

**U.S. Income Tax Return  
for Homeowners Associations**

**1996**

Department of the Treasury  
Internal Revenue Service

► **For Paperwork Reduction Act Notice, see page 2.**

For calendar year 1996 or tax year beginning \_\_\_\_\_, 1996, and ending \_\_\_\_\_, 19

<b>Use IRS label. Otherwise, please print or type.</b>	Name	Employer identification number (see page 4)
	Number, street, and room or suite no. (If a P.O. box, see page 4.)	Date association formed
	City or town, state, and ZIP code	

Check if: (1)  Final return (2)  Change of address (3)  Amended return

<b>A</b> Total exempt function income. Must meet 60% gross income test (see instructions)	<b>A</b>		
<b>B</b> Total expenditures made for purposes described in 90% expenditure test (see instructions)	<b>B</b>		
<b>C</b> Association's total expenditures for the tax year (see instructions)	<b>C</b>		
<b>D</b> Tax-exempt interest received or accrued during the tax year	<b>D</b>		

**Gross Income** (excluding exempt function income)

<b>1</b> Dividends	<b>1</b>		
<b>2</b> Taxable interest	<b>2</b>		
<b>3</b> Gross rents	<b>3</b>		
<b>4</b> Gross royalties	<b>4</b>		
<b>5</b> Capital gain net income (attach Schedule D (Form 1120))	<b>5</b>		
<b>6</b> Net gain (or loss) from Form 4797, Part II, line 20 (attach Form 4797)	<b>6</b>		
<b>7</b> Other income (excluding exempt function income) (attach schedule)	<b>7</b>		
<b>8</b> <b>Gross income</b> (excluding exempt function income). Add lines 1 through 7	<b>8</b>		

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

<b>9</b> Salaries and wages	<b>9</b>		
<b>10</b> Repairs and maintenance	<b>10</b>		
<b>11</b> Rents	<b>11</b>		
<b>12</b> Taxes and licenses	<b>12</b>		
<b>13</b> Interest	<b>13</b>		
<b>14</b> Depreciation (attach Form 4562)	<b>14</b>		
<b>15</b> Other deductions (attach schedule)	<b>15</b>		
<b>16</b> <b>Total deductions.</b> Add lines 9 through 15	<b>16</b>		
<b>17</b> Taxable income before specific deduction of \$100. Subtract line 16 from line 8	<b>17</b>		
<b>18</b> Specific deduction of \$100	<b>18</b>	\$100	00

**Tax and Payments**

<b>19</b> <b>Taxable income.</b> Subtract line 18 from line 17	<b>19</b>		
<b>20</b> Enter 30% of line 19	<b>20</b>		
<b>21</b> Tax credits (see instructions)	<b>21</b>		
<b>22</b> <b>Total tax.</b> Subtract line 21 from line 20. See instructions for recapture of certain credits	<b>22</b>		
<b>23</b> <b>Payments:</b> a 1995 overpayment credited to 1996	<b>23a</b>		
b 1996 estimated tax payments	<b>23b</b>		
c Total	<b>23c</b>		
d Tax deposited with Form 7004	<b>23d</b>		
e Credit from regulated investment companies (attach Form 2439)	<b>23e</b>		
f Credit for Federal tax on fuels (attach Form 4136)	<b>23f</b>		
g Add lines 23c through 23f	<b>23g</b>		
<b>24</b> <b>Tax due.</b> Subtract line 23g from line 22. See instructions for depository method of tax payment	<b>24</b>		
<b>25</b> <b>Overpayment.</b> Subtract line 22 from line 23g	<b>25</b>		
<b>26</b> Enter amount of line 25 you want: <b>Credited to 1997 estimated tax</b> ►	<b>26</b>		<b>Refunded</b> ►

**Please Sign Here** 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 taxpayer) is based on all information of which preparer has any knowledge.

<b>Paid Preparer's Use Only</b>	Preparer's signature	Date	Check if self-employed <input type="checkbox"/>	Preparer's social security number
	Firm's name (or yours if self-employed) and address	EIN	ZIP code	

## Paperwork Reduction Act Notice

We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by Code section 6103.

