

Degrees in consulting are not needed. All it takes is extensive business knowledge and a willingness to help.

Providing Advisory Services to Funeral Directors

By Jack M. Ruhl

The CPA in the local practice unit is uniquely qualified to provide business advisory services to small businesses such as funeral homes. The good news is the concepts that apply to funeral homes readily transfer to other small businesses. In addition funeral directors for whom effective business advisory services have been performed are a potential referral source.

There are 22,000 funeral homes and 54,000 licensed funeral directors in the U.S. (National Funeral Directors Association, 1992). This represents a potential client base that is largely underserved by CPAs. Specifically, there is a large untapped market for CPAs to provide business advisory services (BAS) to funeral directors. Funeral directors need these additional services for at least two reasons. Funeral directors typically have little formal management training, especially with regard to cost analysis. Hence, they frequently lack the background needed to understand the significance of a changing cost structure for the funeral industry or for their individual businesses. Even when funeral directors possess accurate cost information, they often make less than optimal pricing decisions.

BAS is a level of management advisory services. However, the CPA providing BAS does not need the type of technical knowledge typically thought necessary to provide major consulting services, such as extensive knowledge of management information systems. Rather, the BAS provider has extensive business knowledge which can be used to help the funeral director use financial statements and cost analyses to make better strategic decisions.

Why Do I Want Funeral Director Clients?

There are three reasons why funeral directors make good clients. The first is that they are typically long-term, financially responsible clients. This is due to the fact that the ownership and management of funeral homes do not change very often. Funeral homes are often family owned businesses that have been managed by the same family for two or more generations.

Second, funeral homes are typically uncomplicated businesses with relatively few transactions. While there are changes occurring in the funeral industry (for example, increasing numbers of cremations), the changes are easily understood.

Third, BAS can be provided in conjunction with other services being provided to the funeral director. Therefore, there is no need to allocate a large block of time (and staff) to a BAS project, as there might be for an installation of a computerized information system. The CPA can generate BAS ideas while working on other client projects, such as tax or audit work.

Providing BAS

The potential for CPAs to provide critical advisory services to funeral directors depends on the needs of funeral directors for such services. There is undoubtedly such a need. Robert Ninker, the Executive Director of the Illinois Funeral Directors Association was asked about the major problems facing funeral directors today in an interview in the *American Funeral Director*. Ninker stated that a major problem was the problem of profitability in general and inappropriate business practice in the area of pricing in particular.

Why aren't CPAs already providing the needed advisory services to funeral directors? Funeral directors have historically relied on bookkeeping services to provide bookkeeping and tax services, and little more. The bookkeeping for a funeral home is simple, due to the fact that there are comparatively few transactions. Records of sales and payments on account are kept, and bank reconciliations are made each month. The usual tax forms are completed and tax payments made as required. Casket inventories are maintained and petty cash is reconciled.

Because the bookkeeping is so simple, funeral directors often rely on national bookkeeping services. These national bookkeeping services provide funeral directors with items such as cash receipts journals and petty cash journals. The national firm reconciles the funeral home's checking account each month and prepares financial statements. All these services are provided through the mail and over the telephone. The funeral director mails copies of the cash receipts journal, petty cash disbursements journal, and canceled checks to the bookkeeper each month. The bookkeeper then mails the appropriate statements back to the funeral director.

A shortcoming of such centralized national bookkeeping services is that the funeral director clients may fail to appreciate the significance of the information being provided by the cost analyses and financial statements.

The Modern Funeral Practice

Funeral homes are typically small locally owned businesses, managed by funeral director owners. Funeral home size is expressed not in sales dollars per year,

but in the number of traditional funeral services conducted. This number ranges from the teens to a thousand or more funerals per year. Most funeral homes, however, conduct between 50 and 250 traditional funerals per year.

A traditional funeral consists of a visitation or wake at the funeral home and a funeral service conducted at the funeral home, church, synagogue, or graveside.

The sale of a traditional funeral consists of the sale of a service and merchandise. There are three parts to the service: 1) professional services, including embalming, making funeral arrangements, and directing the funeral service, 2) use of the funeral home as a place to embalm the body, hold the visitation, and conduct the funeral, and 3) use of automotive equipment to transport the body from the place of death to the funeral home and from the funeral home to the place of burial or entombment. The merchandise which the funeral director sells is normally limited to the casket and burial vault, although burial clothes and grave markers are usually available.

