

Revenue Ruling 2005-74 Primacy Position

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On November 30, 2005, the IRS issued [Revenue Ruling 2005-74](#), the long awaited position on the taxability of home sale purchase transactions. This is the first formal IRS ruling on relocation home purchase programs since Revenue Ruling 72-339 over 30 years ago. Revenue Ruling 2005-74 provides guidance on how the IRS will tax home sale purchase programs in which an employer, in connection with a company-sponsored relocation, pays benefits.

Appraised Value and Amended Value Transactions

Revenue Ruling 2005-74 provides an endorsement of Appraised Value transactions and of Amended Value transactions that conform to the 11 key elements recommended by ERC. Under the Revenue Ruling, transactions crafted in this manner would be considered two separate independent sales for federal tax purposes and that the holding in *Amdahl v. Commissioner*, 105 T.C. 507 (1997) would not apply. The Revenue Ruling also makes clear that, at least for federal tax purposes, the use of a blank deed does not affect the favorable federal tax treatment of a properly structured program. The conclusions reached in the Revenue Ruling are based on the facts and circumstances of each situation and would apply to circumstances involving substantially similar home sale programs.

Contingent Transactions

The ruling includes a third fact pattern in which a home sale program will not be treated as being comprised of two separate independent sales, but rather as one sale from the transferring employee to the outside buyer; and where the costs paid would be considered taxable income to the transferring employee. In this third situation, the relocation management company is not required to amend its offer at the higher outside purchase price unless and until the relocation management company is able to enter into a sales contract with the outside buyer, the transferring employee retains the right to negotiate the relocation management company's sale to the outside buyer, and proceeds representing the higher amended value are paid to the transferring employee "only if and when" the sale between the relocation management company and the outside buyer closes. In the Revenue Ruling, the IRS describes the sale of the transferring employee to the relocation management company as being "contingent" upon the relocation management company entering into a contract with the outside buyer. While the facts and analysis of this unfavorable situation are not completely clear, the Revenue Ruling appears to suggest that the use of a contingent home sale process would not be viewed as favorable for federal tax purposes by the IRS with home sale costs paid by the employer being considered as taxable income to the transferring employee.

Buyer Value Option Transactions

Revenue Ruling 2005-74 does not specifically mention the Buyer Value Option (BVO). This is viewed as positive in that the IRS has adopted no definitive adverse conclusion regarding the BVO. In substance, a properly structured BVO program adhering to the ERC 11 key elements is essentially an Amended Value transaction without an initial offer. The analysis applicable to the Amended Value transactions would appear to apply to BVO transactions as well with the result being that a BVO transaction conforming to the ERC 11 key elements would be considered nontaxable, however it is not clear at this point what position IRS agents will take. For transactions (both BVO and Amended) containing the unfavorable elements discussed in Situation 3 of the Revenue Ruling, the IRS will likely treat those transactions as taxable to the transferred employee. It is therefore advisable that BVO programs be structured to be in compliance with the ERC 11 key elements and contain an eventual guaranteed appraised value buyout.

Blank Deed and Two-Deed Process

Revenue Ruling 2005-74 holds that the use of a blank deed will not cause an otherwise compliant program to be taxable. However, it should be noted that taking title remains a favorable factor in determining whether the benefits and burdens of ownership have been transferred under both the *Amdahl* and *Grodts & McKay Realty, Inc. v Commissioner*, 77 T.C. 1221 (1981). Consequently, a decision will need to be made whether the use of a two-deed process is advantageous, particularly in situations where a program is not fully in compliance with the ERC recommended 11 key elements. Additionally, at the state level there may still be reasons to use a two-deed process.

What to do?

Current home sale programs, particularly BVO programs, should be reviewed to ensure that the ERC 11 key elements are being followed. Programs that are not conforming need to be reevaluated and a decision made as to whether procedures being followed are defensible and worth the risk of a challenge from the IRS.

Programs found to be deficient should be modified to follow the ERC 11 key elements. The transferred employee should be paid equity upon the acquisition of the property, which in most programs occurs upon the later of the acceptance date or the date the employee has vacated the property. Payment of employee equity should not be delayed until the sale to the outside buyer has closed.

Consider adding a delayed buyout offer to BVO programs where the buyout offer is based on appraisals after some period of marketing. Contract with the transferring employee before contracting with the outside buyer and don't delay contracting with the employee until inspection contingencies are removed from the outside offer. View periodic sale fall-throughs as positive events and don't structure your program such that there is never a fall-through.

Summary

Revenue Ruling 2005-74 is a breakthrough for the relocation industry and corporate home purchase program. It creates a “safe harbor” for home purchase programs following the ERC 11 key elements. Primacy will continue to monitor this issue and will provide additional relevant information as it becomes available.

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Employee Relocation Council Eleven Key Elements

- Any employee ("EMPLOYEE") wishing to take advantage of the Amended Value Option who lists his/her home with a real estate broker must include a suitable exclusion clause in the listing agreement whereby the listing agreement is terminated upon the sale of the home to either the employer or the relocation company
- Under no circumstances should EMPLOYEE accept a down payment from any potential buyer
- Under no circumstances should EMPLOYEE sign an offer presented by any potential buyer
- EMPLOYEE enters into a binding contract ("Contract of Sale") with his/her employer or the relocation service company ("PURCHASER")
- After the execution of the Contract of Sale with PURCHASER and after EMPLOYEE has vacated the home, all of the burdens and benefits of ownership pass to the PURCHASER
- The Contract of Sale between EMPLOYEE and PURCHASER at the higher price is unconditional and not contingent on any event, including the potential buyer obtaining a mortgage commitment
- Neither EMPLOYEE nor the employer in the case of a relocation company transaction exercises any discretion over the subsequent sale of the home by the PURCHASER
- PURCHASER enters into a separate listing agreement with a real estate broker to assist with the resale of the property
- PURCHASER enters into a separate agreement to sell the home to a buyer
- PURCHASER arranges for the transfer of title to the buyer
- The purchase price eventually paid by the buyer has no effect on the purchase price paid to EMPLOYEE