Succession Planning

What Is the Solution for the Continuity of a Perpetual Business?

by Daniel M. Isard, MSFS

THE AGE OF MOST COMPANIES IN THE UNITED STATES is relatively young. Even those huge companies on the Dow Jones (DJIA) are on average barely 20 years old. When we use the concept of a cemetery, they are intended to be perpetual. Perpetual is forever, which is longer than 20 years. While the anticipation of an on-going concern might be into perpetuity, no company on the DJIA can assert that they are committed to running their company in perpetuity. That is what makes a cemetery business so unique.

Funeral homes are a bit different in their on-going concern mentality. Funeral home owners have a mentality of a perpetual provider. However, their historical reliance on a building makes the funeral home a business that is immobile. This means the business within the four walls of the building might change. The population served might change over time. I have seen many Catholic funeral homes become non-sectarian businesses and I have seen Jewish funeral homes become properties serving African Americans. We have all seen buildings that once housed funeral homes become open to non-funeral uses. But funeral homes do not have the limited vision of a succession plan.

We have clearly seen the mass roll-up of funeral homes in the United States from the 1970s to the year 2000. Companies that bought funeral homes would end up selling those same funeral homes to protect their balance sheet from 2000 to 2007 or so. In some cases, those companies owned cemeteries and they sold those cemeteries to another owner. But the concept of each and every cemetery in the country today should identify what its succession planning is!

Know the Tax Status

Most cemeteries in the United States are run under the auspices of a not-for-profit organization. They might be owned by a local government, a private nonprofit group, a religious organization, a national entity for a veteran's cemetery, or a for-profit company but operating as a nonprofit for tax and regulatory purposes. Very few of these are truly "for profit." Obviously, the for-profit cemeteries have to plan for their succession of ownership, but most nonprofit organizations don't think that way. Let me explain why they should and how they can plan for their succession.

For-profit vs. Nonprofit

In a for-profit company, you have owners of the company, officers of the company, and employees of the company. In a closely held company, frequently the owners are the officers and may also be an employee of the entity. In reality, these are three different duties (officer, owner, and employee). In a cemetery that is a nonprofit, there are no individuals that are owners. The officers and employees operate the entity for the benefit of the public at large or the sponsoring organization. For example, in a church cemetery, the cemetery may be a different entity from the church. The church may be the sponsor, but the nonprofit is run for the benefit of the church and the patrons at large.

Ownership

Occasionally, the religious sponsor might sell the rights to the management of the cemetery to an outside entity that has experience in running a cemetery. That is a succession plan. It might cover a finite time period of the management, but it is a succession plan.

For those entities that are owned by municipalities, they have to determine if their city resources are best spent managing and caring for a city/township cemetery. Because the city government does not have a "for-profit" mentality, the revenue generated is usually insufficient to cover the costs of maintaining the property. Therefore, that city cemetery is a line-item of cost on the city budget.

What is the reason that cities continue to own older cemeteries? Many continue to own these properties out of a sense of duty of stewardship. I commend that. But, as I see frequently, if a city tries to sell a cemetery, it will only see the possible sale price as being a onetime infusion in the budget. As I have counseled some cities, their presumption is totally wrong.

Profit

Imagine you have to value a city cemetery. The formula is revenue less cost of operations equals profit. Profit divided by an investment factor equals the Value. In most of the valuations I have performed, the Profit is a negative number. It is a negative number due to the higher costs of operation that a city has to deal with, versus a for-profit business. There is no income from a perpetual care trust to help offset this negative result. That usually causes the city managers to forget about selling the cemetery for a wad of cash.

Religious groups (churches and synagogues) that own cemeteries are doing it as part of their ministry. The single largest religious group owning cemeteries is the Catholic Church. Of course, they are quite diverse in their division into local Diocese, but the ministry purpose is the same. In most of my observations, some religious groups do a great job of managing their cemeteries. They invest in them, with creation of mausoleums and outdoor niche offerings. They have solid sales teams. The cemetery is often a source of revenue for the ministry!

However, when that cemetery is the church graveyard, it is a different story. The offering is on a smaller footprint. A five-acre cemetery cannot attract the top sales teams. The momentum is usually a "low hanging fruit" momentum that causes large sales in the first few years of creation, but those sales fall off after the initial sales period.

Akin to city cemeteries, most states do not mandate that religious groups owning cemeteries fund a perpetual care trust. The theory is the church is the fixture of the property, but churches move. In vacating this property of stewardship, the church graveyard becomes a liability. People don't buy cemeteries that are liabilities.

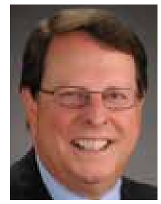
The other types of cemeteries that people don't buy are cemeteries that are either fully sold out or within their last few years of inventory. Why? Regardless of being a church– or city-owned property, the perpetual care trust is usually insufficient for meet the long-term needs. The cost of insurance, utilities, fencing, and mowing is usually far greater than the interest earnings of the trust. Therefore, no one wants to come out of pocket to own a cemetery.

Life Is Short

How can the perpetual care trust not be sufficient to provide for the perpetual care? After all, the trust is not called the "maybe perpetual care trust"! Unfortunately, most states drafted a trust funding requirement that had no real connection to the costs. Like the Social Security funding versus Benefit being out of whack, the perpetual care trust is arrived at by legislative guessing rather than actuarial computations. The amount of funding in annual principal that is sufficient when interest rates are 10% is totally different when the interest rate is only 1%.

Of course, I have witnessed mismanagement of perpetual care trusts. I have seen cases of outright theft of perpetual care funds and some that were more-or-less erroneously invested. Regardless, the preservation of principal of the trust is often more theoretical than actual.

Every owner, manager, and board member of a cemetery must look to the future. What is the solution for the continuity of the management of a perpetual business? This requires a study of the workers and supervisors and identifying how and when they are going to be replaced. If the cemetery requires a third party to step in, make that acknowledgment now. Hire a team to help you plan for the future. Understand one basic fact—the cemetery will outlive you. Your love letter to the cemetery is written as you plan for the next generation of caretakers. M



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