FTI CONSULTING™

AN FTI CONSULTING WHITE PAPER
JULY 2019

COST SEGREGATION STUDIES NOW CRUCIAL TO TAKE FULL ADVANTAGE OF ADDITIONAL BONUS DEPRECIATION BENEFITS

With the approval of the Tax Cuts and Jobs Act (TCJA), it is critical that property owners pay closer attention to the important beneficial changes to the depreciation rules:

- Under the new law, businesses may take advantage of bonus depreciation on both used and new qualified property. Previously, only owners and investors who constructed or purchased new property were able to benefit from bonus depreciation. This is a significant and favorable benefit for owners/purchasers of used property.
- Under the new law, bonus depreciation of 100% can be taken in a taxpayer's first taxable year. This change doubles the former permissible depreciation allowance.
- Properties that can qualify for bonus depreciation benefits include those acquired and placed in service after September 27, 2017 and before January 1, 2023. Property acquired prior to September 28, 2017, but placed in service after September 27, 2017, remain eligible for bonus depreciation under pre-TCJA. Property owners must be warned that closer attention must be paid to the determination of placed-in-service dates, as these dates will be subject to IRS scrutiny.
- Qualified property, also known as Section 1245 property, is defined as tangible personal property with a recovery period of 20 years or less and includes property that is commonly depreciated over a period of five, seven or 15 years. Properties with components that fall into this category will be the greatest beneficiaries of the new law.
- The Modified Accelerated Cost Recovery System (MACRS) general depreciation system (GDS) recovery periods of 39 and 27.5 years for nonresidential and residential rental property will remain the same; however, the alternative depreciation system (ADS) recovery period for residential rental property has been reduced from 40 to 30 years for property placed in service on or after January 1, 2018.
- The Act also changed Section 179 rules that apply to property placed in service in taxable years beginning after December 31, 2017. The maximum amount a taxpayer may now expense has been raised to $1 million and the investment limit was raised to $2.5 million.
- Section 179 definition of qualified real property was expanded and now includes any improvement to a building's interior; unless, improvements are attributable to the enlargement of the building, any elevator or escalator, or the internal structural framework of the building. Moreover, it also includes roofs, HVAC, fire protection, alarm systems, and security systems.

COST SEGREGATION STUDIES NOW CRUCIAL TO TAKE FULL ADVANTAGE OF ADDITIONAL BONUS DEPRECIATION BENEFITS

AN FTI CONSULTING WHITE PAPER
JULY 2019

Consideration of a cost segregation study is now more important than ever. A cost segregation study will identify all qualifying assets and reclassify them into shorter tax recovery periods. Using GDS lives, these assets are generally depreciated over five, seven or 15 years.

In the example below, a taxpayer acquired a used $10,000,000 non-residential property on June 1, 2018. A cost segregation study was performed, and the results are as follows: 20% of five-year personal property is allocated to the basis; 1% to seven-year; 10% to 15-year and 69% to 39-year; the benefits are as follows:

- With a cost segregation study, after the passage of the 2017 Tax Act, **without bonus depreciation**, the taxpayer's first-year tax savings would be approximately **$109,504**. Note the significant difference without a cost segregation analysis.
- With a cost segregation study, after the passage of the 2017 Tax Act and **100% Bonus Depreciation**, the taxpayer's first-year tax savings would be approximately **$794,264**[1]; a difference of $685,285, more than six times the value when bonus depreciation is applied.

Prior to deciding if a cost segregation study should be completed, property owners should consider the new Interest Expense Limitation that was enacted on January 1, 2018. The Net Interest Expense will be limited to 30% of the adjusted taxable income. Taxpayers may be exempt from the Interest Expense Limitation if the average gross receipts over the prior three years are less than $25 million or if the taxpayer is electing real property business depreciation. The election is irrevocable and carries a cost. Electing taxpayers are required to depreciate using ADS for all residential and non-residential real property as well as qualified improvement property. Assets depreciated under ADS are not eligible for bonus depreciation; however, assets with 20 years or less can qualify for bonus depreciation and will be depreciated using GDS.

	With Cost Segregation (No Bonus)	
Life	Depreciable Basis By Life	2018 Depreciation
5-Year	$2,000,000	$400,000
7-Year	$100,000	$14,290
15-Year	$1,000,000	$50,000
39-Year	$6,900,000	$95,979
TOTAL	$10,000,000	$560,269

	Without Cost Segregation	
Life	Depreciable Basis by Life	2018 Depreciation
5-Year	$0	$0
7-Year	$0	$0
15-Year	$0	$0
39-Year	$10,000,000	$139,100
TOTAL	$10,000,000	$139,100

Change in Reported Annual Depreciation	Tax Savings
$421,169	$109,504

	With Cost Segregation - 100% Bonus	
Life	Depreciable Basis by Life	2018 Depreciation
5-Year	$2,000,000	$2,000,000
7-Year	$100,000	$100,000
15-Year	$1,000,000	$1,000,000
39-Year	$6,900,000	$95,979
TOTAL	$10,000,000	$3,195,979

Change in Reported Annual Depreciation	Tax Savings
$3,056,879	$794,789

1 A blended Federal and State tax rate of 26% was applied.

Larry Portal
Senior Managing Director
+1 973 852 8147
larry.portal@fticonsulting.com

Stephen Bertonaschi
Senior Managing Director
+1 973 852 8174
stephen.bertonaschi@fticonsulting.com

Janet Bullens
Manager
+1 832 667 5027
janet.bullens@fticonsulting.com

Celeste Huelmo
Senior Consultant
+1 973 852 8118
celeste.huelmo@fticonsulting.com

FTI CONSULTING™

EXPERTS WITH IMPACT™

About FTI Consulting

FTI Consulting is an independent global business advisory firm dedicated to helping organizations manage change, mitigate risk and resolve disputes: financial, legal, operational, political & regulatory, reputational and transactional. FTI Consulting professionals, located in all major business centers throughout the world, work closely with clients to anticipate, illuminate and overcome complex business challenges and opportunities.

www.fticonsulting.com