

Comments of the Employee Relocation Council on the Initial IRS Coordinated Issue Paper Draft-Relocation Home Purchases

December 3, 2004

ISSUES:

1. Whether amounts paid *by an employer* for relocation services *in acquiring, carrying, and disposing of an employee's house* are income to the employee and wages subject to withholding for federal income taxes, FICA and FUTA, where the employer does not *acquire* the economic benefits and burdens of ownership of the employee's home and the employer *claims the costs as* ordinary and necessary *expenses* under Internal Revenue Code § 162(a).
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2. Whether amounts paid *by an employer* for relocation services *in acquiring, carrying, and disposing of an employee's house* are income to the employee and wages subject to withholding for federal income taxes, FICA and FUTA, where the employer *acquires* the economic benefits and burdens of ownership of the employee's home and *some of the employer's expenses are treated as* capital expenditures under § 1221 *by the Internal Revenue Service*.
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COMMENT: *This could easily be expressed as only one issue, inasmuch as there is no disagreement that if the employer does not obtain the benefits and burdens of ownership all costs are wage income.*
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Generally, no amounts are paid to an employee in a relocation home purchase transaction, except for the purchase price of the home and the employee's share of pro-rated items that were paid by the employee in advance, such as prepaid taxes, mortgage payments, and insurance. All transaction costs, and carrying costs after the purchase, are borne directly by the employer, and payments are made directly to service providers such as real estate brokers, lenders, taxing jurisdictions, settlement attorneys, etc.

The statement of the issue also assumes that all costs will be capital if there is an acquisition of ownership by the employer. This is not the case. First, even under the IRS's longstanding position in Rev. Rul. 82-204, some of the costs are ordinary deductions (for example, the costs of maintaining the property during the ownership period, mortgage interest and taxes, and fees to the relocation company). Second, taxpayers have always disagreed with Rev. Rul. 82-204, believing that the homes are property held for sale in the ordinary course of a trade or business within the meaning of section 1221(1), and not capital assets. Thus, it would be perfectly appropriate for a taxpayer to exclude those costs from

the income of the employee, yet deduct them as an ordinary loss. That is an issue separate from whether the employer acquired the benefits and burdens of ownership. We suggest modifying the statement of the issue to allow for that argument.

CONCLUSIONS:

1. Where the employer does not *acquire* the economic benefits and burdens of ownership of the employee's home, the employer's expenses for relocation services *in acquiring, carrying, and disposing of the home* are ordinary and necessary under § 162(a), and amounts paid *for such relocation services* are income to the employee and wages subject to withholding for federal income tax, FICA and FUTA.
2. Where the employer *acquires* the economic benefits and burdens of ownership of the employee's home, amounts paid *in acquiring, carrying, and disposing of the home* are excluded from the employee's income and are not wages subject to withholding for federal income tax, FICA and FUTA. *Most such costs are capital expenditures, deductible only as a capital loss under section 1221.*

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COMMENT. The conclusions are restated to reflect the issue restatements. Note that conclusion #2 reflects the IRS position in Rev. Rul. 82-204, although as noted taxpayers have always disagreed with that position, and do not accept it.

FACTS:

Companies provide relocation services relating to the sale of an employee's home that generally fall into three categories:

"assigned sales," in which the employee enters into a contract with a third-party buyer to sell the home and then assigns the contract to the employer to complete the sale;

"regular sales," *(also commonly called "appraised value" sales)* in which the employee accepts a *purchase offer* from the employer, based on an appraised value, and *sells the house* to the employer. *The employee may retain legal title through the use of a "deed in blank", or may actually transfer title by deed to the employer;* and

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"amended value sales," which are similar to regular sales, except that the buyout amount is *increased* to reflect *the actual fair market value of the*

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house, if a purchase offer *is* received by the employee from a third-party buyer *that is higher than the employer's appraised value offer*.

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Although such terms as "regular," "assigned," or "amended value sales" are widely used, *and there are universally accepted definitions published by an industry trade group which are ordinarily followed*, it is *still* necessary to look beyond the label to the substance of the transaction in each case.

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COMMENT: The Employee Relocation Council has, since at least 1985, made available to the relocation industry standard definitions of each of the types of home purchase programs, and those definitions are universally accepted. Copies are attached to these comments. In addition, in 1985 ERC published a set of procedures to be followed in a properly structured amended value program, known as the "Eleven Key Elements and Procedures of an Amended Value Program," which are also universally accepted as the industry standard. A copy of the eleven key elements is also attached.

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In addition to referencing the standard definitions, the CIP would be sounder organizationally if it discussed "regular" sales first. The Appraised Value purchase is the most basic relocation home purchase program. Both Assigned Sales and Amended Value transactions are options that allow for marketing by the employee after an appraised value offer has been made by the employer. It is difficult to understand either of them without first having an understanding of the processes involved in an Appraised Value purchase. Consequently, the order of discussion should be modified to put "regular" (Appraised Value) purchases first.

