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Estates Gazette

Focus: Overseas

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Find assets under the floorboards

The numbers game Realising all the assets available from a property deal requires attention to accounting details that a forensic property audit can provide, writes *Martin Brownstone*

Property management is seen as the least flamboyant discipline in the property world – it is the deal makers who receive the plaudits. However, behind every property deal is a requirement to manage and account for that asset acquired and this falls to the property manager or finance director.

Having worked for a landlord, managing agent and a corporate occupier, I have witnessed at first hand when and why assets go missing or payment problems arise.

Forensic property auditing recognises this requirement and ensures that a transaction and its management thereafter have been conducted to the letter of the agreement or lease. It is not the job of the auditing consultant to consider whether a transaction was a favourable one. What he does consider is that the deal was accounted for correctly.

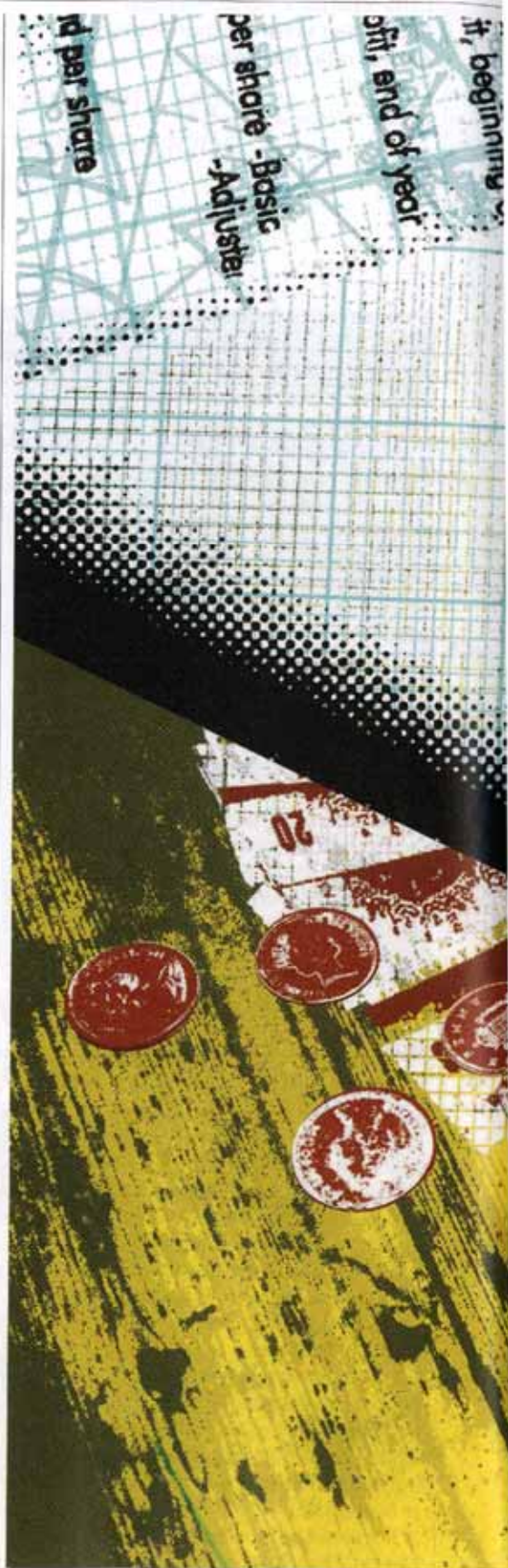
Because property is their sole business, landlords and developers already have expertise in the areas of collecting rent, service charges and insurance premiums. However, some accounting issues, such as VAT, may not be appreciated and landlords and developers could be missing the opportunity to recover monies from Revenue & Customs.

Equally, there are opportunities in connection with business rates where a whole host of reliefs may come into play. Landlords and developers appreciate the importance of getting property administration correct by applying the correct resource.

Different priorities

On the end side of the spectrum is the corporate occupier, such as a multiple retailer, warehouse or trade counter organisation, which has selling and operational matters as its prime focuses. The main concern of a multiple retailer is to maximise sales and ensure that stock is held in the right location at the right time. As a result, the retail and stock departments receive significant monies while the property and human resources functions are seen as necessary evils. This is inappropriate when property costs alone are one of an organisation's major expenses.

An effective property audit should ensure that what has been agreed by a corporate occupier is reflected in the demands of the landlord. Overcharging, mischarging, overpaying and misprocessing can be rife in any organisation, and the more transactions that



Income

12,850,000	1,122,627
9,151,069	2,636,734
<u>9,600,945</u>	<u>4,734,819</u>
(4,026,945)	<u>(2,711,245)</u>
5,184,765	4,463,627
<u>(2,188,827)</u>	<u>(66,914)</u>
2,995,938	
(38,113)	
<u>3,644,386</u>	<u>2,344,768</u>
	6,741,481
	<u>(4,455,454)</u>
	2,286,027
	<u>(838,252)</u>
	1,447,775

and other assets

24	6,602,211	
23	<u>(5,182,192)</u>	
	1,420,019	
25	<u>(452,871)</u>	
26	967,148	

TAXATION

St. Mary's reserve
land med...

go through a property function and the greater the unit cost, the more monies can haemorrhage away.

