



Are Your Relocation Dollars Going To Uncle Sam?

How do you treat the reimbursement of closing costs when a relocating employee sells their home? If you just write a check to your employee for these costs, you are likely paying much more money (company, employee or both) and providing significantly less benefits than you should

In very simple terms, when the employer reimburses an employee the costs of selling the old home, that reimbursement is considered income to the employee and is subject to standard payroll withholdings. Then, depending on company policy the reimbursement is treated in one of two ways by the employer. It will gross-up the reimbursement and keep the employee "whole" after taxes. Or, it will reimburse the closing costs and withhold from that amount thus netting the employee as little as 60% of his/her actual out-of-pocket costs. Regardless of the method chosen by the employer, the Direct Reimbursement of old home closing costs is much more costly (either to the employer or employee) and provides much less benefit than alternative methods available to the employer.

The accompanying table compares the typical costs associated with four different methods of closing/reimbursing for the sale of an employee's home. The first method shown is the Direct Reimbursement of old home closing costs as described above, with the attendant "full gross-up" of that reimbursement so as to make the employee whole after tax. This Direct Reimbursement treatment generates more than 84% in increased costs to the employer due to the Gross-up of the reimbursement and additional company-paid Payroll Costs. And, the employee is still charged with the responsibility of finding an agent, listing the home, marketing the home, negotiating a contract and going to closing. So, the cost of Direct Reimbursement is 12.35% of the Sale Price with little or no benefit to the employee beyond expense reimbursement.

The following three methods of closing an employee's home sale avoid the additional payroll costs associated with Direct Reimbursement. Each is considered an "at risk" position for the company, i.e. the corporation owns the home for a period of time and is thus at risk in the transaction. Accordingly, the cost of closing the home in these three transactions is treated as a business expense as opposed to reimbursement of employee expenses. Thousands of companies employ one or more of these home sale methods, usually through a third party service company that acts as an agent of the corporation in the buying and selling of an employee's home.

In a typical Guaranteed Offer program, an offer value is arrived at, a pre-marketing time is required and one of two outcomes will occur. If an outside buyer is not found by the end of the required marketing period, the company buys the home from the employee for the offer amount and continues to market it as an Inventory property – the costs for this outcome are shown in the second column. If the home is sold during pre-marketing, then the employee's offer will be amended to the outside offer – this is called an Amended Value closing as shown in the third column.

A Guaranteed Offer program can be expensive. In the Inventory example the holding period is assumed at 90 days (from acquired date to close date) and the costs exceed 14% of the

Sale Price. The industry average approaches 20% of direct home sale costs for a Guaranteed Offer program. Most companies that move a relatively small number of employees shy away from a Guaranteed Offer program. They often will state that they are not in the real estate business and want no part of owning an employee's home for an indefinite period of time.

The Amended Value closing is much less expensive because the holding period is much shorter and the company is not exposed to a loss on sale. The true cost of a Guaranteed Offer program is computed as a combination of the Inventory and Amended Value closings. Using the industry Amended Value rate of 75%, i.e. 3 out of 4 homes are sold as Amended Values, yields a weighted average cost of a Guaranteed Offer program of 10.14% of the Sale Price.

In a Guaranteed Offer program, the employee receives the maximum benefit – i.e. they can sell their home and obtain the price they want but they still have the “safety net” of the guaranteed offer to fall back on.

The Buyer Value Option (BVO) program has become very popular in corporate American in recent years as it avoids the cost of lengthy ownership that is possible with a Guaranteed Offer program. With a BVO the employee markets the home until a buyer is secured. The company acquires the home and sells the home at the same value. Typical costs of the BVO program are shown in column four of the table with a total cost at about 8% of the Sale Price.

There are a myriad of issues arising out of the proper treatment of Amended Value and BVO programs, i.e. the risk of ownership, BVO fall through, tax treatments, audit issues, etc. Those issues should be investigated thoroughly before deciding to implement any type of home sale program.

In summary, a Direct Reimbursement program is one of the most expensive home sale programs. In addition, it offers the employee little or no services beyond expense reimbursement. If handled properly, the alternatives described here can save companies substantial amounts of money while providing significantly increased benefits to employees.

HOME SALE TRANSACTION COST COMPARISON

(Typical Transaction Costs for Southeastern U.S.)

	<i>DIRECT REIMBURSEMENT</i>	<i>INVENTORY CLOSING</i>	<i>AMENDED VALUE CLOSING</i>	<i>BUYER VALUE OPTION</i>
<i>Sale Price:</i>	\$ 200,000	\$ 200,000	\$ 200,000	\$ 200,000
<i>Acquisition Costs:</i>				
Pre Title	-	300	300	300
Appraisals	-	1,000	1,000	-
Inspections	-	500	500	-
<i>Total Acquisition Costs</i>	-	1,800	1,800	300
<i>Carrying Costs:</i>		(90 days)	(30 days)	(10 days)
Interest, Taxes, Insurance	-	4,500	1,500	500
Equity Advance Interest	-	900	300	100
Utilities	-	900	300	100
Maintenance	-	600	-	-
Repairs & Improvements	-	1,500	-	-
<i>Total Carrying Costs</i>	-	8,400	2,100	700
<i>Closing Costs:</i>				
Commission (6%)	12,000	12,000	12,000	12,000
Deed Stamps	450	450	450	450
Deed Preparation	100	100	100	100
Misc. Closing Costs	850	750	750	750
Capital Loss (3%)	-	6,000	-	-
<i>Total Closing Costs</i>	13,400	19,300	13,300	13,300
<i>Total Home Sale Cost:</i>	13,400	29,500	17,200	14,300
<i>Gross-Up (40% Employee Tax Rate):</i>	8,900	-	-	-
<i>Payroll Costs (FUTA, SUTA, FICA, WC)</i>	2,400	-	-	-
<i>Total Transaction Cost</i>	\$ 24,700	\$ 29,500	\$ 17,200	\$ 14,300
<i>% Of Sales Price:</i>	12.35%	14.75%	8.60%	7.15%

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