



Cost Segregation Definition

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Cost Segregation Definition

Cost Segregation is a major accelerated Tax Depreciation Benefit that is obtained by performing an analysis or appraisal by a Tax Lawyer or certified tax professional. This appraisal follows guidelines set forth by the IRS Rules and Regulations that governed this benefit.

Cost Segregation is the practice of identifying assets and their costs, and classifying those assets for federal tax purposes. In a cost segregation study, certain costs previously classified as subject to 39-year depreciable life, can instead be classified as personal property or land improvements, with a 3, 5, 7, or 15-year rate of depreciation using accelerated methods. An "engineering-based" study allows a building owner to depreciate a new or existing structure in the shortest amount of time permissible under current tax laws.

The benefits of a cost segregation study include:

An immediate increase in cash flow

A reduction in current tax liability

The deferral of taxes

The ability to reclaim "missed" depreciation deductions from prior years

Benefits of Cost Segregation

- Immediate Increase in Cash Flow.
- Immediate reduction in Tax Liability.
- Ability to defer taxes.
- Reclaim previous years deductions.
- Accelerates the deduction of major construction project costs.
- Can greatly enhance a business's ability to reach profitability.
- Benefits buildings with large amount of equipment such as a car wash facility.
- The Modernwash System fits the general requirements to make it much simpler to use Cost Segregation as a building strategy.
- Check with your tax professional.



COST SEGREGATION DEFINED

“Engineering-based” cost segregation enables commercial real estate owners to reallocate real property (under Code Sec. 1250) to personal property (under Code Sec. 1245). This results in a substantially shorter depreciable tax life and accelerated depreciation methods.

WHY A SPECIALIST IS NEEDED

For both new and existing properties, the IRS requires that engineering-based cost segregation studies be performed in order to realize the maximum depreciation benefits. Engineering-based cost segregation studies provide more precisely segregated property information, giving CPAs the information and detailed supporting documentation they need to meet with strict IRS regulations and requirements for audit defense.

In the IRS Cost Segregation Audit Techniques Guide (ATG), Chapter 4, the prime attribute of a high-quality cost segregation study is “preparation by an individual with expertise and experience.” The Audit Techniques Guide adds: “Preparation of cost segregation studies requires knowledge of both the construction process and the tax law involving property classifications for depreciation purposes. In general, a study by a construction engineer is more reliable than one conducted by someone with no engineering or construction background. Experience in cost estimating and allocation, as well as knowledge of the applicable tax law, are other important criteria.”



TIMOTHY HOGUE is the President and Senior Designer of Modernwash Buildings and Solutions, Inc. Modernwash designs and creates multiple Pre-Fabricated structures for the Carwash as well as the Retail Industry. They utilize a modern HSS frame System that features a proprietary hidden fastening system.

WHAT TYPES OF ITEMS ARE IDENTIFIED?

Through an engineering-based cost segregation study, a wide range of building components, such as electrical installations, plumbing, mechanical components, and finishes can be identified and reclassified into shorter-lived asset classes. This adds up to substantial savings to the client. The Modernwash Building System is an excellent fit meeting the criteria and requirements set forth by the IRS regulations.

WHAT ROLE DOES “TIME VALUE OF MONEY” (TVM) PLAY?

Cost segregation is based on the fundamental principle that “a dollar today is worth more than a dollar tomorrow”. The same logic applies to the statement: “a tax deduction today is worth more than a tax deduction tomorrow”. By accelerating a buildings’ depreciation, property owners can lower their tax liability and thus realize a significant increase in cash flow. This larger cash flow—resulting from postponing tax payments—is available for other investments.

THE IRS’S AUDIT TECHNIQUES GUIDE (ATG)

In late 2004, the IRS released the guidelines their agents must follow for audits of cost segregation studies. This guide reviews the methodologies recognized by the IRS for asset allocation. It examines the various characteristics of a quality study. Referring to the “detailed engineering approach,” the guidelines state: “In general, it is the most methodical and accurate approach, relying

on solid documentation and minimal estimation.”

THE BOTTOM LINE

Cost segregation studies are one of the most valuable tax strategies available to owners of commercial real estate today. This increasingly popular phenomenon, offers facility owners the opportunity to defer taxes, reduce their overall current tax burden, and free up capital by improving their current cash flow. Virtually every taxpayer who owns, constructs, renovates, or acquires a commercial real estate structure stands to benefit from a cost segregation study. By engaging the expertise of a competent tax attorney, property owners can be assured that their study will stand up to the strictest scrutiny of IRS auditors. The Modernwash Building System delivers great design and performance but also has the ability to put money back into your business thru either 7 year accelerated depreciation or increase the speed of your tax savings even more with a cost segregation strategy

Always contact your tax professional for information specific to your situation.