Forensic auditing follows the lifecycle of a tenancy from conception to termination. It ensures not only that initially the incentive is collected, but also that VAT is accounted for on the completion statement. I have a certain amount of sympathy for a client which, owing to changes in personnel, failed to collect its £100,000 capital contribution for moving into a shopping centre.

Problems can occur in respect of overpaying rents. Again, I draw from my experience in looking after a corporate portfolio. A landlord rang us shortly after a quarter day to tell us that we had double paid, then kindly asked us what we would like him to do with the overpaid sum. I admire such landlords and managing agents that pick up the phone to advise of such errors. The worry is that most landlords are not so candid.

Consider service charges. These are usually shrouded in mystery and the recipient has little time, resource or expertise to consider them in detail. As a consequence, such payments can be signed off when it is not known whether capital items or promotional costs have been included when there is no covenant in the lease, or whether there is excessive management charges. Without the proper attention, unscrupulous landlords can take advantage of their tenants' ignorance.

It is fair to say that service charges are not the biggest part of property costs. However, I recall a recovery for a client occupier who had been wrongly charged £500 per quarter on a standalone property in a high street. Going back six years, the recovery amounted to £12,000 – a substantial sum.

Bad side of business rates

Never assume that the business rate demanded is correct. Without wishing to sound too alarmist, for our retailing clients, we are typically able to identify a business rates recovery in one out of five properties.

Although most corporate occupiers will retain agents to negotiate rateable values, this is only the start. I believe that all agents – acquiring, disposing, rating or professional – have the easy job in merely negotiating a figure or deal. Following a rateable value reduction, we are reliant on the billing authority not only charging correctly but also dealing with any refund, interest and a host of reliefs. The clearest opportunities for error relate to splits and mergers and their effects on transitional relief.

Errors created, knowingly or unknowingly, by landlords are particularly difficult to detect. There are numerous safeguards that a corporate occupier can put in place by efficient reporting. It is important to focus on the detail of any particular property and its individual costs. A standard monthly management report suggesting that the property



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department is at variance of 1% under budget is insufficient when there are numerous factors in the equation, such as rent review settlements coming in under budget, business rate refunds and service charge credits.

Although utility costs are relatively small, there are still opportunities to make recoveries, which require external expertise. In one instance, an occupier relocated to an office building and the council granted it a section 44A discretionary business rate relief that affected sewerage charge, resulting in a recovery of £35,000.

Property auditing needs a holistic approach that draws on information from all functions of a business – the property, accounts, marketing and building services departments. For building services, fitting-out works may affect liabilities. The problems arise when an individual in a department in a large company does not know what others around them are doing. Internal communication is key to efficiency; a lack of communication can affect costs.

We regularly advise business recovery departments in the big accountancy firms on the costs of firms in administration, which last year seemed to me to reach a significant number.

WHAT TO LOOK AT

- Rent
- Service charges
- Insurance
- Business rates
- Water
- Utilities
- Recoveries from
 - Landlords
 - Tenants and subtenants
 - Managing agents
 - Central and local government
 - Water and utility providers
 - Revenue & Customs
- Why do things go wrong?
 - Chinese walls
 - Limited expertise
 - No process or process breakdown
 - Refocusing of priorities
 - Changes in personnel
 - Database upgrades
 - Lack of resources

I would not suggest that a forensic audit would have been able to save some of the companies that did go under, but it would have returned monies to the company coffers and created some key earnings to ensure that any generic problem did not recur.

On the high street, most retailers' margins are being squeezed. In buoyant times, the focus is on increasing sales, but there must be a time when it is appropriate to examine business costs to prevent an organisation's downfall.

Mixed view of audit

A property auditor may be welcomed as a knight in shining armour, particularly as his payment is typically assessed on a contingency fee basis. Such an enterprising initiative is usually welcomed by new management.

However, there are always the concerns of long-standing staff who view an audit as a reflection on their effectiveness. This should not be the case. Most people appreciate that a property department may be under-resourced, may not have an accounts department that is accountable to it, and probably has no control over the temporary clerk who may occasionally misprocess a rent demand.

I sympathise with any individual who may have thousands of invoices to process – a slip of a finger may create an incorrect payment, a payment to the wrong vendor or a double payment. Errors are a fact of life and what is important to ensure that they are minimised and, where they do slip through the net, they can be captured by some means of process or reporting – after all, error costs.

Martin Brownstone is the managing director of Marston Associates