

# What You Don't Know Can Hurt You

## A message for owners of **commercial buildings**

In the third quarter of 2006 the IRS allowed International House Of Pancakes a tax savings of over \$8.5 million, mostly due to reclassified depreciation on their commercial property. This was like found money for a corporation whose traditional financial wizards overlooked a little-used tax tool known as "Cost Segregation."

### WHAT IS COST SEGREGATION?

To put it simply, Cost Segregation re-classifies vital portions of a building according to the length of their estimated lifespans. Traditionally, everything in all commercial buildings, including the building itself, was normally depreciated over 39 years – no exceptions, and no matter how illogical.

However, we all know that the carpeting, asphalt, speciality electrical and the like all wear out long before 39 years. With the advent of Cost Segregation each of these vital components can be dealt with individually, according to pre-set standards now allowed to be classified as personal property by the IRS. In fact, the founders of Cost Segregation Services helped set the standards for the initial court ruling. Who else is better qualified to re-evaluate any given building?

### RETROACTIVE TAX BENEFIT...

What came out in the court case was that the IRS recognized their potential liability in the matter and created what was tantamount to a "don't ask, don't tell" policy. For this reason the court had to create a starting point from which commercial property owners could claim accelerated depreciation. With this ruling, all commercial property and tenant improvements placed in service after January, 1986 became eligible for the savings.

### NOT SOME RISKY TAX SCHEME...

Before 1997 the IRS did their best to pretend Cost Segregation did not exist. But in that year they had to admit its validation in court. And, in 1999 they issued a Legal Memorandum which

said that "reclassification of assets into shorter periods would not be contested." In 2004 the IRS reaffirmed the methodology by issuing the Cost Segregation Audit Guide. Until recently, such studies were extremely costly. Further, it was difficult to find experienced engineers from a variety of disciplines who could perform such studies. Thanks to innovative industry leaders like Thomas Nelson of Cost Segregation Services, these evaluations have become much more practical.

### IT MAKES GREAT BUSINESS SENSE...

Owner's bottom-line savings, as much as 25% of the building's value, can be recouped within the first five years of ownership. Nelson's service is ideal for buildings valued at between \$1 million and \$50 million. These savings can be applied to office buildings, apartments, hotels, automobile dealerships, factories, warehouses, restaurants, and more. The potential can be enormous when property is reclassified into an accelerated depreciation schedule.

But each building must be viewed as a unique situation. That's why most tax people shied away from Cost Segregation if they even knew about it.

This is a service all CPAs should know more about for the benefit of their clients.



*"See that sign? It especially applies to Cost Segregation."*

### WHAT YOU DON'T KNOW CAN HURT YOU...

Previously Cost Segregation studies were used by large clients of the Big Four CPA firms on their clients' largest properties. But now you can benefit if you have:

- Purchased real property since 1987
- Constructed new facilities since 1987
- Renovated, expanded, or restored existing property
- Installed improvements in existing buildings
- Paid federal income tax while owning these properties

Is your interest piqued? If so, contact Thomas Nelson at (619) 294-8822, [tnelson@cox.net](mailto:tnelson@cox.net) or [www.SaveIncome.com](http://www.SaveIncome.com)