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Insights

Common Area Maintenance and Operating Expenses in Commercial Leases: What Should and Should Not Be Included?

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In commercial leases, "operating expenses" (often referred to as OPEX, CAM or Common Area Maintenance) generally cover the costs associated with the daily operation, maintenance, and repair of the property. In addition to base rent, landlords will often collect CAM charges as additional rent. This can often lead to a disagreement about what expenses should or should not be included in CAM.

Typical Inclusions in CAM Charges

Common charges typically included in CAM are:

- **Real Estate Taxes:** Property taxes levied by local governments.
- **Property Insurance:** Coverage for the building against various risks like fire, damage, and liability.
- **Utilities for Common Areas:** Costs for electricity, water, gas, and sewer in shared spaces like lobbies, hallways, and parking lots.
- **Maintenance and Repairs:** Routine upkeep of common areas, including landscaping, snow removal, parking lot maintenance, and repairs to the building's core systems (HVAC, elevators, plumbing, roof).
- **Janitorial Services:** Cleaning of common areas.
- **Security:** Costs for security personnel or systems.
- **Property Management Fees:** Fees paid to a property management company for overseeing the building's operations.
- **Administrative Charges:** Sometimes a percentage of the total operating expenses to cover the landlord's administrative costs related to managing the property.

Common Exclusions from CAM Charges

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Commercial leases often specifically exclude certain costs from operating expenses, as these are typically considered the landlord's responsibility or not directly related to the general operation of the property for all tenants.

Common exclusions include:

- **Capital Expenditures/Improvements:** Major structural repairs or upgrades that significantly extend the life or value of the building (e.g., a new roof, HVAC system replacement, major lobby renovations). While sometimes negotiated to be amortized over their useful life and partially passed through, they are generally not considered routine operating expenses.
- **Debt Service:** Mortgage payments (principal and interest) or ground lease payments on the property.
- **Leasing Commissions, Advertising, and Tenant Build-out Costs:** Expenses incurred by the landlord to attract new tenants or prepare individual tenant spaces.
- **Costs Covered by Insurance or Warranties:** Repairs or damages that are reimbursed by insurance proceeds.
- **Legal Fees for Disputes/Negotiations:** Legal costs related to landlord-tenant disputes, lease negotiations for specific tenants, or violations of law present at the commencement of the lease.
- **Depreciation:** The accounting deduction for the wear and tear of an asset.
- **Costs Related to Landlord's Corporate Overhead:** General administrative expenses not directly tied to the specific building's operation.

Legal and Accounting Considerations

The specific inclusions and exclusions can vary significantly based on the type of lease (e.g., Gross, Modified Gross, Triple Net) and are often heavily negotiated. One common provision found in commercial leases ties operating expenses to GAAP (Generally Accepted Accounting Principles), although even then there can be disagreement.

Another common consideration that has emerged is whether cost-saving efforts that would otherwise be considered a capital expenditure should be included in operating expenses. For example, if a landlord installs solar panels on the roof that lessen electricity costs (borne by tenants), should the installation cost be recoverable to the landlord via operating expenses? If so, should they be addressed in the same manner as the amortization of other capital expenditures? Or should they be treated differently given the immediate and ongoing cost savings the tenants realize throughout the term of the lease?

Given the wide array of considerations, landlords and tenants should carefully review the operating expense clauses in their commercial leases. They should clearly understand their financial obligations, consider negotiating what costs should and should not be included in CAM charges, and potentially negotiate caps on controllable operating expenses and audit rights to ensure transparency.