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Four ways for property owners and developers to lower taxes on commercial real estate

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Would you rather keep money for yourself or share it with Uncle Sam?

While we might all prefer to keep the money, many commercial property owners and developers share more than they need to with Uncle Sam, because they are unaware of tax-saving opportunities.

Four of the most often overlooked opportunities include:

Credits for brownfields

Historic rehabilitation credits

Classification of repairs vs. capitalization

Cost-segregation studies

These four opportunities, which are typically considered when developing a tax-planning strategy, can save owners and developers hundreds of thousands or even millions of dollars.

Brownfields. Under Mass. General Law Chapter 21E, if you buy or control polluted property, or if someone contaminates property you own, you're responsible for cleaning it up. While virtually anyone who owns commercial property in Mass. knows that, many owners don't know that they may be able to get the state of Mass. to split the cost.

A tax credit included in the Brownfields Act: Chapter 206 of the Acts of 1998 was created as an incentive for developers to reclaim polluted property, as well as to stimulate economic growth by restoring abandoned properties and putting them back into use. The credit is scheduled to expire on Jan. 1, 2014.

If a project fails to qualify for the 50% credit, it may still qualify for a 25% credit if the owner specifies allowable and prohibited uses for the property. The tax credit is transferable and can be carried forward for up to five years, so even companies with projects that fail to qualify may be able to save money by buying credits from other companies.

Historic Rehabilitation Credits. Rehabilitation of property in a historic district is eligible for a 20% state and federal tax credit. However, development in a historic district is subject to close oversight. In Boston, for example, the Boston Landmarks Commission oversees such development.

Buildings outside of a historic district are still eligible for a 10% rehabilitation tax credit, though, if they were built before 1936.

Repair vs. Capitalization. When a project qualifies as a repair, the entire cost can be depreciated in a year. When it is a capital improvement, it is typically depreciated over 39 years.

While new temporary regulations issued by the Internal Revenue Service as Chapter 263(a) of the Federal Tax Code narrow what qualifies as a repair, there are significant planning opportunities, thanks to provisions that allow taxpayers to write off items that were replaced before being fully depreciated.

Taxpayers who capitalized rather than deducted their repairs and improvements may now be able to reach back and deduct the remaining carrying value as an expense.

For example, before the new rules were issued, a new roof costing $200,000 could be classified as a repair, potentially giving the taxpayer an $80,000 deduction. Now, the cost must be depreciated over 39 years, so the annual depreciation is just a few thousand dollars. However, a new roof is unlikely to last for 39 years, so taxpayers who can determine the value of the old roof can now write off the remaining carrying value when the roof is replaced.

Cost-Segregation Studies. A cost-segregation study is a breakdown and analysis of all assets associated with a building. When a cost-segregation study is performed, depreciation of many costs can be accelerated. It's a way to more accurately measure the depreciation of real property for tax purposes. If no cost-segregation study is conducted, the commercial building you own will be depreciated over 39 years, using the straight-line depreciation method.

Land improvements, which include landscaping, sewers, paving and curbing, can be depreciated over 15 years. Personal property, such as finish carpentry, emergency power generators, cabinets and even certain HVAC units, can be depreciated in five or seven years.

When performed properly, the study should consider potential deductions for hundreds or even thousands of components, including electrical outlets, wood trim, pipes and countertops. By segregating these costs, typically 10% to 30% of the purchase price of a building can be reallocated for depreciation over shorter periods.

Given the cost of commercial development, the right tax-planning strategy can save owners and developers significant dollars.

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