The time needed to complete and file this form will vary depending on individual circumstances. The estimated average time is:

<b>Recordkeeping</b> . . . . .	11 hr., 15 min.
<b>Learning about the law or the form</b> . . . . .	5 hr., 50 min.
<b>Preparing the form</b> . . . . .	13 hr., 43 min.
<b>Copying, assembling, and sending the form to the IRS</b> . . . . .	2 hr., 9 min.

If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. You can write to the Tax Forms Committee, Western Area Distribution Center, Rancho Cordova, CA 95743-0001. **DO NOT** send the tax form to this office. Instead, see **Where To File** on page 3.

A homeowners association should compare its total tax computed on Form 1120-H with its total tax computed on either **Form 1120**, U.S. Corporation Income Tax Return, or **Form 1120-A**, U.S. Corporation Short-Form Income Tax Return. The association may file the form that results in the lowest tax.

**Note:** *The taxable income of a homeowners association that files its tax return on Form 1120-H is taxed at a flat rate of 30%. This rate applies to both ordinary income and capital gains.*

### A Change To Note

If the association's total deposits of social security, Medicare, and withheld income taxes were more than \$50,000 in 1995, it must make electronic deposits for all depository tax liabilities that occur after June 30, 1997. For details, see **Depository Method of Tax Payment** on page 3.

### General Instructions

Section references are to the Internal Revenue Code unless otherwise noted.

### How To Get Forms and Publications

**By personal computer.**—If you subscribe to an on-line service, ask if IRS information is available and, if so, how to access it. Tax forms, instructions, publications, and other IRS information are available through the Internal Revenue Information Service (IRIS), on FedWorld, a government bulletin board. The IRIS menus offer information on available file formats and software needed to read and

print files. You must print the forms to use them; the forms are not designed to be filled out on-screen.

IRIS is directly accessible by modem at 703-321-8020. On the Internet, telnet to iris.irs.ustreas.gov or, for file transfer protocol services, connect to ftp.irs.ustreas.gov. If you are using the World Wide Web, connect to http://www.irs.ustreas.gov. FedWorld's help desk offers technical assistance on accessing IRIS (not tax help) during regular business hours at 703-487-4608.

Tax forms, instructions, and publications are also available on CD-ROM, including prior-year forms starting with the 1991 tax year. For ordering information and software requirements, contact the Government Printing Office's Superintendent of Documents (202-512-1800) or Federal Bulletin Board (202-512-1387).

**By phone and in person.**—To order forms and publications, call 1-800-TAX-FORM (1-800-829-3676). You can also get most forms and publications at your local IRS office.

### Purpose of Form

A homeowners association files Form 1120-H as its income tax return to take advantage of certain tax benefits. These benefits, in effect, allow the association to exclude exempt function income (defined below) from its gross income.

### Definitions

**Homeowners association.**—There are two kinds of homeowners associations:

1. A condominium management association organized and operated to acquire, build, manage, and care for the property in a condominium project substantially all of whose units are homes for individuals, and
2. A residential real estate management association organized and operated to acquire, build, manage, and care for a subdivision, development, or similar area substantially all of whose lots or buildings are homes for individuals.

Regulations section 1.528-4 explains the "substantially all" test. In addition:

- At least 60% of the association's gross income for the tax year must consist of exempt function income (see below).
- At least 90% of the association's expenses for the tax year must consist of expenses to acquire, build, manage, or care for its property.
- No private shareholder or individual can profit from the association's net earnings except by acquiring, building, managing, or caring for association property or by a rebate of excess membership dues or other fees.
- The association must file Form 1120-H to elect under section 528 to be treated as a homeowners association.

**Association property.**—Association property includes real and personal property that:

1. The association holds,
2. The association's members hold in common,
3. The association's members hold privately within the association, and
4. Is owned by a governmental unit and is used to benefit the unit's residents.

For more information, see Regulations section 1.528-3.

**Taxable income.**—Taxable income is the excess, if any, of:

1. Gross income for the tax year, excluding exempt function income, over
2. Allowed deductions directly connected with producing any gross income except exempt function income. Allowed deductions include a specific \$100 deduction. The following are not allowed:
  - Net operating loss deduction (section 172).
  - Deductions under Part VIII of subchapter B (special deductions for corporations).

