

Appendix U: Profitability of crematoria

Introduction

1. In this Appendix we set out the specifics of analysing the profitability of crematoria in this market investigation. This should be read in conjunction with Appendix Q which details our approach to analysing profitability within this market investigation more widely.
2. In this Appendix, we explain the analysis we have undertaken in order to come to our profitability conclusions, and how we have taken into account the various submissions we have received from parties in response to our profitability working papers¹ and the PDR.²
3. The Appendix is structured as follows:
 - (a) First, we set out the scope of our profitability analysis, in terms of the relevant business activities, time period and companies covered.
 - (b) Second, we discuss our approach to ROCE analysis for crematoria services, with a focus on:
 - (i) Identification and valuation of capital employed; and
 - (ii) adjustments to EBIT.
 - (c) Third, we set out the results of our ROCE analysis, first for the largest providers of crematoria services, and then for the local authority crematoria, together with some commentary on those results.
 - (d) Fourth, we provide our conclusions based on the results of our analysis.
4. In an annex to this Appendix, we show the results of our analysis of the CIPFA Dataset, which includes information on the financial performance of a number of local authority crematoria and makes comparisons with the financial performance of the largest private crematorium operators.

¹ During the course of our investigation we have published two working papers in relation to this profitability analysis. On 24 July 2019, we published a working paper titled '[Approach to profitability and financial analysis](#)' (the 'profitability approach paper') setting out in detail our proposed methodological approach to the financial and profitability analysis. Further, on 20 February 2020, we published a working paper titled [Crematoria Profitability Analysis](#)' (the 'crematoria profitability paper') which presented initial profitability results.

² Funerals Market Investigation PDR

Scope of our analysis

5. Our financial analysis is focused on:
 - (a) The four largest crematorium operators:
 - (i) Dignity;
 - (ii) Westerleigh;
 - (iii) Memoria;
 - (iv) LCC; and
 - (b) A random sample of 22 local authority operated crematoria ('local authority crematoria') in the remaining portion of the sector.
6. Together, these operators run 117 crematoria located throughout the United Kingdom.³
7. In terms of the time period for the analysis we considered the 2014 to 2018 period. We planned to request 2019 data from all crematoria and to update our analysis accordingly. However, as a result of the COVID-19 pandemic (as further detailed in Section 1) we were unable to do so.⁴

ROCE Analysis

Approach to ROCE analysis

8. The overarching conceptual approach to return on capital employed ('ROCE') is further detailed in Appendix Q. Here we consider ROCE in the context of our analysis of crematoria.
9. ROCE is calculated as earnings before interest and tax ('EBIT') as a percentage of the capital employed by the party to provide crematoria services.
10. As set out in paragraphs 25 to 43 of Appendix Q, we are guided by the following key principles in carrying out our analysis:

³ According to the Cremation Society, there are approximately 300 crematoria in the UK.

⁴ We note that Dignity chose to provide us with 2019 financial information as part of their response to the crematoria profitability working paper. As we do not have 2019 financial information from other crematoria we have not presented this in our findings.

- (a) Return on capital compared with the weighted average cost of capital ('WACC') is our primary means of measuring profitability.⁵
 - (b) We determine the ROCE using operating profits and net operating capital employed. The general principle is that all revenues, costs, assets and liabilities necessarily arising from the operation of the business to supply the in-scope activities (ie the provision of crematoria services) should be included. We exclude financing costs, and taxation on income and any associated corporation tax or deferred tax.
 - (c) We start with accounting profits and the balance sheets for the operating units of the firms that undertook the relevant activities, and then make adjustments to arrive at a more economically meaningful measure of profitability.
 - (d) We also require common cost and asset allocations where a firm undertakes other business activities in addition to those which we are reviewing in the market investigation.
11. The main adjustments to accounting data set out in this paper relate to adjustments required to the value of capital employed in the business, together with associated impacts on the profit and loss account ("P&L").
 12. As noted in Appendix Q, the value of assets in the capital employed input should reflect their current value to the business ('VTB'). Modern equivalent asset value ('MEAV') is the most common outcome of a VTB assessment. This is the depreciated replacement cost of the asset in its current condition today. However, where the value in use of an asset (or its net realisable value) is less than its depreciated replacement cost, the value to the business of that asset is this lower figure.
 13. In most cases, therefore, we have sought to identify the MEAV of assets in order to estimate the capital employed by crematoria. In a few cases, we consider that certain assets would not be replaced (in their current size/form or location), such that a lower asset value is more appropriate. Our approach, therefore, seeks to identify the level of capital employed which is reflective of what a new entrant would need to enter and operate within a competitive market.

⁵ We use ROCE, where data permits, as this can be computed annually and thus provides greater insights into trends over time and the drivers of profits above the 'normal' level. In addition to looking at ROCE as a percentage, we also consider the related profitability metrics of economic profits per cremation, and economic profits as a percentage of "cost plus" in order to obtain a fuller picture of profitability. Economic profits are defined as $EBIT - (\text{Capital employed} \times WACC)$. Cost plus is defined as $\text{Revenues} - EBIT + (\text{Capital employed} \times WACC)$.

14. We have assessed the financial information provided by crematorium operators that are within the scope of our analysis and considered their comments on the adjustments they consider necessary to update their financial information to reflect replacement cost.

Identification and valuation of capital employed

15. This section of the Appendix sets out our approach to: (1) the identification of the operating capital employed required to provide crematoria services and (2) the valuation of those assets.
16. The main categories of assets recorded on the balance sheets of the four largest crematorium operators are:
 - (a) Tangible fixed assets, such as land, buildings and cremator equipment;
 - (b) intangible fixed assets, such as goodwill;
 - (c) working capital, which comprises operating current assets such as inventory, trade debtors, other debtors and VAT, and operating current liabilities such as trade creditors and other creditors; and
 - (d) other current assets such as cash.
17. In this section, we consider each of these categories of assets in turn and set out the approach that we have taken to the recognition and valuation of these assets in our analysis.

Tangible fixed assets

18. The tangible fixed assets related to the provision of crematoria services are typically, land, buildings and cremator equipment.
19. These assets tend to be valued on the balance sheet at historic cost less any depreciation charged against the asset over its useful life, apart from land which is not depreciated. In some cases, assets will have been 'fair valued' on acquisition (see paragraph 22 below). We asked the parties questions to inform our understanding of the cost of replacing these assets. We asked whether:
 - (a) net book value ('NBV') was a good approximation for the cost of replacing the assets in their current condition. For example, could you:
 - (i) purchase your land and construct the cremation buildings at a cost in line with the net book values etc?

(ii) purchase your cremation equipment at their net book values?

20. All parties noted that NBVs were not a good proxy for replacement cost, as explained in more detail below.
21. Memoria said, 'There are two major reasons why accounting values do not form a good proxy for replacement cost in Memoria's case: Depreciation [...] [and] increases in site sizes and relevant costs [...]'.
22. Westerleigh also told us that 'The net book value of tangible fixed assets are based on depreciated cost (ie when the asset/land was acquired), including where relevant fair value adjustments on business combinations.' Moreover, 'the depreciation of tangible fixed assets in line with accounting standards is not designed to derive the replacement costs of an asset at the balance sheet date'.
23. Dignity told us that it does not consider the NBV of crematoria in the Fixed Asset Register ('FAR') to be a reliable estimate of the replacement costs for its portfolio of crematoria.
24. Finally, LCC told us that 'The NBV is not a good approximation for the cost of replacing the main assets required to provide crematoria services'.
25. Parties also noted that it is standard in the crematoria sector that there is not typically a second-hand or resale value for crematoria assets.
26. Westerleigh stated 'If replaced, plant and equipment would be replaced with new equipment. Therefore, depreciated cost would significantly understate the cost of a new replacement.'

Land

Approach to valuing land

27. We consulted on our [Approach to Valuation of Crematoria Land](#) ('land valuation consultation'), in which we proposed commissioning an independent, expert report on the MEAV of land employed by the crematoria for which we did not have recent information on acquisition costs.
28. In the land valuation consultation, we explained our view that, in the context of the crematorium sector, 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:

- (a) Be appropriately located to serve the population served by the existing crematorium;
 - (b) meet the relevant criteria for a suitable plot for a crematorium in terms of size, aspect, road access etc;⁶ and
 - (c) have, or have a reasonable prospect of obtaining, planning permission for use as a crematorium.
29. We highlighted that these criteria meant that the MEAV would not necessarily be a valuation for the same site as is currently employed by a firm. For example, the MEAV may be either smaller or larger than the existing site or in a different location.
30. In addition, we noted that the MEAV should reflect a situation of ‘normal’ market conditions, ie where both the buyer and seller of land have a number of potential options such that neither party is a necessary counterparty for the other.
31. However, we did not receive any bids from experts in response to either of our two invitations to tender.⁷
32. Therefore, we considered the range of information collected to date on land valuations to identify the most reliable estimates of replacement cost. We considered:
- (a) the carrying values of land in parties’ financial records;
 - (b) the Cushman & Wakefield report submitted by Dignity; and
 - (c) information on recent purchase costs collected from Memoria, Dignity and Westerleigh.
33. We observed that the carrying value of land in the parties’ financial records was unlikely to provide a good proxy for the MEAV of this asset in many cases and, furthermore, was not recorded on a consistent basis across the parties. For example, [redacted], while Westerleigh’s assets were revalued in 2016 at the time of its acquisition by Ontario Teachers’ Pension Plan and

⁶ [The Siting and Planning of Crematoria](#)

⁷ In response to the first procurement round, we sought feedback from potential suppliers regarding their reasons for not bidding. A number of parties indicated that the timing of the procurement process (in December) and the two-week timeframe for submitting bids had prevented them from participating. Hence, we re-ran the process in January/February 2020 and extended the time period for submitting bids (from two to three weeks). However, this second process also failed to generate any bids.

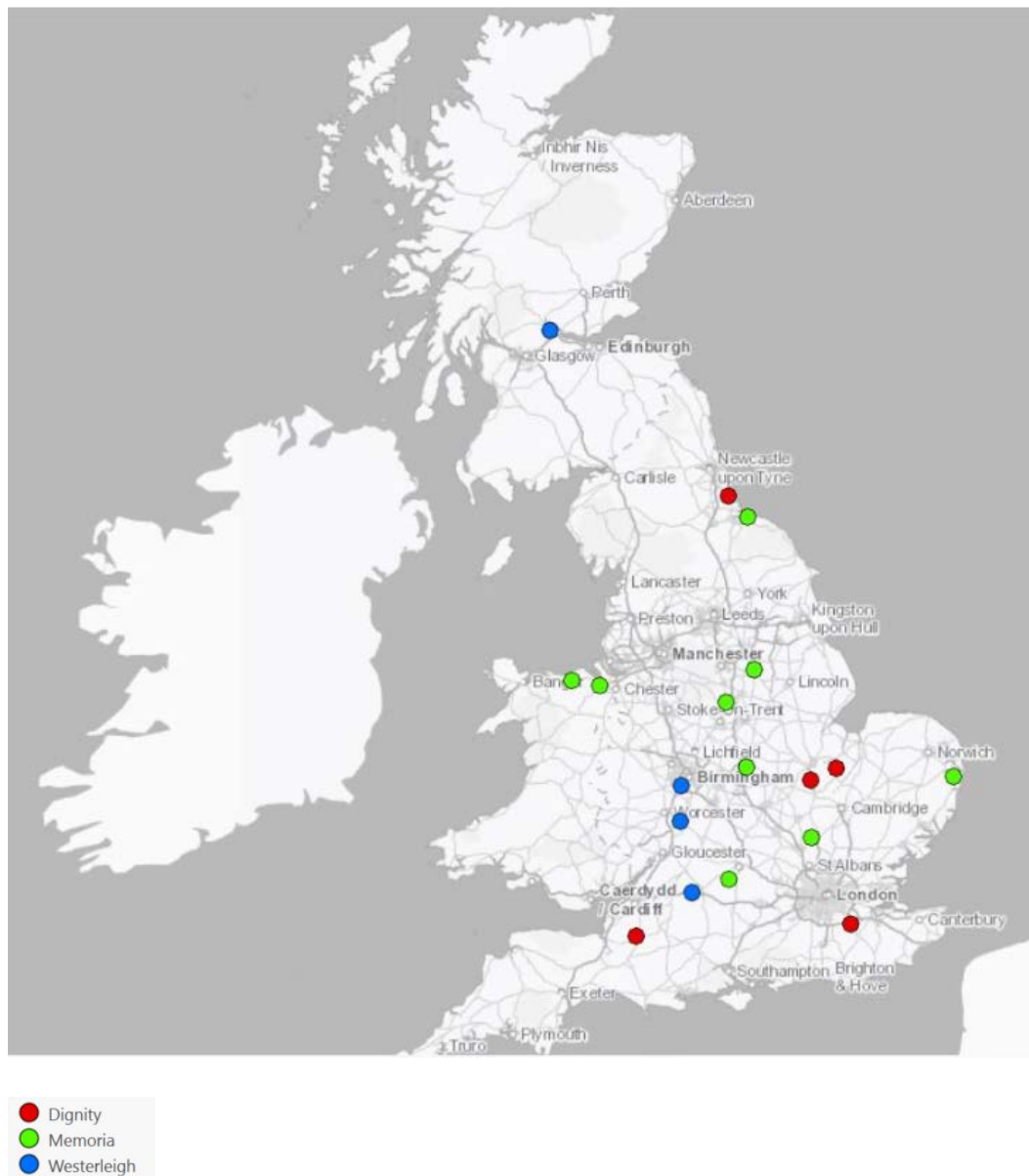
Universities Superannuation Scheme. In other cases, land was recorded at cost at the date of acquisition which was many years ago.

