

Frequently Asked Questions:

What is a Cost Segregation Study (CSS)?

CSS is an engineering analysis that reclassifies or segregates real estate components and improvements between real and personal property to accelerate the depreciation periods from 39 or 27.5 years to 15, 7, or 5 years.

How does a cost segregation work?

Building costs are generally classified for federal income tax purposes into three categories; (1) Tangible Personal Property, (2) Land Improvements, and (3) Real Property.

Each has a different recovery period and method under the Modified Accelerated Cost Recovery System (MACRS). An engineering-based analysis is performed by an engineer with in-depth knowledge of construction methods, materials, and building components to properly identify the assets that will be reclassified to take advantage of accelerated depreciation. The study typically takes 2 to 4 weeks to complete, after the site visit.

What properties qualify?

Properties qualify if: 1.) Purchased, constructed, or remodeled property after Dec. 31, 1986, and 2.) Owner anticipates holding the property for at least a few years.

When should a study be done?

Ideally a study should be completed in the tax year the building or improvements are placed in service. However, IRS revenue procedures allow taxpayers to "catch up" on the depreciation that was not claimed from the first day the property was placed in service without amending prior years' tax returns. Furthermore, the IRS recently allowed for the "catch up" period all in the first year rather than over 4 years, when the Revenue Procedure 99-49 was first introduced. A cost segregation study can be performed on any property constructed, acquired or remodeled after Dec. 31, 1986.

Why haven't I heard of this?

CSS was first applied by major accounting firms with in-house engineering departments. Only the largest properties owned by their most significant clients were targeted. Accountants now partner with engineering firms to deliver this same service to commercial property owners at very affordable rates.

How much does a typical study cost?

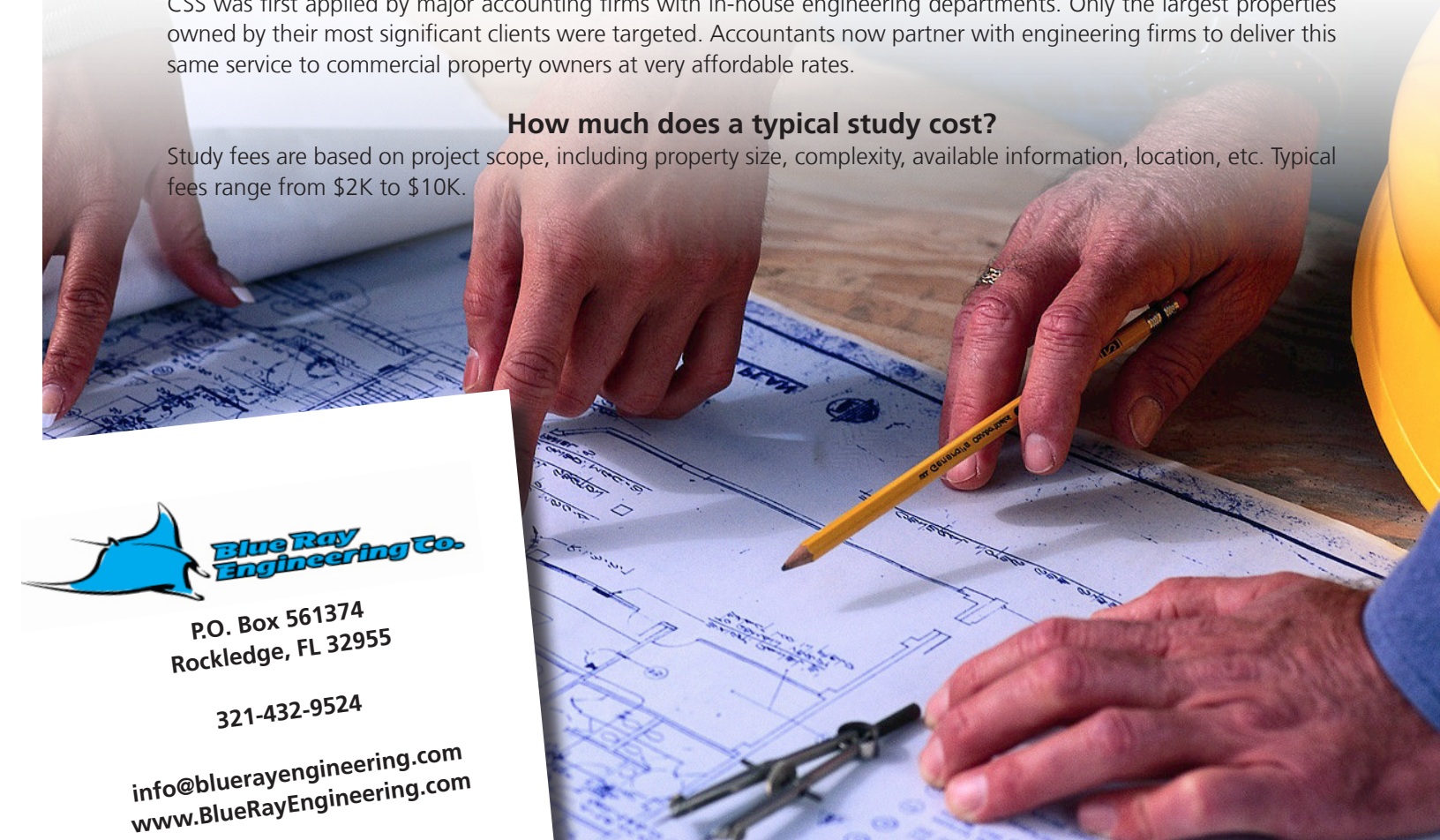
Study fees are based on project scope, including property size, complexity, available information, location, etc. Typical fees range from \$2K to \$10K.

