

Lynden Gate Residents Ltd

Accounts to 30th June 2011 and service charge projections

At the AGM in December 2010 we proposed that service charges should rise by £350 in each of the years up to year ending June 2014 taking fees to £4,600 for that year and for the foreseeable future. We are now proposing to increase fees by only £100 to £4,000 for the year to 30th June 2013 and to hold them broadly at that rate for the foreseeable future. This is because the redecoration started in 2007 and finished in 2008 has held up better than expected and we now intend to start the next redecoration in 2013, a year later than previously planned.

The auditors have produced the “Directors’ Report and Financial Statements” which has been circulated with the AGM papers. In this note I explain our expenditure and financial position, both now and for a few years into the future. I also discuss the level of service charges that we will need to levy – outlining the unknown factors with which we have to contend and the choices that we will have to make.

The Basics

In very simple terms the annual service charge covers two types of expenditure:-

- Normal Administrative Expenses of typically around £100,000 pa – such things as salaries, garden maintenance and insurance.
- Exceptional Items – mainly periodic or one-off maintenance costs, of which the “triennial” redecoration historically at around £600,000 (but expected to be larger in future) is by far the largest. In some previous years there have also been abnormal Administrative Expenses, mainly legal expenses relating to litigation.

The annual accounts always show a profit in a year when there is no redecoration. This profit is added to the “Redecorating and major maintenance reserve” which recognises the future liability to redecorate. And the balance of cash that we will eventually use for the redecoration builds up in the balance sheet. In a year in which we carry out a redecoration we make a loss which reduces both the balance of that reserve and, obviously, the balance of cash in the balance sheet. Then we start all over again.

There are 70 houses on the estate and last year annual fees were £3550. In very rough terms £1350 of this covered operating costs and £2200 was “saved” to provide for the periodic decoration and other one-off maintenance.

The last few pages of the Directors’ Report and Financial Statements show the accounts in summary over the last 5 years.

Administrative Expenses

There are no major issues relating to normal Administrative Expenses although residents may wish to quiz directors over their stewardship. The summary of the last 5 years' shows a fairly consistent annual cost of around £80,000 - £100,000. The increase in the later years was largely in Employment Costs due to the increase in numbers of staff from 2 to 3 in the middle of 2006/7.

Redecoration and maintenance costs

Routine repairs and maintenance (of the gates and pumps for example) is included in normal Administrative Expenses. In addition we incur larger amounts of one-off redecoration and maintenance costs. These account for about 65% of the service charges.

The annual cost of redecoration is the single most expensive item although we only spend the money every 4 or 5 years. The total cost of the most recent redecoration was £572,000 of which £107,000 was spent in 2006/7 and £465,000 in 2007/8.

We occasionally incur smaller one-off maintenance costs and, as the estate ages, we can expect such expenditures to become more frequent particularly as we get to grips with the gradual repair of the road surfaces. In 2007/8 "Other major maintenance" costs of £22,574 were spent on repairs to the road surface in the garage area at the south west corner of Seaton Close, in 2008/9 road and pavement patch repairs cost £16,601, in 2009/10 we incurred costs of £37,967 on "mid-term" redecoration, surveyor's fees and drain investigation and in 2010/11 £31,182 on interim redecoration.

There are several choices that we have to make in managing these costs and these are discussed below in the context of a review of our long term maintenance requirements which was carried out for us in 2009 by King Sturge.

The key cost drivers

The King Sturge review identified 4 main areas which will drive our costs:-

- Continual one-off repairs such as road patching or drain repairs;
- The periodic redecoration;
- Replacement of the total road surface;
- Replacement or repair of all underground services – drains and electricity.

Continual one-off repairs have been increasing in recent years particularly as the road surface ages and we carry out patch repairs. But these repairs are not only for roads – for example the King Sturge survey determined that we needed to carry out a repair to the drains at the top end of Seaton. This does not cover routine and minor maintenance which are included in Administrative Expenses.

It is impossible to forecast the level of continual one-off repair costs with any accuracy. For the purposes of fee calculations we have assumed £20,000 pa for the foreseeable future.

