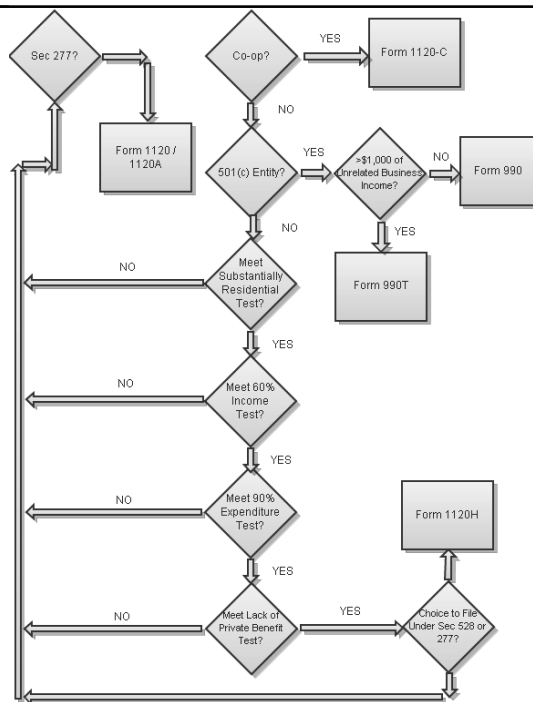


Fundamentals of Preparing a Tax Return for Associations

John M. Barbery, CPA
Barbery & Associates, CPA, Inc.





Forms

- 1120H – Entity taxed under Section 528. Tax rate is flat 30% (32% for timeshares). Must be filed timely. Election to file is binding.
- 1120 (1120-A) – Entity taxed under Section 277. Uses corporate tax rate schedule.
- 990 – A few HOA's as defined by Sec 501(c) may qualify as tax exempt and may file Form 990



Types of Associations

- Condominium Management Associations – built as homes for individuals
- Residential Real Estate Management Associations – built as homes for individuals
- Timeshare Associations – members hold rights to use or ownership interests in real property



Section 528

- Allows filing of Form 1120H, provided specific requirements are met.
- Income and expenses are classified as either exempt or non-exempt
- Flat tax rate of 30% or 32% if timeshare




Requirements for Section 528

- Substantially Residential Test – at least 85% of units must be used as residences. (85% of sq. ft for condos; 85% of lots zoned residential for HOA's)
- 60% Income Test – 60% of gross income must consist of exempt function income
- 90% Expenditure Test – 90% of expenses must be qualifying expenses
- Lack of Private Benefit – No member may profit from net earnings

Exempt v. Non-Exempt Function Income

Exempt Function Income	Non-Exempt Function Income
<p>Must pass four tests to qualify as exempt:</p> <ul style="list-style-type: none"> ➤ Source Test – Amounts received must be for membership assessments from owners of residential units. ➤ Nature Test – Amounts paid must be based solely on their membership in the association. Should be ratable. ➤ Purpose Test – Amounts received must be for qualified purposes. ➤ Gross Income Test – Tax exempt interest, excess assessments that are refunded or applied against future years and capital assessment are not included in gross income when computing the 60% test. 	<ul style="list-style-type: none"> ➤ Revenue from non-association property ➤ Non-member's use of association property ➤ Amounts charged to association members for specific services (unless fees are charged ratably to all unit owners): <ul style="list-style-type: none"> • Guest Fees • Pool Passes • Parking Fees



Exempt Function Expenses v. Non-Exempt Expenses

Exempt:

- Expenditures for activities provided to or on behalf of the association members.

Non-Exempt

- Expenses directly incurred for the production of non-exempt income.
- Administrative expenses can be allocated however cannot exceed 10% or the 90% test will fail.



Section 277

- Requires filing of Form 1120 or 1120-A
- Categorizes income and expenses into membership and non-membership.
- NOL losses generated on non-membership activities follow Section 172 NOL rules.

Membership v. Non-Membership Income

Membership Income

- Income received by an association in their capacity as association members as opposed to customers in receipt of goods/services.

