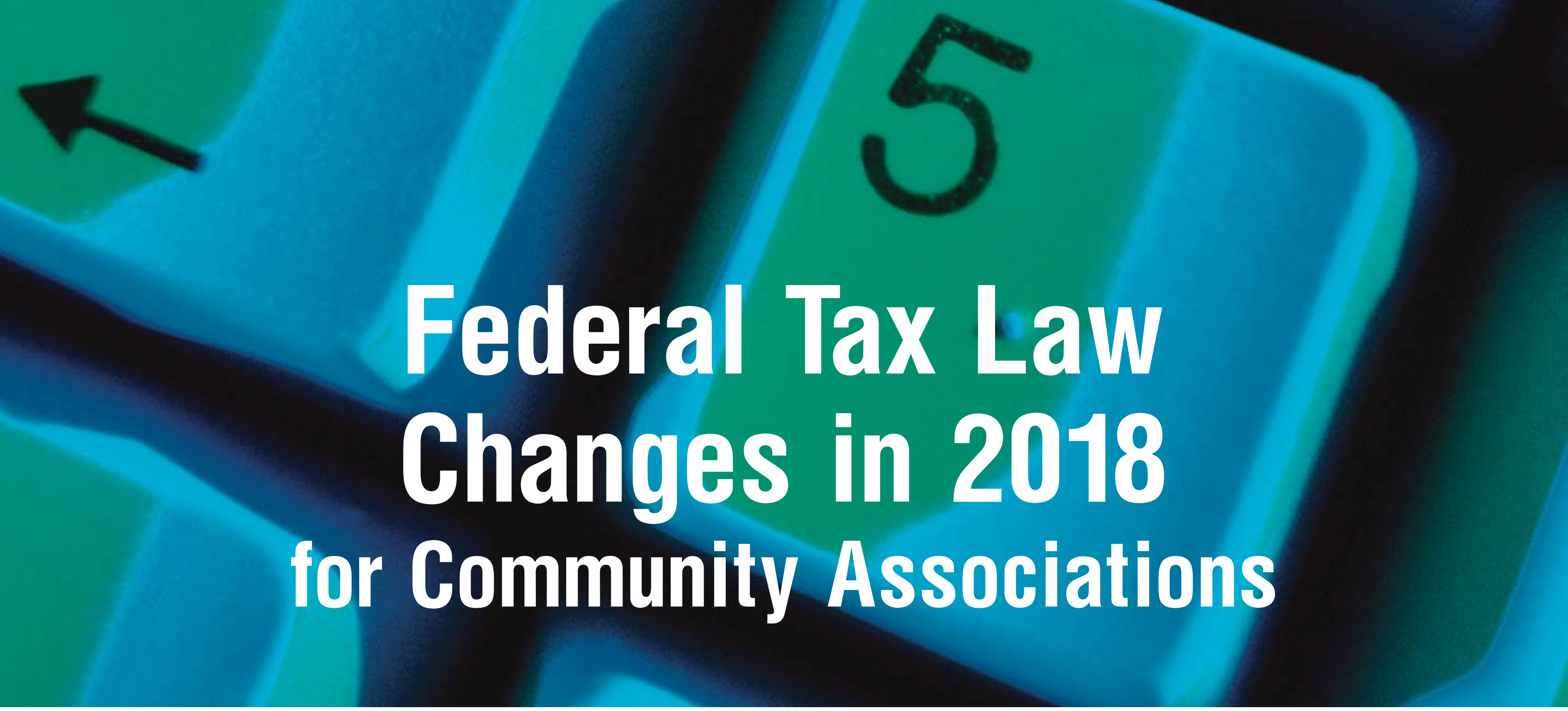

# Federal Tax Law Changes in 2018

## for Community Associations

Gayle Cagianut

Qualifying residential homeowners and condominium associations have the unique option in Federal taxation to file one of two tax forms. (This discussion does not include non-residential, timeshare, cooperatives, commercial or exempt associations). Community associations can file form 1120-H, U.S. Income Tax Return for Homeowners Associations or they can file form 1120, U.S. Corporation Income Tax Return. The determination as to which tax return to file is outside the scope of this analysis. However, it should be noted that if the association qualifies to file form 1120-H, this is an annual election and an association can change between the two tax returns each year.

The new Federal tax law makes no changes to form 1120-H. There is a flat tax rate on taxable income of 30%. That remains the same.

However, there is a Federal tax rate change when filing form 1120 effective January 1, 2018. From 2005 through 2017 there was a phased tax rate schedule as follows:

| Over | But not over | Tax is | Of amount over |
|---|---|---|---|
| $0 | $50,000 | 15% | $0 |
| $50,000 | $75,000 | $7,500 + 25% | $50,000 |
| $75,000 | $100,000 | 13,750 + 34% | $75,000 |
| $100,000 | $335,000 | $22,250 + 39% | $100,000 |
| $335,000 | $10,000,000 | $113,900 + 34% | $335,000 |
| $10,000,000 | $15,000,000 | $3,400,000 +35% | $10,000,000 |
| $15,000,000 | $18,333,333 | $5,150,000 + 38% | $15,000,000 |
| $18,333,333 | – | 35% | $0 |

It is common to hear that the U.S. corporate tax rate has been 35%. However, as noted above, that is not entirely true – and especially not for most community associations. In our experience, we have found that the majority of associations have taxable income under $50,000; thus, their tax rate has been 15%.

Under the new tax law there is a permanent flat corporate rate of 21%. Thus, many community associations will actually see an increase in their tax rate from 15% to 21% when they file their 2018 1120 tax returns.

Additionally, while we are not discussing the pros and cons of filing 1120 vs. 1120-H, it should be noted that filing 1120 is a much riskier tax option and requires much more diligent accounting and financial reporting. At times, the community association has been swayed into filing form 1120 due to the 15% tax differential. However, now that the tax rate difference is 9%, (21% vs. 30%) some associations may consider the cost versus benefits and conclude that the risk is no longer worthwhile for only a 9% tax savings.

For those associations filing form 1120, there are some additional tax law changes:

- Expensing of short-lived assets (rather than depreciating them). This is fully in effect through 2022, and then gradually phased out by 2026.
- Elimination of net operating loss carrybacks and limitations on carryforwards.
- Elimination of the corporate alternative minimum tax.

Quite frankly, most associations will not be affected by the above items. The large, high taxable income community associations should discuss all the new tax law ramifications with their tax preparer. However, most associations filing form 1120 are limited in their ability to use the above deductions. Non-membership and investment income is taxable. Tax regulations (IRC Section 277) do not allow for an offset to taxable income from membership losses, including depreciation deductions. Again, this is another reason that filing form 1120 is a more complex matter than form 1120-H.

**Summary of Impact on Community Associations**

- Form 1120-H – No Change
- Form 1120 – If taxable income under $50K, tax rate increase from 15% to 21%
- Form 1120 - If taxable income over $50K – would need analysis based on specifics