

## Do landlords lose when chains promote Web?

By Steve McLinden

RETAILERS CONTINUE TO USE the Internet to drive sales, and though this makes sense, it leads some observers to wonder whether the landlords are losing out. Under pressure to squeeze as much as they can from an ever-shrinking supply of retail space, these retailers fade the line between store, Web and catalog sales.

There is more. Shoppers are increasingly eschewing the mails in favor of visiting physical stores to exchange or return items bought online or through a catalog; then they return home to order merchandise they have just seen promoted in the store but which is available only online, and this is throwing the retailers' sales-accounting systems out of whack.

Rents are tied to store sales, of course, so the question of where to credit these cross-channel transactions looms ever larger, and all the more as landlords get squeezed between tenant downsizings on the one hand and store closures on the other. "As that financial pressure continues to grow, we need to make sure that the accounting side for retailers is properly handled at the store level," said Kenneth S. Lamy, president of the New Orleans-based Lamy Group, a retail industry financial management consulting firm.

How often such store-initiated Web sales go unreported is hard to determine, Lamy says. "The only way to test how a retailer is handling this is to conduct a sales and compliance examination, also known as a tenant sales audit," he said.

One executive of a national shopping center ownership firm has noted a marked increase

in the number of retailers using store space to advertise items available online but not at their stores. "They feel they don't have to report that sale to the landlord," said this source, who requested anonymity. "And, of course, they don't have to rent space to stock that merchandise. This has not turned into a big problem yet, but it seems to be happening with more frequency."

Some chains and their landlords are starting to address the issue by means of lease language that deals specifically with such transactions. "Typically, if a store accommodates customers by allowing them to place an order or letting them pick up Internet or catalog merchandise there, many merchants don't consider it a store sale," Lamy said. "However, unless they are specifically excluded by the gross-sales definition in their leases, these transactions should still be reported to the landlord." Typically, lease language accounts for such sales as occurring "in, at, on or from" the use of a store, says Lamy. "Many leases are well worded, but not as well worded as they need to be."

Ivan Friedman, who heads New York City-based RCS Real Estate Advisors, says this accounting controversy is not new. "Landlords have been dealing with cell phone [sellers] for a long time," Friedman said. "While they get a percentage of the sale of cell phones, they typically don't get money from the sales of contracts." In a lot of cases, the debate is moot, Friedman says, because most tenants do not reach a point in gross sales volume at which they must begin paying a fixed percentage to the

landlord as additional rent. "In my opinion, the lease language has gotten pretty tight already," Friedman said. "The only thing the landlord can do is negotiate individually with retailers to get a percentage of Internet sales."

The quantity of Internet-only sales spurred by in-store promotion "is minimal," says George Whalin, president of Retail Management Consultants, of San Marcos, Calif. On the contrary, Web sites are often used to drive customers into stores for more expensive purchases that do get factored into rents. "About 70 to 75 percent of the higher-ticket items are researched on the Web before the customer goes into the store," said Whalin. "In fact, every retailer I know that has a decent Web site uses it as leverage to drive people into the store." Whalin argues that landlords should "partner with retailers on this accounting issue and not fight them. There are moneymaking opportunities on the Web for the smart mall companies as well. They can link to their retailers' Web sites and help drive additional traffic."

Consultant Jeffrey Green says retailers, like landlords, are under increasing economic pressure to perform. "Investors are clamoring for more productivity out of smaller and smaller store sizes," said Green, who runs Jeff Green Partners, a Mill Valley, Calif.-based property owner services firm. "So to remain vital, retailers are pushing to stay strong in all three channels."

E-commerce specialist Jeff Grau says retailers can use a Web site as the means to supply items that are out of stock in the physical store,

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rather than lose the sale as the customer goes elsewhere. Grau, a senior analyst at eMarketer, a New York City-based online marketing research firm, says consumers' habit of researching high-ticket items before buying at the store actually boosts brick-and-mortar sales, particularly in consumer electronics. "Once at a Best Buy or RadioShack, they will pick up a cable or make some other purchase they didn't plan on making," Grau said. "It's only human nature. So there is that benefit in reverse to consider." Further, he said, multichannel retailers "can't

possibly offer everything in their stores that they can in their online store. The Internet gives them that endless aisle." At the same time, if an online sale is cheaper against the cost of stocking an item, this seems to indicate the need for a new model of landlord compensation, he says.

The economy being what it is now, consumers are increasing their online purchases, says Grau. In fact, U.S. online retail sales are expected to rise 17 percent this year, to \$204 billion, from \$169 billion last year, according to Forrester Research.

Another issue the shopping center industry

has yet to fully confront is how to account for items bought online or by catalog but returned to a store. "If a sale was never originally included in store revenue and reported there, a merchant shouldn't be reducing its store sales numbers for returns that originated from the Internet or a catalog," Lamy said. "So there are potential opportunities for underreporting there too. It's something that the industry should address."

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