PROPERTY TAXES AND THE GROWING MILLENNIAL IMPACT ON THE RETAIL SECTOR

By Kirk Garza

As researchers continue to debate how market conditions affect the value of commercial real estate, one thing is certain: Appraisal districts across Texas are recalculating taxable property values. To ensure fair tax assessments, it is crucial for retail property owners to monitor demographic and technological changes that can disrupt retailers' sales and a shopping center's overall income potential.

Here are a few points for taxpayers to broach when helping assessors determine correct taxable property value.

Consumers spent more on dining out than at the grocery store last year, a historical first, according to Marcus and Millichap's 2016 U.S. Retail Investment Forecast. With millennials dining out more than other age groups, this trend will likely continue.

Some landlords are shifting the balance of stores, restaurants and bars at their properties to lure millennial shoppers.

Conversely, changing consumer demand is weighing on outdated shopping centers that require significant renovation to remain relevant. Even with the right updates, a center could suffer from external obsolescence, or conditions outside the property that reduce its value.

Millennial Impact

The growing influence of millennials has also increased demand for convenience commerce.

Businesses such as Instacart now enable consumers in some markets to order groceries and goods directly from major grocery chains using smartphones, to be delivered to their home in as little as one hour.

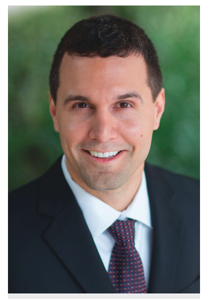
E-commerce companies are adapting services that were once accessible only in a retail space and delivering those conveniences to the consumer. Entrepreneurs have already begun to experiment with mobile services ranging from dog grooming, manicures, hair styling and even massage therapy.

As the availability of services grows in step with millennials' disposable income, owners of shopping centers offering similar services may see a decrease in foot traffic within their developments.

Shopping centers with tenants that cannot adapt to this service delivery model may be exposed to significant vacancy risk.

Adapting to the Market

Many national retailers adapting to e-commerce growth have announced store closures in 2016. Many of these retailers are investing significant capital into their omnichannel platform, suggesting that additional store closures are still to come.



Kirk Garza
Popp Hutcheson PLLC

With the continued growth of e-commerce, some industry observers believe that retailers will reduce the size of their showrooms or sales floors to allow more square footage for warehouse fulfillment space.

More warehouse space would allow retailers to process merchandise for pickup or delivery without interfering with the shopping space for customer foot traffic.

In this scenario, market rental rates that represent part showroom and part warehouse space would be appropriate for assessors to use when applying the income approach to value.

Adapting to Change

Taxpayers must always ensure that assessors use correct rates and values as comparables, otherwise the assessor could reach an improper value.

Additionally, as retailers across the nation continue to experiment with smaller store footprints, assessors must consider the potential for that trend to reduce the market value of large boxes and inline spaces, with a corresponding impact on property values.

Shifting demographics, the evolution of convenience commerce and retailers' adaptation to e-commerce can profoundly increase or decrease a retail property's value.

These trends demand that assessors carefully analyze a property's individual characteristics as well as the market area in which the subject is located.

Apparel tenants may be the most at risk of losing sales, but landlords must also consider the viability of other tenants that could occupy the retail space at market rents.

The assessor should consider this uncertainty when selecting capitalization rates. Also discuss with the assessor year-over-year changes in income and expenses, and in tenant health, within the subject property.

By protesting property taxes, landlords can pass any tax savings onto their tenants, who typically reimburse the landlord for taxes, depending on the terms of the lease. In addition, a successful tax protest may enable the landlord to quote lower operating expenses, which can help attract and retain retailers.

Correct analysis can identify any obsolescence that may exist, enabling the assessor to adjust taxable value accordingly.

And with a more accurate picture of the property's marketability, the assessor will be in a better position to judge proper market rents, vacancy and collection loss, and capitalization rates. Only with all these essential pieces can the assessor correctly determine a retail property's taxable value. ■

Kirk Garza is an MAI and licensed Texas Property Tax Consultant with the Texas law firm Popp Hutcheson, PLLC. The firm devotes its practice to the representation of taxpayers in property tax disputes and is the Texas member of the American Property Tax Counsel (APTC), the national affiliation of property tax attorneys. Garza can be reached at kirk.garza@property-tax.com.