

Four Strategies to Understand and Defend Against Poor Audit Rights and Restrictions

By Dave Robinson on September 24, 2024



I recently led a session at the **National Retail Tenants Association Annual Conference** on audit rights and restrictions that focused on the critical topic of verifying “pass-through” Common Area Maintenance (CAM) charges and expenses, a pivotal aspect of cost management for large retail tenants managing leased properties. This session delved into the complexities and strategies essential for effective oversight in this vital area of retail tenancy.

In principle, the tenant is only required to reimburse the landlord for CAM expenses agreed to in the lease. However, due to a variety of reasons, tenants can be overcharged on CAM expenses, which can greatly increase their costs over their entire portfolio. Accordingly, it is paramount for a tenant to be able to audit their expenses and seek reimbursement in the event they have been overcharged on CAM. Unfortunately, there are a host of barriers/defenses impeding a tenant's ability to obtain the necessary information in order to verify the CAM.

Here are some of the more common issues in CAM disputes:

1. **Lease Audit Rights:** In general, if the lease is silent as to auditing CAM charges, a tenant has the right to audit these charges and to request supporting documentation. However, the lease itself may prohibit/restrict a tenant's rights to audit, often under the guise of an audit “rights” provision. Usually, the audit provisions in a lease restrict a tenant's rights by limiting the period a tenant can audit, barring audits after a certain period of time, or even restricting the type of documentation a tenant can receive. Accordingly, it is critical to negotiate audit provisions that do not substantially restrict a tenant's right to audit and receive backup documents.
2. **Non-Disclosure Agreements:** Often, the landlord may require a non-disclosure agreement (NDA) to preserve confidential information as a condition of audit. Before signing such an agreement, the tenant should first determine whether the lease requires it. Second, the tenant should review the NDA terms to make sure that they do not modify or waive the lease or the tenant's right to audit.
3. **Estoppels:** Estoppels are legal documents that are commonly used in transactions related to purchases or refinancing of commercial real estate. At their essence, an estoppel is a statement by the tenant that the landlord is not in breach of the lease, which assures the purchaser/lender that there are no hidden liabilities that could undermine the transaction. However, an estoppel certificate is potentially a trap for the unwary because the landlord could later use it as a barrier to a CAM claim. Indeed, there is a potential risk that the tenant has waived any claims occurring before the date of the estoppel. Accordingly, if a tenant has not audited the premises in question, to preserve any such claims, it must include a disclaimer in the estoppel certificate

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preserving its rights to audit. Additionally, as a side note, an estoppel request is an opportune time to audit because the landlord is motivated to quickly resolve the audit and close its transaction.

4. **Withholding Rent:** Tenants may be tempted to withhold rent where the landlord is non-responsive concerning a CAM audit or rejects a claim for reimbursement as an alternative to a lawsuit. However, this strategy could backfire because the failure to pay rent is a default under the lease unless there is an explicit right to offset rent. As such, withholding rent could give the landlord the right to terminate the lease and evict the tenant. Many jurisdictions have a “fast track” eviction actions, so tenants could be faced with lawsuit where they have only a few weeks or months before having a trial of the merits. So, the tenant’s attempt to avoid litigation could actually draw them into a fast tracked and more expensive litigation with the added “bonus” that if they lose, they also lose the premises and likely be liable for years of rent remaining on the lease. Accordingly, tenants should carefully examine their options with counsel before withholding rent.

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