Schermerhorn v. Commissioner, 4 T.C. 652 (1945)

An employer's reimbursement to an employee for a loss incurred on the sale of the employee's home, necessitated by a job-related relocation, is considered part of the amount realized from the sale, not additional compensation.

Summary

The taxpayer, Schermerhorn, sold his home at a loss to relocate closer to his job at the request of his employer, RCA. RCA reimbursed him for the loss on the sale. The Tax Court addressed whether this reimbursement should be treated as additional compensation taxable as income, or as part of the amount realized from the sale of the home, affecting the calculation of capital gain or loss. The court held that the reimbursement was part of the amount realized, as it was directly tied to the sale and intended to make the employee whole, not to compensate for services. Therefore, it did not constitute taxable income.

Facts

The taxpayer was employed by RCA and owned a home in Bronxville, New York.
RCA requested that the taxpayer relocate closer to its laboratories in Princeton, New Jersey, requiring him to sell his home.
The taxpayer sold his home for $19,000, incurring a loss because his adjusted basis was $33,644.20.
RCA reimbursed the taxpayer for the $14,644.20 loss.
The reimbursement was explicitly intended to cover the loss from the home sale, ensuring the taxpayer was not financially disadvantaged by the relocation.

Procedural History

The Commissioner of Internal Revenue determined that the reimbursement was taxable income and assessed a deficiency.
The taxpayer petitioned the Tax Court for a redetermination of the deficiency.
The Tax Court reviewed the facts and arguments presented by both parties.

Issue(s)

Whether the reimbursement received by the taxpayer from RCA for the loss on the sale of his home should be treated as additional compensation taxable as income under Section 22(a) of the Internal Revenue Code, or as part of the amount realized from the sale of the home under Section 111.

Holding

No, because the reimbursement was directly related to the sale of the home and intended to make the taxpayer whole from the loss incurred due to the relocation, not to compensate him for his services.

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Court’s Reasoning

The court reasoned that the reimbursement was not intended as additional compensation. The amount paid would not have been provided had the taxpayer not sold his home at a loss. The agreement between the taxpayer and RCA was that if the taxpayer had to sell his home at a loss to change his residence to Princeton for the company’s convenience, RCA would reimburse him for the loss. The court stated that the payment by RCA was definitely a part of the sale transaction.
The court used a hypothetical involving insurance to illustrate its point: “Suppose that petitioner had some kind of a policy of insurance which insured him against a loss from the sale of his private residence and under such a policy collected $14,644.20 to reimburse him for such loss, could it be contended that petitioner would have to return such $14,644.20 as a part of his gross income? We think not. Such $14,-644.20 would merely be a restoration of his capital and would not be taxable income.”
The court distinguished the case from *Old Colony Trust Co. v. Commissioner* and *Levey v. Helvering*, where reimbursements for income taxes paid by employees were considered additional compensation. In those cases, the reimbursements were directly tied to the performance of services, unlike the reimbursement for the loss on the home sale.

Practical Implications

This case clarifies the tax treatment of employer reimbursements for losses incurred by employees due to required relocations.
It establishes that such reimbursements are generally treated as adjustments to the sale price of the asset (the home), rather than as taxable income.
Attorneys advising clients on relocation packages should ensure that reimbursement policies clearly articulate the intent to cover relocation-related losses, rather than providing supplemental compensation.
Later cases may distinguish *Schermerhorn* if the reimbursement is structured or intended as a bonus or incentive, rather than a direct offset for a loss on a home sale.
This case highlights the importance of documenting the specific purpose of any payments made by an employer to an employee, especially in the context of relocation.

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