

**OPERATING COSTS  
AND SERVICE  
CHARGES IN OFFICES  
IN POLAND**

2011-2017

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Knight Frank Sp. z o. o. is part of the Knight Frank Group, leader of the international group of property advisors. We have over 27 years of experience on the Polish property market. We manage a commercial real estate portfolio of office and mixed-use buildings as well as a portfolio of retail and logistics properties. In order to analyse running costs and service charges, we have selected 40 buildings of A/A+ class and B/B+ class located in Warsaw, Poznan, Wroclaw, Krakow, Tricity and Lodz, built after 1998. The analysis encompasses the years 2011-2017.

Commercial space leasing is linked to the necessity of carrying the costs to benefit the owner which include: rent, service charges (often referred to as additional rent) and utility payments. The amount of the rent and service charges as well as the method of reconciling utilities are usually regulated by the lease agreement. The service charges and utilities carried by the tenant cover all operating costs of the owner to maintain the property. Additional costs such as costs borne to complete and finance a project, modernise or renovate in order to maintain or enhance the property standard, costs of securing new tenants and arranging the space to their requirement, administrative costs or costs resulting from individual tenants' requests are the costs of the owner.

# SERVICE CHARGES

Service charges in office buildings are settled in accordance with the terms agreed in the lease agreement. There are three types of settling of accounts in the real estate market.

## Fixed Costs

– the tenant pays a fixed fee for running costs determined in the lease agreement. The costs incurred do not need to be reconciled. If the final sum is higher than the set fee total, the landlord will cover the difference; and if the final sum is lower than the difference remains with the landlord.

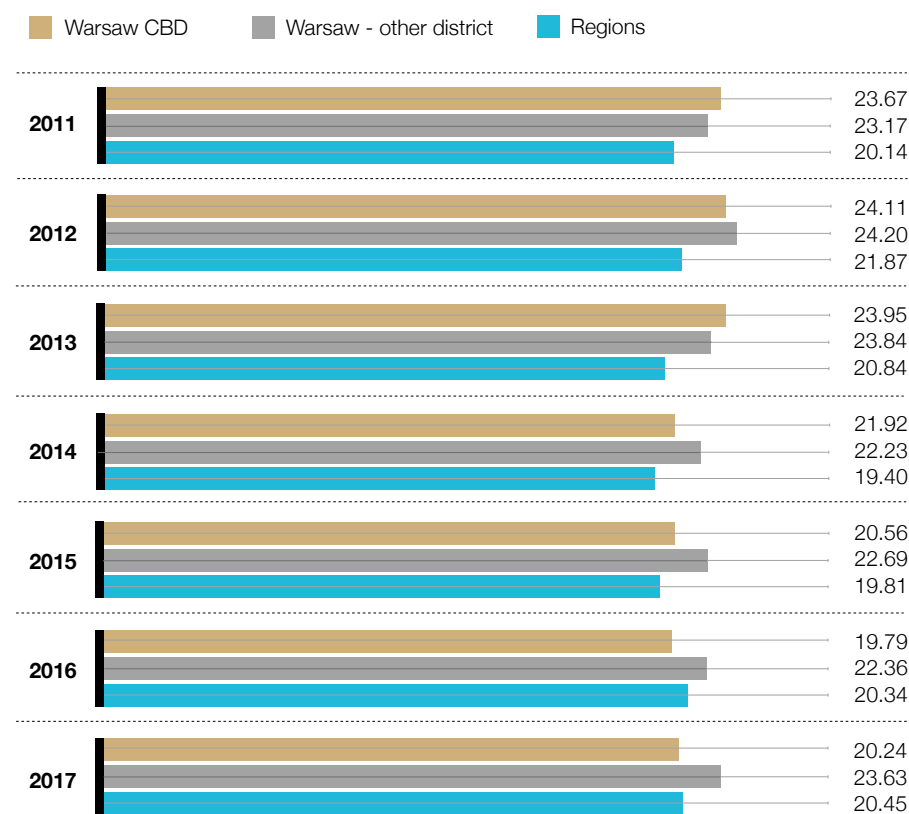
## “Variable” Costs

– the tenant makes a pre-payment for the total of running costs of the building, which are settled after a year (or more frequently) and the tenant will either pay any extra difference; or, if overpaid, it will be accounted for in the next monthly payments.

## Combined Costs

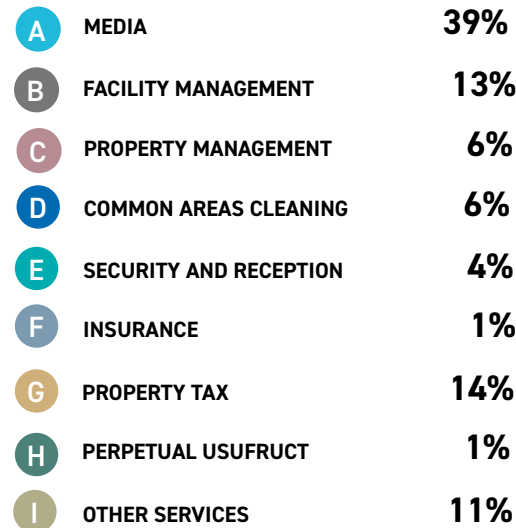
– the accounts settled depend on a divide (in accordance with the lease agreement) of costs independent of the tenant (taxes, insurance, utilities) which are settled in full, as well as costs incurred by the tenant, such as the costs of specific services in the property. That part of the costs can be fixed, or can be subject to a maximum increase, such as no more than 3-5% per annum.

