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Client Information Bulletin
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Maximizing Tax Benefits of Installment Sales

Special tax rules apply to real estate gains

If you are trying to sell appreciated commercial real estate in today's market, you may have to compromise. For instance, if you refuse to budge on price, you might have to make other reasonable concessions, such as agreeing to an installment sale for a buyer with limited liquidity. As the name implies, the buyer pays you in a series of installments instead of providing all the cash up front.

This could actually be beneficial from a tax perspective if payments are made over two years or more. In that case, not only do you defer some of the tax due on the appreciation in value, but you may reduce your tax liability.

Background: With an installment sale of real estate, you generally are in line for preferential tax treatment. First, the gain is generally taxed as a long-term gain (i.e., you have owned the property for longer than one year), resulting in a maximum capital gain rate of 15%, or 20% if you are in the top ordinary income tax bracket. Even if you are also liable for the 3.8% Medicare surtax on net investment income, the maximum combined tax rate at the federal level is limited to 23.8%.

Second, only a portion of your gain is taxable in the year of the sale. The remainder is taxable in the years in which payments are received. By spreading out the tax over several years, you might pay less tax overall because more of the capital gain may be taxed at the 15% rate.

The taxable portion of each payment is based on the "gross profit ratio." Gross profit ratio is determined by dividing the gross profit from the real estate sale by the price.

Example: Suppose you acquired commercial real estate 10 years ago that has an adjusted basis of $600,000. You agree to sell the property in 2015 for $1.5 million in three annual installments of $500,000 each. Because your gross profit is $900,000 ($1.5 million – $600,000), the taxable percentage of each installment received is 60% ($900,000 ÷ $1.5 million). When you report the sale on your 2015 tax return, you have to pay tax on only $300,000 of gain (60% of $500,000).

Any depreciation claimed on the property must be recaptured as ordinary income to the extent that it exceeds the amount allowed under the straight-line method. The adjusted basis of the property is increased by the amount of recaptured income, thus decreasing the gain realized in future years.

But watch out for a little-known tax trap. If the sale price of your property (other than farm property or personal property) exceeds $150,000, interest must be paid on the deferred tax to the extent

Inside

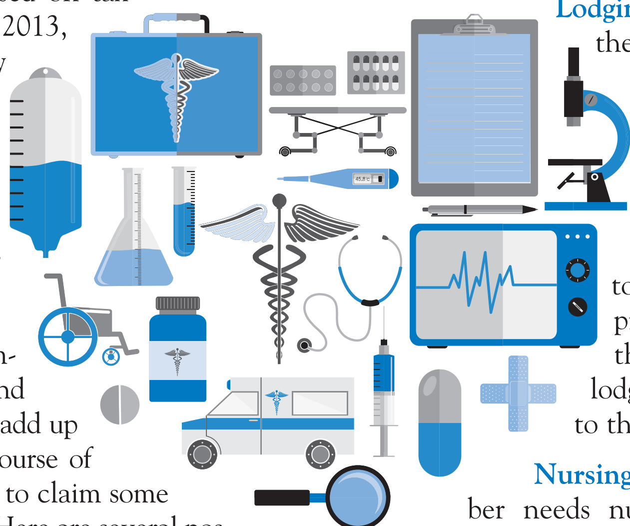
that your outstanding installment obligations exceed the $5 million mark.

Finally, if it suits your purposes, you can elect to forgo installment sale treatment when you file your 2015 tax return. This could be advantageous if 2015 is an unusually low-income year for you. Consult your tax advisers before arranging an installment sale of real estate or making any tax return decisions.

How to Clear the Medical Deduction Hurdle

Don't overlook common deductible expenses

In the past, it was difficult to qualify for medical expense deductions. Now, some pundits would say that it is "nearly impossible." Based on tax law changes that took effect in 2013, most taxpayers can deduct only unreimbursed expenses in excess of 10% of their adjusted gross income (AGI), up from 7.5% of AGI under prior law. For taxpayers who are aged 65 or older, the threshold remains at 7.5% of AGI, but only through 2016.



Nevertheless, you should not completely give up hope. Medical and dental expenses for the family can add up to a surprising amount over the course of the year. And you may be entitled to claim some expenses you had not counted on. Here are several possibilities you could easily overlook.

