EPISODE 1025

[INTRODUCTION]

[00:00:00] ANNOUNCER: Welcome to The Real Estate Syndication Show. Whether you are a seasoned investor or building a new real estate business, this is the show for you. Whitney Sewell talks to top experts in the business. Our goal is to help you master real estate syndication.

And now your host, Whitney Sewell.

[INTERVIEW]

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Whitney Sewell: This is your daily real estate syndication show. I am your host, Whitney Sewell. It's that time a week again, where my business partner, Sam Rust, takes over the show and interviews our guest. I hope you enjoy the show.

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Sam Rust: This is your daily real estate syndication show. I'm your host, Sam Rust. And it's a pleasure to welcome Joseph Viery to the show. Joseph is the principal at US Tax Advisors Group, as a cost segregation expert so property owners differ, or eliminate millions of dollars in income taxes by leveraging IRS compliant cost segregation studies. Joseph ,welcome to the show. Thanks for joining us today.

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Joseph Viery: Well, thanks for having me on Sam.

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SR: Excellent. I was looking at your career, definitely have spent quite a bit of time in the tech space, excited to have you on to talk about cost segregation and some of how that applies not

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just to large multifamily to some smaller stuff as well but maybe for people who haven't heard of cost segregation study. If you could explain it a 30,000 foot level what we're doing, because it sounds a little bit like a scam, I know the first time I heard about it I was a little specific I was like wait, I can differ or eliminate that much in taxes. This can't be legit. How is it legit?

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JV: Well, okay so I laughed so hard because when I first started, which was in 2007or 2008, I can't remember, but it was a long time ago. That was the big buzz, you get to a property owner of the account name, this is a scam, it's got to be a scam. It's not a scam and and basically this accelerated depreciation has been around. I've heard some say oh since the 30s, but I have 1930s but I have no idea if that's true or not all I can tell you is the modern day there was a there was a court case in 1997, and the judge voted on a ruled on the side of the, the company Hospital Corporation of America which was suing the IRS. And he was so upset with the IRS's attitude towards accelerated depreciation, even though they said yeah this is the right way you should, you know, he said look, IRS, I want you to publish a document. So it took a couple years and in 2004 IRS published the audit technique guidelines, and it's on the internet.

So, just type in IRS audit technique guidelines for cost segregation and you'll see why it's legitimate. There's no question. It is the way you depreciate a building. And, what we're doing is complex but it's simple. So, I'll give you the simple high level version, all we're doing is we are breaking out the personal property of the building. And, the land improvements of the building, because they have shorter lives, and I can give you one example if I point to somebody who owns a multifamily or single-family pulling down the carpet, to the carpet and say well this last 27 and a half years which is straight line for residential, they would say you crazy I'll be lucky if I get five years. Well, the IRS recognizes that all across the building, so about 25% of the building, can be put in shorter lives. And, because it's putting shorter lives. It is because it can be put into shorter lives. It can be then combined with the 27 and a half year, and it gives the client, the acceleration of their depreciation. So, instead of waiting 27 and a half years for the client, the owner of the building gets -- if they get all of the depreciation, the year they bought the building so they bought it in 2020 for the 2020 tax return. I would give them that 25% as their, their deduction for additional depreciation rather than if they just did straight line.

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SR: That makes a lot of sense. So, at a high level we're just pushing forward depreciation pulling it from the entire life and compressing it into some smaller windows based on IRS approved guidelines.

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JV: Yes. And there is a concept called 100% bonus depreciation which was the new tax law. A couple years ago, the Trump tax law. And basically the reason why they get it all at once is because they get 100% of every life of an asset that's 20 years or less. Well, I just mentioned five year which is the inside of the building, 15-year which is the upside of the building. So, that's under 20 years. So, what I find is that 25%, they get all in by 2022 by winning in 2021. If you bought one this year, you'll get it for 21 tax returns.

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SR: Is the federal government looking at doing away with that as part of Biden's new tax plan that he's floating around me? It's very early in the process so who's to say but is that even on the table at this point to do away with bonus depreciation?

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JV: Okay, a couple things. Number one is, I am not an accountant, although I walk in that world, so I can't give tax advice, and I'm not a politician. However, I will just give you my opinion and my opinion is this -- I don't see how they could pull that off. No matter what, capital gains rates could increase. They probably will. But as far as getting rid of the bonus, depreciation goes into tax year 2022 anyway. But you can still get your value of cost segregation, but instead of getting it all in that year that you buy it, it just means there's going to be trails for five years.