34. Next, we reviewed the Cushman & Wakefield report submitted by Dignity. This report gave the (depreciated) replacement cost of Dignity's crematoria land and buildings. However, we were concerned that the approach adopted was likely to result in an over-valuation of the land on an MEAV basis. For example, Cushman & Wakefield valued a number of the sites ([X] out of [X]) on the basis of residential or long-term residential alternative use. In contrast, Memoria told us that 'the vast majority of all UK crematoria applications in the last 20 years have been proposed on land designated for open-countryside.' As residential land is generally the most valuable land use in the UK and agricultural land is one of the lowest value land uses, this approach is likely to over-value the land, even taking into account the fact that a crematorium operator is likely to have to pay a material premium over agricultural use value for a suitable site (ie one that is able to gain planning permission).
35. We compared the average price per acre of land estimated by Cushman & Wakefield for Dignity with the average price per acre paid by firms opening new crematoria in the last ten years. Cushman & Wakefield's report implies a valuation of [£500-700k] per acre for Dignity's existing sites. In comparison, recent entrants have paid an average of around £103,000 per acre.⁸ This difference appears to have been driven in part by the valuation of a few very large sites at residential valuations with no adjustment for their size in the Cushman & Wakefield report.⁹ In practice, at the land valuation provided by Cushman & Wakefield, such sites would not be economic for use as a crematorium. If these sites are excluded, the average price per acre declines to [less than £200k]. We note that this estimate is still significantly more than crematorium operators have paid in recent years.
36. Finally, we considered the information we collected on purchase costs incurred since 2010. As Figure 1 below shows, this data includes 18 sites with broad geographic coverage in the UK, although none of the sites are located in Greater London, ie within the M25. We consider that this information is likely to provide a good proxy for the MEAV of land, given that it reflects the actual costs incurred by crematorium operators for sites of a suitable size, location and aspect and which have been able to obtain planning permission for use as crematoria.

⁸ This figure has been revised following the provision of further transaction values by crematorium operators. When we published our profitability working paper, the average price per acre from recent transactions was £89.5k.

⁹ These sites are Dignity's crematoria in [X].

Figure 1: Map of coverage of purchase costs of land since 2010 and key



37. Figure 1 shows the coverage of recent land purchase costs for the 18 data points used. Three of these 18 sites have not yet opened but were purchased after 2010 and have obtained planning permission. We have not included transactions where the purchase of land has not yet been completed as the development of a crematorium on such a site is uncertain and, in any case, not likely to be completed for a few years. As such, these purchase costs may not be reflective of the costs of replacing the land asset during the 2014 to 2018 period.
38. In carrying out our profitability analysis on crematoria, we drew primarily on recent purchase prices in order to identify a reasonable per acre valuation for crematorium land. These transactions form the basis of our 'Case One' results. Recognising the uncertainty in this area we also considered a

sensitivity with higher land value to understand whether this had a material impact on our analysis, named 'Case Two'. We considered the cases as follows:

- (a) Case One¹⁰: we valued all sites in the UK at £103,000 per acre, based on evidence from recent transactions. We capped the size of the “modern equivalent” plot of land at 20 acres and included all revenues earned from crematorium operators’ sites (cremation fees, memorials and burial revenues) in earnings. In addition, we capitalised average planning costs of a further £428,000 per site, as explained in paragraph 41.
 - (b) Case Two¹¹: we valued all sites in the UK at [£200-300k] per acre based on evidence from the Cushman & Wakefield report¹², submitted by Dignity. All other assumptions are the same as in Case One.
39. When we performed our analysis, we initially performed another sensitivity: we valued all sites in the UK at £103,000 per acre but capped the size of sites at 10 acres and excluded all revenues and costs associated with burials. In this sensitivity we also capitalised average planning costs of £428,000 per site.
40. When we performed this sensitivity, we noted that the results were very similar to those of Case One outlined above. As such we have not considered this sensitivity further in our analysis but instead continue with Case One and Case Two outlined at paragraph 38.
41. Finally, we gathered information on the costs incurred by Dignity, Westerleigh and Memoria in obtaining planning permission for sites in the past ten years. We calculated the average cost of obtaining planning permission for a crematorium, and then adjusted this for the probability of failing to obtain permission. This gave a planning cost of £428,000 per site. We added this cost to the calculated value of land for all crematoria built prior to 2010. For those built in recent years, we used the actual planning costs incurred as provided by the parties.
42. We note that it is likely that some parties have expensed the planning costs incurred through their P&L, which we have capitalised on the balance sheet.

¹⁰ Case one was referred to as the 'Base case' in our PDR

¹¹ Case two was referred to as the 'Sensitivity' in our PDR

¹² This figure of [£200-300k] was calculated by including all sites in the Cushman & Wakefield report located outside the M25, ie excluding the 3 sites in Greater London. We note that this figure includes one relatively large site ([£]), which has a valuation of £[£]million and, as a result, would not be replaced. As explained in paragraph 35, excluding this site (but including one Greater London site, [£], with a more moderate valuation), reduces the average value per acre to £[£]. For this reason, we consider our use of [£200-300k] to be very generous to the parties.

Therefore, for parties which have opened new sites during the Historic Period it is likely these costs have been double counted. Where this has occurred, it will artificially reduce the party's ROCE. This effect will be particularly significant for those operators who have opened a significant number of new crematoria over the relevant period, ie Memoria and Westerleigh.

Parties' views

43. In response to our profitability working paper and the PDR, parties made a number of submissions relating to: our use of transactions since 2010 to value land; our decision to cap the size of a replacement site; our inclusion of burial revenues and costs in the firms' earnings and our decision not to capitalise leasehold assets.
- *Use of recent transactions*
44. Westerleigh told us that it would 'assume land value increases of [X] per annum' and that the 'effect of using a constant land value over the five-year period does not therefore reflect reality based on Westerleigh's experience and inflates the ROCE'.¹³ We understand this to mean that Westerleigh considers we should not include or place weight on earlier transactions in the period 2010 to 2019, as they would have a lower value, or that we should inflate earlier transaction values by [X]% per year to obtain a 2018 value.
45. Dignity told us that Case One was unrealistic and went on to say that it 'considers that the per acre cost of replacing the land of its crematoria is best approximated by the values reported by Cushman & Wakefield. Case Two should, therefore, be the starting point of the CMA's assessment'.¹⁴
46. Dignity told us that the CMA 'must obtain valuation advice from an appropriately qualified specialist to value the crematoria of other providers included in the CMA's analysis'.¹⁵
47. Dignity provided average land values per acre by land type from 2017, as estimated by the Valuation Office Agency. Dignity told us that the 'CMA should use the land values from the UK Valuation Office Agency to estimate the replacement of crematoria in urban areas'.¹⁶

¹³ Westerleigh response to crematoria working paper dated 17 June, page 20, paragraph 80

¹⁴ Dignity response to Crematoria profitability working paper, dated 12 June, page 8, paragraph 4.5

¹⁵ Dignity response to Crematoria profitability working paper, dated 12 June, page 1, paragraph 1.2 (C)

¹⁶ Dignity response to Crematoria profitability working paper, dated 12 June, page 11, paragraph 6.3

48. Dignity noted that the CMA 'based its valuation estimates on a sample of 18 recent crematoria land transactions' but submitted that the sample was 'not representative of crematoria in the UK'.¹⁷ Dignity told us that 'over two-thirds of crematoria in the UK are in 'Urban' areas' and that 'the CMA's sample of 18 is biased to 'Rural' areas'.¹⁸
49. Dignity submitted that 'The CMA's biased sample leads to its unrealistically low land value estimate of £103,000 per acre'.¹⁹
50. Dignity submitted that the CMA's use of completed recent transactions introduces a selection bias into the analysis because it excludes situations where Dignity has 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.²⁰
51. Memoria went on to say that: 'Land valuation is a critical component of crematoria capital values and therefore of ROCE, and such a crude approach to valuation for Memoria's rivals is therefore unlikely to provide reliable comparisons across crematoria or reliable results for individual crematoria sites'.

- *Exclusion of London values from sensitivity*

52. In response to our Crematoria profitability paper, LCC submitted analysis that suggests that London crematoria charged lower prices on average than non-London crematoria, while undertaking 20% lower volumes per unit. LCC explained that adopting the CMA's methodology for estimating capital employed and assuming a 10-acre site size, a median crematorium in London would be expected to have capital employed of approximately £25 million²¹. Our ROCE analysis would suggest that such a business should be making an 8% return on this capital employed, which equates to "normal" profits of £2 million per annum. In contrast, LCC estimates that the median London crematorium may only earn revenues of around £0.8 million, with profits likely to be considerably below this figure. LCC concluded that either our methodology for assessing the level of capital employed in a crematoria is

¹⁷ Dignity response to PDR, annex, pages 12 to 13, paragraphs 3.10-3.11

¹⁸ Dignity response to PDR, annex, page 13, paragraph 3.11

¹⁹ Dignity response to PDR, annex, page 15, paragraph 3.12

²⁰ Dignity response to Crematoria profitability working paper, dated 12 June, page 8, paragraph 4.4 (D)

²¹ This analysis was based on one of the sensitivities presented in our Crematoria working paper, where we capped site sizes at 10 acres and used a land value of [£1.75million-£2million] per acre for sites within the M25.

wrong or, alternatively, the London crematoria market has a very serious issue around the long-term sustainability of crematoria provision.²²

53. In response to our PDR, Dignity told us that by ‘assuming away sites that are ‘uneconomic to replace in their current locations’, the CMA is clearly biasing the excess profits test’.²³ Dignity went on to state that the sensitivity should ‘simply be the Sensitivity Two²⁴ from the working paper, now with a 20-acre cap (if a cap is applied at all)’.²⁵
54. Memoria submitted that ‘the relevance of the fact that these sites [meaning sites located in London] would not be built in these locations at current valuations is unclear’.
55. LCC told us that ‘cost calculations fail to take sufficient account of the variation in land values by location, the variation in other costs and asset values by location’.²⁶
 - *Capping site sizes and including burials revenues*
56. Westerleigh told us that it spends ‘considerable time and investment selecting sites with large grounds that guarantee a peaceful setting free from noise and pollution [...] This enables Westerleigh to differentiate itself from incumbent crematoria [...] and is an important aspect of the 'qualitative pull' of Westerleigh's sites’.²⁷
57. Westerleigh also told us that its ‘[redacted]’.²⁸
58. Further, Westerleigh told us that ‘the CMA's approach implicitly assumes that Westerleigh has made irrational commercial decisions to acquire more land than it needs. It is not open to the CMA to make assumptions of this nature.’²⁹
59. However, [another view expressed was] [redacted] that ‘MEAV analysis should assess alternative sites against currently and potentially smaller plot sizes, enabling a more dynamic structure of the market to exist over time’.

²² LCC response to Crematoria working paper, page 18, paragraphs 6.4-6.8.

²³ Dignity response to PDR, annex, page 16, paragraph 3.17

²⁴ Sensitivity Two referenced here refers to a sensitivity performed in the crematoria profitability working paper where all sites were valued using the Cushman & Wakefield report, ie a value per acre of [£200-300k] for non-London sites and a value of [£1.75million-£2million] for sites within the M25.

²⁵ Dignity response to PDR, annex, page 16, paragraph 3.19

²⁶ LCC response to PDR, page 2, paragraph 3.1

²⁷ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 9, paragraphs 32 to 36

²⁸ Westerleigh response to PDR, page 37, paragraph 121

²⁹ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 10, paragraph 38

60. LCC told us that ‘Local authority (LA) and private crematoria operators had traditionally constructed large crematoria but there was evidence that new builds were getting smaller. [...] LCC considered that the industry and the planning authorities would need to adopt a collaborative approach in the future to avoid the potential for over capacity. For example, planning authorities may not allow a facility that can cater for 3,000 cremations per year, but there might be scope for an 800 to 900 facility. LCC had not heard of any risk in the market of there being an overcapacity issue.’³⁰
61. Dignity submitted that ‘The CMA retains Dignity’s burials revenues in EBIT despite reducing the size of the capital base [...] This inflates ROCE by increasing revenues without matching capital employed.’³¹
62. Westerleigh told us that our inclusion of revenue from burials in Westerleigh’s earnings unfairly inflates its ROCE for the purposes of assessing competitive dynamics in the crematoria sector, noting that burial services are explicitly excluded from our definition of ‘crematoria services’. Westerleigh told us that only ten of its portfolio of crematoria sites have burial grounds, and at only [X] of its sites does burial activity account for more than [X] of total funerals.³²
63. Westerleigh explained that the overheads incrementally incurred in relation to burial are typically negligible for most sites, [X]. This means that including revenue from burials materially overstates Westerleigh’s ROCE from the provision of cremation services. In addition, Westerleigh told us that it was not possible to split overhead expenses between cremation and burial revenue streams because [X].³³
- *Capitalising leasehold land*
64. Westerleigh noted that [X]³⁴ of [its] current operational sites are long-term leaseholds typically with terms of [X]³⁵ and that ‘the CMA places no value on the land operated under these leasehold assets’.³⁶
65. Westerleigh went on to tell us that ‘The leaseholds are therefore simply a financing choice and the leasing costs are financing costs equivalent to the

³⁰ LCC hearing summary, page 2, paragraph 9

³¹ Dignity response to Crematoria profitability working paper, dated 12 June, page 10, paragraph 7.1

³² Westerleigh response to Crematoria profitability working paper, dated 17 June, page 25, paragraphs 100-103.

