UNDERSTANDING THE FINANCIAL RESPONSIBILITIES OF RELOCATION MANAGEMENT COMPANIES

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When people ask me what business we're in, I respond with the obvious answer: "We're in the employee relocation business. We help companies relocate their employees to new job locations." That usually gets an understanding nod. Then I add: "But we're also similar to a bank, in that we handle a lot of money on behalf of our clients." That answer elicits a quizzical look or even a double-take, "Did I hear right?"

In my nearly four decades in this business, I have found that the financial responsibilities of a relocation management company (or RMC) are the least understood of all its functions. For reasons discussed in this paper, I recommend that corporate clients pay much more attention to this responsibility.

In this paper, I will cover five topics that explain the depth of the challenges associated with an RMC's financial responsibilities.

1. The nature of the financial function of an RMC
2. How RMCs are different from other financial entities
3. The magnitude of the function relative to typical relocation activity
4. The risks involved for clients in the way that their funds are managed
5. The systems and processes that ensure the safety and security of client funds

WHAT ARE THE FINANCIAL RESPONSIBILITIES OF AN RMC?

THERE ARE TWO MAIN REASONS THAT CORPORATIONS OUTSOURCE EMPLOYEE RELOCATION.

1. The first is that relocation is a complicated process that involves the employee and their family completing many personal activities, such as selling a home, in which most employers do not want to be involved. Adding to that complexity is the fact that there is always pressure to get the relocation done quickly. Companies want their employees on the job, and at the new location, yesterday!

2. Second, to efficiently complete a relocation, payments must be made in a timely manner to a wide variety of suppliers, such as household goods movers, appraisers, and temporary housing companies. Most of these expenses are considered income to the employee and must be accounted for accordingly. Making these kinds of payments is not something that corporate payroll systems or expense management systems are designed to do.

In fact, it is very convenient for a corporate client to make larger, periodic payments to an RMC and have the RMC make and account for the specific payments to suppliers, as well as reimbursements to employees. To do this, the RMC must handle a substantial amount of funds on behalf of the client.

An experienced RMC is equipped to order authorized services, verify that they are successfully provided by qualified suppliers, and pay the suppliers on time. These expenses are typically referred to as “Direct Costs.” Often, they involve very large outlays, such as paying closing costs on a new home or paying for a substantial household goods shipment.

Importantly, an RMC must also reimburse the employee for authorized out-of-pocket expenses. Prompt payment of these expenses is very important to the employee who is trying to manage personal finances during a disruptive time in their life.

HOW IS RMC FINANCIAL MANAGEMENT DIFFERENT FROM OTHER FINANCIAL ENTITIES?

Unfortunately, it is not easy to define the legal and accounting boundaries for the financial responsibilities of an RMC. Certainly, an RMC has a high degree of financial responsibility to its clients, but it is not a legal fiduciary. An RMC is not a bank, a trust company, or an agent of the client — even though it shares many characteristics with each.

THERE ARE TWO FACTORS THAT COMPLICATE MATTERS.

1. First, while not being an agent, the RMC acts as a middleman. The RMC orders services in its own name to be provided to employees of corporate clients based on a Master Service Agreement (MSA) that obligates the corporate client to reimburse the RMC for such payments. If a client doesn't pay, then the RMC is at risk.

2. Second, like most businesses, RMCs account for their financial performance using fiscal year, general ledger accounting. However, employee relocations do not fall neatly into fiscal time periods. Rather, each relocation is a unique event with its own start date and end date.

Managing the direct costs of a relocation requires a different kind of accounting, generally referred to as "event" or "project" accounting. In other words, accounting for a relocation is similar to tracking the costs of a construction project from beginning to end, independent of fiscal years.

HOW MUCH CLIENT MONEY DOES THE TYPICAL RMC MANAGE?

Employee relocation is expensive. The amount an employer might pay for an individual move could range from as little as a $5,000 “lump sum” for a new college hire to over $200,000 for all expenses associated with an executive homeowner with a family. Most programs involve a wide mix of employees with different compensation levels and personal circumstances. On average, a company that moves 100 employees a year will likely spend around $50,000 per employee, or about $5 million a year, on direct costs for relocation.

Relocation is also cyclical. Most relocations occur during the six months from April through September. If, in our 100-move example, 75% of client funds are spent over these months, that equates to a spend of about $20,000 per day. Under a normal billing and payment schedule, at any one time, the RMC will be holding about $300,000 of the client’s cash.

A medium-sized RMC will handle 15,000 to 20,000 moves a year. If you do the math, you can see that, at any given time, the RMC could have $50 to $60 million of client funds on deposit. And, in the course of a year, handle over $1 billion of client money.

