Funeral directors and crematoria services market investigation

Dignity plc response to the CMA's working papers on Crematoria Profitability and Cost of Capital

1. Overview

1.1 Dignity plc ("**Dignity**") welcomes the opportunity to comment on the CMA's working papers as part of its market investigation. This submission addresses the CMA's working papers on *Crematoria Profitability* and *Cost of Capital Analysis* published on 20 February 2020. On 28 February 2020 the CMA also provided Dignity with the spreadsheet model of the CMA's analysis of Dignity's profitability.[1]

1.2 There are three crucial points the CMA should note:

(A) Dignity's ability to comment fully on the analyses in these working papers, particularly related to profits across the market, is substantially constrained by the number of confidentiality redactions and the lack of access to the underlying data. As a result, these are Dignity's preliminary comments and may be updated following access to redacted information and underlying data.

(B) [✂]. Dignity welcomes the CMA's indication that it will collect more recent data.[2] [✂]. Dignity expects other cremation providers will have experienced similar pressures. Dignity also expects that the pandemic has accelerated the growth of direct cremations as consumers will be more familiar with alternative options post the pandemic. These impacts are likely to have lasting negative effects on revenues and profitability in the market.

(C) The CMA must obtain valuation advice from an appropriately qualified specialist to value the crematoria of other providers included in the CMA's analysis. Dignity acknowledges that valuing crematoria is outside the CMA's expertise and so has submitted an opinion from Cushman & Wakefield for its own sites. The CMA notes that it was unable to retain a valuation specialist over the Christmas / New Year period, but given the crucial importance of the valuations to the ROCE estimates, and the very large differences in results between the CMA and the specialists at Cushman & Wakefield, Dignity considers this is a necessary input.

1.3 This paper is structured as follows:

- Part 2 comments on the CMA's findings on Dignity's ROCEs.
- Part 3 comments on the CMA's findings on market-wide ROCEs.
- Part 4 examines in more detail the approach to land valuation.

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1 File 'Dignity Crematoria Profitability CONFIDENTIAL 566117700_2.xlsx' sent to Dignity on 28 February 2020.

2 Paragraph 26 of the working paper.

- Part 5 examines in more detail the approach to building valuation.
- Part 6 comments on the approach to local authorities' costs.
- Part 7 examines the approach to EBIT.
- Part 8 provides some comments on the approach to WACC.
- Part 9 describes a few data issues that have been identified in the CMA's analysis of Dignity's profitability.

1.4 Appendix A provides additional evidence of land value estimates from the UK Valuation Office Agency (VOA).

2. The CMA's findings on Dignity's ROCE

2.1 Dignity has carried out its own calculation of Dignity's ROCE estimates, applying the CMA's methodology to Dignity's 2019 data (Figure 1) and addressing issues that have been found in the CMA's data and approach (Figure 2).

2.2 Figure 1 below shows the CMA's ROCE for Dignity (*Firm A* in the working paper) against the estimated WACC under the CMA's three scenarios: the "**Base Case**"; "**Scenario One**" in Dignity's own analysis refers to 'Sensitivity One' at Table 2 of the working paper; and "**Scenario Two**" refers to 'Sensitivity Two' at Table 3 of the working paper.

2.3 Dignity explains later in this paper why it disagrees with the CMA's decisions (i) to cap the total acreage of each site at 10 acres; and (ii) to omit certain key assets from Dignity's capital employed (affecting 8 of 46 Dignity crematoria in particular). Dignity does not address these issues in Figure 1.[3]

2.4 Dignity notes that <u>Scenario Two provides a more reliable basis</u> on which to measure the value of the capital employed than the assumptions in the CMA's Base Case. Scenario Two is based on the independent valuation of the expert firm Cushman & Wakefield – a firm previously instructed by the Competition Commission to conduct land and property valuations.[4]

2.5 Even when assuming the 10 acre cap and omitting key asset values, Dignity's ROCE under Scenario Two [✂].

Figure 1 [✂]

[✂]

Notes: [✂]

Figure 2 below further adjusts the CMA's analysis in two ways. First, it includes conservative estimates of the capital employed at the eight sites that the CMA currently omits from Dignity's capital employed. Second, it removes the CMA's 10 acre cap assumption. [✂].

