COMPASS COMMERCIAL, ITRA GLOBAL

Providing commercial real estate services by advocating for our corporate clients' interests and increasing their profits.

Tips on Reviewing Your Annual Expense Reconciliation

For tenants with net leases, the annual expense reconciliation bill from your landlord will arrive soon. The landlord's accompanying letter goes something like this: "Building expenses in 2018 were higher than budgeted. Please pay the attached invoice within 30 days and have a nice day." Sometimes tenants receive a credit. In either case, your company should carefully review the expenses passed on to you by your landlord for the prior year.

Expense audits contain specialized lease language. Many leases require that your company hire a CPA if you wish to conduct an official audit of the landlord's books and records. Other leases don't grant a tenant's right to audit, so your landlord might not share any operating expense details with you. Most landlords will provide some detail to tenants which you can then compare against your prior year expenses. Real estate tax costs can be found online, so you can confirm your tax costs without input from your landlord.

If you do an official audit, you or your CPA will check for errors or overcharges, and also for things that shouldn't have been charged as an operating expense at all. Keep in mind that most leases contain language about what can or cannot be charged to tenants as a building operating expense, so this should be clear cut. However, some leases are vague about what can be charged. Landlords tend to structure leases to their advantage so that they are able to pass through as many expenses as possible to the building tenants.

Is a parking lot pothole repair an operating expense? Yes. Is removing 30% of the parking lot and installing all new asphalt an operating expense? For many landlords, the answer is yes again. Should all or some of

The Compass Commercial Difference:

Your Advocate:

We represent only tenants and users of commercial real estate—never landlords or developers.

Your Expert:

Our team of seasoned professionals negotiate on your behalf, lowering your cost. We use our years of experience to leverage your negotiating power.

Your Local & Global Representative:

We provide broad geographic coverage and seamless representation in multiple markets through offices around the world.

Your Trusted Advisor:

You will always receive objective, unbiased advice. Our team will save your hours of time researching, conducting negotiations and other services or your behalf.

COMPASS
COMMERCIAL

Need some help? Just call us at 248.817.5400

Info@compass-commercial.com

www.compass-commercial.com

that work be landlord's capital expense? Maybe. This depends on how your lease is written and you may find that your lease may not be completely clear on what constitutes a repair versus a replacement.

Many office buildings today are adding building amenities such as fitness centers, training rooms, food service, conference rooms, lounges, bike storage, etc. How did your landlord pay to create these amenity spaces? How did they pay for the tables, chairs, or equipment in these areas? Is there any rent being charged for these spaces in the building expenses? These are questions that a tenant can ask their property manager without conducting a full-scale audit and then compare what they say against what is written in their lease.

Other expense items that tenants should review pertain to how the landlord charges management fees along with any building staff dedicated to the property. In some buildings, there is a percentage fee charged as a management fee. In other situations, especially larger properties, there is a management fee plus the cost of onsite employees that manage the building. Is the landlord charging these costs correctly and in compliance with your lease? Is your landlord charging any costs for employees that don't actually work on your building or that are executives of the management company? Ask these questions.

As you review your operating expenses and tax pass-throughs, don't just look at the total amount. It's important to compare segments of expenses and taxes against each other year-to-year. By doing this, you will recognize significant changes in certain expense categories year-to-year. Then you can inquire accordingly about what changed or why things changed.

One final word of advice: review your annual expense and tax reconciliation even if you receive a credit. Just because the total amount of building expenses was less than what you were charged doesn't mean that everything you were charged was in compliance with your lease. Operating expenses and tax costs can be a significant part of your total occupancy cost, so it is worth reviewing your reconciliation each year. Some companies audit their expenses every three to five years because they have large spaces. If you contact your property manager each year and inquire about expenses and the budget, they will be less likely to charge expenses that are not allowed in your lease.

Article submitted by Wayne Teig / ITRA Global Minneapolis-St. Paul, Minnesota USA