If facilities are used (or personnel are employed) for both exempt and nonexempt purposes, see Regulations section 1.528-10.

**Exempt function income.**—Exempt function income consists of membership dues or other fees received from those who own the association's residential units or lots. This income must come from the members as owners, not as customers, of the association's services.

Assessments or fees for a common activity qualify but charges for providing services do not qualify.

**Examples.**—In general, exempt function income includes assessments made to:

1. Pay principal, interest, and real estate taxes on association property.
2. Maintain association property.
3. Clear snow from public areas and remove trash.

Income that is **not** exempt function income includes:

1. Amounts that are not includable in the organization's gross income other than under section 528 (for example, tax-exempt interest).
2. Payments from nonmembers.
3. Payments from members for special use of the organization's facilities, apart from the use generally available to all members.
4. Interest on amounts in a sinking fund.
5. Payments for work done on nonassociation property.
6. Members' payments for transportation.

For more information, see Regulations section 1.528-9.

### Electing To File Form 1120-H

By filing a properly completed Form 1120-H, the association elects to take advantage of the tax benefits provided by section 528. The election is made separately for each tax year and generally must be made by the due date, including extensions, of the income tax return. However, see Temporary Regulations section 301.9100-2T for information on a 12-month extension of time to make the election. This extension does not extend the time to pay the tax. Once Form 1120-H is filed, the association cannot revoke its election for that year unless the Commissioner consents. The association may request the Commissioner's consent by filing a ruling request with the IRS. A user fee must be paid with all ruling requests. For more information on ruling requests, see Rev. Proc. 96-1, 1996-1, C.B. 385.

If the association does not elect to use Form 1120-H, it must file the applicable income tax return (Form 1120, etc.).

If the association is tax exempt under section 501, do not file Form 1120-H. See section 6033 and related sections. If the association loses its exempt status, see Regulations section 1.528-8(e).

## When To File

In general, an association must file Form 1120-H by the 15th day of the 3rd month after the end of the tax year.

If the due date falls on a Saturday, Sunday, or legal holiday, file on the next business day.

**Extension.**—File **Form 7004**, Application for Automatic Extension of Time To File Corporation Income Tax Return, to request a 6-month extension of time to file.

## Where To File

If the association's principal office is located in	Use the following Internal Revenue Service Center address
New Jersey, New York (New York City and counties of Nassau, Rockland, Suffolk, and Westchester)	Holtsville, NY 00501
New York (all other counties), Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, Vermont	Andover, MA 05501
Florida, Georgia, South Carolina	Atlanta, GA 39901
Indiana, Kentucky, Michigan, Ohio, West Virginia	Cincinnati, OH 45999
Kansas, New Mexico, Oklahoma, Texas	Austin, TX 73301
Alaska, Arizona, California (counties of Alpine, Amador, Butte, Calaveras, Colusa, Contra Costa, Del Norte, El Dorado, Glenn, Humboldt, Lake, Lassen, Marin, Mendocino, Modoc, Napa, Nevada, Placer, Plumas, Sacramento, San Joaquin, Shasta, Sierra, Siskiyou, Solano, Sonoma, Sutter, Tehama, Trinity, Yolo, and Yuba), Colorado, Idaho, Montana, Nebraska, Nevada, North Dakota, Oregon, South Dakota, Utah, Washington, Wyoming	Ogden, UT 84201
California (all other counties), Hawaii	Fresno, CA 93888
Illinois, Iowa, Minnesota, Missouri, Wisconsin	Kansas City, MO 64999
Alabama, Arkansas, Louisiana, Mississippi, North Carolina, Tennessee	Memphis, TN 37501
Delaware, District of Columbia, Maryland, Pennsylvania, Virginia	Philadelphia, PA 19255

Associations having their principal place of business outside the United States must file with the Internal Revenue Service Center, Philadelphia, PA 19255.

## Who Must Sign

The return must be signed and dated by the president, vice-president, treasurer, assistant treasurer, chief accounting officer, or any other association officer (such as a tax officer) authorized to sign. Receivers, trustees, or assignees must sign and date any return filed on behalf of an association.

