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CASES NOTED

INCOME TAX—REIMBURSEMENT OF EMPLOYEE'S INCIDENTAL MOVING EXPENSES—AN INEQUALITY REAPPEARS IN THE CODE

On December 1, 1961, the petitioner was permanently transferred by his employer from California to Wyoming. The transfer was made solely at the behest of his employer. The petitioner attempted to buy a residence for his family in Wyoming, but due to a significant housing shortage, was unable to do so until December 20, 1961.¹ Therefore, the petitioner was forced to reside in a hotel while his family remained in California. During the interim he continued to maintain his family but was reimbursed by his employer *only* for his meals, lodging, and incidental expenses while at the hotel prior to his family's arrival. The petitioner did not include 718.54 dollars, the amount of such reimbursement, in his gross income. The Commissioner determined that the reimbursement was includable in gross income² and not deductible because it constituted personal living expenses.³ On petition to the Tax Court, *held*, for petitioner: where the move was *solely* at the behest of and *primarily* for the benefit of the employer and the temporary expenditures were outside the control of the taxpayer, reimbursements for temporary living costs at the new job site were not compensatory in nature and are excluded from gross income. *Homer H. Starr*, 46 T.C. No. 78 (Sept. 26, 1966).⁴

The sixteenth amendment gives Congress the power to tax *income* "from whatever source derived . . ." ⁵ The term income has not, however, lent itself to an exact definition.⁶ In *Commissioner v. Smith*,⁷ the court in dealing with the issue of compensation for personal services stated:

1. The house was unavailable until January 20, 1962, and the petitioner and his family did not actually move in until January 29, 1962.

2. INT. REV. CODE OF 1954, § 61(a).

3. INT. REV. CODE OF 1954, § 262 provides: "Except as otherwise expressly provided . . . no deduction shall be allowed for personal, living, or family expenses."

4. This case was appealed to the Tenth Circuit Court of Appeals on December 27, 1967.

5. The statutory definition of gross income in § 61(a) of the 1954 Code provides that "gross income means all income from whatever source derived, including but not limited to the following items"

6. The Supreme Court made an early but futile attempt to provide an all inclusive definition of income in *Eisner v. Macomber*, 252 U.S. 189, 207 (1920). In *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426 (1955) the Court refused to lend credence to the taxpayer's contention that the definition of income as used in *Eisner* required a narrow reading of section 61(a).

[I]n *Eisner* . . . [the term income was defined] as "the gain derived from capital, from labor, or from both combined." The Court was there endeavoring to determine whether the distribution of a corporate stock dividend constituted a realized gain to the stockholder [I]t was not meant to provide a touchstone to all future gross income questions.

Commissioner v. Glenshaw Glass Co., *supra* at 430.

7. 324 U.S. 177, 181 (1944).

"Section 22(a) [the forerunner of Section 61(a)] . . . is broad enough to include in taxable income any economic or financial benefit conferred on the employee as compensation, whatever the form or mode by which it is effected." In *Commissioner v. Glenshaw Glass Co.*,⁸ the court in determining that a "windfall" gain was within the scope of section 61(a), stated:

Congress applied no limitation as to the source of taxable receipts, nor restrictive labels as to their nature. And the Court has given a liberal construction to this broad phraseology in recognition of the intention of Congress to tax all gains except those specifically exempted [W]e cannot but ascribe content to the catchall provision [§ 22(a) of the 1939 Code] The importance of that phrase has been too frequently recognized . . . to say now that it adds nothing to the meaning of "gross income."⁹

Accordingly, the Service's position was that the taxpayer was denied exclusion of the reimbursement from income, and where the taxpayer included the reimbursement in income, his request for a deduction was disallowed.¹⁰ The court's position was uniform, whether the employee was new or old.¹¹

Revenue Ruling 54-429,¹² however, provided an exception to the *Smith*¹³ concept of income by excluding from income reimbursements received by an employee for moving expenses. This exclusion was limited to

8. *Supra* note 6.

9. *Commissioner v. Glenshaw Glass Co.*, *supra* note 6, at 430.