Levels of running costs in the years 2011-2017 (PLN/sq m/per month)





Service charges - average share of particular cost groups in the years  
2011-2017 (PLN/sq m/per month)



Lease agreements usually commit the tenants to cover all of the service charges. The way in which this commitment is to be fulfilled is written in the lease agreement. Depending on the agreement, the tenant covers: running costs and utilities. The lease agreement will include a list of service charges covered by the operating costs. This list is usually open and will encompass any current charges incurred through upkeep of the property. Excluded are utilities costs. The amount of service charges converted over squared meters of the rented space depends on many factors. Amongst others: location, size of the property, its technological advancement, geographical location, ownership of the land, level of depreciation and many more.

# 1. SERVICE CHARGES VS OPERATING COSTS

Lease agreements usually oblige tenants to carry all operating costs. The form in which the costs are carried is defined by the lease agreement. Depending on how the lease agreement is constructed, the tenant pays for:

- Service charges
- Utilities consumption

Lease agreements also include a list of operating costs covered by the service charges. The list is usually open and includes all ongoing property maintenance costs. Utilities are excluded from the list.

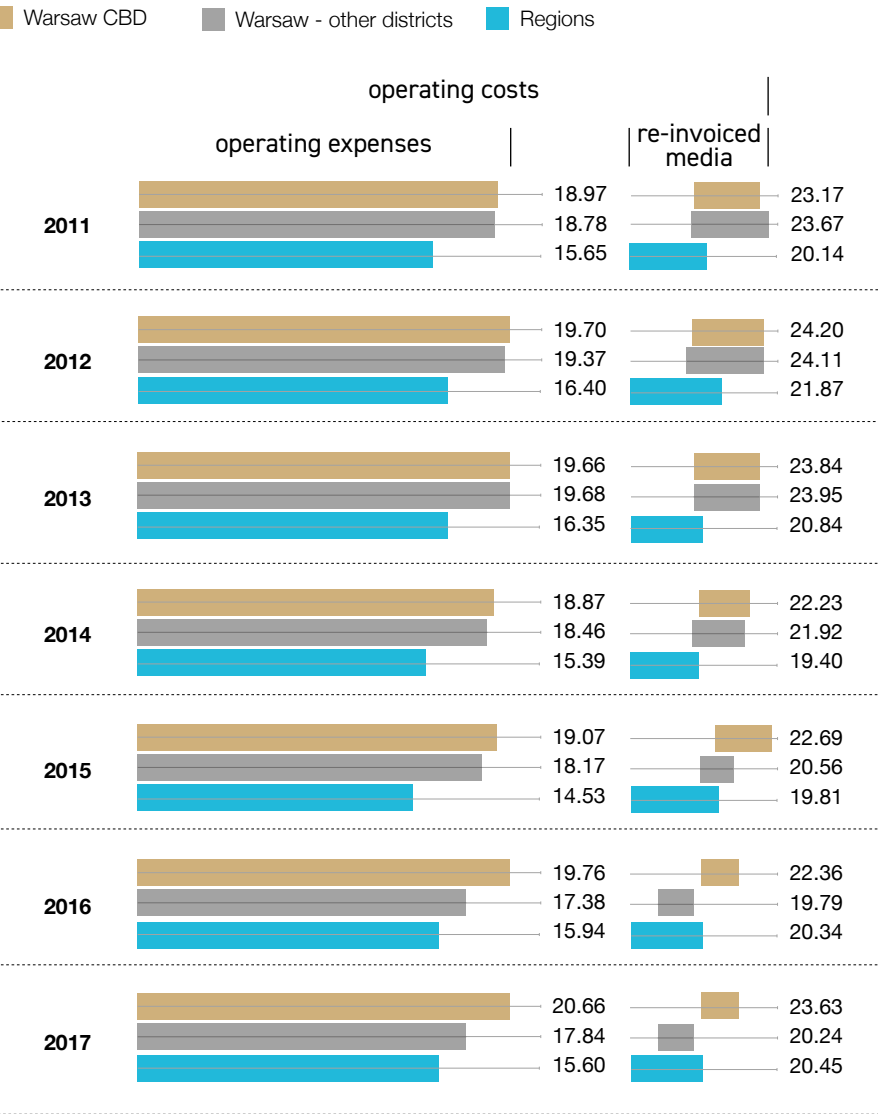
The utilities consumption costs are divided among the tenants in full or in part according to the provisions set out in the lease agreement. Invoicing is based on direct consumption measured by individual meters or by an algorithm based on the relation between the occupied space, space dimensions and devices installed on the premises. Particular lease agreement clauses allow to exclude even up to 100% of utilities consumption costs from the service charges. It is an important element which shapes the final cost. Lease agreements allow tenants to control how much they pay. The most frequently used clause is the right to audit – after the ending of the fiscal year – the correctness of the reconciliation and legitimacy of the carried service charges.