³³ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 25, paragraphs 104-105.

³⁴ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 11, paragraph 41.

³⁵ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 11, paragraph 41

³⁶ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 11, paragraph 42

financing used to fund purchase of a freehold'³⁷ and 'Indeed, under new accounting rules (IFRS 16), leaseholds are required to be included in the balance sheets as right of use assets, with the rentals being treated as a financing cost. Westerleigh could choose to adopt IFRS and apply the relevant policy for leasehold capitalisation'.³⁸

66. Further, Westerleigh told us that at [redacted] of its leasehold sites it has purchased free hold land at or adjacent to the leasehold site: [redacted].³⁹
67. Westerleigh also told us that it is incorrect that 'capitalising leasehold assets would be offset by the removal of lease payments from P&L'.⁴⁰
68. Similarly, Dignity told us that the land of five of its crematoria sites operated under long-term leases should have been capitalised or the values from Cushman and Wakefield used.⁴¹
69. Memoria noted that 'the CMA does appear to have adjusted the value of Memoria sites that were purchased but subject to royalty payments [...] but only in relation to sites for which Memoria also paid an up front land cost [redacted].

CMA Approach

- *Use of recent transactions*

70. We note parties' views on our approach to land valuation and the appointment of a specialist. As explained above, two separate invitations to tender did not generate any bids and as such we proceeded to use the range of information available to us on recent transactions by crematorium operators to identify the most reliable estimate for the value of land per acre. Where parties have provided further information on recent (completed) transaction values, we have updated our analysis to take these into account.
71. We recognise that the approach we have used produces average, rather than site-specific land valuations. As a result, we have taken care to draw our conclusions at the aggregate rather than site specific level, eg at the level of private crematoria companies and the local authority sample as a whole, rather than focussing on the results for individual sites.

³⁷ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 12, paragraph 46

³⁸ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 12, paragraph 47

³⁹ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 12, paragraph 45

⁴⁰ Westerleigh response to PDR, page 40, para 133

⁴¹ Dignity response to PDR, Annex 1, paragraph 3.23

72. We consider that estimating the replacement cost of crematoria sites based on 18 transactions drawn from across the country over the last 10 years is likely to produce reasonably reliable valuations. These transactions reflect the actual sites that firms have chosen in terms of size, location and layout, and the actual costs they have incurred to secure those in the open market. We note that, to the extent that crematoria have market power and are able to make supernormal profits, and planning restrictions limit the availability of suitable sites, these transaction values may be bid up above the level that would be observed if the market for cremation services were well-functioning. This may introduce a circularity in our analysis, masking some of the supernormal profits. We have not sought to adjust for this factor but observe that it may bias our ROCE estimates downwards.
73. With respect to Dignity's point about a large proportion of the transactions being in rural areas, this reflects the sites that have been chosen by crematorium operators over the last decade, which we believe provides strong evidence that such sites and locations reflect the modern equivalent asset of existing crematoria. We considered this further in the context of LCC's submission regarding our approach to valuing sites in Greater London and the actual profitability of such sites (see paragraph 52).
74. We have considered Dignity's submission that we should include pricing from the Valuation Office Agency ('VOA'). However, the VOA data relates to general categories of land eg residential, commercial, industrial and agricultural, whereas the figures we have used reflect what crematorium operators have actually paid for land suitable for use as a crematorium. We consider that the latter is likely to provide a more accurate estimate of the cost of replacing crematoria sites, than the VOA's data on general categories of land.
75. While we are comfortable that estimating the replacement cost of crematoria sites based on recent transactions is the best available approach, we recognise that our dataset is limited to 18 sites. As a result, it may not fully reflect the average replacement cost of the whole UK portfolio of crematoria to the extent that the sites built in recent years may serve (somewhat) different geographic locations from existing sites and to the extent that, if operators wished to replace existing sites, they might choose locations that were more urban, on average, than these transactions. This may be a particular issue in the Greater London area, where the distances between central areas and greenfield sites are significantly greater than for other cities in the UK, and where we do not have much evidence regarding the types of sites that operators might choose and the associated costs they would incur.
76. In this context, we note the following evidence is relevant:

- (a) The average value per acre estimated by Cushman & Wakefield for Dignity's estate was £[redacted], once three outlier sites (which were both particularly large and particularly expensive per acre) were excluded. This valuation largely reflected the existing locations of sites (ie whether they were in urban or rural areas);⁴²
- (b) The Cushman & Wakefield report which valued Dignity's London sites at an average price of around [£1.75million-£2million] per acre, comprised the following valuations:
 - (i) East London Crematorium: just over £[redacted]million, which equates to £[redacted]million per acre for the 33-acre site;
 - (ii) South London Crematorium: £[redacted]million, which equates to just over £[redacted]million per acre for the 63-acre site; and
 - (iii) Beckenham Crematorium: just under £[redacted]million, which equates to around £[redacted] per acre for the 44-acre site;
- (c) Dignity recently paid £[redacted]million for a 7-acre site with planning permission for a crematorium near Sevenoaks, just outside the M25. This is equivalent to around £[redacted] [£400,000-£450,000] per acre, once we remove our estimate of average planning costs of £428,000.

77. We agree with LCC's conclusion that, at the level of land values in London set out in the Cushman & Wakefield report (of [£1.75 – £2 million]), it is not possible for a crematorium to make a return equal to its cost of capital. This is consistent with our observation that new crematoria have not opened in London in recent years. This suggests that, if deprived of these assets, crematorium operators would not seek to replace them – at least not in their existing size/form and locations. We thought that, to the extent that central locations were particularly important, operators may seek to use significantly smaller sites (where possible).⁴³ Alternatively, operators may seek more standard-sized sites further from the centre of London.

78. Cushman & Wakefield's valuation of Dignity's Beckenham site suggests that it is possible to acquire suitable land for a crematorium within the M25 at a per-acre price that is around 25% above our average from recent transactions and

⁴² Cushman & Wakefield valued 32 out of 41 sites in their existing locations, as opposed to identifying an alternative plot of land nearby.

⁴³ We note that there are currently a few crematoria on small plots, ie of less than 3 acres.

less than a third of the price that Dignity paid for its Sevenoaks site (the value of which has been included in our transaction average figure of £103,000).⁴⁴

79. Together this evidence does not suggest that our average transaction figure is likely to be significantly wrong, when applied as an average across the UK. However, recognising the uncertainties around land valuation, the limited data that we have available and the observation that the recent transactions may be more rural than average (in the context of the thought experiment of all existing crematoria being replaced), we have placed some weight on our “Case Two” when interpreting the results of our analysis. This case is based on a land valuation of [£200-300k] per acre, which we consider is highly favourable to the parties as a national average figure, ie it allows for very significantly higher land values in Greater London and other large urban areas.

- *Capping site sizes and including burials revenues*

80. We considered Westerleigh’s submissions that its freehold sites are close to [X] acres in size and that it has, in some instances, [X]. However, we observe that i) the average site size acquired in the last 10 years by the private operators has been just under 10 acres, ii) the average size of Westerleigh’s crematoria is 20.5 acres and this figure is skewed upwards by 4 sites which are over 40 acres each⁴⁵, and iii) that the two largest sites (purchased in the last decade) were only just over 20 acres (21 acres each). This suggests that a site size cap of 20 acres is reasonably generous.⁴⁶

81. We noted parties’ responses regarding the inclusion of burials income in revenue. While we agree that burials are a separate activity from providing cremation services (and are not the focus of this market investigation), they are generally provided using much of the same cost base (land, grounds maintenance etc), for example, see Westerleigh’s submission in paragraph 63 above. The fact that an operator incurs negligible incremental overhead costs from providing burial services, suggests a significant efficiency from providing cremation and burial services jointly. For this reason, and in light of our decision to cap site sizes at 20 acres, which allows significant space for burials, we think that excluding burial revenues and the negligible incremental

⁴⁴ We observe that when purchasing a site in Sevenoaks, which was relatively expensive, Dignity chose a smaller than average plot, which may reflect the trade-off we discussed in paragraph 75 between size, price and location.

⁴⁵ CMA analysis of source data

⁴⁶ Separately, we note that we have included up to 20 acres of freehold land where this has been purchased in addition to leasehold land at Westerleigh’s sites.

overhead costs would provide a distorted view of the profitability of crematoria services.

82. In addition, we note the following practical challenges to separating out burial or cemetery revenues and costs:
- (a) Dignity told us that it was not able to separate out the costs of providing burials from the general running of its crematoria sites.
 - (b) Westerleigh told us that costs associated with the closed cemeteries at [redacted] sites cannot be excluded as these are [redacted]. In order for Westerleigh to operate these crematoria, the costs of maintaining the closed cemeteries are necessary and unavoidable. In tendering the operation of crematoria and the maintenance of closed cemeteries over the long term [redacted], the local authorities in question have outsourced the risks involved with these closed cemeteries.⁴⁷
83. Therefore, we have included burials revenues and costs in our profitability analysis.
- *Capitalising leasehold land*
84. Next, we considered parties' submissions that we should capitalise land held on long leaseholds and include this in their capital employed on the basis that the choice between leasehold and freehold reflected a financing rather than operational decision.
85. We recognise that crematorium operators may choose between leasehold and freehold for financing reasons, but we do not think that there is a compelling reason to capitalise leasehold assets in this case. In particular:
- (a) We would not expect such an adjustment to have a significant impact on our measure of economic profits since the increase in asset values would be offset by the removal of lease payments from the P&L;⁴⁸
 - (b) we note that the two largest private crematorium operators both have a mix of leasehold and freehold sites, hence comparisons between them are not distorted by our approach;
 - (c) our estimate of the weighted average cost of capital of a crematorium operator, includes a relatively low level of gearing, which is consistent with

⁴⁷ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 25, footnote 46.

⁴⁸ While ROCE percentages can be affected by these decisions, this would not have an impact on our interpretation of the firms' profitability, which takes into account a number of metrics.

a business model that holds a reduced level of freehold assets (eg a mix of owned and leased land). Memoria, which owns all its sites, told us that it supported a significantly higher level of gearing than the 30% to 40% range we have used in estimating the WACC for crematoria; and

(d) finally, we note that lease payments are a matter of fact, reflecting the actual costs that parties are incurring for the land on which crematoria are sited. Replacing these costs with our assessment of land values introduces a further judgement, and we do not believe that there is a compelling reason to make such an adjustment.

86. Where a party has indicated that it owns freehold land at a site otherwise considered to be leasehold, we have included the freehold land, subject to the 20-acre site size cap.
87. However, in light of parties' submissions, we performed a sensitivity whereby sites identified by the parties as held under long-term leases were included in their capital employed and corresponding rental income was removed from the Profit and Loss account. The results of the sensitivity can be found at paragraphs 241 and 242.
88. We noted Memoria's submission regarding the treatment of its sites subject to royalty payments. We understood that of Memoria's sites, two were purchased via significant capital payments with an additional land royalty payable each year based on the number of cremations performed at the site, while for one it incurred no upfront cost⁴⁹ but pays the landowner entirely via a royalty.
89. For those sites which comprised both capital and land royalty elements, we considered that they formed part of Memoria's asset base and that the land royalty element constituted part of the value of the asset. As such, we valued the royalty using the net present value of future cashflows and added this to the initial upfront cost. The value of land royalties paid were stripped out of the Profit and Loss account and these assets were included in Memoria's capital employed.
90. For the site for which Memoria pays only a land royalty, we concluded that only the upfront payments of stamp duty land tax and planning costs should be included within Memoria's estimation of capital employed and did not perform any adjustment to the land royalty payments made through the Profit and Loss account.

⁴⁹ Except for stamp duty land tax and planning costs

- *Increase in land value over time*

91. We considered Westerleigh's point regarding the potential increase in land values over time. First, we note that our sample includes transactions from 2010 to 2019 (inclusive) and therefore represents a reasonable average value for the 2014 to 2018 period. We do not agree that using only the most recent transaction values would be appropriate in this context as that would be likely to overstate the average value for the period. Second, to the extent that land values have increased over the relevant period, these capital gains should be passed through the P&L as profits since economic profitability analysis requires the full articulation of the accounts. Such gains would increase EBIT over the period and, therefore, ROCE. The overall impact on measured ROCE is, therefore, ambiguous. Finally, we think that reducing our effective sample size, ie limiting ourselves to those transactions that took place in 2018 only (to reflect values at the end of the period), would be more likely to introduce bias into our analysis as we would lose broad coverage of the country.

- *Our revised approach*

92. We have not altered our approach from that set out at paragraph 38 based on the submissions made by parties since the PDR. Sensitivity analysis performed on the future profitability of crematoria and the capitalisation of leasehold land can be found in the Interpretation of our analysis section of this appendix.