Figure 2 [✂]

[✂]

Notes: [✂].

2.6 The CMA's view in the working paper of Dignity earning excessive profits relies crucially on the CMA's assumptions: (i) to use its own asset value estimates rather than those of professional valuation specialists (and, as shown below, also the UK's Valuation Office

3 However, Dignity's version of this analysis corrects an error found in the CMA's spreadsheet on how the 10 acre cap was applied. Please refer to paragraph 9.1 (A).

4 DTZ (now Cushman & Wakefield) was commissioned by the Competition Commission (CC) to undertake the valuation of the portfolio of private hospitals during the CC's Private Healthcare market investigation. See full report at: https://assets.publishing.service.gov.uk/media/533aed46e5274a566000001f/Appendix_6.15.pdf.

Agency estimates); (ii) to exclude certain assets from the capital employed; and, (iii) to cap sites at 10 acres. **Dignity does not believe these assumptions are sound**.

2.7 Dignity identifies in this paper further adjustments that should be made, [✂]. The WACC benchmark applied should also be in excess of 10% rather than the 8% assumed.

3. The CMA's findings on market-wide ROCE

3.1 The CMA's analysis covers less than 40% of the crematoria market (on the basis of either revenues or volumes) [5] and the CMA itself identifies that *"[t]he provision of crematoria services in the UK is highly fragmented..."*.[6] This makes generalised conclusions on the overall market based on this small part of the market risky. It also means that the CMA cannot conclude that a 'substantial' portion of the market is earning excessive profits in line with its Market Investigation guidelines.

3.2 Dignity disagrees with the CMA that it is a safe assumption that *"[w]ith regard to the fragmented portion of the sector (around 70% of cremations by volume), [the CMA] consider that a random sample of 22 crematoria, which comprises approximately 11% of volumes from this part of the sector, is likely to provide information that is statistically representative of the sector as a whole*".[7] When faced with a highly differentiated and fragmented sector, a large sample is needed to find statistically meaningful results.

3.3 Currently the CMA's local authority analysis relates to just 14 of the proposed 22 local authority crematoria. Dignity does not consider this to be a large enough sample size given that local authorities comprise the majority of the market. Further, the working paper does not assess where these local authorities are in terms of investment cycle and how the CMA has assessed the need for re-investment in its analyses.

3.4 The working paper shows that under the CMA's assumptions in Scenario Two (using the specialist valuer estimates, values also much more in line with those of the UK Valuation Office Agency), at least three of the four large private crematoria operators did not have a ROCE above WACC over the five-year period. Dignity notes also that its own ROCE estimates would fall further when adjustments explained in this paper are included. Furthermore, the ROCE of at least two local authority crematoria did not cover the WACC. This does <u>not</u> suggest a substantial part of the market is earning excessive profitability.

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5 Paragraph 22 of the Working Paper suggests that the CMA's analysis covers 118 of approximately 300 crematoria in the UK. However, Footnote 1 of the working paper notes that "*In this present paper we present the results of fourteen of these [22] local authority crematoria. The remaining eight have been excluded at the current time due to potential issues with the data submitted.*"

6 Paragraph 21 of the Working Paper.

7 Paragraph 22 of the Working Paper.

4. Approach to Land Valuation

4.1 It is clear that properly incorporating the value of land in the capital employed is crucial to the accuracy of the ROCE assessment. Dignity provided the CMA with a valuation report by Cushman & Wakefield, calculated on a conservative basis, which considered available land and planning issues. Dignity also called for the CMA to conduct detailed valuations in its response to the first profitability approach paper dated 9 August 2019.[8]

4.2 Dignity welcomed the CMA's acknowledgement of the importance of finding an independent valuation expert.[9] It notes that these efforts have been unsuccessful, in part due to the timing of the CMA's tenders.[10]

4.3 However, given the crucial importance of this building block in the ROCE analysis (and potentially also to price control design), Dignity considers it unsatisfactory that no appropriately qualified and experienced specialists have been instructed by the CMA.