Non-Membership Income

- Revenue derived from the following:
 - Non-association property
 - Non-members use of association property
 - Amounts charged to association members for specific services

Membership v. Non-Membership Expenses

Membership Expenses

- Expenses incurred for the benefit of the association

Non-Membership Expenses

- Expenses directly incurred for the production of non-member income and an allocation of administrative expenses.



Revenue Ruling 70-604

- Election made on the tax return to carry over “excess contributions” from members to the following tax year without including that amount as taxable income.
- Election should be made by the members prior to filing the tax return.
- Not necessary to specify the amount of the election.



Capital Contributions

Generally, replacement funds, capital improvement assessments, litigation and insurance proceeds.

There are seven factors which determine whether a contribution is capital in nature:

1. Purpose of the assessment must be capital in nature
2. Must be advanced notice
3. Must be accounted for as a capital contribution
4. Must be held for the purpose only
5. Must be held in a separate bank account
6. Must be expended eventually for that purpose
7. Must increase the capital account of the unit owner



IRC 118 and IRC 263

- IRC 118: all contributions to capital are excluded from income
- IRC 263: No deduction can be taken for capital expenditures.
 - Painting is not considered capital
 - Intention and purpose are determining factors of whether an item is capital in nature.

You Name It Condo Association, Inc.

Example Tax Return and Work Papers

You Name It Condo Association, Inc.
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE

For the Year Ended December 31, 2009

	Operating Fund	Replacement Fund	Total
REVENUES			
Owner assessments	\$ 650,000	\$ 70,000	\$ 720,000
Initiation fees	5,000	-	5,000
Interest income	-	2,500	2,500
Other income	15,000	-	15,000
TOTAL REVENUES	<u>670,000</u>	<u>72,500</u>	<u>742,500</u>
EXPENDITURES - (See Supplementary Schedule)			
Reserves	-	25,000	25,000
Common area	10,000	-	10,000
Building maintenance	64,000	-	64,000
Grounds maintenance	64,000	-	64,000
Pool & clubhouse maintenance	12,000	-	12,000
Security & fire services	50,000	-	50,000
Utilities	180,000	-	180,000
General & administrative	234,000	-	234,000
TOTAL EXPENDITURES	<u>614,000</u>	<u>25,000</u>	<u>639,000</u>
OTHER INCOME / (EXPENSE)			
Federal income tax	-	-	-
TOTAL OTHER INCOME / (EXPENSE)	<u>-</u>	<u>-</u>	<u>-</u>
NET REVENUES IN EXCESS OF EXPENDITURES / (EXPENDITURES IN EXCESS OF REVENUES)	<u>56,000</u>	<u>47,500</u>	<u>103,500</u>
Beginning accumulated excess of revenues over expenditures / (excess expenditures over revenues)	(40,000)	375,000	335,000
Ending accumulated excess of revenues over expenditures	<u>\$ 16,000</u>	<u>\$ 422,500</u>	<u>\$ 438,500</u>

You Name It Condo Association, Inc.
Income Tax Worksheet, Form 1120H
For the Year Ended December 31, 2009

REVENUES	Total	* Capital Items	Net Amounts	Non-Exempt Percentage	Exempt Function	Non-Exempt Function
Owner assessments	\$ 720,000	\$ 70,000	\$ 650,000	0.00%	\$ 650,000	\$ -
Initiation fees	5,000	-	5,000	0.00%	5,000	-
Interest income	2,500	-	2,500	100.00%	-	2,500
Miscellaneous income	15,000	-	15,000	10.00%	13,500	1,500
TOTAL REVENUES	742,500	70,000	672,500		668,500	4,000
EXPENDITURES						
Reserves	25,000	20,000	5,000	0.00%	5,000	-
Common area	10,000	-	10,000	0.00%	10,000	-
Building maintenance	64,000	-	64,000	0.00%	64,000	-
Grounds maintenance	64,000	-	64,000	0.00%	64,000	-
Pool & clubhouse maintenance	12,000	-	12,000	0.00%	12,000	-
Security & fire services	50,000	-	50,000	0.00%	50,000	-
Utilities	180,000	-	180,000	0.00%	180,000	-
General & administrative	234,000	-	234,000	Specifically Allocated	225,215	8,785
TOTAL EXPENDITURES	639,000	20,000	619,000		610,215	8,785
NET REVENUES IN EXCESS OF EXPENDITURES	103,500	50,000	53,500		58,285	(4,785)
FORM 1120H EXCLUSION						
NET FORM 1120H TAXABLE INCOME						(100)
FORM 1120H TAX						
						(4,885)
60% INCOME TEST						
<u>EXEMPT FUNCTION INCOME</u>		<u>668,500</u>	<u>99.41%</u>			
<u>TOTAL INCOME</u>		<u>672,500</u>				
90% EXPENDITURE TEST						
<u>QUALIFYING EXPENDITURES</u>		<u>610,215</u>	<u>95.50%</u>			
<u>TOTAL EXPENDITURES</u>		<u>639,000</u>				