So, you are still going to get the big bang for the buck. It's like the old going back to the old days. But as far as any changes to deplete depreciation, with the button. Man depreciation is so important to build the owners. I don't think there's any way they're going to touch that at all.

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SR: Yeah, so substantively the depreciation it's not going away, and I would agree with you there, it's just too big of a deal for too many voters. But the bonus depreciation itself is that ability to accelerate it all in one year that expires next year, so next year.

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JV: So you're right next year, and then it gradually got so the 23 and 75%, 74, 50%, 75, is that right to do three four. Okay, you know, it gradually phases out but who knows what Congress is going to, they may decide to continue, 100% bonus depends on how the economy is doing.

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SR: Yeah. Now, and by the time that it comes up for a decision or there's an ability to make a different decision. We're probably going to have a different Congress. So, who's to say? Never prognosticate the weather or politicians.

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JV: But here's one point, I would take the depreciation, if it's out there. I think you should always take it because you'll never get hurt by doing accelerated depreciation. Even if you get it on the back end, you're going to get it. It's just a matter of when you're going to get in tax your 2021 or you're gonna have to wait to when you sell the property five years down the road, doesn't make any difference you'll still get the benefit. So if you're on the fence in cash flows not a problem. I would say just do it, the depreciation then will be in the bank, and you use it when you use it because depreciation losses are good for 15 years. And you just use it up as you go. Each year if you use it all in one year. It's gone. But if it takes you five years, little by little, that's you can take all of it over five years.

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SR: So the federal government, obviously is giving us this leeway to take the depreciation a couple of different ways. Your firm, US Tax Advisors Group, assists people in completing these cost segregation studies. But you don't get to ride for free, all the way through usually our projects, you know, to five year old three to seven years if we're going to extend the windows a little bit, and there's such a thing as depreciation recapture.

Could you walk us through what that process looks like, especially for owners of these larger multifamily properties you know maybe 15, 20, 40 million, you know they've realized a substantial amount of gain by realizing those depreciation at the front end, but then they're getting ready to sell. What's that process like on the back end?

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JV: Okay, it's complex, it's complicated. But here is Joe's opinion because I talked to a lot of audiences that have a lot of CFOS, and now I'm talking about the big buildings. I'm not talking about small single family homes. I'm talking about $500 million buildings. And basically, the consensus because I try and nail this down with every CFO. And what I've come up with is a two years hold.

So, in other words if you know the property for two years. I think you should move forward and do cost segregation, if you're a flipper, or it's less than two years, I would be the one telling the client, you probably don't want to do it because of depreciation recapture. And what does this all mean? It means this if I save you $1 in taxes this year. What are you going to do with that dollar, because you're gonna have to pay me. So, you're going to have to, you know, pay me, and then you're going to have to, you know, have that dollar for long enough to make money on that dollar.

Now, my clients are very successful. My clients are buildings you know all over the United States, and their big buildings, and bottom line is if I give them $1 their IRR is like 60%, 70%. So, a two year old is not a problem, so they could have that dollar for two years. And their IRR is 60%, and they have to pay me and then they have to pay depreciation recapture back, they're saying yeah we'll do this all day long.

A lot of accountants just don't get the time value of money and what that means, the clients the owners do, because they're saying well I'm going to write this check out to the IRS for whatever $5,000 $10,000, $100,000. I want to keep that money and buy more real estate. And that's what we were able to do. Here's how. I'll just make this real simple, it's a very complex part of the depreciation. But, the bottom line is what we share with our clients, is that when you do cost segregation, you are able now to tell the IRS. How much of that five year property has been used up just like getting a laptop, buying a truck, you're using it up it's not going to be worth the same amount when you finally sell it. So let's say two years down the road and you're talking about five year property, what we would tell the client in the accountant to do is tell the IRS, you're going to take to two years, or 20% of that depreciation off the table because basically I used it up. It's not as valuable anymore. So, what have we've just done? We've taken from the basis of the building, that's in the depreciation taken, we've taken that off the table. So, actually cost segregation reduces depreciation recapture. If you have a savvy accountant, and they know what they're doing. So, I haven't had the depreciation capture push back in so long. I would have to study, because most of our clients just know. Forget about it. It's not not an important card, you know, in the whole equation.

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SR: Yeah. Are there any other special circumstances that would either push you towards doing cost segregation even if you're holding it for less than two years, or on the flip side, maybe a situation where you might not recommend a cost segregation?