If an association officer completes Form 1120-H, the Paid Preparer's space should remain blank. Anyone who prepares Form 1120-H but does not charge the association should not sign the return. Generally, anyone who is paid to prepare the return must sign it and fill in the Paid Preparer's Use Only area.

The paid preparer must complete the required preparer information and:

- Sign the return, by hand, in the space provided for the preparer's signature (signature stamps and labels are not acceptable).
- Give a copy of the return to the taxpayer.

## Accounting Methods

Taxable income must be computed using the method of accounting regularly used in keeping the association's books and records. Generally, permissible methods include the cash, accrual, or any other method authorized by the Internal Revenue Code. In all cases, the method used must clearly reflect taxable income.

Generally, an accrual basis taxpayer can deduct accrued expenses in the tax year in which (1) all events that determine the liability have occurred, (2) the amount of the liability can be figured with reasonable accuracy, and (3) economic performance takes place with respect to the expense. There are exceptions for recurring items. See section 461(h) and the related regulations for the rules for determining when economic performance takes place.

Generally, the association may change the method of accounting used to report taxable income (for income as a whole or any material item) only by getting consent on **Form 3115**, Application for Change in Accounting Method. For more information, get **Pub. 538**, Accounting Periods and Methods.

## Change in Accounting Period

Generally, before changing an accounting period, the association must get the Commissioner's approval (Regulations section 1.442-1) by filing **Form 1128**, Application To Adopt, Change, or Retain a Tax Year. Also see **Pub. 538**.

## Rounding Off to Whole Dollars

The association may show amounts on the return and accompanying schedules as whole dollars. To do so, drop any amount less than 50 cents and increase any amount from 50 cents through 99 cents to the next higher dollar.

## Depository Method of Tax Payment

The association must pay the tax due in full no later than the 15th day of the 3rd month after the end of the tax year. Some associations (described below) are required to electronically deposit all depository taxes, including association income tax payments.

**Electronic deposit requirement.**—If the association's total deposits of social security, Medicare, and withheld income taxes were more than \$50,000 in 1995, it must make electronic deposits for all depository tax liabilities that occur after June 30, 1997. If the association was required to deposit by electronic funds transfer in prior years, continue to do so in 1997. The Electronic Federal Tax Payment System (EFTPS) must be used to make electronic deposits. If the association is required to make deposits by electronic funds transfer and fails to do so, it may be subject to a 10% penalty. Associations that are not required to make electronic deposits may voluntarily participate in EFTPS. For information on EFTPS, call 1-800-945-8400 or 1-800-555-4477. (These numbers are for EFTPS information only.)

## Form 8109, Federal Tax Deposit Coupon.—

If the association does not use EFTPS, deposit fund income tax payments (and estimated tax payments) with **Form 8109**. Do not send deposits directly to an IRS office. Mail or deliver the completed **Form 8109** with the payment to a qualified depository for Federal taxes or to the Federal Reserve bank (FRB) servicing the association's geographic area. Make checks or money orders payable to that depository or FRB. To help ensure proper crediting, write the association's EIN, the tax period to which the deposit applies, and "Form 1120-H" on the check or money order. Records of these deposits will be sent to the IRS.

A penalty may be imposed if the deposits are mailed or delivered to an IRS office rather than to an authorized depository or FRB. For more information on deposits, see the instructions in the coupon booklet (**Form 8109**) and **Pub. 583**, Starting a Business and Keeping Records.

**Caution:** *If the association owes tax when it files Form 1120-H, do not include the payment with the tax return. Instead, mail or deliver the payment with Form 8109 to a qualified depository or FRB, or use EFTPS, if applicable.*

## Estimated Tax, Alternative Minimum Tax, Investment Credit, and Jobs Credit

These items do not apply to homeowners associations electing to file Form 1120-H. However, a homeowners association that does **not** elect to file Form 1120-H may be required to make payments of estimated tax. Because the election is **not** made until the return is filed, Form 1120-H provides lines for estimated tax payments and the crediting of overpayments against estimated tax if payments or overpayments apply.