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An employer relocation program may provide that the employee sells *his or her* home to the employer. Alternatively, the program may provide that the employee sells *his or her* home to a relocation firm that works for the employer, and then the employer or relocation services company sells the home to a third party.

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Sometimes, *this transaction is accomplished by a*, two-deed structure whereby one deed is used to transfer the home from the employee to the employer/relocation firm and another is used in the sale from the employer/relocation firm to a third party. The employer or relocation services company takes the title and then the title is transferred to the ultimate purchaser of the property.

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In contrast to the above "double deed process", many companies use the "deed in blank" process. *Although the home is still sold to the employer or relocation company*, the employee signs a deed-in-blank and the buyer's *name*, remains blank. When the employer or relocation firm sells the property and *that* transaction closes, the name of the purchaser is inserted on the deed. *Record* title to the property remains, *in the transferring employee's name until the closing*

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of the sale of the property to the ultimate purchaser, who takes title of the property. Although the employer or relocation firm is legally entitled to add its own name to the deed and take title at any time, it usually does not take title to the property unless the property will be in its inventory of unsold homes for a considerable period of time. In either a two-deed or blank deed transaction, after closing with the employee the employer or relocation management company ordinarily would, as the buyer, be responsible for all aspects of home ownership until the property is sold to the ultimate purchaser.

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COMMENT: The two immediately preceding paragraphs actually describe the same transaction. That is, the employer buys the employee's house, and assumes the benefits and burdens of ownership. Title may be passed either by using a blank deed (which is the traditional and, until recently, universally used procedure), or by a two-deed structure, which has been adopted by some companies in the last three years or so as a response to assertions by IRS agents that the blank deed was unacceptable after the Amdahl case.

Depending upon the facts of the particular transaction or program, the employer or relocation services company may also be entitled to benefits associated with ownership, such as appreciation in the property.

The legal documents of the relocation services program may not always reflect the actual course of dealings among the parties. The deed-in-blank process, in and of itself, is not the sole determining factor to be considered. This factor should be analyzed, along with the specific facts, documents and operation of the program to determine whether the employer/relocation services company or the employee bears the economic benefits and burdens of ownership.

Expenses incurred in connection with the sale of an employee's home may include carrying costs such as the mortgage, insurance, real estate taxes, utilities, repairs and maintenance, capital improvements, etc., until the home is sold, title transferred, and the deed recorded in the names of qualified, unrelated, third party purchasers. However, under an employer's relocation program, a relocation service company could incur these costs.

Expenses are also incurred by the employer or relocation service company (RSC) in the acquisition of an employee's home, such as appraisal fees, etc., and in the disposition of the home, such as broker's commissions, title fees, recordation fees, etc.

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That is, the employer or relocation service company incurs the usual and customary acquisition, carrying, and selling fees and costs that would be incurred in any real estate transaction.

Under *the most common* employer relocation program, *the* employer reimburses the relocation service company for losses incurred when the employee's home was sold to unrelated qualified third party buyers at a price less than the appraised value, and for *all* other *property related* expenses.

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COMMENT: The preceding paragraph describes a "cost-plus" relocation arrangement between employer and relocation company, which is the most common agreement for services. Some agreements, however, are "fixed fee," in which the relocation company charges the employer a specific amount per house (usually based upon a percentage of the house value), and itself bears all losses and costs. For example, federal government relocation programs are conducted under fixed fee contracts.

Employer's deductions for relocation services expenses may be reflected on the employer's Form 1120 as an ordinary and necessary expense deduction under § 162(a). For an ordinary expense, the deduction is often claimed on Form 1120, line 26, Other Deductions. Other employer's may claim *some of* the relocation services expenses as capital losses on Form 1120, Schedule D. Here, the expense may often be reported on the return as "Other Deductions - Employee Home Sales". *And, some employers may claim some of the expenses as ordinary losses.*

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Home relocation expenses determined to be capital expenses may be less advantageous for a corporation, because, generally, the expenses may only be deducted against capital gains, and many corporations may have no capital gains.

Employers and industry associations utilizing relocation services programs have requested consistent tax treatment for this issue. They have generally indicated that the basic tax treatment of home purchases is not at issue. That is, if the programs are properly structured bona fide purchases and sales, most costs are not taxable to employees as wages and income. Rather questions exist about the consistent treatment of *particular* relocation services program arrangements and procedures.

Employers and industry associations have indicated that, due to *Internal Revenue Service employment tax agents' interpretation of the Amdahl case as prohibiting its use*, they have already begun moving to eliminate the blank deed arrangement and implementing procedures so employers take title by deed in *most* home purchases transactions. *However, they have also requested that the IRS National Office rule on the issues, and specifically that it reiterate its thirty year acceptance of the use of blank deeds in these transactions.*

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COMMENT: The relocation industry believes that much of the analysis in Amdahl is erroneous, including its reliance on the use of the blank deed to find that the transactions were not true purchases and sales. Indeed, the government's own briefs in Amdahl took the position that the blank deed is not inconsistent with a completed sale. The move to two deeds has been prompted, rather, by employment tax agents adopting that part of the Amdahl opinion that relies upon the blank deed. The industry believes that there is nothing wrong with use of a blank deed in these transactions, in which all of the burdens and benefits of ownership are passed to the employer or relocation company, and would expect that many companies would return to its use if that use is deemed acceptable by the IRS. The substance of these transactions is the same with or without a blank deed, that is, a completed sale to the employer, who becomes the new owner. Use of two deeds significantly increases the costs to the employer of these transactions.