4.4 Instead, the CMA simply assumes (i) a £90,000 per acre 'Base Case', and (ii) caps the site sizes to 10 acres.[11] Dignity disagrees with these assumptions, and also with the labelling of this approach as a 'Base Case'. It is unrealistic for the following reasons:

(A) First, the CMA Base Case uses a single, unadjusted value for land across the UK. Indeed, the CMA itself notes (at paragraph 143, emphasis added): "*that the use of average purchase price per acre may not reflect the actual costs that a crematoria operator might face in a particular geographic location as land values <u>vary materially</u> across the UK.*"

(B) Second, the Base Case's simplified approach pays no attention to the CMA's core principle that the best estimate of the MEAV of a plot of land currently in use as a crematorium is the current market price of the lowest cost, suitable site that an operator could purchase to serve the relevant local market. In particular, such a site should:

(i) Be appropriately located to serve the population served by the existing crematorium;

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8 Dignity explained in that response the emerging findings of the Cushman & Wakefield valuations, and noted: "*Given the material impact on the asset values for Dignity, with a relatively newer crematoria portfolio, we expect the adjustments necessary for local authority crematoria will be even more substantial. Dignity would, therefore, recommend that the CMA conducts similar detailed analysis for other crematoria.*"

9 Paragraph 63 notes that "*In our view, the ideal approach to valuation of land for older sites would have been to conduct an external valuation exercise of land values for all crematoria within our sample. However, it has not proven possible within the constraints of this investigation to conduct such an exercise*".

10 Footnote 8 of the working paper.

11 The Base Case values the replacement cost of land for the 118 crematoria in the sample based on the purchase costs of 14 land transactions since 2010. The CMA then calculates the average cost per acre across these 14 transactions (c.£90,000 per acre) and uses this average to estimate the value of land acquired by the other 104 crematoria not covered by the sample, and capping their size at 10 acres. Paragraph 71 of the Working Paper.

(ii) Meet the relevant criteria for a suitable plot for a crematorium in terms of size, aspect and road access; and

(iii) Have, or have a high likelihood of obtaining, planning permission for use as a crematorium.

(C) Third, as shown in Table 1 below, the CMA's sample of 14 recent land transactions consists almost entirely of sites located in rural areas (and, as the CMA notes, none are in Greater London). The average land cost of £90,000 would not allow a replacement crematorium in a more urban area.[12] Appendix A presents evidence from the **UK Valuation Office Agency** (VOA) that the average land value for a site used for non-agricultural purposes across England is <u>at least</u> £350,000 per acre and much higher in urban areas even excluding London (see Appendix A). The CMA's sample is biased to rural transactions and is not reflective of what would actually have to be paid to replace the sites in their existing urban settings. This is evident also in the Cushman & Wakefield report which actually sought to identify appropriate alternative sites in the local area of existing crematoria.

Table 1
Sample of 14 crematoria used in CMA's land valuation analysis

Opening year	Crematorium name	Operator	Type of area
2010	West Lothian Crematorium	Westerleigh	Rural
2010	Fenland Crematorium	Dignity	Rural
2011	Mendip Crematorium	Dignity	Rural
2014	Kirkleatham Memorial Limited	Memoria	Rural
2015	Amber Valley Memorial Limited	Memoria	Urban
2015	South Leicestershire Memorial Limited	Memoria	Rural
2015	Waveney Crematorium and Memorial Park	Memoria	Rural
2015	South Oxfordshire Crematorium	Memoria	Rural
2015	Westerleigh Crematorium	Westerleigh	Rural
2016	Denbighshire Memorial Limited	Memoria	Rural
2017	North Hertfordshire Memorial Park and Crematorium	Memoria	Rural
2018	The Vale Crematorium	Westerleigh	Rural
2018	Flintshire Memorial Park and Crematorium	Memoria	Urban
2018	North Wiltshire Crematorium	Westerleigh	Rural
2019	Barnby Moor Memorial Park & Crematorium	Memoria	Rural

