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(L-R) PGA of America Chief Membership Officer, John Easterbrook, PGA of America CEO, Seth Waugh, PGA of America Past President, Paul Levy and PGA of America President, Suzy Whaley. (Photo by Montana Pritchard/PGA of America)

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Delving Deeper into the Details of Merger

Since the recent publication of "Understanding the Motivations of Merger" many additional questions have been asked regarding mergers of clubs and homeowners associations ("HOAs") across the country. Here are some answers to the most frequently asked questions regarding merger.

1) Is merger a "one size fits all" solution to all club's problems? No. Merger is a not a panacea. While a merger can achieve many positive results in a variety of situations, it will not solve all club's problems and is not appropriate for every club.

The facts and circumstances of each club and community must be reviewed independently and considered accordingly.

2) What factors contribute to making a club an ideal candidate for merger? Several factors affect a potential merger including the legal structure of the club and of the community, the requirements of membership (including but not limited to whether membership is mandatory for property owners in the community), the complexity of the governing documents of the club and/or the community, the demographics of the members and the status of the development (i.e., is the developer still involved in the project and is the real estate in the process of development or redevelopment?).

3) Does the club need to be a 501(c)(7) to merge? No. There is no requirement that a club be a 501(c)(7) in order to merge. While there are not a large number of "for profit" clubs comparatively located within residential communities, a "for profit" club could merge with the corresponding HOA.

Regardless of the tax status of the club, taxes paid after the merger will be determined on the basis of the tax status of the HOA. This is because the club as a legal entity ceases to exist upon the effective date of the merger and the HOA is only the surviving entity.

4) Will all mergers result in considerable tax savings? Most merged clubs will experience some tax savings from a merger. However, it must be emphasized that a decision to merge should not be based on tax savings alone. If a merger is undertaken solely for tax savings, the relevant taxing authorities could disregard the merger for tax purposes and any such savings could be lost.

Qualified club tax professionals should evaluate all potential tax savings to quantify the potential savings and compare those amounts to any costs associated with a merger.

5) What types of tax savings could there possibly be with a merger? In appropriate circumstances, a merger may result in real property, tangible property and sales tax savings post-merger.

Careful reading of the applicable tax laws and exemptions are essential to the analysis. For example, when non-resident memberships are offered by the merged HOA, some of the potential exemptions are eliminated.

6) How does the merger affect a member's property taxes? Clubs pay property taxes on the assessed value of the facilities owned by the club and members primarily pay for those taxes through their dues. The amount of taxes paid is determined by the local tax assessor based on the "assessed value" of those facilities.

Once a merger is complete, the property taxes formerly paid by the club will be paid either by the HOA, or if an exemption is available, by the owners of the individual lots and homes.

In Florida, for example, assuming a club's facilities are used exclusively for the benefit of property owners within the community, the merger would result in the HOA qualifying for a real property tax exemption for all of the club facilities.

In the first year post-merger, the real property taxes, which were paid by the club pre-merger would be allocated to the individual lots and homes within the community.

Then, in subsequent years, the assessed value of the lots and homes for tax purposes is recalculated on the basis of comparable sales of the lots and homes, rather than on the basis of the re-allocation of the club facilities.

In most instances, the net effect of this recalculation is the elimination of any net increase in real property taxes on the individual lots and homes as a direct result of the merger.

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7) How does the merger affect a member's sales taxes? Member's typically pay sales tax on amounts paid to clubs for dues. Depending on the particular state, sales tax ranges widely from approximately four percent to over nine percent in California, Washington and Louisiana.

In states such as Florida, which allow an exemption for the lowest category of "dues" paid to community associations rather than clubs, the savings on sales tax could be substantial.

These questions, as well as numerous others, must be answered for each particular club before making a final decision before effectuating a merger of a club with an HOA. As is the case with all legal and financial decisions of this magnitude, consult with applicable trusted advisors to provide the answers you need to make the best decision. BR

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