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Don't Forget to Review Your Annual Expense Reconciliation

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For tenants with net leases, the annual expense reconciliation bill from your landlord will arrive soon. While sometimes tenants receive a credit, often they receive an invoice to pay. In either case, you should carefully review the expenses passed through to your company by your landlord for the prior year. This is especially important given the impacts of Covid-19, which caused much lower actual occupancy for office buildings.

For office building tenants, here are the top five things to look for in your expense reconciliation this spring:

1. **Utility Costs**: The expenses for electricity should be lower because of the lower number of hours that office spaces were occupied. When computers and lights aren't on, the amount of electricity used is less.

2. **Trash Removal**: If there isn't as much trash, the cost should be lower as compared to previous years, provided that the property manager modified the service accordingly.

3. **Snow Removal**: Some office buildings didn't plow the entire parking lot during the pandemic because less plowed stalls were needed. Hopefully that will be the case for your building and result in lower costs versus prior years. That said, snow removal costs are a function of how much it snowed as well, so the savings could be offset if your area had more snow than in prior years.

4. **Janitorial Services**: When the spaces aren't occupied, the amount of cleaning should logically be less. However, some building owners and managers adding cleaning services to combat Covid-19. Each building will be different.

5. **Gross Up Clause**: This is a lease clause and not an official expense. However, the landlord's use of a gross up clause does increase a tenant's expenses. The gross up clause allows the landlord to artificially increase occupancy sensitive expenses like utility costs, trash removal, and janitorial services, when the total building occupancy is less than a certain percentage occupancy.

The percentage noted in your lease might say 100%, 95%, 90%, 85% so you will need to check your lease to find out this number. Landlords use the word “occupancy or occupied” interchangeably with “leased”. So, if your building is 100% leased, then there should not be any gross up of expenses, even if very few people were actually using the building during the pandemic.

It is important to compare your 2021 actual expenses versus 2019 total actual expenses since 2019 was the last year not impacted by the pandemic. That will provide a basis of comparison for your building when it was actively being used versus any drop in usage due to pandemic concerns.

It makes sense to review your annual expense and tax reconciliation even if you are receiving a credit. Just because the total amount of building expenses was less than what you were charged does not mean that everything you were charged followed The terms in 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. If you contact your property manager each year to check on expenses, they will be less likely to charge expenses that are not allowed in your lease.

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