* Capital Items does not include Painting reserves

You Name It Condo Association, Inc.
Income Tax Worksheet, Form 1120H
For the Year Ended December 31, 2009

	Jan - Dec 09	Allocation %	NonExempt Expenses
Administrative expenses			
Payroll fees	150	5%	8
Depreciation	2,700	0%	0
Wages - office	75,000	5%	3,750
Payroll tax expense - office	4,500	5%	225
Accounting and audit fees	30,000	5%	1,500
Bank charges	500	5%	25
Dues & subscriptions	600	0%	0
Equipment rental - admin	14,000	0%	0
Janitorial / cleaning expense	2,500	0%	0
Insurance	30,000	0%	0
Legal fees	48,000	5%	2,400
License & fees	4,000	0%	0
Office expense	9,000	5%	450
Postage and delivery	5,000	5%	250
Repairs & maintenance	1,000	0%	0
Telephone	3,500	5%	175
Cell phones	2,000	0%	0
Temp labor	600	0%	0
Miscellaneous	910	0%	0
Interest expense	40	5%	2
Total Administrative expenses	234,000	5%	8,785
Gain / loss from sale of fixed assets			0
Total Expenses			8,785

U.S. Income Tax Return for Homeowners Associations

OMB No. 1545-0127

2009

Form 1120-H

Department of the Treasury Internal Revenue Service

See separate instructions.

For calendar year 2009 or tax year beginning and ending

Name: You Name It Condo Association, Inc.

Employer identification number: 12-3456789

Address: 1234 Name It Lane, Orlando, FL 12345

Date association formed: 01/01/2001

Check type: (1) Final return (2) Name change (3) Address change (4) Amended return

A Check type of homeowners association: Condominium management association Residential real estate association Timeshare association

B Total exempt function income. Must meet 60% gross income test (see instructions) 668,500

C Total expenditures made for purposes described in 50% expenditure test (see instructions) 639,000

D Association's total expenditures for the tax year (see instructions) 619,300

E Tax-exempt interest received or accrued during the tax year

Gross Income (excluding exempt function income)

1 Dividends 1

2 Taxable interest 2 2,500

3 Gross rents 3

4 Gross royalties 4

5 Capital gain net income (attach Schedule D (Form 1120)) 5

6 Net gain or (loss) from Form 4797, Part II, line 17 (attach Form 4797) 6

7 Other income (excluding exempt function income) (attach schedule) Stat 1 7 1,500

8 Gross income (including exempt function income). Add lines 1 through 7 8 4,000

Deductions (directly connected to the production of gross income, excluding exempt function income)

9 Salaries and wages 9 3,750

10 Repairs and maintenance 10

11 Rents 11

12 Taxes and licenses 12 225

13 Interest 13 2

14 Depreciation (attach Form 4562) 14

15 Other deductions (attach schedule) Stat 2 15 4,808

16 Total deductions. Add lines 9 through 15 16 8,785

17 Taxable income before specific deduction of \$100. Subtract line 16 from line 8 17 -4,785

18 Specific deduction of \$100 18 100

Tax and Payments

19 Taxable income. Subtract line 18 from line 17 19 -4,885

20 Enter 30% of line 19. (Timeshare associations, enter 32% of line 19) 20 0

21 Tax credits (see instructions) 21

22 Total tax. Subtract line 21 from line 20. See instructions for recapture of certain credits 22 0

23 a 2008 overpayment credited to 2009 23a

b 2009 estimated tax payments 23b

c Total 23c

d Tax deposited with Form 7004 23d

e Credit for tax paid on undistributed capital gains (attach Form 2439) 23e

f Credit for federal tax paid on fuels (attach Form 4136) 23f

23g 0

24 Amount owed. Subtract line 23g from line 22 (see instructions) 24 0

25 Overpayment. Subtract line 22 from line 23g 25

26 Enter amount of line 25 you want credited to 2010 estimated tax 26

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than the taxpayer) is based on all information of which preparer has any knowledge.