The periodic redecoration is likely to cost a lot more next time and we are assuming £900,000. This is partly because building costs are rising faster than general inflation (to some extent driven by the Olympics, to some extent by raw material cost rises) and partly due to an enhanced specification. The specification is driven by redecoration frequency – we judge that residents have no appetite for redecoration every 3 years and we anticipate the consensus being that we should go for a 5 year gap, perhaps even 6 years – and this demands a somewhat more extensive specification. And the gap between redecorations has a substantial impact on annual fees since it reflects the number of years over which we can save up the required funds.

The replacement of the total road surface would cost about £900,000. It would be a major logistical exercise, probably involving the demolition of some garages to allow alternative access to the site. Something of a nightmare but, as was discussed last year, we do not believe that this work needs to be done. The subject was first raised as a cosmetic exercise – increasing the value of our properties by having a better looking road. Time and economic circumstances have changed and we do not believe there would be any consensus of residents’ opinion in favour of such a project unless it became absolutely necessary. And the King Sturge review leads us to believe that to be unlikely.

We might well face the need to carry out underground repairs or replacement of substantial *parts* of the road surface but we would do this using our patching methodology and not as a total surface replacement.

Replacement or repair of all underground services would only arise if we were to undertake the replacement of the total road surface. In those circumstances it would be foolish NOT to replace the underground services. However, since we do not believe we will go for total surface replacement, we are similarly unlikely to go for total replacement of underground services although we might well have to deal with them piecemeal.

All in all a picture still with a lot of uncertainties and variables. Let us now turn to the level of maintenance fees that is appropriate given these uncertainties.

Service charges

We believe that residents do not wish to be faced with demands out of the blue to deal with emergencies or unforeseen circumstances and that, given the degree of uncertainty in requirements, it is better to build reserves and prepare for generously estimated costs.

It was therefore agreed at the AGM in December 2010 that we would raise service charges to £3,900 for 2011/12 and [probably] by £350 a year for at least the subsequent 2

years. The word [probably] was inserted because although this feels like a long-term commitment, in practice we only make the decision for one year at a time and all assumptions can be reviewed again before setting the charges for the next year.

And we have reviewed those assumptions and, in particular, decided that the condition of the estate is such that we do not need to redecorate starting in 2012 but can delay until the following year. This is a six year gap from the redecoration carried out in 2007 and 2008 and we feel now that it is reasonably safe to assume a five year gap in future.

The effect of all these assumptions, as shown in the financial projections in the attachment, is:-

- Service charges reach £4,000 pa in the year to June 2013 but do not rise thereafter
- There is one redecoration in the period starting in 2013 and ending in 2014
- We have allowed £20,000 pa for one-off repairs.
- There is no allowance for any substantial road resurfacing or underground work in the period.
- The Redecoration Reserve at June 30th 2016 would be about £450,000 and increasing by about £150,000 per year. This would be in line with another £900,000 redecoration starting in 2018 (a gap of 5 years) and being largely paid for in early 2019, but
- there is no building of reserves for future road resurfacing or underground works so, if our assumptions here prove to be wrong, it might be necessary in the future to increase service charges.

These projections are similar in nature to those made last year, but with a significant change in assumption on the appropriate frequency of redecoration and therefore the required level of fees. We believe that they are reasonable (although, as I am bound to say, we might have to face unforeseen circumstances). Therefore it will be proposed at the 2011 AGM that service charges for 2012/13 be raised to £4,000 pa as discussed above.

Neil Chisman
1 Beaufort Close

1 November 2011

Attachment

Lynden Gate 5 year financial forecast

Year ending 30th June	2011	2012	2013	2014	2015	2016
Annual service charge £/house	£3,550	£3,900	£4,000	£4,000	£4,000	£4,000

Profit and Loss Account - £000s

Turnover	248	273	280	280	280	280
Administrative expenses	-96	-98	-101	-103	-106	-109
Operating Profit	152	175	179	177	174	171
External decorating	-31		-200	-700		-40
Other major maintenance		-20	-20	-20	-20	-20
Profit before interest and tax	121	155	-41	-543	154	111
Interest receivable	1	6	8	7	2	4
Tax	0	-1	-2	-1	0	-1
Profit trans'd to redecc'n reserve	122	159	-35	-538	156	114

Balance Sheet

Debtors and cash	609	769	735	198	354	469
less Creditors	-12	-13	-13	-14	-15	-15
Net Assets	597	756	722	184	340	454
Called up share capital	4	4	4	4	4	4
Redecc'n reserve	593	752	718	180	336	450
Net assets	597	756	722	184	340	454