existence a Management Corporation”*.

Section 14 of the *Sabah Enactment No 9* also states that as soon as a file of the subsidiary register is opened in respect of a subdivided building, a management corporation consisting of all the subsidiary owners shall be established.

Section 41(5) (b) outlines one of the first duties of the corporation, namely *“to decide whether to conform or to vary any amounts determined as contributions to the management fund”*.

Section 19(3) (a-b) of the Sabah Enactment similarly states that the management corporation may determine from time to time the amounts to be raised for the management fund.

Neither the Act nor the Sabah Enactment makes any explicit reference to the term service charge but refers to the term '*management fund*' in Sections 45 and 63 of the Act and Section 19 of the Enactment.

For residential subdivided buildings, the first encounter with the term 'service charges' is when the purchaser reads through the standard sale and purchase agreement. The provision of importance here is Section 16 Schedule H of the *Housing Developers (Control and Licensing) Act 1966, Regulation 1989* which reads as follows:

"The Purchaser shall be liable for the maintenance and management of the common property and for the services provided by the Vendor prior to the establishment of a management corporation under the Strata Title Act 1985."

Schedule H falls under the Standard Sales and Purchase Agreement. The service charges are paid to the vendor or developer. There is no explicit definition of service charges but when it is read in conjunction with other provisions of Schedule H it can be taken to mean the expenditure incurred in the maintenance and management of the common property.

Section 31 of Schedule H of the Housing Developers Act defines common property as:

".....so much of the land as is not comprised in any parcel (including any accessory parcel) or any provisional block and the fixtures and fittings including lifts, refuse chutes, drains, sewers, pipes, wires, cables and ducts and all other facilities and installations used or capable of being used or enjoyed in common by all the purchasers".

This definition is more detailed compared to the definition of common property accorded in the Strata Titles Act 1985 which reads as follows:

"Common property means so much of the lot as is not comprised in any parcel (including any accessory parcel), or any provisional block as shown in an approved strata plan".

This definition is similar to the definition of common property in Section 2 the Land (Subsidiary Title) Enactment No 9 of 1972 of Sabah which reads:

“Common property” means in relation to a subdivided building:-

- a. The land on which the building stands, together with so much of the building as is excluded from the parcels and
- b. The remainder of the lot, together with any other building standing thereon.

This means that as far as residential subdivided buildings are concerned the common property and the constituents of service charges are defined twice i.e. once in Schedule H and once in the Strata Title Act. It is also defined in the Sabah Enactment.

This preference is only accorded to residential buildings as there are no other statutory provisions which govern commercial and industrial subdivided buildings other than the Strata Titles Act 1985 and the Sabah Enactment No 9 of 1972.

As stated previously there seems to be a general perception that service charge is similar to the management fund. The *Sabah Enactment* explains the use of the “management fund” for the purposes of controlling, managing and administering the common property, paying rent, rates and premiums of insurance and discharging any other obligation of the management corporation.

This means that the management fund includes items such as quit rent and assessment, which as we know it are the prerogative of the parcel proprietor as these items are normally explicitly specified in tenancy agreements as being the responsibility of the landlord. Therefore, it is apparent that insufficient thought has gone into the specific definitions of “service charge” and “management fund” in the Housing Developers Act and Strata Titles Act.

This loose usage of service charge in one legislation and the non-reference to it in another will eventually lead to confusion and perhaps the exploitation of the tenant in the event the management fund is taken to be equivalent to service charges (Singh, 1999).

It is reiterated here that the provision for services charges in the Standard Sale and Purchase Agreement are only mandatory for residential development as defined in the Housing Developers Act. As Schedule H is not applicable to subdivided commercial and industrial development, the inclusion of service charge provisions in the sale and purchase agreement is open to contractual arrangement but with reference to the *Strata Title Act 1985* and the *Sabah Enactment No 9 of 1972*.

For non-strata titled buildings which are rented to various tenants, the landlord recovers service charges by incorporating various clauses in the tenancy agreement making it the obligation of the management and maintenance of the common property of the building.

The definition of “common property” commonly employed in tenancy agreements is:

“Common property means in relation to the building:

- i. That portion or portions of the said land on which so much of the building stands together with so much of the building as is excluded from the individual parcels of the demised area and car park at the building; and
- ii. The remainder of the said Land together with any other building standing thereon”.