Another frequently used clause is to limit the increases of service charges influenced by the owner to a given percent on a year-to-year basis.

Level of service charges in the years 2011-2017 (PLN/sq m/month)

	2011	2012	2013	2014	2015	2016	2017
Warsaw CBD	18.97	19.70	19.66	18.87	19.07	19.76	20.66
Warsaw - other districts	18.78	19.37	19.68	18.46	18.17	17.38	17.84
Regions	15.65	16.40	16.35	15.39	14.53	15.94	15.60

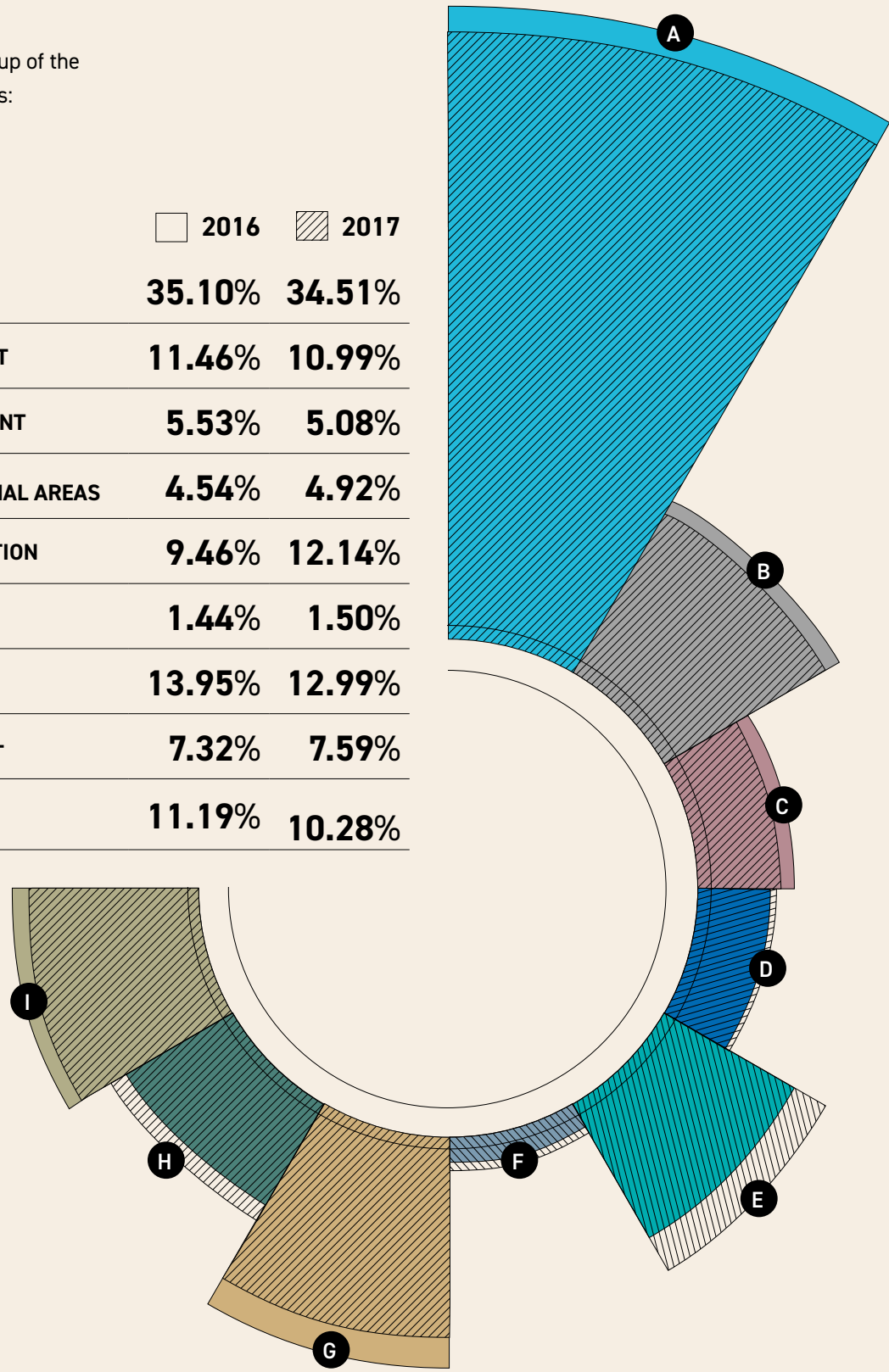
Average monthly amount of costs and service charges in the years 2011-2017 (PLN/sq m/month)



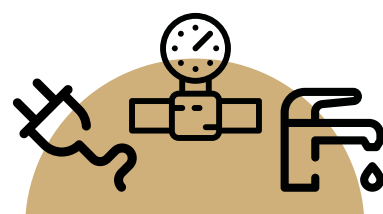
## 2. COMPONENTS OF SERVICE CHARGES

Service charges are made up of the following groups of charges:

	2016	2017
<b>A MEDIA CONSUMPTION</b>	<b>35.10%</b>	<b>34.51%</b>
<b>B FACILITY MANAGEMENT</b>	<b>11.46%</b>	<b>10.99%</b>
<b>C PROPERTY MANAGEMENT</b>	<b>5.53%</b>	<b>5.08%</b>
<b>D CLEANING OF COMMUNAL AREAS</b>	<b>4.54%</b>	<b>4.92%</b>
<b>E SECURITY AND RECEPTION</b>	<b>9.46%</b>	<b>12.14%</b>
<b>F INSURANCE</b>	<b>1.44%</b>	<b>1.50%</b>
<b>G PROPERTY TAX</b>	<b>13.95%</b>	<b>12.99%</b>
<b>H PERPETUAL USUFRUCT</b>	<b>7.32%</b>	<b>7.59%</b>
<b>I OTHER SERVICES</b>	<b>11.19%</b>	<b>10.28%</b>



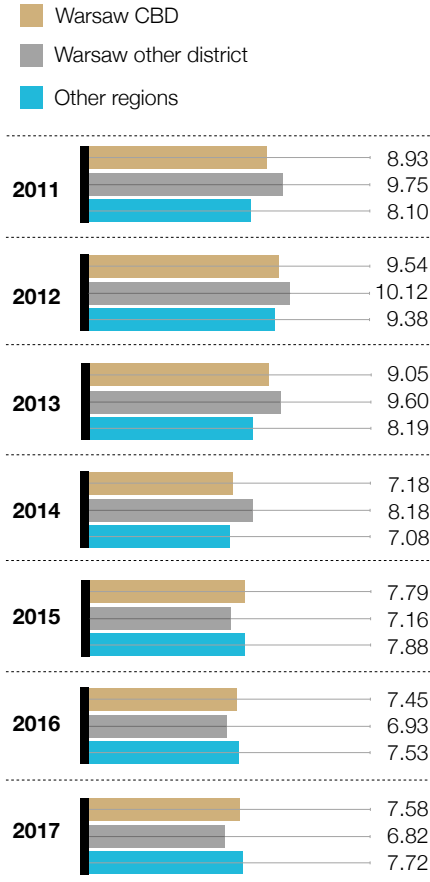
## 3. ANALYSIS OF SERVICE CHARGES ACROSS SPLIT GROUPS



### MEDIA

This group includes assumption costs of electricity, heating, gas, water usage and drainage and sewage costs.

Average costs of utilities in the years 2011-2017 (PLN/sq m/month)



2017

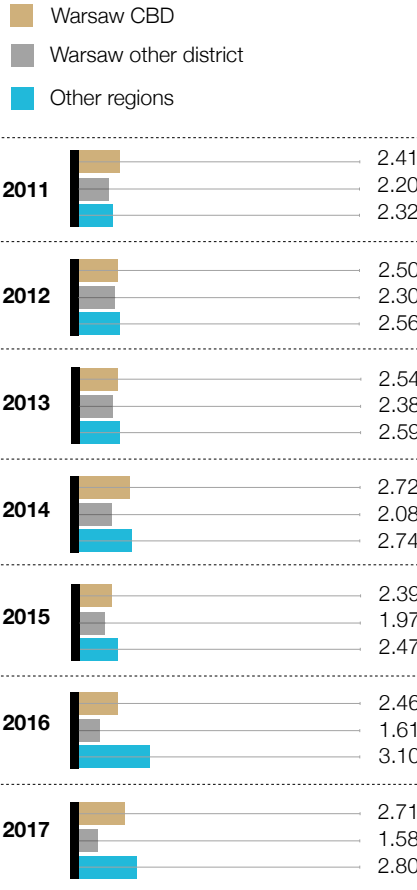
In 2017, the cost of supplying and usage of utilities in the analysed property portfolio made up, similarly to that in 2016, approx. 35% of the total costs. Despite the observed increase of electricity prices, the total costs have not increased. This has been influenced by more frequent investments of property owners in renewable energy solutions, such as LED lighting, movement sensors etc., as well as a general commitment to save energy and involvement in pro-ecological activities. So far as in 2018 it was possible to negotiate lower electricity rates, analytics predict an increase in rates in the next few years. In 2018 there was a major increase in gas rates, which will have direct effect on costs of heating in properties with gas installations. For some time now there is an expectation of an increase in water rates.



### FACILITY MANAGEMENT

This group includes facility management (permanent facility management team onsite and/or mobile service), technical installations and elevator maintenance. Technical maintenance of all installations is usually handed over to a single company, excluding

Average technical service (FM) costs in the years 2011-2017 (PLN/sq m/month)

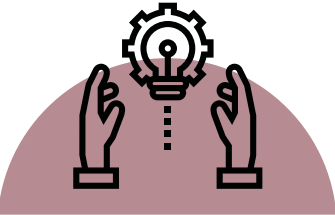


elevator and escalator maintenance, which is commissioned to specialised service providers.

2017

In 2017 there was no observed significant changes in costs of technical services and the whole amount has remained at a level around 11%. We are going to assume, however, that looking at the increasing rate of salaries of security personnel, there could be a potential increase in cost of technical services in the next few years. FM specialists are employed on a contractual basis in technical companies but their salary is often at a similar rate as that of security staff albeit a best much more advanced level of qualifications is necessary.

We have also noticed a drain in qualified and experienced FM technicians from property service providers, where work is often in shifts, unpredictable, carries a lot of responsibility and needs resilience to stress, in order to provide the relevant property services. This contributes to frequent changes in the FM teams and will most likely lead to an increase in salary for technical staff, which will increase the rate of the service provided. It seems to be more likely to come across mobile FM services rather than a permanent property based FM teams.