Prescription drugs: Amounts paid for prescription drugs and insulin are considered to be deductible medical expenses. But over-the-counter medications are generally not deductible.

Transportation costs: The deductible amount is not limited to the actual cost of the physician's or hospital's services. You may also deduct the cost of traveling to and from the treatment (even if similar treatment is available nearby). If you travel by car, you can either deduct your actual automobile expenses or a flat rate established annually by the IRS (23 cents per mile in 2015). Although the flat rate method is more convenient, you may come out ahead by keeping track of your actual expenses.

Lodging costs: You can also deduct the cost of staying in a hotel or motel while you receive medical care away from home. However, the accommodations cannot be "lavish or extravagant." The deductible amount for lodging is limited to $50 per day. If a companion's presence on the trip is required, the cost of the companion's lodging is also deductible (subject to the $50-per-day limit).

Nursing care: If you or a family member needs nursing services in the home, the cost of such services is a deductible medical expense. The medical care does not have to be provided by a registered or trained nurse. In other words, you can pay someone else (e.g., another family member) to provide the care and deduct the expense.

Insurance: Medical insurance premiums paid with after-tax income count toward the deduction. This includes the cost of long-term care insurance up to certain limits based on your age.

Capital improvements: You can deduct the cost of a home improvement if the improvement is made for a medical reason. For instance, the cost of installing central air conditioning to alleviate a child's asthma is deductible. The amount eligible for the deduction equals the cost above the increase in value of your home. **Side benefit:** The cost of maintaining and operating the improvement also qualifies for the deduction.

This is just an overview of several common expenses that may qualify for the medical deduction. There is a long list of more unusual expenses that have been approved by the IRS or the courts. These costs may push you over the threshold for deducting medical expenses in 2015.

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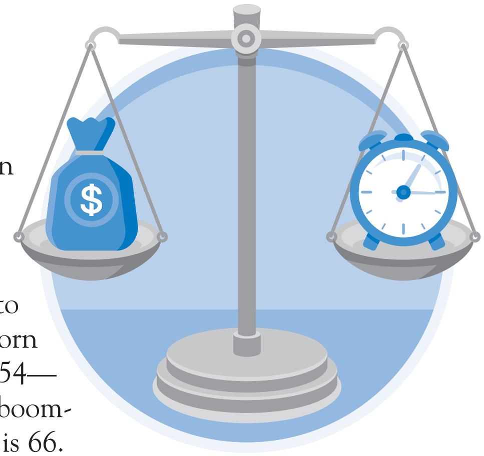
When to Take Social Security Benefits

Difficult decision as retirement nears



If you are approaching retirement, one of the key decisions you will face is when to begin receiving Social Security benefits. It is not an easy call, and the answer usually depends on your personal circumstances. Keeping that in mind, here is a brief summary of the rules provided by the Social Security Administration (SSA).

Essentially, there are three basic methods to consider: (1) early retirement, (2) normal or "full" retirement, or (3) late retirement. We have provided a brief description of each one.

1. Early retirement: You are eligible to begin receiving Social Security retiree benefits as early as age 62. However, you will receive a reduced benefit if you retire before the normal age for receiving full benefits. For example, if you retire at age 62, your benefit will be about 25% lower than what it would be if you wait until you reach your full retirement age.

2. Normal retirement: The age at which you can begin receiving full retirement benefits depends on when you were born. If you were born in 1948 or earlier, you are already eligible for full Social Security benefits. If you were born between 1943 and 1960, the age for receiving full retirement benefits gradually increases to age 67. For those born between 1943 and 1954—including many baby boomers—the "magic age" is 66.

3. Late retirement: You may choose to keep working beyond the age to receive full retirement benefits or delay your application for retirement benefits. Or you may not have a real choice if you need the income from your salary. In any event, consider the following points:

♦ Each additional year you work adds another year of earnings to your Social Security record. Higher lifetime earnings may provide greater benefits to you in retirement.

♦ Your benefit will increase automatically by a certain percentage from the time you reach your full retirement age until you start receiving your benefits or until you reach age 70. The percentage varies depending on your year of birth.

