COST SEGREGATION INSIGHTS

January 2018

UPDATE: HOUSE OF REPRESENTATIVES DID NOT ADOPT 25-YEAR REAL PROPERTY TAX LIFE

As reported in our December 2017 publication of Insights, the U.S. Senate proposed shortening the depreciation of long-lived real property from 27.5 & 39-year to 25-years, which was not outlined in the U.S. House of Representatives version of the “Tax Cuts and Jobs Act”. The final version of the Tax Cuts and Jobs Act of 2017 was signed into law on December 22, 2017.

Depreciation of long-lived real property remains at 27.5-years (residential property) and 39-year (non-residential property). Taxpayers can continue to benefit from the accelerated depreciation provided by a cost segregation study.

Table 2 of the December 2017 Insights article (attached) presents representative additional tax savings benefit by property type of conducting a cost segregation study for a $10 million investment by property type under the current 27.5 and 39-year depreciation periods.

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December 2017

In this issue we examine the benefits of moving from 27.5 and 39-year straight-line tax depreciation recovery periods to the 25-year straight-line tax depreciation recovery period as proposed by the U.S. Senate. We then examine the increased benefit of using a quality cost segregation study.

IMPACT OF SHORTENING COMMERCIAL REAL PROPERTY TAX LIFE TO A 25-YEAR RECOVERY PERIOD

As part of the "Tax Cuts and Jobs Act", the Senate is proposing shortening the depreciation of real property to 25-years. A shortening of the real property tax life from 27.5-years for commercial residential real estate and 39-years commercial non-residential real estate will have a positive effect on tax savings to owners and investors of U.S. owned commercial property. Increased tax savings will allow for reinvestment in personal property, real property, intangible property and human capital.

As presented in Table 1, a decrease from 27.5 and 39-year to 25-year straight-line depreciation, will increase net present value tax savings by $9,960 for every $1 million spent when 27.5-year property is reclassified to 25-years and $42,847 when 39-year property is reclassified to 25-years.

Table 1

Property Type	Current Depreciation Period (Years)	Proposed Depreciation Period (Years)	Incremental Net Present Value Tax Savings*
Apartment / Multi-Family	27.5	25	$99,607
Assisted Living / Senior Living Facility	39	25	$428,478
Automobile Dealership	39	25	$428,478
Bank	39	25	$428,478
Computer Operations / Technology Center	39	25	$428,478
Fitness Center / Health Club	39	25	$428,478
Golf Course	39	25	$428,478
Grocery Store	39	25	$428,478
Hotel and Motel	39	25	$428,478
Manufacturing - Heavy	39	25	$428,478
Manufacturing - Light	39	25	$428,478
Medical Office Building / Surgery Center	39	25	$428,478
Office Building	39	25	$428,478
Research and Development	39	25	$428,478
Restaurants	39	25	$428,478
Retail Store	39	25	$428,478
Self Storage Facility	39	25	$428,478
Shopping Malls - Regional or Strip	39	25	$428,478
Tenant Improvements	39	25	$428,478
Theater	39	25	$428,478
Warehouse	39	25	$428,478

* Represents tax savings on a $10 million investment.

Under the Senate's proposed tax bill, U.S. tax payers will receive even greater tax savings from applying accelerated depreciation of building components through a cost segregation study.

By analyzing the commercial building components of sample properties, we can identify building components that are considered personal property, support personal property, and site improvements eligible for reclassification as 5, 7 and 15-year property, respectively. Typically, 10% to 30% of a property's value is eligible for reclassification.

Table 2 presents the additional tax savings benefit of conducting a cost segregation study for a $10 million investment by property type under the current 27.5 and 39-year depreciation periods compared to the proposed 25-year recovery period.

Table 2

Property Type	Current Net Present Value Tax Savings 27.5 & 39 Year	Proposed Net Present Value Tax Savings 25 Year	Additional Net Present Value Tax Savings
Apartment / Multi-Family	$100,762	$192,899	$92,137
Assisted Living / Senior Living Facility	$334,474	$677,256	$342,782
Automobile Dealership	$627,139	$894,938	$267,799
Bank	$376,283	$708,354	$332,070
Computer Operations / Technology Center	$668,948	$926,035	$257,087
Fitness Center / Health Club	$418,093	$739,451	$321,358
Golf Course	$501,711	$801,646	$299,935
Grocery Store	$418,093	$739,451	$321,358
Hotel and Motel	$418,093	$739,451	$321,358
Manufacturing - Heavy	$752,567	$988,230	$235,663
Manufacturing - Light	$501,711	$801,646	$299,935
Medical Office Building / Surgery Center	$501,711	$801,646	$299,935
Office Building	$501,711	$801,646	$299,935
Research and Development	$668,948	$926,035	$257,087
Restaurants	$501,711	$801,646	$299,935
Retail Store	$418,093	$739,451	$321,358
Self Storage Facility	$836,185	$1,050,424	$214,239
Shopping Malls - Regional or Strip	$334,474	$677,256	$342,782
Tenant Improvements	$501,711	$801,646	$299,935
Theater	$418,093	$739,451	$321,358
Warehouse	$125,428	$521,770	$396,342

In conclusion, if the proposed 25-year recovery period makes its way into law, potential tax savings resulting from a cost segregation study could provide an additional $100,000 to $400,000 of tax savings on a $10 million property.

To learn more about how Porto Leone Consulting can work with you, please contact Walter O'Connell at 212.273.1143 x203 or WalterO@PLC-LLC.com.

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Our team is comprised of innovative professionals with diverse backgrounds and expertise. Most of our professionals originated from Big Four accounting firms with a common goal to provide concierge service, high-quality and timely valuation services for our clients.

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