These different provisions do not rely on any statutory instruments and are also open to contractual arrangement. This has inevitably led to a diverse approach and resultant inconsistency in the application of service charge provisions and definitions of common property in tenancy agreements.

(ii) The Constituents of Service Charges and Outgoings

Many researchers have attempted to break down service charge into components or dimensions. However, there often seems to be confusion between components of the service itself and the components of its apportionments. In the complex environment of services, it is difficult to use objective constituents for determining its role. Most of the services incurred in managing a property as an investment is commonly defined as ‘outgoing’. More precisely outgoings are defined as follows:

“Outgoings are the cost incurred by the owner of an interest in property, usually calculated on a yearly basis, e.g. management, repairs, rates, insurance and rent payable to the holder of a superior interest, as appropriate to his contractual or other liabilities. It is prudent to make annual provision for future items involving expenditure at intervals of more than one year”.

Schedule G and H of the *Housing Developers Act* do not define outgoings but refer to it as all that including quit rent, rates, taxes, assessment and other charges. Based on the two definitions above and the previous definitions of service charges it can be deduced that part of the outgoings are attributable to service charges. Thus the basic formula is:

$$\text{OUTGOING} = \text{SERVICES CHARGES} + \text{EXPENDITURES}$$

Service charge provisions are incorporated in tenancy agreements to ensure that the landlord's capital asset is being maintained at the tenant's expense. From the tenant's point of view, especially where the building is in multiple occupations, a uniformity of service charge is guaranteed together with a sensible and economical method of keeping the property in shape.

However in practice, tenants often complain that certain services are not being provided or that the services are of a poor standard. Sometimes the tenant even goes to the extent of accusing that the services are too extravagant. The tenant always suspects that he is paying too much for too little.

The constituents of service charge will vary according to the type of building, type of usage, size, term of tenancy or lease agreement as well as any explicit definitions in the agreements.

Through examination on various publications, policies and papers, it was noted that a service charges normally cover the following items:

1 Lifts and escalators	24 All common area electrical consumption and central air conditioning electricity consumption.
2 Air conditioning system	25 All common area water consumption and sewerage charges
3 Standby Generator	26 Car park license
4 Fire fighting system	27 Costs for fixtures and fittings
5 Electrical installations	28 Lightning protection equipment: Repairs and maintenance, contract costs
6 Refuse compactor	29 Building automated systems: Repairs and maintenance, contract costs
7 Automatic sliding doors	30 Public address systems
8 Flood gates	31 MATV and CCTV systems
9 Automatic car park barrier gate	32 Music royalty
10 Façade gondola	33 Advertising and promotions
11 Watchman's clock	34 Radio pager for management staff: Rental, license and repairs
12 Cleaning services	35 Sinking funds
13 Security services	36 Financial expenses on money borrowed for the maintenance of the complex
14 Landscaping	37 Insurance premiums
15 Name sign	38 Professional property management fees
16 Tenants directory	
17 Swimming pool	
18 Gymnasium/games rooms	
19 Squash court/tennis court	
20 Pest control	
21 All general repair and maintenance carried out on the building	
22 All sundry expenses incurred for the building	
23 All employment charges for labour directly employed for the management of the building	

The second part of the formula is 'Other Expenditure' which normally consists of quit rent, assessment, all other rates, duties, taxes, charges and other payments imposed by government and or other statutory/local authority charges and expenditure of a capital nature for the asset.

According to the RICS *Code of Practice*, the service charge apportionment has been classified into seven cost headings that further determine the rate of service charge to be imposed. The cost headings; management, utilities, soft services, hard services, income, insurance and exceptional expenditure cover a wide range of service activities that distinguish the base operational cost to allow benchmarking basis to take place (RICS, 2006).

In the United Kingdom the court have made it clear that interest can only be recouped through the service charge if the lease agreement expressly permits it (**Frobisher Second Investments Ltd v Kiloran Trust Co. Ltd (1980) 1 All ER 488 and Boldmark Ltd. v Cohen and Others (1985) 277 EG 735**).

Tenants must pay service charges but they have a right to know what they are paying for and whether it is fair and reasonable (**Finchbourne Ltd v Rodrigues (1976) 3 All ER 581**). However, it would be irrelevant for the tenant themselves if they wouldn't care less on what they are paying and have been paying for. This is true in the Malaysian scenario whereby on top of the tenant's ignorance, various parties involved in property leasing transaction has their own hidden agenda. This then leads to the next issue of service charge apportionment and service charge accountability (Singh, 1996).

