

Rev. Rul. 61-137, 1961-2 C.B. 118, amplified Rev. Rul. 77-70

To acquire property with which to operate, a newly organized cemetery company purchased land for an undeterminable total purchase price which is to be paid for on the basis of a percentage of the gross proceeds realized from the sale of individual lots. Held, the organization is not entitled to exemption from Federal income tax under section 501(c)(13) of the Internal Revenue Code of 1954.

The Internal Revenue Service has been requested to advise whether a cemetery company which purchases cemetery property for no fixed total price but instead for an undeterminable price based on a percentage of the proceeds from the sale of individual lots is entitled to exemption as a cemetery company described in section 501(c)(13) of the Internal Revenue Code of 1954.

The organization was incorporated under the laws of its state for the purpose of owning and operating a nonprofit cemetery company for the burial or disposal of human remains, with powers to do all things necessary or incident to the carrying out of such purposes. The articles of incorporation provide that the organization shall be under the direction and control of seven trustees. Under the bylaws, each lot owner is declared to be a member with one vote in the proceedings of the organization. The articles also provide that no part of the net earnings of the organization shall inure to any private shareholder or individual.

The information presented discloses that subsequent to its organization but prior to the commencing of sales operations, the organization purchased a tract of land from its organizers. The land was conveyed to the organization pursuant to a contract of sale providing for a purchase price of 35 percent of the sales price of any and all cemetery graves or lots sold from such land. There was no stipulation in the contract of sale stating the total amount to be paid for the land. The reasonable appraised value of the acreage at the time of conveyance was less than one-half of the amount which the vendor could reasonably expect to realize under his contract with the cemetery company on the basis of current lot prices.

The activities of the instant corporation consist of owning, operating and maintaining a cemetery for the interment of human remains. The receipts are derived from sales of grave sites, burial services and interment supplies. Expenditures are made for salaries, commissions to salesmen of burial sites, taxes, payments on cemetery property, insurance, maintenance of cemetery property, payments into the perpetual care fund and miscellaneous operating expenses.

Section 501(c) of the Code describes certain organizations exempt from income tax under section 501(a) and reads, in part, as follows:

(13) Cemetery companies owned and operated exclusively for the benefit of their members or which are not operated for profit; and any corporation chartered solely for burial purposes as a cemetery corporation and not permitted by its charter to engage in any business not necessarily incident to that purpose, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

In *Forest Lawn Memorial Park Association, Inc., v. Commissioner*, 45 B.T.A. 1091 (1941), where the association entered into a contract for the purchase of cemetery lands on the basis of a percentage of the gross proceeds from the sale of individual lots, etc., the United States Board of Tax Appeals held, in part, that there was no inurement of the organization's net earnings to the benefit of any private individual, because the amounts paid as the purchase price of the land were deductions from gross receipts and thus never became a part of the organization's net earnings. The *Forest Lawn Memorial Park Association, Inc.*, case is not followed as a precedent in the disposition of similar cases. See *nonacquiescence*, C.B. 1960-2, 8. Also, the Board's holding in that case is contrary in principle to the decisions in *Texas Trade School v. Commissioner*, 30 T.C. 642 (1958), affirmed, 272 Fed. (2d) 168 (1959); *Mabee Petroleum Corporation v. United States*, 203 Fed (2d) 872 (1953); *Northern Illinois College of Optometry*, Tax Court Memorandum Opinion, entered August 23, 1943. The first of the cited cases involved the payment of excessive rentals and the latter two involved the payment of excessive compensation. The courts found that such payments constituted inurement of net earnings of the organizations to the payees.

Where a cemetery company acquires land at an undeterminable price, to be paid for on the basis of a percentage of the proceeds from the sale of individual lots from the tract, the vendor of the land has a continuing interest in the land. Any appreciation in value, whether it be due to the state of the market generally or the cemetery's own efforts in undertaking capital improvements, etc., will result in a benefit to the vendor of the land. Continuing participation in the earnings of the cemetery company will also ordinarily result in receipt by the vendor of a total price substantially in excess of the reasonable value of the land at the time of its sale to the cemetery company. Under these circumstances it is concluded that the purchase price is unreasonable and that a cemetery company which enters into such a contract of sale may not qualify for exemption under section 501(c)(13) of the Code.

In the instant case, the facts show that no fixed purchase price has been set for the property, the amount received by the vendor is based on a percentage of the sale prices of individual lots sold each year, and if a normal selling period is assumed the vendor stands to receive ultimately for the property an amount more than double the value of the land at the time of its sale to the cemetery corporation.

Applying the foregoing reasoning to these facts, it is held that the instant organization is not entitled to exemption from Federal income tax as a cemetery company described in section 501(c)(13) of the Internal Revenue Code of 1954.