Cedar Park Cemetery Ass’n, Inc. v. Commissioner, T.C. Memo. 1954-48 (1954)

A taxpayer using the accrual method of accounting does not recognize income from executory contracts where significant contingencies exist and the cost of performance is not reasonably determinable.

Summary

Cedar Park Cemetery Association entered into contracts to sell burial spaces in a mausoleum unit that was under construction. The Tax Court held that the payments received under these contracts were not taxable income in the year of receipt because the contracts were executory and contingent. The cemetery was not obligated to complete the unit, and purchasers could receive refunds or elect alternative spaces. Additionally, the final cost of construction was not determinable at the end of the tax year. Because the contracts weren’t completed sales and costs were uncertain, the court sided with the taxpayer. The court also addressed the deductibility of commission payments, finding that these were properly deducted when paid due to wartime wage stabilization regulations.

Facts

- Cedar Park Cemetery Association (petitioner) sold burial rights or spaces in a planned mausoleum unit (Fourth Unit).
- Contracts allowed purchasers to receive a refund with interest if the unit was not built or if they were dissatisfied with changes.
- Purchasers under non-escrow contracts could choose alternative spaces of equal or greater value within the cemetery and receive credit for payments made.
- Title to the burial spaces would not transfer until the unit’s construction was complete.
- At the end of 1945, construction of the Fourth Unit was limited to the foundation and concrete floor slab, and many construction contracts had not been awarded.
- The petitioner also paid sales commissions in 1945 for services rendered in 1943 to Wilson Brothers and Sharp.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in Cedar Park’s 1945 income tax, arguing that payments received under the burial space contracts were taxable income. The Commissioner also disallowed a deduction for commission payments. Cedar Park petitioned the Tax Court for a redetermination of the deficiencies.

Issue(s)

1. Whether the contracts for burial space constituted completed sales in 1945, resulting in taxable income to the petitioner in that year.
2. Whether the petitioner was entitled to deduct in 1945 the commission payments made to Wilson brothers and Sharp for services rendered in 1943.

Holding

1. No, because the contracts were executory and contingent contracts to sell, not completed sales.
2. Yes, because the commission payments, when combined with prior payments, constituted reasonable compensation, and wartime regulations prevented accrual of the deduction in 1943.

Court's Reasoning

Regarding the income from burial space contracts, the court reasoned that since the contracts were executory and contingent, they could not be considered completed sales in 1945. The petitioner was not obligated to complete the mausoleum unit, and purchasers had options to receive refunds or select alternative spaces. Quoting *United States Industrial Alcohol Co. v. Helvering*, 137 F.2d 511, the court emphasized that "a sales agreement from which either the seller or the buyer may withdraw is not a completed sale." Moreover, the court found that the cost of constructing the unit was not determinable at the end of 1945, creating further uncertainty. Referring to *Veenstra & DeHaan Coal Co., 11 T.C. 964*, the court stated that taxing the payments would require treating the contracts as closed sales and either arbitrarily estimating the petitioner's cost or using actual costs from later years, violating established principles.

Regarding the commission payments, the court found the total compensation reasonable and that the Emergency Price Control Act of 1942 and related executive orders prevented the accrual of the increased commission expense in 1943. The court noted that "any wage or salary payment made in contravention thereof shall be disregarded…for the purpose of calculating deductions under the Revenue Laws of the United States." Since approval for the increased commission rate was not obtained, the liability for the additional commissions did not accrue until the restrictions were lifted in 1945. The subsequent payment was deductible because the total compensation was deemed reasonable.

Practical Implications

This case illustrates that income is not recognized under the accrual method when significant contingencies exist and costs are not reasonably determinable. It highlights the importance of analyzing the terms of contracts to determine whether a completed sale has occurred for tax purposes. The ruling also demonstrates how wartime regulations can impact the timing of deductions. Attorneys should consider this case when advising clients on income recognition for advance payments on projects with uncertain completion dates or costs, particularly in situations involving regulatory constraints on compensation. Later cases would likely analyze whether the contingencies were genuine and substantial or merely for tax avoidance purposes.

