

MANAGING RESERVE EXPENDITURES

ALTERNATIVE NAME

WHY CAN'T THINGS JUST BREAK ACCORDING TO SCHEDULE?

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WHAT QUALIFIES AS A RESERVE EXPENDITURE

- 1. NEW CONSTRUCTION, POOLS, TENNIS COURTS, GAZEBOS, LAND IMPROVEMENTS ETC.
- 2. MAJOR REPAIRS AND REPLACEMENTS (CAPITAL IMPROVEMENTS).
- MOST ACCEPTED DEFINITION, IF THE EXPENDITURE EITHER EXTENDS THE LIFE OF AN ASSET OR INCREASES ITS OPERATING EFFICIENCY OR BOTH THEN IT QUALIFIES AS A CAPITAL IMPROVEMENT.
- MOST COMMON EXAMPLE GIVEN IS THAT OF ROOFING. A PATCH JOB ON A PORTION OF THE ROOF WOULD NOT EXTEND THE LIFE OF A ROOF WHERE A COMPLETE REPLACEMENT WOULD.

FINANCIAL CONSIDERATIONS

- DISBURSEMENTS FOR “MAJOR REPAIRS AND REPLACEMENTS” SHOULD BE ISSUED THROUGH THE RESERVE FUND BANK ACCOUNTS. IF NOT POSSIBLE TO DO, EITHER ISSUE A CHECK OR TRANSFER INTO THE OPERATING ACCOUNT, THIS SHOULD BE CLEARLY NOTED THAT THIS TRANSACTION IS FOR A SPECIFIC PROJECT AND NOT A GENERAL TRANSFER THAT COULD BE INTERPRETED AS GENERAL FUNDING TO THE OPERATING ACCOUNT.

FINANCIAL CONSIDERATIONS

- PAYMENTS FOR MAJOR IMPROVEMENTS FROM THE OPERATING ACCOUNT ARE NOT OPERATING EXPENSES
- THESE SHOULD BE SHOWN AS
- 1. TRANSFERS TO THE RESERVE THEN PAID OUT.
- 2. INTER-FUND RECEIVABLE AND REPAID AS SOON AS POSSIBLE.

LARGE REPAIRS

- ASSOCIATIONS SHOULD CONSIDER ESTABLISHING A “DEFERRED MAINTENANCE FUND”. THESE FUNDS ARE COLLECTED TO PROVIDE FUNDS FOR LARGE REPAIR BILLS THAT ARE NOT MAJOR REPAIRS AND REPLACEMENTS, PAINTING EXTERIOR OF THE BUILDING, REFINISH DECKING ETC.
- REPAIR BILLS REGARDLESS OF THE AMOUNT ARE REPAIR BILLS. THERE IS NO DOLLAR AMOUNT THAT DETERMINES IF AN ITEM IS A REPAIR OR CAPITAL IMPROVEMENT.

TAX CONSIDERATIONS

- CONTRIBUTIONS INTO RESERVES FOR MAJOR REPAIRS AND REPLACEMENTS ARE CONSIDERED CONTRIBUTED TO CAPITAL NOT MEMBERSHIP INCOME TO THE ASSOCIATION.
- CONVERSELY DISBURSEMENTS FOR IMPROVEMENTS ARE NOT DEDUCTIBLE AS MEMBERSHIP EXPENSES REGARDLESS OF THE FUND PAID OUT OF.

TAX CONSIDERATIONS

- JUST AS RESERVE FUNDING IS NOT CONSIDERED MEMBERSHIP INCOME TRANSFERS BACK TO THE OPERATING FUND COULD BE CONSIDERED TAXABLE.
- TO AVOID THIS AN INTER-FUND RECEIVABLE PAYABLE SHOULD BE ESTABLISHED FOR THE AMOUNTS TRANSFERRED BACK TO THE OPERATING FUND.
- THE NEED FOR THE TRANSFER COULD OFFSET ANY INCOME TAKEN BACK TO THE OPERATING FUND.

TAX CONSIDERATIONS

- REALITY CHECK: WE HAVE SEEN NUMEROUS ASSOCIATIONS WITH LARGE INTER-FUND RECEIVABLES DUE TO RESERVE FUND, MOST OF WHICH DO NOT HAVE THE ABILITY TO REPAY THE DEBT.
- MANY PROPERTY MANAGERS AND ASSOCIATIONS ARE UNAWARE OF THE EXISTANCE OR PROBLEMS THIS COULD CAUSE.
- PROPERTY MANAGERS NEED TO REVIEW THE BALANCE SHEET AND FOOTNOTES IN THE FINANCIAL STATEMENTS OF THE ASSOCIATIONS THEY REPRESENT. IF A SIGNIFICANT INTER-FUND BALANCE EXISTS A CONVERSATION NEEDS TO TAKE PLACE WITH THE ASSOCIATION AND ACCOUNTING FIRM TO PLAN FOR A RESOLUTION.