Most states require that managers of funeral homes be licensed funeral directors. The amount of formal management training possessed by the manager varies greatly. This is due in part to the fact that state licenser requirements vary greatly. Thus, some managers possess not only degrees in mortuary science, but also degrees in business. Other managers have completed only a year of mortuary school and a year of undergraduate training. Therefore, there is wide variation in the abilities of funeral directors to 1) understand the implications of cost analyses and projections, and 2) take the appropriate strategic steps.

Funeral Industry Cost Structure

The cost structure in the funeral industry is characterized as consisting largely of fixed costs. An example of these costs is provided in the accompanying figure. These costs are incurred by almost all funeral homes in the U.S. In 1990, the average cost of conducting a traditional funeral service—professional services, (embalming, etc.), use of the funeral home, and use of automotive equipment—was \$2,402. Close examination reveals that most of the costs are fixed, at least in the short run. These fixed costs

relate to the investment in buildings, landscaping, and equipment. Funeral directors do not appreciate the importance of distinguishing between fixed and variable costs when they make pricing decisions. The CPA can identify and explain the problems caused by steadily increasing fixed costs. The most critical is an increased break-even point.

Increased Break-Even Point

Everything else being equal, increasing fixed costs mean that a funeral home must sell more units in order to reach its break-even point, assuming that the per unit contribution margin does not change. "Unit" refers to a sale of a funeral service.

In the case of a funeral home, this means that more traditional funerals must be sold. For several reasons, this is not easily accomplished. The first reason is that, the national death rate is declining. The death rate for 1989 was 866.3 deaths per 100,000 population. This was two percent below the national rate in 1988. The death rate is expected to continue to decline. Another impediment to selling more traditional funeral services is the rise in the number of cremations. Nationally, the cremation rate is 17.02%. This figure fluctuates significantly, depending on the part of the country the funeral home is located in. The cremation rate in California in 1990 was 40.12%. The number of deaths in the community represents the maximum number of traditional funerals which can be sold.

Facing rising fixed costs, the funeral director must consider the potential for increasing the contribution margin per funeral service sold. An increase contribution margin can be accomplished by increasing the average sales revenue per funeral or lowering the variable costs per funeral. Increasing the average sales revenue per funeral is possible, although difficult, because families usually have a ceiling on the amount they are willing or able to pay for a funeral.

It is also difficult to substantially lower the variable costs per funeral. The major items of variable cost are the casket and burial vault. The cost of caskets and vaults are generally consistent among manufacturers. Most funeral directors do not have the option of receiving a quantity discount by purchasing large numbers of caskets in a single order. Vaults are

not purchased in quantity; they are purchased only as needed.

Covering Fixed Costs

CPAs may suggest ways that funeral directors can respond strategically to rising fixed costs. A strategic response is an action that is generally long range in nature. Three examples are 1) operate multiple funeral homes, 2) convert fixed costs to variable costs, and 3) market related goods.

Operate Multiple Locations. For many years there have been many small, owner-operated funeral homes in small towns in America. For example, in one small Michigan town, South Haven, there were at one time two owner-operated funeral homes. Each of these funeral homes conducted between 50 and 150 funerals per year. Since each was independently owned, each had significant fixed costs to cover. These consisted of the fixed costs associated with buildings, vehicles, salaries, taxes, and utilities.

In the early 1980s, a third funeral home located in nearby Benton Harbor, purchased the two South Haven funeral homes. This resulted in two funeral homes (one in South Haven and one in Benton Harbor) under one ownership. The result was a significant savings of fixed costs. The buildings and vehicles associated with one of the South Haven funeral homes were sold, which resulted in savings of salaries, taxes, vehicle maintenance costs, and utilities.

Convert Fixed Costs to Variable Costs.

One of the more significant fixed costs associated with a funeral home is the cost of purchasing, maintaining, and insuring motor vehicles. Three motor vehicles are necessary for any funeral home's operations: a removal car, a hearse, and a limousine. The cost of purchasing and insuring these vehicles is a fixed cost.

