



TAX ALERT

SALES TAX UPDATE FOR COMMON INTEREST REALTY ASSOCIATIONS

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The Division of Taxation recently released additional interpretations of the new sales tax requirements that went into effect October 1, 2006. The following is a summary of what has been clarified and what still remains unclear. The details of these releases from the Division of Taxation can be found at www.state.nj.us/treasury/taxation in the “news” section. This update addresses the areas we believe to be particularly relevant to Common Interest Realty Associations (CIRAs). These areas include:

- ◆ **Membership fees and dues for health, fitness and athletic facilities**
- ◆ **Residential parking**
- ◆ **Security**
- ◆ **Landscaping**

In many cases we have provided the full text of these releases as the application to specific circumstances may not yet have been addressed. Taxpayers may consider taking positions based on the information provided to date and are encouraged to contact us regarding new developments.

Initiation Fees, Membership Fees and Dues

Many communities that have golf courses require a separate membership fee for those who choose to use the community’s golf course, health club or recreation facilities. This membership fee may or may not be in addition to greens fees. While greens fees are not subject to sales tax (fees for participatory sports are not subject to sales tax – see below) it appears that membership fees will be subject to tax. It is important to note that the new sales tax requirements are not applicable to membership fees assessed to new purchases in the community as an incident of ownership. The following is an excerpt from the NJ Division of Taxation release on September 29, 2006, “Tax Notes – Initiation Fees, Membership Fees and Dues.”

Frequently Asked Questions

1. *A private country club sells a share of stock in the corporation as a membership and/or initiation fee. The club charges annual dues to each member as well. Which fees are subject to tax?*

Since the stock purchase in this case is “in the nature of” an initiation fee because it is a condition precedent to membership, both fees are subject to tax.



2. *A condominium association levies an association fee on all owners of property in the complex for the upkeep of the grounds, which includes facilities such as a swimming pool, clubhouse with fitness equipment, tennis or basketball courts. All owners must pay the fee as a condition of ownership. Is the association fee a taxable membership fee?*

No. The association fee is a condition of ownership in the community and does not merely entitle members access to or use of the facilities.

3. *A social organization sells memberships which entitle its members to engage in dining and social activities while at the club. The organization also maintains a swimming pool or other health, fitness or sporting facility that is available to members for an additional membership fee. Which fees are subject to tax?*

The membership which allows access to only the dining and social facilities is not subject to tax; however, a separate fee to access the health, fitness or sporting facility is taxable. If both fees are not separately charged and stated to members, the entire charge is a taxable membership.

Based on question three above, it appears that if the health, fitness or sporting facility access fees are not assessed to every homeowner as incident to ownership then they are subject to sales tax. We understand that some organizations have proposed creating prepaid greens fees or a season pass in lieu of membership fees. It is unclear as to whether such an approach will be acceptable.

This same release also addressed additional information with respect to capital assessments, green fees and guest fees as shown below:

Capital Assessments

Separately stated charges assessed against members for the purpose of making improvements to the facility are not deemed to be membership dues or fees and thus, are not subject to sales tax.

Admissions Charges for Participation Sports

The law still contains an exemption for admissions charges to or for the use of any facility where the patron will be a participant in sporting activities. Admissions to bowling alleys, swimming pools, golf courses, baseball batting cages and pool halls remain exempt from tax. The taxability of such admission charges are unaffected by the new law. However, the new law does impose tax on membership fees or dues paid to the same type of facilities.

Guest Fees

A club or organization may allow limited or occasional use of the property or facilities to non-members. Fees charged to non-members such as guest fees are not membership fees and are not subject to tax; for example, a fee charged to a non-member to play a round of golf or a one day pass to a fitness center.

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Strategies

Consider the following strategies:

1. Establish increased greens fees (active participation admission charges) and reduce membership fees by a like amount. This will require careful budgeting as it will cause the source of income to be more variable than fixed.
2. Segregate and separately bill any portion of the membership fee that is allocable to amounts set aside for capital replacements. As such, assessments for capital improvements are not subject to sales tax.
3. Consider a community-wide fee to support the operation of the golf course.

Parking, Storing or Garaging a Motor Vehicle

Effective October 1, 2006 sales tax will be imposed on receipts from parking, storing or garaging a motor vehicle, excluding charges for residential or employee parking.

The sales tax applies to certain parking but does not apply to the sale of residential parking. For purposes of the exception for residential parking, the following is an excerpt from the New Jersey Division of Taxation's "Tax Notes – Parking, Storing and Garaging a Motor Vehicle," dated October 2, 2006.

“Residential parking” means parking provided to the occupants of a residence who park on the same premises that constitutes their primary residence;

“Same premises” means an area within the residence, an area adjacent to the residence, or any area owned or leased by the landlord, condominium association, or cooperative for the purpose of providing parking for its residents.

“Residence” means a single family home, a duplex, a condominium unit, cooperative unit, a townhouse unit, a school dormitory, an apartment or a mobile home used by a person or persons as a place of primary residence or adobe. “Residence” does not include a hotel, motel, a summer camp, a resort lodge or other dwellings of a temporary or transient nature.

Parking privileges provided for in a lease or in a separate writing between landlord and tenant, a condominium association and the owner of the unit, or between a cooperative and one of its members is nontaxable residential parking.

