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In This Issue:
Association Spotlight
HOA Pulse Articles
Web Articles

Safeguarding the Finances of your Association

Suggestions for Financial Control

With recent news media coverage on associations who appear to have lost funds due to actions by management companies, the question often becomes, how can an association prevent this from happening to them?

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Association Spotlight
Stone Curves Association
Tucson, Arizona

The Summer Rains Can Wreak Havoc On Your Communities!

Addressing and maintaining those areas that show key signs of drainage problems will keep your asphalt problems to a minimum.

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Tax Exempt Homeowners Associations

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New Cases Added

Aberdeen Owners v. Bristol Lakes Homeowners
Acacia On The Green Condominium Association, Inc. v. Gottlieb
Adams v. Newport Crest Homeowners Association

Stone Curves Association is a cohousing development located in central Tucson, Arizona.

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Association Spotlight

Stone Curves Association

2

[Stone Curves Association](#) is a cohousing development located in central Tucson, Arizona. It consists of 48 condominium units, but clearly represents a unique lifestyle. Stone Curves vision statement says it all – “A cohousing community that fosters diversity, respect for the environment, and harmony with each other and our greater community.” Stone Curves is a self-managed association.

For those not familiar with the concept of cohousing, Wikipedia defines it as “A type of intentional community composed of private homes supplemented by shared facilities. The community is planned, owned and managed by the residents – who also share activities which may include cooking, dining, child care, gardening, and governance of the community. Common facilities may include a kitchen, dining room, laundry, child care facilities, offices, internet access, guest rooms, and recreational features.”

The Common House is the focal point of the community. The Common House was beautifully and carefully designed to offer something for everyone to enjoy. On the ground floor is a library, a living room/TV room, office/computer room, a laundry room, a kids room, a sumptuous dining room, and a well-appointed kitchen, all surrounding a garden plaza. On the second floor of the Common House you'll see an exercise room, craft room, teen room, plus three guest bedrooms.

In addition, there is a lovely swimming pool and hot tub. The Association boasts a recently completed workshop/maintenance building and a children's playground complete with slump block tunnel and hillside slide and an enclosed dog run.

The design of the homes fits in well with Tucson's classic architectural style. Consistent with the Association's vision, employing the principals of permaculture the project includes a community vegetable garden, herb garden, fruit trees, a chicken enclosure, nine 1,000 gallon water cisterns that capture rare rainwater to use for irrigation and to minimize potable water usage.

And, if you're wondering where the “curves” in the Association's name comes from, you need look no further than the functional and artistic design of the walls surrounding and within the community.



With recent news media coverage on associations who appear to have lost funds due to actions by management companies, the question often becomes, how can an association prevent this from happening to them? For starters, it may be helpful to compare actions taken by an association who appears to be missing a significant amount of money from actions taken by an association who does not appear to be missing any funds.

Association 1 received a monthly balance sheet, income and expense statement from its management company. It never received any backup documentation to support the financial statement, such as the monthly bank statement. It did not receive a ledger showing the checks written on the Association's account. It also did not have a Board member who reviewed all invoices and signed all checks before the checks were sent. In fact, no Board member had any access to the Association's accounts. The management company had the only signing power for all of the Association's accounts (including checking, savings, and any reserve accounts).

In Association 2, the entire Board received a monthly balance sheet, income and expense statement from its management company. In addition, the treasurer of the Board received a copy of all of the backup documentation to support the income and expense statement, bank reconciliation, all invoices paid, and a copy of the check register. All checks required both the treasurer and the managing agent's signature. The management company had no signing authority for the reserve accounts of the Association. The Board member with signing power had full access to the bank records, as this person was a signer on the bank account.

Can you guess which association is missing funds? If you guessed Association 1, you are correct. Now, does that mean that every association that operates like Association 1 is going to lose funds? Obviously not. However, just like a person who shuts their garage door is less likely to get items stolen from their garage, an association that institutes tighter controls over its finances is less likely to see them taken because the opportunity is reduced or eliminated.

