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Cost Segregation Frequently Asked Questions

> **McGuire Sponsel's experienced staff utilizes their construction and tax law knowledge to secure maximum benefits for clients.**
>
> – David McGuire
> Director
> McGuire Sponsel

McGuire Sponsel has helped many clients understand the benefits of performing a cost segregation study. Through these experiences, we recognized the importance of answering some of the most frequently asked questions for the rest of the CPA industry. A cost segregation study can be a valuable tool to create substantial tax and cash flow benefits. Here are the answers to some of the most common questions we hear about cost segregation.

What types of properties qualify?

Any property held for a business purpose is subject to depreciation and may benefit from a review. This includes both new and existing properties. Commonly overlooked opportunities include:

- Hotels
- Offices
- Manufacturing Facilities
- Retail Units
- Assisted Living Facilities
- Tenant Improvements
- Multifamily Units

Can a cost segregation study be applied retroactively to existing properties?

Yes, a 481(a) or catch-up adjustment allows a taxpayer to receive substantial benefit with their next tax filing. The catch-up adjustment brings accelerated depreciation benefits from prior years into the current year as one single adjustment. The result is often a substantial reduction of current year tax liability.

Is cost segregation approved by the IRS?

The IRS sees cost segregation as a legitimate method for determining the useful life of building components. This has been held up in various court decisions and IRS publications. The IRS came out with an Audit Guide which not only confirms this position, but also lists a number of relevant court cases.

What about tenant improvements?

Tenant improvements can also be reviewed. Often tenant improvements have a higher percentage of personal property, which can lead to a higher benefit for the taxpayer.

Can anyone complete a cost segregation study?

The short answer to this is no. The IRS likes to see someone with knowledge in both the construction process and the tax law. The IRS states that a tax analyst's experience may have a bearing on the accuracy of the study. Furthermore, in our experience, studies done by less qualified people generally lead to lower benefits as money is often left on the table.

Why can't I just apply a percentage to my purchase/construction?

This is known as the "rule of thumb" approach. In most cases this will be thrown out under audit. A recent decision by the Oregon Tax Court, in the case of Ronald and Daryl Pearce, confirmed that this methodology will not be accepted under audit. In this case the court threw out the results as not having basis.

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How large does a property need to be for a study to make sense?
This is not an easy answer. The benefits of the study depend on many variables, including the type of property and the situation of the taxpayer. McGuire Sponsel is happy to put together a cost benefit analysis. In most cases, properties under $500,000 do not make sense unless they are held in a portfolio of assets.

Why should I choose McGuire Sponsel?
McGuire Sponsel's staff and management are seen as experts in this area. Not only does McGuire Sponsel have an excellent track record with completing quality studies, but they can also work with you on more complex transactions. Many situations require a more detailed analysis to ensure the taxpayer can utilize the benefits. These situations can include passive loss issues, asset based acquisitions, and 1031 transactions.

Are there times when a cost segregation study should not be done?
In certain circumstances a cost segregation study does not make sense. This may include a situation where there is a plan to flip the property in 1-3 years, or a situation where the taxpayer is in a long term loss for tax purposes. However, some of these limitations are based on perception. An expert should be consulted prior to deciding if a study should move forward or not.

Are there other things a building owner should consider?
The IRS provides other incentives for building owners. These include 179D energy efficient building deductions and tax credits for solar and other alternative energy systems.

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