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Retirement Homes to Pay Higher Taxes

The IRS intends to collect on the billions of dollars of taxes that come from entrance fees retirement homes charge to the elderly who use their services. Some of these retirement homes are profit making organizations whereas others are non profits. For those that are profit making ones, they are taxed on their entrance fees themselves. For those that are non profit making, they are taxed on income derived from their entrance fees like fixed deposit interests.

Two cases in point are the Classic Residence by Hyatt which is a profit making retirement home and the Mission Ridge, a nonprofit retirement home. In both cases, the likely effect of taxation on their entrance fees and derived income will be an increase in their fees to the retirees who use the facilities. Generally, these homes can charge entrance fees anywhere from $250,000 to $2 million. This fee is generally refundable when the retirees leave the homes either through death or moving to another location.

It is not unusual for retirees to sell their homes and use the profits to pay for the entrance fees. When these retirees enter the community they usually start in an independent living arrangement where they enjoy living and nursing home care all within the same community.

The IRS claims that Classic Residence has been underpaying their taxes by $107 million over the years. On the other hand, Classic Residence themselves contend that their entrance fees should be classified as an interest free loan and thus should not be taxable. But if the IRS wins its claim then it would set a precedent on all other profit making retirement homes that number between 100 and 150 across the country.

In the case of Mission Ridge, their entrance fees are used as a form of collateral to back bonds. The IRS stand on this matter is that if the nonprofit retirement homes make more money in interest than it is due to pay on the bonds, then they should pay taxes on the profits from that interest. This is known as the �arbitrage rule�.

Depending on the state of the economy, the retirement homes are likely to make a profit in the interest on their entrance fees. If the IRS wins this ruling, bonds for nonprofit retirement homes would be classed as a higher risk than they are now and would carry higher interest rates. Furthermore, the calculations that need to be done to maintain the necessary arbitrage records for the IRS would be very extensive.

The Mission Ridge case is also another precedent-setting one that is likely to affect several hundred other nonprofit retirement homes in the US.