The following is a list of controls that an association should consider implementing to help safeguard its finances:

1. Make sure that your management company does not commingle your association funds of other associations. This type of accounting can make it very easy for a management company to "rob Peter to pay Paul". Your association needs to have its own separate bank accounts for all of its funds.
2. Obtain a full accounting of your funds every month. Make sure that you are not just receiving a statement of income and expenditures. You need to receive a balance sheet, a copy of your bank statement and related reconciliation, along with the documentation to show what checks have been written and to whom.



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3. Consider requiring that all checks be approved by a Board member before the check is written. Additionally, consider requiring that all checks be signed by at least one member of the Board. This prevents easy flow of funds out of the Association's accounts, and oversight of all checks written.
4. Make sure that a Board member has the ability of obtaining a copy of the bank statement directly, rather than just through the management company, or have the ability to review the bank account online. This prevents a management company from falsifying a bank statement.
5. Keep association reserve funds separate from the operating funds, and consider not having the management company as a signer on its reserve accounts.
6. Have your annual audit, review, or compilation performed by a Certified Public Accountant. Even though Arizona law only requires a compilation, at a minimum, a compilation is not much more than a financial statement. Therefore, the association should consider having an audit or review performed rather than just a compilation. Additionally, make sure that the service is performed by a Certified Public Accountant regulated by the Arizona State Board of Accountancy. (Note: Non-CPA accountants are not regulated by the Arizona State Board of Accountancy.)

Although the above steps cannot prevent all possible losses, they will help establish roadblocks to help protect the association's funds.

In summary, the Board of Directors needs to remember that it has a fiduciary duty to its members. Part of that fiduciary duty is the protection of the association's assets. Therefore, the Board should make sure that it is taking proactive steps to help protect the financial assets of the association.

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The Summer Rains Can Wreak Havoc On Your Communities

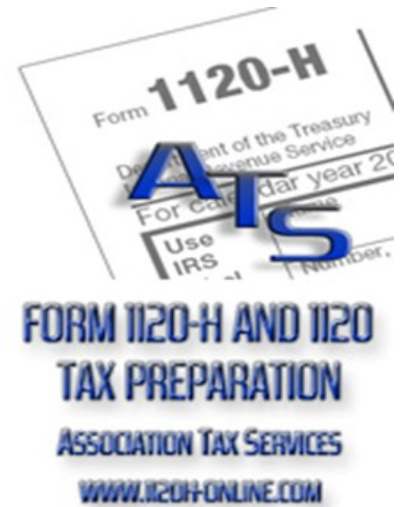
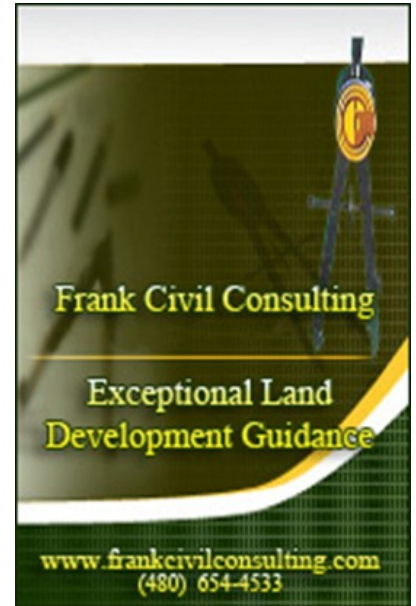
By: Michael Frank

Residing in Arizona for over 45 years, we are used to this time of year where the state receives increased moisture and humidity from the southeast and the Gulf of Mexico. This weather pattern is called "Monsoon" which is Spanish for "season". It's that "season" again and the state can expect to receive increased amounts of rain (especially in the late afternoon and early evening) as a result. That is why addressing drainage issues within your community are so critical to the life of your pavement. Because we are in a dryer climate, it is easy to often overlook the consequences that are created due to poor drainage in common and paved areas within your communities. Rarely do we see the ponding water or damage that result from rain events. Especially during this time of year, these problems come to light and sometimes in a dramatic way. Not only is standing water a nuisance to your residents, it is a major source of structural failure to your paved surfaces.