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JV: Well, they're not recommending again, I just think it's not worth going through all of that because you know you're going to have to identify all of that you're gonna have to help me. So, a lot of buildings don't have construction plans and we're construction engineers that those are gold, and we realize you're not going to have construction plans that the building was built in the 19, you know, 50, 60, 70, 80 is getting plans for, forget about it.

So, bottom line is, it's not worth the pain to try and, you know, help us out and get you know appraisals and all this. So, if it's two years or less, again, I think that would that without even looking at the math. Now where it would be advantageous is I've had this happen where I've had a flipper, who owed a lot of money, $200,000 in taxes and he goes, you know what, I am going to still do cost segregation, because I know if I can take that $200,000, I can make a lot

of money on that $200,000. So, it's worth it for me. I don't care if I have to pay it back depreciation recapture, I'm going to still do it because I'm bailing myself out from writing that chapter for $200,000.

So, I think it just depends on the investors ability, what can they do with that money. You know, that's the biggest thing the other issue that would come about, is. And this is one of the strongest, the concept of passive investors versus active. So basically, I know, again, this gets complex but I'll make it a very high level, basically the passive investor is one who has another source of income. That's a passive investor. So let's say it's a doctor. The doctor buys a building, he's a passive investor because he's getting a check from his medical business, and that's is active income. So, there are rules against using passive losses, what happened in the 1980s is that, again, I'll pick on doctors, is the doctors were buying slum ridden houses that were not even, you know inhabitable, and they were using the appreciation to wipe out their taxes on the doctors in Congress and the IRS say no, no, no, no, you can't do that so they came up with the passive active rules. So what I would do to make this very crystal clear is simply ask your account, I would get an estimate from me, we don't charge us for estimates, and I'd go back to the accountant and I'd say Mr Accountant, Mr. Joe's gonna give me $25,000 in passive losses. Can I use them? Let them tell you the answer is no. Don't move forward, don't do it.

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SR: And generally, you can use passive losses to offset passive gains. And then if you're active in the investment so on the general partnership side of a real estate syndication in our little ecosystem, then you get to use that to offset other income or all active income assuming you meet the real estate professional guidelines.

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JV: But the important thing is what you just nailed down, is that a lot of accountants don't know this, what I create in passive losses can be used against any passive income. It doesn't have to be that one apartment complex, you know, in Boulder, Colorado, it can be used for any passive investment as a group, you can group all your past losses, and all your passive income together. That's important to realize so there are many many circumstances where even though I'm giving passive losses, they can use them.

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SR: I mean we keep coming back to this, neither of us are accountants. So, this is just general pontification, this is not sound tax advice. But having a good CPA on your team whether you're a limited partner or a passive investor or an active investor, it's really important.

We've discovered that in life bridge capital, you know, with different firms that we've worked with there's different ways to look at guidelines and then there's just, you know, different levels of acumen, and up to speed on what's going on in real estate tax law. How do you recommend finding a good accountant?

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JV: I think. Call Sam. No, you probably need to stay in your world of real estate and ask your other contacts, ask the Joe, US Tax Advisors Group. As you know, Sam's ask everybody out there who's involved in real estate and say this is my situation. I want to find somebody who specializes in real estate and who is a good accountant.

The location of the accountant office is not important so as long as you find somebody good as long as you find somebody that you feel is charging you fair, you know, value, then just ask your network of groups and I think most people in real estate they have a network of advisors, they should. And they should be able to pick one but make sure they're, they're involved in real estate I've seen this so many times where you get the accountant who basically deals with people who work for corporations they're not investors, that's like they don't know they can't even spell depreciation.

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SR: Definitely an underrated yet hugely valuable part of your team, even if you're a passive investor is making sure that you've got an account and that recognizes what to do with potential passive losses and help you strategize around reducing your taxable income.

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JV: Yes.

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SR: Generally, Joe we've had all of our projects we've done cost segregation studies, you know, like bridge capital we're doing larger projects, you know, $15 million, and up a large apartment complexes. And I've always heard that you know if it's under $500,000 or it's a single-family home you generally don't want to fiddle with a cost segregation study because it's going to cost more than it's worth, but then you just alluded to maybe some flippers doing cost segregation just they recognize time value of money and deferring it eaten by a year is huge for them. Is that general rule of thumb true or am I misinformed that single-family homes usually aren't worth doing cost seg?

