

SELECTED AREAS OF COST

Chapter 61 - Relocation Costs

Authoritative Sources

[FAR 31.205-35](#) Relocation Costs

[FAR 31.205-46](#) Travel Costs

[Joint Travel Regulations](#) (JTR)

This chapter provides supplemental guidance on auditing relocation costs in accordance with FAR 31.205-35.

This chapter addresses the following topics:

61-1 Generation Information

61-2 General Audit Guidelines

61-2.1 Conditions for Allowability of Relocation

61-2.2 Unallowable Relocation Costs

61-3 Relocation Costs of Special Circumstances

61-3.1 Mass Relocations

61-3.2 State and Local Transfer Tax

61-3.3 Calculation of Tax Gross-up

61-1 General Information

The cost principle for allowability of relocation costs is FAR 31.205-35. It defines relocation costs as costs incident to the permanent change of duty assignment for a period of 12 months or more of an existing employee or upon recruitment of a new employee. Relocation costs are usually comprised of:

(1) cost of travel and transportation of household goods for the employee and immediate family members,

(2) cost of advance trips to find a permanent residence,

(3) closing costs (including state and local transfer taxes) incidental to sale of prior residence,

Chapter 61

- (4) expenses such as the costs of cancelling an unexpired lease and rental differential payments,
- (5) costs for acquisition of new house,
- (6) continuing mortgage interest at the old residence,
- (7) interest differential between the old and new mortgage and rental differential payments where the relocated employee retains ownership of a vacated home in the old location and rents at the new location, and
- (8) miscellaneous expenses.

Costs of travel for the employee and the employee's family to the new duty station and for house hunting trips include per diem costs which are also subject to FAR 31.205-46. (See 61-3 below.)

The costs of relocating an employee are generally substantial. Evaluation of the contractor's policies and procedures as well as employment agreements as to reasonableness and compliance with FAR requirements is an important step of any audit program when significant costs are charged to Government work. The allocation methods should be reviewed to determine that proper costs are being charged to benefiting contracts. In this regard, relocation costs should generally be charged to the receiving segment. Tests of individual personnel actions should be included to determine if established practices are being followed. When the contractor's policies and procedures are inadequate to control the incurrence of and accounting for unallowable costs, individual voucher testing must determine if the costs are allowable in accordance with FAR 31.205-35.

61-2 General Audit Guidelines

The contractor's relocation costs must be reasonable and allocable, and must meet the criteria listed in FAR 31.205-35(b) to be allowable. FAR 31.205-35(a) lists specifically allowable relocation costs and 31.205-35(c) lists expressly unallowable costs.

61-2.1 Conditions for Allowability of Relocation

Allowable relocation costs for an existing or new employee must involve a permanent change of duty assignment. Relocation assignments should normally last at least 12 months. When an undue number of such relocation assignments are terminated or completed in less than 12 months, the auditor should evaluate the reasons and recommend remedial action if appropriate. Relocation costs in excess of constructive temporary duty assignment costs should be questioned if the contractor should have known at the time of the assignment that it would not continue for a period of 12 months or more.

Failure to fulfill the 12-month requirement of a permanent change of duty assignment agreement for reasons within the employee's control requires the contractor to refund or

credit the relocation costs to the Government (FAR 31.205-35(d)). The auditor should encourage contractors to include recapture provisions in relocation agreements if this is not a practice. The provision should then be monitored by the auditor to assure that an adequate contractor follow-up system is in place to collect refunds when appropriate. The auditor should assure that a proper portion of any such refunds is credited to the Government. However, the contractor is required to make appropriate refunds to the Government whether or not the contractor recovers relocation payments from the employee.

FAR 31.205-35(f)(4), the recapture rule is not applicable to return relocation costs of a new employee who:

(1) is hired specifically for a long-term (at least 12 months) field project or contract assignment;

(2) is entitled to return relocation under the terms of his or her employment contract; and

(3) is not a permanent employee and is released from employment upon completion of the assignment for which he or she was hired.

This exception is applicable to only those employees who meet all three requirements. Accordingly, it is not applicable to the existing employees who are reassigned to field projects.

61-2.2 Reimbursement on a Lump-sum Basis

Reimbursement on a lump-sum basis is not limited to a maximum amount provided the costs are “adequately supported by data on the individual elements (e.g., transportation, lodging, and meals) comprising the build-up of the lump-sum amount to be paid based on the circumstances of the particular employee’s relocation” (FAR 31.205-35(b)(6)(i)). Contrastingly, miscellaneous costs as referenced in FAR 31.205-35(a)(5) are limited to a maximum lump-sum amount of \$5,000 (FAR 31.205-35(b)(5)).

