

# Dark Store Theory

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**B**ig-box retailers throughout the country—most of them corporate giants such as Home Depot, Lowe’s, and Target—are challenging the manner in which local governments assess the value of their properties. Their goal: lowering their tax bills. The tactic is known as the “dark store theory.” It occurs when retailers say their taxes should be calculated as if their stores were vacant or “dark,” rather than when they are at full capacity. When they succeed, and they have been succeeding, the amount of annual property taxes they pay can drop dramatically.<sup>1</sup>

## **ARGUMENT**

Because they are customized to a specific use, big-box retailers contend the buildings they occupy are difficult to sell. So far, the courts have agreed, and retailers across the country have seen their taxes go down by hundreds of millions of dollars.<sup>1</sup>

According to *Education Week*, the trend is most pronounced in the upper Midwest, where hundreds of lawsuits and appeals have been launched in Indiana, Michigan, and Wisconsin. In Michigan specifically, the argument has been made in roughly two-thirds of the state’s counties, resulting in a loss of at least \$75 million in property taxes between 2013 and 2015.<sup>1</sup>

## **MOTIVATION**

Real estate taxes are typically one of the largest expense items on the income statements and balance sheets of most brick and mortar retailers. In today’s growing e-commerce marketplace, retailers are being forced to close their less profitable stores. As one of the largest expenses, a store’s tax burden weighs heavily among the factors a retailer will consider in deciding which stores to close.

## **DEED RESTRICTIONS**

One of the principal reasons big-box retail stores remain vacant after closing is they use anti-competitive restrictions to prohibit the sale of the property to other big-box retailers or other similar retail users. When a retailer quits a store, it’s often just moving down the road or across town, and they don’t want a competitor to move into its empty space. So, they use deed restrictions to prohibit the future sale of food, clothing, garden equipment or whatever else might be considered competitive. The use of these restrictions makes the real estate harder to sell, as it’s simply not comparable to a property with no restrictions.

## SELF-IMPOSED FUNCTIONAL OBSOLESCENCE

Big-box retailers have also argued their stores are built to serve the needs of their specific big box and have limited functional utility to other retailers. However, their use of anti-competitive (deed) restrictions suggests otherwise: the stores are functionally useful to an array of other competing retailers who are otherwise prohibited from using them because of the deed restrictions. Notably, in 2016 the Michigan Court of Appeals concluded that while these restrictions distorted the market for big-box stores, the resulting low sale prices alone did not reflect functional obsolescence. That is, to argue a hindrance in a property's ability to function in the market, one must identify or explain the deficiencies impeding functionality – a fact that is likely to have important implications moving forward.

## COLLATERAL DAMAGE

In the past several years, legislators in Michigan and many other states have attempted to pass legislation intended to prevent big-box retailers from considering vacant or "dark" stores when valuing properties. Although thus far largely unsuccessful, these legislative attempts continue to gain momentum, and new legislation is in the works across many states that would close the "loophole." However, it turns out, one thing is certain: when big-box retailers shutter their brick and mortar locations—everyone loses, especially the local communities that depend on these stores, not only for their property tax revenues, but also



for the jobs they provide and the goods they sell.

At Environmental Consulting & Technology, Inc. (ECT), we will continue to follow this developing issue, particularly regarding the matter of functional obsolescence and how such a determination might provide opportunities for communities to leverage the reassessed values of big-box stores to facilitate the demolition and redeployment of vacated properties under a variety of state programs, including the Michigan Brownfield Redevelopment Financing Act and the Florida Community Redevelopment Act.

### Reference:

1. Vara-Orta, Francisco. (2017, August 2). Tax Breaks for Big-Box Stores Can Drain Money from Schools. Education Week.

Retrieved from:

<https://www.edweek.org/ew/articles/2017/08/03/tax-breaks-for-big-box-stores-can-drain.html>

## ABOUT ECT

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