



Set Reasonable Charge For After-Hours HVAC Service

Issue to Negotiate

A tenant at your office building wants you to supply after-hours HVAC at its space. How should you set the cost for the after-hours HVAC? With sky-high energy costs these days, this added expense may not be trivial.

Your View

You want to be adequately reimbursed for providing the after-hours HVAC. After all, you are providing a building service to the tenant beyond what you usually provide. Therefore, you will try to set the cost of after-hours HVAC at the market rate. Plus, even if your regulatory authority bars you from marking up utility costs, you are not barred from recouping the cost of the use of your equipment, such as chillers, compressors, and fans.

Tenant's View

The tenant may worry that your version of the market rate will be more than it should pay. Instead, the tenant may demand that you pass through only your "actual cost" of the after-hours HVAC service, which is typically a lot less than the market rate. Also, the tenant may try to require you to exclude equipment depreciation and administrative fees from the actual cost formula.

Compromise: Set Charge at Actual Cost Plus Related Costs

To appease your tenant, agree that the charge of after-hours HVAC will be set at

your actual cost, says Santa Monica, Calif., attorney Susan Fowler McNally, who contacted us recently after confronting this issue with a tenant's auditor. The auditor had questioned the reasonableness of an owner's market rate charge for after-hours HVAC.

However, McNally adds that you should also make the tenant pay all costs related to your actual cost of after-hours HVAC. For example, your engineer's time to turn on and off the after-hours HVAC should be in addition to your actual cost because it is not part of the engineer's basic services, she explains. Thus, the tenant should pay extra for it.

Plus, you should insist that the tenant also pay equipment depreciation because its extra use of the HVAC equipment will shorten the equipment's useful life. Also, ask for an administrative fee to process the after-hours HVAC cost, suggests McNally.

To get this compromise, add the following language to your lease, says McNally (make sure you define "After-Hours HVAC" elsewhere in the lease):

Model Lease Language

Landlord will provide the After-Hours HVAC at Landlord's "Actual Cost," which is defined as the sum of the actual costs incurred by Landlord in providing any particular service, including Landlord's direct costs, engineering labor cost, applicable depreciation related to the increased

utilization of equipment to provide the service, repair and maintenance costs, and Landlord's reasonable estimate of related administrative cost for such service (to the extent not duplicative of costs included in Operating Expenses).

PRACTICAL POINTER:

Get the right to pass through the entire cost of after-hours HVAC to the tenant if the tenant is requesting that the engineer perform the after-hours HVAC related-service for itself, and not for any other tenants, says McNally. This is true even if the engineer is not required to work overtime. Performing these after-hours HVAC services for the tenant alone takes away time the engineer has to perform basic services that benefit all of the building's tenants, she explains.

After-Hours HVAC Actual Cost Formula

The tenant may demand that you also include an after-hours HVAC actual cost formula in the lease. This will force you to disclose all fees included in your actual cost, explains McNally. Here is a sample of

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Susan Fowler McNally is a partner at Gilchrist & Rutter in Santa Monica, Calif. Her practice focuses on commercial real estate and business transactions.

After-Hours HVAC *continued*

an actual cost formula that McNally used in one of her leases:

After Hours HVAC Actual Cost Formula

Direct Costs Cost Per Hour

Chiller \$10.10

Chilled Water Pumps..... 1.19

Condensor Pumps 3.71

Cooling Tower Fan 2.73

Air Compressor..... 7.35

Floor Fan 1.43

Engineering Labor

Engineering labor cost
& overhead allocation 18.65

Equipment Depreciation

Equipment Cost/Equipment Life (20 years)
at normal annual operating hours..... 3.70

Repairs and Maintenance

Yearly Cost/Annual Operating Hours . 0.70

Total Hourly Rate \$49.56

If you include an actual cost formula in your lease, be sure to add a disclaimer to help protect your wallet, advises McNally. The disclaimer should state that:

▪ The hourly rate listed in the formula is intended for informational purposes only,

and is designed to show how you will be charged for after-hours HVAC service;

▪ You are not making any representation that the hourly rate actually charged to the tenant will be the same as the hourly rate listed in the formula; and

▪ The hourly rate covers actual costs and direct overhead that was not otherwise reimbursed to you, plus an administrative fee.

To get such a disclaimer, add the following language to your lease after the actual cost formula, says McNally:

Model Lease Language

The hourly rate shown above is for informational purposes only, in order to indicate the methodology for charging for after-hours HVAC under the Lease. Landlord makes no representation or warranty that the after-hours hourly rate charged to Tenant under the Lease will be the same as the rate shown above. The foregoing categories of costs shall be utilized in determining the after-hours HVAC hourly charge at the Building, which rate will be established on a historical and projected use basis (as the foregoing example has been). The hourly rate

will cover only actual costs and direct overhead (to the extent such costs or overhead are not otherwise reimbursed to Landlord) plus an administrative charge payable to Landlord of *[insert percentage, e.g., five percent (5%)]* of the total costs and expenses (excluding such administrative charge) included in the after-hours rate.

Be sure to show your Model Lease Language to an attorney in your area before using it in your lease.

CLLI Source

Susan Fowler McNally, Esq.: Partner, Gilchrist & Rutter, 1299 Ocean Ave., Ste. 900, Santa Monica, CA 90401, (310) 393-4000.

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