Buildings

93. Consistent with Appendix Q, our approach was to ask parties for evidence on what a good approximation for MEAV would be, where book value was not. All large crematorium operators confirmed book value is not a good approximation for NBV, so we used replacement cost estimates prepared for the purposes of insurance as a proxy for MEAV.
94. For each crematorium owned by each party, we revalued the building based on the replacement cost estimate included in the parties' insurance policy and applied depreciation.
95. Where a party did not provide the replacement cost estimate for its crematorium, we valued its building using a simple average of the estimates provided by other parties. We removed four replacement cost estimates from this calculation, as their estimates did not appear to be credible as full reinstatement costs.

96. We applied straight line depreciation to the building from the point at which the crematorium was first constructed using a useful economic life of 100 years. Where the building was over 100 years old, we recorded a value of £nil. In our set of 117 crematoria, there are 9 fully depreciated buildings.

Parties' views

97. Memoria told us that it 'does not believe that its buildings will realistically have a useful economic life of 100 years [X]. It is unclear why the CMA has felt the need to depart from Memoria's own depreciation schedule', [X].
98. However, LCC told us that it 'does not consider that a generalised assumption by the CMA that all crematoria buildings cease to have any remaining useful life and hence no value beyond 100 years is reasonable or sustainable'⁵⁰ and provided evidence that the average age of a crematorium in the UK is 51 years, and in London is 76 years.⁵¹
99. Dignity also told us that '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.'⁵²
100. Similarly, Westerleigh told us that the 'CMA's approach wrongly depreciates capital improvements to sites based on the age of the site. The CMA's calculations use latest replacement cost for insurance purposes, depreciated based on the age of the site, with an assumed total life of 100 years. This methodology means that recent improvements and enhancements to the site are overly depreciated, understating the capital employed in the asset.' Westerleigh told us that adjusting for recent capital improvements would reduce measured ROCE by 0.1 percentage point.⁵³
101. In response to the crematoria working paper, Dignity told us that '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'.⁵⁴
102. Similarly, Westerleigh submitted that our approach to valuing land (and buildings) 'makes no allowance for land development costs associated with

⁵⁰ LCC response to Crematoria working paper, page 16, paragraph 5.35

⁵¹ LCC response to Crematoria working paper, page 16, paragraph 5.31

⁵² Dignity response to Crematoria profitability working paper, dated 12 June, page 9, paragraph 5.3

⁵³ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 24, paragraph 98

⁵⁴ Dignity response to Crematoria profitability working paper, dated 12 June, page 10, paragraphs 5.6-5.7

initially developing a site for a crematorium, including extensive site design, enabling and preparation work including the provision of off-site infrastructure and services. Westerleigh explained that for a typical site this would include inter alia:

- (a) Ground stabilisation and site remediation including removal or capping of contamination;
- (b) earthworks within the site to provide appropriate development levels on which to build and provide landscape grounds;
- (c) the formation of suitable new access, and in most cases extensive off-site highway improvement, works to the adjoining highway network under S278 Agreements such as construction of new right turn lane;
- (d) the provision of all services to the site (water, electricity, gas, drainage and telecoms) and/or the diversion and/or upgrading of existing services and construction of land drainage infrastructure within the site;
- (e) the construction of roadways, parking areas and pathways within the site; and
- (f) landscaping – the preparation of the site including importing significant quantities of topsoil and carrying out extensive landscaping works across the site.

The replacement cost will not include all the costs necessary to undertake the development of a new site, such as agent, engineer, architect and legal fees.'. Westerleigh told us that collectively these costs can 'commonly be around [redacted] or more per site' and are not included in either the benchmark land costs or the replacement cost of buildings for insurance purposes.⁵⁵

103. Westerleigh said that it has 'recently undertaken a review of its replacement costs by a qualified surveyor for its 2020 insurance renewal. The 2018 valuation, used by the CMA, significantly underestimated re-instatement costs.'⁵⁶
104. Westerleigh told us that [redacted] and that these should be included in its capital employed figure.⁵⁷

⁵⁵ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 22, paragraphs 87-89.

⁵⁶ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 21, paragraph 83

⁵⁷ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 23, paragraph 92

105. Westerleigh noted that its Aylesbury Vale site should be included in assets under construction⁵⁸ and submitted that capital expenditure on leasehold buildings at two of its sites should also be capitalised.⁵⁹
106. Regarding the valuation of assets, LCC told us that ‘applying “notional depreciation” is [...] fundamentally flawed’ and stated that FRS 102⁶⁰ crematoria operators are permitted to value or revalue their assets to ‘their income generating capabilities’.⁶¹

Our approach

107. In general buildings are depreciated over 50 years. However, we observed that a large proportion of crematoria are used for more than 50 years: 48 of the 117 crematoria we analysed were built prior to 1970 and are still in use. This represents 41% of the crematoria analysed in our profitability assessment.
108. Further, nine of those 117 crematoria were built prior to 1920 and thus are over 100 years old, and still in use. We considered whether this suggested that we should assume a longer useful economic life, eg 150 years. However, we noted Memoria’s submission that it would not wish to use its buildings for more than 50 years in order to maintain quality standards.
109. We recognise that any single UEL choice will be an approximation, with some buildings being used for longer, while others will become obsolete more rapidly. However, we thought that it was important to take a consistent approach across crematorium operators. Therefore, on the basis of the evidence we have as to how long crematoria are operated (in practice), we concluded that a 100-year UEL assumption was appropriate. To the extent that sites have a longer economic life, this means that “too much” depreciation is being charged against these assets each year. This effect will offset⁶² the effect on ROCE arising from capital values being understated, with an overall ambiguous effect on measured profitability.
110. Next, we considered parties’ submissions regarding the depreciation of capital improvements made to sites after their original construction. While we agreed that our approach would over-depreciate recent capital investments in sites

⁵⁸ Westerleigh explained that it had erroneously been excluded from this balance sheet line in the information originally provided to the CMA.

⁵⁹ Westerleigh response to PDR, paragraph 136

⁶⁰ FRS 102 is the principle accounting standard in the UK financial reporting regime.

⁶¹ LCC response to Crematoria working paper, page 16, paragraph 5.37

⁶² We note that this offset might be partial, full, or even may exceed the impact of the understatement of capital employed.

from the point when they were made, the fact that we have used the most recent insurance values for the whole period means that it will also effectively include such enhancements in capital employed (and a depreciation charge thereon) in earlier years when they had not been made. It is not clear to us whether Westerleigh has adjusted for this off-setting effect in its analysis. In any case, making adjustments for all such specific investments would add significant complexity to our analysis, introduces risks around cherry-picking⁶³ and, from Westerleigh's submission (see paragraph 100), the potential impact on ROCE can be expected to be de minimis. Therefore, we have not changed our approach in this way.

111. Regarding the insurance values we used as the replacement cost for crematoria buildings, we note the parties' views that these may not contain costs relating to the establishment of a site. However, we do not agree that the valuations undertaken for insurance purposes do not adequately cover all the costs highlighted by Westerleigh (see paragraph 102). The Royal Institute of Chartered Surveyors (RICS) produces guidance on how reinstatement costs should be estimated and states that:

"It is advisable for the net rebuilding cost of the whole property to include:

- (a) the cost of rebuilding the whole of the building in its present design and materials, to its existing shape and size, including basements, foundations and retaining walls... and*
- (b) all external works and services such as drainage, manholes, water supply, electricity supply, boundary structures and outbuildings (if required by the policy).*

...It is advisable for the reinstatement cost assessment to include... an allowance for demolition of any remaining sections of the building and associated site clearance prior to reinstatement... It is worth considering additional demolition costs, where applicable, due to factors such as site access difficulties, demolition of reinforced concrete and high-level working...

It is advisable to ensure that the reinstatement cost assessment (RCA) makes allowance for fees necessarily and reasonably incurred in the reinstatement or repair of a building. This should relate to the charges of architects, engineers, surveyors, and anyone else whose services are required if the work is to be done satisfactorily... Professional fees for dealing with reinstatement of

⁶³ For example, crematorium operators may have an incentive to tell us about enhancements to their sites but not about specific impairments.

*damage will often be higher than those for procuring new buildings, and it is advisable to make due allowance for this factor.”*⁶⁴

112. Therefore, while reinstatement costs may not include all elements of external works (in all cases), these figures will include costs that we would not expect an operator to include when building a new crematorium (eg site demolition costs and, potentially, higher professional fees). Separately, we note that the costs of dealing with contaminated land can be expected to be reflected in the price paid for the land, and therefore we do not consider that a further allowance should be made for such costs in our analysis. Therefore, we consider that our use of insurance reinstatement costs provides a reasonable approximation of the replacement cost of crematoria, without requiring further adjustment.
113. We disagree with Westerleigh’s assertion that 2020 insurance replacement costs should be used, as this valuation was carried out outside the relevant period, which ended in 2018. We cross-checked the average insurance value of a Westerleigh site, as of 2018, with that of Dignity for the same year and noted that these gave similar average replacement costs. Therefore, we do not find the evidence supports the view that Westerleigh’s 2018 insurance values are likely to particularly undervalue its sites.⁶⁵ Further, we note that we have been generous in taking the 2018 values and using throughout the Historic Period for the following reasons:
- (a) First, it is clear from Dignity and Westerleigh’s evidence that insurance replacement costs increased significantly over the Historic Period, meaning that using the latest date inflates the average capital value of assets earlier in the period; and
 - (b) the fact that these have increased suggests that a holding gain should be recognised in the P&L account. No such gain has been included in the P&L which means that profits and therefore ROCE are likely to be understated.
114. As noted at paragraph 85, we have not capitalised any assets held under leases, including those managed by parties on behalf of local authorities, and therefore do not propose any adjustments to points raised by parties on this matter.

⁶⁴ See [RICS Guidance on Reinstatement Cost Assessments](#).

⁶⁵ Moreover, as noted in other contexts, where assets have increased in value over time, these capital gains should be reflected in the earnings of the firms due to the need to fully articulate the accounts for economic profitability analysis. Such an approach would materially increase the measured profitability of the crematoria.

115. We note that parties' comments regarding adoption of FRS 102 to value assets. However, we consider that the assets included in the capital employed input to profitability analysis should reflect their current VTB. As noted at paragraph 12, The MEAV is the most common outcome of a VTB assessment. This approach is consistent with our Guidelines, which state that the CMA considers MEA values to be the economically meaningful measure for the purpose of measuring profitability in most cases.⁶⁶
116. We noted Westerleigh's submission regarding capital expenditure at leasehold sites and included the expenditure in our calculation of capital employed at the two sites submitted by Westerleigh. We have also included Aylesbury Vale at cost in Westerleigh's balance sheet in 2018.

Other fixed assets

117. For all other categories of fixed assets employed by crematoria (including cremators), we considered that the net book value was likely to be a good proxy for the depreciated replacement cost. These assets have relatively shorter asset lives than land and buildings such that historic cost will be closer to current replacement cost. In addition, parties are responsible for choosing a depreciation schedule that approximates the useful economic lives ('UELS') of these assets, such that the decline in NBV should broadly match the timeframe over which the asset wears out and needs replacing.
118. Therefore, we have not sought to revalue any other categories of tangible assets.

Intangible fixed assets

119. In this section we consider intangible fixed assets.

Our approach to recognition and valuation of intangible assets

120. The CMA guidelines set the criteria for consideration when determining whether to recognise an intangible asset for the purposes of profitability analysis or not. The guidelines state that we may consider the inclusion of intangible assets where the following criteria are met:
- (a) It must comprise a cost that has been incurred primarily to obtain earnings in the future.

⁶⁶ CC3 (Revised), Annex A, paragraph 14

(b) This cost must be additional to costs necessarily incurred at the time in running the business.

(c) It must be identifiable in creating an asset separate from any assets arising from the general running of the business.⁶⁷

121. The main category of intangible assets recorded on the balance sheets of the large crematoria is goodwill. However, we also consider whether it would be appropriate to recognise the other types of intangible assets that the parties have put to us above.

- *Goodwill*

122. Goodwill arises where a price is paid for a business which exceeds the fair value of tangible assets plus separately identifiable intangible assets. When firms acquire other firms and pay a price in excess of the net assets, they are incurring costs which are primarily to obtain earnings in the future. Furthermore, these costs are additional to those needed to run the business.

123. However, such purchased goodwill, by definition, is not an asset that is separable from the running of the business. It is profits generated from running the business - above those needed to cover costs, including asset costs. Goodwill should not therefore be included in the capital employed because it breaches the third recognition criterion, criterion (c) set out in paragraph 120.

124. Further, including goodwill is 'circular' when trying to assess whether profits have been above the level needed to cover costs, including asset costs. Ultimately, if all future profits were capitalised, it would be not be possible to identify supernormal profits under a ROCE versus WACC framework.⁶⁸

- *Other types of intangible assets*

125. Memoria and Westerleigh have both suggested that brand and reputation for providing a high-quality service are important intangible assets that should be recognised in their capital employed.

