THE UNMALLING OF AMERICA

How Municipalities Are Navigating the Changing Retail Landscape

By Gregory Scruggs

THE STRUGGLING BANGOR MALL is a national parable of changing retail habits. Built on a former dairy farm in Maine, the mall threw open its doors in October 1978, growing to serve up to two-thirds of the state's population with a plum location off a main thoroughfare, Interstate 95, in the middle of the state. For decades, the mall contributed handsomely to the local tax base, to the tune of $1.2 million per year. In recent years, however, the cream-colored structure with blue trim that once anchored Maine's third-largest city has gone through the same hard times affecting shopping malls across the country.

Over the past two decades, consumers nationwide have made significant shifts in their shopping habits, migrating to online retail and returning to traditional commercial corridors and shopping districts in economically strong metro areas. Meanwhile, Walmart has consolidated its position as the nation's largest brick-and-mortar retailer, with a strong clientele of rural, exurban, and small-town customers. As a result, once-venerable retail brands like Sears and Toys 'R' Us have faced bankruptcy.

This disruption has created a checkerboard of vacancies nationwide, including on the expansive 88 acres of the Bangor Mall, which is now anchored by Dick's Sporting Goods and Furniture Mattresses & More. Other longtime retailers in the space, like department store JCPenney, have signed lease extensions, though the mall's very future remains wobbly as out-of-state owners grapple with retail headwinds. In 2017, then-owner Simon Property Group of Indianapolis—which owns retail properties in 37 U.S. states and Puerto Rico, as well as in Europe and Asia—defaulted on an $80 million loan that had used the mall as collateral. The property was sold at auction to a New York-based investor trio in February 2019 for $12.6 million, less than half of its assessed value.

Those assessments have fallen precipitously in recent years due to the decrease in estimated net operating income and increase in vacancy, according to Bangor City Assessor Philip Drew. The mall has seen consecutive year-over-year reductions of roughly 25 percent, from $60.9 million in 2017 to $46.3 million in 2018 to $34.6 million in 2019. In both 2017 and 2018, years that saw the departures of flagship tenants Macy's and Sears, respectively, the mall's owner paid its taxes, but appealed for reductions in its assessment given the precarious situation at the property. Drew denied the requests, and his decisions have been appealed to the State of Maine Board of Property Tax Review.

Credit: uschools/iStock.

In Bangor, Maine, fiscal losses related to the decline of the city's 88-acre shopping mall, left, have been offset by reinvestments in the downtown area, right. Credits (left to right): Ten-X Commercial, Denis Tangney Jr/iStock.

In the meantime, the Bangor Mall's tax bill has dropped below $1 million for the first time in two decades. Such an outcome may sound like a major hit to Bangor's budget, but the blow turned out to be manageable, Drew says. The mall accounts for 1.31 percent of the city's total taxable valuation. But the shifts at the mall aren't the only changes afoot: overall, Bangor collected more property tax revenue this year than last. "The city's taxable valuation growth has recently occurred in the downtown district, with a new bank campus owned by Bangor Savings Bank valued at $22 million and the remodel of downtown structures to satisfy the demand for downtown apartments," Drew says.

In other words, while a mall on the edge of town sputters, Bangor's downtown is thriving, and the loss of property and sales tax from one has been compensated for by the other. It's the result of a downtown revitalization plan Bangor started in the 1990s. It's also part of a growing counternarrative to the dominant media story of the past decade, which predicted that the surge in online shopping would spell the end for brick-and-mortar retail, potentially damaging municipal fiscal health along the way.

As this shift plays out in communities large and small across the United States, the facts are more complicated than those media accounts would suggest—and the outlook is more optimistic than the headlines portend. By implementing proactive measures from investing in downtowns to rethinking the use of the valuable acreage occupied by malls, Bangor and other jurisdictions are demonstrating how to navigate the changing retail tides.

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Why Retail Matters to Municipalities

Retail typically accounts for approximately one-quarter of all commercial property value. Whether retail is make or break for a municipal budget, however, varies widely.

That local governments fund their operations in large part on property taxes is no secret (see Figure 1). The revenue source accounts for 72 percent of the total local taxes collected in 2015. While the ratio of residential to commercial properties varies from community to community, as do the respective tax rates placed upon those properties, retail typically accounts for approximately one-quarter of all commercial property value. Whether retail is make or break for a municipal budget, however, varies widely.

