



The Escalation Handbook for Office Buildings

A Guide to Understanding, Preparing and
Grossing Up Expense Escalations

THIRD EDITION

William H. Brownfield, CRE, CCIM
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BOMA
International

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FOREWORD

Many property owners and managers lament the difficulties of determining a fair process for calculating the escalation of expenses in an office lease, both before and after a lease is signed. During lease negotiations, both owners and tenants confront the problem of deciding how to treat rising expenses in subsequent years. If the total expenses in a building rise from one year to the next, is it attributable to a higher cost of doing business or is it attributable to a rising occupancy level in the building? If it is both, how much of the total rise is attributable to each, and who should pay for them?

This book, updated to include evolving industry practices of the last decade, provides insight and understanding of the varying escalation methodology used in office building leases, as well as how to calculate the amounts that are recoverable under a lease. The methods include the practices described as “grossing up” the actual expenses in a building to adjust for less than full occupancy levels, and amortizing capital expenditures. Using expense calculations that reflect what the building would cost to operate if it were full, the owner and the tenant can equitably allocate expense changes caused by shifts in occupancy levels or changes in the cost of services provided.

ABOUT THE AUTHORS

William H. Brownfield resides in Houston, Texas. He is actively involved in buying, selling, managing and leasing office buildings. He has been responsible for managing more than 28 million square feet of office properties and has helped acquire \$1 billion in real estate assets. Bill has been an active member of BOMA, IREM, CCIM and CRE and is a contributing author to *The BOMA Magazine* and the *Journal of Property Management*. He is a Counselor of Real Estate (CRE), a Certified Commercial Investment Member (CCIM), a former Certified Property Manager (CPM) and received his Master of Business Administration and B.S. in Business Management degrees from Missouri State University.

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Larry co-founded Brownfield & Mayerhofer in 1998, and led the design team for ARGUS Office Escalations (formerly known as BOMA's Escalation System for Office Buildings). He provides support for the product along with escalation training, seminars, webinars and client consulting.

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PREFACE

Twenty-five years have passed since this handbook was originally published by BOMA International. Fifteen years have passed since our last update, and as you might expect, the office building industry has continued to change and grow and improve during that time.

Not surprisingly, lease documents and operating expense escalations for office buildings have evolved along with the industry, and this update is designed to explain those changes to you in an easy-to-understand manner. We hope to have achieved this goal.

What's New?

First, we have added **SECTION THREE: NEW TOPICS**, which is comprised of three new Chapters whose subjects have grown in importance relative to escalation theory, as each one has become a common topic of discussion:

- **CHAPTER EIGHT: Expense Caps.** In larger cities, 90 percent or more of tenants hire office leasing brokers to represent them during lease negotiations. Capping controllable operating expenses has become a favorite topic of negotiations. In this Chapter, we explain expense caps and help you understand how to properly calculate them for your tenant leases.
- **CHAPTER NINE: Managing An Escalation Audit.** Most sophisticated tenants now perform annual audits of escalation billings to ensure that their share of operating costs is in line with what their leases specify. This Chapter will help you prepare for those audits and help you successfully manage the process so that your tenant relationships will remain positive.

- **CHAPTER TEN: Going Green, Getting Rated.**

BOMA 360, LEED and other performance rating systems have transformed how the office building industry thinks about and builds environments for office workers. Who should pay for costs associated with Going Green? This is just one of several questions being asked by industry professionals, so we include a discussion of how these issues can have an impact on the calculation of operating expense escalations.

Second, we have included an **Addendum** entitled:

- **Q&A from BOMA Escalation Seminars & Webinars.** We've taught numerous escalation seminars and webinars around the country. Some have been given to private groups, but most have been sponsored by BOMA International. With thousands of attendees, you can imagine the broad range of questions asked by industry professionals at these educational events. Their questions, and our answers, have been assembled into seven major categories that we hope you will find useful when researching different topics as you prepare future escalation billings for your tenants or when tenants or auditors quiz you about your methodology.

We have also updated numerous charts and Exhibits throughout all Chapters to reflect office building expenses that are current with today's operating environment.

What Hasn't Changed?

Lease language is rarely the same for any two tenants and is continually modified to suit each building due to continual and evolving negotiations