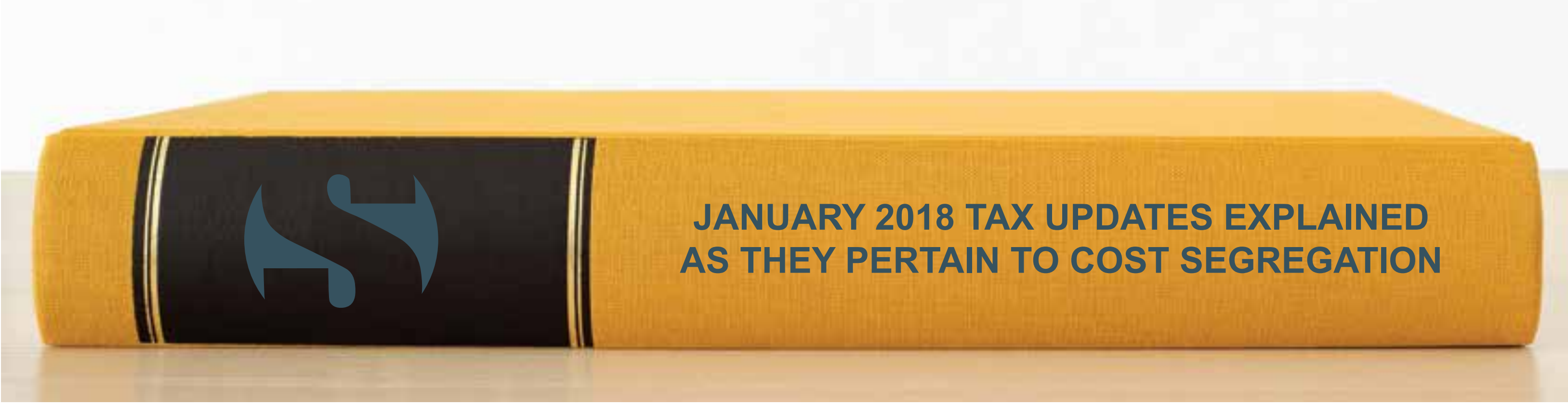

JANUARY 2018 TAX UPDATES EXPLAINED AS THEY PERTAIN TO COST SEGREGATION

The new tax laws are out and with them come important changes. While not all aspects affect cost segregation, some will have a substantial impact. Below, we highlight the biggest areas of concern and what they mean to you.

The most important things to note:

For 2017 assets there is only one major change: Bonus deprecation goes from 50% to 100% for property acquired and placed into service after 9/27/17. More detail on this change can be found below.

The remainder of the changes will affect 2018 assets. Note the major change here: The effective tax rate for 2018 and beyond will need to be adjusted due to the drop in the highest marginal federal rate from 39.6% to 37%.

QUALIFIED PROPERTIES

Qualified leasehold improvement property, qualified retail improvement property, and qualified restaurant property will go away for any property placed in service after 12/31/2017.

Qualified improvement property (“QIP”) will be the only “qualified” property starting 1/1/18.

Items to note:

QIP retains its prior definition

QIP is supposed to be 15-yr property, but is still technically 39-yr property because Congress made an error when they drafted the legislation. The staff of the House Ways and Means Committee has indicated that a technical correction is forthcoming.

As a 39-yr property, QIP is not eligible for bonus depreciation starting 1/1/18, but if the technical correction referenced above is made, and the recovery period is reduced to 15 years, it would then become eligible for bonus deprecation.

QIP placed in service in 2016 & 2017 is still eligible for bonus deprecation.

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BONUS DEPRECIATION

Bonus deprecation goes from 50% to 100% for **property acquired and placed into service** after 9/27/17.

The word "acquired" is important here. The new law expressly states that if there was a binding contract to acquire the property in place before 9/28/17, then the property was not acquired after 9/27/17. Therefore, it must be depreciated using the old rules.

What does this mean? Well, in a situation where construction was ongoing at the end of 2017, the contract for the construction was likely entered into prior to the 9/28 cutoff. Therefore, the construction would only be eligible for the 50% bonus depreciation allowance if it was placed into service in 2017. Any assets placed in service in 2018 will be subject to the 40% bonus rate.

Other bonus depreciation items to note:

The bonus depreciation percentage is scheduled to start decreasing in 2023, but it's anyone's guess as to what the law will be at that time.

Bonus depreciation is now allowed on used property acquired and placed into service after 9/27/17, so long as the taxpayer has not used the property at any time prior to the acquisition, and as long as it meets the other requirements of qualifying property (generally, meaning it must have a recovery period of 20 years or less).

CHANGES ASSOCIATED WITH THE ADS

Bonus depreciation is not allowed on property required to be depreciated under the Alternative Depreciation System (ADS). This has always been the case, but more businesses will be subject to ADS.

Take note:

The ADS recovery period for nonresidential real property is still 40 yrs. However, the ADS recovery period for residential real property has dropped from 40 to 30 years.

The ADS recovery period for QIP was supposed to go from 40 years to 20 years, but that provision was mishandled as well. So, while it may become a 20-yr recovery period if technical corrections are made, right now it's still 40 years because it's nonresidential real property.

You might be asking yourself why any of this matters, but it may matter a lot. Starting in 2018, many real property trade or business clients may be forced to make an election out of an interest expense limitation provision, and as part of that election, they'll be required to use ADS on tttheir residential rental property, nonresidential real estate, and qualified improvement property (so no bonus on ADS QIP), but not on tttheir 1245 property or land improvements.

179 EXPENSING

There are new regulations around 179 expensing, but due to the 100% bonus (if corrected) for QIP, 179 will be less of a concern.

However, the following assets, which may not qualify as QIP, do qualify to be expensed under 179:

- Roofs,
- HVAC property,
- Fire protection and alarm systems
- Security systems.

The limits in 2018 will be $1,000,000 with the phase out dollar-for-dollar beginning at $2,500,000 of qualifying assets placed in service during the same tax year.

AUTOMOTIVE DEALERSHIPS

Many dealership clients will no longer be eligible for bonus depreciation due to a provision involving floor plan financing. This will apply to dealers of vehicles designed to transport persons or property on a public street, boats, and farm machinery or equipment. Because of the complexity of these regulations, please reach out to us on a case-by-case basis to discuss.