Water can and does percolate beneath asphalt. It penetrates between concrete and pavement. It can also be a major source of environmental issues like mosquitoes. Unfortunately, these items are generally ignored until it's too late and the damage has been done. Proper drainage off of pavement surfaces coupled with an ongoing maintenance plan will extend the life of your pavement for years. However, should the drainage concerns be overlooked, even with maintenance, your pavement life will suffer. Don't overlook the key signs of drainage problems within your community. They include staining of the pavement surface, silt and debris built up in spillways or catch basins, clogged drywells, clogged roof drains, landscape overtaking drainage release points within the community, and more.

Addressing and maintaining these areas will keep your "season" bright and your asphalt problems to a minimum. We encourage you to contact us to complete an onsite drainage inspection of your properties. The minor amount invested in this research could save your community substantially during "monsoon" time and throughout the year.

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Tax Exempt Homeowners Associations

By: Gary Porter, CPA

Most discussions of homeowners association taxation focus on the issue of Form 1120 versus Form 1120-H. But, that discussion ignores the small minority of associations that qualify as exempt associations under Internal Revenue Code (IRC) Section 501(c)(4). The primary benefits of qualification for exemption under this section are (a) the elimination of income taxes on interest income from reserves (as well as other exempt function income), and (b) the elimination of the tax risks that are inherent in Form 1120.

But, most associations will not qualify for exemption. For instance, all condominium associations are automatically excluded because the maintenance of the exterior of personal residences (the condominium unit) is one of the primary functions of the condominium association. This is a prohibited transaction under 501(c)(4), as it is considered to confer a private benefit to the unit owners. Townhome associations that provide exterior maintenance are likewise disqualified. In addition, those associations that are formed as cooperative housing corporations are also required to apply the mandatory requirements of Subchapter T as the code and may not qualify under 501(c)(4).

What this leaves as potentially qualifying associations are planned developments, whether residential, commercial, or industrial in nature. As long as they do not provide exterior maintenance of privately owned structures, such as residences or commercial buildings, these associations are not automatically excluded from consideration of qualification under IRC Section 501(c)(4).

However, Treasury Regulations Section 1.501(c)(4)-1 provides that a qualifying organization must not be organized or operated for profit, and must be operated exclusively for the promotion of social welfare. Revenue Ruling 74-99 further restricts qualification by establishing three requirements for qualification for complete tax exemption under IRC Section 501(c)(4):

- The common areas owned and/or maintained by the association must be for the use and enjoyment of the general public.
- The association must not conduct activities directed to the exterior maintenance of private residences.
- The association must serve a “community” that bears a reasonably recognizable relationship to an area ordinarily identified as a governmental subdivision or unit or district thereof.

Let’s examine what each of these requirements really means.

The first restriction above, the “public use and enjoyment” requirement, is known as the “public access” clause. An example of this type of an association is one that maintains common areas such as extensive slopes, fences, monument signs, and parks and does not have security patrol that restricts access. A variation of this is that there may be some restrictions such as limited access to pool and tennis court areas. So long as they are not substantial, significant restrictions, the association will still qualify.



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The second restriction above eliminates all condominium associations. It does not eliminate master associations that may contain condominium association subdivisions. Master associations that may include a small percentage of condominiums that are not part of a separate association could still qualify, but this is much more difficult.

The third restriction, “serving a community” does not mean that the association itself must BE a community; it must just serve a community. For non-gated associations that have sufficient public access, service to their surrounding community is virtually automatic. For associations that don’t have sufficient public access to those outside the association, there are still two ways to qualify; (1) the association covers the same geographic territory as a governmental unit. An example of this would be an association that has approximately the same geographical boundaries as a City or other governmental entity, (2) the association itself qualifies as a community. By definition, this generally must be a very large or very remote association in that it has such a large population that it would in and of itself qualify as a community even if there are restrictions on access. This is very rare and is not usually encountered in urban areas.