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JV: That's a double edged sword but the answer is yes no. But here's the deal, when I started like everybody back in 2008, we were all, if you go to the audit technique guidelines, and that's

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our Bible so we play by the IRS rules. And that's what we do. And so, bottom line is the audit technique guidelines if you go to whatever it is chapter one, it's a list. I think seven different methodologies recognize the top one and that's the one that we always use. It's called the detailed engineering approach, and that means you have a construction engineer who basically goes through the plans the drawings and we go out and we have to look at the building we have to measure everything we have to document it we have to take pictures and bottom line that takes a lot of engineering, hours, and a lot of money. So you're right, I mean in the old days you couldn't touch it, a building with the basis of under $500,000.

And again, I think your audience is savvy enough but when I say building basis, land is not depreciable, so you've got to carve out land, US Tax Advisors, we're not land appraisers, so we leave that to the client and the accountant to come up with whatever application they want to give to land. So, now I've got the building basis to work with. So if the building basis is under $500,000, and the building is in Denver. Well, I'm not going to send somebody to fly to Denver, it wouldn't make financial sense. So, bottom line is about five years ago we came up with another technique which is listed as one of the acceptable techniques. It's called the modeling technique we use an engineered based statistical analysis, and we can use our satellite software to do the to do the look of the property, we get the information from the client very simple like an appraisal. And basically we can do everything in our offices and these studies cost hundreds of dollars.

So, bottom line is now we're talking about how small of a building, I've seriously done single family homes and Alabama years ago with that, that had been a basis for $20- $25,000. So, today. Those don't exist anymore, but bottom line is, any single-family home that you buy in the United States, we can now probably give you the numbers that are going to work we're going to be able to accelerate your depreciation. But you still have to look at the same thing you have to look at what are you going to do with the depreciation, how much is the cost for the study. The one thing you get when you use US Tax Advisors Group as you get us to defend you up there's an audit or questions. Now you're going to ask me, Joe, how often do we get audited? Well, I'll tell you what we play by the rules. And we don't get audited.

We've had clients get audited but they got out of it for other reasons, and then the auditor, the agent would say way to me You did cost segregation let's look at that and then they come back and ask a question, how did you calculate the square footage of the countertops, and all that? And then we tell them, here's my engineer he'll explain. So the engineer does all of them, and then that's it they say okay thanks bye.

So, we have not been. We're not party to any audits, but if we, if you were audited we would go to bat for you and we'd answer our work, we had explained how we came up with our findings,

and they're all like i said i get a you know we play by the rulebook so everything is is pretty much after the end of the conversation it's over and done with.

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SR: Yeah, that's fantastic. I appreciate you going into some detail on that.Q uestion that comes to mind, so you talked about the detailed engineering approach, which is, I think what most multifamily syndicators are familiar with, go through that whole engineering process. And then this modeling technique, which is a lot more scalable you can scale down to a lot smaller properties. Why not use the modeling technique for larger properties? Is it because you have to be more conservative in your estimates and you're not extracting as much value, or as could be extracted if you did the detailed approach?

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JV: Here's what happened, the talent that wrote our program, this was their conclusion, big, and by the way, we may go over a little bit like the 5-10,000, but we don't go over it very much farther than 500,000. And what we decided was that we felt we could not defend our work with the IRS. If the numbers in the analysis, and the algorithms get sloppy and sloppier as the building basis increases, and we just decided it's not worth our time to try to defend work that we thought would be to the point of maybe not even being able to defend. We feel very comfortable with 500,000 or less. No problem, but over 500,000, we won't do it. We have to do the full detailed approach.

But, now here's one thing I want to explain to everybody, the modeling approach is not meant to replace everything that the full detailed approach does. So, for example, one of the values of doing cost segregation. If you're doing a value add property by multifamily you're going in and each I know exactly what you're going to do, you're going to rip out the counters, you're going to rip out the flooring, you're going to be you're going to paint it you're going to, you know, blah, blah, blah. I've been involved in many of those. And what we do is when you have the detailed approach, you have how many linear feet of the counters, and, and, and when we did the, the analysis, what the value is. Because when you go in there and you rip that stuff out and you throw it away, that all has right off value modeling will not give you that we're not we're not giving you linear feet of countertops, we have no idea too much time in work. We're just telling you you can use the modeling to accelerate the depreciation. That's what we're giving you but the detailed engineering approach for someone that has a building over 500,000, even though it's going to cost more, might be well worth that I've had many times where the dispositions, the stuff they threw away…

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SR: So we've definitely seen the value of having those detailed figures, so we can go back and our value-add projects and write off everything that we're pulling out and send into the landfill or send into Habitat for Humanity or wherever they end up.