Some funeral directors are able to convert these fixed costs into variable costs by renting these vehicles. Verhey, Inc., of Grand Rapids, Michigan, rents hearses and limousines to funeral homes on a per funeral basis. Verhey is responsible for the upkeep and insurance on the vehicles. Thus, a funeral home needs to own only one vehicle, the removal car.

A second fixed cost which may be converted to a variable cost is the cost of hiring an embalmer. In most instances, an embalmer is salaried. Hence, the

embalmer's wages represent a fixed cost. When he or she is not preparing bodies for burial, the embalmer may be performing other tasks, or is idle. One way

to convert the fixed cost of employing a full time embalmer is through the use of a trade embalmer.

A trade embalmer is an independent

contractor who sells his or her skills to many different funeral homes. Thus, a trade embalmer may embalm 300 bodies in one year, but for 25 different funeral homes. The amount charged by trade embalmers varies widely, depending on the area of the country. For example, one trade embalmer in Kalamazoo, Michigan, charges \$45 per embalming, while a trade embalmer in Chicago charges \$150 per embalming. As an independent contractor, the trade embalmer is responsible for paying his own benefits, such as Social Security, health, and retirement. The benefit to the owner of the funeral home is that his or her embalming cost with a trade embalmer is a variable cost.

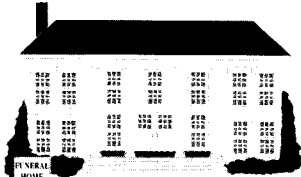





Market Related Goods. One product for possible additional revenues is the cemetery marker. Cemetery markers, sometimes referred to as headstones, are made of various materials such as marble or granite. The marker is placed at the gravesite shortly after burial has taken place. The markers are manufactured elsewhere, and available at a wholesale price to the funeral director. There is often a 100% markup on cemetery markers.

Advising the Funeral Director on Pricing Decisions

When the consumer purchases a funeral, the price of the individual parts is clearly indicated. For example, the price of the casket is clearly separate from the price of the service component of the traditional funeral. Therefore, a consumer may purchase the standard service offered by the funeral home and purchase either an inexpensive, moderately priced, or expensive casket.

Funeral directors do not price their services and merchandise appropriately. Specifically, they underprice their services and overprice their merchandise. A 1991 survey of funeral home operations conducted by the National Funeral Directors Association indicated that the average price for the service portion of a funeral was \$1,814. This price does not include the price of the casket, burial vault, cemetery lot, and grave opening. However, another survey conducted by Federated Funeral Directors of America for approximately the same time period indicated that the average cost to the funeral director to provide the service portion of a traditional funeral was \$2,402. Thus, on average, funeral directors were reporting costs which exceeded the prices

TYPICAL COST BEHAVIOR OF MAJOR FUNERAL HOME COSTS IN 1991

Category	Cost Cost	Cost Behavior Pattern	
		Specific Variable	Fixed
Building 	Chapel Visitation Rooms Preparation Room Furniture, Equipment Utilities Maintenance & Insurance	✓ ✓ ✓ ✓ ✓	✓ ✓ ✓ ✓
Improvements 	Parking Lot, Landscaping Maintenance & Insurance		✓ ✓
Salaries & Benefits 	Owner, Embalmer Funeral Attendants	✓	✓
Automotive 	Removal Car, Hearse, Limousine Fuel Maintenance & Insurance	✓	✓ ✓
Cost of Sales 	Caskets, Burial Vaults		✓
Miscellaneous 	Embalming Fluid, Supplies	✓	

charged by \$588 (\$2,402 - \$1,814). The shortfall was presumably made up for with the casket and vault sale.

One reason why funeral directors price their services below their costs is that buildings and equipment for many funeral homes are fully depreciated for both financial and tax purposes. Since these items have zero book value, funeral directors do not see why it is necessary to earn any return on them. Put differently, a funeral home may have a fair market value greatly exceeding \$1 million, but a book value of zero. The funeral director ignores the fact that he or she should be earning a reasonable return on the investment. Thus, the return on the physical facilities is "backed out" of the costs of the service portion of the traditional funeral. The BAS provider can address these pricing issues.