5.0 BASIS APPORTIONMENT OF SERVICE CHARGES

As we have pointed out earlier, the apportionment of elements that quantify to the price of service charge should be justified. The apportionment must rest on the basis of "not for profit, not for loss" and value for money for respective parties in the lease or tenancy (RICS, 2006).

This tenancy or lease will normally establish the basis on which the service charge costs are to be apportioned. Where the property is a strata titled property, then the sale and purchase agreement will be this legal document to spell out the basis of apportionment (Singh, 1996). Tenancy agreements also spell out the basis but in more simplified terms.

There are several methods that are used in determination of service charge for commercial buildings. RICS (2006) indicated that the most common bases of contribution are; a fixed amount; a fixed percentage; weighted floor area and a fair reasonable proportion. However, the most common method used in practice is on the basis of floor area occupied where the service charge payable is that proportion of the total costs which the floor area of the unit bears to the overall floor area.

A more equitable basis would be to use a differential rate for the common areas and other ancillary accommodation such as hawkker centers, recreational accommodation and conference rooms (Singh, 1996).

The Strata Titles Act does not prescribe the method of establishing the share units i.e. whether it should be on the basis of floor areas, usage or property value of the parcel. Section 9(g) merely states that the share units must be equitable.

Another method of apportioning service charges is by referring to the rateable values of the property. The disadvantage of this method is that rate able values can change and that the determination of the rates is outside the control of the interested parties. Service charges are controllable costs but the tenant does not have any automatic input into their management (Singh, 1996; RICS 2006).

6.0 SERVICE CHARGES ACCOUNTABILITY

This is perhaps the most contentious issue concerning service charges. Most tenancy agreements state that in the event that service charges are increased, the tenant has to bear the increase. Often no mention is made of the reverse case where in the event that service charge collected more than the actual costs are. What happens to the surplus money?. Naturally landlords prefer to be silent on this matter as it is indeed additional income to them.

There is a need to ensure more accountability in service charge accounting. The case of **Finchbourne Ltd v Rodrigues (1976) 3 All ER 581** makes it clear that the charges must be fair and reasonable. The property personnel involved in ascertaining service charges must show professionalism.

In view of this, it is recommended that service charge accountability is enshrined within tenancy agreements and sale and purchase agreements for strata parcels. Some measure of service charge accountability can be seen from Schedule H of the Housing Developers Act in Section 16(3) which states that every written notice to the purchaser of a subdivided parcel requesting for the payment of service charge statement issued by the Vendor.

Singh (1996) has recommended that the following treatment of service charges must be considered for implementation:

- a. The constituent items of service charges must be judiciously established having regard to the length of the tenancy/lease.
- b. The initial expenditure for the service charge is first estimated at the beginning of the first year the building is tenanted and the tenant is required to pay the service charge quarterly in advance.
- c. As soon as practicable after the end of the first and subsequent accounting years, the landlord must engage auditor to prepare an account to be certified as true relating to the service charge amounts.
- d. If the service charges for the end of the first year exceed the sum estimated in the beginning of the first year, the amount of the excess must be paid by the tenant to the landlord.
- e. If the service charges are less than the amount estimated in the first year, the amount of overpayment must be credited to the tenant against the next payment of the service charge and in the case of the last year of tenancy is should be refunded to the tenant upon demand.
- f. All sums received by the landlord as service charge must be held by the landlord in trust during the periods of all tenancies.
- g. The landlord will use the service charge for the use the charges were intended for and must not exercise any use for his own benefit or in any manner inconsistent with the purpose of this trust.
- h. If the tenant disputes any of the items in the service charge list, the tenant must within one month of being informed of the service charge make it known to the landlord.
- i. The dispute must then be determined by a registered valuer/property manager, agreed upon by the landlord and tenant or in the event this is not agreeable, within one method, a registered valuer/property manager nominated on the application of either party in writing by the President of the Institution of Surveyors Malaysia or the President of the Board of Valuers, Appraisers and Estate Agents Malaysia. The registered valuer/property manager appointed either by the two parties in dispute or by the President is appointed not as an arbitrator but as an expert. His fees shall be borne equally by both parties.
- j. The tenant cannot dispute the cost of any of the work or service included in the calculation of the service charges on the grounds that the work can be carried out at a cost less than what the landlord had actually incurred or estimated in good faith.
- k. In the event there is a dispute, the tenant must not withhold payment of the service charge. The payment will have to be made by the tenant 'under protest'. Where there is an over or

under payment an appropriate adjustment will be made.