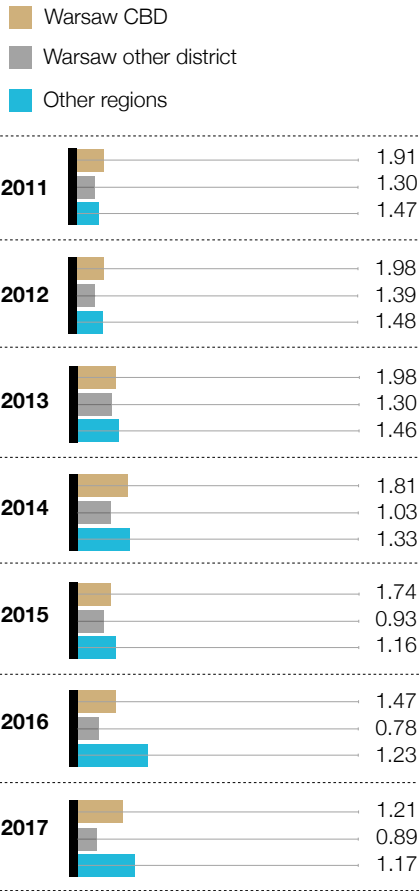
## PROPERTY MANAGEMENT

Property management in Poland is a term far wider than in Western European countries. In Poland, property management includes all ongoing activities necessary for the efficient and safe functioning of the property and the collection reconciliation of rent and service charges.

All services related to property management are usually handed over to a single entity.

Property management does not include bookkeeping services of the

**Average monthly property management in office buildings in the years 2011-2017**  
(PLN/sq m/month)



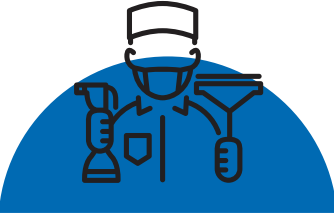
special purpose company.

### 2017

In 2017 we have observed insignificant changes in the costs of property management. Even though it is quite a low cost in general, it has seen a minimal decrease. This is most likely due to a decrease in rent charges as well as an increase in empty buildings, which have a direct influence on the management costs. It is most commonly defined as being a fixed percentage from accounted rent charges, excluding any rebates and discounts. This situation on the market is causing that more often, the cost of property management is a lump sum. However, the decrease in rates

for management services in the past few years is not directly proportionate to the amount of work and responsibilities of the property manager.

The scope of services is defined in the property management contract, on the basis of which the property manager can operate. In addition, a lack of legal definition of management on the Polish market means that the market decides on which services are provided. The creation of new laws, greater demands from clients as well as a change in type of funds have caused a constant rise in expectations in a day-to-day providers of building management services.

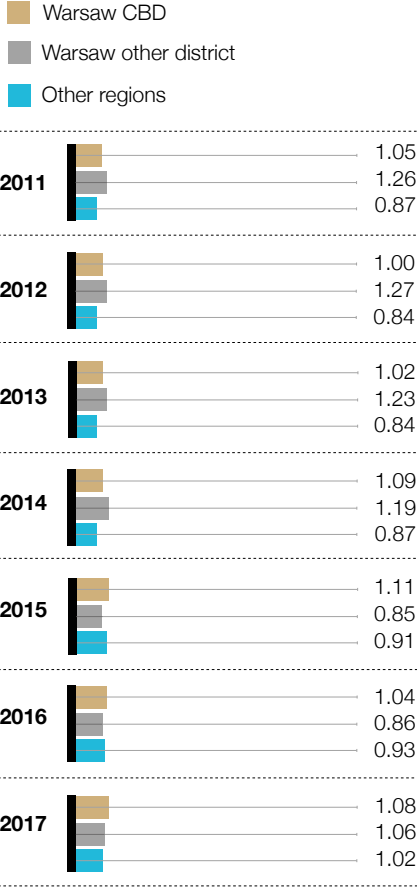


## COMMON AREAS CLEANING

Common areas cleaning includes the cleaning of common areas accessible inside the property including the car park and maintaining the area around the property. The costs also include buying the necessary cleaning materials.

In modern office properties common areas (excluding car parks) amount from 3% to 7% of the total building area, which significantly influences the amount of cleaning costs.

**Average common areas cleaning costs of office properties in the years 2011-2017**  
(PLN/sq m/month)



### 2017

In 2017 the cost of cleaning remained similar to that in 2016, regardless of changes to salaries as well as hourly rates. Most companies did not decide to increase their prices for services, or raised them minimally. Unfortunately, more companies have the issue of not enough 'hands to work' and so more often than not, that reflects on the quality of work. They have resolved to hiring foreigners, which seems to be an increasing trend in the next few years.



## SECURITY AND RECEPTION

The services include reception services, open usually during office working hours, the constant presence of security staff and mobile intervention patrols. The security headcount onsite depends on the property size and its layout plan. Usually during evening hours, there are two security employees present. Due to safety reasons, security services are handed over to a specialised and licensed provider.