## Interest and Penalties

**Interest.**—Interest is charged on taxes paid late even if an extension of time to file is granted. Interest is also charged on penalties imposed for failure to file, negligence, fraud, gross valuation overstatements, and substantial understatement of tax from the due date (including extensions) to the date of payment. The interest charge is figured at a rate determined under section 6621.

**Penalty for late filing of return.**—In addition to losing the right to elect to file Form 1120-H, a homeowners association that does not file its tax return by the due date including extensions, may be penalized 5% of the unpaid tax for each month or part of a month the return is late, up to a maximum of 25% of the unpaid tax. The minimum penalty for a return that is more than 60 days late is the smaller of the tax due or \$100. The penalty will not be imposed if the association can show that the failure to file on time was due to reasonable cause. Associations that file late must attach a statement explaining the reasonable cause.

**Penalty for late payment of tax.**—An association that does not pay the tax when due may have to pay a penalty of 1/2 of 1% of the unpaid tax for each month or part of a month the tax is not paid, up to a maximum of 25% of the unpaid tax. The penalty will not be imposed if the association can show that the failure to pay on time was due to reasonable cause.

**Other penalties.**—Other penalties can be imposed for negligence, substantial understatement of tax, and fraud. See sections 6662 and 6663.

## Other Forms and Statements That May Be Required

The association may have to file any of the following:

**Form W-2**, Wage and Tax Statement.

**Form W-3**, Transmittal of Wage and Tax Statements.

**Form 940 or Form 940-EZ**, Employer's Annual Federal Unemployment (FUTA) Tax Return. The association may be liable for FUTA tax and may have to file Form 940 or Form 940-EZ if it paid wages of \$1,500 or more in any calendar quarter in the calendar year (or for the preceding calendar year) or one or more employees worked for the association for some part of a day in any calendar year (or the preceding calendar year).

**Form 941**, Employer's Quarterly Federal Tax Return. File this form quarterly to report income tax withheld and employer and employee social security and Medicare taxes.

**Form 945**, Annual Return of Withheld Federal Income Tax. File Form 945 to report income tax withheld from nonpayroll distributions or payments.

**Form 1098**, Mortgage Interest Statement. This form is used to report the receipt of \$600 or more of mortgage interest in the course of the association's trade or business during any calendar year.

**Forms 1099-A, B, DIV, INT, MISC, and S.** Use these information returns to report abandonments, acquisitions through foreclosure, proceeds from broker and barter exchange transactions, certain dividends and distributions, interest payments, medical and dental health care payments, miscellaneous income payments, nonemployee compensation, and proceeds from real estate transactions. Also use these returns to report amounts that were received as a nominee on behalf of another person.

For more information, see the instructions for Forms 1098, 1099, 5498, and W-2G.

**Note:** Every association must file Form 1099-MISC if, in the course of its trade or business, it makes payments of rents, commissions, or other fixed or determinable income (see section 6041) totaling \$600 or more to any one person during the calendar year.

**Form 8300**, Report of Cash Payments Over \$10,000 Received in a Trade or Business. File this form to report the receipt of more than \$10,000 in cash or foreign currency in one transaction or in a series of related transactions.

**Attachments.**—Attach **Form 4136**, Credit for Federal Tax Paid on Fuels, to Form 1120-H. Attach schedules in alphabetical order and other forms in numerical order after Form 4136.

Complete every applicable entry space on Form 1120-H. Do not write "See attached" instead of completing the entry spaces. If you need more space on the forms or schedules, attach separate sheets. Use the same size and format as on the printed forms. But show the totals on the printed forms. Attach these separate sheets after all the schedules and forms. Be sure to put the association's name and EIN on each sheet.

## Specific Instructions

**Period covered.**—File the 1996 return for calendar year 1996 and fiscal years that begin in 1996 and end in 1997. For a fiscal year, fill in the tax year space at the top of the form.

**Note:** The 1996 Form 1120-H may also be used if (1) the organization has a tax year of less than 12 months that begins and ends in 1997 and (2) the 1997 Form 1120-H is not available at the time the organization is required to file its return. However, the association must show its 1997 tax year on the 1996 Form 1120-H and must incorporate any tax law changes that are effective for tax years beginning after 1996.