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JV: You know be the leader on that because a lot of accountants still don't get it. They don't understand that all of that stuff that's thrown away has value that's all able to write off.

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SR: One of the things is, we're getting close to the end here Joe, that I wanted to touch on as I was browsing through your website was the 45L tax credit, and I don't want us to get stuck in in the morass and all the details that are there but if you could at a high level, just give our audience, a brief overview of what 45 L encompasses?

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JV: Okay, 45 L and 179 D are energy studies and where they draw the line is anything under four stories or less is a 45 L project. Anything above four stories is the 179 D, and what you're getting is you're getting energy tax credits and what the IRS, the government whatever you want to say that what they're doing is they're telling the, the owner, that if you make improvements to the building, and you improve the energy in three areas, you're going to qualify for $2,000 per door tax credit. Tax credits are valuable, they're not like extra depreciation and tax credit is the $2,000 tax credit if you've got a even a 10 unit building you're going to get $20,000 just wipe off your taxes. That's how powerful a tax credit is whereas when I talk about appreciation depreciation is an expense.

So, if somebody wants to know how much money you're going to save out of your pocket. Take the losses I estimate and deduct that and use your tax rate. So, if you're on the 40% tax rate and I save you, I give you $100,000, you're going to save $40,000. A $2,000 tax credit means you are actually going to save $2,000 in taxes. So very powerful and what the three areas that we're looking at, is we're looking at the HVAC system. Pretty simple. It means the air conditioner and the heating. And guess what, any that you buy the day is going to be energy compliant because in most states around the country you can't even buy an hv AC unit that's not compliant. Number two is the electrical appliances, the light bulbs, the light fixtures are they are they, when you bought the new ones are the energy compliant. And the third one is the energy envelope, the doors, the seals, the windows. Will they reduce the energy consumption? And the only problem about doing this, is that we're very competitive with rates that are very good. However, we do have to send an engineer to the location. So that's the issue. It's not the cost of the study, it's the cost of the study. After I send somebody to Alabama. So, therefore, if there's only two ways to do this either you have a large portfolio. Meaning, you've got 20 single-family homes that you fixed up, or you can combine with

friends, because if I have to say oh and guess what my engineer has to drive. Because there's testing material, we can't figure a way out to fly it out there. So he's got to get he's got it, he's got to drive out to Alabama. And so that all takes time and money so that's the only problem with the 45 L, but even if you can find somebody in Alabama to do it. It's, it's big, so look into it if somebody wants me to help them out I help anybody out by email by phone call me, and I'll put you in touch with my engineer, and I can give you more information but most value add, you are taking care of you are increasing the energy envelope.

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SR: Very interesting so it doesn't apply just to new development, you can also take advantage of that tax credit, on a value add.

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JV: Right.

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SR: Okay. And can you combine the 45 L like is it the same engineer on your side that does the 45 L and the cost segregation?

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JV: No, that's a different you know I hate to say it is a different animal. You know on one side the construction engineers, the other guys an energy engineer and the energy engineer has his hat on, and all he's doing is the testing for the energy savings and there is testing that has to be done.

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SR: Awesome, well I really appreciate you shedding light on cost segregation, some of the finer points there Joe, as well as the 45 L tax credit, definitely look forward to learning more about that.

In the meantime, where can our audience find out more about you, your company and how can they get in touch with you?

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JV: I think the website's the best. It's US Tax Advisors Group which is ustaginc.com. So, my email is joev. My last name is Viery, so joev@ustaginc.com. If you go to our website and fill out the input page, we will give you a no cost estimate on how much tax savings we'll be able to provide. And so I advise everybody just go online, go to our input form. Give us the answers to a few questions and we'll respond back with the free estimate.

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SR: Fantastic. Well thanks Joe, really appreciate it. Thank you to our audience for joining us on another episode of The Real Estate syndication show.

0:27:07.0 ANNOUNCER: Thank you for listening to The Real Estate Syndication Show, brought to you by Lifebridge Capital. Lifebridge Capital works with investors nationwide to invest in real estate while also donating 50% of its profits to assist parents who are committing to adoption. Lifebridge Capital, making a difference one investor and one child at a time. Connect online at www.lifebridgecapital.com for free material and videos to further your success.

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