### 2017

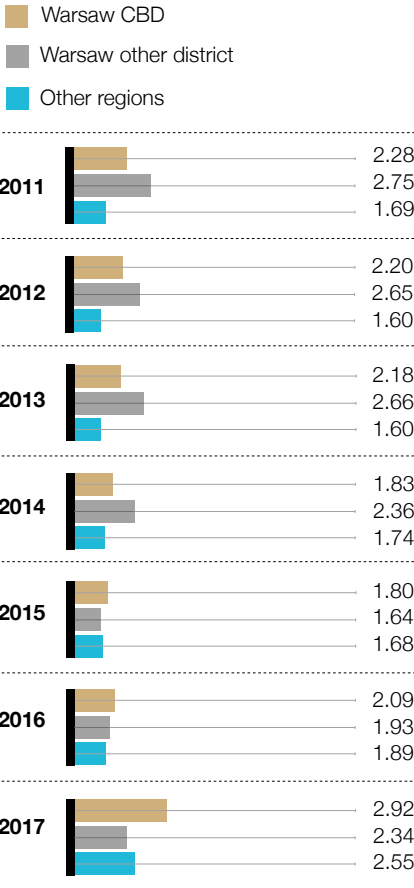
From January 2017, there has been a change in the law regarding minimum wage. Salaries have marginally increased, raising the hourly rate of pay to 13 PLN. The cost of security, where the main element is the cost of hiring personnel, have increased from 20 percent to 40 percent. That does not mean, that each building has had such an increase in security costs. Thanks to the diligent efforts of property managers and investments of property owners in parts of their buildings, additional technical services have been introduced (cameras, electric gates, etc.), which allow the optimisation of the number of security personnel necessary to service the property, but whilst also keeping the increase of costs at bay.

From January 2018, there has again been a minimal increase in salaries and hourly rates of pay. It seems that this tendency will uphold, meaning that each year there will be

an increase of these costs.

More often we are seeing the need to split the service of security and reception personnel. There are greater expectations of reception personnel, as well as the need to limit their rotation, meaning that property owners and managers often use professional companies servicing only receptions of properties. The cost of such a service is higher, however allows to introduce a completely different level of service for the tenant/guest and changes the perception of the building in a constantly demanding and difficult property market.

**Average security costs in the years 2011-2017**  
(PLN/sq m/month)



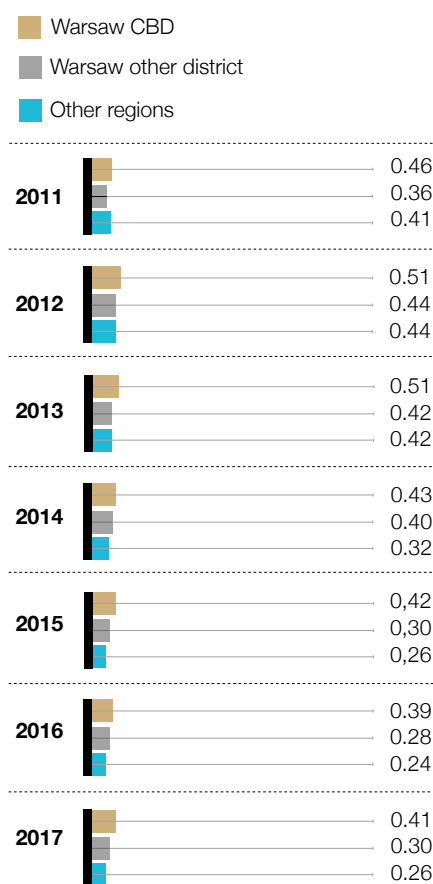




## INSURANCE

Insurance costs include annual charges for property insurance in full scope and property liability insurance. The lease agreement defines, if the insurance also

**Average insurance costs in the years 2011-2017** (PLN/sq m/month)



covers property insurance from loss of rent and terrorist attack.

In the past few years, the laws regarding insurance have not changed, and their rate has remained the same in 2017, as well as the previous year. Insurance is counted as part of the charges not influenced by the property owners, however it is they who negotiate it and that will depend on the chosen insurance company, the amount of properties in their portfolio, as well as levels of excess for different types of occurrences.



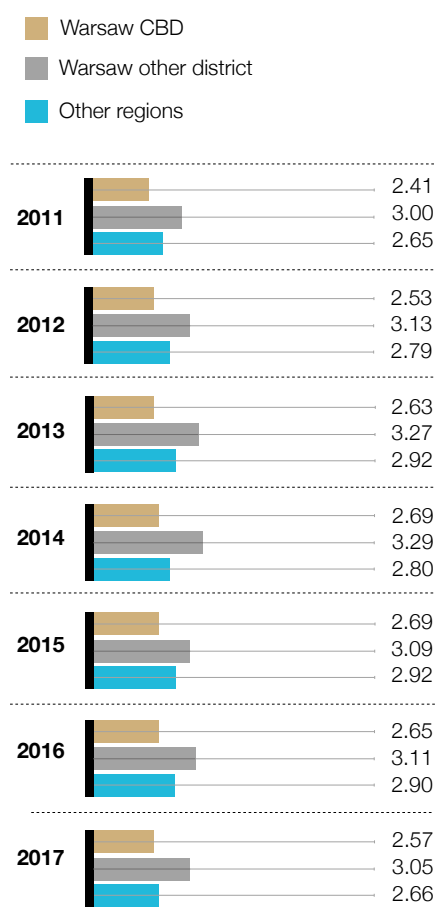
## PROPERTY TAX

Property tax includes land, buildings or their parts associated with business activity, as well as building structures. In accordance with information given and announced by members of self-government, the rates a property owner must pay each calendar year must be calculated to figure out the amount of property tax payable, and it must be declared.

