KBKG Repair vs. Capitalization: Improvement Decision Tree - Final Regulations

Considering the appropriate Unit of Property (UOP), does the expenditure:

(Last Updated 3-20-2015)

Correct a material defect/condition that existed before acquisition?

Possibly

Materially increase the capacity, productivity, efficiency, quality, strength, or output?

Possibly

Is a material addition?

Possibly

Change the use of the property from its intended use when it was placed in service?

Possibly

Rebuild the UOP to "like new" condition after the end of its class life (ADS life)?

Possibly

Replace a Major Component or Substantial Structural Part?

Possibly

Return UOP to ordinary operating condition after deteriorated (in a state of disrepair)?

Possibly

Result in a basis adjustment or loss deduction for component removed?

Possibly

Was the expenditure "incurred by reason of an improvement" or did it directly benefit an improvement?

Possibly

Even if the defect was not known at the time of acquisition: Answer = YES

Particular Event - compare condition of UOP just before event vs. after expenditure

What do you compare against to see if it's a betterment?

Normal Wear - compare condition just after expenditure vs. last time it was updated or when placed in service

Even if the defect was not known at the time of acquisition: Answer = YES

If using improved but comparable part only due to technology advancing (i.e. impractical to use old type) Answer = NO

If there was physical enlargement, expansion, or extension: Answer = YES

Example 1. Office is converted to showroom: Answer = YES

Example 2. Three retail spaces converted to one retail space: Answer = NO

If brought to remanufactured or similar status under federal guidelines or manufacturer original specs. Answer = NO

If replacing a large physical portion of UOP. Answer = YES (Generally, replacing < 33%: Answer = NO)

If replacing part that performs discrete & critical function in operation of UOP (ex. such as a central furnace): Answer = YES

If minor part breaks during normal use & causes UOP to temporarily cease to function: Answer = NO

Based on "facts and circumstances"

Replacing only incidental component, even if it affects function of UOP (i.e. such as roof shingles or HVAC switch): Answer = NO

If basis adjustment due to casualty loss, sale, or exchange of component. Answer = YES.

Was it done in conjunction or at the same time as an improvement to a UOP?

Was the cost necessary or critical to complete the associated improvement.

Possible Repair Expense

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KBKG Building Unit of Property & Major Components Chart (updated 05-16-17)

This chart was created to help users identify building systems & typical "major components" in real estate assets. Replacing a major component is a capital expenditure, while replacing an incidental component can be expensed.

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<tbody>
<tr>
<td>Roof System (membrane, insulation &amp; structural supports)</td>
<td>Landscaping incl: shrubs, trees, ground cover, lawn, irrigation</td>
<td>Heating System (boilers, furnaces, radiators)</td>
<td>Service &amp; Distribution (panel boards, transformers, switch gear, metering)</td>
<td>Plumbing fixtures (sinks, toilets, tubs etc.)</td>
<td>Sprinkler System (piping, heads, pumps)</td>
<td>Building security alarms (detectors, sirens, wiring)</td>
<td>Gas piping incl. to/from property line &amp; other bldgs.</td>
<td>Stair &amp; Handrail</td>
<td>Elevator Car</td>
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<td>Foundation</td>
<td>Storm drainage incl: wells, catch basins, piping, lift stations</td>
<td>Cooling System (compressors, chillers, cooling towers)</td>
<td>Lighting (interior &amp; exterior building mounted)</td>
<td>Wastewater System (drains, waste &amp; vent piping)</td>
<td>Fire Alarms (detection &amp; warning devices, controls)</td>
<td>Fire Escapes</td>
<td>Stair &amp; Handrail</td>
<td>Drive System (motors, truss, controls)</td>
<td>Drive System (motors, lift, controls)</td>
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<td>Other structural load bearing elements, inc: stairs</td>
<td>Site lighting (pole lights, bollard lights, up lights, wiring)</td>
<td>Site Electrical Utilities</td>
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<td>Domestic Water (supply piping and fittings)</td>
<td>Exit lighting &amp; signage</td>
<td>Extinguishers &amp; hoses</td>
<td>Suspension system (counterweights, framing, guide rails)</td>
<td>Elevator Car</td>
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<td>Exterior Wall System</td>
<td>Site Structures (gazebo, carport, monument signs)</td>
<td>Branch Wiring (outlets, conduit, wire, devices etc.)</td>
<td>Electrical System</td>
<td>Water Heater</td>
<td>Site Piping Utilities</td>
<td>Building access &amp; control System</td>
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<td>Elevator Car</td>
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<td>Ceilings</td>
<td>Paving (roads, driveway, parking areas, sidewalks, curbing)</td>
<td>Emergency Power Systems</td>
<td>HVAC System</td>
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* Building unit of property (UOP) rules apply to each building structure located on a single property.

** Building system components with a different tax life are separate units of property. For example, a cost segregation study separating HVAC into 5 year & 39 year categories for a restaurant creates two separate HVAC units of property.

**Lessee of Building**
Must apply the same units of property above but only to the portion of the building being leased.

**Personal Property**
UOP are parts that are "functionally interdependent" i.e. placing one part in service is dependent on placing the other part in service.

**Plant Property**
UOP is each component that performs a discrete and critical function. Generally each piece of machinery or equipment purchased separately.

**Network Assets**
UOP is determined by taxpayers particular facts

**Definitions**
**Plant Property**
Machinery & Equipment used to perform an industrial process such as manufacturing, generation, warehousing, distribution, automated materials handling, or other similar activities

**Network Assets**
Railroad track, oil & gas pipelines, water & sewage pipelines, power transmission & distribution lines, telephone & cable lines; -- owned or leased by taxpayers in each of those respective industries.

**Major Component**
Part or combination of parts that performs a discrete and critical function in the operation of the unit of property

**Incidental Component**
Relatively small, inexpensive, or minor part that performs a discrete and critical function for the UOP. Generally, not capitalized because of it’s size, cost, or significance.

Examples: Asphalt sealer, HVAC thermostats, HVAC fan coils, HVAC registers, Plumbing valves and fittings, lighting or power control devices, hardware, escalator handrail, paint, roof shingles.

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