10. OLD EMPLOYEES:

In *Le Grand v. United States*, 105 F. Supp. 177 (N.D. Ohio 1952), the taxpayer's employer gave him one fourth of the purchase price of a house at his new job location. The court held that such payment was remuneration for his continued services and was not a gift as the taxpayer contended. In *Jesse S. Rinehart*, 18 T.C. 672 (1952), the employee was required to include in income money given to him by his employer as part payment for a house at his new location. The case was distinguished from *Otto Sorg Schairer*, *infra* note 11, in that *Rinehart* had suffered no loss on the sale of his old residence; whereas *Schairer's* payment was expressly provided to compensate him for any loss on the sale of his old residence. See also *H. Willis Nichols*, 13 T.C. 916 (1949), where the taxpayer was denied a deduction from income for the cost of moving his household effects at his own expense.

NEW EMPLOYEES:

In *Baxter D. McClain*, 2 B.T.A. 726 (1925), a new employee was denied a deduction for reimbursed moving (travel expenses and freight charges) expenses paid by his new employer. The employee in *York v. Commissioner*, 160 F.2d 385 (D.C. Cir. 1947), was denied a deduction for direct moving expenses incurred by him in moving to a new job location.

11. *Ibid.* But see *Otto Sorg Schairer*, 9 T.C. 549 (1947), *overruled by Harris W. Bradley*, 39 T.C. 652 (1963), *aff'd*, 324 F.2d 610 (4th Cir. 1963). The Tax Court concluded that the employer's payment to an existing employee for any loss he incurred on the sale of his residence was not income to the employee. The move was made for the benefit of the employer. The employee included the payment as part of the "amount realized" on the sale of the house and not as additional income.

12. 1954-2 CUM. BULL. 53.

13. *Supra* note 7.

payments received by an employee from his employer in moving himself and his family from one permanent station to another permanent station. Since the ruling required that the move be primarily for the employer's benefit, the Service concluded that such payments were not "compensatory in nature" and therefore not includable in income.¹⁴ The ruling did not, however, apply to expenses incurred by the employee after he reached his new station and was awaiting permanent facilities,¹⁵ nor did it apply to reimbursements received by an employee from a new employer.¹⁶

In *John E. Cavanagh*¹⁷ the Tax Court successfully extended the application of the exclusionary rule laid down in Revenue Ruling 54-429¹⁸ to include both reimbursed direct and indirect moving expenses. In *Cavanagh* the employee was required to wait a period of ten to fifteen days at his new job location for the delivery of his household effects. Under an agreement with his employer he was reimbursed for the amount of living costs he sustained which were in excess of the ordinary living expenses of his family while his household effects were in transit.¹⁹ The Tax Court excluded this payment from gross income, stating that reimbursements for *extraordinary* living expenses did not come within the purview of section 61(a).²⁰

14. [I]t is concluded that (1) amounts received by an employee from his employer representing allowances or reimbursements for moving himself, his immediate family, household goods and personal effects, in case of a transfer in the interest of his employer, from one official station to another for permanent duty, do not represent compensation within the meaning of section 22(a) [forerunner of section 61(a) of the 1954 Code] In any case in which the transfer is made primarily for the benefit of the employee, any allowance or reimbursement received by the employee is includable in his gross income.

Supra note 12, at 53.

Prior to this ruling, the only allowable exclusion for reimbursed moving expenses was in G.M.C. 18430, 1937-1 CUM. BULL. 137. An employee who was transferred by the State Department at the Government's convenience, could exclude from income the amount received by him as reimbursement for the cost of the moving expenses of himself and his family. *Contra*, I.T. 3022, XV-2 CUM. BULL. 76 (1936), requiring the inclusion in income of the cost of transporting dependents of Coast Guard personnel, the cost of which was paid by the Government; O.D. 1135, 5 CUM. BULL. 174 (1921), holding that costs of transportation paid by the government for dependents of army officers are in the nature of additional compensation.

15. This type of expense is generally termed an "incidental" or "nontransportational" expense in contrast to the term "direct" moving expense. The latter includes the cost of transporting the taxpayer and his family to the new location, moving furniture and other household effects from the old to the new residence, and the expenses incurred by the taxpayer and his family for meals and lodging while in transit to the new location. Examples of incidental expenses include meals and lodging at the new job location, prior house hunting trips, and expenses related to the sale of the taxpayer's old residence.