May the IRS discuss the return with the preparer shown below (see note 2)? Yes No

Sign Here: Signature of officer First Last Date Preparer's Name

You Name It Condo Association, Inc.
Income Tax Worksheet, Form 1120
For the Year Ended December 31, 2009

	Total	Description	M-J Items	Preliminary amounts	Carryover allocation	Final Amounts	Non-Member	Member
REVENUES								
Owner assessments	\$ 720,000	Capital item	\$ (70,000)	\$ 650,000	\$ (46,970)	\$ 603,030	\$ -	\$ 603,030
Initiation fees	5,000		-	5,000	-	5,000	-	5,000
Interest income	2,500		-	2,500	-	2,500	-	2,500
Other income	15,000		-	15,000	-	15,000	13,515	1,485
TOTAL REVENUES	742,500		(70,000)	672,500	(46,970)	625,530	16,015	609,515
EXPENDITURES								
Reserves	(25,000)	Capital item	20,000	(5,000)	-	(5,000)	-	(5,000)
Common areas	(10,000)		-	(10,000)	-	(10,000)	-	(10,000)
Building maintenance	(64,000)		-	(64,000)	-	(64,000)	-	(64,000)
Grounds maintenance	(64,000)		-	(64,000)	-	(64,000)	-	(64,000)
Pool & clubhouse maintenance	(12,000)		-	(12,000)	-	(12,000)	-	(12,000)
Security & fire services	(50,000)		-	(50,000)	-	(50,000)	-	(50,000)
Utilities	(180,000)		-	(180,000)	-	(180,000)	-	(180,000)
General & administrative, less bad debt	(230,000)	Depreciation	700	(229,300)	(4,000)	(233,300)	(8,785)	(224,515)
TOTAL EXPENDITURES	(635,000)		20,700	(614,300)	(4,000)	(618,300)	(8,785)	(609,515)
OTHER INCOME/EXPENSE								
Bad Debt Expense	(4,000)	Bad Debt	4,000	-	-	-	-	-
Federal income tax expense	-	Fed Inc Tax	-	-	-	-	-	-
TOTAL OTHER INCOME/EXPENSE	(4,000)		4,000	-	-	-	-	-
EXCESS (DEFICIT)	103,500		(45,300)	58,200	(60,970)	7,230	7,230	-
Tax Adjustments:								
Income Carryovers: (Rev. Rul. 70-604 - Other Income line 10)								
Prior Year	-		-	-	-	-	-	-
Current Year	(46,970)		(46,970)	46,970	-	-	-	-
Total	(46,970)		(46,970)	46,970	-	-	-	-
Deduction Carryover (Sec 277 - Other Deductions line 26)								
Prior Year	(4,000)		(4,000)	4,000	-	-	-	-
Current Year	-		-	-	-	-	-	-
Total	(4,000)		(4,000)	4,000	-	-	-	-
INCOME	103,500		(86,270)	17,230	-	7,230	7,230	-
FEDERAL INCOME TAX								
Current Year Carryover Calculation								
Preliminary tax excess (deficit)				58,200				
Deduct nonmember income (or add loss)				(7,230)				
Add prior year income carryover				(4,000)				
Deduct prior year membership loss carryover				(4,000)				
Current year membership income (deduction) carryover				49,970				

You Name It Condo Association, Inc.
M-1 Reconciliation
TYE: 12/31/06

Net income per books:	\$ 103,500
Federal income tax	-
Bad debt expense	4,000
Capital expenditures (line 5) *Capital expenditures from reserves	20,000
Section 277 carryover (line 8) *Sec 277 member deductions carryover	(4,000)
Capital contributions (line 7) *Capital contributions to reserves	(70,000)
Rev Ruling 70-604 carryover (line 7) *Rev. Rul. 70-604 excess member income carryover	(46,970)
Book Depreciation	2,700
Tax Depreciation	(2,000)
Rounding	-
Net income per return	\$ 7,230