126. We consider that in order to develop a trade name, brand or reputation, firms may incur costs with the aim of generating earnings in the future and such

⁶⁷ CC3 (Revised) Annex A, paragraph 14

⁶⁸ Because profits would be capitalised into the capital employed based on future cashflows discounted at the WACC. So, capital employed = profits/WACC (the formula for discounting into perpetuity) and therefore ROCE = profit/capital employed = WACC.

costs may be additional to the costs incurred in the general running of the business.⁶⁹ On this basis, such expenditure meets two out of three of the CMA's criteria for recognition of intangible assets. However, the information that we have gathered to date does not support the view that crematoria do, in fact, incur material costs in seeking to develop a trade name, brand or reputation, particularly those which are additional to the costs incurred in the general running of the business. For example, we note that many crematoria seek to build relationships with local funeral directors and establish their reputations in the local area by providing high quality services. While such activities can be expected to develop the reputation of the crematorium and thereby generate earnings in the future, they are clearly also part of the general running of the business, seeking to attract customers in the short-term and delivering services to them.

127. Furthermore, with respect to the third criteria, ie that the asset created be separable from those assets arising from the general running of the business, the information that we have gathered to date does not seem to indicate there is a separate, intangible asset. The local brand and/or reputation of a crematorium does not appear to be separable from the rest of the business since it appears to be strongly associated with a particular site and could not easily be separated from that site.
128. Therefore, we do not consider it appropriate to include a separate brand/reputation asset in the capital employed by crematoria.

Working capital and cash

129. Working capital comprises inventory, trade debtors and other debtors and operating current liabilities such as trade creditors and other creditors. These assets are necessary for the provision of crematoria services and therefore we have included them in our calculation of capital employed.
130. As noted in paragraph 10, financing costs and balances are excluded from the calculation of EBIT and capital employed. We have therefore excluded cash balances from the calculation as this represents a means of funding the capital employed of the business rather than being an operational balance.
131. For the large crematoria, we have used the relevant current assets and liabilities information on their balance sheets. However, some of the local authority crematoria were unable to provide us with a detailed balance sheet

⁶⁹ For example, there are certain costs which give rise to brand values that may not be addition to those incurred from the running of the business. For example, consistently providing a good quality service, via well-trained and well-paid staff may give rise to a higher brand value.

breakdown and therefore we estimated their working capital on the following basis.

132. In the first instance, we sought to use data from those parties in our analysis who had provided full working capital information to estimate average debtor, creditor and inventory days and apply these estimates to the P&L information of the other parties in order to model working capital balances for the latter. However, we observed that the recording of cost of goods sold ('COGS') is inconsistent across the industry, with some parties not recording any COGS, ie all their costs are recorded as overheads, and others having significant COGS balances. This meant that our estimates of creditor and inventory days were also inconsistent and that these figures could not, in any case, be applied to those local authorities that did not record COGS separately. Therefore, we adopted an alternative approach of estimating debtors, creditors and inventories as a proportion of total revenues and applying these percentages to the revenues of the crematoria that had not been able to identify separate working capital balances to model these. Our analysis indicated that trade debtors were on average 7.5% of revenues, inventories 1.5% of revenues and trade creditors were 5.0% of revenues.⁷⁰

Adjustments to EBIT

133. In addition to considering capital employed, we considered the need to make adjustments to EBIT.
134. EBIT is the earnings made by the party before interest and tax. Naturally, therefore, interest and tax revenues and costs are excluded. We made some additional adjustments to EBIT to ensure we used a figure which was meaningful for profitability purposes. This section details the adjustments we made.

Income

135. As noted at paragraph 38, in both our Case One and Case Two we have included all revenues earned from crematorium operators' sites (cremation fees, memorials and burial revenues) in earnings. We have therefore also included the corresponding costs.

⁷⁰ These figures represent the averages over the Relevant Period. While there were year-on-year fluctuations in our estimates, we considered that these were likely to represent 'noise' in the data rather than differing working capital requirements over time (as we do not believe there has been any change in the basic business model of crematoria over this period) and therefore chose to use the period average.

136. Where revenues and/or costs associated with burials were previously separated out or not included, we have added these back to the EBIT of the relevant party.
137. We note that LCC does not carry out burials and so in its case, revenue and costs represent cremations and memorials only.

Depreciation of buildings

138. Having revalued buildings using insurance replacement cost, we also took into account the corresponding impact on EBIT: as the value of their parties' buildings increased, the depreciation charge thereon also increased.
139. We calculated the depreciation charge corresponding to the revalued buildings. We then removed the parties' own depreciation charge and replaced this with the recalculated value.
140. Westerleigh told us that it is inappropriate to depreciate buildings for the full year in the year of opening as 'property should be depreciated when available for use'.⁷¹
141. We noted Westerleigh's point and considered its materiality and the need to be consistent across operators. We considered the impact of Westerleigh's proposed change and noted that it had an impact of between 0.03% and 0.05% per year in each year of the Historic Period.
142. However, we do not have sufficient data to perform this adjustment for all of the remaining large crematoria. Given the relative immateriality of this change we do not consider it to be appropriate or necessary to roll out to the other providers.

Other

143. Regarding non-underlying cost items Dignity told us that 'it would be appropriate to include a portion of these costs, as even a new entrant will – from time to time in the normal course of business – need to incur restructuring and regulatory costs'.
144. Westerleigh told us that it '[redacted]'.⁷²

⁷¹ Westerleigh response to PDR, page 46, paragraph 136

⁷² Westerleigh response to Crematoria profitability working paper, dated 17 June, page 31, paragraph 109

145. Westerleigh argued that 'given these costs have been incurred and the uncertainty around planning and development that means these projects may not go ahead, Westerleigh believes that these costs should be recognised as incurred and historic earnings adjusted accordingly'.⁷³
146. However, since we have capitalised the costs of obtaining planning permission in land values, allowing for these expenses in the P&L would be double counting. Therefore, we do not agree with Westerleigh and have not recognised these costs in their P&L.
147. Our approach to the calculation of planning permission costs is detailed at paragraph 41. We have not included any other non-underlying costs.
148. To ensure that the EBIT figure used in our ROCE calculation was meaningful we removed any income or costs not associated with running a crematorium. As such we asked parties to provide a breakdown of Overhead costs; identified such costs and added these back to EBIT. Examples of these costs include distributions to reserves and costs of financing.
149. This process involved correspondence with local authority crematoria to ensure an accurate breakdown of overhead costs was obtained and that the EBIT figure obtained was reliable. We also engaged in communication with the local authorities to ensure that costs recorded related to crematoria and not other local authority costs.
150. Memoria queried why loan guarantee costs have been treated as non-cost item.
151. In line with the CMA's standard practice, we have determined the ROCE of each party using operating profits excluding financing costs e.g. interest and sources of finance, regardless of whether they are short or long-term. Loan guarantee costs constitute a cost of finance and therefore have been excluded from EBIT for the purposes of our ROCE calculation. More information can be found at Appendix Q – Profitability methodology.

Large crematoria results

152. In this section we present the results of our analysis of the profitability of the four largest private crematorium operators.

⁷³ Westerleigh response to Crematoria profitability working paper, dated 17 June, page 31, paragraph 110

153. The ROCE figures have been calculated using capital employed and EBIT derived as per our explanations above. We also consider average total revenue, cost-plus and economic profits per cremation.
154. Economic profits are the profits left over, after the providers of capital have been paid a market-based return on their investment, which is equal to the capital employed multiplied by the WACC. It is calculated as EBIT less WACC x Capital Employed. For the purposes of our profitability analysis, we have calculated WACC at 8%. Further details concerning our WACC calculation can be found in Appendix R.
155. Cost plus is the calculation of all costs plus the cost of capital (ie the capital employed multiplied by WACC). This demonstrates the total cost of the provision of crematoria services, including an allowance for a reasonable return on capital (debt plus equity).
156. Economic profits as a percentage of cost plus ('EP/CP') demonstrates how much above or below the price at which the firm would have made a 'normal' return, prices have been.
157. Average revenue per cremation has been calculated as total revenues divided by volume of cremations. For Dignity, Westerleigh and Memoria this total figure includes burials income, as well as income from cremations and memorials, in both Case One and Case Two. As a result, the average revenue per cremation figure for these three operators will be inflated when compared with LCC and the local authority crematoria. We do not draw inferences from these figures when interpreting the results of our analysis.

Firm A

158. Firm A's results using Case One are detailed below.

Table 1: Firm A's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£]
Cost plus/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£]
Economic profits/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£] [300-350]
EP/CP	[£]	[£]	[£]	[£]	[£]	[£]
Adjusted ROCE (%)	[£]	[£]	[£]	[£]	[£]	[£] [20-30%]
Volume of cremations	[£]	[£]	[£]	[£]	[£]	[£]
Volume of cremations/crematorium	[£]	[£]	[£]	[£]	[£]	[£]

Source: CMA analysis

Notes:

When performing the land revaluation, [£] out of [£] of Firm A's owned sites used the actual price paid for land. The remaining [£] were recalculated using the method at paragraph 38.

In a small number of cases, where Firm A [£], we capitalised the land and removed the rent costs from the P&L.

[§] % of Firm A's estate was built in the last 10 years⁷⁴ and [§] of its crematoria were fully depreciated for the entirety of the Historic Period.

159. Under Case One, Firm A earned returns significantly and persistently above our estimate of its cost of capital, with a ROCE of [20-30]%, compared with our estimate of WACC of 8%.
160. We note that [§] is such that our use of average land purchase costs is likely to produce reasonably accurate total land valuations, and therefore profitability metrics, at the company level.

Table 2: Firm A's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[§]	[§]	[§]	[§]	[§]	[§]
Cost plus/cremation (£)	[§]	[§]	[§]	[§]	[§]	[§]
Economic profits/cremation (£)	[§]	[§]	[§]	[§]	[§]	[§] [250-300]
EP/CP	[§]	[§]	[§]	[§]	[§]	[§]
Adjusted ROCE (%)	[§]	[§]	[§]	[§]	[§]	[§] [10-20%]
Volume of cremations	[§]	[§]	[§]	[§]	[§]	[§]
Volume of cremations/crematorium	[§]	[§]	[§]	[§]	[§]	[§]

Source: CMA analysis

161. Under Case Two, Firm A's average ROCE decreases by [§] percentage points to [10-20%] (compared with a WACC of 8%) and average economic profits declined to £[250-300] per cremation. We note that under Case Two Firm A is still earning returns which are materially above its weighted average cost of capital.

Firm B

162. Firm B's results using Case One are detailed below.

Table 3: Firm B's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[§]	[§]	[§]	[§]	[§]	[§]
Cost plus/cremation (£)	[§]	[§]	[§]	[§]	[§]	[§]
Economic profits/cremation (£)	[§]	[§]	[§]	[§]	[§]	[§] [100-150]
EP/CP	[§]	[§]	[§]	[§]	[§]	[§]
Adjusted ROCE (%)	[§]	[§]	[§]	[§]	[§]	[§] [10-20%]
Volume of cremations	[§]	[§]	[§]	[§]	[§]	[§]
Volume of cremations/crematorium	[§]	[§]	[§]	[§]	[§]	[§]

Source: CMA analysis

Notes:

[§]. When performing the land revaluation, [§] out of [§] of Firm B's owned sites used the actual price paid for land. The remaining [§] of Firm B's owned sites were recalculated using the method at paragraph 38.

[§] % of Firm B's estate has been built in the last 10 years. [§].

⁷⁴ [Funerals Market Investigation Crematoria: Outcomes](#), paragraph 67

163. Our ROCE estimates for Firm B show that it earned returns above our estimate of its cost of capital across the Historic Period, with average economic profits per cremation of £[100-150].
164. Further, we note that Firm B has expanded significantly over the period, opening [X] sites between 2013 and 2018, and, as a result, we expect their profitability to be depressed by the fact that they had a large number of sites building up their volumes. As a result, we consider that Firm B's financial performance is unlikely to reflect the profits that the business might expect to earn once its crematoria reached maturity.

Table 4: Firm B's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [100-150]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [10-20%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]
Volume of cremations/crematorium	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

165. Our ROCE estimates for Firm B decrease by [X] percentage points under Case Two. Average economic profits decreased to £[100-150], under Case Two. We note that under Case Two Firm B is still earning returns which are above its weighted average cost of capital.

Firm C

166. [X] Case One [X].

Table 5: Firm C's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [(100)-(150)]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [0-10%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]
Volume of cremations/crematorium	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

167. Over the 2014 to 2018 period, Firm C earned returns below or equal to our estimate of its weighted average cost of capital. There is a clear upward trend in profitability, with ROCE increasing from [0-10%] in 2014 to [0-10%] in 2018, which appears to be driven by growth in cremation volumes as Firm C's sites [X]. In this context, we observe that Firm C's results are unlikely to reflect the

profits that the business might expect to earn once its crematoria reached maturity.

168. When performing the land revaluation, [X] of Firm C's owned sites used the actual price paid for land. [X].⁷⁵

169. [X].

Firm D

Table 6: Firm D's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [(100)-(150)]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [0-10%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]
Volume of cremations/crematorium	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

Table 7: Firm D's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [(200)-(250)]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [0-10%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]
Volume of cremations/crematorium	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

170. Under both Case One and Case Two, Firm D makes returns significantly below our estimate of its weighted average cost of capital. We note Firm D [X] than Firm A and Firm B. Further, we note that Firm D opened a new facility in [X], which may have reduced its profitability as this new site builds volumes.

171. When performing the land revaluation, [X] of Firm D's sites used the actual price paid for land and therefore [X] were recalculated using the method at paragraph 38.

⁷⁵ Firm C has royalty arrangements with the seller of land for these sites, whereby it pays a portion of cremation fees to the seller each year. The CMA has calculated the present value of these arrangements and included it within the value of land.

