



Engineering-Based Cost Segregation Study — Short-Term Rental
Property

8742 N Hayden Rd
Scottsdale, AZ 85258

Purchase Price

\$750,000

Accelerated Asset Reclassification

\$134,610

Depreciable Basis

\$517,725

Report Number

CSS-20260314-21450

Prepared for: Sample Report — STR Investor

Study Date: March 14, 2026

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Engineering-Based Cost Segregation Report

CSS-WP-010

Dear Sample Report — STR Investor,

Cost Seg Smart was engaged to perform an engineering-based cost segregation study for the property located at 8742 N Hayden Rd, Scottsdale, AZ 85258. This study is intended to identify and classify assets for accelerated depreciation purposes in accordance with applicable tax regulations.

The procedures utilized in this study included an engineering-based analysis using construction cost manuals, IRS asset classification guidance, and property characteristics derived from public records and taxpayer-provided information. This analysis was performed in accordance with the IRS Cost Segregation Audit Techniques Guide (ATG).

The study identified a total of \$134,610 in accelerated depreciation, representing 26.0% of the depreciable basis. This includes \$99,405 classified as 5-year property and \$32,602 as 15-year property. The applicable bonus depreciation rate for the property is 100% as it was placed in service in 2025.

The study was conducted based on information provided by the taxpayer, and the results are subject to the accuracy of this data. The findings are contingent upon the completeness and correctness of the information provided.

The scope of this study was limited to the identification and classification of assets for depreciation purposes and does not constitute a valuation. It is recommended that these findings be reviewed with a qualified tax advisor to ensure alignment with the taxpayer's specific tax situation.

Report No.: CSS-20260314-21450

Sincerely,

Cost Seg Smart Engineering & Tax Analysis Team costsegsmart.com

If your CPA has questions about this report, they can reach us directly at support@costsegsmart.com.

1. Executive Summary

Short-Term Rental Property

CSS-WP-100

The study identified \$134,610 of assets eligible for accelerated depreciation — 26.0% of the property's depreciable basis.

The subject property is classified as Residential Rental Property under IRC §168(e)(2) with a default recovery period of 27.5 years. The purpose of this study is to identify components eligible for accelerated depreciation, thereby optimizing the timing of depreciation deductions. In the context of a short-term rental (STR), material participation under IRC §469 may be relevant, and the analysis of Furniture, Fixtures, and Equipment (FF&E;) is crucial. The study found that 26.0% of the property's depreciable basis qualifies for accelerated depreciation.

Scope of Work

This cost segregation study was performed to identify property components that may qualify for accelerated depreciation under the Modified Accelerated Cost Recovery System (MACRS) in accordance with Internal Revenue Code §168. The analysis applied an engineering-based cost approach using construction cost data, public records, and taxpayer-provided information, combined with applicable IRS asset classification guidance, to allocate portions of the building cost to shorter recovery period property.

The study was conducted in a manner consistent with the principles outlined in the IRS Cost Segregation Audit Techniques Guide (ATG). The results presented in this report are intended to assist the taxpayer and their tax advisor in determining appropriate depreciation treatment for federal income tax purposes.

All cost allocations in this report represent estimates derived from construction cost data, public records, property characteristics, and applicable tax guidance. This study does not constitute tax, legal, or accounting advice and should be reviewed by the taxpayer's qualified tax advisor prior to filing.

Reclassification Results

Our analysis identified **\$134,610** (26.0% of depreciable basis) in building systems eligible for reclassification into shorter MACRS recovery periods.

This study identified **\$134,610** of building components eligible for shorter MACRS recovery periods, which may generate a first-year deduction of up to **\$134,610** under 100% bonus depreciation, subject to the taxpayer's individual tax circumstances.

Tax Timing Impact

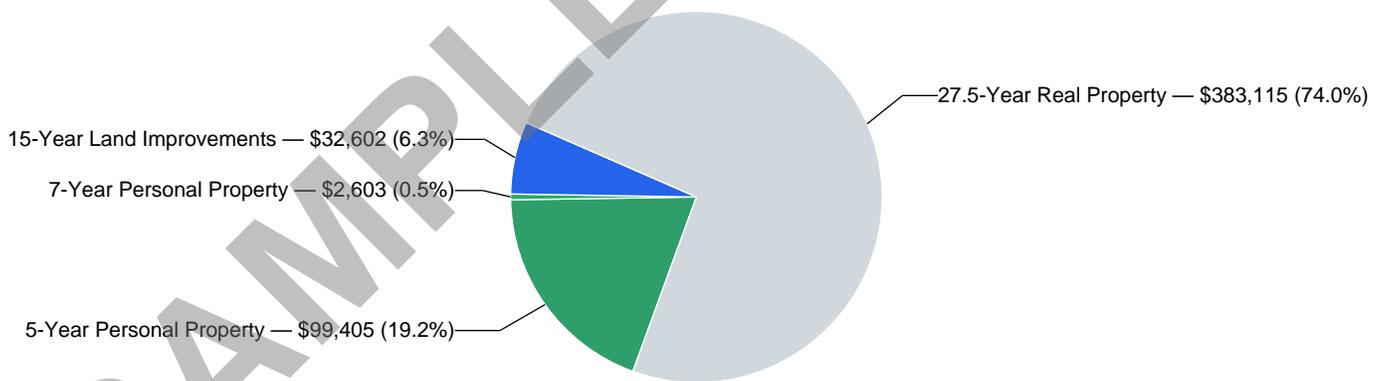
For the placed-in-service year of 2025, the applicable bonus depreciation rate is 100% under IRC §168(k). Current federal tax law has restored 100% bonus depreciation for qualified property placed in service in 2025 and later, allowing for immediate expensing of eligible assets.

Engineering Analysis Summary

Based on the wood frame residential construction typical of 2018-era builds in the Scottsdale, AZ market, our analysis identified component-level allocations consistent with properties of this age, construction class, and quality tier. This short-term rental property includes hospitality-grade furnishings, fixtures, and equipment (FF&E;) classified as 5-year and 7-year personal property under Rev. Proc. 87-56. FF&E; items identified include furniture, electronics, linens, kitchen smallwares, and decorative items subject to accelerated recovery periods.

Metric	Value
Purchase Price	\$750,000
Land Value (Non-Depreciable)	\$232,275
Total Depreciable Basis	\$517,725
5-Year Personal Property	\$99,405 (19.2%)
15-Year Land Improvements	\$32,602 (6.3%)
27.5-Year Real Property	\$383,115 (74.0%)
Total Accelerated Asset Reclassification	\$134,610 (26.0%)

Depreciable Basis Allocation by MACRS Class



Estimated First-Year Tax Savings (100% Bonus Depreciation)

Tax Bracket	First-Year Deduction	Estimated Tax Savings
24%	\$134,610	\$32,306
32%	\$134,610	\$43,075
37%	\$134,610	\$49,806

Replacement Cost New (RCN) estimates were developed using industry construction cost databases and calibrated to the subject property's market-implied improvement value. The resulting cost allocation is reconciled to the taxpayer's depreciable basis of **\$517,725** so that all component-level costs collectively equal the recorded acquisition price less land value, consistent with cost approach methodology described in the IRS Cost Segregation Audit Techniques Guide (ATG). Modeled construction costs closely align with the transaction price, consistent with typical construction cost patterns for this property type and market.

Industry Benchmarks

This study identified 26.0% accelerated depreciation, which is consistent with the observed market range of 25%-40% for short-term rental properties of this vintage and quality tier.