16. Although no mention was made of reimbursements received by a new employee in Rev. Rul. 54-429, *supra* note 12, the problem was soon decided in Rev. Rul. 55-140, 1955-1 CUM. BULL. 317. The Service took the position that such reimbursements must be included in income and were nondeductible as personal, living, or family expenses.

17. 36 T.C. 300 (1961).

18. *Supra* note 12.

19. *Supra* note 17, at 301.

20. INT. REV. CODE OF 1954. The Commissioner subsequently issued a *nonacquiescence*, 1962-2 CUM. BULL. 6. *But cf.* Harris W. Bradley, 39 T.C. 652 (1963), *aff'd*, 324 F.2d 610

Cavanagh also recognized the problem of determining when a taxpayer is a new or old employee.²¹ Although this issue is no longer pertinent in the area of direct moving expenses,²² it still appears in the area of incidental expenses.

A further attempt to extend Revenue Ruling 54-429²³ was made by the Tax Court in *Walter H. Mendel*.²⁴ The incidental moving expenses in excess of the reimbursement received from the employer were deducted from income. The court sustained the deduction by extending the decision of *Cavanagh* on the ground that reasonable amounts spent by the taxpayer in a transfer of job locations at the employer's request were not a personal expense and were therefore deductible as an ordinary and necessary business expense.²⁵ The Fourth Circuit reversed,²⁶ however, stating that while Revenue Ruling 54-429 excluded certain reimbursements from gross income, it did not make unreimbursed expenses deductible per se. The court concluded that the expenses constituted personal living expenses and were therefore not deductible.²⁷

(4th Cir. 1963) (reimbursement for loss on sale of residence); Paul Light, 30 P-H Tax Ct. Mem. 1611 (1961), *aff'd per curiam*, 310 F.2d 716 (5th Cir. 1962) (deduction denied for reimbursed expenses incurred at the new job location); Ernest Pederson, 46 T.C. No. 13 (May 2, 1966) (reimbursement included in income for expenses incurred in sale of old residence). For cases involving new employees see *Wells v. Commissioner*, 356 F.2d 922 (3d Cir. 1966) (loss incurred on a lease deposit reimbursed by the employer constituted taxable income); *Koons v. United States*, 315 F.2d 542 (9th Cir. 1963) (the fair market value of the additional compensation is the measure of such benefit); *United States v. Woodall*, 255 F.2d 370 (10th Cir. 1957) (reimbursement for actual travel and moving expenses included in income); *Willis B. Ferebee*, 39 T.C. 801 (1963) (reimbursement for direct and incidental moving expenses constituted taxable income); *Alan J. Vandermade*, 36 T.C. 607 (1961) (reimbursed moving expenses of "loaned" employee included in income).

21. In *Cavanagh*, *supra* note 17, the petitioner while living in Washington, D.C. accepted a position with a company located in California. The petitioner remained in Washington for a period of five weeks before moving to California. During such time, he engaged in business for his new employer. The Tax Court held that he was an old employee. This case should be contrasted with *Alan J. Vandermade*, *supra* note 20, where the petitioner went to work for a new employer on a temporary basis not exceeding six months. This arrangement was entered into between the petitioner's old and new employer. Both employers paid the petitioner a salary during the trial period. If the petitioner or the new employer were not satisfied, the petitioner was free to resume work for his old employer. When the petitioner decided to continue working for his new employer, reimbursements received for moving expenses from the new employer were required to be included in income. The court held that the petitioner, at the time of the second agreement, was a new employee. See also Judge Hoit's concurring opinion in *Willis B. Ferebee*, *supra* note 20, at 806, dealing with the new versus old distinction:

I feel that we should not compound the confusion already evident from the line of cases . . . deciding this case on what seems to me to be the unrealistic and arbitrary basis of oldness or newness of the employment involved We should look to the particular facts and circumstances of each case. . . . The fact that in the new employment cases the facts generally support a finding of taxable income does not mean that any payment to an "old" employee is tax free.

22. INT. REV. CODE OF 1954, § 217, applicable to taxpayers after December 31, 1963.

23. *Supra* note 12.