PLANNING

- IN YEARS WHERE THE OPERATING FUND HAS RESULTED IN A SIGNIFICANT SUPPLUS THE ASSOCIATION CAN ELECT UNDER REVENUE RULE 70-604 TO DEFER. THIS SHOULD BE VOTED UPON AT EVERY ANNUAL MEETING AND RATIFIED BY THE BOARD OF DIRECTORS.
- IN THE FOLLOWING YEAR THE FUNDS COULD BE USED TO PAY FOR LARGE REPAIR EXPENSES, SNOW FALL AND COULD GET TRANSFERRED INTO THE RESERVE FUND.
- COPY OF THE ELECTION FORM ATTACHED.

SALES TAX

- TRUE CAPITAL IMPROVEMENTS AND MAJOR REPAIRS AND REPLACEMENTS ARE NOT SUBJECT TO SALES TAX CHARGED BY THE VENDOR. SEE ST 8 ATTACHED.
- EXCEPTIONS EXIST:
 - 1. INSTALLATION AND MONITORING OF SECURITY SYSTEMS ARE SUBJECT TO TAX.
 - 2. FLOOR COVERING ALWAYS TAXABLE.
 - 3. SEE STATE OF NJ DIVISION OF TAXATION PUBLICATION LIST AT:
 - <http://www.state.nj.us/treasury/taxation/pubs.shtml>

Association Resolution for Revenue Ruling 70-604 Election -
Excess Income Applied to the Following Year's Assessments

RESOLUTION OF THE _____ ASSOCIATION

RE: EXCESS INCOME APPLIED TO THE FOLLOWING YEAR'S ASSESSMENTS - REVENUE RULING 70-604

WHEREAS, the _____ Association is a non profit, mutual benefit corporation duly organized and existing under the laws of the State of _____

and
WHEREAS, the members desire that the corporation shall act in full accordance with the rulings and regulations of the Internal Revenue Service;

NOW, THEREFORE, the members hereby adopt the following resolution by and on behalf of the _____ Association:

RESOLVED, that any excess of membership income over membership expenses for the year ended _____ shall be applied against the subsequent tax year member assessments as provided by IRS Revenue Ruling 70-604.

This resolution is adopted and made a part of the minutes of the meeting of _____

BY:

President

ATTESTED:

Secretary

State of New Jersey
DIVISION OF TAXATION

SALES TAX

FORM ST-8

CERTIFICATE OF EXEMPT
CAPITAL IMPROVEMENT

MAY BE ISSUED ONLY BY THE OWNER OF THE REAL PROPERTY
MAY NOT BE ISSUED FOR THE PURCHASE OF MATERIALS

A registered New Jersey contractor must collect the tax on the amount charged for labor and services under the contract unless the owner gives him a fully completed Certificate of Exempt Capital Improvement.

To be completed by both owner of real property and contractor, and retained by contractor. Read instructions on back of this certificate. Do not send this form to the Division of Taxation.

(Name of Contractor) _____
(Address of Contractor) _____
(Contractor's New Jersey Certificate of Authority Number) _____

THE FOLLOWING INFORMATION MUST BE FURNISHED:

*The nature of the contract is as follows (describe the exempt capital improvement to be made): _____

The address or location where work is to be performed: _____

TOTAL AMOUNT OF CONTRACT \$ _____

The undersigned hereby certifies that he is not required to pay sales and use tax with respect to charges for installation of tangible personal property, because the performance of the contract will result in an exempt capital improvement to real property. The undersigned purchaser hereby affirms (under the penalties for perjury and false swearing) that all of the information shown in this Certificate is true.

<p>CONTRACTOR'S CERTIFICATION</p> <p>I certify that all sales and use tax due has been or will be paid by the undersigned on purchases of materials incorporated or consumed in the performance of the contract described herein.</p> <p>(Signature of Contractor) _____ (Date) _____</p>	<p>PROPERTY OWNER'S SIGNATURE</p> <p>(Name of owner of real property) _____ (Address of owner of real property) _____ By _____ (Signature of owner, partner, officer of corporation, etc.)* _____ (Date) _____</p>
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Any person making representations on this certificate which are willfully false may be subject to such penalties as may be provided for by law.

Required

INSTRUCTIONS

TO THE PROPERTY OWNER: In cases where the contractor performs work which results in an exempt capital improvement to your house or land (real property), he may NOT charge you any sales tax if you issue to him a fully completed Certificate of Exempt Capital Improvement (Form ST-8). It is important to distinguish between an exempt capital improvement and a taxable capital improvement, repair or installation. If the fulfillment of a contract only maintains the existing value of the property, it is a repair and not a capital improvement. Where an improvement results in an increase in the capital value of the real property, it is generally considered that a capital improvement has been performed. (But see below list of taxable capital improvements.)