"In some communities dependent on malls, they can make up 20 to 30 percent of their tax base and other taxpayers may have been paying relatively less," says Lincoln Institute of Land Policy Fellow Ron Rakow, former assessor for the City of Boston. Rakow has conducted research on the tax implications of the changing retail environment. "If the mall isn't doing as well, the community is either going to have to reduce services or increase taxes for others."

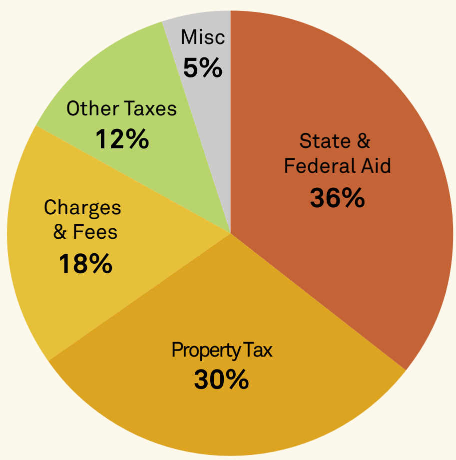
Onondaga County, which surrounds Syracuse, New York, is among those communities facing such tough choices. ShoppingTown Mall opened in 1954, placing it among the earliest U.S. shopping malls. A succession of major tenants, including Macy's, Dick's Sporting Goods, JCPenney, and Sears, has closed since 2015. The mall's assessment has dropped precipitously as well, from $53 million in 2008 to $36 million in 2014. Meanwhile, the mall's owner, Moonbeam LLC, has resisted paying its tax bill to Onondaga County. In June 2019, the company missed a deadline to pay $9.7 million in back taxes dating to 2015. The county is trying to foreclose on the mall in order to redevelop the site, but in August 2019 the company announced its intention to head to bankruptcy court to avoid losing the property.

It's not just property taxes that are a factor, of course. "Retail is huge, not only from a property tax standpoint, but also [in terms of] sales tax," says Marc Moffitt, senior research analyst at the Denton (Texas) Central Appraisal District and an adjunct faculty member at the University of North Texas.

Sales and other non-property taxes account for about 12 percent of municipal tax revenue. So far, that revenue stream appears to be holding steady nationwide. In the Rockefeller Institute's most recent state revenue report, covering the fourth quarter of 2017, sales tax collection increased 4.8 percent, doubling the typical quarterly average (Dadayan 2018).

The combination of property and sales tax that retailers provide makes for a potent one-two punch. "There are Texas towns that are 80 percent residential, but the 20 percent that is commercial makes up the tax base," Moffitt says.

FIGURE 1 Local Government General Revenue Sources



Source: U.S. Census, 2017 Census of Governments: Finance

At left, a shopping mall demolition in Westminster, Colorado. Credit: JohnGiez/Flickr CC BY 2.0. At right, Sears closing in Holyoke, Massachusetts. Credit: JJBers/Flickr CC BY 2.0.

Reinvesting in Downtowns

There are 8.5 billion square feet of retail space in the United States, which equates to 24.5 square feet of retail space per capita, or five times Europe's average of 4.5 square feet per capita.

Moffitt looks to the 13 regional malls sprawled across the Dallas-Fort Worth metro area where he lives as a classic example of the overbuilt mall environment. "How many regional malls can you have in one region?" he asks.

Local governments have seen the mall contraction coming. Most malls have been struggling to maintain close to full occupancy for at least a decade, sometimes up to two decades. "The general trends support the fact that increasing vacancy rates are likely for some regional malls," Bangor assessor Drew says. Moffitt predicts that such vacancies will increase 20 percent over the next five years.

That makes the forthcoming decade a crucial transition period as consumers vote with their feet and their wallets, staking out a preference for denser, walkable urban environments over big-box stores and shopping malls. In 2019, a report from the George Washington University School of Business and Smart Growth America claimed that "walkable urban places," which meet a certain threshold of real estate, walkability, and human interaction density, were gaining market share faster than their suburban counterparts in the country's 30 largest metro areas (Loh 2019).

This trend includes both infill in central cities and the urban redevelopment of traditionally car-oriented outer areas. While booming metropolitan economies are driving this increasingly urban pattern in the built environment—New York City, Washington, DC, Chicago, Boston, the San Francisco Bay area, and Seattle top the list—smaller communities are catching on.