24. 41 T.C. 32 (1963).

25. INT. REV. CODE OF 1954, § 162(a) provides: "There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business. . . ."

26. *Commissioner v. Mendel*, 351 F.2d 580 (4th Cir. 1965).

27. INT. REV. CODE OF 1954, § 262.

The holding in *Mendel* is consistent with the view that since Congress intended the term income to be broadly construed,²⁸ the courts will not recognize a deduction absent a statutory provision permitting it.²⁹

Recently, in *England v. United States*,³⁰ the Seventh Circuit reversed a district court decision that excluded from income reimbursements received by an employee for certain *extraordinary* incidental moving expenses. The lower court had reasoned that since the transfer was solely at the request of the employer, any reasonable expenses incurred, whether direct or incidental, were really the cost of the employer. On appeal, the Commissioner contended that under Revenue Ruling 54-429³¹ reimbursements for incidental expenses were income to the taxpayer. The appellate court sustained the Commissioner's argument that Revenue Ruling 54-429 had correctly interpreted section 61(a) of the Code. They therefore included in income the incidental expense reimbursements and denied a deduction under the personal expense section of the Code.³² Furthermore, the court agreed with the Government that *Cavanagh* had incorrectly construed Revenue Ruling 54-429.

Subsequent to the *England* decision, the Commissioner issued Revenue Ruling 65-158,³³ which was designed to clarify his previous position toward reimbursed moving expenses.³⁴ The ruling listed various reimbursed nontransportational items,³⁵ which, although related to an employee's move, were nevertheless deemed additional compensation for services. Specifically citing the *England* case, the Commissioner noted that there were no substantial differences between expenses incurred while awaiting a permanent residence at the new job location and those for which advice had been requested. In both cases the expenses were "essentially personal . . . expenses of the employee, rather than business expenses of the employer."³⁶

In the instant case the Tax Court restricted the primary issue to one of determining the limit to which "interest or benefit" of the employer could be extended. Confronted with *England*,³⁷ the majority concluded

28. *Commissioner v. Jacobson*, 336 U.S. 28 (1949).

29. *Royer's, Inc. v. United States*, 265 F.2d 615, 617 (5th Cir. 1959).

30. 345 F.2d 414 (7th Cir. 1965).

31. *Supra* note 12.

32. *Supra* note 3.

33. 1965-1 CUM BULL. 34.

34. Rev. Rul. 54-429; *supra* note 12.

35. Specific examples of the items concerning which advice has been sought are: preliminary trips to the new place of employment to locate a suitable residence; the amount by which the net selling price of the employee's residence at the former place of employment fell below its appraised value; fee incurred in connection with the sale of that residence and the purchase of a different residence at the new place of employment; charges for connecting and disconnecting appliances and utilities; alteration and installment of rugs and draperies at the new residence; drivers and auto licenses required by the State to which the employee moved; and similar costs related to the move.

Supra note 33, at 34.

36. *Ibid.*

37. *Supra* note 30.

that the cases relied on by the Seventh Circuit were not directly on point. The court maintained that to refuse an exclusion from income of reimbursed incidental moving expenses *under any circumstances* did not coincide with present legislative intent³⁸ nor "the economic realities of the situation."³⁹ Under proper circumstances, which were shown in the instant case,

[T]he concept of the "interest of the employer" covers those costs which are actually incurred to effect the change in location, including those temporary living expenses at the new post of duty. In so holding, we do not feel that we have opened an avenue for unwarranted advantage.⁴⁰

The *Mendel*⁴¹ case was distinguished on the ground that to allow a deduction was not relevant to the problem of excluding reimbursed expenses from gross income.⁴²

With the addition of section 217, as provided by the 1964 Revenue Act,⁴³ a deduction is allowed for reasonable expenses paid by an employee in moving to a new job location. The deduction applies to both new and old employees. If the employee is reimbursed by his employer, he can still deduct his expenses if he includes in income the amount of the reimbursement. However, section 217 does not permit a deduction for incidental moving expenses. By statute, Congress attempted to equalize the moving expense dilemma. The *Starr* decision, which extended Revenue Ruling 54-429⁴⁴ to its logical conclusion, once again provided an inequality in the tax treatment of moving expenses.

