Decision Tree for ICCFA Members re Tax Treatment of Sales of Burial Plots

Evaluating the Impact of the Tax Law Changes in the Tax Cut and Jobs Act of 2017 and FASB ASC Topic 606 on Revenue Recognition

I. Is all or a portion of the amount received from the purchaser of a burial plot deposited in a trust?

A. If yes

1. Neither the Tax Cut and Jobs Act of 2017 (TCJA), FASB Topic 606, nor the cemetery's financial reporting treatment of burial plots sales has any effect on a member's tax treatment of burial plot sales if the sales proceeds are held in a trust.

2. Accordingly, sales proceeds are not taxable to a member while the proceeds remain in trust.

3. If the trust elects section 685 status, income earned by the trust is taxable to the trust.

4. If the trust does not elect section 685 status, income earned by the trust is taxable to the purchaser because the IRS treats the trust as a grantor trust in favor of the purchaser.

B. If no

1. If all or a portion of the proceeds from the sale of burial plots are retained by a member, or if proceeds originally contributed to a trust are subsequently distributed from the trust to a member, the sales proceeds are taxable to the member in the manner described below.

2. In that case, the tax treatment of the sales proceeds is affected by whether the member uses the cash or the accrual method of accounting, and if the accrual method is used, when the member reports the sales proceeds as revenue in the member's financial statements.

3. Prior to the enactment of TCJA, the financial reporting treatment of the sales proceeds was irrelevant to its tax treatment, so this is an entirely new impact from the new tax law.

4. The reason ICCFA is filing comments with the IRS is to attempt to influence the IRS's interpretation of the provisions in TCJA in a manner that is favorable to the industry and to enable members to better understand the tax consequences under the new tax law and financial reporting rules.

5. Again, all of the following discussion is applicable only to the portion of burial plot sales proceeds that are not held in trust.

II. Is the member using the cash or the accrual method of accounting for tax purposes?

A. If using the cash method for tax purposes

1. Eligibility

a. TCJA increased the limit on the size of a member that is eligible to use the cash method of accounting for tax purposes.

b. Under TCJA, the annual limit on average annual gross receipts was increased from $10 million to $25 million, so many more members will be able to elect to use the cash method of accounting for tax purposes.

2. Preferability of cash or accrual method

a. Unfortunately, it is not a simple task to determine whether a member that is eligible to use the cash method of accounting for tax purposes would be better off using that method or instead using the accrual method.

b. All we can do at this point is summarize what we think the tax consequences are for each of those alternatives, so that a member can compare them based on its own facts.

c. However, to be safe, it would be wise to wait on this decision until the IRS responds to ICCFA's comments, so that we can be sure of the tax consequences of each of the alternatives.

3. Tax consequences of using the cash method

a. It is likely that a member using the cash method for tax purposes would not have to report revenue from sales of burial plots except as the member collects the sales proceeds from the purchaser (or receives a distribution of sales proceeds out of a trust).

b. It is less clear whether the member is entitled to reduce the sale proceeds reported as revenue for tax purposes by the member's adjusted basis in the burial plot (i.e, the cost of the plot) or whether, instead, a member must wait until the entire purchase price is collected and title to the plot passes to the purchaser.

c. In comments that ICCFA filed, ICCFA has requested that the IRS allow a basis offset to any revenue that is reported for tax purposes.

d. In any event, a member's financial reporting treatment of the sales proceeds is irrelevant if the member uses the cash method of accounting for tax purposes. All of the new financial conformity rules in TCJA which are discussed below only apply to members using the accrual method for tax purposes.

e. However, in order for a member to decide whether the cash method of accounting is preferable to the accrual method, the member would need to compare the foregoing tax consequences under the cash method with the discussion below relating to the tax consequences of using the accrual method.

B. If using the accrual method

1. See discussion in sections III and IV, below.

III. If the member is using the accrual method, what are the tax consequences with respect to the sale of a burial plot?

A. Introduction

1. The first set of alternative tax consequences depend on the terms of a member's burial plot sales contracts.

2. There are two alternative possibilities according to the IRS.

A. If a burial plot contract provides that in the event of default by the purchaser, a member has an enforceable right to sue purchaser for the unpaid balance of the purchase price of the burial plot, then the following tax consequences result.

1. In proceedings involving ICCFA about 20 years ago, the IRS reached the decision that if a member's burial plot sales contracts provide the member with the unequivocal right to sue the purchaser for the unpaid balance of the sales price, then the sale of the plot is treated as complete for tax purposes when the contract is initially signed, regardless of the lack of payment of the sales price by the purchaser.

a. The IRS ruled that it doesn't matter whether the member ever sues a purchaser for the unpaid balance of the sales price of the plot upon the default by the purchaser.

b. The IRS ruled that it doesn't matter whether any portion of the sales price has been paid by the purchaser.

c. The IRS ruled that it doesn't matter whether the purchaser has the right to title and possession of the plot upon the execution of the sales contract.

2. In all of the foregoing circumstances, a member must include the entire sales price of the plot in gross income for tax purposes (except for any proceeds in trust) and the member may reduce the sales price by the member's adjusted basis (i.e., cost) in the plot that was sold.

3. In this circumstances, the tax treatment of the member is not affected at all by the member's financial reporting treatment of the transaction.

4. Accordingly, the new provisions in TCJA are irrelevant to the member's tax treatment in this circumstance.

B. If instead, a burial plot contract provides that in the event of a default by the purchaser, the member's rights are limited to retaining the portion of the sales proceeds previously collected from the purchaser, so that the member has no right to sue the purchaser for unpaid balance of sales price, then the following tax consequences result.

