Why Bother with a Perpetual Care Fund Study?

by Hayden Burrus

A CEMETERY ORGANIZATION HAS FINANCIAL STATEMENTS like no other business. I am not thinking of the revenues and expenses, assets and liabilities, that are contained in every other business. I am thinking of their building blocks—in particular, the perpetual care fund, and the underlying perpetual care liability to which it is indelibly linked. A perpetual care fund study calculates the value of these items and how it changes over time.

Think 'Asset'

The perpetual care fund is an asset, and its calculated value is the sum of all securities and income producing assets that are allocated to perpetual care. For the most part, this calculation is very straightforward.

Think 'in Perpetuity'

The perpetual care liability is the future cost of all maintenance and upkeep of the cemeteries between now and … forever (*i.e.*, "in perpetuity"). Cutting the grass, replacing the mowers and tractors when they reach the end of their functional life, re-roofing buildings every 20 years or so, and restoration of the grounds after a 1 in 100-year natural disaster are all costs that must be quantified and adjusted for inflation.

Think 'Cost Allocation'

In addition, the timing of all these expenses must be scheduled out so that the appropriate amount of future investment gains from the perpetual care fund can be allocated to that future expense. For example, if one of the perpetual care liabilities is the cost of a new roof to be built on the main office building of the cemetery in 2040, the perpetual care fund can generate 17 years of investment gains before assets must be spent on the new roof. As a result, the full cost of the new roof does not have to be allocated to this expense.

Think 'Indirect Relationship'

The perpetual care fund and its associated liability are usually much larger than any other asset or liability that should be displayed on a cemetery organization's balance sheet.

Typically, the amount of the perpetual care liability has very little direct relationship to the value of the cemetery's perpetual care fund. The perpetual care liability may be more than, equal to, or less than the value of the perpetual care fund (if a fund exists at all).

Some cemetery executives put very little effort in

Most cemeterians who … [perform] a perpetual care adequacy study, determine that a full, comprehensive analysis of perpetual care assets and obligation are necessary every three to five years.

calculating exactly what this liability amount is. Often the liability is just assumed to be equal to the amount in the perpetual care fund without any research or analysis backing up that assumption.

To the extent that the perpetual care liability is more than the value of the perpetual care fund, then overall value of the cemetery organization will decrease. In fact, the value of a cemetery organization after considering both its perpetual care fund and perpetual care liability can even be negative!

Think 'Timing'

Expected future contributions to the perpetual care fund are an important part of a perpetual care fund study. These contributions significantly affect the overall value and viability of a cemetery. To the extent that a cemetery has a disciplined, formulaic approach to its perpetual care fund contribution practices (*e.g.*, a percentage of plot, crypt, or niche sales), the value of future contributions can be forecast into the future.

Future contributions will increase due to inflation and decrease once sales decline when cemetery inventory starts to become depleted. When calculating the value of future contributions, it is important to consider the timing of these contributions. The sooner the perpetual care fund contributions are made, the more time they have to experience investment gains for the fund.

Think 'Long-term Equity'

Future contributions to the perpetual care fund are not part of a true accounting balance sheet, as a balance sheet is a financial statement that contains details of a company's assets and liabilities at a specific point of time in the past.

However, adding future contributions to an organization's detailed study regarding the perpetual care fund can help management know if its cemetery is likely to be successful in achieving and maintaining positive equity for the long-term.

Think 'Potential Risks'

Even though perpetual care assets and obligations significantly affect the operating results and financial condition of an entity, many cemeterians don't perform a perpetual care adequacy study and spend no effort calculating these values—nor do they even include estimates on their financial statements.

This approach creates several risks for the cemetery. First, it casts doubt on the entire calculation of the value and long-term viability of the cemetery. A cemetery with negative equity (liabilities greater than assets) is not viable long-term, and not even sellable in the short to medium-term.

Cemetery operators leading a negative equity cemetery when including perpetual care should be working furiously to right the ship and increase the assets in the perpetual care fund and/or decrease the perpetual care liability so that there is positive equity in the property.

Think 'Liability vs. Equity'

A cemetery that has positive equity may still be in trouble if its equity is decreasing. This will occur whenever the perpetual care liability is increasing faster than the assets in the perpetual care fund.

Common causes of perpetual care liability increases include when additional high maintenance structures are added to the cemetery, maintenance standards increase, or general maintenance costs grow faster than inflation.

A cemetery experiencing this should explore reining in costs, or at least the rate of increase in costs. If costs cannot be reduced, then the cemetery must deposit more money into its perpetual care fund or increase the rate of its annual deposits.

Think 'Analysis Every 3 to 5 Years'

Since the changes in the total perpetual care liability are as important as its value at any one time, it is important for cemeteries to update their calculation of their perpetual care funds and liabilities.

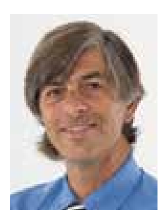
Each year, as the balance sheet is updated, the perpetual care liability will change. It is possible that perpetual care liability increases are causing the value of the cemetery to decrease over time. If the perpetual care liability is not regularly calculated, cemetery management will not become aware of risks to the cemetery's long-term viability.

Most cemeterians who make an effort to consider the effect of perpetual care on the cemetery's equity by performing a perpetual care adequacy study, determine that a full, comprehensive analysis of perpetual care assets and obligation are necessary every three to five years.

Guard the Fund

Finally, from a legal viewpoint, if a third party is seeking to get possession of cemetery funds (*e.g.*, lawsuit, financial distress of the cemetery or an affiliated organization), the perpetual care fund can be viewed as uncommitted funds and available for challenge if it does not have a perpetual care liability attached in order to document and support it.

A perpetual care fund study establishes and quantifies the liability and the fact that perpetual care funds are a deposit on future expenses, instead of unassigned assets available for other financial obligations of the cemetery.



Hayden Burrus is president and principal actuary of PerpetualCareAdequacy.com. He has been studying perpetual care funds and creating customized perpetual care funding models for over 20 years. He is a regular speaker and writer for industry conferences and trade publications. His educational background is in Mathematics and Actuarial Science. He can be reached at (561) 279-2323 or HBurrus@PerpetualCareAdequacy.com.