Further, this issue is currently on the Priority Guidance Plan for 2004-2005, and the National Office expects to issue a ruling prior to June 30, 2005.

DISCUSSION:

Internal Revenue Code section 61(a) defines "gross income" as all income from whatever source derived, including, but not limited to compensation for services, including fees, commissions and fringe benefits.

Section 82 of the Code provides generally that gross income includes, as compensation for services, "any amount received or accrued, directly or indirectly, by an individual as a payment for or reimbursement of expenses of moving from one residence to another residence which is attributable to employment or self-employment." Section 1.82-1(a)(2) of the regulations provides, in part, that amounts for moving expenses are considered received or accrued by an individual as reimbursement or payment whether received in the form of money, property, or services. Section 1.82-1(a)(3) provides, in part, that amounts are considered as being received or accrued whether received directly (paid or provided to an individual by an employer) or indirectly (paid to a third party on behalf of an individual by an employer).

Since its amendment, effective January 1, 1994, § 82 provides an exception for any fringe benefit that is excluded from gross income as a qualified moving expense reimbursement under § 132(a)(6). Section 132(g) defines "qualified moving expense reimbursement" as any amount received, directly or indirectly, by an individual from an employer as a payment for or reimbursement of expenses that would be deductible as moving expenses under § 217 if directly paid or incurred by the individual.

Just as with the exceptions from gross income contained in §§ 82 and 132, the Code excepts from the definition of “wages” for purposes of FICA, FUTA and federal income tax withholding, remuneration paid to or on behalf of an employee if (and to the extent that) at the time of the payment of such remuneration it is reasonable to believe¹ that a corresponding deduction is allowable to the employee under § 217, determined without regard to § 217(n). I.R.C. §§ 3121(a)(11), 3306(b)(9) and 3401(a)(15). Thus, various expenditures incurred must be examined in light of § 217 to determine the wage implications.

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Section 217(a) provides that a deduction shall be allowed for “moving expenses paid or incurred during the taxable year in connection with the commencement of work by the taxpayer as an employee or self-employed individual at a new principal place of work.” Although § 217(b) formerly allowed a deduction for qualified residence sale expenses such as real estate commissions, effective January 1, 1994, § 217(b) was amended to limit the definition of moving expenses to reasonable expenses incurred for moving goods and for traveling, including lodging. As a result, many expenditures that were deductible under § 217 are no longer deductible under this section (e.g., qualified reasonable residence sale expenses incident to the sale of a former residence, including, in particular, broker’s commissions). Since certain relocation expenditures clearly are no longer deductible by the individual under § 217, the reasonable belief exceptions discussed above do not apply here to except the amounts from “wages” under 3121(a)(11), 3306(b)(9) and 3401(a)(15).

Section 162(a)(1) allows a deduction for ordinary and necessary business expenses, including a reasonable allowance for salaries or other compensation for personal services actually rendered.

Section 1201 provides an alternative tax for corporations when sales or exchanges of capital assets produce a net capital gain.

Section 165(a) provides that a deduction is allowed for any loss sustained during the tax year that is not compensated for by insurance or otherwise.

Section 165(f) provides that losses from the sale or exchange of capital assets are allowed only to the extent allowed by sections 1211 and 1212.

Section 1221(a) defines the term "capital asset" as property held by a taxpayer (whether or not connected with his trade or business) but does not include: (1)

¹ Treas. Reg. § 31.3121(a)(11)-1(a) provides that the reasonable belief contemplated by § 3121(a)(11) may be based upon any evidence reasonably sufficient to induce such belief, even though such evidence may be insufficient upon closer examination to establish that a deduction is allowable under § 217. The reasonable belief shall be based on the application of § 217 and the regulations thereunder. Treas. Reg. §§ 31.3306(b)(9)-1(a) and 31.3401(a)(15)-1 contain similar provisions with respect to FUTA and federal income tax withholding, respectively.

stock in trade of the taxpayer..., (2) property, used in his trade or business, of a character subject to depreciation..., (3) a copyright, composition, letter..., (4) accounts or notes receivable acquired in the ordinary course of business and (5) a publication of the U.S. Government.

Sections 3101 and 3111 impose FICA tax equal to a prescribed percentage of the wages received by an employee or paid by an employer, respectively, with respect to employment. Section 3301 imposes FUTA tax on the total wages paid by the employer during the calendar year. Section 3402 requires that every employer withhold income tax from the payment of wages.