Source: Dignity research based on Figure 2 in CMA's Working Paper 'Crematoria: Profitability' and ONS Rural-Urban Classification (https://geoportal.statistics.gov.uk/datasets/20467878cc20410d961a3f71db356b6d).
Notes: although the postcode of the Flintshire Memorial Park and Crematorium is classified by the ONS as located in a 'Urban city and town' area, satellite images show that the location corresponds to an agricultural area far outside of Liverpool.

12 Nine of the CMA's sites above were from Memoria. Paragraph 57 of the working paper gives Memoria's view that in several cases its existing sites would have "*a significantly higher cost today than is recorded even in the undepreciated book value of the land*".

(D) Fourth, Dignity provided information to the CMA on the purchase cost of land of more recent transactions although these sites have not yet opened.[13] On many occasions, Dignity has also been prevented from acquiring a site because the asking price was too high – this introduces a selection bias in looking only at actuals when aborted purchase prices are not included.

4.5 Dignity, therefore, considers that the per acre cost of replacing the land of its crematoria is best approximated by the values reported by Cushman & Wakefield. Scenario Two should, therefore, be the starting point of the CMA's assessment. These estimates are also in line with the estimates from the UK Valuation Office Agency. The CMA's 'Base Case' valuation assumption is unrealistic.

4.6 Further, Dignity does <u>not</u> agree with the CMA's decision to cap the size of sites at 10 acres. Dignity maintains many sites with infrastructure and grounds in excess of 10 acres, allowing Dignity to maintain memorial and burial revenues which are included in the EBIT.

4.7 Dignity has previously explained to the CMA the integrated nature of sites.[14] Dignity has further provided detailed estimates of the proportion of grounds covered by graves.[15] The 10 acre assumption is not a reliable basis on which to replace the existing crematoria in the UK and yet has crucial impact on the CMA's ROCE conclusions – without this assumption, Dignity's ROCE [✄].

5. Approach to Building Valuation

5.1 The CMA's approach to valuing the replacement cost of crematoria property assets is based on the replacement cost estimate included in the parties' insurance policies.[16] The CMA then depreciates the property values of these 38 sites based on each crematorium's opening year using straight-line depreciation assuming an Useful Economic Life (UEL) of 100 years.

5.2 For Dignity, the CMA included no property asset value for three Dignity sites (East London, Birmingham, and South London), treating these as fully depreciated. The CMA also included no property asset value for five sites that Dignity leases from a local

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13 For example, Dignity acquired the Sevenoaks and Drumpellier sites for £[✄] and £[✄] per acre, respectively.

14 See Dignity's response to the *Approach to Valuation of Crematoria Land* working paper, 18 December 2019. Examples of the integrated nature of sites include: (i) Dignity has to invest in maintaining the burial areas (even if not revenue earning), as failing to do so would undermine the crematorium experience, brand and site safety; (ii) When a site (e.g. chapel and / or parking) is being used for a burial service, Dignity would typically not perform a cremation service at the same time; and (iii) Memorials are often interred next to or inside an existing grave plot (e.g. of a family member) or inside a family mausoleum.

15 For further information on Dignity's burial grounds please see the response to Question 18 of the CMA questionnaire of 8 August 2019.

16 Paragraph 81 of CMA's Working Paper 'Crematoria: Profitability'

authority (Stockport, Enfield, Rotherham, Weston-Super-Mare, and Bury[17]). The CMA, therefore, included the EBIT for these eight (of 46) sites in the ROCE analysis, but with no matching capital employed.

5.3 First, treating three crematoria as fully depreciated does not take account of significant investments that have been made over the years to keep these properties in working order. Some of these investments are capitalised in Dignity's Fixed Asset Register, which displays a positive NBV as shown in Table 2. More importantly, however, the site appraisal exercise conducted by Cushman & Wakefield evaluated the replacement cost of these properties at more than £[✄] (adjusted for depreciation and obsolescence).[18] [✄].