The Need to Make a Reasonable Return on Investment. The funeral director needs to be told that he or she should be earning a reasonable return on investment, and part of that investment is in assets tied up in the funeral home's physical plant. The investment exists whether or not it appears on the funeral home's balance sheet or not. Some funeral directors will be amazed with the low return on investment they are earning when the investment in fixed assets is considered.

Point Out the Potential Hazards of Mispricing. Hazard one is that the funeral director will not be able to compensate for underpricing the service component through the casket or vault sale. Funeral directors cannot rely on the sale of merchandise to recover costs when little or no merchandise is sold. This scenario is becoming increasingly common due to the increasing number of cremations in the U.S. In a cremation service the merchandise sale consists of a disposable receptacle used for the cremation, which may retail for as little as \$150. If the funeral director is underpricing the service component of his product by \$500 or more, the cremation sale will result in a loss to the funeral director.

Explore the Merchandise Markup. The question to ask the funeral director is, "Why are you marking the casket (and/or burial vault) up X%?" While families compare prices for the service portion of the traditional funeral, they normally do not compare prices for the merchandise portion of the traditional

funeral. This is due to the fact that it is very difficult to compare one casket with another or one burial vault with another. There are a variety of casket and burial vault manufacturers, and the quality of their products is not easily compared. Therefore funeral directors feel more comfortable marking up the casket and burial vault rather than the service portion of the traditional funeral, which may be roughly compared across funeral homes.

Given that these products are not easily compared, what is the optimal markup, given the goals of the funeral director? That is, should all caskets have the same percentage markup? What is the role of casket price in the family's decision to select a particular casket? Will the casket markup change if the funeral service is priced according to the funeral director's actual costs?

Miscellaneous BAS That Can Be Provided

CPAs can provide other useful services to funeral directors. The first is acting as a liaison with the bank. This service is particularly useful for funeral directors who are thinking about building another funeral home in a nearby city or suburb or renovating their existing funeral homes. In order to carry out such ambitious plans, funeral directors will need bank financing, and CPAs can provide the audited financial statements needed by the banker and can accompany the funeral director to the bank as needed.

CPAs can also provide useful unbiased opinions about certain "goodwill" costs. Goodwill costs are costs incurred to generate goodwill in the community. These include granting employees time off to participate in civic and community activities as well as paying employees expenses to join service organizations. While such employee activities are commendable, it is not always clear that they generate more than negligible goodwill for the funeral home. The funeral director manager may be willing to carefully consider such costs if so advised by his or her CPA.

Marketing Tips

Providing a differentiated product is the key to marketing your services to funeral directors.

Join service Clubs. In marketing your

services to professional groups, it makes sense to join the same service organizations that the professionals join. This may be difficult with certain professionals (such as physicians or attorneys), but not funeral directors. Funeral directors are almost always members of organizations such as the Kiwanis, Lions, Optimists, Rotary, etc. While you are getting to know the funeral directors, you can also get to know some other business people in your community, which may lead to other engagements.

An especially powerful way to market yourself at these service club meetings is to volunteer to be the speaker. I served as program chairman for the Optimist Club for two years and was always glad to have someone volunteer to speak at one of our luncheon meetings.

Speak at Funeral Directors' Association Meetings. Every state has a statewide organization of funeral directors. The state organization is divided into regions, all of which hold monthly meetings. As with service clubs, these meetings feature guest speakers. From personal experience, I can attest to the fact that funeral directors like listening to CPAs.

You can learn about the details of these state or regional meetings from a funeral director client. Bulletins are published by the state funeral directors' societies which list the dates, times, and places of the meetings. Your funeral director client would probably be happy to pass your name along to the program chairman of the regional or state meeting as a willing guest speaker.

Transferability to Other Industries

Marketing and providing consulting services to funeral homes can be a first start towards providing business advisory services to other small businesses. The first step is to obtain a good understanding of the industry in which the small business operates. Then apply common sense and some of the basic cost principles discussed here, and you will be on the road to a successful business advisory practice. □

Jack M. Rubl, PhD, is an Assistant Professor of Accounting at Louisiana State University. The author appreciates the assistance of Professors Bart Hartman of Louisiana State University and Larry Parker of Case Western Reserve University in writing the article.