1. In this circumstance, which is probably the situation in the vast majority of cases involving ICCFA's members, the tax consequences are significantly affected by TCJA and the new financial conformity rule in TCJA. Thus, a member's financial reporting treatment of the burial plot sales revenue becomes relevant.

2. Most of the comments filed by ICCFA with the IRS relate to this situation.

3. Since the tax consequences in this situation vary dramatically depending on the member's financial reporting treatment of the transaction, the explanation of the alternative tax consequences set forth below is subdivided into separate sections based on the member's financial reporting treatment of burial plot sales proceeds.

4, These tax consequences are discussed in section IV, below.

IV. Tax consequences depending on a member's financial reporting treatment of burial plot sales proceeds

A. Reminder

1. This discussion applies only if the member:

a. Receives sales proceeds outside of a trust;

b. The member uses the accrual method of accounting for tax purposes;

c. The member's sales contract does not provide an enforceable right to sue the purchaser for the unpaid balance of the sales price of the plot in the event of default by the purchaser.

d. If any one or more of the foregoing statements is not correct ina particular situation, the member need not read further and should instead review the preceding summary for a discussion of the member's situation.

B. Alternative One -- Member reports the entire sales proceeds, less the cost of the plot, as income in its financial statements upon the execution of the sales contract.

1. In that case, new provisions in TCJA might be interpreted by the IRS as requiring the member to report the entire sales price as gross income for tax purposes at the same time that the income is reported for financial reporting purposes.

a. Under this interpretation, it would not matter that the taxpayer has not collected any of the sales proceeds.

b. This is a subject on which ICCFA submitted comments.

c. ICCFA asked the IRS to reject this adverse interpretation of the financial conformity provisions in TCJA.

2. In addition, if revenue is required to be reported for tax purposes, the IRS might deny a member the right to offset against the revenue reported for tax purposes the member's adjusted basis (i.e., cost) in the burial plot on the theory that there is not yet a present sale of the plot for tax purposes.

a. Even though a member would offset its basis against the revenue reported in its financial statements, the IRS might interpret the new rules in a way that disallows such basis offset for tax purposes because title to the plot does not pass to the purchaser until the entire sales price is paid by the purchaser.

b. This is an important subject on which ICCFA submitted comments.

c. ICCFA asked the IRS not to require acceleration of revenue in these circumstances, but if this suggestion is rejected, to at least allow a deduction of the member's basis in the burial plot if the IRS requires recognition of the sales price as revenue for tax purposes.

C. Member reports the entire sales proceeds, less the cost of the plot, as income in its financial statements when a certain percentage of the sales price, but less than the entire purchase price, is paid by the purchaser.

1. Under this scenario, in the taxable years before the threshold amount of the sales price that must be paid by the purchaser prior to triggering revenue recognition in the member's financial statements, the member would be deferring in its financial statements the portion of the sales proceeds that has been collected from the purchaser.

a. Notwithstanding the member's deferral of revenue in its financial statements, under present tax rules, any collected sales proceeds could not be deferred for tax purposes.

b. ICCFA has submitted comments requesting the IRS to change its deferral rules to permit deferral of the collected sales proceeds under the general rules for tax deferral of advance payments.

c. Unfortunately, under the new provisions in TCJA, that deferral of revenue in these circumstances would be limited to one year beyond the end of the year of receipt of the advance payment.

d. However, a one-year deferral of each year's progress payments would be better than no deferral of progress payments.

2. Once a member has collected sufficient proceeds to trigger recognition of the entire sales price in its financial statements, new provisions in TCJA might be interpreted by the IRS as requiring the member to report the entire sales price in gross income for tax purposes at the same time that the income is reported for financial reporting purposes.

a. Under this interpretation, it would not matter that the taxpayer has not received all of the sales proceeds.

b. This is a subject on which ICCFA submitted comments.

c. ICCFA asked the IRS to reject this adverse interpretation.

3. In addition, the IRS might deny a member the right to offset against any revenue that must be reported as gross income for tax purposes the member's adjusted basis (i.e., cost) in the burial plot on the theory that there is not yet a present sale of the plot for tax purposes.

    a. Even though the member offsets its basis in the plot against the revenue from the sale of the plot reported in its financial statements, the IRS might interpret the new rules to disallow that basis offset for tax purposes because title to the plot does not pass to the purchaser until the entire sales price is paid by the purchaser.

    b. In other words, the IRS might require a member to report the entire sales price in gross income for tax purposes, but allow no offsetting deduction for the cost of the plot until the entire sales price is paid by the purchaser and title to the plot passes to the purchaser.

    c. This is a critically important subject on which ICCFA submitted comments.

    d. ICCFA asked the IRS not to require acceleration of revenue for tax purposes in these circumstances, but if this suggestion is rejected, to at least allow a member to offset its basis in the burial plot against any sales revenue that must be recognized for tax purposes.

D. Member does not report any sales proceeds in its financial statements until the entire sales price is paid by the purchaser.

1. As explained above, under present income deferral rules, a member would not be entitled to defer for tax purposes any sales proceeds that have been collected, notwithstanding that such amounts have been deferred in the member's financial statements.

2. ICCFA has filed comments requesting the IRS to permit the deferral of advance payments from gross income for tax purposes to the same extent that other industries are entitled to that deferral.

3. In addition, ICCFA has requested that the IRS permit a member to offset against any sales proceeds that are reported for tax purposes the member's adjusted basis (i.e., cost) in the burial plot.

Les Schneider
For ICCFA
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