IRC §§3121(a), 3306(b), and 3401(a) provide that the term wages for the purpose of FICA taxes, unemployment taxes and income taxes includes all remuneration for employment. Treas. Reg. §31.3121(a)(11)-1(b) states that except as provided in paragraph (a) of the treasury regulations or in a numbered paragraph of section 3121(a), amounts paid to or on behalf of an employee for moving expenses are wages for the purpose of IRC §3121. There are parallel regulations for unemployment and income taxes. See Treas. Reg. §§3306(b)(9)-1 and 31.3401(a)(15)-1.

IRC §§3121(a)(11), 3306(b)(9), and 3401(a)(15) exclude from the definition of wages amounts paid to or on behalf of an employee if at the time of the payment of such remuneration, it is reasonable to believe that a corresponding deduction is allowable under IRC §217.

Treas. Reg. §31.3121(a)(11)-1(a) states that the reasonable belief contemplated by the statute may be based upon evidence reasonably sufficient to induce such belief, even though such evidence may be insufficient upon closer examination by the district director or the courts. The reasonable belief shall be based upon the application of section 217 and the regulations thereunder. Similar provisions are set forth in Treas. Reg. 31.3306(b)(9)-1(a) for employment taxes and Treas. Reg. §31.3401(a)(15)-1(a) for withheld income taxes.

The issues discussed in this paper are whether the sale of an employee's home through an employer's relocation program are, in substance, two sales - a sale by the employee to the employer, followed by a sale by the employer to a third-party buyer - or only one sale, from the employee to the third-party buyer.²

² A related question is whether the relocation company was acting as agent for the employer, for the employee, or acquiring and reselling the homes in its own right. Where RSC acted at the direction of the employer, was reimbursed for its costs, and was paid a fee, we conclude that RSC did not assume the benefits and burdens of ownership in the homes and was generally acting as employer's agent. (Note that this does not necessarily mean that employer acquired ownership of the homes; as discussed below, in certain circumstances, the employer itself may act, through RSC, as the employee's agent in completing the sale of the homes.) In this discussion, we will generally refer to the actions of "employer," even though they may actually be performed by RSC, acting on employer's behalf.

A sale occurs for federal tax purposes upon the transfer of the benefits and burdens of ownership. Grodt & McKay Realty, Inc. v. Commissioner, 77 TC 1221, 1237 (1981). Whether the benefits and burdens of ownership have been transferred is a question of fact which must be ascertained from the intention of the parties as evidenced by the written agreements read in the light of attending facts and circumstances. Id. See also Major Realty v. Commissioner, 749 F.2d 1483, 1486 (11th Cir. 1985); Commissioner v. Segall, 114 F.2d 706, 709-11 (6th Cir. 1940), cert. denied, 313 US 562 (1941); Yelencsics v. Commissioner, 74 TC 1513 (1980).

Among the factors considered by courts in determining when (or whether) the benefits and burdens of ownership are transferred are: (1) whether legal title passes; (2) how the parties treat the transaction; (3) whether an equity was acquired in the property; (4) whether the contract creates a present obligation to execute and deliver a deed and a present obligation on the purchaser to make payments; (5) whether the right of possession is vested in the purchaser; (6) which party pays the property taxes; (7) which party bears the risk of loss or damage to the property; and (8) which party receives the profits from the operation and sale of the property. Grodt & McKay, 77 TC at 1237-1238.

Although, as indicated, the passage of legal title is a significant factor, it is not a determinative one. Devoe v. Commissioner, 66 TC 904 (1976).³

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When the transfer of an employee's home occurs in connection with an employment relationship, amounts paid by the employer *to or on behalf of the employee* are *sometimes* characterized as additional compensation under § 61 of the Internal Revenue Code, rather than as proceeds from the sale of the home under § 1001.⁴ In other situations, however, the employer is treated for federal tax purposes as purchasing and reselling an employee's home,⁵ and this can be

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³ Compare, for example, Rev. Rul. 69-93, 1969-1 C.B. 139 (execution of contract to sell real estate in the future is not a realization event; sale occurs, and gain realized, when deed passes or when possession and benefits and burdens of ownership are, from a practical standpoint, transferred to the buyer), with Rev. Rul. 72-252, 1972 C.B. 193 (sale occurs, prior to deed transfer, when purchaser executes unconditional contract to purchase timberlands, acquires possession, and assumes other burdens and privileges of ownership).

⁴ See Bradley v. Commissioner, 39 TC 652 (1963), overruling Schairer v. Commissioner, 9 TC 549 (1947), aff'd, 324 F.2d 610 (4th Cir. 1963) (employer reimbursement for loss on home sale guarantee). See also Amdahl Corp. v. Commissioner, 108 TC 507 (1997); Keener v. Commissioner, 59 TC 302 (1972); Lull v. Commissioner, 51 TC 841 (1969), aff'd, 434 F.2d 615 (9th Cir. 1970); Karsten v. Commissioner, TC Memo. 1975-202.