WHAT ARE THE CLIENT RISKS ASSOCIATED WITH AN RMC'S FINANCIAL RESPONSIBILITY?

There are two kinds of risk involved in an RMC meeting its financial responsibilities. The first is a **misuse of funds** which includes misappropriation, fraud, and human error. Fortunately, fraud is not an issue with relocation management companies. But accounting and service errors do occur. Payments can be made to or from the wrong accounts or for services not authorized by the client's relocation policy. All of that is potentially costly for the client.

The second risk is more subtle and more serious. It involves the **co-mingling of client funds with RMC corporate funds** and using client funds for the RMC's business purposes. Frankly, these large quantities of funds on hand can be a tempting source of financial resources to pay corporate expenses or make a corporate investment. "Why borrow money from a bank when you have access to these funds?"

In short, if there is not a clear distinction between client funds and RMC corporate funds, serious problems can arise. The RMC may not have the cash to pay the direct costs of an employee's relocation. Or worse, the RMC may not be able to return funds to the corporate client when requested, exposing both the client and the RMC to serious financial risk.

The question here is: "When does money paid by a client become the corporate funds of the RMC?" The answer is very simple: Only when funds can be classified as "revenue" to the RMC.

The vast majority of funds paid to an RMC by a client are for the purpose of paying the direct costs of an employee's relocation. They ARE NOT revenue to the RMC.

Revenue earned by the RMC typically consists of service fees paid by the client and referral fees paid by suppliers. These distinctions are, or should be, clearly defined in the MSA with the corporate client. In addition, there are well-established accounting principles that apply to revenue recognition by an RMC.

It should be a fundamental business practice that an RMC pays all of its own corporate expenses, i.e., employee payroll or rent, and makeS all of its corporate investments, only from corporate funds that it clearly owns. That is, funds derived from the revenue it has earned or investments made by its business owners. It should not use funds intended to pay the direct costs of relocation.

HOW SHOULD CORPORATE CLIENT FUNDS BE MANAGED BY AN RMC?

Finally, what mechanisms should be in place to minimize the risks identified above? The first risk, misuse of funds, is relatively easy to mitigate. Most client MSAs contain a provision that allows the client to audit individual transactions of each relocation to ensure that they comply with the client's relocation policies and the MSA. In short, periodic audits are an effective mitigation of this risk.

The second risk, **co-mingling of funds**, is more complicated to address because mitigation depends on the RMC's internal accounting practices and procedures. Therefore, three key questions that corporate clients should ask are:

1. How are client funds accounted for?
2. What controls are in place to ensure that client funds are not co-mingled with the RMC's corporate funds?
3. What mechanisms ensure continued compliance with established procedures?

To answer these questions, and to mitigate these risks, I recommend that corporate clients verify that their RMC:

- Maintains a **separate, project-based accounting system** for tracking individual employee relocation expenses that aggregates to a corporate client account level, separate from the general ledger used to run the RMC business
- Has implemented **internal accounting policies and practices** that ensure that client funds are not used for the RMC's business purposes
- Provides **annual audited financial statements**, prepared by independent accountants, in accordance with Generally Accepted Accounting Principles (GAAP).

Importantly, there are no industry standards for how RMCs meet their financial obligations to their corporate clients. It, therefore, becomes the responsibility of the corporate client to ensure that these kinds of policies and procedures are in place before awarding business to an RMC.

If you only take away a single thing from this paper, I have one overriding recommendation: *Require your RMC to provide annual, independently audited, financial statements prepared in accordance with GAAP*.

The amount of money and risk a corporation has when engaging with an RMC can be surprising. With proper checks and balances in place for the financial responsibility an RMC bears, both the risk of misuse of funds and co-mingling of funds are greatly reduced.

Unfortunately, the topics addressed in this paper are seldom, if ever, thoroughly addressed during the RMC selection process. It's time for corporate clients to more clearly understand and articulate what they expect from RMCs when it comes to meeting their financial responsibilities.

ABOUT NUCOMPASS MOBILITY

As a full-service relocation management company, NuCompass helps corporations move from tactical to strategic to meet their talent mobility objectives. Bringing together global mobility services and technology in innovative ways, NuCompass streamlines the process to increase productivity, reduce costs, and enhance the relocation experience.

ABOUT FRANK PATITUCCI

Frank Patitucci is Chairman and CFO of NuCompass Mobility. He has more than 30 years of experience in the relocation, real estate, and mortgage industries. Frank has received the Editorial Achievement Award, Meritorious Service Award, and Distinguished Service Award from the Worldwide Employee Relocation