



Cost Segregation Studies: Increase Cash Flow by Accelerating Depreciation Benefits

The principle goal of a cost segregation study is to increase near term cash flow by accelerating depreciation on commercial real estate. If you've constructed a new building, renovated an existing building, finished out new leasehold improvements, or acquired an existing facility, you may be paying too much federal income tax.

We work with companies nationwide to increase cash flow by accelerating depreciation. For businesses that own or lease a facility, depreciation is a significant and often overlooked opportunity to reduce near term federal tax liability.

PERFORMING A TRADITIONAL COST SEGREGATION STUDY

A traditional cost segregation study focuses on maximizing the depreciation of § 1245¹ tangible personal property. It may be conducted on any building owned by a tax paying company that does not show an operating loss or will be profitable in the near future. Good cost segregation opportunities include:

- + New construction, leasehold improvements and renovations
- + Acquisitions of property
- + Buildings previously placed in service without a cost segregation study that are currently depreciating entirely over 27.5 or 39 years
- + Phase II Subsurface Investigations and Remediation
- + Clients with a large asset base such as large retailers that have numerous small assets

PERFORMING AN ENHANCED COST SEGREGATION STUDY

An enhanced study has all the benefits of a traditional cost segregation study with the added focus of addressing the new tangible property regulations under § 263(a)²: It is designed to maximize current as well as future opportunities for repairs expensing under the Tangible Property Regulations. Enhanced studies include:

- + Breakdown of the facility into broad "units of property" on a building by building basis
- + Detailed breakdown of specific systems such as electrical, mechanical and plumbing into their major components for future write offs
- + Separation of each tenant suite into its own units of property

PERFORMING A DISPOSITIONS STUDY

A dispositions study identifies assets or partial assets that have been permanently removed from service. The Tangible Property Regulations allow the remaining undepreciated basis to be expensed. In the case of major renovations to existing real estate, cost segregation dispositions studies are the most effective means of assigning a value to the property that is being demolished.

¹ Treas. Reg. § 162-4(a)

² Treas. Reg. § 168(1)-8

BBG COST SEGREGATION PROCESS:

Cost segregation reclassifies the components of a building into shorter class lives. For example, a building's floor, roof and walls might be classified as 39-year real property; site improvements such as sidewalks and landscaping would be classified as 15-year real property; communications equipment and general office furnishings as 7-year tangible personal property; and carpeting, decorative lighting and computer associated items as 5-year personal property.

THE BENEFITS OF COST SEGREGATION:

The benefits of cost segregation, resulting from a deferral of tax payment and accelerated depreciation, are easy to demonstrate. For each dollar that is reclassified into a 7-year class life, the taxpayer realizes from \$ 0.15 to more than \$0.20 in the cumulative present value of taxes deferred. Similarly, for each dollar that is reclassified into a 5-year class life, the taxpayer realizes from \$0.19 to more than \$0.23. The exact amounts depend on factors such as the tax rate, discount rate and whether the subject property qualifies for bonus depreciation. In most recent years, an additional 50% - 100% bonus depreciation applies to the shorter life property.

EXAMPLE:

A \$10 million office building has a 35 percent tax rate and an 8 percent discount rate. If 8 percent of the building is reclassified into a 5-year class life, 1 percent into 7-year, and 8 percent into 15-year, the cumulative present value of taxes deferred, using the half-year convention, is over \$261,000.

BBG COST SEGREGATION TEAM:

- + Understands correct methodologies and employs accurate engineering-based estimating techniques
- + Works with a client's CPA to determine which strategies, needs and timetables are most appropriate
- + Educates our clients in how they may best contribute to the cost segregation process without incurring additional expenses
- + Senior staff that stay abreast of the latest revenue rulings, legislation and court cases pertaining to cost segregation Provides break-out of all of the assets that are considered in a cost segregation study per the IRS Audit Techniques Guide

Whether you are buying, building or improving a building, BBG can help maximize your federal tax deductions through an in-depth cost segregation study.

WHO IS BBG?

BBG is a leading national commercial real-estate valuation, advisory and assessment BBG has more than 26 offices in key markets nationwide providing broad geographical coverage and local market knowledge. BBG Advisory Services provides four major lines of services to our clients. This includes Valuations and Audit Support for Financial Reporting, Cost Segregation, Insurance Valuations and Valuation Consulting.

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