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LANDLORD CONSIDERATIONS AND RECOVERY PROVISIONS

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In the consideration of leases, lawyers are often asked to review the provisions relating to recoveries by a landlord for operating costs and property taxes. Leases that state that they are “net” leases often are not when a review of the provisions dealing with a landlord’s recoveries is undertaken. These provisions often contain exceptions which prohibit recoveries of certain items, and in certain instances. There are often exceptions for specific tenants, negotiated as a business item in the offer to lease, for government tenants, anchor tenants and big box tenants.

Each landlord should sit down and undertake a careful analysis of the recovery provisions in its leases. In undertaking such an analysis the landlord’s accountant or accounting staff needs to be engaged. Test calculations need to be run to determine what is and what is not recoverable.

It is also necessary to ensure that when entering into an offer to lease that the provisions relating to additional rent mirror or do not conflict with the terms of the standard form of lease.

If it is the landlord’s intention to provide exceptions or ceilings for government, large box and anchor tenants, does the landlord intend to pass on to other tenants the projected shortfall? If so, the provisions providing for recovery need to be drafted to give the landlord the right to charge any shortfall to other tenants. Prior to doing this a business consideration needs to be made, and that is the consideration of the impact on the costs being charged to the other tenants and the impact on the landlord’s competitiveness in the marketplace, which will impact on the landlord’s ability to lease, or cause the landlord to absorb all or part of such amounts thus reducing its rate of return.

When a landlord is considering changes in the recovery provisions in its standard form of lease, or upon the acquisition of a new property and considering imposing its standard lease rather than use the lease utilized by the previous owner, a landlord must undertake a careful review of the lease utilized by the previous landlord and what it is proposing as a replacement. The review needs to determine how they will complement each other, and to ensure that there not an uneven recovery of costs. It also has the potential



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of creating an accounting nightmare in that recoveries will then differ from tenant to tenant, with the result that the landlord cannot impose a blanket recovery program, but must review each tenant's lease separately and make an allocation separate to each tenant. An aggregate calculation of such will determine whether the landlord has made a full recovery or is subsidizing the recoveries. It is to be noted what is not recovered by the landlord from the tenants will be borne by the landlord. A landlord does not want to be in a situation where after a number of years the actual costs greatly exceed what the landlord is able to recover from a tenant, and the shortfall is borne by the landlord out of the basic rent, such that the landlord is in a real loss position.

The foregoing is not meant to be complete and comprehensive, but is meant to cause landlords to undertake the appropriate review of its leases and its procedures to ensure that it maximizes its recoveries.

For advice on the foregoing and other lease drafting tips, please contact a member of the Commercial Leasing Practice Group at Richards Buell Sutton LLP.



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