

Real Estate Investors can Lower Your Income Tax with Cost Segregation



Presented by Yonah Weiss
Cost Segregation Expert

Presentation Topics

Webinar: Tuesday, March 26, 2019

Understanding Cost Segregation



Overview: Depreciation and Cost Segregation



What are the Benefits of a Cost Seg study?



What is Bonus Depreciation?



Who should do a Cost Seg study?
When is the best time?



What is a Real Estate Professional

Case Study

🏠 Stepping into the shoes of a
Multi-Family Property Owner

Selecting a Cost Seg Provider

🏠 About Madison SPECS....
*Specialized Property Engineering and
Cost Segregation*

🏠 The MCRES Family of Companies

Depreciation and Cost Segregation

An Overview

- 🏠 Property must be depreciated by tax law
- 🏠 39 years for Commercial property
27.5 years for Residential property
- 🏠 But there is a ***tax planning technique*** that can separate and accelerate property into various depreciable categories
- 🏠 With Cost Segregation, ***property can be depreciated over much shorter time periods: 5, 7, 15, and 27.5 or 39-year categories.***

Depreciation and Cost Segregation

An Overview

\$1,000,000 Purchase Price

(\$150,000) Land Allocation (15%)

\$850,000 Depreciable Basis

Depreciation and Cost Segregation

An Overview

\$1,000,000 Purchase Price

(\$150,000) Land Allocation (15%)

\$850,000 Depreciable Basis

Straight-Line Depreciation Deduction

\$21,794 (for 39 years)

\$30,909 (for 27.5 years)

Cost Segregation

An Overview

A Cost Segregation study determines HOW MUCH of a specific building cost goes into each category, and documents it.

- 🏠 Breaks out components into shorter term life
- 🏠 Accelerates tax depreciation deductions
- 🏠 Produces significant non-cash deductions
- 🏠 Re-classifies real property expenditures



Asset Classes

5-Year Property Personal-Tangible

- Building Mounted Flood Lighting
- Cable TV Systems
- Cabinetry
- Closet Shelving
- Decorative Lighting
- Decorative Moldings
- Dryer Vent Kit
- Kitchen Appliances
- Rubber Floor
- Special Purpose Plumbing
- Telephone Rough-in
- Vinyl Floors and Base
- Window Treatments
- Special Purpose Electrical
- Mailboxes
- Millwork
- Mirror
- Carpeting
- Ceiling Fan
- Equipment
- Furniture
- Wood Base
- Appliances

15-Year Property Land Improvements

- Asphalt Paving
- Concrete Curbing
- Concrete Paving
- Monument Sign
- Fencing
- Landscaping
- Pavement Markings
- Playground Equipment
- Pool
- Retaining Wall
- Site FF &E
- Site Signage

Cost Segregation Benefits

On average, \$1 Million of reclassified assets can generate about *\$200,000 of after-tax cash savings* for many property types!*

↓ Reduces Tax Liability

↑ Increases Cash Flow

Ⓢ Time Value of Money

✓ Bonus Depreciation

* Note: The amount of tax savings varies based on multiple variables of the property and owner.



What is **Bonus Depreciation?**

Tax Cuts and Jobs Act of 2017

- 50% or 100% of depreciation in year 1
- Useful life under 20 years
- Not allowed for property purchased and sold in same year

Benefits

- Accelerate tax depreciation deductions
- Produce significant non-cash deductions



Who should do a **Cost Segregation Study?**

It applies to **ALL** real estate owners who are current income taxpayers.

- 🏠 Individuals
- 🏠 Estates and Trusts
- 🏠 Corporations
- 🏠 Partnerships
- 🏠 LLCs



Active vs. Passive Real Estate Professional

- **Active Real Estate** – real estate activity or business in which the taxpayer works on a regular, continuous, and substantial basis.
- **Passive Real Estate** – real estate activity or business in which the taxpayer does not materially participate on a regular, continuous, and substantial basis.
 - **Active Real Estate losses** offset against all active OR passive income.
 - **Passive Real Estate losses** only offset other passive investment activity income.