Table 2
Extract of Dignity's property assets (2018)

[✄]

Source: [✄].

5.4 Second, the capital employed excludes the five sites operated by Dignity on behalf of local authorities from the total property capital base, but the revenues generated from these crematoria are included. The capital employed associated with these 5 sites ranges from £20 million (i.e. land value under the Base Case and building value) to £124 million (i.e. land value under Scenario Two and building value) as shown in Table 3 below.

Table 3
Estimated land and building values of 5 Dignity sites operated on behalf of local authorities

[✄]

Source: [✄]
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5.5 IFRS 16 has resulted in Dignity capitalising long-term leases for these crematoria. Dignity's Annual Report 2019 provides a detailed analysis of the impacts of IFRS 16 on pages 117 and 118 (see **Annex 2.1** submitted alongside this response). IFRS 16 has

17 Dignity notes that the CMA mis-classified the Bury crematorium as being managed on behalf of local authority – Dignity owns that crematorium. Also, the CMA mis-classified the Shrewsbury crematorium as being owned by Dignity – this crematorium is managed by Dignity on behalf of the local authority.

18 These values exclude the replacement costs of the following items : (i) plant and machinery (in particular the cost associated with replacing cremators), (ii) fixtures and fittings (including but not limited to internal fit-out, audio visual equipment, and security systems), (iii) costs associated with installing utilities and services at the property (e.g. drainage, gas, electricity and sewage), (iv) landscaping works to replace memorial gardens, and (v) costs associated with securing planning consent and other professional and legal fees.

resulted in the recognition of £95 million of right-of-use assets, of which over 30% related to the crematoria business. This increases capital employed and lowers ROCE.[19]

5.6 Thirdly, the insurance values which the CMA relies on to estimate the replacement cost of crematoria buildings do not take account of costs incurred relating to the establishment of a site such as drainage, groundworks, and landscaping costs. These costs can be substantial depending on certain geographical aspects of a site (flatness of the ground, acreage, presence of natural obstacles, etc.). The true costs of replacement would be substantially higher. Further, private operators must account also for irrecoverable VAT.

5.7 For example, Dignity recently contracted a construction company (Surgo) to conduct the site preparation work at the Castle Eden crematorium (this site has not yet opened). Table 4 below provides a breakdown of the costs involved in the site development process. As the table indicates, more than £[✂][20] (over half the costs, and before VAT) consist of site preparation work. This proportion of total costs is low compared to other Dignity sites as the site is relatively small (around 14 acres) and the land is fairly flat and thus required minimal cut and fill.

Table 4
Cost breakdown of site preparation project at Castle Eden Crematorium

[✂]

Source: [✂]

5.8 It is Dignity's view, therefore, that the capital employed in crematoria buildings and infrastructure is underestimated currently by over [✂] even on a conservative basis. [✂].

6. Approach to local authority crematoria costs and capital employed

6.1 The CMA's concerns about profitability appear to be driven by the high ROCEs calculated for 12 (of 14) of the local authority crematoria – these local authorities appear to have higher ROCEs than those of the private operators.

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19 More detailed calculations on IFRS 16 are provided in **Annex 2.2** and **Annex 2.3** submitted alongside this response.

20 This is calculated as the sum of costs for site preparation, external works, drainage, external services, Section 278 works, and preliminaries.

6.2 Given the importance of the local authority estimates to the CMA's findings, Dignity would welcome further analysis by the CMA of whether local authorities properly accounted for operating costs in their P&L estimates – e.g. salary costs, grounds keeping, maintenance, and management costs.

6.3 As many local authority crematoria are also in urban areas, it will be necessary to assess whether the land and property values assumed by the CMA would fairly reflect the cost of a modern equivalent asset replacement. The CMA should use the land values from the UK Valuation Office Agency (see Appendix A) to estimate the replacement of crematoria in urban areas, such as Manchester, Birmingham, Liverpool, etc. Applying only the increased value to those crematoria in London in Scenario Two is unsound for crematoria in other cities of the UK.