⁵ See, e.g., Rev. Rul. 72-339, 1972-2 C.B. 31 (employee realizes gain on sale of residence to employer but does not realize income for real estate commission neither paid nor incurred). Cf. Rev. Rul. 82-204, 1982-2 C.B. 192 (homes purchased from employees under relocation plan are capital assets in the hands of the employer); Azar Nut v. Commissioner, 94 TC 455 (1990), aff'd, 931 F.2d 314 (5th Cir. 1991) (same).

the case even when a deed-in-blank procedure is used and the employee retains legal title until the sale to a third party.⁶

In Amdahl, 108 T.C. 507 (1997), the Tax Court examined relocation expenses. In that case the taxpayer paid the relocation expenses of its employees and provided financial assistance in connection with the sale of their residences. The employer contracted with a relocation services company to **purchase** the employees' residences. The RSC paid the employees for their equity in the homes based upon appraised values and paid the costs of maintaining the properties until a third party purchaser could be found. The employer reimbursed the relocation services company for its costs and paid the RSC a fee for its services. The employer also reimbursed the RSC for any losses if the property sold for less than the appraised value. Conversely, the relocation services company credited to the employer any gains resulting from sales at prices greater than the appraised values. Although not obligated to do so, the employer paid over any gains to the relocating employees. The employer deducted the amounts paid as expenses under I.R.C. § 162. The IRS disallowed the deduction, asserting that the amounts claimed were really capital in nature.

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In Amdahl the Tax Court held that the appraised value and assigned sale home purchase transactions undertaken by the RSC on behalf of Amdahl were not two sales but were merely sales by the employees to third party purchasers, with Amdahl assisting and bearing the costs. A principal factor cited by the Court in reaching this result was the failure to take title by deed in the first transaction. The Court held that, where the employer does not receive beneficial ownership of the relocating employee's residence and the employee continues to retain the benefits and burdens of ownership, the employer's relocation expenses are deductible under I.R.C. § 162(a) and are not capital expenditures under § 1221. The Court premised its conclusion on its findings that the taxpayer employer did not acquire legal or beneficial ownership of the residences and that the relocation program was one of several employee benefits provided to employees to encourage them to relocate. The last sentence of the Court's opinion states: "We find that the payments to the RSC conferred employee benefits to relocating employees and are deductible expenses under section 162(a)." The Court's opinion raised the issue of whether the payments to the RSC were subject to FICA and FUTA taxes and ITW.

In any given employer relocation **home purchase** program, the key question is whether, for a certain period of time, the economic burdens and benefits of ownership are transferred to the employer (or the employer's agent). The economic burdens and benefits of ownership are dependent upon the substance of the documents, facts and circumstances of the employer's relocation services

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⁶ See, e.g., Treas. Reg. § 1.6045-4(r), Example (2).

program. Applying this analysis to the present issues, we separately address the three categories of sales engaged in under typical employer relocation programs.

1. Assigned Sales

In an "assigned sale," *after the employer appraises the home and offers to buy it for the appraised value*, the employee offers the residence for sale, locates a buyer *other than the employer*, and negotiates and signs a contract for the sale of the residence. *At that point, the employee's side of the sales contract is* assigned to RSC, which, acting as agent for the employer, completes the sale.

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In such cases, the excess of the sales price over the *employer's original offer* is *not* paid to the employee *until closing of the sale to the outside buyer*. It appears that any interest acquired by the employer is subject to a binding pre-existing obligation to transfer the residence to the third-party buyer for the contract price. Although documents may describe the employee as offering the home for sale on behalf of RSC, and there may a period of time, after the employee vacates the home but prior to closing *with the outside buyer*, during which the employer may have the right of possession and be responsible for maintenance and certain other expenses, it does not appear that the employer bears *all* risk of loss or any possibility of gain on these transactions.⁷ In substance, the transaction is similar to "direct reimbursement" transactions, in which an employee sells a home and is simply reimbursed by the employer for closing costs and other expenses. Since the employer does not acquire either legal or beneficial ownership in the property in an assigned sale, we conclude that there is only one sale in such cases, from the employee to the third-party purchaser.⁸

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Thus, for "assigned sales", since the employer generally does not *acquire* the economic benefits and burdens of ownership, the employer's expenses for relocation *home purchase and sale* services are ordinary and necessary under § 162(a). In addition, amounts paid to an employee are income to the employee and wages subject to withholding for federal income tax, FICA and FUTA.

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COMMENT: We agree that an assigned sale results in taxable wages to the employee, but our analysis differs slightly. We are attaching a copy of the Employee Relocation Council submission to the Income Tax & Accounting Division of Chief Counsel in connection with the ruling project currently on the Priority Guidance Plan, which contains what we consider a more accurate description of an assigned sale transaction, and the reasons it is not treated as a purchase by the employer. We recommend the CIP adopt both the factual

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⁷ Another factor indicating that no sale to the employer occurs is *that*, if the assigned sale fell through, the employee would retain the power to dispose of the residence. See, e.g., *Amdahl*, 108 TC at 522-23.