♦ In addition, your decision may be complicated if you expect to claim benefits based on your spouse's earning record. Typically, a spouse who has not worked—or one who has had low earnings—may receive up to one-half of the other spouse's full benefit. If you are eligible to receive both your own retirement benefits and spousal benefits, your own benefits are paid out first. However, if your benefits as a spouse would exceed your own retirement benefits, you may receive a combination of benefits equaling the higher benefit.

Once you have reached your full retirement age, you may choose to receive only your spouse's benefits. In that case, you will continue accruing delayed retirement credits on your own Social Security record. Then you may file for benefits at a later date, up to age 70, and receive a higher monthly benefit based on the delayed retirement credits.

Last, but not least: Other special rules may apply for widows and widowers, divorced spouses, and those entitled to receive disability benefits. You can find more information on these topics by visiting the SSA Web site at www.ssa.gov. Finally, do not hesitate to consult your professional advisers before you make a determination as to when to begin benefits.

All Aboard for Retraining

Are your employees doing a good job with all the tools at their disposal? Don't assume that a trained employee is a productive employee. Due to changes, especially those involving technology, you might embark on a retraining program.

It is important to treat retraining as a reward, not a punishment. This will help employees sharpen their skills. If you take a positive approach, your employees will be more likely to embrace new ways of doing things.

Seven Ways to Build a Corporate Culture

Practical steps for workplace improvement

Does your business maintain a favorable working environment? This could mean the difference between a successful company that continues to grow and a struggling enterprise that weighs itself down. Of course, building a winning corporate culture is easier said than done, but here are seven steps that may push you in the right direction.

1. Establish your identity. Who are you and what do you represent? This is your company, and you are the driving force behind it, so the culture should be a reflection of your personality. For instance, if you project a "work hard, play hard" mentality, this will likely set the tone for the rest of the workplace. On the other hand, if you have a low-key personality, your business may adopt a relaxed atmosphere.

2. Learn from both the good and the bad. Undoubtedly, you have worked at other places with positive influences and some with negative influences. Draw lessons from these experiences to incorporate the positives into your own structure while eliminating the negatives. Think about what cultivated or deterred success.

3. Find complementary workers. This does not mean you should only hire people who are exactly like you. In fact, you might go the other way and find employees who are the opposite of your personality to give your company more balance. Identify your weaknesses, and go from there. As an example, if you are not good at crunching numbers, your right-hand person should be.

4. Open the lines of communication. As you begin to develop the corporate culture, talk to your employees. Give people a platform to express their opinions. They may provide valuable insights that you can utilize or fine-tune according to your needs.

5. Have fun while you are working. If work is completely tedious, it will likely have a dampening effect on productivity. Of course, some businesses have more leeway than others, but there are various ways to engage employees that are not strictly "work." For example, a company picnic featuring contests or a group expedition to a restaurant can be conducive to morale-building.

6. Emphasize teamwork. Your corporate culture should improve if you make it clear that you are "all in it together," rather than just being a group of individuals. It will make it easier for employees to embrace your vision for the company if they feel they are a part of the team. What's more, if you hold events where spouses and significant others are included, loyalty will grow.

7. Reinforce the prior steps. Building a better corporate culture is not a one-time event. It takes place over time, and reinforcement is often needed. Keep your eye on the prize throughout the entire year.

Of course, your corporate culture will continue to evolve as workers come and go, and you adapt to those changes as well. But building a solid foundation in the first place is essential to the process.

Facts and Figures

Timely points of particular interest

➡**Detective Work**—Generally, payments to compensate a worker are taxable, unless the payment is attributable to personal injury or sickness. **New case:** A retired Los Angeles police detective received vacation and sick time pay while on temporary disability leave. He argued that this amount was exempt from tax under a workers' compensation law. But the Tax Court would not characterize it as payment for injury or illness.

➡**Return Policies**—Do you have a return policy for goods that are purchased from your company? If you have opted to implement such a policy, make sure it is clear and understandable by consumers. Whenever possible, be specific (e.g., goods must be returned within 10 days). Avoid any inconsistencies such as the imposition of varying terms at different business locations.