6.4 There is also large variation that should be investigated further. On an economic profit per cremation basis, the 14 local authority crematoria range from -£800 to £500 per cremation.

7. Approach to EBIT

7.1 The CMA retains Dignity's burials revenues in EBIT despite reducing the size of the capital base (with the assumption of the 10 acre cap excluding cemetery grounds). Burial revenues averaged around [✂]% of Dignity's annual revenues in 2018 (i.e. in excess of £[✂] per annum). This inflates ROCE by increasing revenues without matching capital employed. Dignity disagrees with the CMA that this is "*a relatively small proportion of revenues*" and would have a "*relatively minor*" effect on ROCE.[21]

7.2 Dignity has previously explained how burial grounds affect the revenues and costs of a crematorium.[22] Dignity has also provided estimates for the proportion of grounds covered by graves.[23] The CMA has not taken this information into account in either its EBIT or land valuation analysis, and by including the burial revenues in EBIT while also bluntly capping the site size at 10-acres, is producing unrealistic and inflated ROCE estimates.

7.3 Dignity supports the CMA's initiative to collect additional financial data from parties for 2019 in order to provide the most up-to-date view on the sector. Dignity has updated the CMA's P&L and Balance Sheets information to include 2019 actuals and 2020 forecasts (see **Annex 2.4 – 2.6** submitted alongside this response). [✂].[24] Dignity also submits its Fixed Asset Register information to include 2019 (see **Annex 2.7** submitted alongside this response).

21 Paragraph 108 of the Working Paper.

22 See Dignity's response to *Approach to Valuation of Crematoria Land* Paper, December 2019.

23 See Dignity's response to Question 18 of the CMA questionnaire of 8 August 2019.

24 [✂].

8. The estimated WACC benchmark

8.1 The CMA estimates an 8% benchmark WACC, derived using the capital asset pricing model (CAPM), with this point estimate applied across the 2014-2018 period. Table 5 shows that this estimate sits within the range estimated by the CMA.[25]

Table 5
CMA estimates of WACC

	Low	High
Real RFR	-0.5%	0.5%
Real TMR	5.0%	6.5%
ERP	5.5%	6.0%
Asset beta	0.5	0.8
Equity beta	0.8	1.1
Real CoE	3.7%	7.0%
CPI	1.5%	1.5%
Nominal CoE	5.3%	8.6%
Nominal CoD	3.50%	4.50%
Gearing	40%	30%
Nominal pre-tax WACC	**5.3%**	**8.8%**

Source: Working Paper, Table 1

8.2 First, Dignity considers that the upper bound of the WACC range should be used. Each of the components of the WACC are estimates based on samples and assumptions, with the associated risks of measurement error. All points within the range are plausible, including the upper bound (8.8% in the table above). It is unreasonable then to set a lower point estimate as the benchmark against which to assess 'excessive profits' when higher levels are similarly plausible.

8.3 Second, Dignity is the only listed UK company. Using the CMA's own figures for Dignity reported in the working paper, the upper bound of Dignity's WACC range is 10% (see Table 6 below). This level is more in line with what Dignity itself used to make decisions during the period.[26]

8.4 Third, none of the other companies used in the CMA's sample operate in the UK. As the CMA has identified in its International Comparison Working Paper, there are significant differences between countries in terms of the dynamics of and risks facing funeral, cremation and burial activities. It is unsurprising to see this reflected in the wide variation

25 Paragraph 4 of the 'Cost of capital analysis' Working Paper.

26 During the relevant period, Dignity has relied on a pre-tax nominal WACC of [✂]% to [✂]% when conducting acquisition and investment appraisals relating to certain funeral branches and crematoria (see Dignity's response to the CMA's put-back paper).

in betas and gearings between the companies in the sample. It is not, therefore, clear that these are satisfactory comparators to develop a benchmark WACC for the UK market.