IRS Cost Segregation ATG Compliance

This study was prepared using the engineering cost approach described in the IRS Cost Segregation Audit Techniques Guide (ATG), including:

- ✓ Component-level asset identification and classification
- ✓ Engineering cost estimation using industry construction cost databases
- ✓ Reconciliation of allocated costs to taxpayer depreciable basis
- ✓ Legal authority for asset classification (IRC §§1245, 1250)
- ✓ MACRS recovery schedules compliant with Rev. Proc. 87-56
- ✓ Documentation sufficient for IRS examination

Prepared using industry-standard cost databases including RSMeans Construction Cost Data, BLS Producer Price Index adjustments, and regional construction cost factors. The methodology and documentation address the 13 principal elements of a quality cost segregation study described in the IRS Cost Segregation ATG.

CPA Quick-Reference Summary

Property Facts

Property Address	8742 N Hayden Rd, Scottsdale, AZ 85258
Property Type	Short-Term Rental
Year Built	2018
Purchase Price	\$750,000
Land Value (Non-Depreciable)	\$232,275
Depreciable Basis	\$517,725
Placed in Service	2025-01-15

Basis Allocation Summary

Asset Class	Amount	% of Basis
5-Year Personal Property	\$99,405	19.2%

7-Year Personal Property	\$2,603	0.5%
15-Year Land Improvements	\$32,602	6.3%
27.5-Year Real Property	\$383,115	74.0%
Total Accelerated Property	\$134,610	26.0%

Estimated Year-1 Depreciation (100% Bonus)

Asset Class	Accelerated Basis	Bonus Rate	Year-1 Deduction
5-Year Property	\$99,405	100%	\$99,405
7-Year Property	\$2,603	100%	\$2,603
15-Year Property	\$32,602	100%	\$32,602
Total Year-1 Deduction			\$134,610

Estimated Tax Savings

Tax Bracket	Estimated Tax Savings
24%	\$32,306
32%	\$43,075
37%	\$49,806

Typical accelerated depreciation ranges for short-term rental properties constructed between 1980 and 2020 are approximately 25%–40% of depreciable basis. The **26.0%** allocation identified in this study falls within the expected range for properties of this type and construction class.

Method Summary

- Engineering-based cost approach using construction cost data and public records
- Allocation based on IRS Cost Segregation Audit Techniques Guide (ATG)
- Asset classifications supported by IRC §168, Rev. Proc. 87-56, and relevant case law

CPA Filing Sheet

Property: 8742 N Hayden Rd, Scottsdale, AZ 85258
Placed in Service: 2025-01-15
Total Depreciable Basis: \$517,725

Accelerated Asset Schedule

Asset Class	Amount	Recovery Period	Convention	Bonus Eligible
Personal Property	\$99,405	5 years	Half-year	Yes (100%)
Personal Property (7-yr)	\$2,603	7 years	Half-year	Yes (100%)
Land Improvements	\$32,602	15 years	Half-year	Yes (100%)
Building (27.5-yr)	\$383,115	27.5 years	Mid-month	No

Depreciation Software Entry Instructions

Enter the following assets in your depreciation software (Lacerte, ProSeries, Drake, UltraTax, or equivalent):

Asset 1 — Personal Property (5-Year)

Basis: \$99,405
 Life: 5 years | Method: 200% DB | Convention: Half-year
 Bonus Depreciation: 100%

Asset 2 — Personal Property (7-Year)

Basis: \$2,603
 Life: 7 years | Method: 200% DB | Convention: Half-year
 Bonus Depreciation: 100%

Asset 3 — Land Improvements (15-Year)

Basis: \$32,602
 Life: 15 years | Method: 150% DB | Convention: Half-year
 Bonus Depreciation: 100%

Asset 4 — Building (27.5-Year)

Basis: \$383,115
 Life: 27.5 years | Method: Straight-line | Convention: Mid-month
 Bonus Depreciation: Not eligible

Note: These entries reflect the reclassification identified in this study. The taxpayer should file Form 3115 (Change in Accounting Method) if the property was placed in service in a prior tax year. Consult with your tax advisor regarding the appropriate filing method.

SAMPLE REPORT

2. Property Summary

CSS-WP-200

Property Detail	Information
Owner	Sample Report — STR Investor
Property Address	8742 N Hayden Rd, Scottsdale, AZ 85258
Property Type	Short-Term Rental
Date of Acquisition	2025-01-15
Placed in Service	2025-01-15
Purchase Price	\$750,000
Building Area	2,400 SF
Year Built	2018
Bedrooms / Bathrooms	4 BR / 3 BA
Construction Type	Wood Frame Residential
Property Features	Standard

Property Classification

This property is classified as **Residential Rental Property** under IRC Section 168(e)(2)(A). The default recovery period for the building structure is **27.5 years** under the General Depreciation System (GDS) of MACRS. Through cost segregation, certain components are reclassified to shorter recovery periods as permitted by the Internal Revenue Code.

3. Cost Allocation Summary

CSS-WP-210

\$134,610 of the property's \$517,725 depreciable basis was reclassified into shorter recovery periods.

The following table summarizes the allocation of the property's depreciable basis among the various MACRS recovery period categories. Components have been classified based on their function, construction, and relationship to the building per IRS guidelines.

Asset Category	IRS Recovery Period	Allocated Cost	% of Basis
Personal Property	5-Year MACRS	\$99,405	19.2%
Personal Property	7-Year MACRS	\$2,603	0.5%
Land Improvements	15-Year MACRS	\$32,602	6.3%
Real Property (Building)	27.5-Year Straight Line	\$383,115	74.0%
Total Depreciable Basis		\$517,725	100.0%
Total Accelerated (Reclassified)		\$134,610	26.0%

This study identifies shorter-life personal property and land improvements eligible for accelerated depreciation from the property's total depreciable basis. Modeled replacement cost components are reconciled to actual basis so that total allocated costs tie to the taxpayer's transaction price less land. Detailed component support appears in Sections 4 and 5; cost derivation methodology is documented in Appendix A.

Key Accelerated Components

The following table summarizes the principal components reclassified to shorter recovery periods. Items below 1% of total accelerated basis are grouped into category subtotals.

Component	Allocated Cost	MACRS Class
Bedroom Furniture (Beds, Dressers, Nightstands)	\$16,272	5-Year
Living Area Furniture (Sofas, Tables, Chairs)	\$13,678	5-Year
Carpet & Pad	\$9,252	5-Year
Appliances	\$8,409	5-Year

Televisions & Electronics	\$6,710	5-Year
Light Fixtures	\$5,934	5-Year
Outdoor Furniture & Accessories	\$5,544	5-Year
Vinyl/Laminate Flooring	\$4,868	5-Year
Linens, Bedding & Towels	\$3,828	5-Year
Dining Furniture	\$3,316	5-Year
Removable Kitchen Fixtures	\$2,940	5-Year
Kitchen Smallwares & Cookware	\$2,583	5-Year
Bathroom Accessories & Fixtures	\$2,278	5-Year
Window Treatments	\$2,061	5-Year
Removable Laminate Surfaces	\$1,751	5-Year
Closet Shelving	\$1,721	5-Year
Door Hardware & Accessories	\$1,525	5-Year
Ceiling Fans	\$1,466	5-Year
<i>Other 5-Year Components (6 items)</i>	\$5,268	5-Year
Subtotal — 5-Year	\$99,405	
Decorative Items & Artwork	\$2,603	7-Year
Subtotal — 7-Year	\$2,603	
Concrete Paving & Walks	\$7,445	15-Year
Wood Deck/Porch	\$5,737	15-Year
Landscaping	\$5,168	15-Year
Fencing	\$4,431	15-Year
Asphalt Paving	\$2,765	15-Year
Exterior Lighting	\$1,881	15-Year
Storm Drainage & Grading	\$1,844	15-Year
Irrigation System	\$1,618	15-Year
Retaining Walls	\$1,446	15-Year

Other 15-Year Components (1 items)	\$266	15-Year
Subtotal — 15-Year	\$32,602	
Total Accelerated (Reclassified)	\$134,610	

Property Characterization (IRC §1245 / §1250)

Asset Category	IRC Section	Recapture Treatment	Amount
5-Year Personal Property	§1245	Ordinary income recapture	\$99,405
7-Year Personal Property	§1245	Ordinary income recapture	\$2,603
15-Year Land Improvements	§1250	25% unrecaptured §1250 gain	\$32,602
27.5-Year Real Property	§1250	25% unrecaptured §1250 gain	\$383,115

Tax Impact Analysis

Tax Scenario	Amount
Year 1 Depreciation WITHOUT Cost Segregation	\$18,826
Year 1 Depreciation WITH Cost Segregation + 100% Bonus	\$148,541
Additional First-Year Deduction	\$129,715
Estimated Federal Tax Reduction (37% marginal rate)	\$47,995
Estimated Federal Tax Reduction (32% marginal rate)	\$41,509
Estimated Federal Tax Reduction (24% marginal rate)	\$31,132

Note: The reclassified asset total (\$134,610) differs from the additional first-year deduction (\$129,715) because these assets would have received \$4,895 in standard straight-line depreciation regardless of cost segregation.