### 2017

In 2017, tax rates in most cities and counties remained at the same level as the previous year. In 2018, the Ministry of Finance published higher possible rates of tax for property surface areas in use and

**Average rates of property tax for office buildings in years 2011-2017** (PLN/sq m/month)



surface areas of land. Most autonomous bodies took advantage of the highest possible rates and that raised the property tax to 23,10 PLN per meter squared of surface area of the building, and to 0,91 PLN for surface areas of land.

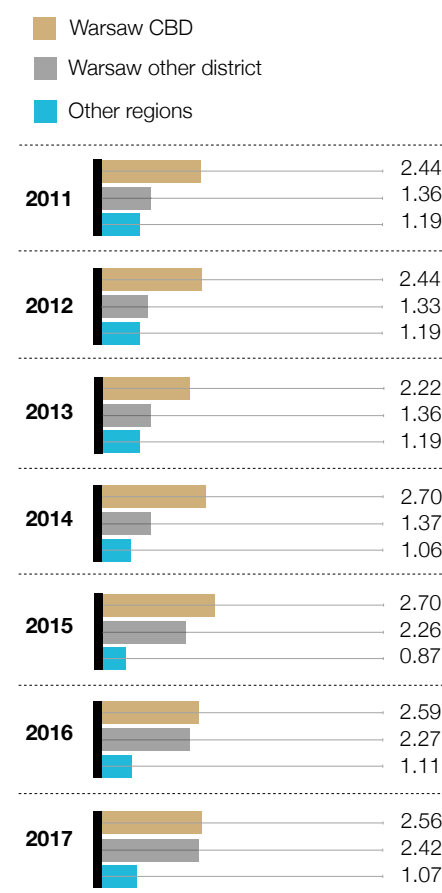


## PERPETUAL USUFRUCT

Perpetual usufruct law or a long lease is a form of land interests used in the Central European countries. Within the property portfolio under Knight Frank's management, some 60% of owners in Warsaw is regulated by this law. In regional cities, it equates to some 40%. The amount of the annual charge is 3% (for land used for commercial purposes) of the land's value as estimated by the land owner, such as the State Treasury or a regional government unit (municipality, council, voivodship).

It is most likely that from January 2019, land used for residential properties will be changed into freehold ownership, however for commercial properties it is necessary to seek the permission of the European Commission, to which the Ministry of Investments and Development is currently presenting. There is no potential Bill in this area yet, so it is unknown under which circumstances this would happen.

**Average annual perpetual usufruct charge in years 2011-2017** (PLN/sq m/month)



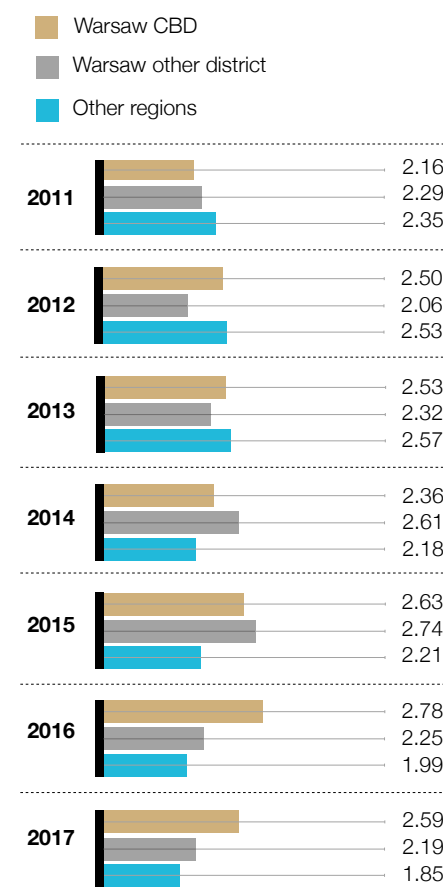
## OTHER COSTS

This is the most varied costs group as it depends on the property and service agreements. It includes cost such as: repairs and ongoing

refurbishments, spare parts, various systems maintenance, technical supervision inspections, annual and 5 years construction reviews, mat rentals, pest control, seasonal decoration, green area maintenance etc.

The above costs are often unequally distributed in time (5-years inspections) and difficult to estimate beforehand (snow removal). They are also difficult to compare.