Table 6
CMA estimates of WACC based on Dignity's own beta and gearing level

	Low	**High**
Real RFR	-0.50%	0.50%
Real TMR	5.00%	6.50%
ERP	5.50%	6.00%
Asset beta	0.41	0.94
Equity beta	0.67	1.53
Real CoE	3.20%	9.70%
CPI	1.50%	1.50%
Nominal CoE	4.70%	11.20%
Nominal CoD	3.50%	4.50%
Gearing	41.00%	41.00%
Nominal pre-tax WACC	**4.90%**	**10.00%**

8.5 Finally, the CMA rejects the inclusion of a 'small company premium'. In the context of the thousands of 'atomistic' competitors in the funeral services market this seems extraordinary. Indeed, it is surprising even in the context of a standalone crematorium, facing high investment costs and a fixed location (limiting diversification), with revenues of under £2.5 million per annum – this would be a 'small' business.

8.6 Over 60% of the funeral services market comprises tiny independents. The majority are 'micro' or 'small' businesses. These tiny companies have a different risk profile to the six listed companies in the CMA's analysis above. As examples, an investor in a small funeral provider may face additional risks because: (i) smaller provider revenues would be less diversified in terms of the products and geographic markets served, and so more volatile;[27] (ii) smaller providers would face greater key-person risk; and (iii) an interest in a privately-held company may be less easy to trade than an interest in a publicly-traded company.

8.7 The CMA says that smaller firms may incur higher costs of debt but that its estimates are consistent with what it received from independents. The CMA's funeral services profitability working paper indicates, however, that it received information from only a small number of independents, and even for these there were data deficiencies. Therefore, the CMA should collect further data from small independents. The CMA has previously found that SMEs face more limited borrowing options and so higher borrowing

27 The CMA's own analysis in the price dispersion and funeral profitability working papers shows the volatility in small independent' revenues and margin year-on-year.

costs, suggesting it is unlikely the majority of the funeral services market faces the same cost of debt as the six listed companies.[28]

8.8 If the CMA is rejecting a 'small company premium' in the context of the funeral services market where most operators are micro businesses then the CMA is, in effect, suggesting a small company premium should never be applied in any market in the UK. This would be at odds with previous regulatory decisions in the UK that have included small company premiums.

8.9 The CMA should increase the benchmark WACC applied for the funeral services market to reflect the risk facing the majority of participants in the market.

8.10 Overall, therefore, a WACC in excess of 10% would be a more reasonable estimate given the circumstances of the UK market.

9. Errors in the modelling

9.1 Dignity identified data errors in the CMA's spreadsheet, in particular:

(A) The CMA has not capped the size of sites located outside the London area to 10 acres. Instead, it is using actual acreage for these sites.

(B) The CMA has mis-classified two Dignity sites, namely Bury and Shrewsbury. In particular, the CMA classifies the Bury crematorium as being managed on behalf of local authority. This is incorrect – Dignity owns this crematorium. Also, the CMA classifies the Shrewsbury crematorium as being owned by Dignity. This is incorrect – Dignity manages this site on behalf of the local authority.

(C) The CMA has mis-reported the acreage of the Wyre Forest crematorium site as 13 acres while this should be 24 acres.

28 CMA Retail Banking Market Investigation, 2016.

Appendix A: Evidence of land value estimates from the Valuation Office Agency

The VOA is the executive agency working in co-operation with the UK HM Revenue & Customs department and its role is to give the government the valuations and property advice needed to support taxation and benefits.[29]

The VOA has published land value estimates for the purpose of policy appraisal. These values are based on a number of assumptions. For example, residual land value is appraised from a social perspective and thus deduct allowances for things like developer's profits, marketing costs, and fees. Also, agricultural land values do not include any hope value for the fact that the site would be a crematorium. These assumptions mean these land values are likely a lower bound for the replacement value of crematoria.