- I. Where the landlord deems it is desirable in accordance with the principles of professional property management to add, subtract vary or change any of the service charge components, the landlord will give all tenants written notice of such changes and the change in the cost. The landlord will have the right to implement such changes within two months after informing all tenants unless the landlord receives written objections from the tenants within one month of the date of the notice.

7.0 SERVICE CHARGE IN COMMERCIAL PROPERTIES

In the case of commercial leases such as purpose built office buildings, the service charge payments are expressed in the same manner as rent. The significance of reserving the service charge as rent is that if the tenant defaults the landlords can distraint for the whole sum owing (both rent and service charge). Distraint (whereby the tenant's goods are seized by the bailiff to make good the loss to the landlord) can only be levied in respect of rent or items reserved as rent.

If the service charge and rental components are expressly separated in the tenancy agreement, then the service charge is not reserved as rent and the landlord does not have the right to distraint for the service charge elements, although he has the right to distraint for the rental element (**Concord Graphics Ltd. v Andromeda Investment SA (1982) 256 EG 386**) (Singh, 1996).

The landlord, however still has a right to take action against the tenant for a breach of the agreement. There is also an advantage in separating the service charge from the rent whereby such arrangement attracts a lower Stamp Duty. However, the landlord must weigh the advantages and disadvantages carefully.

Service charge provisions must normally endeavor to identify all the items of service charges that are known and in respect of which the landlord requires the tenant to reimburse him. However, there are instances where items may be omitted in error or circumstances where the premises and the expectations and requirements of tenant change over a period.

It is quite obvious that the longer the tenancy or lease, the greater are the chances of changes in the normal standards of amenities required by tenants and provided by landlords. For example, techniques of building are changing and commercial and industrial premises might in the near future opt to utilize solar panels to supply the energy required to run the building if it proves to be cheaper than conventionally generated electricity.

It is therefore to have a 'sweeping up' clause in the agreements which would provide the landlord with the means to recover through the service charge the maintenance costs of additional facilities provided for the benefit of the tenant. The clause must of course be drawn up suitably so that the landlord is not given a blank cheque to provide a lot of amenities that the tenants do not want.

Due to the complication and uniqueness in determination of service charge for commercial properties, Chan (2005) has indicated that there is a significant need of proper study and analysis to determine the actual service charge that can be fairly imposed for commercial properties in Malaysia as there is no two buildings can be the same.

8.0 CONCLUSIONS

Malaysia's landlord and tenant law, in many respects, is still in its infancy. (Buang, 2004). Even in the UK, commercial service charges are mercifully free from regulation by parliament and are entirely contractual in nature, i.e. governed by the lease itself (Marco, 2006). The newly established RICS Code of Practice on service charges in commercial property that will commence in April 2007 is identified to be the main references to implement best practices in the UK commercial leases.

From the foregoing, it is evident that there is a dire need to establish an equitable balance between the landlord and the tenant insofar as service charges are concerned. Both the tenant and landlord have a right to know what the constituents of service charges are and both must have a recourse to question if there any element of an unjust nature. It is felt that this can be achieved by revamping the present mechanism of providing clauses in tenancy agreements on service charges.

Together with this, a proper definition of service charge should be adopted for multi-tenanted buildings. The present situation where different legislations make reference to different terms concerning service charges must be clarified. There should be some form of continuity and not confusion between the different legislations.

Perhaps a step forward would be to ensure that all sale and purchase agreements of strata titled buildings have provisions for service charges instead of the present situation where only the standard sale and purchase agreement for residential strata titled buildings makes explicit provisions in the present standard sale and purchase agreement are sufficient. There is certainly scope for improvement.

An important lesson of the reviews is that the Malaysian scenario lack the information required in determining the apportionment of service charge. What is important is to introduce a mechanism to ensure that the collection of services charges is equitable to both the landlord and the tenant. The final situation should not give either party any unfair advantage over the other. In Malaysia such a mechanism is needed in the absence of adequate legislation to protect the tenant and landlord.

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