First-Year Depreciation Comparison

Cost segregation increases first-year depreciation by \$129,715, concentrating the majority of tax benefits in Year 1 through bonus depreciation.



SAMPLE REPORT

4. Detailed Component Breakdown

CSS-WP-220

35 components reclassified into accelerated categories; 17 structural components itemized at their default recovery period.

The following tables provide a detailed breakdown of all building components identified in this study, organized by MACRS recovery period. Each component has been individually assessed based on its function, construction type, and applicable IRS asset classification. Direct asset costs and indirect cost allocations are shown separately for full transparency.

5-Year Personal Property (IRC Section 1245)

Component	Asset Cost	Indirect Costs	Total Depreciable Basis
Carpet & Pad	\$8,647	\$2,162	\$9,252
Vinyl/Laminate Flooring	\$4,549	\$1,137	\$4,868
Removable Kitchen Fixtures	\$2,748	\$687	\$2,940
Bathroom Accessories & Fixtures	\$2,129	\$532	\$2,278
Removable Laminate Surfaces	\$1,637	\$409	\$1,751
Appliances	\$7,860	\$1,965	\$8,409
Window Treatments	\$1,926	\$482	\$2,061
Door Hardware & Accessories	\$1,425	\$356	\$1,525
Light Fixtures	\$5,546	\$1,387	\$5,934
Ceiling Fans	\$1,370	\$342	\$1,466
Removable Plumbing Trim	\$1,013	\$253	\$1,084
Smoke/CO Detectors	\$345	\$86	\$370
Closet Shelving	\$1,609	\$402	\$1,721
Decorative Millwork	\$945	\$236	\$1,011
Specialty Electrical	\$1,160	\$290	\$1,241
Bathroom Hardware	\$834	\$208	\$892
Kitchen Hood & Ventilation	\$627	\$157	\$670
Bedroom Furniture (Beds, Dressers, Nightstands)	\$15,208	\$3,802	\$16,272

Living Area Furniture (Sofas, Tables, Chairs)	\$12,784	\$3,196	\$13,678
Dining Furniture	\$3,099	\$775	\$3,316
Televisions & Electronics	\$6,272	\$1,568	\$6,710
Linens, Bedding & Towels	\$3,577	\$894	\$3,828
Kitchen Smallwares & Cookware	\$2,414	\$604	\$2,583
Outdoor Furniture & Accessories	\$5,182	\$1,295	\$5,544
Subtotal	\$92,906	\$23,227	\$99,405

7-Year Personal Property (IRC Section 1245)

Component	Asset Cost	Indirect Costs	Total Depreciable Basis
Decorative Items & Artwork	\$2,433	\$608	\$2,603
Subtotal	\$2,433	\$608	\$2,603

15-Year Land Improvements (IRC Section 1250)

Component	Asset Cost	Indirect Costs	Total Depreciable Basis
Concrete Paving & Walks	\$6,958	\$1,739	\$7,445
Asphalt Paving	\$2,584	\$646	\$2,765
Fencing	\$4,142	\$1,035	\$4,431
Landscaping	\$4,830	\$1,208	\$5,168
Irrigation System	\$1,513	\$378	\$1,618
Exterior Lighting	\$1,758	\$440	\$1,881
Retaining Walls	\$1,352	\$338	\$1,446
Wood Deck/Porch	\$5,362	\$1,340	\$5,737
Storm Drainage & Grading	\$1,723	\$431	\$1,844
Mailbox & Site Accessories	\$249	\$62	\$266
Subtotal	\$30,471	\$7,618	\$32,602

27.5-Year Real Property (IRC Section 1250)

The following components constitute the structural building envelope and core building systems that remain classified as residential rental property under IRC §168(e)(2)(A). These components — including foundation, framing, roofing, exterior envelope, core HVAC, plumbing, and electrical distribution — are inherently permanent and integral to the building's operation. They are depreciated over 27.5 years using the straight-line method.

Component	Asset Cost	Indirect Costs	Total Depreciable Basis
Foundation	\$34,922	\$8,730	\$37,364
Framing	\$55,324	\$13,831	\$59,193
Roofing	\$24,416	\$6,104	\$26,124
Exterior Walls & Siding	\$25,550	\$6,388	\$27,338
Windows & Exterior Doors	\$22,321	\$5,580	\$23,883
Insulation	\$11,365	\$2,841	\$12,160
Drywall & Finishing	\$26,857	\$6,714	\$28,736
Interior Paint	\$8,584	\$2,146	\$9,184
Kitchen Cabinets (Built-in)	\$8,676	\$2,169	\$9,282
Bathroom Vanities (Built-in)	\$3,099	\$775	\$3,316
Interior Doors	\$3,342	\$835	\$3,575
Tile Flooring	\$13,814	\$3,453	\$14,780
Plumbing Systems	\$39,569	\$9,892	\$42,337
Electrical Systems	\$32,209	\$8,052	\$34,462
HVAC Systems	\$34,712	\$8,678	\$37,139
Fire Sprinkler System	\$6,826	\$1,706	\$7,303
Permanently Affixed Countertops	\$6,486	\$1,621	\$6,939
Subtotal	\$358,071	\$89,518	\$383,115

4b. Indirect Cost Allocation

Construction costs include both direct costs (labor and materials for individual components) and indirect costs (overhead expenses necessary for the overall construction project). Indirect costs are allocated proportionally across all building components based on their direct cost share, consistent with the IRS Cost Segregation Audit Techniques Guide (ATG) methodology.

Indirect Cost Category	% of Direct Costs	Allocated Amount
Architectural & Engineering Fees	4.0%	\$19,355
General Conditions & Supervision	5.5%	\$26,613
Equipment Rentals & Tools	3.5%	\$16,936
Permits & Inspections	2.0%	\$9,678
Insurance & Bonding	2.5%	\$12,097
Contractor Overhead & Profit	5.0%	\$24,194
Miscellaneous Indirects	2.5%	\$12,097
Total Indirect Costs	25.0%	\$120,970

Total direct costs: \$483,881. Indirect cost rate applied: 25.0% of direct costs. Indirect costs are allocated pro-rata to each component based on its share of total direct costs, consistent with IRS ATG guidance on indirect cost allocation for cost segregation studies.

4c. Reconciliation of Costs

The IRS Cost Segregation Audit Techniques Guide requires that estimated costs be reconciled back to actual costs or purchase price. The following reconciliation demonstrates that all allocated costs sum to the property's actual depreciable basis, with no unexplained variance.