When the lump-sum reimbursement approach is used, the amount is an estimate that is established prior to incurring the costs. Any subsequent adjustments to reflect the employee’s actual costs are unallowable (FAR 31.205-35(b)(6)(ii)). Accordingly, the auditor should ensure the contractor has established policies and procedures for estimating the lump-sum amount, and should question any amounts that are not adequately supported by data comprising the build-up and/or represent adjustments to reflect actual costs.

61-2.3 Unallowable Relocation Cost

Per FAR 31.205-35(c), unallowable relocation costs include:

(1) loss on the sale of a home;

(2) continuing mortgage principal (not interest) payments on the residence being sold;

(3) certain costs incident to the acquisition of a new home as shown in FAR 31.205-35(c)(2); and

(4) costs incident to furnishing or obtaining equity, nonequity, or lower-than-market-rate loans to employees.

In addition, FAR 31.205-35(d) requires the contractor to refund or credit contract costs for amounts previously charged to relocate an employee if the employee resigns for voluntary reasons within 12 months after relocation. Termination of employment for illness, disabling injury, or death is not generally within the employee's control and, therefore, would not serve as a basis for compelling contractors to refund or credit relocation costs to the Government.

61-3 Relocation Costs of Special Circumstances

61-3.1 Mass Relocations

Large scale or mass relocation of employees may result in abnormal total relocation costs. FAR 31.205-35(e) recognizes that questions may arise as to the reasonableness and allocability of the total amount, even though the items comprising the total are otherwise allowable. FAR 31.109, Advance Agreements, provides the means by which parameters of reasonableness and allocability of special or mass relocation may be agreed upon in advance between the Government and the contractor. In absence of an advance agreement, the provisions of FAR 31.2, should be used by the auditor for determination of reasonableness and allocability.

If the auditor learns that large scale employee relocations are to be made which may result in significant costs to prospective or existing Government contracts, the auditor should report the matter to the cognizant ACO with a recommendation for an advance agreement regarding the allowability of such costs. The recommendation should cite important areas for agreement such as:

(1) the segments of the company among which the costs are to be equitably distributed,

(2) the length of time over which the costs are to be amortized, and

(3) the employees eligible for reimbursement of relocation costs.

After coordination with the local ACO, the auditor should provide any needed information to other contracting officers who are concerned.

Depending on the circumstances, as covered in FAR 31.109, an advance agreement may be negotiated by the local ACO, the CACO, or a PCO. Be responsive to any

request from the designated Government negotiator for audit assistance in establishing the negotiation objective.

61-3.2 State and Local Transfer Tax

Some state or local governments may impose taxes on sales of homes. If the tax is imposed on the seller (employee) by law, it is considered a form of transfer tax which must be satisfied before the sale can be consummated and would qualify as closing costs described in FAR 31.205-35(a)(3). However, agreement to pay the tax not imposed on the seller by law, in the interest of making a sale or for other reasons, would not qualify as an item of closing costs and would be unallowable.

61-3.3 Calculation of Tax Gross-up

A common method for calculating the tax gross-up is:

Tax Gross-Up Factor	=	$x / 1.0 - x$
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(where x = employee's marginal tax rate)

For example, assume that the employee's marginal tax rate is 28 percent and the non-deductible moving expenses are \$50,000. A company would commonly compute the tax gross-up amount as follows:

$$\text{Tax gross-up factor} = 0.28 / (1.0 - 0.28) = 0.3888888$$

$$\text{Tax gross-up amount} = \$50,000 \times 0.3888888 = \$19,444.44$$

Simply increasing the employee's \$50,000 payment by the 28 percent marginal tax rate (i.e., \$14,000) will not make the employee whole. This is because the employee must also pay taxes on the additional \$14,000. The tax gross-up amount must be sufficient to pay not only the additional tax on the taxable relocation expenses, but the taxes on all amounts paid to the employee to reimburse the additional employee taxes. The formula shown above reaches that result. In essence, the formula summarizes the following computations:

Taxable Amount	Tax Paid (@ 28%)
\$50,000.00	\$14,000.00
\$14,000.00	\$3,920.00
\$3,920.00	\$1,097.60
\$1,097.60	\$307.33

Chapter 61

Taxable Amount	Tax Paid (@ 28%)
\$307.33	\$86.05
\$86.05	\$24.09
\$24.09	\$6.75
\$6.75	\$1.89
\$1.89	\$0.53
\$0.53	\$0.15
\$0.15	\$0.04
\$0.04	\$0.01
Total Tax	\$19,444.44