Parking charges paid to a homeowners’ association are not subject to sales tax provided that the parking facility is owned or leased and operated by the association; the association is comprised solely of owners or residents of the residential dwelling units; and the parking charges are paid by the members to the association. [emphasis added]

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For parking facilities that provide both residential and nonresidential parking, the operator or parking vendor must keep a record of the sale including the name of the resident, the residential address of the resident, and the amount of the sale in order to substantiate that the sale is for residential parking purposes.

The Division of Taxation has not clarified whether there is a sales tax on parking fees paid to a garage owner in a mixed use project where the owner is not the Association but may be a unit owner in the Association (i.e. if the garage is structured as a separate unit and then sold to a nonresident). It is possible that the intent is not to tax a resident for “on premises” parking although such parking is provided by an entity where the homeowner is not a unit owner. The actual language above is not specific in this circumstance and we hope that further clarification will be forthcoming.

Security

Effective October 1, 2006 sales tax will be imposed on investigation and security services. The Division of Taxation offered further clarification on October 12, 2006 when it issued “Tax Notes – Investigation and Security Services.” The following is an excerpt:

On and after October 1, 2006, P.L. 2006, c.44 imposes tax on “Investigation and Security Services.” See N.J.S.A. 54:32B-3(b)(11). For further clarification we are providing the following clarification issued by the Division of Taxation – Tax Notes – Investigation and Security Services.

The law defines “Investigation and Security Services” as:

- 1. Investigation and Detective Services, including detective agencies and private investigators, and fingerprint, polygraph; missing person tracing and skip tracing services;*
- 2. Security Guard and Patrol Services including bodyguard and personal protection, guard dog, guard, patrol, and security services;*
- 3. Armored Car Services; and*
- 4. Security Systems Services, including security, burglar and fire alarm installation, repair or monitoring services. [N.J.S.A. 54:32B-2(xx)]*

Many associations use third parties to provide personnel whom provide a variety of “front door” functions, such as doorman, security, valet, etc. There is currently no guidance as to whether these services constitute security.

Presumably, the determination as to whether a portion of services performed constitute “security” services is a factual one.

The provision regarding security services relates to outsourced services; employees providing security services are not subject to sales tax.

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Landscaping

Another area effected by the new tax law is landscaping service. It is important to remember that many services performed by a landscaper, such as mowing, have always been subject to sales tax. Previously, to the extent that a landscaper's work resulted in a capital improvement such as planting trees, grading, etc, such services were not subject to sales tax. The following excerpt is from the Division of Taxation's "Tax Notes - Landscaping Services" issued on September 29, 2006.

Capital Improvements Performed by Landscapers and Similar Businesses

Effective October 1, 2006, charges for certain defined landscaping services are subject to tax. See N.J.S.A. 54:32B-3(b) (2), as amended and P.L. 2006, c. 44. The tax is applicable whether a landscaper is hired by a property owner or by a general contractor.

Thus, the labor to install the following types of capital improvements to real property, which was previously exempt, is subject to 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. This also includes tree/stump removal. Any clearing and filling of land that is not associated with the installation of the above property is not subject to tax, for example, clearing land for a new development. Since the installation of structures remains exempt (see below), clearing and filling land performed in connection with the installation of structures remains exempt from tax.*

Other services which may be performed by a landscaper such as the installation of a new fence, low-voltage lighting, a pond, underground sprinkler system, hardscaping (i.e. installation of deck, paver patio, walkway, driveway, swimming pool deck, retaining walls, etc.), and similar structures, remain capital improvements to real property and are unaffected by the new law. Thus, the installation labor is still exempt from sales tax.

Repair and Maintenance Services

The Sales and Use Tax Act currently imposes tax on charges for maintaining, servicing and repairing real property. N.J.S.A. 54:32B-3(b)(4). Repair and maintenance services performed by landscapers are subject to tax under this provision. The following are examples of taxable repair and maintenance services performed by landscapers:

- ◆ *Lawn mowing*
- ◆ *Lawn reseeding*
- ◆ *Lawn fertilizing*

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- ◆ *Tree maintenance (trimming, pruning, spraying, bracing, cabling, grafting, coppicing, suckering and feeding)*
- ◆ *Weed/Insect control*
- ◆ *Soil aerating, sterilizing and mulching*

The law has not changed in this regard and these services remain subject to tax.

Collecting Tax from Customers

A contractor performing “landscaping services” must collect 7% sales tax on the gross sales receipt. However, at the option of the landscaper, the actual cost of materials used and upon which the landscaper paid tax may be separately stated on the invoice. The separate statement of the actual cost of materials would not be subject to the collection of tax. The law has not changed in this regard. Whenever a contractor performs a taxable service, if the customer is billed a lump sum amount, the entire receipt is taxable. If the contractor separately states the actual cost of materials from the taxable labor, the customer would only be charged tax on the labor portion.

Associations should ask landscapers to provide invoices that separately state material charges to reduce the tax due.

The changes outlined in this alert represent a general overview of the new laws. It is also important to remember that while the focus of this Alert has been on recent interpretations of the new laws by the Division of Taxation, these interpretations, by themselves, do not have the force of law. To the extent that a taxpayer can prove that these interpretations are inconsistent with the statutory underpinnings, alternative conclusions may be reached.

Look for future alerts from W&G as additional details and further clarification of these changes become available.

For clarification or more information on these and other tax matters, contact your W&G tax advisor at 732-846-3000.