⁸ This conclusion with respect to assigned sales appears to be consistent with the holding of the Tax Court in *Amdahl*, which involved an employee relocation program similar in many respects to the issues discussed here.

description and the analysis, and also that it refer to the standard definition of an Assigned Sale promulgated ERC in 1985, referred to earlier.

We also believe, as noted above, that the CIP would be improved by moving the discussion of Assigned Sales to follow the discussion of Appraised Value purchases. In order to fully understand an Assigned Sale, it is necessary to understand the basic Appraised Value transaction of which it is an option. Indeed, if the employee with an Assigned Sale option fails to find a buyer, the transaction will be completed as a garden variety Appraised Value employer purchase.

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2. Regular (*Appraised Value*) sales.

In a "regular sale," commonly referred to as an "Appraised Value" purchase in the relocation industry, the employee signs a contract to sell the house to the employer or a relocation company, based upon two or more appraisals. When the employee signs the contract, under most programs the employee becomes entitled to receive an "equity advance" from the employer, based on the appraised value of the home, less the amount of the mortgage and other liabilities, with certain adjustments. The equity advance is not a loan. It is an advance payment of all or a portion of that part of the purchase price representing the employee's equity in the home. It is not reflected by a promissory note. Any repayment obligation is entirely based upon the sale contract. The employee has no obligation or responsibility to repay this amount, unless the sale contract does not close (for example, because the employee breaches the agreement or is unable to deliver clear title).

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COMMENT: The advance payment discussed above is often confused with a bridge loan, which is also an advance of all or a part of the employee's equity but occurs before the employer and employee have signed a purchase contract. Such a pre-contract "equity advance" is in fact a loan, and is evidenced by a promissory note. Usually, the loan is interest-free. Section 1.7872-5T(c) of the regulations exempts such relocation bridge or mortgage loans from the imputed interest provisions.

Upon the later of the contract date or the date the employee vacates the property, the employer becomes entitled to possession, takes over responsibility for all damages, losses, insurance and expenses, including the mortgage and taxes, and is entitled to any gain on a subsequent sale. Although the employee may remain legally liable to the mortgage lender until the employer resells the

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house, the employer (through RSC) agrees to be personally liable to the employee for the mortgage.⁹

At the possession date, the employee delivers to the employer a blank deed to the property, as discussed above. Since the employer ordinarily does not take and record title in its own name, it is true that legal title is retained by the employee for a period of time. However, just as the employee has a right to the cash equity payment and mortgage liability relief, RSC has a present right to require the employee to transfer legal title, either to itself or to a party of its choosing, and is authorized to do so by completing and executing the deed in blank.^{10 11}

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After *the sale contract is signed*, the employer is *not* entitled to possession of the home *until* the agreed possession date, *which ordinarily occurs only when the employee vacates the premises and the employer pays any remaining equity over the advance payment made at contract signing. However, after the sale contract* is signed, with the proviso that possession may not be granted to a third-party purchaser prior to the possession date, RSC, in consultation with the employer, *usually* is authorized to list, offer for sale, and/or sell the residence for such price and on such terms and conditions as RSC may authorize.

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After *the sale contract is signed but before closing with the employer (that is, while the employee is still in possession)*, the employee would remain liable for any action that would result in a lien or encumbrance on the property, *and for all costs, expenses, damages, etc.* At closing, however, as noted above, the employer assumes the liability to pay or indemnify the employee with respect to

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⁹ See § 1.1001-2(a)(4)(ii) (amount realized by transferor of property includes amount of recourse liability secured by the property if another person agrees to pay the liability, whether or not transferor is in fact released from liability).

¹⁰ It is not clear whether the employee has the right to compel the employer to take title to the home, at least after some period of time. However, such a seller's right to specific performance of the contract may not be overly significant, given that an employee who complies with the agreement effectively has the present right to the equity payment, as well as relief from mortgage liability, taxes, and other costs of ownership.

¹¹ The fact that the employer has the ability to declare the contract void if title defects are discovered and not cured by the employee appears to be a standard provision that, in itself, would not prevent equitable ownership from shifting to the purchaser under the sales contract.

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debt secured by the property, assumes **all** risks of loss,¹² and agrees to pay for maintenance, repair, insurance, taxes, closing and selling costs.

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COMMENT: The statement in footnote 13 is incorrect. None of the referenced costs would be deducted from an equity payment. Just as in any real estate sale between unrelated persons, the buyer (the employer) is liable for the costs only after closing with the seller (the employee). The "buyout" date and the possession date are the same, that is, when the employee vacates the home. After signing a contract, and receiving an advance payment of all or part of his or her equity, the employee usually is still in possession of the home and responsible, as is any seller after signing of a contract but before closing, for the ordinary costs of owning and maintaining the home. But those costs would not affect the amount of equity. They are the normal carrying costs an owner incurs, and until closing with the employer the employee is still the owner.