As an aid to determine whether a contract is for a repair to real property or a capital improvement to real property, the treatment of such transaction for income tax purposes under the Federal Internal Revenue Code may be used as a guide. If you have any doubt whether the work to be performed constitutes a repair or an exempt capital improvement, you should communicate with the Division of Taxation and describe in detail such work.

The following are examples of *exempt* capital improvements:

- New construction (other than taxable capital improvements listed below)
- In-ground swim pool, installation of
- New central air conditioner installation
- Painting a newly constructed house
- New hot water heater installation
- Patio, construction of
- New roof, installation of
- Porch enclosure, construction of
- New heating system installation
- Paneling, installation of
- Rewiring
- New electrical outlets installed
- New siding, installation of
- Garage, construction of
- Storm doors and windows, original or initial installation of

The following are examples of *taxable* capital improvements. This form cannot be issued for these services, which are subject to sales tax on and after October 1, 2006:

- Seeding, sodding, grass plugging of new lawns, planting trees, shrubs, hedges, plants, etc.
- Clearing and filling land associated with seeding, sodding, grass plugging of new lawns, or planting trees, shrubs, hedges, plants, etc., including tree/stump removal
- Installing carpeting and other flooring
- Installing a hard-wired security, burglar or fire alarm system

TO THE CONTRACTOR: If you enter into a contract to add to or improve real property by an exempt capital improvement (see examples above) and the property owner issues to you a properly completed Certificate of Exempt Capital Improvement, which you must retain, you should not collect sales tax from the property owner. (You are required to pay sales tax to your supplier on the purchase of the tangible personal property you purchase for use in performing the contract irrespective of whether the work constitutes a repair or a capital improvement.)

However, if you enter into a contract to repair, maintain, or service real or tangible personal property, or to install a taxable capital improvement, you must collect tax on the charge for labor or services performed in accordance with the contract.

Registered sellers who accept fully completed exemption certificates within 90 days subsequent to the date of sale are relieved of liability for the collection and payment of sales tax on the transactions covered by the exemption certificate. The following information must be obtained from a purchaser in order for the exemption certificate to be fully completed:

- Purchaser's name and address;
- Purchaser's type of business;
- Reason(s) for exemption;
- Purchaser's New Jersey tax identification number or, for a purchaser that is not registered in New Jersey, the Federal employer identification number or out-of-State registration number. Individual purchasers must include their driver's license number.
- If a paper exemption certificate is used (including tax), the signature of the purchaser.

The seller's name and address are not required and are not considered when determining if an exemption certificate is fully completed. A seller that enters data elements from paper into an electronic format is not required to retain the paper exemption certificate.

The seller may, therefore, accept this certificate as a basis for exempting sales to the signatory purchaser and is relieved of liability even if it is determined that the purchaser improperly claimed the exemption. If it is determined that the purchaser improperly claimed an exemption, the purchaser will be held liable for the nonpayment of the tax.

2. Retention of Certificates - Certificates must be retained by the seller for a period of not less than four years from the date of the last sale covered by the certificate. Certificates must be in the physical possession of the seller and available for inspection.

3. Acceptance of an exemption certificate in an audit situation - On and after October 1, 2011, if the seller either has not obtained an exemption certificate or the seller has obtained an incomplete exemption certificate, the seller has at least 120 days after the Division's request for substantiation of the claimed exemption to either:

1. Obtain a fully completed exemption certificate from the purchaser, taken in good faith, which, in an audit situation, means that the seller obtain a certificate claiming an exemption that:
 - (a) was statutorily available on the date of the transaction, and
 - (b) could be applicable to the item being purchased, and
 - (c) is reasonable for the purchaser's type of business; OR
2. Obtain other information establishing that the transaction was not subject to the tax.

If the seller obtains this information, the seller is relieved of any liability for the tax on the transaction unless it is discovered through the audit process that the seller had knowledge or had reason to know at the time such information was provided that the information relating to the exemption claimed was materially false or the seller otherwise knowingly participated in activity intended to purposefully evade the tax that is properly due on the transaction. The burden is on the Division to establish that the seller had knowledge or had reason to know at the time the information was provided that the information was materially false.

FOR MORE INFORMATION: Read publication S&U-6 (Sales Tax Exemption Administration) at <http://www.state.nj.us/treasury/taxation/pdf/pubs/sales/sug6.pdf>

DO NOT MAIL THIS FORM TO THE DIVISION OF TAXATION.
This form is to be completed by purchaser and given to and retained by seller.