172. [X] built in the last 10 years and [X] were fully depreciated for the Historic Period.

Local authority crematoria results

ROCE analysis results

173. As noted in the introduction to this paper we selected a random sample of twenty-two local authority crematoria to carry out financial analysis on, being:

- (a) Wellingborough Council (Nene Valley);
- (b) Sheffield City Council (City Road Crematorium);
- (c) Bracknell Forest Council (Easthampstead Park Cemetery and Crematorium);
- (d) Dudley Council (Gornal Wood Crematorium);
- (e) Slough City Council (Slough Crematorium);
- (f) Hartlepool Borough Council (Stranton Crematorium);
- (g) Wakefield Council (Pontefract Crematorium);
- (h) Liverpool Council (Anfield Crematorium);
- (i) Carlisle City Council (Carlisle Crematorium);
- (j) Coventry City Council (Canley Garden Crematorium);
- (k) Luton Borough Council (Value Crematorium);
- (l) Perth & Kinross Council (Perth Crematorium);
- (m) North East Surrey Council (North East Surrey Crematorium);
- (n) Sunderland City Council (Sunderland Crematorium);
- (o) Gwynedd Council (Bangor Crematorium);
- (p) Chesterfield Council (Chesterfield and District Crematorium);
- (q) Yeovil Council (Yeovil Crematorium);
- (r) Cheshire East Council (Crewe Crematorium);
- (s) City of Edinburgh Council (Mortonhall Crematorium);

- (t) Lambeth (Lambeth Crematorium);
- (u) Plymouth Council (Efford Crematorium); and
- (v) Gwent Council (Gwent Crematorium).

174. We have presented the results of these local authority crematoria below. The parties have not been identified for confidentiality reasons and have been labelled as LA1 to LA 22.⁷⁶ We considered the financial information provided by LA11 and LA17 to be unreliable. As a result, while we have shown the results for these local authorities below, we have excluded them from our further analysis of the results, including our weighted average profit metrics and our detriment estimate.

175. We note that the use of average land purchase price per acre may not reflect the actual costs that a crematorium operator might face in a particular geographic location as land values vary materially across the UK. As a result, our approach to land valuation is likely to give more robust operator-level results for the larger crematorium operators which have a large number and geographic spread of sites than for individual local authority crematoria. Therefore, we consider the results of our analysis to be indicative for individual local authority crematoria and we consider averages for this group as a whole in assessing these results at paragraph 232.

LA 1

Table 8: LA 1 revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
<i>Revenue/cremation (£)</i>	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
<i>Cost plus/cremation (£)</i>	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
<i>Economic profits/cremation (£)</i>	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [150-200]
<i>EP/CP</i>	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
<i>Adjusted ROCE (%)</i>	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [10-20%]
<i>Volume of cremations</i>	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Source: CMA analysis

176. Under Case One, LA 1 earned returns of [10-20%] on average over the period and economic profits of £[150-200] per cremation.

⁷⁶ The order in which results are presented in the paragraphs below is not of the same as in paragraph 173.

Table 9: LA 1 revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Cost plus/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Economic profits/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [100-150]
EP/CP	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Adjusted ROCE (%)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [10-20%]
Volume of cremations	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Source: CMA analysis

177. Under Case Two, LA 1's ROCE decreased to [10-20%] on average over the period and economic profits decreased to £[100-150] per cremation over the period.

LA 2

Table 10: LA 2's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Cost plus/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Economic profits/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [150-200]
EP/CP	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Adjusted ROCE (%)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [10-20%]
Volume of cremations	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Source: CMA analysis

178. In Case One, LA 2 earned returns of [10-20%] on average over the period and economic profits of £[150-200] per cremation.

Table 11: LA 2's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Cost plus/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Economic profits/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [50-100]
EP/CP	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Adjusted ROCE (%)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [10-20%]
Volume of cremations	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Source: CMA analysis

179. In Case Two, LA 2's ROCE reduced to [10-20%] on average over the period, and its economic profit to £[50-100] per cremation.

LA 3

Table 12: LA 3's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Cost plus/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Economic profits/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [200-250]
EP/CP	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Adjusted ROCE (%)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [20-30%]
Volume of cremations	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Source: CMA analysis

180. Under Case One LA 3 earned a ROCE of [20-30%] and economic profits per cremation of £[200-250].

Table 13: LA 3's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [100-150]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [10-20%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

181. Under Case Two, LA 3's ROCE declines to [10-20%] and its economic profits per cremation to £[100-150].

LA 4

Table 14: LA 4's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [0-(50)]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [0-10%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

182. In Case One, LA 4 earned a ROCE of [0-10%] and economic losses per cremation of £[0-(50)].

Table 15: LA 4's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [(200)-(250)]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [0-10%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

183. In Case Two, LA 4's ROCE declined to [0-10%] and its economic losses per cremation increased to £[(200)-(250)].

184. The low returns for LA 4 appear to be driven primarily by a relatively low average revenue per cremation.

LA 5

Table 16: LA 5's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [350-400]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [20-30%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

185. Under Case One, LA 5 earned a ROCE of [20-30%] and economic profits per cremation of £[350-400].

Table 17: LA 5's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [250-300]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [10-20%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

186. Under Case Two LA 5's ROCE declines to [10-20%] and its economic profits per cremation to £[250-300].

LA 6

Table 18: LA 6's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [300-350]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [20-30%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

Notes: For LA 6 the CMA valued the insurance replacement cost of its building as an average figure across local authority crematoria, as the figure provided did not appear credible as a full reinstatement cost (it appeared too low).

187. Under Case One, LA 6 earned a ROCE of [20-30%] and economic profits per cremation of £[300-350].

Table 19: LA 6's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [250-300]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [20-30%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

188. Under Case Two, LA 6's ROCE declines to [20-30%] and its economic profits per cremation to £[250-300].

LA 7

Table 20: LA 7's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£]
Cost plus/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£]
Economic profits/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£] [50-100]
EP/CP	[£]	[£]	[£]	[£]	[£]	[£]
Adjusted ROCE (%)	[£]	[£]	[£]	[£]	[£]	[£] [10-20%]
Volume of cremations	[£]	[£]	[£]	[£]	[£]	[£]

Source: CMA analysis

189. LA 7's buildings are fully depreciated throughout the Historic Period as they were constructed in [£].

190. In Case One, LA 7 earned a ROCE of [10-20%], such that it made economic profits (of around £[50-100] per cremation) over the 2014 to 2018 period.

Table 21: LA 7's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£]
Cost plus/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£]
Economic profits/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£] [(150)-(200)]
EP/CP	[£]	[£]	[£]	[£]	[£]	[£]
Adjusted ROCE (%)	[£]	[£]	[£]	[£]	[£]	[£] [0-10%]
Volume of cremations	[£]	[£]	[£]	[£]	[£]	[£]

Source: CMA analysis

191. In Case Two, LA 7's ROCE declines to [0-10%], such that it made economic losses (of around £[(150)-(200)] per cremation) over the 2014 to 2018 period.

192. LA7's relatively low(er) returns appear to be driven primarily by a high cost plus per cremation, which may be the result of the relatively low volumes of cremations undertaken.

LA 8

Table 22: LA 8's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£]
Cost plus/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£]
Economic profits/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£] [200-250]
EP/CP	[£]	[£]	[£]	[£]	[£]	[£]
Adjusted ROCE (%)	[£]	[£]	[£]	[£]	[£]	[£] [10-20%]
Volume of cremations	[£]	[£]	[£]	[£]	[£]	[£]

Source: CMA analysis

193. Under Case One, LA 8 earned a ROCE of [10-20%] and economic profits per cremation of £[200-250].

Table 23: LA 8's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [50-100]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [10-20%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

194. Under Case Two, LA 8 ROCE declines to [10-20%] and its economic profits per cremation to £[50-100].

LA 9

Table 24: LA 9's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [350-400]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [20-30%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

195. LA 9's buildings were fully depreciated throughout the Historic Period. They were constructed in [X].

196. Under Case One, LA 9 earned a ROCE of [20-30%] and economic profits per cremation of £[350-400].

Table 25: LA 9's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [150-200]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [10-20%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

197. Under Case Two, LA 9's ROCE decreases to [10-20%] and its economic profits per cremation to £[150-200].

LA 10

Table 26: LA 10's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [100-150]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [10-20%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

Notes: LA 10 was unable to provide us with information on the volume of cremations undertaken at its site. Therefore, the volume of cremations was obtained from publicly available information from The Cremation Society.⁷⁷

198. Under Case One, LA 10 earned a ROCE of [10-20%] and its average economic profits per cremation of around £[100-150].

Table 27: LA 10's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£]
Cost plus/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£]
Economic profits/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£] [0-50]
EP/CP	[£]	[£]	[£]	[£]	[£]	[£]
Adjusted ROCE (%)	[£]	[£]	[£]	[£]	[£]	[£] [0-10%]
Volume of cremations	[£]	[£]	[£]	[£]	[£]	[£]

Source: CMA analysis

199. Under Case Two, LA 10's ROCE declines to [0-10%] and average economic profits per cremation decline to around £[0-50].

LA 11

Table 28: LA 11's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£]
Cost plus/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£]
Economic profits/cremation (£)	[£]	[£]	[£]	[£]	[£]	[£] [450-500]
EP/CP	[£]	[£]	[£]	[£]	[£]	[£]
Adjusted ROCE (%)	[£]	[£]	[£]	[£]	[£]	[£] [50-60%]
Volume of cremations	[£]	[£]	[£]	[£]	[£]	[£]

Source: CMA analysis

200. Under Case One, LA 11 earned a ROCE of [50-60%] and economic profits of £[450-500] per cremation. However, we note that LA 11 has a particularly low cost plus per cremation. This may be the result of undertaking a very high volume of cremations, spreading relatively fixed costs over a larger number of cremations. However, we cannot exclude the possibility that the total costs provided by LA 11 are understated. Therefore, as we cannot be confident of the reliability of these results, we have excluded LA 11's results when aggregating results across local authorities. We note that this approach is conservative and may result in the understatement of profits at the industry level.

⁷⁷ The Cremation Society is a registered charity which collects data from both private and public crematoria on a voluntary basis.

Table 29: LA 11's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [400-450]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [40-50%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

201. Under Case Two, LA 11's ROCE declines to [40-50%] and its economic profits to £[400-450] per cremation.

LA 12

Table 30: LA 12's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [350-400]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [30-40%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

202. Under Case One, LA 12 earned a ROCE of [30-40%] and economic profits per cremation of £[350-400].

Table 31: LA 12's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [300-350]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [20-30%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

203. Under Case Two, LA 12's ROCE declines to [20-30%] and economic profits per cremation to £[300-350].

LA 13

Table 32: LA 13's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [(600)-(650)]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [0-10%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

204. LA 13 [X].

205. Under Case One, LA 13 earned a ROCE of between [x] and [x] across the Historic Period. It made economic losses across the 2016 to 2018 period, although these have declined rapidly as its volumes have increased.
206. LA 13 [x] was able to provide us with recent evidence on the MEAV of its land and buildings. In carrying out our analysis, therefore, we have not needed to revalue its land. As a result, we only have Case One results for LA 13, calculated using its own land values.

LA 14

Table 33: LA 14's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[x]	[x]	[x]	[x]	[x]	[x]
Cost plus/cremation (£)	[x]	[x]	[x]	[x]	[x]	[x]
Economic profits/cremation (£)	[x]	[x]	[x]	[x]	[x]	[x] [50-100]
EP/CP	[x]	[x]	[x]	[x]	[x]	[x]
Adjusted ROCE (%)	[x]	[x]	[x]	[x]	[x]	[x] [10-20%]
Volume of cremations	[x]	[x]	[x]	[x]	[x]	[x]

Source: CMA analysis

207. In Case One, LA 14 earned a ROCE of [10-20%], ie above our estimate of its weighted average cost of capital, and economic profits per cremation of £[50-100].

Table 34: LA 14's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[x]	[x]	[x]	[x]	[x]	[x]
Cost plus/cremation (£)	[x]	[x]	[x]	[x]	[x]	[x]
Economic profits/cremation (£)	[x]	[x]	[x]	[x]	[x]	[x] [0-(50)]
EP/CP	[x]	[x]	[x]	[x]	[x]	[x]
Adjusted ROCE (%)	[x]	[x]	[x]	[x]	[x]	[x] [0-10%]
Volume of cremations	[x]	[x]	[x]	[x]	[x]	[x]

Source: CMA analysis

208. In Case Two, LA 14's ROCE declines to [0-10%], ie just below our estimate of its weighted average cost of capital, and it makes a small economic loss on average over the period.

LA 15

Table 35: LA 15's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[x]	[x]	[x]	[x]	[x]	[x]
Cost plus/cremation (£)	[x]	[x]	[x]	[x]	[x]	[x]
Economic profits/cremation (£)	[x]	[x]	[x]	[x]	[x]	[x] [0-(50)]
EP/CP	[x]	[x]	[x]	[x]	[x]	[x]
Adjusted ROCE (%)	[x]	[x]	[x]	[x]	[x]	[x] [0-10%]
Volume of cremations	[x]	[x]	[x]	[x]	[x]	[x]

Source: CMA analysis

Notes:

LA 15 was unable to provide the CMA with the insurance replacement cost of its building and therefore the CMA valued the insurance replacement cost of its building as an average figure across local authority crematoria.