Real Estate Professional

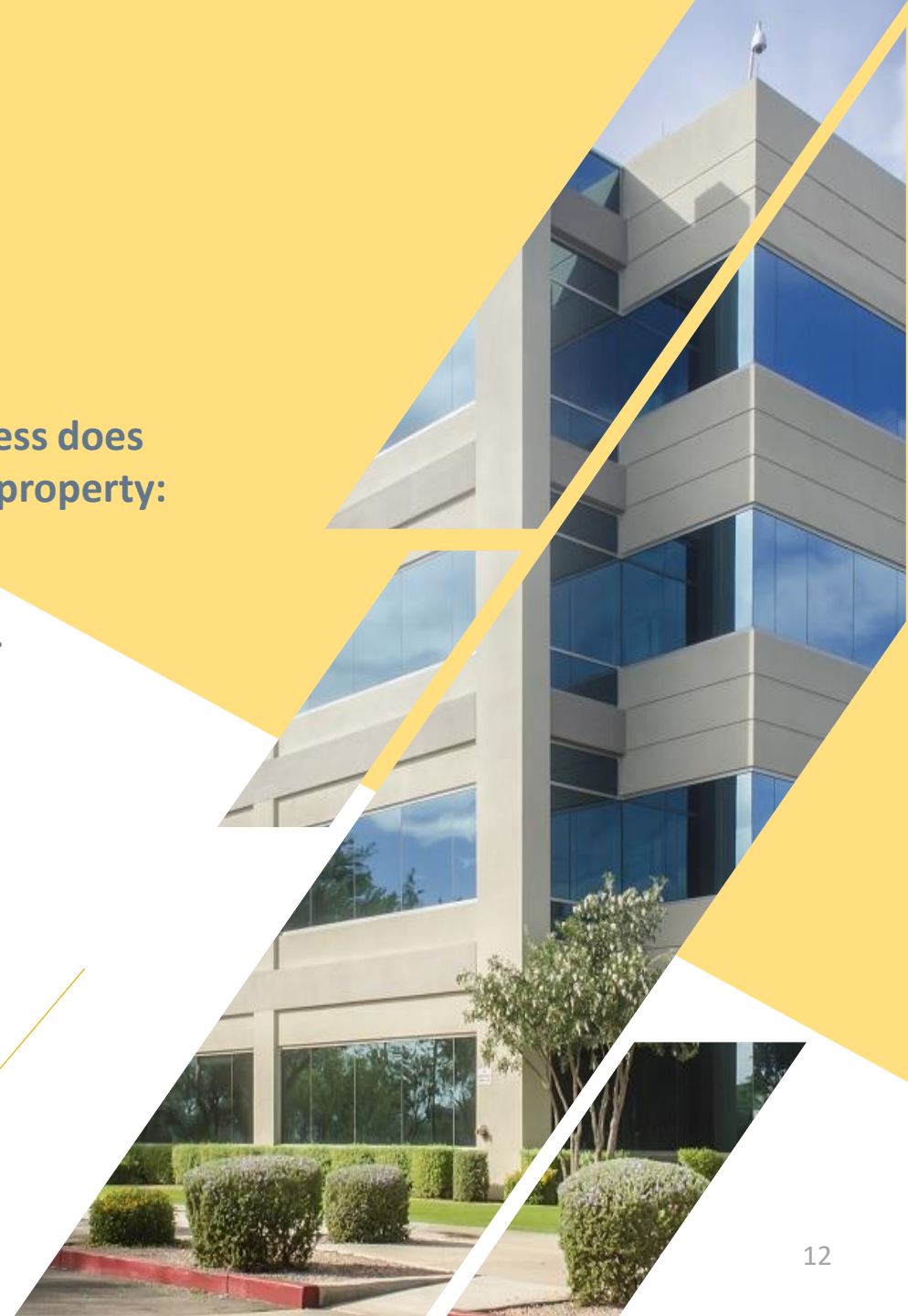
A Definition

You qualify as a RE professional for the year if you OR YOUR SPOUSE met both of the following requirements:

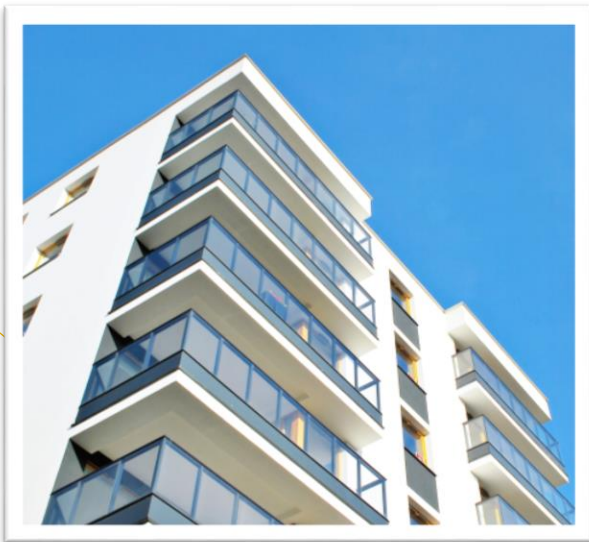
- More than half of the personal services you performed in all trades or businesses during the tax year were performed in real property trades or businesses in which you materially participated.
- You performed more than 750 hours of services during the tax year in real estate

A real property trade or business does any of the following with real property:

- 🏠 Develops or redevelops it
- 🏠 Constructs or reconstructs it.
- 🏠 Acquires it
- 🏠 Converts it
- 🏠 Rents or leases it
- 🏠 Operates or manages it
- 🏠 Brokers it



When is the best time to do a Cost Segregation Study?



After the acquisition
of a property



After a renovation
or addition



On a newly
constructed property



Look-back study
Purchased in
previous tax year

Case Study on Cost Segregation

Stepping into a Multi-Family Owner's shoes

- 🏠 A multifamily Investment group purchased a, a 188-unit garden-style apartment building, in El Paso, TX for \$9,250,000
- 🏠 Without cost segregation, the depreciation on this property would have been \$285,881 annually.



Case Study on Cost Segregation

Stepping into a Multi-Family Owner's shoes

Purchase Price was \$9,250,000

Assets were reclassified as follows:

- 🏠 \$1,387,500 - Land allocation (15%)
Non-Depreciable
- 🏠 \$5,680,235 – 27.5 year property (72%)
- 🏠 \$555,121 - 15-year property (7%)
- 🏠 \$1,627,143 - 5-year property (21%)

Total amount of tax benefit: \$2,182,265



What should you look for in a Cost Segregation Study?

Principal Elements of A Quality Cost Segregation Study*

- Preparation By An Individual with Expertise and Experience
- Detailed Description Of The Methodology
- Use Of Appropriate Documentation
- Interviews Conducted With Appropriate Parties
- Use Of A Common Nomenclature
- Use Of A Standard Numbering System
- Explanation Of The Legal Analysis
- Determination Of Unit Costs And Engineering "Take-Offs"
- Organization Of Assets Into Lists Or Groups
- Reconciliation Of Total Allocated Costs To Total Actual Costs
- Explanation Of The Treatment Of Indirect Costs
- Identification And Listing Of § Property
- Consideration Of Related Aspects (e.g., IRC § 263A, Change in Accounting Method And Sampling Techniques)

**Taken directly from the IRS
Cost Segregation Audit
Techniques Guide*

About Madison SPECS

Specialized Engineering and Cost Segregation

- In-house team of experienced engineers, accountants and tax experts on staff – no need to outsource
- Big-4 accounting firm leadership with deep expertise
- 13,000 studies nationwide in the last 12 years
- \$3 Billion in Tax Savings!
- 100% Audit Protection

Madison CRES Family of Companies

Commercial Real Estate Services

- Madison SPECS is a division of Madison Commercial Real Estate Services (MCRES).
- MCRES is a group of independent but related companies including Madison SPECS, Madison Title, LeaseProbe / Real Diligence / Real Physical Diligence, Madison 1031, and DocProbe.
- We provide a comprehensive set of specialty tax, transactional and management services for property used for business or investment.

Disclaimer

- 🏠 We are not offering advice. Seek outside counsel. Consult with a legal and/or tax professional.
- 🏠 The information contained in this presentation is a general overview and subject to change. New tax law is currently under review. Perform your own due diligence for your specific situation.



Contact Us

For more information about a specific property or to request a complimentary **Feasibility Analysis**, you can reach me at:

Yonah Weiss, Cost Segregation Expert

732-298-9002 or

yweiss@madisonspecs.com