U.S. Corporation Income Tax Return
For calendar year 2009 or tax year beginning... ending... 2009

1120 Form 1120-2009
OMB No. 1545-0047

Name: **You Name It Condo Association, Inc.**
Employer identification number: **12-3456789**

Address: **1234 Name It Lane, Orlando, FL 12345**
Date incorporated: **01/01/2001**

Total assets (see instructions): **\$ 454,790**

1a	Gross receipts or sales	1c	
2	Cost of goods sold (Schedule A, line 8)	2	
3	Gross profit. Subtract line 2 from line 1a	3	
4	Dividends (Schedule C, line 19)	4	
5	Interest	5	2,500
6	Gross rents	6	
7	Gross royalties	7	
8	Capital gain net income (attach Schedule D (Form 1120))	8	
9	Net gain or (loss) from Form 4797, Part II, line 17 (attach Form 4797)	9	
10	Other income (see Instructions—attach schedule)	10	623,030
11	Total income. Add lines 3 through 10	11	623,530
12	Compensation of officers (Schedule E, line 4)	12	
13	Salaries and wages (less employment credits)	13	
14	Repairs and maintenance	14	
15	Bad debts	15	
16	Rents	16	
17	Taxes and licenses	17	
18	Interest	18	
19	Charitable contributions	19	
20	Depreciation from Form 4562 not claimed on Schedule A or elsewhere on return (attach Form 4562)	20	
21	Depreciation	21	
22	Advertising	22	
23	Pension, profit-sharing, etc., plans	23	
24	Employee benefit programs	24	
25	Domestic production activities deduction (attach Form 8903)	25	
26	Other deductions (attach schedule)	26	618,300
27	Total deductions. Add lines 12 through 26	27	618,300
28	Taxable income before net operating loss deduction and special deductions. Subtract line 27 from line 11	28	7,230
29	Less: a Net operating loss deduction (see instructions)	29a	
	b Special deductions (Schedule C, line 20)	29b	
30	Taxable income. Subtract line 29c from line 28 (see instructions)	30	7,230
31	Total tax (Schedule J, line 10)	31	1,085
32a	2009 overpayment credited to 2009	32a	
32b	2009 estimated tax payments	32b	
32c	2009 refund applied for on Form 4466	32c	
32d	Tax deposited with Form 7004	32d	
32e	Credits (1) Form 3029 (2) Form 4138	32e	
32f	Refundable credits from Form 3600, line 19c, and Form 8827, line 5c	32f	
32g	Estimated tax penalty (see Instructions). Check if Form 2220 is attached	32g	
34	Amount owed. If line 32h is smaller than the total of lines 31 and 33, enter amount owed	34	1,085
35	Overpayment. If line 32h is larger than the total of lines 31 and 33, enter amount overpaid	35	
36	Enter amount from line 35 you want credited to 2010 estimated tax	36	

Sign Here: **First Last** President

Schedule L	Balance Sheets per Books		End of tax year	
	(a)	(b)	(c)	(d)
Assets				
1	Cash	333,300		445,800
2a	Trade notes and accounts receivable	8,500	4,000	
b	Less allowance for bad debts		8,500	4,000
3	Inventories			
4	U.S. government obligations			
5	Tax-exempt securities (see instructions)			
6	Other current assets (at val.) Stat. 3		200	200
7	Loans to shareholders			
8	Mortgage and real estate loans			
9	Other investments (attach sch.)			
10a	Buildings and other depreciable assets	5,000	7,700	
b	Less accumulated depreciation	2,250	2,750	4,790
11a	Depreciable assets			
b	Less accumulated depreciation			
12	Land (net of any amortization)			
13a	Intangible assets (amortizable only)			
b	Less accumulated amortization			
14	Other assets (attach sch.)			
15	Total assets	344,750		454,790
Liabilities and Shareholders' Equity				
16	Accounts payable	7,250		9,090
17	Mortgages, notes, bonds payable (if less than 1 year)			
18	Other current liabilities (at val.) Stat. 4	2,500		3,200
19	Loans from shareholders			
20	Mortgages, notes, bonds payable (if 1 year or more)			
21	Other liabilities (attach schedule)			
22	Capital stock: a Preferred stock			
b	Common stock			
23	Additional paid-in capital			
24	Retained earnings—agreements (at val.) Stat. 5	375,000		422,500
25	Retained earnings—unappropriated	-40,000		20,000
26	Assessments to be made (at val.)			
27	Less cost of treasury stock			
28	Total liabilities and shareholders' equity	344,750		454,790

