

Association of Condominium,
Townhouse, and
Homeowners Associations



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**ACTHA's
SPRING CONFERENCE**
Sat., April 16

**Details on pages
6 & 7**

YES. ASSOCIATIONS DO FILE TAXES.

By Steve Silberman of Marcum, LLP

As a CPA, one of the most frequently asked questions I get from Board members is: Are we a not-for-profit corporation and if we are, do we have to file an income tax return?

First of all, most associations are usually incorporated as not-for-profit corporations by the developer. If this did not happen to your association, I recommend hiring an attorney to incorporate your association as a not-for-profit corporation, even though you could go to the Secretary of State's website yourself to incorporate. Once incorporated, you must remember that each year your association has to file an annual report with the Illinois Secretary of State and pay an annual fee in order to stay incorporated.

Residential condominiums, townhomes, and homeowners' associations are not-for-profit corporations that generally do not qualify for Federal income tax-exempt status. Residential associations may be taxed under Internal Revenue Code (IRC) Section 277 or may elect to be taxed under IRC Section 528. Under IRC Section 277, associations file Federal Form 1120 and under IRC Section 528, associations file Federal Form 1120-H. An association can decide annually which form it would like to file. So let's discuss which form is right for your association and the differences between each form.

FEDERAL FORM 1120-H

Federal Form 1120-H was developed so that associations would not be taxed for carrying out its main function of managing

Continued on page 4

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LEGISLATIVE UPDATE

In the February issue, introduced legislation (at press time) was included. Since then, more bills have been introduced and the synopsis of each is below. To view the full text of a bill go to: www.ilga.gov and type the bill number in the left-side box.

HB 6243 (Jesiel) Creates the Short-Term Residential Rental Property Act. Provides that a short-term residential rental property listed on internet-enabled platforms shall not be regulated by a unit of local government in a manner more restrictive than bed and breakfast establishments.

HB 5927 (Fine) Amends the Common Interest Community Association Act (CICCA). Provides that the board has the authority to adopt and amend rules and regulations covering the details of the operation and use of the parcel after a meeting of the unit owners called for the specific purpose of discussing the proposed rules and regulations. Provides procedural requirements. Provides that no rule or regulation may impair any rights guaranteed by the First Amendment to the Constitution of the United States or Section 4 of Article I of the Illinois Constitution including, but not limited to, the free exercise of religion, nor may any rules or regulations conflict with the provisions of the Act or the declaration, operating agreement, or bylaws. Provides that no rule or regulation shall prohibit any reasonable accommodation for religious practices, including the attachment of religiously-mandated objects to the front-door area of a unit.

HB 5812 (Breen) Amends the Condominium and Common Interest Community Ombudsperson Act. Makes numerous technical and substantive changes in provisions concerning: definitions; the Office of the Condominium and Common Interest Community Ombudsperson; the Office's website; the written policy for receiving complaints; requests for assistance; dispute resolution; confidentiality; and reporting requirements. Repeals a Section concerning registration. Effective July 1, 2016.

HB 5696 (Cassidy) Amends the Common Interest Community Association Act and the Condominium Property Act. Provides that the term "acceptable technological means" includes, among other things, any generally available technology that, by rule of the association, is deemed to provide reasonable security, reliability, identification, and verifiability. Provides that acceptable technological means may be used to conduct association business, including: notice required to be sent or received; signature, vote, consent, or approval required to be obtained; and the performance of obligations or exercise of rights. Provides that Sections concerning the use of technology do not apply to any notices required: (i) under the Forcible Entry and Detainer Article of the Code of Civil Procedure; or (ii) in connection with foreclosure proceedings in enforcement of any lien rights" under the Act (instead of "notices required under [the Forcible Entry and Detainer Article] of the Code of Civil Procedure related to: (i) an action by the common interest community association to collect a common expense; or (ii) foreclosure proceedings in enforcement of any lien rights" under the Act).

HB 4959 (Batinick) Amends the Community Association Manager Licensing and Disciplinary Act. Removes the requirement that the Department of Financial and Professional Regulation use licensing examination standards from the National Organization for Competency Assurances. Provides that no supervisory community association manager may be the designated supervisory community association manager for more than one firm, corporation, limited liability company, or other legal entity (rather than no community association manager may be the licensee-in-charge for more than one firm, corporation, limited liability company, or other legal entity). Provides that the Department may require a person whose license is lapsed to complete a period of evaluated experience (rather than evaluated clinical experience). Makes technical changes. Amends the Real Estate License Act of 2000. Includes limited liability companies in provisions concerning a sponsoring broker in an employment agreement with a licensee. Makes grammatical changes.

NOT SURE WHAT ANY OF THIS MEANS? ACTHA will offer a Legal Forum/Ask an Attorney at the Spring Conference on Sat., April 16 at Drury Lane in Oakbrook. See details on Page 6/7. Registration also available online.