A. Basis Determination

Item	Amount	Notes
Purchase Price / Total Project Cost	\$750,000	Per closing statement
Less: Land Value (31.0%)	(\$232,275)	Land allocation per statistical
Depreciable Basis	\$517,725	= Total Project Cost - Land

B. Cost Segregation Allocation

Asset Category	Recovery Period	Allocated Cost
Non-Depreciable Land	N/A	\$232,275
Personal Property	5-Year MACRS	\$99,405
Personal Property	7-Year MACRS	\$2,603
Land Improvements	15-Year MACRS	\$32,602
Real Property (Building)	27.5-Year Straight Line	\$383,115
Total		\$750,000

C. Reconciliation Verification

Reconciliation Item	Amount
A. Total Project Cost (Purchase Price)	\$750,000
B. Total Allocated per Cost Segregation Study	\$750,000
Variance (A - B)	\$0

All allocated costs reconcile to the property's total project cost to the penny. No unexplained variance exists between the purchase price and the sum of all cost segregation allocations (land + depreciable components).

5. Engineering Rationale by Category

CSS-WP-230

The following narratives describe the engineering basis for reclassifying specific building components from the default recovery period to accelerated MACRS classes. Each classification is supported by IRS guidance, Treasury Regulations, and relevant Tax Court precedent.

Floor Coverings

Floor coverings such as carpet, vinyl, and laminate are classified as 5-year property based on their nature as tangible personal property under Treas. Reg. §1.48-1(e)(1). The Whiteco six-factor test supports this classification, considering factors such as the typical 5-10 year replacement cycle and the lack of permanent attachment to the structure.

Cabinetry

Removable cabinetry is classified as 5-year property due to its method of attachment and lack of functional interdependence with the building structure. Built-in cabinetry, which is permanently affixed and integral to the building's function, would be classified under the longer recovery period of 27.5 years.

Electrical

Decorative and specialized electrical components, such as light fixtures and specialty electrical systems, are classified as 5-year property under Rev. Proc. 87-56 Asset Classes 00.11 and 00.12. These components are distinct from the core building electrical systems, which serve the building's overall utility and are classified under a longer recovery period.

Plumbing Fixtures

Removable plumbing accessories, such as bathroom hardware, are classified as 5-year property due to their nature as tangible personal property. These items are not integral to the building's plumbing infrastructure, which is classified under a longer recovery period of 27.5 years.

Site Work

Site improvements such as concrete paving, asphalt paving, and landscaping are classified as 15-year property under IRC §168(e)(4). These improvements are not integral to the building structure and are considered land improvements, which have a distinct recovery period.

Appliances

Appliances are classified as 5-year personal property based on their freestanding nature and the IRS ATG guidance. This classification distinguishes them from built-in systems that are integral to the building's function.

Finishes

Finish materials such as removable laminate surfaces and decorative millwork are classified as 5-year property due to their nature as removable and decorative finishes. These are distinct from permanently affixed surfaces, which would be classified under a longer recovery period.

FF&E;

In the context of a short-term rental, FF&E; is classified as 5-year property due to its nature as hospitality-grade furnishings. This classification is consistent with Rev. Proc. 87-56 Asset Class 00.11, which distinguishes FF&E; from structural improvements.

FF&E; Substantiation Note: The FF&E; values in this study are estimated using per-square-foot cost models calibrated to hospitality-industry furnishing standards, not from a physical inventory or purchase receipts. If the taxpayer maintains itemized FF&E; purchase records, invoices, or a furnished-unit inventory list, those actual costs should be substituted for the estimates in this report. Actual cost documentation strengthens the defensibility of FF&E; allocations under IRS examination. The taxpayer's CPA should review FF&E; totals against available records before filing.

6. MACRS Depreciation Schedules

CSS-WP-300

With 100% bonus depreciation, the estimated first-year depreciation deduction on reclassified assets is \$134,610.

The following schedules show the annual depreciation deductions under MACRS for each asset category. The 5-year and 15-year property schedules include 100% bonus depreciation in Year 1 under current federal tax law (IRC §168(k)), effective for property placed in service in 2025 and later.

5-Year Personal Property (with 100% Bonus)

Year	Annual Deduction	Cumulative	Remaining Basis
1	\$99,405	\$99,405	\$0
2	\$0	\$99,405	\$0
3	\$0	\$99,405	\$0
4	\$0	\$99,405	\$0
5	\$0	\$99,405	\$0
6	\$0	\$99,405	\$0

7-Year Personal Property (with 100% Bonus)

Year	Annual Deduction	Cumulative	Remaining Basis
1	\$2,603	\$2,603	\$0
2	\$0	\$2,603	\$0
3	\$0	\$2,603	\$0
4	\$0	\$2,603	\$0
5	\$0	\$2,603	\$0
6	\$0	\$2,603	\$0
7	\$0	\$2,603	\$0
8	\$0	\$2,603	\$0

15-Year Land Improvements (with 100% Bonus)

Year	Annual Deduction	Cumulative	Remaining Basis
1	\$32,602	\$32,602	\$0

2	\$0	\$32,602	\$0
3	\$0	\$32,602	\$0
4	\$0	\$32,602	\$0
5	\$0	\$32,602	\$0
6	\$0	\$32,602	\$0
7	\$0	\$32,602	\$0
8	\$0	\$32,602	\$0
9	\$0	\$32,602	\$0
10	\$0	\$32,602	\$0
11	\$0	\$32,602	\$0
12	\$0	\$32,602	\$0
13	\$0	\$32,602	\$0
14	\$0	\$32,602	\$0
15	\$0	\$32,602	\$0
16	\$0	\$32,602	\$0

27.5-Year Real Property (Straight-Line)

Year	Annual Deduction	Cumulative	Remaining Basis
1	\$6,966	\$6,966	\$376,149
2	\$13,931	\$20,897	\$362,218
3	\$13,931	\$34,829	\$348,287
4	\$13,931	\$48,760	\$334,355
5	\$13,931	\$62,692	\$320,424
6	\$13,931	\$76,623	\$306,492
7	\$13,931	\$90,554	\$292,561
8	\$13,931	\$104,486	\$278,629
9	\$13,931	\$118,417	\$264,698
10	\$13,931	\$132,349	\$250,766
11	\$13,931	\$146,280	\$236,835
12	\$13,931	\$160,212	\$222,903
13	\$13,931	\$174,143	\$208,972
14	\$13,931	\$188,075	\$195,040

15	\$13,931	\$202,006	\$181,109
16	\$13,931	\$215,938	\$167,178
17	\$13,931	\$229,869	\$153,246
18	\$13,931	\$243,801	\$139,315
19	\$13,931	\$257,732	\$125,383
20	\$13,931	\$271,663	\$111,452
21	\$13,931	\$285,595	\$97,520
22	\$13,931	\$299,526	\$83,589
23	\$13,931	\$313,458	\$69,657
24	\$13,931	\$327,389	\$55,726
25	\$13,931	\$341,321	\$41,794
26	\$13,931	\$355,252	\$27,863
27	\$13,931	\$369,184	\$13,931
28	\$6,966	\$376,149	\$6,966

7. Net Present Value Analysis

CSS-WP-310

Accelerating deductions into earlier years increases their present value — a dollar of tax savings today is worth more than one spread over decades.

The NPV analysis assumes a 5% discount rate and a 37% marginal tax rate to evaluate the present value of accelerated deductions. Accelerated deductions in earlier years are worth more in present-value terms, but actual savings depend on the taxpayer's specific rate and circumstances.

Cost segregation does not change the total depreciation allowed over the life of the property. It accelerates deductions into earlier years, increasing the present value of the associated tax savings.

