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Shopping malls get a facelift and find savings by accelerating depreciation

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Popular media is full of gloom and doom predictions regarding the death of the shopping mall, citing the fact that 400 shopping malls in the U.S. have been repositioned or closed in the past decade, and no new shopping malls have been completed since 2009. However, the shifting landscape of retail markets does not signal the death of the shopping mall. Rather, the traditional shopping mall is experiencing an evolution as investors and developers work to meet the changing needs of the next generation of shoppers.

There are many influences, which are changing the shape and direction of the traditional American shopping mall. Competition among regular retailers is stiffer than ever, as on-line shopping and new delivery channels erode sales for "brick-and-mortar" stores. As a result, many department store anchors have disappeared due to bankruptcies and consolidations. And, consequently, the focus of the shopping mall industry has shifted. The success of today's shopping mall depends on the quality and character of its public environment, as much if not more than the quality of its shopping. The mall has become a gathering place, a location where people interact comfortably and spend time with others. In essence, its become the social hub for physically connecting and interacting with others.

Shopping Malls Renovate to
Provide Connectivity
and Community

In place of the standard shopping mall cube, developers are remaking malls with new design concepts, updated retail formats, and engaging public environments and amenities, all intended to draw an audience. Today's shopping mall offers a more urban experience, with pedestrian-friendly, street-front retail space and restaurants. Developers are using beautiful landscaping/gardens and outdoor spaces with seating to act as pedestrian centers and that also serve as a buffer between neighborhoods.

Another technique shopping mall developers are using to create a sense of community is to add decorative elements that as unifying structures, such as sculptures, fountains and/or plazas. These unique features add character and charm, giving the mall a better image as a destination.

To avoid traffic congestion, road layouts and circulation patterns are being improved by strategically locating parking areas and sidewalk connections. Clear signage and pathways also encourage movement in a pedestrian environment.

Offsetting the Cost of
Mall Renovations by
Accelerating Depreciation

Until now, the traditional shopping mall had relied on major department stores as anchors to draw customers. More recently, malls are looking at other avenues to attract customers, from entertainment venues such as movie theaters or outdoor concert areas, to off-price big box stores, such as Filene's Basement or Designer Shoe Warehouse.

While new construction has stalled, developers are rehabilitating and repositioning existing mall sites across the country. Renovating an aging mall is a tremendous investment. Many older malls were built before current construction standards. The construction materials, smoke detectors or fire sprinklers may all need to be updated. In addition, most malls were built without the expectation of other uses, such as offices, hotels or cinemas. Developers must ensure that the structure and infrastructure can hold up to the new demands on the water, gas and electric systems.

Such projects can incur huge expenses. Thankfully, the IRS does give direction in the classification and examination of improvement costs, in order to recover costs through depreciation of tangible property. For example, awnings and canopies, lightweight double action Eliason doors, and adhesive floor covering can all be reclassified as five-year property. Concrete foundations and footings, pole-mounted lighting systems, and parking lot surfaces can be reclassified as 15-year property. Reclassifying these assets as five-year or 15-year depreciation schedule can offset some of the investment in the makeover of a shopping center, resulting in significant tax savings for mall developers.

Most recently the IRS issued new regulations (TD 9564) on how to treat amounts paid to acquire, produce, or improve tangible property. Included in the new regulations is the "unit of property" concept. These new regulations reaffirm the concept of a write-off study. Previously, a building was treated as one unit; all renovation work was viewed within its relationship to the entire building. This allowed for the immediate expensing of repairs. Under the "unit of property" concept, a building is broken down into as many as nine structural components, with each component viewed as its own unit. While this limits the ability to deduct these expenses in the year incurred, with careful planning, it allows the opportunity for the taxpayer to take retirement losses for assets removed in the renovation. This should bode well for shopping malls and other real estate investments where the owners are putting in significant renovation dollars.

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