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Most significant, in the case of a "regular sale", the employer, not the employee, will sustain any loss or benefit from any gain resulting from a differential between the amount of cash and debt relief furnished to the employee and the amount received by the employer from a sale to a third-party purchaser. Since, unlike an assigned sale, there is no **signed contract from a** purchaser for the home, the possibility of gain or loss to the employer exists, and the employer **will** in fact sustain losses on **virtually all** "regular sales."

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Summarizing, in a typical "regular sale" under an employer's relocation policy, *the employee signs a binding contract to sell the property to the employer. After closing of that sale (usually when the homeowner vacates the home), the homeowner retains legal title (subject to the employer/RSC's power of disposition and right to take legal title itself at any time), and transfers rights to possession, control, and appreciation in the value of the property. In return, the homeowner receives his or her equity (sometimes in the form of an advance payment that the homeowner has no personal liability to repay unless the sale fails to close); assumption of, or indemnification for, liability on the mortgage; and the employer's assumption of all of the costs and other burdens of ownership, including the risk that the property will depreciate in value. While the*

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¹² Even when a contract is silent regarding which party to a real estate sales contract bears the risk of loss, most jurisdictions place the risk of most types of loss on the purchaser, at least once possession has been transferred, under the doctrine of equitable conversion or the Uniform Vendor and Purchaser Risk Act. In the present discussion, the specificity of the buyout agreement with respect to risk of loss makes it unnecessary to look to local law to resolve this question.

¹⁴ This conclusion is based on the assumption that, once an employee accepts the *purchase* offer in a regular sale, the appraised-value *purchase* amount is final, and under no circumstances can the employee subsequently switch to either an assigned or amended-value sale.

employer may be motivated to acquire the benefits and burdens of ownership by a desire to facilitate employee relocations, this motivation is not incompatible with a conclusion that the employer acquired the property. See Rev. Ruls. 72-339 and 82-204; § 1.6045-4(r). Balancing all the factors, we conclude that an employee's acceptance of a *purchase offer from the employer, and the closing of that transaction*, in a "regular sale" shifts beneficial *and equitable* ownership to the employer, so that for federal tax purposes there is a sale from the employee to the employer (or its agent, RSC), followed by a separate sale from the employer/RSC to a third-party purchaser.¹⁴

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Thus, for "regular sales", where the employer *acquires* the economic benefits and burdens of ownership, *most of* the employer's expenses *incurred in purchasing and selling the home* are capital expenditures under § 1221. The amounts paid to an employee under the relocation program are excluded from the employee's income and are not wages subject to withholding for federal income tax, FICA and FUTA.

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COMMENT: Although we agree with the conclusion that the employer acquires ownership in a typical regular (Appraised Value) sale, and with much of the discussion of the burdens and benefits of ownership, both the factual discussion and the analysis suggest some confusion as to the actual structure of such transactions. We note that there is a standard definition of such transactions that is universally accepted within the relocation industry, which is attached. We have attempted to incorporate the missing elements of that definition into the discussion above.

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Most significantly, the CIP discussion refers to a "buyout" in a way that suggests confusion as to when a sale actually occurs. There is no "buyout" when the contract of sale is signed, unless the employee has already vacated the house and is ready to turn over possession. As in any real estate sale, that contract is executory until closing. That is, the seller (employee) has promised to sell, and the buyer (employer) has promised to buy, under the terms and conditions stated in the contract. The sale is not a completed "buyout" (a purchase and sale) until closing, usually when the employee vacates the house. Until that time, just as in any other real estate sale, the employee has the right to possession, and is obligated for all risks, expenses, losses, etc. The employer may be given the right to market and show the house, but has no other present rights to the home. The employee may be entitled at contract signing to an "equity advance." This is the equivalent of the downpayment in other real estate sales. It is usually a percentage (e.g. 95%) of the equity, and, as you correctly point out, is not a loan. It is simply an advance payment of a part of the purchase price. But it does not mean that the contract is closed. That event only happens when the employee vacates the house and turns over a deed and possession to the employer, and the employer pays any remaining equity to the employee and assumes liability for all costs, expenses, etc.

We recommend that the CIP discussion incorporate the standard definition we have attached, and the facts and analysis contained in our submission to IT & A, also attached.

3. Amended-value sales.

In terms of the extent to which the transaction shifts the incidents of ownership, amended-value sales appear to fall somewhere in between assigned sales and regular sales.

COMMENT: This is not true. The Amended Value Option is merely a way of determining a purchase price that more accurately reflects the actual fair market value of the house. It is helpful in overcoming employee suspicion of the accuracy of employer appraisals, and sometimes in reducing the employer's costs. But it results in precisely the same shift of incidents of ownership as does a regular transaction, and at exactly the same time. It is merely a pricing option in a regular, Appraised Value sale.