Scenario	NPV of Tax Savings from Depreciation
Without Cost Segregation (Straight-Line)	\$99,571
With Cost Segregation + Bonus Depreciation	\$121,116
NPV Benefit of Cost Segregation	\$21,545

Assumptions: Discount rate: 5.0% | Marginal tax rate: 37% (illustrative — actual rate depends on taxpayer's specific situation) | 100% bonus depreciation applied to eligible 5-year and 15-year property (per IRC §168(k) for placed-in-service year) | Half-year convention applied to first and last years of all MACRS schedules. This analysis does not account for passive activity loss limitations, depreciation recapture, or state tax variations.

8. Depreciation Recapture Considerations

CSS-WP-320

Cost segregation accelerates when deductions are taken, not how much — total lifetime depreciation remains the same.

Depreciation recapture considerations for this property involve IRC §1245 for ordinary income recapture of personal property and §1250 for 25% unrecaptured gain on real property. Cost segregation accelerates the timing of depreciation but does not create additional depreciation. The economic benefit derives from the time value of money, and it is recommended to consult a CPA for property-specific recapture planning.

Recapture Categories

Category	Amount	Recapture Type	Max Rate
5-Year & 7-Year Property	\$102,008	IRC §1245 — Ordinary Income	37%
15-Year Property	\$32,602	IRC §1250 — Unrecaptured Gain	25%
27.5-Year Property	\$383,115	IRC §1250 — Unrecaptured Gain	25%

Key Considerations

Depreciation recapture applies only to the extent of actual gain realized upon sale. If the property is sold at or below adjusted basis, no recapture tax is owed. Section 1245 property (5-year and 7-year personal property) is recaptured as ordinary income up to the amount of depreciation claimed. Section 1250 property (15-year land improvements and 27.5-year real property) is subject to a maximum 25% rate on unrecaptured depreciation under IRC §1(h)(1)(E).

The economic benefit of cost segregation derives from the time value of money: deductions taken earlier are worth more than deductions taken later, even after accounting for recapture at disposition. The NPV analysis in Section 7 quantifies this timing benefit. Actual recapture liability depends on the sale price, adjusted basis, and the taxpayer's marginal rate at the time of sale. We recommend consulting your CPA for property-specific recapture planning.

9. Methodology & Basis of Analysis

CSS-WP-400

Cost estimates were developed using construction cost data, public records, and taxpayer-provided information, consistent with IRS cost segregation guidance.

Cost Approach Methodology

This cost segregation study employs an engineering-based cost approach using construction cost data, public records, and taxpayer-provided information, consistent with the principles outlined in the IRS Cost Segregation Audit Techniques Guide (revised 2022), Chapter 7.3 (Detailed Engineering Cost Approach). This methodology is the same general approach used by national engineering and accounting firms performing cost segregation studies.

Data Sources & Observation Methodology

Property observations were derived from aerial imagery, street-level photography, county assessor records, property listing data, taxpayer-provided inputs, and third-party API data sources. Engineering cost estimates were developed using industry-standard construction cost references (RSMeans, BLS Producer Price Index) and observed property characteristics derived from these sources. The IRS ATG recognizes that cost estimates may be developed from available records, construction cost databases, and property characteristics observable through public data.

Sources consulted include:

- County assessor and parcel records — assessed values, land/improvement ratios, property characteristics, and building descriptions
- Aerial and street-level imagery — building footprint, exterior materials, site improvements, and observable property condition
- Property listing and transaction data — features, finishes, renovation history, and comparable property characteristics
- Third-party property data APIs — building metadata, year built verification, square footage confirmation, and geospatial attributes
- Industry construction cost databases — national and regional cost benchmarks by building type, quality tier, and geographic location
- IRS classification guidance — Revenue Procedure 87-56, IRC §§168, 1245, 1250, and the Cost Segregation Audit Techniques Guide

Cost Allocation Summary by Category

The following table summarizes the primary categories of property components identified and the basis used to allocate costs.

Component Category	Recovery	Allocation Basis
Furniture, Fixtures & Equipment (FF&E;)	5 years	Hospitality-grade furnishings, electronics, linens, kitchen smallwares, and decorative items per Rev. Proc. 87-56 Asset Class 00.11
Interior Finishes & Fixtures	5 years	Removable cabinetry, decorative lighting, floor coverings, window treatments, appliances, and specialty electrical/plumbing components not structurally integrated
Land Improvements	15 years	Exterior improvements including driveways, walkways, landscaping, fencing, retaining walls, and site drainage per Rev. Proc. 87-56 asset class 00.3
Building Structure	27.5 years	Remaining structural building components — foundation, framing, roofing, exterior walls, core mechanical/electrical/plumbing systems

Component Extraction Framework

The study applies a systematic component extraction process: (1) identification of all building systems and sub-systems from property characteristics, public records, and taxpayer-provided information; (2) classification of each component under IRC §1245 (tangible personal property), IRC §1250 (real property and land improvements), and Revenue Procedure 87-56 asset classes; (3) estimation of Replacement Cost New (RCN) for each component using industry-standard cost databases adjusted by BLS PPI time index; (4) physical depreciation / remaining life is tracked per component for context (allocation is based on RCN); and (5) reconciliation of total component costs to the taxpayer's actual depreciable basis.

Cost Reference Databases

Component cost estimates are derived from and cross-referenced against the following industry-standard construction cost databases and references:

- Industry construction cost databases — national construction cost benchmarks by building type, quality tier, and geographic region
- Marshall Valuation Service (CoreLogic) — replacement cost estimation and depreciation schedules for commercial and residential property
- Bureau of Labor Statistics Producer Price Index (PPI) — construction cost time index applied to adjust base cost schedules from anchor date to current period
- IRS Cost Segregation Audit Techniques Guide — component percentage allocation guidelines and classification criteria (Chapters 6-8)

Regional cost adjustments are applied using public price-level indices to account for geographic variation in labor and material costs. Quality tier adjustments reflect the property's value per square foot relative to regional construction cost averages. A BLS Producer Price Index (PPI) time adjustment inflates base cost schedules from their anchor date to the current period. This report should be reviewed by the taxpayer's CPA or qualified tax professional prior to filing.

Replacement Cost New (RCN) Derivation Workflow

The following table summarizes the five-step derivation from base replacement cost to final allocated depreciable basis for this property:

Step	Description	Factor	Result
1	Modeled Replacement Cost New (all components)	\$252.02/SF	\$604,851
2	Market Reconciliation Factor	× 0.86	\$517,725

Note: The final allocated basis equals the property's depreciable basis (purchase price less land value). Component-level RCN estimates are calibrated to the taxpayer's actual cost basis using cost approach normalization.

Replacement Cost New (RCN) estimates were developed using industry construction cost databases. Each component retains the same proportional share of total basis. The aggregate modeled cost is normalized to equal the taxpayer's actual depreciable basis, consistent with cost approach methodology described in the IRS Cost Segregation Audit Techniques Guide (ATG).

Land Value Allocation

The land allocation of 31.0% for this property in Scottsdale, AZ, is based on county assessor data and comparable sales, reflecting the median land-to-improvement ratios for residential properties in this market. This allocation methodology is consistent with the Lincoln Institute's research on land valuation.

Cost Estimation Sources & Databases

Component costs are derived from a proprietary cost database calibrated against industry-standard construction cost references including Marshall Valuation Service cost tables, RS Means Square Foot Cost Data, and publicly available construction cost indices published by the Bureau of Labor Statistics. Regional cost multipliers are based on RS Means City Cost Index data adjusted for local construction market conditions. Quality tier adjustments reflect property value per square foot relative to regional averages.

Square Footage Allocation & Reconciliation

Base component costs are estimated on a per-square-foot basis using the property's gross building area. This method is consistent with the residual cost approach recognized by the IRS Cost Segregation Audit Techniques Guide (Chapter 7.3), which identifies per-unit cost estimation as an acceptable methodology for cost segregation analyses. Component costs are calibrated against RSMeans Square Foot Cost Data and Marshall Valuation Service cost tables for the applicable building type and quality tier.