38. The court took note of the Senate Report in § 217 of the 1954 Revenue Act. The report stated that although a deduction will be allowed for moving expenses under § 217 (limited to direct moving expenses)

[N]o inference should be drawn from this, however, that moving expense exclusions under existing law are necessarily limited to these . . . categories. . . . The question of whether the exclusion for *existing employees* extends beyond these . . . categories is left for *judicial interpretation*.

S. REP. NO. 830, 88th Cong., 2d Sess. 71-72 (1964). (Emphasis added.)

39. Today, due to our expanded economy, the great demand for skilled labor requires that they become a mobile force. By reimbursing his employees for all moving costs, the employer insures their presence in needed areas. Reimbursement plans presently in existence indicate that the costs are in reality the costs of the employer, not the employee. Homer H. Starr, ¶ 46.78 P-H T.C. at 46-533 (Sept. 26, 1966).

40. ¶ 46.78 P-H T.C. at 46-533.

41. *Supra* note 26.

42. In the instant case the employee was required to bear a double burden. He had to maintain his family in California and himself in Wyoming. The *Cavanagh* rationale of extraordinary expenses should apply in this situation. What could be a more extraordinary expense than having to maintain two residences because of an unrequested transfer?

43. INT. REV. CODE OF 1954. Section 217 now allows a new or old employee to exclude from income any reimbursements received for direct moving expenses. The instant tax court case extends the exclusion for incidental moving expenses only to reimbursed old employees. Therefore, the courts are faced with first determining whether an employee is new or old before allowing an exclusion for reimbursed incidental moving expenses.

44. *Supra* note 12.

On the basis of the instant case, an old employee who is reimbursed for incidental moving expenses enjoys a tax advantage over his co-worker who, when reimbursed for his incidental moving expenses, was a newly hired employee. The former can exclude his reimbursement from income, while the latter, under Revenue Ruling 65-158⁴⁵ and section 217, is not afforded this privilege. This inequality also pertains to a new or old employee who is not reimbursed for his incidental moving expenses. The Tax Court in *Starr* stated that the availability of a deduction was not relevant to the problem of excludability. Therefore, under the rationale of the instant case, it is most likely that a deduction for incidental moving expenses under section 217 will still be disallowed.

As the law now exists it provides: (1) an exclusion from income for reimbursed moving expenses received by an old employee; (2) an inclusion in income, with no deduction allowed, for reimbursed incidental moving expenses received by a new employee; (3) a denial of deduction by a new or old employee not reimbursed for incidental moving expenses.

Any attempt to resolve the problem of incidental reimbursed moving expenses requires that a variety of approaches be considered. First, the instant case could be overruled or a *nonacquiescence* issued by the Commissioner. This would, in effect, sustain the *England* decision and the Service's interpretation of section 61(a) in Revenue Ruling 65-158. Second, both the above ruling and the *England* case could be struck by legislation, and all moving expenses, whether direct or incidental, would be required to come within the purview of section 217 of the Code. This action, although providing equality in the moving expense area of the tax law, would impair the mobility of labor and ignore the "economic realities of the situation" so often alluded to in the instant case. The best solution, in the writer's opinion, would be the enactment of legislation specifically providing for an exclusion from income of reimbursed incidental moving expenses, and the allowance of a deduction for unreimbursed incidental moving expenses. Legislation to this effect was recently attempted, but Congress adjourned before a vote could be taken upon the bill.⁴⁶

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45. *Supra* note 33.

46. S. 3181, 89th Cong., 2d Sess. (1966). The bill would have allowed an exclusion from income of reimbursements received by an employee for expenses incurred for the following: a house hunting trip between the new and old job location, a thirty day limit for temporary living expenses at the new job location, expenses incidental to the sale or exchange of a taxpayer's old residence, expenses incidental to the purchase of a new residence at the new job location, and other miscellaneous expenses connected with the transfer limited to two weeks of the employee's weekly salary or one thousand dollars, whichever is smaller. The transfer must be to a place at least twenty miles from the employee's previous place of work, and the taxpayer must have been an employee of the employer for the preceding year.