Sheboygan, Wisconsin, on the shores of Lake Michigan, is seeing the fruits of decades of work to revitalize its downtown. The construction of two malls in the area in the early 1970s "essentially sapped the economic life out of the downtown," according to *Downtowns: Revitalizing the Centers of Small Urban Communities* (Buriyidi 2015). The city began to explore strategies for bringing residents and shoppers back downtown as early as the 1980s, creating a retail-focused Business Improvement District in the 1990s, but the local shopping hub, Memorial Mall, remained a significant player in the financial mix. A decade ago, the city lost $1.3 million in annual tax revenue when Memorial Mall, which eventually closed in 2017, challenged its tax assessment.

The mall wasn't the only commercial taxpayer to take issue with its bill; Walmart is now seeking tax reductions of $90,000 and $180,000 for 2017 and 2018. The effort by Walmart is one of many initiated by the retailer in municipalities across the country, and is part of an ongoing conflict between big-box retailers and municipalities regarding the fairness of property tax assessments. The tension has led to legal appeals in at least 21 states over the past 10 years, according to a survey of the International Association of Assessing Officers conducted by *CityLab* in 2018, and has led at least four states to consider legislation that would regulate assessments for big-box properties.

Despite these losses, Sheboygan has managed to maintain its existing city services without increasing residential property taxes. How? Parallel with Memorial Mall's demise, Acuity Insurance has bet big on the 50,000-person beach town 60 miles north of Milwaukee. The mid-sized insurance company, founded in 1925 and active in 27 states, has made major investments in its corporate headquarters in Sheboygan, expanding the building and hiring hundreds of people. Although the headquarters itself is located outside of downtown, new downtown apartments have sprung up to house its growing staff, contributing to the ongoing revitalization effort there. Sheboygan is also investing in a downtown innovation district and launching a pop-up retail program that offers short-term leases to small business owners.

As in Bangor, these downtown development efforts have helped Sheboygan absorb the loss of a mall that was once a major contributor to its tax base. This kind of rebound isn't feasible everywhere, Rakow points out: "If a community's economy and population is not growing and healthy, it will be difficult for [businesses] to thrive, whether in a mall or downtown." But in Sheboygan, officials are demonstrating that there can be life after the mall.

"While in the past it was one of the higher valued properties, the loss of value affects the mindset more than the pocketbook," says Sheboygan City Assessor Mike Grota.

Ripe for Redevelopment

Today's malls, some say, are the wrong use for the right site. That is, they generally have good locations near major roadways and in some cases public transit, and the large parcels of land they occupy are serviced with water, sewer, and electricity. "Malls as a property type are dead," says Moffitt, who says it's not *if* but *when* malls go under and are ready for redevelopment.

"What malls are worth right now is their dirt. Their structures have little to no value," Moffitt adds. "Investors view malls as mixed-use redevelopment opportunities better able to serve the community, and they are going to provide a much more robust sales and property tax base."

Stories of successful mall transformations are emerging. "Mall properties may no longer be exclusively retail on a forward-going basis," says Rakow. "To keep them economically viable and maintain the foot traffic that smaller retailers are so dependent on, other uses like museums, health clubs, and specialty food stores are coming into malls."

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Such a radical change from the mall as an exclusively retail environment may conflict with land use policy. Instead of serving as an obstacle to this transition, local government can seize the reins to help secure an economically vibrant future. "There is a whole new notion of communities working with mall owners if there are zoning or land use issues," says Rakow.

The nonprofit Kidzu Children's Museum occupies 8,500 square feet in University Place mall in North Carolina, and is planning to expand into an adjacent storefront, as depicted in this rendering. Credit: Courtesy of Kidzu.

Such is the case with University Place in Chapel Hill, North Carolina. In 2016, it was among the college town's top 10 taxpayers. The next year, it fell off that perch. "The square footage of the center represents a significant retail presence in our market," Chapel Hill Economic Development Officer Dwight Bassett says. "We would like to see new investment create new value and become a top taxpayer again."

For over a decade since Washington, DC–based Madison Marquette purchased the faltering mall, Chapel Hill has accommodated changes to the site from a traditional internal mall to one more externally facing. Now the mall is home to a children's museum, health club, and CrossFit studio. One large retail space was converted to Southern Season, a specialty food store that offers a wine- and beer-tasting bar, cooking classes, and a full-service restaurant.

"We allowed a new entrance on a major road, changed our sign ordinance and temporarily had our library located at the mall while we rebuilt our library," Bassett says. "I think that being a partner and constantly asking how we can help facilitate moving the center to a different market destination has been a key piece of the role we have played to date."

