

UNDERSTANDING TAXES AND COMMUNITY ASSOCIATIONS

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Most community associations are formed as non-profit corporations. This simply means that the organization is not going to retain a profit for the members above the necessary expenses. Many people confuse this with what the IRS designates as a 'tax-exempt' corporation.

Non-profit corporations are not necessarily tax-exempt. Only certain businesses can qualify as tax exempt, and only then, after a long application process with the IRS. The bottom line is that a community association will have to file annual federal and state tax returns, but usually don't owe taxes. So even though a community association could probably qualify for tax exempt status it is probably not worth bothering with.

The annual tax returns are fairly simple to fill out, but I often suggest that the Board hire an accountant. In this way the Board is delegating to a professional, and an outside third party is looking over the association's financial records every year.

The other issue for community associations is property taxes on common areas. This does not include condominiums because the common elements are considered to be in shared ownership by all the unit owners. Except in condominiums, the common areas are actually owned by the association and not the homeowners.

When the tax assessor first evaluates the common areas they are usually owned by the developer of the subdivision or the developer run association. At this time the assessor assigns a tax valuation based upon the nature of the property; open space, pool, clubhouse, etc... This is done without regards as to whether or not the parcels are owned by an association. Therefore, an annual tax is levied and a bill is sent to the developer.

It is usually when the control of the Board is turned over from the developer to the homeowners that a tax appeal is filed regarding the common areas. The appeal is based upon two principals; double taxation and fair market value.

When the tax assessor values a home in a community association he or she takes into consideration the owner's right to the use any amenities and the value added to the home because of the common areas. Therefore, if the common areas are also taxed the homeowners are in effect paying twice.

The other basis for appeal is lack of fair market value. Practically speaking, it would almost be impossible to sell a common area because it contains so many restrictions regarding use for the owner/members. Nobody would want to knowingly purchase a common area. From the fair market approach the common areas have little to no value.

The tax appeal is usually successful, which means that the common areas are assigned a 'nominal' tax value. The effect is different for various counties, but it usually means that the association will either no longer owe any taxes, or owe very little. Unfortunately, there is no way to be reimbursed for the property taxes paid in the past.