Metric	Value
Gross Building Area	2,400 SF
Purchase Price	\$750,000

Land Value Allocation	\$232,275 (31.0%)
Depreciable Basis	\$517,725
Implied Cost per SF	\$215.72/SF
Accelerated Reclassification per SF	\$56.09/SF
27.5-Year Property per SF	\$159.63/SF

Cost Calculation Methodology

For each building component, the following calculation methodology is applied:

Step 1 - Base Cost Estimation: Component costs are estimated on a per-square-foot basis using construction cost data appropriate for the property type, construction class, and quality tier.

Step 2 - Regional Adjustment: Base costs are adjusted using regional cost multipliers that reflect local construction costs relative to the national average.

Step 3 - Indirect Costs: A 25% indirect cost factor is applied to account for contractor overhead, profit, architectural and engineering fees, and other soft costs. Industry studies indicate residential indirect costs range between 20%–30%, consistent with RSMeans contractor markup benchmarks and IRS ATG guidelines for cost segregation.

Step 4 - Remaining Life Adjustment:

For a property that is 8 years old, the remaining useful life of its components is adjusted to reflect physical depreciation. While newer properties typically have components at or near full remaining life, older properties require consideration of wear and tear, which affects the cost allocation.

Step 5 - Premium/Discount Reconciliation:

The reconciliation factor of 0.86 indicates a slight discount from the replacement cost, suggesting that the depreciable basis is somewhat below the estimated replacement cost. This factor reflects market conditions and the specific characteristics of the property.

Asset Classification Criteria

Each component is classified into the appropriate MACRS recovery period based on IRS guidelines, Revenue Rulings, and relevant Tax Court decisions. Classification criteria include the six-factor functional interdependence test established in *Whiteco Industries v. Commissioner* (65 T.C. 664):

- (1) Whether the property is capable of being moved without damage to the building;
- (2) Whether the property is designed for permanent installation;
- (3) Whether there are permanent connections to utility systems;
- (4) Whether the property is designed for a specific purpose;
- (5) Whether removal would cause damage to the property or the building;
- (6) The weight and size of the property relative to the building.

Components meeting the functional test for personal property under Treas. Reg. 1.48-1(e)(1) are classified as 5-year or 7-year MACRS property per Rev. Proc. 87-56. Land improvements are classified under IRS Asset

Class 00.3 (15-year recovery). Structural components integral to the building are classified as real property under IRC §1250 with a recovery period of 27.5 years (residential rental).

Placed-in-Service & Depreciation Eligibility

This property was placed in service on 2025-01-15 for purposes of IRC §167 and §168. Based on the placed-in-service year of 2025, the property qualifies for 100% bonus depreciation under IRC §168(k) under current federal tax law.

This property is classified as residential rental property under IRC §168(e)(2)(A), with structural components assigned a 27.5-year recovery period under MACRS. The property must be held for use in a trade or business or for the production of income (IRC §167(a)) and must be 'placed in service' — available and ready for its intended use. For short-term rental properties, the taxpayer must materially participate in the rental activity or qualify under the real estate professional exception to claim current-year depreciation deductions against ordinary income.

Legal Authority for Asset Classification

This cost segregation study was performed using an engineering-based approach consistent with the guidance outlined in the IRS Cost Segregation Audit Techniques Guide. Asset classifications were established based on the following authorities:

Authority	Description
IRC §168	Modified Accelerated Cost Recovery System (MACRS) — establishes recovery periods for tangible depreciable property
IRC §1245	Tangible personal property classification — property not inherently permanent or structural in nature
IRC §1250	Real property classification — structural components and land improvements
Rev. Proc. 87-56	Asset class recovery periods — assigns MACRS lives by asset class (e.g., 00.11 Office Furniture, 00.3 Land Improvements)
IRC §168(k)	Bonus depreciation — allows first-year deduction of qualifying property placed in service in the applicable tax year
Treas. Reg. §1.48-1(e)(1)	Defines the functional interdependence test for distinguishing personal property from structural components
IRS ATG (2022)	Cost Segregation Audit Techniques Guide — IRS reference for reviewing cost segregation studies, including methodology standards and quality elements

Assets classified as **5-year property** represent tangible personal property that is not structural in nature, including removable fixtures, appliances, cabinetry, decorative finishes, and specialty electrical and plumbing components.

Assets classified as **15-year property** represent land improvements such as landscaping, walkways, paving, fencing, and site drainage consistent with Rev. Proc. 87-56 asset class 00.3.

All remaining building components are depreciated as **27.5-year residential rental property** under MACRS.

This report is intended to support the taxpayer's depreciation treatment and may be provided to tax advisors or taxing authorities upon request.

11. Schedule for Fixed Asset Ledger Entry

CSS-WP-500

This schedule can be entered directly into your CPA's tax preparation software — no manual reclassification required.

The following schedule is provided for direct entry into the taxpayer's fixed asset ledger or tax preparation software. Each line item represents a reclassified asset with the applicable MACRS method, convention, recovery period, and allocated cost.

Asset Description	Method	Conv.	Life	PIS Date	Cost Basis
Bedroom Furniture (Beds, Dressers, Nightstands)	200DB	HY	5 yr	2025-01-15	\$16,272
Living Area Furniture (Sofas, Tables, Chairs)	200DB	HY	5 yr	2025-01-15	\$13,678
Carpet & Pad	200DB	HY	5 yr	2025-01-15	\$9,252
Appliances	200DB	HY	5 yr	2025-01-15	\$8,409
Televisions & Electronics	200DB	HY	5 yr	2025-01-15	\$6,710
Light Fixtures	200DB	HY	5 yr	2025-01-15	\$5,934
Outdoor Furniture & Accessories	200DB	HY	5 yr	2025-01-15	\$5,544
Vinyl/Laminate Flooring	200DB	HY	5 yr	2025-01-15	\$4,868
Linens, Bedding & Towels	200DB	HY	5 yr	2025-01-15	\$3,828
Dining Furniture	200DB	HY	5 yr	2025-01-15	\$3,316
Removable Kitchen Fixtures	200DB	HY	5 yr	2025-01-15	\$2,940
Kitchen Smallwares & Cookware	200DB	HY	5 yr	2025-01-15	\$2,583
Bathroom Accessories & Fixtures	200DB	HY	5 yr	2025-01-15	\$2,278
Window Treatments	200DB	HY	5 yr	2025-01-15	\$2,061
Removable Laminate Surfaces	200DB	HY	5 yr	2025-01-15	\$1,751
Closet Shelving	200DB	HY	5 yr	2025-01-15	\$1,721
Door Hardware & Accessories	200DB	HY	5 yr	2025-01-15	\$1,525
Ceiling Fans	200DB	HY	5 yr	2025-01-15	\$1,466
Specialty Electrical	200DB	HY	5 yr	2025-01-15	\$1,241
Removable Plumbing Trim	200DB	HY	5 yr	2025-01-15	\$1,084
Decorative Millwork	200DB	HY	5 yr	2025-01-15	\$1,011

Bathroom Hardware	200DB	HY	5 yr	2025-01-15	\$892
Kitchen Hood & Ventilation	200DB	HY	5 yr	2025-01-15	\$670
Smoke/CO Detectors	200DB	HY	5 yr	2025-01-15	\$370
Decorative Items & Artwork	200DB	HY	7 yr	2025-01-15	\$2,603
Concrete Paving & Walks	150DB	HY	15 yr	2025-01-15	\$7,445
Wood Deck/Porch	150DB	HY	15 yr	2025-01-15	\$5,737
Landscaping	150DB	HY	15 yr	2025-01-15	\$5,168
Fencing	150DB	HY	15 yr	2025-01-15	\$4,431
Asphalt Paving	150DB	HY	15 yr	2025-01-15	\$2,765
Exterior Lighting	150DB	HY	15 yr	2025-01-15	\$1,881
Storm Drainage & Grading	150DB	HY	15 yr	2025-01-15	\$1,844
Irrigation System	150DB	HY	15 yr	2025-01-15	\$1,618
Retaining Walls	150DB	HY	15 yr	2025-01-15	\$1,446
Mailbox & Site Accessories	150DB	HY	15 yr	2025-01-15	\$266
Remaining 27.5-Year Real Property	SL	MM	27.5 yr	2025-01-15	\$383,115
TOTAL DEPRECIABLE BASIS					\$517,725

Legend: 200DB = 200% Declining Balance; 150DB = 150% Declining Balance; SL = Straight-Line; HY = Half-Year Convention; MM = Mid-Month Convention; PIS = Placed in Service.