But not every mall transformation works out successfully. The Hickory Hollow Mall in the Antioch neighborhood of Nashville, Tennessee, lost the last of its two remaining department stores in 2011 and ultimately closed its doors. The mall's owners repositioned the property with a new name—Global Mall at the Crossings—and added a new community center, a community college satellite campus, a library, and a recreation center. As a potential anchor, the mall also hosts a practice rink for Nashville's NHL franchise. However, even after pumping in over $50 million, the mall continues to struggle. In November 2019, a plan to transform the mall into Nashville's first "innovation district" collapsed when a local developer backed out of the deal. Many of Hickory Hollow's storefronts continue to sit vacant. Without money coming in, the structure has fallen into disrepair.

Another path for malls is linked to the success of e-commerce: their location has proven appealing to Amazon for its distribution centers. While communities were initially eager to offer tax breaks to the online retail giant—especially in the course of its search for a second headquarters—that has begun to shift, according to Rakow. "Communities have caught on to Amazon," Rakow says. "Since Amazon needs to have these distribution centers strategically placed, communities aren't so quick to give tax incentives and breaks for the facilities. Amazon should pay its fair share just like any brick-and-mortar store. The notion of giving incentives doesn't seem like it's a wise fiscal practice."

Moffitt argues there are catalyzing moments when a small investment by the public sector, such as forgoing some property tax revenue, can pay a huge dividend. He points to Colin Creek Mall in Plano, Texas. A developer bought the dying mall, valued at just $10 million, with the benefit of a local property tax incentive and will recast the site with $1 billion in commercial development. "They are going to have 15 to 20 restaurants that spin off a ton of sales and liquor tax," Moffitt says. "It's a total game changer when it comes to the tax base."

Cultivating Offline Commerce

Four in every five U.S. consumers makes online purchases (Smith 2016), and nearly 40 percent of those online shoppers buy something on Amazon at least once a month (Selyukh 2018). That tendency impacts the built environment, but perhaps not as severely as often thought. “The internet shopping trend has magnified what I believe is a market oversaturation with retail space,” Moffitt says. In other words, a trend that was already underway has been exacerbated.

Moffitt breaks it down to simple supply and demand. “In a given 10-mile radius there are only so many discretionary dollars available to spend,” he says. “Those dollars either go to brick-and-mortar stores or go online. If some of those are going online out of convenience, what’s going to happen is those online sales are going to cannibalize a local brick-and-mortar store [selling the same types of products].”

But Moffitt says retail is far from dead. He points out that U.S. retail real estate currently sits at over 95 percent occupancy, which is even higher than at the 2007 peak before the Great Recession. New retail space continues to be built out and leased. And the future eaters and drinkers at Colin Creek Mall represent another truism about the changing retail landscape, per Moffitt: “There’s a lot of stuff you don’t buy on Amazon.”

Bars, restaurants, hair salons, barbershops, gyms, pet day care, and yoga studios are all types of retail businesses based on experiences or consumption rather than on goods. They are much better positioned to thrive in the new retail era.

For example, London School of Economics professor Lindsay Relihan has studied early adopters of online grocery platforms. In the first two years since switching to some measure of online grocery shopping, those consumers reduce their spending at grocery stores by 4.5 percent but increase their spending at coffee shops by 7.6 percent (Relihan 2017).

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Some experiences cannot be replicated online, and communities are counting on that to help support their local businesses. Credit: Brewbooks/Flickr CC BY 2.0.

"Policies that support a transition to service-oriented retail, and the density and accessibility of that retail, are likely to be key to local retail health," she says. "Transitions are very disruptive in the short run, but I don't see any reason why fiscal health should necessarily decline in the long run."

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Such service-oriented businesses, which rely heavily on foot traffic, tend to be located on main streets and traditional commercial corridors. Those locations are now "the most desirable from a retail real estate perspective," Rakow says. "They command fairly high rents and have lower vacancy." This trend bodes well for urban locations and less so for post-war suburban areas that lack the dense fabric of a main street or commercial corridor.

At the end of the day, Amazon and the acceleration of e-commerce still account for only about 10 to 11 percent of retail sales (USDC 2019). CBRE expects that market share to grow to just over 15 percent by 2022. Meanwhile, Walmart's big-box stores on the urban fringe continue to thrive, even as cities reinvest in their downtowns. As customer proclivities and technologies evolve, few can predict what the retail landscape might look like 10 or 20 years from now. But one thing is certain, as municipal leaders in Bangor, Sheboygan, Chapel Hill, and many other communities are discovering: keeping up with changing retail habits and their impact on fiscal health requires flexibility, creativity, and foresight.

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