

Yes, HOA, You Must File a Tax Return

By Brett Hersh, EA, MBA

There are over 330,000 community associations in the United States. These associations regulate over 26 million households and over 68 million residents. Over ninety-five percent of these associations are homeowner associations whose members own either a residence or a condominium.

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Homeowner Associations are a fact of modern living. They span the country and come in all shapes and sizes. Some HOAs maintain skyscrapers filled with spacious condominiums owned by city elite. Others manage residential communities comprised of hundreds of homes dotting large swaths of suburbia. The vast majority of HOA's, however, are much smaller and primarily tasked with maintaining the roads and mowing common areas for a handful to several dozen home owners.

Regardless of the location and size of these HOAs, all have one thing in common. Each and every Homeowners Association in the United States must file a tax return each and every year. This fact arrives as a shock to many HOA directors who believe they are exempt from taxation because their HOA is not a business – it is registered with their state as a nonprofit or a tax exempt association.

Unfortunately, this is not the case. The IRS completely ignores the state-registered structure of their HOA. To be treated as a nonprofit by the IRS, an HOA must formally apply and be granted the very rare honor of being approved as a 501(C) organization. Historically, HOAs that had not received formal nonprofit approval were treated as corporations for tax purposes and forced to file a business tax return, Form 1120, each year.

This policy placed HOAs in a confusing situation that did not reflect their reality. Although most HOAs are not true nonprofits – organized to benefit the general public, they are definitely not in business – selling a product or service to generate profit! They are volunteer organizations (if you're in an HOA, you know how loosely I use this term) created to enforce the common covenants and maintain the common areas of their community.

Homeowner Associations remained in this tax no-mans-land until 1976 when congress passed the Tax Reform Act of 1976. The Tax Reform Act of 1976 created Form 1120-H and a tax definition of what a homeowners association is and, therefore, who can file Form 1120-H. I will not elaborate on this definition here – it's rather convoluted and wordy – but suffice it to say that the vast majority of HOAs meet this definition.

Those who most easily qualify to file Form 1120-H are HOA's that function solely to collect dues and assessments from members and to use these dues and assessments to manage and maintain HOA property. Many HOAs that easily qualify will also have some interest income from savings or certificates of deposits – interest earned on funds set aside to repair and replace HOA property.

HOAs that easily qualify to use Form 1120-H will not have additional income from nonmembers or members for the oil well royalties, cell tower rental, or the use of amenities such as swimming pools, clubhouse rentals, or laundromats. Although many HOAs that receive these forms of income will still qualify to file Form 1120-H, making that determination, as well as preparing the return, becomes much more complicated.

**For most HOAs
preparing Form 1120-
H is relatively simple.**

For HOAs that easily qualify, however, preparing Form 1120-H is relatively simple. So simple, in fact, that OvernightAccountant.com, a firm for which I am an instructor, has allowed me to develop a course to help HOAs prepare their own Form 1120-H (at a small fraction of the cost of hiring a professional). If you're a director for an HOA that easily qualifies to file Form 1120-H, I invite you to learn more about our Form 1120-H Basics Course.

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