Valuable Tax Savings Imbedded in Buildings

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If you own real estate and pay federal income taxes, you can benefit from the results of a cost segregation study. A cost segregation study is an analysis performed by trained professionals to identify property that should be classified as tangible personal property or land improvements, rather than real property that is depreciated over 27.5 or 39 years. This allows the taxpayer to identify property that can be depreciated over 5, 7 or 15 years instead of the 27.5 or 39 years that typically apply to real estate. **This acceleration of deductions results in substantial tax savings benefits.**

Cost segregation studies apply to both newly acquired or constructed property, leasehold improvements/fit-ups and property that was placed in service in prior years (post 1986). For property placed in service in prior years, the IRS allows a “catch up” deduction in year 1 for the additional depreciation deductions that are identified in a cost segregation study that you were entitled to but did not claim in previous years. This can generate substantial tax savings in the first year of the study.

There is no limitation on the cost of property that is eligible for a cost segregation study. The benefit of a study for a smaller building will be less than that of a larger property but may still be very beneficial. We have worked with several industries to provide cost segregation studies including auto dealerships, banks, commercial and residential property owners, medical facilities and manufacturing facilities.

For property placed in service in years 2014, additional tax incentives available include 50% bonus depreciation and the increased limit in section 179 expense to $500,000. Bonus depreciation allows taxpayers to write off 50% of qualified tangible property with a recovery period of 20 years or less and certain qualified leasehold improvement property that is placed in service in 2014. Thus, the 5, 7 and 15 year property that is identified in a study may qualify for this additional depreciation deduction that wouldn’t normally be identified if the property was being depreciated over 27.5 or 39 years. **These tax incentives for 2014 make cost segregation studies even more beneficial for the current tax year. Similar tax incentives are also available for property placed in service in tax years 2008-2013.**

One of Dean Dorton’s most recent cost segregation studies on a $9.4 million apartment complex that was constructed in 2013 generated tax savings in the first year of $827,000. The present value of accelerated deductions (discounted at 8%) exceeded $690,000. The return on investment for this study was 127.8 to 1.

Tangible Assets Regulations and Cost Segregation Studies

The new tangible assets regulations expand the definition of a disposition of property to include the retirement of structural components of a building, resulting in tax benefit opportunities to the taxpayer. Prior to these regulations, taxpayers were required to capitalize and depreciate the costs to replace a structural component of the building while continuing to recover the cost of the original structural component. **The regulations now expand the definition of a disposition to include the structural component that is being replaced using a reasonable method of identification of the replaced component.** If the taxpayer had a cost segregation study completed on the property upon acquisition, the cost of each building component would be segregated within the report. Upon disposition of each component, the value of the replaced property is easily identified using this study.

For example – A taxpayer replaces the roof of a building. Under the old regulations, the taxpayer could not take a loss on the retirement of the old roof that was replaced. Rather, the taxpayer would continue depreciating the replaced roof and would be required to capitalize and depreciate the cost of the replacement roof. Under the new regulations, the cost of the original roof would be identified and a disposition loss claimed in the year that the replacement roof is placed in service. A cost segregation study breaks down each building component, making it easy to identify the cost of the replaced unit of property.

Dean Dorton most recently identified a $260,000 disposition deduction on a replacement of an HVAC chiller by utilizing the cost segregation study that was performed on the original acquisition of the building.

Dean Dorton uses an Atlanta-based engineering firm to provide cost segregation studies to our clients. This engineering firm conducts studies that conform to the Cost Segregation Audit Techniques Guide issued by the IRS. They have performed over 15,000 studies and have successfully defended all challenges brought forth by the IRS.

If you believe that you may be a candidate for a cost segregation study, please contact Brandi Marcum by calling 859-425-7678. We would be happy to provide you with a free estimate of the cost and benefits of a study of your property.