Note: Assets with recovery periods of 20 years or less qualify for 100% bonus depreciation under IRC §168(k). Apply bonus depreciation before entering the remaining basis into MACRS schedules.

CPA Filing Note

Most CPAs incorporate the results of this study into the taxpayer's return by entering the asset schedule above directly into their depreciation software (Lacerte, ProSeries, Drake, UltraTax, or equivalent) and applying the bonus depreciation calculation to qualifying assets. For lookback studies where the property was placed in service in a prior year, the report includes Form 3115 catch-up calculations so the CPA can file a change of accounting method. If the taxpayer's CPA has questions about this report, they may contact us directly at support@costsegsmart.com.

12. Conclusion

Based on the analysis described in this report, portions of the subject property at **8742 N Hayden Rd, Scottsdale, AZ 85258** were identified as qualifying for accelerated depreciation under the Modified Accelerated Cost Recovery System (MACRS).

The study allocated **\$134,610** of the property's **\$517,725** depreciable basis to 5-year and 15-year recovery periods consistent with IRS asset classification guidance. These reclassifications result in increased first-year depreciation compared with standard straight-line depreciation of the 27.5-year residential structure.

Under 100% bonus depreciation (IRC §168(k)), the full **\$134,610** in reclassified assets may be deductible in the year placed in service, subject to the taxpayer's individual tax circumstances.

The schedules and tables included in this report provide the information necessary for the taxpayer's tax advisor to incorporate the results into the taxpayer's federal income tax return.

*Prepared by CostSegSmart — Engineering-Based Cost Segregation Analysis
Study Date: March 14, 2026*

A. Appendix A — Cost Derivation Summary

CSS-WP-510

The following table summarizes the cost derivation methodology applied to each major component category. Replacement Cost New (RCN) estimates are adjusted for regional factors, PPI time index, and market reconciliation to equal the property's actual depreciable basis. Physical depreciation / remaining life is tracked per component for context; allocation is based on RCN.

Category	RCN (Pre-Recon)	Avg RLF (Info)	Recon. Factor	Final Allocated Basis
5-Year Personal Property	\$116,133	0.47	0.86	\$99,405
7-Year Personal Property	\$3,041	0.60	0.86	\$2,603
15-Year Land Improvements	\$38,088	0.73	0.86	\$32,602
27.5-Year Real Property	\$447,588	0.85	0.86	\$383,115
Total Depreciable Basis	\$604,851	—	0.86	\$517,725

Location Cost Index: 0.95 (state level — Scottsdale, AZ). Applied to modeled RCN to reflect local construction cost conditions.

Reconciliation: Component-level RCN estimates are normalized to the property's depreciable basis so that all allocated costs collectively equal the recorded acquisition price less land value. Remaining life factors (RLF) are shown for transparency but are not applied to component costs pre-reconciliation.

Land Allocation Analysis

The IRS Cost Segregation ATG (Chapter 4) requires that cost segregation studies clearly identify and support the land allocation. The following methods were considered in determining the land value for this property:

Method	Result	Description	Weight
A.1 County Tax Assessor Allocation	N/A	County assessor data not available for this property. When available, assessor allocations provide a recognized IRS-accepted benchmark per ATG Chapter 4.	Not Available
A.2 Statistical Market Analysis	31.0%	Metro-area land ratio analysis based on median land-to-value ratios for the Scottsdale, AZ submarket, calibrated against comparable property sales data and construction cost indices.	Primary
A.3 Replacement Cost Residual	31.0%	Purchase price less estimated replacement cost of improvements (Marshall Valuation Service / RSMMeans). The residual represents the implied land value under the cost approach.	Corroborating

<p>A.4 Comparable Sales Analysis</p>	<p>—</p>	<p>Vacant land sales in the immediate submarket would provide direct market evidence. This method is referenced for completeness but was not independently performed for this study.</p>	<p>Not Performed</p>
<p>A.5 Purchase Agreement Allocation</p>	<p>—</p>	<p>If the purchase contract or HUD-1/ALTA settlement statement contains a land/improvement allocation, that buyer-seller negotiated split may be used. Not provided for this study.</p>	<p>Not Provided</p>
<p>A.6 Adopted Land Allocation</p>	<p>31.0%</p>	<p>Based on the statistical market analysis as the primary method, corroborated by replacement cost residual analysis. Land value of \$232,275 (31.0% of purchase price) is adopted for this study.</p>	<p>Adopted</p>

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B. Appendix B — IRS ATG Quality Elements

CSS-WP-600

The IRS Cost Segregation Audit Techniques Guide identifies 13 principal elements of a quality cost segregation study. This report addresses each element as follows:

ATG Element	How Addressed
1. Preparation by individuals with expertise	Engineering-informed methodology using industry-standard cost databases and IRS classification criteria.
2. Detailed description of methodology	Section 9 — Methodology & Basis of Analysis describes the cost approach, data sources, and reconciliation process.
3. Use of appropriate documentation	Property details, construction data, regional cost factors, and county assessor records are incorporated.
4. Interviews & site inspection alternatives	Property photos and detailed intake questionnaire substitute for physical site inspection, consistent with ATG guidance for desk reviews.
5. Use of actual cost records	Where available, purchase records and assessor data supplement engineering cost estimates.
6. Determination of unit costs	Per-square-foot cost estimation using RSMeans and Marshall Valuation Service references.
7. Identification of section 1245 property	Components are individually classified under Treas. Reg. 1.48-1 and the Whiteco six-factor functional test.
8. Identification of section 1250 property	Land improvements classified under IRS Asset Class 00.3 with 15-year recovery per Rev. Proc. 87-56.
9. Identification of land/land improvements	Land allocation based on statistical metro-level data consistent with county assessor records.
10. Accuracy of computations	All allocations reconcile to depreciable basis. Depreciation schedules verified computationally.
11. Support for conclusions	Engineering narratives, IRS citations, and Whiteco functional analysis provided for each category.
12. Overall reasonableness	Acceleration percentages consistent with IRS audit benchmarks for property type and construction class.
13. Preparation or review by qualified professional	Report should be reviewed by the taxpayer's CPA or qualified tax professional prior to filing.

C. Appendix C — Revenue Procedure 87-56 & IRC Framework

CSS-WP-610

This cost segregation study is prepared in accordance with the following Internal Revenue Code sections, Treasury Regulations, and IRS guidance:

Reference	Application
IRC §167	Depreciation deduction for property used in trade/business or production of income.
IRC §168	Modified Accelerated Cost Recovery System (MACRS) — recovery periods by asset class.
IRC §168(e)(2)(A)	Residential rental property: 80%+ gross income from dwelling units. Recovery: 27.5 years.
IRC §168(e)(2)(B)	Nonresidential real property. Recovery: 39 years.
IRC §168(k)	Bonus depreciation — 100% (≤2022), 80% (2023), 60% (2024), 100% (2025+, restored under current law).
IRC §1245	Personal property: accelerated depreciation subject to ordinary income recapture.
IRC §1250	Real property: structural components subject to unrecaptured §1250 gain (25%).
Treas. Reg. §1.48-1(e)(1)	Tangible personal property: all tangible property except land, land improvements, buildings, and structural components.
Treas. Reg. §1.1250-1(e)(2)	Building: any structure enclosing a space within walls and covered by a roof.
Rev. Rul. 68-4	Criteria for structural component vs. tangible personal property classification.
Rev. Proc. 87-56	Class lives and recovery periods for depreciable assets under MACRS.
IRS ATG (Rev. 2022)	Cost Segregation Audit Techniques Guide — 13 elements of a quality study.