The exemption process requires a formal, extensive application. Qualifying is not automatic. However, even if the IRS denies the initial application, you can get a second chance at approval with the IRS Appeals Office. And, once an association is granted exemption by the IRS, it must file Form 990, which is far more complex than either Form 1120-H or Form 1120. Form 990 also requires an association to disclose key employee compensation and establish formal policies not required of other associations. In addition, both the application and any Form 990 tax returns are considered public documents and copies must be provided to any member of the public that makes a request.

In my opinion, the benefits for an association far outweigh any perceived negatives. The tax law is complex and generally requires assistance by a qualified professional having experience with tax exempt associations. There are some pitfalls and traps. My experience includes regaining exempt status for several associations who had their exempt status revoked by IRS because their advisors did not have the specialized knowledge or experience to properly argue their case with the IRS.

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Article Title	Article Summary	State
Homeowners need to keep eye on upcoming bills	Upcoming bills before the Legislature, are summarized for the State of Nevada	Nevada
Rochester Hills Residents, Tired of Recurring Power Outages, Ask City for Help	Residents continuously face outages and are asking the city for help	Michigan
Kids' lemonade stand curtailed by their homeowners association	Children with a lemonade stand cause HOA to file a complaint stating they are going against bylaws	Florida
Proposed Park, Disc Golf Course Angers Some Helotes Residents	Residents oppose new recreation area that would eliminate greenbelt.	Texas
New Push for a Condo Ombudsman	A bill is proposed to establish an ombudsman within the Department of Consumer Protection, for dealing with condo associations and their residents	Connecticut
What to watch for in a self-managed association	Self managed associations cause concern because the board responsibilities are greater and it is easier for errors to occur	Illinois
County fights for woman's civil rights	Local government is fighting HOA for the civil rights of an elderly woman who is struggling to keep her dog	Florida
Rob Samouce: New condominium directors have 90 days to sign certification papers	New board members have 90 days to provide a written certification and certificate of completion of education.	Florida
Legislation proposed to regulate homeowners associations	A bill being presented to the Indiana General Assembly would allow the Attorney General's office to regulate HOAs.	Indiana
Rental Forum: Tips on filing nuisance lawsuit in small claims court	Woman bothered by piano playing in home next to hers, wants to know the proper way to handle the problem.	Illinois
Senator wrote HOA bills while working for HOA	Senator has introduced seven bills to regulate HOAs after being employed by an HOA	Nevada
Condo fees aren't always fair, but necessary	Special assessments, common areas and board elections are the topics addressed in this Q & A	Florida
Las Vegas judge blocks foreclosure by HOA collection agency	A judge issued a temporary restraining order blocking a planned foreclosure of a home by a collection agency for an HOA	Nevada
Florida HOA says keep your kids inside	An HOA in Florida is in discussion to possibly ban children, in their subdivision, from playing outside.	Florida

Article Title	Article Summary	State
<u>HOA repair turns into long paperwork shuffle</u>	Challenge with a homeowner over assessments for fences and balconies, has caused years of unnecessary communications.	Nevada
<u>SVLA Could Dissolve</u>	Residents must vote to renew CC&Rs or terminate HOA.	California
<u>New River Valley neighbor needs intervention if she's hoarding animals</u>	Unfriendly neighbor has numerous cats which goes against rules of subdivision	Virginia
<u>Officials say Lewis Creek project will evolve, flourish</u>	Project to repair damage to Lewis Creek, has homeowners angry that the work has turned the area into a "war zone" destroying their oasis and lowering their home values.	North Carolina
<u>Failed asphalt mix a mess for Wellington residents</u>	Newly paved road causing damage to area properties	Florida
<u>Town Home Residents Shocked by Assessment</u>	Homeowners shocked by special assessment for yard care and snow removal.	Nebraska
<u>Court ruling: New laws may not apply to your condo or HOA</u>	Experts say to check governing documents for language that says state laws apply or that they are subject to amendment, otherwise they may not apply to your community.	Florida
<u>When does HOA enforcement become unreasonable?</u>	Amendments to the Planned Community and Condo Act are being proposed	North Carolina
<u>Yacht Club holding Town of Dillon in Contempt</u>	Condo association is claiming the town is disobeying court orders	Colorado