Table 7 below shows the average land values per acre by land type, including and excluding London. It indicates that all land types except agricultural land are estimated at more than £350k per acre on average, and this value increases to almost £500k per acre when including London sites. Residential and Commercial (central city) land types are valued at over £1 million per acre on average.

Table 7
Average land values per acre by land type (2017)

Land type	Average land value per acre (£)	
	Inc. London	Excl. London
Residential Land	2,518,253	1,122,685
Industrial land	493,076	355,440
Commercial Land: Office Edge of City Centre	6,650,372	1,493,445
Commercial Land: Office Out of Town - Business Park	N/A	452,462
Agricultural Land	9,051	9,038

Source: Valuation Office Agency.
Notes: Average residential land values are calculated on the basis of estimated land values reported at the District Council level whereas average land values for all other land types are calculated on the basis of estimated land values reported at the LEP level.

Table 8 below shows the average land values per acre by crematorium used in the CMA's sample of 14 crematoria to estimate a land value of £90k per acre. It shows that the average land value of a site located in the same District Council or Local Enterprise Partnership (LEP[30]) area as 11 of these 14 crematoria[31] is at least £328k per acre if the site is not used for agricultural purposes.

29 https://www.gov.uk/government/organisations/valuation-office-agency

30 There are 38 LEPs in England. LEPs are voluntary partnerships between local authorities and businesses set up in 2011 by the Department for Business, Innovation and Skills to help determine local economic priorities and lead economic growth and job creation within the local area.

31 Three of the 14 crematoria are located outside England and fall outside the scope of the VOA data.

Table 8
Average land values per acre by crematorium used in the CMA's sample

Crematorium	District Council	LEP	Average land value per acre (£)				
			Residential Land	Industrial land	Commercial Land: Office Edge of City Centre	Commercial Land: Office Out of Town - Business Park	Agricultural Land
West Lothian Crematorium	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Fenland Crematorium	Fenland	Greater Cambridge and Greater Peterborough	196,356	328,947	4,405,870	892,713	8,502
Mendip Crematorium	Mendip	Heart of the South West	621,457	247,976	735,830	264,170	7,996
Kirkleatham Memorial Limited	Redcar & Cleveland	Tees Valley	149,798	129,555	350,202	149,798	6,984
Amber Valley Memorial Limited	Amber Valley	Derby, Derbyshire, Nottingham and Nottinghamshire	283,401	218,623	514,170	267,206	8,806
South Leicestershire Memorial Limited	Blaby	Leicester and Leicestershire	1,040,486	240,891	502,024	267,206	8,907
Waveney Crematorium and Memorial Park	Suffolk Coastal	New Anglia	906,883	228,745	458,502	237,854	8,502
South Oxfordshire Crematorium	Vale of White Horse	Oxfordshire	1,631,579	647,773	1,546,559	1,319,838	10,121
North Wiltshire Crematorium	Wiltshire	Swindon and Wiltshire	751,012	344,130	481,781	388,664	8,502
Denbighshire Memorial Limited	N/A	N/A	N/A	N/A	N/A	N/A	N/A
North Hertfordshire Memorial Park and Crematorium	North Hertfordshire	Hertfordshire	2,358,300	718,623	1,842,105	781,377	9,514
The Vale Crematorium	Wychavon	Worcestershire	827,935	283,401	350,202	283,401	8,603
Flintshire Memorial Park and Crematorium	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Barnby Moor Memorial Park & Crematorium	Bassetlaw	Sheffield City Region	149,798	222,672	350,202	222,672	9,211
Average			**810,637**	**328,303**	**1,048,859**	**461,354**	**8,695**

Source: Valuation Office Agency.
Notes: West Lothian, Denbighshire, and Flintshire crematoria are located outside England and are outside the scope of the VOA. Residential land values per acre are calculated at the District Council level whereas other land values for other land types are calculated at the LEP level. Land values reported for Industrial and Commercial land types correspond to the average land value per acre across all largest towns covered by the relevant LEP for which the VOA reported an estimate of land value.