Continued from page 1

and maintaining the common elements. Commercial condominium associations cannot file Federal Form 1120-H. IRC Section 528 states that income and expenses must be allocated between exempt function activities and nonexempt function activities. Associations are only taxed on its net non-exempt function income at a Federal tax rate of 30%. (Timeshare Associations are taxed at a Federal tax rate of 32%). So what is exempt and non-exempt function income?

Exempt Function Income

is: Operating income received as assessments from owners of condominium, townhome or HOAs. They also can be assessments received from developers on unsold units or lots. These assessments must be assessed ratably to be exempt function income.

Non-exempt Function Income (or taxable income) is:

1) Income from non-association property - commercial operations and interest and dividends. 2) Income from non-members for use of association property. 3) User charges to association members for special services unless the user charge is assessed once in a twelve month period and the benefit lasts for the entire 12 month period. An example of a user charge is laundry income.

The advantages of Federal Form 1120-H are as follows:

1. Associations are not taxed on exempt function income.
2. The tax form is a one page form, with supplementary schedules, so it costs less to prepare.
3. The form has less risk than Federal Form 1120. There are

four tests that have to be met to file Federal Form 1120-H, but most residential associations will qualify.

4. Fund accounting is not required since capital or reserve assessments are not taxed.
5. No election forms are required like on Federal Form 1120.
6. As long as you keep filing Federal Form 1120-H, no estimated taxes are required.

FEDERAL FORM 1120

The key advantage of Federal Form 1120 is that an association could pay tax at a lower rate than Federal Form 1120-H. Income tax rates start out at 15% on the first \$50,000, however, the risk of compliance is far greater since an association must follow certain required procedures. Also, since the form is much longer and more complex it costs more to prepare than Federal Form 1120-H.

IRC Section 277 states that income for Federal Form 1120 should be allocated between membership and non-membership income. An association can be taxed on both if there is net income, however, an association can make an annual election to defer net membership income.

Revenue Ruling 70-604 allows associations to defer net membership income for one year but if the association has net membership income in the next year then the association would have to pay tax in the next year on the deferred income. An association can also make an election under Revenue Ruling 70-604 to refund net membership income, but in my 30+ plus years of working with associations, I have never

seen an association refund money. A question that I get asked about all the time is: Can our association transfer excess net membership income to reserves and then not have to pay taxes on this excess? The answer is NO if you are filing Federal Form 1120.

IRC Section 118 states that an association cannot transfer excess net membership income to reserves to avoid paying taxes since you cannot re-characterize what the assessments were for originally. In order for Revenue Ruling 70-604 to be valid, the election has to be made annually by all members (usually at the annual meeting) and it should preferably be made before the end of the year. The dollar amount does not have to be specified.

Capital contributions (reserve assessments) will be treated as non-taxable on Federal Form 1120 if certain guidelines are followed:

1. The purpose of the assessment must be capital in nature. The reserve study supports the purpose of the capital assessment. However, painting, even if it was included in your reserve study, is an operating assessment, not a capital assessment.
2. Members must have advance notice. Distributing copies of the budget to the members is considered advance notice.
3. The assessment must be accounted for as a capital contribution and held for that purpose. The books and records, along with the budget should segregate operating and reserve (capital) activities. Therefore, the association should use fund accounting.

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4. Reserve (capital) assessments should be deposited into a separate account and reserve expenditures should be paid out of this separate account. An association can pay for capital expenditures out of the operating fund account as long as the reserve account reimburses the operating account in a relatively short period of time.

Now that you have a brief understanding of the two forms, you might be wondering which form should your association be using? This is a hard question to answer

unless your CPA knows the facts and issues associated with your association.

Usually if your association has little interest income and no (or minimal) user fees you will file Federal Form 1120-H. As interest income grows, your association should look at filing Federal Form 1120 as an alternative. If your association has minimal interest income, but you have a net loss from your net membership (for example due to a painting project) you may want to file Federal Form 1120 since that loss gets carried forward. If your asso-

ciation files Federal Form 1120 because of the large amount of non-membership income, you want to make sure that you do tax planning ahead of time to minimize your net membership income.

You now should have a better understanding about the different types of Federal income tax returns and which Federal income tax return is right for your association.

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www.actha.org or WWW.CONDOEDUCATION.COM

BEGIN THE DAY

8—9:30 a.m.

GENERAL SESSION: Legal Forum/Ask an Attorney

This session will begin with an update on the various changes affecting community associations and what you need to know so your association can stay on the right path. The Ask an Attorney session will follow. Preference will be given to questions submitted in advance. Panelists: Stuart Fullett of Fullett Rosenlund Anderson, David Hartwell of Penland and Hartwell and State Senator Heather Steans

Your choice! Pick one program from each of the time slots offered!

11:30 a.m.— 12:30 p.m.