**Average property costs in years 2011-2017** (PLN/sq m/month)





# WHAT'S NEW IN OFFICE BUILDINGS?

## RODO

RODO (PL) – or GDPR (ENG) – General Data Protection Regulation came into effect on 25th May 2018, and affects all companies who in whatever way process personal data. Companies processing personal data must keep to strict guidelines, such as:

- Acknowledging new legislation for clients (such as the right to be forgotten – meaning removal of all and any personal data from the database on request, right to change of information or removal to a different data administrator)
- A ban on profiling, so any automatic processing of data
- Minimalizing of processing of data
- Obligation to sign agreement to entrust all data forming relations
- Privacy by design and privacy by default

- Rule of calling for inspection of protection of personal data
- Necessity of authorising designated employees to process personal data
- Failure to uphold GDPR can be fined from 10-20 mln EUR or 2-4% of annual company revenue. As GDPR is a new regulation for the whole of the European Union, it is certain that everyone, including property owners and managers, will be learning over

the next few months how to adjust functionality of properties to the new laws.

It is definitely necessary to inform all property users, as well as visitors, that their data is being processed and who the administrator is. It is essential that appropriate adjustment of individual data collections is made and limiting all collections of data to a minimum.



## CERTIFICATE WELL

There has been a lot of discussion on the property market about balanced development and green certificates. Today, green certificates BREEAM and LEED are the standard. Each new building has one and most existing office buildings have successfully been certified. Currently on the market, we are moving towards WELL certificates. These certificates can be obtained for the whole building or just the office of a specific tenant.

The WELL certificates focus on the health and wellbeing of people working in the building. To gain the WELL certification, workers must have access to daylight, adequate amounts and quality of fresh air, adequate noise levels, comfortable temperatures. The certification focuses on measures of the quality of the environment inside the building, but the location and transport connections, communal and outside areas, evacuation procedures are also taken into account.

## INCOME TAX FROM PROPERTY

From 1st January 2018, an income tax from commercial property was introduced. The legislators had in mind the closure of any loop-holes in income tax laws from physical persons as well as income tax from legal persons, and introduced the so-called minimum income tax for taxpayers who own commercial real estate with an initial value exceeding PLN 10 million. The amendment is part of the legislator's struggle with optimisation of income tax. Office buildings, as well as retail properties will be taxed.

The property market had widely discussed the introduction of this tax, as well as the possibility to account for this in running charges covered by tenants. It is definite that after the first year's accounts will be



settled that this comes into power, we will be able to see how many property owners have gone for such a solution. We must take into account, however that standard lease agreements do not include this in the service charges. This is an income tax, and its amount will directly depend on the financial politics of the tenant.

## RELATIONSHIP WITH OUR NATURAL ENVIRONMENT

The last few years have brought a new trend of a pro-ecological lifestyle. Apart from the ever-present popular healthy living lifestyle, we are becoming more interested in our surrounding nature. We are trying to protect it, support its growth and reap its benefits. This trend is also noticeable in office buildings. Apart from a larger amount of greenery inside the buildings (green receptions, corners, walls) as well as outside, where more and more parking spaces are being turned into recreation spaces, etc. We can also observe an increase in amenities for the surrounding fauna. It is now the trend to educate oneself in ecology/nature as well as create infrastructure around buildings to accommodate plants and animals. Rooftop beehives, bird feeders, shelters for bats and bugs are becoming omnipresent. Building regulations are being updated and dogs are becoming the most frequent office guest, as man's best friend. All of these efforts come from needing to feel unity between other living beings. Lifestyle habits have changed and one of the reasons is definitely a generational change, as well as the necessity to combat stress. We're spending more time playing sport, outdoors. We should not be away from nature when we want to take a moment to more away from our busy work duties.





## BIOPHILIC

The feeling of being one with other living organisms. The element of human nature, tendency to be part of a natural process and to live surrounded by life. This theory has been conceived by Erich Fromm, and developed by Edward O. Wilson – an American biologist and zoologist. This theory has been continued in office building designs (biophilic design) as well as organisation of work in the office environment. The model biophils have used in their interior designs are: visual contact with nature, arrhythmic sensory stimulation, change in temperature and air flow, presence of water, dynamic air and scattered light, a connection with natural systems. They all have been finding their reflecion in interior materials, appliances, decorations, projected installations or sounds, in order to improve our physical and psychological condition as the main factor influencing the quality of work.



## CIRCADIAN LIGHTING

Is lighting corresponding to the time of day, changing intensity and shade according to the time. This means regular physical and mental change of one's activity levels, depending on time of day or night. The lighting works together with this system to positively affect human functioning, and can also improve productivity levels. The shade of light also helps, in the morning after sunrise is warm, as well as around the time of sunset in the evening.



## GENERATION C

People born after 1990, starting their first employment. This generation is labelled using three adjectives: connect, communicate, change; it works in the internet world and always connected to mobile device, as well as leading a separate life on social media.

People who value a flexible work schedule, working from home, on flexible contracts. It can be expected that they will have a significant influence on the functioning of companies in the future. Employers are going to have to adjust to a flexible schedule ('half and half' – work partially done from anywhere, partly in the office). Generation C also feels the need to change jobs regularly, needs constant development and fulfilment of their passions.



## WELL BUILDING STANDARD

This is a system of certification created by IWBI TM (International Well Building Institute TM). It is the first system that is dedicated to health and wellbeing of workers of a whole building or its part. It is based on the idea that as so much time is spent in an office building, what is its impact on the people working inside? The surrounding environment has a great effect on our health, productivity and wellbeing. The certification is proof that the property has been designed in a way that is promoting in its entirety, or in part, a healthy lifestyle.



## Notes...





COMMERCIAL  
MARKET

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