**Address.**—Include the suite, room, or other unit number after the street address. If a pre-addressed label is used, include this information on the label.

If the Post Office does not deliver mail to the street address and the association has a P.O. box, show the box number instead of the street address.

**Note:** If a change in address occurs after the return is filed, the association can use **Form 8822**, Change of Address, to notify the IRS of the new address.

**Employer identification number (EIN).**—Show the correct EIN in the space provided. If the association does not have an EIN, it should apply for one on **Form SS-4**, Application for Employer Identification Number. Form SS-4 can be obtained at most IRS and Social Security Administration (SSA) offices, or by calling 1-800-TAX-FORM. If the association has not received its EIN by the time the return is due, write "Applied for" in the space for the EIN. See Pub. 583 for more information.

**Final return, change of address, or amended return.**—If the association ceases to exist, file Form 1120-H and check the "Final return" box at the top of the form. If the association has changed its address since it last filed a return, check the box for "Change of address."

To amend a previously filed Form 1120-H, file a corrected Form 1120-H and check the "Amended return" box at the top of the form.

**Item A—60% exempt function income test.**—At least 60% of the association's gross income for the tax year must consist of exempt function income (see **Definitions** on page 2).

**Item B—90% expenditure test.**—At least 90% of the association's expenditures for the tax year must consist of expenses to acquire, build, manage, and care for property. Include current and capital expenditures. Use the association's accounting method to figure the total.

Include:

1. Salary for an association manager or secretary.
2. Expenses for gardening, paving, street signs, security guards, and property taxes assessed on association property.
3. Current operating and capital expenditures for tennis courts, swimming pools, recreation halls, etc.
4. Replacement costs for common buildings, heating, air conditioning, elevators, etc.

Do not include expenditures for property that is not association property. Also, do not include investments or transfers of funds held to meet future costs. An example would be transfers to a sinking fund to replace a roof, even if the roof is association property.

**Item C.**—Enter the association's total expenditures for the tax year including those expenditures directly related to exempt function income. Use the association's accounting method to figure the entry for item C.

**Item D.**—Show any tax-exempt interest received or accrued. Include any exempt-interest dividend received as a shareholder in a mutual fund or other regulated investment company.

**Line 21—Tax credits.**—The association may qualify for the following tax credits:

*Foreign tax credit.* See **Form 1118**, Foreign Tax Credit—Corporations.

*Credit for fuel produced from a nonconventional source.* See section 29 for a definition of qualified fuels, provisions for figuring the credit, and other special rules.

*Alcohol fuel credit.* See **Form 6478**, Credit for Alcohol Used as Fuel, and section 40.

*Credit for increasing research activities.* See **Form 6765**, Credit for Increasing Research Activities, and section 41.

*Low-income housing credit.* See **Form 8586**, Low-Income Housing Credit, and section 42.

*Enhanced oil recovery credit.* See **Form 8830**, Enhanced Oil Recovery Credit, and section 43.

*Disabled access credit.* See **Form 8826**, Disabled Access Credit, and section 44.

*Qualified electric vehicle credit.* See **Form 8834**, Qualified Electric Vehicle Credit, and section 30.

*Renewable electricity production credit.* See **Form 8835**, Renewable Electricity Production Credit, and section 45.

Enter the total amount of credits on line 21 and attach the appropriate form(s).

**Line 22.**—If the association must recapture any of the low-income housing credit (or the qualified electric vehicle credit), include the amount of the recapture in the total for line 22. To the right of the entry space, write "LIH recapture" (or "QEV recapture") and the amount. See **Form 8611**, Recapture of Low-Income Housing Credit, and section 42(j) for more details. See Regulations section 1.30-1 for details on how to figure the recapture for the qualified electric vehicle credit.

**Backup withholding.**—If the association had income tax withheld from any payments it received, because, for example, it failed to give the payer its correct employer identification number, include this amount in the total for line 23g. This type of withholding is called "backup withholding." Show the amount withheld in the blank space in the right-hand column between lines 22 and 23g, and write "backup withholding."