209. In Case One, LA 15's average ROCE was [0-10%] and it made economic losses of £[0-(50)] per cremation.
210. As noted at paragraph 148 when performing our analysis we added back any distributions to reserves to EBIT to ensure the figure used in ROCE was meaningful. LA 15 was unable to provide us with a breakdown of its overhead costs in order for us to perform this activity. However, the information provided by LA 15 suggests that its overhead costs include such distributions. As such it is very likely LA 15's profitability is understated due to the inclusion of distributions in overheads costs.

Table 36: LA 15's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [(50)-(100)]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [0-10%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

211. In Case Two, LA 15's average ROCE decreased to [0-10%] and its economic losses increased to £[(50)-(100)].

LA 16

Table 37: LA 16's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [0-50]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [0-10%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

Notes:

LA 16 was unable to provide the CMA with the insurance replacement cost of its building and therefore the CMA valued the insurance replacement cost of its building as an average figure across local authority crematoria.

212. In Case One, LA 16 earned an average ROCE of [0-10%], and average economic profits per cremation of £[0-50].

Table 38: LA 16’s revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Cost plus/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Economic profits/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [0-(50)]
EP/CP	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Adjusted ROCE (%)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [0-10%]
Volume of cremations	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Source: CMA analysis

213. In Case Two, LA 16’s average ROCE declines to [0-10%], and it makes a small economic loss on average over the period.

LA 17

Table 39: LA 17’s revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Cost plus/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Economic profits/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [(150)-(200)]
EP/CP	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Adjusted ROCE (%)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [0-10%]
Volume of cremations	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Source: CMA analysis

214. In Case One, LA 17’s average ROCE was [0-10%], which is significantly below our estimate of its cost of capital.

215. We present the results of LA 17 above. However, we have a number of concerns about the reliability of the data provided to us.⁷⁸ For example, average revenue per cremation varies significantly from one year to the next and is very significantly below the price listed on LA 17’s website. As we cannot be confident of the reliability of these results, LA 17’s results have been excluded when aggregating results across local authorities.

Table 40: LA 17’s revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Cost plus/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Economic profits/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [(300)-(350)]
EP/CP	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Adjusted ROCE (%)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [0-10%]
Volume of cremations	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Source: CMA analysis

216. In Case Two, LA 17’s average ROCE decreased to [0-10%].

⁷⁸ In normal circumstances, we would have requested for information and/or clarifications in relation to such data. However, the COVID-19 pandemic has made further data collection problematic.

LA 18

Table 41: LA 18's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [200-250]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [20-30%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

217. In Case One, LA 18 earned an average ROCE of [20-30%], significantly above our estimate of its weighted average cost of capital, with average economic profits per cremation of £[200-250].

Table 42: LA 18's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [100-150]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [10-20%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

218. In Case Two, LA 18's ROCE decreased to [10-20%]; still significantly above our estimate of its weighted average cost of capital. Economic profits per cremation declined to £[100-150] on average across the period.

LA 19

Table 43: LA 19's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [50-100]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [10-20%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

219. In Case One, LA 19 earned an average ROCE of [10-20%] and economic profits of £[50-100] per cremation on average.

Table 44: LA 19's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [50-100]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [10-20%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

220. In Case Two, LA 19's ROCE declines to [10-20%] and its average economic profits per cremation to £[50-100].

LA 20

Table 45: LA 20's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [100-150]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [10-20%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

221. In Case One, LA 20 earned an average ROCE of [10-20%], and average economic profits per cremation of £[100-150].

222. In 2017 LA 20 was affected by [X] and this is the only year in which it made a loss.

Table 46: LA 20's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [0-50]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [0-10%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

223. In Case Two, LA 20's ROCE reduced to [0-10%] and its economic profits per cremation to £[0-50].

LA 21

Table 47: LA 21's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Cost plus/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X]
Economic profits/cremation (£)	[X]	[X]	[X]	[X]	[X]	[X] [350-400]
EP/CP	[X]	[X]	[X]	[X]	[X]	[X]
Adjusted ROCE (%)	[X]	[X]	[X]	[X]	[X]	[X] [20-30%]
Volume of cremations	[X]	[X]	[X]	[X]	[X]	[X]

Source: CMA analysis

224. In Case One, LA 21's ROCE was [20-30%] and its average economic profits per cremation were £[350-400].

Table 48: LA 21's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Cost plus/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Economic profits/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [150-200]
EP/CP	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Adjusted ROCE (%)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [10-20%]
Volume of cremations	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Source: CMA analysis

225. In Case Two, LA 21's ROCE declines to [10-20%] and its average economic profits per cremation to £[150-200].

LA 22

Table 49: LA 22's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case One

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Cost plus/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Economic profits/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [0-50]
EP/CP	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Adjusted ROCE (%)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [0-10%]
Volume of cremations	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Source: CMA analysis

226. LA 22 [REDACTED]. Average results presented are of 2014-15 and 2017-18.

227. In Case One, LA 22 earned an average ROCE of [0-10%] and economic profits per cremation of £[0-50].

Table 50: LA 22's revenue, cost plus and economic profits per cremation, ROCE % and volume of cremations over the Historic Period: Case Two

	2014	2015	2016	2017	2018	Average
Revenue/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Cost plus/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Economic profits/cremation (£)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [(50)-(100)]
EP/CP	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Adjusted ROCE (%)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED] [0-10%]
Volume of cremations	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Source: CMA analysis

228. In Case Two, LA 22's ROCE declines to [0-10%] and its economic profits per cremation to a loss of £[(50)-(100)].

Discussion of the results of our analysis

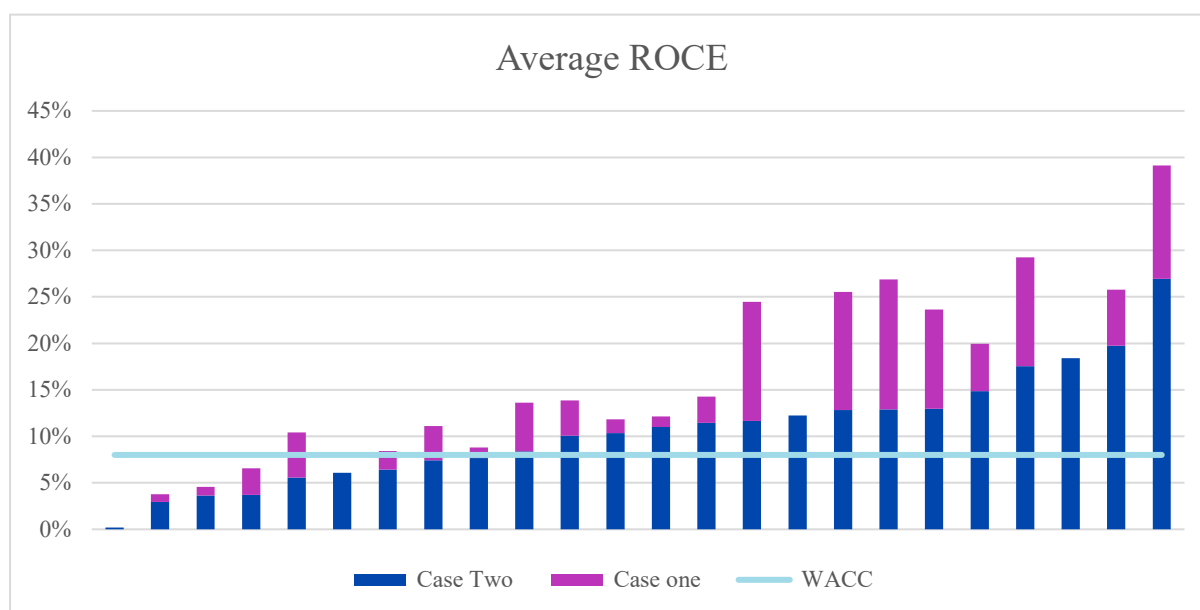
229. Our analysis shows that both Firm A and Firm B, as well as the majority of the local authority crematoria analysed, have persistently earned returns that are in excess of our estimate of the weighted average cost of capital under both our Case One and Case Two, in some cases significantly so. We note that both Firm B and Firm C's returns are likely to have been reduced over the

2014 to 2018 period as a result of being in a growth phase and that they may be expected to earn higher returns in the future than in the past.

230. The following two figures show:

- (a) the average ROCE per firm for the four largest and 20 local authority crematoria analysed (ie excluding LA 11 and LA 17 as noted above); and
- (b) the (weighted) average returns earned by 20 local authority crematoria over the 2014 to 2018 period.

Figure 2: Average ROCE per firm across 2014 to 2018 (%): Case One and Case Two



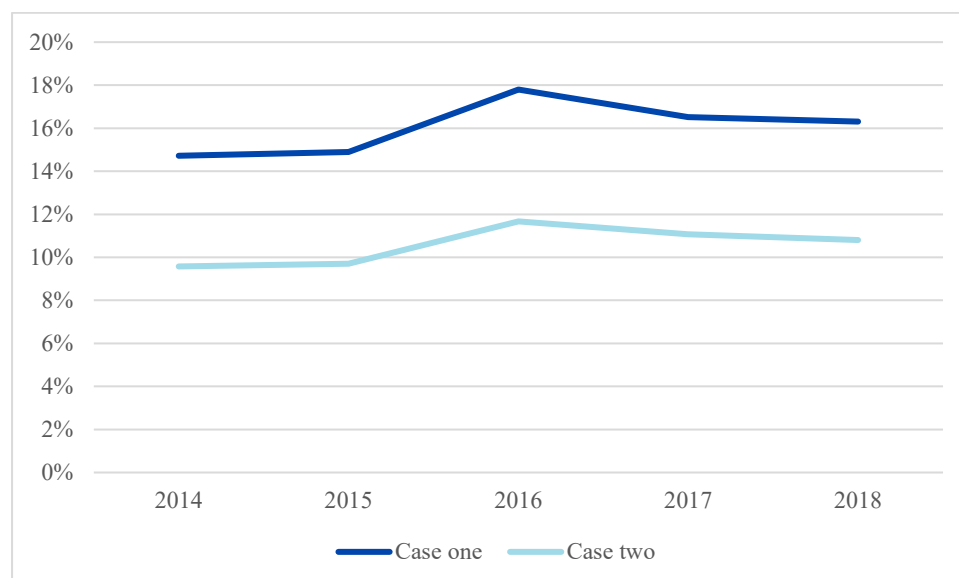
Source: CMA Analysis

Notes:

- a) The chart above is a composite bar chart.
- b) The parties have not been identified for confidentiality reasons.
- c) The chart is structured with bars representing the lowest average ROCE per party earned on the left, and the highest on the right under Case One and Case Two
- d) Case One is shown in purple and Case Two is shown in dark blue
- e) The lowest bar in Case One is just above 0%, and the highest is at approximately 39%.
- f) The lowest bar in Case Two is just above 0% and the highest is at approximately 27%

231. Figure 2 shows the average ROCE earned over the 2014 to 2018 period by party under both Case One and Case Two. While there is significant variability in the returns earned by the crematorium operators, nineteen of twenty-four parties are earning returns above the estimated 8% weighted average cost of capital under Case One, while only five are earning returns that are below the weighted average cost of capital. Under Case Two, fifteen of twenty-four parties are earning returns above the estimated 8% weighted average cost of capital, while nine are earning returns that are in line with or below the weighted average cost of capital.

Figure 3: ROCE of the local authority crematoria, 2014 to 2018 (%)



Source: CMA Analysis

Notes:

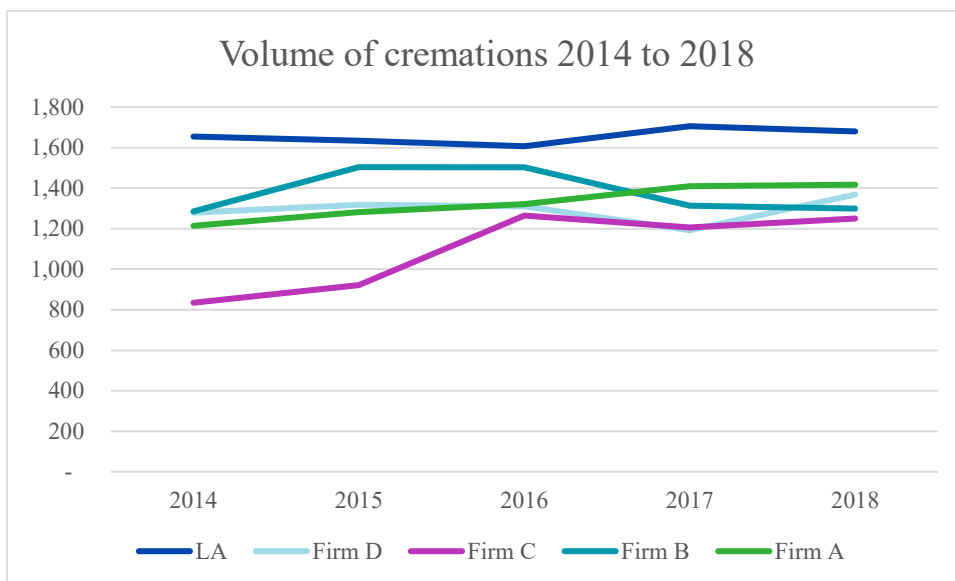
- The chart above is a line chart spanning from 2014 to 2018 inclusive. The line represents the weighted average ROCE of the local authority crematoria under Case One and Case Two
- Case One is shown in dark blue and Case Two is shown in light blue
- The chart demonstrates that the weighted average ROCE of the local authority crematoria increased to a high in 2016, then decreased slightly.
- The line shows that total ROCE under Case One starts at 15% in 2014, increasing to over 16% in 2018. There is a high of nearly 18% in 2016.
- Under Case Two, total ROCE starts at just under 10% and ends at just under 11%. There is a high of 12% in 2016.