However, as implemented in a typical relocation program, the amended-value sales more closely resemble assigned sales than regular sales. Acceptance of a higher, amended value for the "buyout" amount is contingent on the employer entering into a binding sales contract with the prospective third-party purchaser.¹⁵

COMMENT: This is also not true. The employer's offer of a higher amount is in no way contingent on the employer being able to enter into a binding sales contract with a prospective third party purchaser. Once such a purchaser is identified, and the employer is satisfied that the offer is bona fide, the employer increases its offer to match the outside offer, and the employee accepts. At that point, the employer does not have, and may not be able to enter into, a signed contract with the outside buyer. The footnote is also erroneous for the same reason. Once the employee accepts the amended offer, the employee no longer has any interest in the disposition of the home.

In an amended-value sale, unlike a regular sale, the employee generally retains the right to approve any offer or counter-offer.

¹⁵ Where an employer is not able to enter into a binding contract, presumably in such a case the employee would retain control over disposition of the residence.

COMMENT: This statement is true only until the employee accepts the employer's amended offer. During the employee's own marketing period, as in any real estate sale, the employee may make counter offers, etc, in an attempt to obtain the best price for the home. Once he or she is satisfied with an offer, however, turns that offer over to the employer for evaluation, and accepts an amended purchase offer from the employer based upon that outside price, the employee has no further involvement in the outside sale, and any offers or counteroffers would be the sole province of the employer.

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As in the case of an assigned sale, when the third-party sale closes, the proceeds representing the increased "amended value" amount are distributed to the employee, not the employer or RSC.¹⁶

COMMENT: This is incorrect. Unlike an assigned sale, the employee is entitled to the entire proceeds of the sale, including the increased amended amount, at closing with the employer. That payment does not depend upon the closing of the employer's own sale. Later, if the outside sale does not close, or needs to be renegotiated (as sometimes happens), it is the employer who is responsible. This is because the outside sale is not one in which the employee is involved at all after he or she contracts to sell the house to the employer at the amended value. The outside sale is simply used as a pricing mechanism to determine the true market value of the property, and to give the employer a head start on finding a buyer of its own.

Thus, in the typical employer amended-value transactions, the employer does not appear to have any possibility of benefit from appreciation in the property, the employee retains significant control over its disposition, and the employer's loss exposure is limited.

COMMENT: As in a regular transaction, the employer has the benefit of any appreciation in the property after it enters into a binding contract with the employee. If it is unable to enter into a contract with the outside buyer found by the employee, or it is able to enter a contract but the sale falls through, the employer will benefit from any subsequent appreciation in the property. The employer is not required to contract with the buyer the employee identified. The employer may elect to sell to a different buyer, particularly if it gets a better offer. The employer also bears the burden of any loss, and all the burden of expense, damage, liability, etc.

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¹⁶ It also appears that homes in amended-value transactions are held in the employer's "inventory" for shorter periods of time than in the case of regular sales.

The employee does not retain any interest in or rights to disposition of the home. Once the employee accepts the employer's offer, the employee has no further rights of any kind concerning disposition of the home.

The employer hopes, by encouraging the employee to find a potential buyer, to limit its exposure to costs by reducing the holding period for the house. But its exposure to costs is still substantial, as is the risk that it will simply have paid the employee a higher price for the house and increase its own loss because it is unable to enter into or close a contract with the buyer the employee identified. While a goal of an amended value program is to reduce inventory time, that goal is not always obtained. Every house will still be in inventory for some period after the employee vacates it, and some for very substantial periods.

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Accordingly, we conclude that the amended-value sales, like the assigned sales, are in substance and form one sale, from the employee to the third-party buyer.¹⁷

Thus, for "amended-value sales", since the employer generally does not *acquire* the economic benefits and burdens of ownership, the employer's expenses for relocation services are ordinary and necessary under § 162(a). In addition, amounts paid to an employee are income to the employee and wages subject to withholding for federal income tax, FICA and FUTA

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COMMENT: This discussion does not accurately reflect a standard Amended Value program. As with the other programs discussed, we are attaching a standard definition that is universally accepted in the relocation industry. Moreover, since 1985 most companies have adopted and followed the "Eleven Key Elements and Procedures of an Amended Value Option," published by the Employee Relocation Council, which provide a structure for the amended value program that insures two bona fide, independent sale transactions. The eleven key elements are universally understood in the relocation industry to be the proper way to structure an amended value program. We are attaching a copy for your information. The CIP should reflect those standards.

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We believe the suggestion in footnote 17 that other programs, differently structured, could be a sale should apply to the standard, eleven key element amended value option we have described. It is the industry standard, and is the program being considered by the Office of Chief Counsel in its Priority Guidance Plan project. The CIP discussion should be modified to describe that program, incorporate the analysis in our submission to IT & A, and reach the result suggested by footnote 17.

¹⁷ We stress that this conclusion is based on the present discussion of amended-value transactions. Other employer relocation service programs, differently structured, could be a sale for federal tax purposes.