Leadership - Role of President & Function of Board: This session will cover qualities of successful leaders, how to set a vision for association board and how to recruit and develop good board members. The President should set the standard and build a knowledgeable and committed team. Presenters: Tanya Briggs of LaGrange Tower Condo Assn., Marcia Caruso of Caruso Management Group, Maureen Gold of Harborside III Condo Assn.,

11:30 a.m.— 12:30 p.m.

Ponds, Trees & Natural Landscaping - Enhancement or Nuisance: Native vegetation and sustainable landscaping are the practices of enlightened environmentalists. The panelists will share ideas and methods to transition your ponds, trees and landscaping so they will be easier to maintain. Associations can reduce the expense of maintenance when the transition is complete. Presenters: Chris Berg of Independent Association Managers, Tom Tyler of Bartlett Tree Experts, Sarah Zink of Integrated Lakes Management

11:30 a.m.— 12:30 p.m.

What's the Big Deal About Reserve Studies: If you have one, that's a good start. If you don't, you should begin the process now. But having one is not doing any good if you don't use it to your advantage. Learn how to use it for budgeting, to account for your reserve funds, report expenditures, and other uses of the information in the study. Presenters: Mark Canteay of Canteay Associates and Rosemary Wert of Community Specialists

1:30 p.m.— 2:30 p.m.

Oops! Some Acts Can Cause Big Messes: This session will describe some of the mistakes boards make, such as, approving contracts that are not in compliance with the governing documents, not giving proper notice, making decisions outside of proper meetings and more. Learn from others' mistakes so you can avoid these common pitfalls. Presenters: Marshall Dickler of Dickler Kahn Slowikowski & Zavell, Amanda Paton of Marcum, Janice Subasic of ACM Community Management

1:30 p.m.— 2:30 p.m.

Leasing & Crime Free Policies - Enhance Your Community: Many municipalities are assisting their local associations by encouraging adoption of policies to have safer and more neighborly communities. The panelists will give examples of tenant screening and leasing policies that have been proven effective and the methods to put this in practice. Presenters: John Bickley of Kovitz Shifrin Nesbit and William Townsell of the Chicago Police Dept. Community Outreach

1:30 p.m.— 2:30 p.m.

Rules - It's a New Set of Problems: How should your association handle the social issues that now crop up and don't have easy solutions? These present day nuisances include smoking and marijuana, noises, odors, pets, service animals, and more. Learn how to develop and revise rules so they will be enforceable. Presenters: Andrea Sorgani of Alma Property Management and Jim Webb of Keay and Costello

END THE DAY: 2:30—3:30 p.m.

Ask a Professional: Steve Silberman of Marcum, Kim May of Advanced Property Specialists, Ron Sirotzki of Hollinger Insurance Services, and Attorney Charles VanderVennet

Registration Form

YES!! I want to register for the Conference and Trade Show on Saturday, April 16 at the Drury Lane in Oakbrook Terrace. **Full Conference Access includes:** seminars, continental breakfast, sit-down lunch, Trade Show, parking and all seminar hand-outs.

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REGISTRATION FEES: ACTHA members: \$45 each \$ _____
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Non-Members: \$120 each \$ _____
TOTAL AMOUNT DUE \$ _____

_____ Amount Enclosed; Make check payable to "ACTHA" and remit to 11 E. Adams, Ste. 1107, Chicago, IL 60603 or register online at ww.actha.org: *NOTE: No refunds are given after April 1 and there will be an additional charge of \$10 per person for anyone registering after April 14 or at the door. All cancellations are subject to a 25% handling fee.*

QUESTIONS???? Preference will be given to questions submitted in advance for the Ask an Attorney and/or Ask a Professional Panels. What is your question? (PLEASE PRINT and ATTACH)



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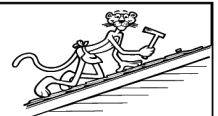
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Question of the Month

By: Howard Dakoff of Levenfeld Pearlstein / 2 N. LaSalle, Chicago 60602
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Q. Does “fee simple” mean the owner owns the property curb-to-curb or is it more complicated than that?

A. “Fee Simple” is a legal term/concept describing a classification of an ownership interest in real estate. Examples of other classifications could be a life estate (i.e. a person has a right to occupy real estate for their life, but upon their death, ownership passes to someone else) or a tenancy. The term “fee simple” designates an ownership interest under common law, but in and of itself does not contain any boundaries such as curb to curb because the boundaries of what is owned (or leased, or part of a life estate) is covered by the terms of the legal description that of real estate - that may be owned by “fee simple” - in conjunction with the declaration for a community association. For example, a townhome unit may be owned by fee simple with boundaries curb to curb or it is equally possible townhome unit ownership consists only the structure itself; it just depends on the townhome declaration and how the real estate is classified and legally described.

ACTHA IS PLEASED TO ANNOUNCE THAT STATE SENATOR HEATHER STEANS will participate in the Legal/Legislative Forum on Sat., April 16. Sen. Steans was the Senate sponsor of the Condo and Common Interest Community Ombudsperson Act. She will update attendees on the new law and what associations will need to do to be in compliance beginning July 1.