

Abstract: A cost segregation study is a strategic tax planning tool that allows a business property owner to accelerate depreciation deductions. That, in turn, will enable the owner to reduce taxable income and increase cash flow. Take a look at the powerful tax benefits of this tool.

Unlocking tax savings: The benefits of a cost segregation study

A cost segregation study is a strategic tax planning tool that allows a business property owner to accelerate depreciation deductions. That, in turn, will enable the owner to reduce taxable income and increase cash flow. A cost segregation study can be performed by an expert in the field. The study separates various building components — such as electrical systems, certain plumbing systems and removable carpeting. It then allows the personal property to be reclassified for tax purposes and deducted over a much shorter period. This strategy has been consistently upheld in the courts.

Fundamentals of depreciation

Business buildings generally have a 39-year depreciation period. Typically, companies depreciate a building's structural components — including walls, windows, HVAC systems, plumbing and wiring — along with the building. Personal property (such as equipment, machinery, furniture and fixtures) is eligible for accelerated depreciation, usually over five or seven years.

Often, businesses allocate all, or most, of their buildings' acquisition or construction costs to real property, overlooking opportunities to allocate costs to shorter-lived personal property or land improvements. Items that appear to be “part of a building” may, in fact, be personal property. Examples include removable wall and floor coverings, removable partitions, awnings, canopies, window treatments and signs.

Shine a light on outdoor savings

Rules for outdoor lighting, parking lots, landscaping and fencing are tricky but can still lead to current tax deductions in certain situations. These expenditures are generally treated as capital improvements, subject to the 15-year depreciation rule. For instance, if you replace your business lighting to upgrade it or provide greater security at night, it qualifies as a deductible capital improvement. Similarly, landscaping projects designed to boost your curb appeal or provide environmental benefits are considered capital improvements.

On the other hand, routine maintenance — such as the costs of mowing and watering the lawn surrounding your business building — typically fall into the category of deductible business expenses, just like minor repairs.

Identifying costs

A cost segregation study combines accounting and engineering techniques to identify building costs that are properly allocable to tangible personal property rather than real property. Although

the relative costs and benefits of a cost segregation study will depend on your particular facts and circumstances, it can be a valuable investment.

It may allow you to accelerate depreciation deductions on certain items, thereby reducing taxes and boosting cash flow. And, under the Tax Cuts and Jobs Act, the potential benefits of a cost segregation study may be even greater than they were years ago because of enhancements to certain depreciation-related tax breaks.

Worth checking out

Cost segregation studies have costs of their own, but the potential long-term tax benefits may make it worthwhile to undertake the process. Contact our firm for further details.