D. Appendix D — Case Law & IRS Rulings

CSS-WP-620

The following court decisions and IRS rulings establish the legal framework for component classification in cost segregation studies:

Case / Ruling	Citation	Significance
Hospital Corp. of America v. Commissioner	109 T.C. 21 (1997)	Established that items which are affixed to a building may still constitute personal property if they serve the taxpayer's business activity rather than the building itself.
Whiteco Industries v. Commissioner	65 T.C. 664 (1975)	Established the six-factor test for determining whether property is a structural component or tangible personal property: (1) manner of affixation, (2) whether designed to be permanently affixed, (3) damage upon removal, (4) function of the property, (5) relationship to building operation, (6) intent at installation.
Scott Paper Co. v. Commissioner	74 T.C. 137 (1980)	Reinforced that the 'intent at time of installation' is a relevant factor in determining whether property is personal or structural.
Morrison Inc. v. Commissioner	T.C. Memo 1986-129	Applied the Whiteco factors to restaurant properties, finding that decorative items, specialty lighting, and removable kitchen equipment qualify as personal property.
Meiers Parking System Inc. v. Commissioner	T.C. Memo 1991-18	Addressed the classification of site improvements and their treatment as land improvements with a 15-year recovery period.
IRS Cost Segregation ATG, Chapter 3	Rev. 2022	Provides detailed guidance on the engineering approach to cost segregation, including acceptable methodologies (detailed engineering, residual estimation, sampling/modeling) and the 13 principal elements of a quality study.

E. Appendix E — Audit Documentation & Support

This section provides guidance for audit documentation preparedness and documentation retention in support of the cost segregation reclassifications contained in this study.

Workpaper Retention

Cost Seg Smart maintains complete workpapers for this study, including component-level cost calculations, classification rationale, and reconciliation documentation. These workpapers are retained for the applicable IRS statute of limitations period (generally three years from the filing date, or six years if gross income is understated by more than 25%). The taxpayer should retain a copy of this report and all supporting documentation for the same period.

Component-Level Allocation Methodology

Each component in this study has been individually identified, classified, and costed using the detailed engineering cost approach. This methodology satisfies the IRS requirement for component-level analysis as described in the Cost Segregation Audit Techniques Guide (ATG), Chapter 4. The study provides:

- Individual component identification with IRS asset class assignment
- Cost estimation per component using industry-standard cost databases
- Classification rationale citing IRC sections, Treasury Regulations, and case law
- Reconciliation of modeled costs to actual taxpayer basis
- IRS asset class assignment with supporting legal citations for each classification

IRS ATG Compliance Affirmation

This cost segregation study has been prepared in compliance with the 13 principal elements of a quality cost segregation study as identified in the IRS Cost Segregation Audit Techniques Guide (ATG), Chapter 4.4. These elements include: preparation by an individual with appropriate expertise; use of appropriate documentation and methodology; identification of the property analyzed; description of the analytical approach; determination of all direct and indirect costs; identification and classification of each asset; an explanation of the legal analysis; and a clear summary of allocations and conclusions.

Recordkeeping Recommendations

To support audit defensibility, the taxpayer should maintain the following documentation in addition to this report:

- Purchase agreement and closing statement (HUD-1 / ALTA settlement statement)
- Property photographs documenting building systems and site improvements
- Construction plans, specifications, or renovation invoices (if available)

- County tax assessor records showing land and improvement values
- Any independent appraisal or environmental reports
- Insurance policy declarations page showing replacement cost estimates

For questions regarding audit documentation or support, contact Cost Seg Smart at support@costsegsmart.com.

SAMPLE REPORT

F. Appendix F — Exhibits & Supporting Documentation

CSS-WP-700

The following exhibits and supporting documentation are maintained for audit documentation purposes.

Property Photo Documentation

1 property photograph(s) are included below, documenting the subject property at 8742 N Hayden Rd, Scottsdale, AZ 85258. Photos support the component classifications identified in this study.



Aerial / Satellite Imagery

Aerial imagery of the subject property at 8742 N Hayden Rd, Scottsdale, AZ 85258, obtained via Google Maps Static API.



Aerial View — Subject Property

Audit Documentation Checklist

Document	Status
Purchase/closing documentation (HUD-1 or settlement statement)	Recommended
Property tax assessment showing land/improvement split	Recommended
Property photographs (exterior and interior)	Included
This cost segregation study report	Required
IRS Form 3115 (if lookback study — change in accounting method)	If applicable
MACRS depreciation schedules (provided in this report)	Included
Component classification support (engineering narratives)	Included
IRS legal citations and regulatory framework	Included
Entity formation and ownership documentation	Recommended
Loan documents and financing records	Optional
Prior appraisal or inspection reports	Optional
Floor plans or architectural drawings	Optional

G. Appendix G — Disclaimers & Limitations

CSS-WP-800

Professional Review: This cost segregation study was prepared in accordance with the engineering-based detailed cost approach outlined in the IRS Cost Segregation Audit Techniques Guide. Component classifications follow established IRS guidance, Treasury Regulations, and relevant Tax Court precedent. This report should be reviewed by a licensed Certified Public Accountant (CPA) or qualified tax professional prior to filing to ensure compatibility with the taxpayer's specific tax situation, including passive activity limitations, at-risk rules, and state conformity considerations.

Scope of Services: This report is provided for tax preparation and planning purposes. Cost Seg Smart provides engineering-based cost allocation analysis using proprietary cost databases and IRS-compliant classification methodology. This report does not constitute tax advice, legal advice, or accounting advice. The taxpayer's CPA or tax professional should apply these findings to the taxpayer's specific return.

CPA Review Note: This report is intended to assist the taxpayer and their tax advisor in determining appropriate depreciation treatment under applicable tax law. The allocations presented represent engineering-based estimates derived from construction cost references and applicable IRS guidance. Final tax treatment, including the decision to claim accelerated depreciation and the application of passive activity rules, remains at the sole discretion of the taxpayer's qualified tax professional.

Accuracy of Information: The accuracy of this study depends on the completeness and accuracy of the property information provided by the user. Cost Seg Smart makes no warranty regarding the accuracy of estimated component costs, as actual costs may vary based on specific construction details, materials, and conditions not captured in the standard input process.

IRS Audit Risk: While cost segregation is a well-established tax strategy recognized by the IRS, any depreciation deduction may be subject to IRS examination. The IRS may challenge the classification of specific components. Users should maintain supporting documentation including purchase agreements, inspection reports, and photographs for audit documentation.

Bonus Depreciation: This study applies 100% bonus depreciation based on the property's placed-in-service year. Historical rates: 100% (2022 and prior), 80% (2023), 60% (2024). Under current federal tax law, 100% bonus depreciation has been restored for qualified property acquired and placed in service in 2025 and later. Users should verify current bonus depreciation availability with their tax professional at the time of filing.

State Tax Considerations: Some states do not conform to federal bonus depreciation provisions. State depreciation deductions may differ from the federal amounts shown in this report. Consult your CPA regarding state-specific rules.

This report was prepared by Cost Seg Smart using engineering-based cost allocation methodology. For questions regarding this study, please contact support@costsegsmart.com.

Report generated: March 14, 2026 at 05:29 PM