Cost Segregation Services

WWW.BLUERAYENGINEERING.COM

Did You Know?

Cost segregation studies can be performed on buildings either purchased, constructed or renovated up to 15 years ago with a minimum building value of generally no less than \$300,000.



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Benefits of a Cost Segregation Study

What is a cost segregation study?

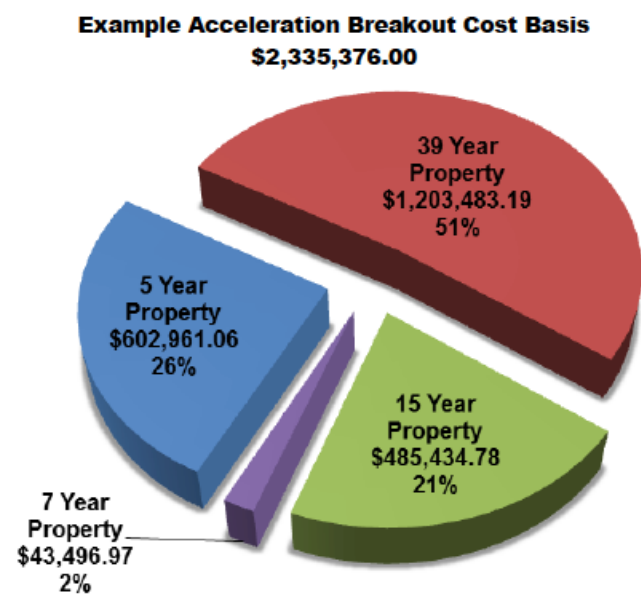
Cost segregation is a strategic tool that allows commercial property owners to accelerate depreciation. This increases cash flow and defers federal and state income taxes. The cost segregation goal is to identify assets that normally have a 39 or 27.5 year class life and accelerate approximately 20%-50% into shorter depreciable lives.

Who qualifies for a cost segregation study?

Individuals who have acquired, constructed or renovated commercial property after December 31, 1986. and having a value of approximately \$300,000. or greater.

Benefits

- Material reductions in your federal and state tax liabilities for the year of the study and the next decade - typically hundreds of thousands of dollars.
- Immediate increase in cash flow through accelerated depreciation deductions by reducing Federal and State income taxes.
- Large amount of "catch up" depreciation in the current tax year.
- Justification for reduction in real estate property taxes.
- Justification for reduction in property insurance costs
- Identifies the components of a building, which can be classified as personal property versus real property for write-off versus capitalization prior to demolition & rehabilitation.



Engineering Based Cost Segregation Study Estimated Reallocation Percentages

Warehouse	15% - 25%
Marina	15% - 35%
Office	20% - 45%
Private Education	20% - 35%
Apartment Bldg.	20% - 40%
Retail	25% - 35%
Sports Complex	25% - 40%
Auto Dealership	25% - 50%
Hotel	25% - 35%
Restaurant	25% - 35%
Medical Facility	25% - 45%
Golf Course	25% - 40%
Manufacturing	30% - 50%
Data Center	30% - 50%

Reasons benefits are often overlooked

- CPAs and/or commercial property owners are not aware of the magnitude or importance of the potential benefits.
- All components of "real estate" are incorrectly assumed to be "real property" for federal tax purposes.
- Requires familiarity with numerous IRS sections, regulations, revenue rulings and case law.
- Engineering expertise needed to extract the required details from drawings, contractor invoices, payment applications, and the constructed property. Often the property is purchased well after original construction and the necessary information is not available.

What Should a Cost Segregation Study Include?

The IRS states that a quality cost segregation study should be well-documented and accurate. Each study should classify assets into property classes, explain the rationale used to classify the assets, substantiate the cost basis of each asset and reconcile total allocated costs to actual costs. Blue Ray Engineering's reports include these principle elements:

- Executive Summary
- Narrative Including:
 - Detailed description of methodology
 - Explanation of property classifications
 - Explanation of cost sources
 - Explanation of asset classes
 - Explanation of direct/indirect cost methodology
 - Explanation of engineering procedures used for determining property units & costs
 - Comprehensive property description
- Schedule of Contractor's Pay Requests (if newly constructed or renovated)
- Schedule of Indirect vs. Direct Costs
- Schedule of Property Take-off Quantities and Costs
- Photograph Exhibit



Why Blue Ray Engineering?

- Preparation by a firm that has performed hundreds of studies throughout the U.S.
- IRS guidelines state that cost segregation should be engineering based, relying on solid documentation, field measurements, using minimal estimation and following the most methodical and accurate approach
- Comprehensive in-house and client review process
- Competitive pricing



Blue Ray Engineering's Cost Segregation Process

1. Client/CPA-partner requests a FREE property analysis by submitting the Property Profile Form
2. Project manager analyzes the project, quotes the study fee and calculates the net present value of the anticipated depreciation and return on investment
3. Project engages and the client gathers all available design drawings, contractor's pay requests and other construction documents
4. Our engineers conduct a site visit to determine the amount of accelerable property, verify information contained in the drawings and/or pay requests
5. Typically 2 to 4 weeks after the site visit, the draft study report is presented to the client for review and the project is finalized