Schedule M-1 Reconciliation of Income (Loss) per Books With Income per Return
 Note: Schedule M-3 required instead of Schedule M-1 if total assets are \$10 million or more—see instructions

1	Net income (loss) per books	103,500	7	Income reported on books this year not included on this return (Items 2):	
2	Federal income tax per books			Tax-exempt interest	
3	Excess of capital losses over capital gains			Stat. 7	116,970
4	Income subject to tax not recorded on books this year (Items 3):			8	Deductions on this return not charged against book income this year (Items 4):
5	Expenses recorded on books this year not deducted on this return (Items 4):			a	Depreciation
a	Depreciation			b	Charitable contributions
b	Charitable contributions			c	Other
c	Other			Stat. 8	4,000
Stat. 6	24,700	24,700	9	Add lines 7 and 8	120,970
6	Add lines 1 through 5	128,200	10	Income (page 1, line 28)—line 9 less line 9	7,230

Schedule M-2 Analysis of Unappropriated Retained Earnings per Books (Line 25, Schedule 1)

1	Balance at beginning of year	-40,000	5	Distributions:	
2	Net income (loss) per books	103,500	a	Cash	
3	Other increases (Items 2):		b	Stock	
			c	Property	
			6	Other decreases (Items 3):	68,200
			7	Add lines 5 and 6	68,200
4	Add lines 1, 2, and 3	63,200	8	Balance at end of year (line 4 less line 7)	20,000

Statement 1 - Form 1120, Page 1, Line 10 - Other Income

Description	Amount
Owner assessments	\$ 650,000
Initiation Fees	5,000
Other income	15,000
Rev Rul. 70-604	-46,570
Total	\$ 623,030

Statement 2 - Form 1120, Page 1, Line 26 - Other Deductions

Description	Amount
Reserve expenditures	\$ 5,000
Common area	10,000
Building maintenance	64,000
Grounds maintenance	64,000
Pool & clubhouse maintenance	12,000
Security & fire services	50,000
Utilities	180,000
General & admin	223,300
Sec 277	4,000
Total	\$ 618,300

Statement 3 - Form 1120, Page 5, Schedule L, Line 6 - Other Current Assets

Description	Beginning of Year	End of Year
Other Current Assets	\$ 200	\$ 200
Total	\$ 200	\$ 200

Statement 4 - Form 1120, Page 5, Schedule L, Line 18 - Other Current Liabilities

Description	Beginning of Year	End of Year
Other Current Liabilities	\$ 2,500	\$ 3,200
Total	\$ 2,500	\$ 3,200

Statement 5 - Form 1120, Page 5, Schedule L, Line 24 - Retained Earnings - Appropriated

Description	Beginning of Year	End of Year
RE - Appropriated	\$ 375,000	\$ 422,500
Total	\$ 375,000	\$ 422,500

Statement 6 - Form 1120, Page 5, Schedule M-1, Line 5 - Expenses on Books Not on Return

Description	Amount
Bad debt expense	\$ 4,000
Capital expenditures from reserves	20,000
Book / Tax difference deprec	700
Total	\$ 24,700

Statement 7 - Form 1120, Page 5, Schedule M-1, Line 7 - Income on Books Not on Return

Description	Amount
Capital contributions to reserves	\$ 70,000
Rev Rul. 70-604 excess member income carryover	46,970
Total	\$ 116,970

Statement 8 - Form 1120, Page 5, Schedule M-1, Line 8 - Deductions on Return Not on Books

Description	Amount
Sec 277 member deductions carryover	\$ 4,000
Total	\$ 4,000

Questions?