



## **Cost segregation studies hold the key to year-end tax savings: Do not miss this boat!**

November 19, 2007 - Spotlights

You recently purchased, constructed or inherited a property and now it's time to allocate the purchase price, cost or inherited basis between land and building. Once satisfied with this allocation, you depreciate the building over 39 years (27.5 years for residential property), the IRS required tax life.

That's not, however, the end of the story. Did you know that you may be giving up as much as 5% or more of the total cost of your building in lost tax benefits? Isn't taking advantage of the non-cash depreciation deductions one of the reasons you invest in real estate? If you are wondering, as most real estate investors are, how to maximize tax benefits and deductions, read on.

A cost segregation study (CSS) can provide property owners and tenants with significant fit-up costs, the benefit of shifting certain property costs from a 39-year life to 15-year, seven-year, and even five-year lives. Items such as landscaping, site fencing, parking lots, floor covering, wall covering, window treatment, process electrical, process plumbing and decorative millwork are just a few examples of costs that fall into shorter lived asset classes. Performing a CSS to accelerate depreciation can lead to significant tax savings and increased cash flow, and can be a terrific component of any year-end tax plan.

While this concept may seem straightforward and simple, it takes a trained team of professionals to properly prepare a CSS in accordance with published IRS guidance. A trained tax professional identifies the specific components that will qualify as shorter lived assets while a trained engineering professional performs the detailed cost allocations. The tax professional also needs to know the "rules of the road" when it comes to what the IRS expects to see in a quality CSS report.

A CSS is not for everyone, but if you can answer "yes" to the following questions you may be a prime candidate for one:

1. Can you benefit from accelerating depreciation deductions?
2. Do you expect to hold the property for at least two or three years?
3. Is the cost of the property at least \$1.5 million?

One actual example of the impact of a CSS involves a shopping center, which was acquired in mid-2006 for \$10.5 million, excluding the land component. As originally calculated, depreciation expenses for the years 2006 to 2011 were approximately \$1.45 million. As a result of a cost segregation study performed in 2006, the company was able to increase its depreciation deduction over the same period by more than \$1.25 million. This results in tax savings and additional cash flow of over \$525,000 for that six-year period.

Savings of this magnitude are very common. A CSS can be performed even after the tax year has ended as long as the results of the study are included in the current year's tax return. Taxpayers can benefit from a CSS not only on a property they have recently purchased, constructed or inherited,

but for properties they have owned for many years. Current IRS rules allow the catch-up of missed depreciation deductions on properties acquired many years ago by filing an automatic change in accounting form with their current year's tax return. The missed deductions from the prior years are all caught up and deducted in the current year. No amended returns are required to obtain this extraordinary benefit.

Studies have been effectively performed for a multitude of properties, including apartment buildings, office buildings, manufacturing facilities, restaurants, hotels, shopping centers, medical facilities, and many more. As a result, many taxpayers make CSS a regular part of their property purchasing process, and attorneys regularly advise clients who inherit property to inquire about their qualifications for a study.

The savings derived from these studies flow right to the bottom line in tax savings and cash flow. The time to act is now. Do not miss this boat!

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