232. Figure 3 shows the (weighted) average ROCE earned by local authority crematoria over 2014 to 2018 under Case One and Case Two.⁷⁹ It demonstrates that these crematoria, as a group, are earning returns significantly in excess of their WACC under both cases.

233. Figure 3 shows that the profitability of local authority crematoria has increased by between 1 and 2 percentage points, on average, over the relevant period. In addition, we observe that local authority crematoria are more profitable, on average, than the large private crematoria. These higher average returns appear to be due to a combination of higher average volumes per crematorium and owning older assets, which are therefore more depreciated, partially offset by earning lower average revenues per cremation.

⁷⁹ Calculated as the total EBIT earned by local authority crematoria divided by the total capital employed of local authority crematoria, for each year in the period.

Figure 4: Volume of cremations from 2014 to 2018



Source: CMA Analysis

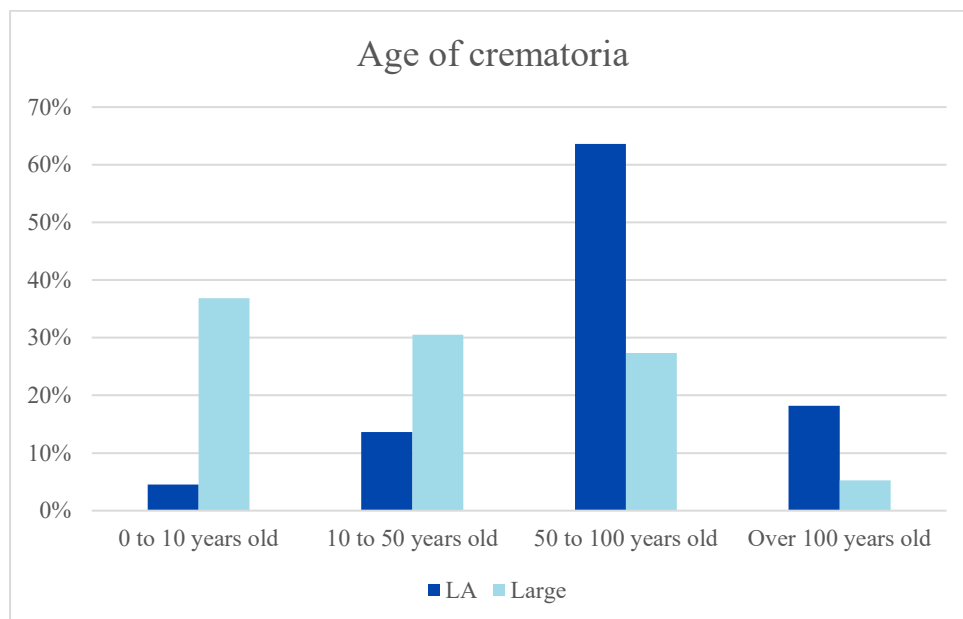
Notes:

- a) The chart above is a line chart spanning from 2014 to 2018 inclusive. The lines represent the volume of cremations performed by private crematoria and the average volume performed by local authority crematoria.
- b) The chart demonstrates that the average volume of cremations performed by local authority crematoria is higher than the volume performed by any of the large crematorium operators in each year from 2014 to 2018.

234. Figure 4 shows the average volume of cremations performed by the local authorities in our sample and the average volume of cremations performed at each crematorium by large crematoria in each year from 2014 to 2018.

235. This shows that each year in the Historic Period, the average volume of cremations performed at local authority crematoria was higher than at any of the large crematoria. We note that at least part of this difference is due to the private operators opening a number of new crematoria over the relevant period, with these new sites reducing the average volumes per crematorium as they build up their volumes to maturity in the first few years of operation. This effect is particularly clear for Firm C and Firm B. Given this pattern of opening new crematoria over the relevant period, we expect the private operators' average volumes per crematorium to increase in the future.

Figure 5: Age of crematoria buildings



Source: CMA Analysis

Notes:

- a) The chart above is a bar chart.
- b) The chart above shows the age of crematoria buildings in four categories: 0-10 years old; 10-50 years old; 50-100 years old and over 100 years old.
- c) The chart shows the percentage of crematoria in our sample in each group, split by local authority (shown in dark blue) and large crematoria (in light blue).
- d) The chart shows that the percentage of local authority crematoria increases, with most (just over 60%) being in the 50-100 years old category. Most large crematoria in our sample are in the 0-10 years old (nearly 40%).

236. Figure 5 displays the age of crematoria buildings split by local authority and large crematoria by percentage⁸⁰ in the following categories:

- (a) 0 to 10 years old;
- (b) 10 to 50 years old;
- (c) 50 to 100 years old; and
- (d) Over 100 years old.

237. This shows that the local authority crematoria are skewed towards owning older buildings, with 64% in the 50-100 years old category and 18% over 100 years old. Conversely, the large crematoria in our sample tend to own newer buildings: 37% are 0-10 years old; 31% are 10 to 50 years old; 27% 50 to 100 years old and only 5% are over 100 years old.

⁸⁰ ie the percentage of local authority crematoria in our sample which fall into the following categories.

Capitalising leasehold land

238. As noted at paragraphs 67 and 68 [Firm B] and [Firm A] considered that the land at a number of sites held under long-term leases should be capitalised.
239. We considered the points raised and performed a sensitivity whereby land held under long-term leases was included in parties' capital employed and corresponding rental income was removed from the Profit and Loss account. This sensitivity was performed for all large crematoria but not for our sample of local authority crematoria, as all of them owned the land for their crematoria.
240. We performed the sensitivity under both Case One and Case Two land valuations.

Table 51: Large crematoria ROCE with capitalisation of long-term leases, Case One

	2014	2015	2016	2017	2018	Average
Firm A	15.9%	18.9%	20.4%	21.8%	21.5%	19.7%
Firm B	9.9%	13.5%	11.0%	10.1%	9.6%	10.7%
Firm C	1.8%	2.7%	5.8%	6.3%	7.4%	5.4%
Firm D	3.8%	3.8%	3.4%	3.6%	3.5%	3.6%

Source: CMA analysis

241. This sensitivity demonstrates that even where land held under long-term leases is capitalised, [Firms A and B] both still show a ROCE which is in excess of their cost of capital.

Table 52: Large crematoria ROCE with capitalisation of long-term leases, Case Two

	2014	2015	2016	2017	2018	Average
Firm A	11.7%	13.9%	15.0%	16.1%	15.8%	14.5%
Firm B	7.4%	10.1%	8.3%	7.5%	7.4%	8.1%
Firm C	1.8%	2.7%	5.8%	6.3%	7.4%	5.4%
Firm D	2.8%	2.7%	2.5%	2.7%	2.6%	2.7%

Source: CMA analysis

242. Table 52 demonstrates that [Firm A and B] achieve a ROCE equal to, or in excess of, their cost of capital, even when land is valued at a higher price per acre than the CMA considers to be reasonable, although under Case Two this finding is marginal for Firm B.
243. We disagree with parties that it is correct to capitalise land held under long-term leases and include it within the capital employed input to the ROCE calculation. Given that the results of this sensitivity analysis demonstrate that both [Firms A and B] achieved ROCE in line with, or in excess of, our estimate of their cost of capital, coupled with the likelihood of increasing profitability in the future for [Firms B and C], we do not consider that this analysis alters our findings of profits higher than would be expected in a well-functioning market and so have not considered it further.

Interpretation of our analysis

244. We received a number of submissions from crematorium operators regarding our analysis and interpretation of their profitability. In this section, we summarise their views and set out the conclusions that we draw from our profitability analysis.

Parties' views

Market coverage

245. In its response to the crematoria profitability paper, Dignity stated that 'The CMA's analysis covers less than 40% of the crematoria market (on the basis of either revenues or volumes) [...] This makes generalised conclusions on the overall market based on this small part of the market risky'.⁸¹
246. Memoria told us that the proposed sample size appears very small, comprising just 22 smaller crematoria which is around 10% of the population of smaller providers and therefore it did not provide sufficient detail to assess whether it would lead to a successful understanding of smaller crematoria (including local authorities).
247. Further, Memoria stated that the 'stratification proposed to establish a representative sample appears overly simplistic, controlling only for ownership [...] region and volumes [...] Memoria would expect local demographics, the mix of burials versus cremation/memorialisation and local competitive structure to also play a role in driving profitability of local authority crematoria'.
248. Westerleigh stated 'The CMA [...] proposes a light-touch 'small sample' approach meaning that information on profitability of only 30% of the market would be collected'.
249. Westerleigh also highlighted the CMA's guidelines which state that 'Profitability analysis is relevant "where profitability of firms representing a substantial part of the market has exceeded the cost of capital over a sustained period"'.⁸²

⁸¹ Dignity response to Crematoria profitability working paper, dated 12 June, page 5, paragraph 3.1

⁸² CC3 (revised) paragraph 118

250. LCC told us that they noted we had selected a random sample of LA providers, however it did not follow ‘that a random sample is either adequate or representative’⁸³ and provided information from the Pharos 2019 report of crematoria prices. LCC concluded that the sample of local authority crematoria was ‘significantly skewed towards higher charging LAs’.⁸⁴⁸⁵
251. LCC also noted that, based on the Pharos 2019 report, of the top 37 crematoria charging £950 or more: two are owned by local authorities; two by independent crematoria and the remainder by Dignity, Westerleigh and Memoria.⁸⁶ LCC stated that this ‘could be due to crematoria age or quality/heritage with newer facilities perhaps charging a legitimate price premium for newer and/or better premises’.⁸⁷
252. LCC told us that ‘the CMA need to attempt to analyse return on capital by geography and local competitive dynamics’.⁸⁸
253. Finally, Dignity told us it had ‘significant concerns that the cost bases for Local Authorities will not have been measured correctly; for example, understating the allocation of central costs’.⁸⁹

Time period

254. Dignity told us that ‘the long-lives of crematoria assets also means that investigating profitability trends with only a six-year window may not give a representative view’.
255. Dignity also told us that [✂].⁹⁰
256. With regards to the time period, Memoria told us that ‘it will be important to recognise in interpreting the results that this will not cover a full business cycle, or the lifespan of the key crematoria assets’. It continued: ‘this has been a period in the development of the crematoria market when years of underinvestment and under-capacity are in the process of being reversed’.
257. Westerleigh told us that investments in crematoria were large and risky and that the CMA guidelines notes that where such investments have been made,

⁸³ LCC response to Crematoria working paper, page 7, paragraph 4.18

⁸⁴ LCC response to Crematoria working paper, page 8, table

⁸⁵ LCC response to Crematoria working paper, page 8, paragraph 4.24

⁸⁶ LCC response to Crematoria working paper, page 9, paragraph 4.30

⁸⁷ LCC response to Crematoria working paper, page 11, paragraph 4.31

⁸⁸ LCC response to Crematoria working paper, page 8, paragraph 4.26

⁸⁹ Dignity response to PDR, annex, page 10, paragraph 3.3

⁹⁰ Dignity response to Crematoria profitability working paper, dated 12 June, page 1, paragraph 1.2B

the CMA ‘would expect to see a normal level of profits restored over a relatively long timescale’. On this basis, Westerleigh concluded that ‘the CMA’s proposed approach in the working paper therefore does not appear consistent with either the characteristics of the sector or its own guidance’.

258. Westerleigh further highlighted that ‘five years is not a sufficient time period to identify trends’.

Competitive benchmark

259. Westerleigh told us that the CMA’s interpretation of Westerleigh’s profitability ‘applies a threshold for “excess profits” that is erroneously predicated on an assumption that a “well-functioning market” would provide operators with no incentive to invest in that market’.⁹¹ We take this to mean that Westerleigh thinks that crematorium operators in the market would not invest in the market if they did not earn returns which were more than their cost of capital.

260. However, Westerleigh submitted that [redacted]⁹² but noted that it ‘[redacted]’.⁹³

Future profitability

261. Memoria told us that ‘[redacted]’ as: ‘most of Memoria’s sites are already well established and [redacted]’ and ‘[w]hen inevitable future increases in cremator maintenance costs are taken into account [redacted]’.⁹⁴
262. Memoria further noted that ‘there is no clear relationship between age of site and utilisation or profitability for sites that are more than a couple of years old’.⁹⁵
263. Regarding the argument that the return the business might be expected to earn once its crematoria reached maturity, Westerleigh submitted that ‘[redacted]’.⁹⁶ Westerleigh also stated that ‘[redacted]’.⁹⁷

⁹¹ Westerleigh response to PDR, page 36, para 118

⁹² Westerleigh response to PDR, page 36, para 119

⁹³ Westerleigh response to PDR, page 37, paragraph 125.

⁹⁴ Memoria response to PDR, page 30, section 4.1

⁹⁵ Memoria response to PDR, page 30, section 4.1

⁹⁶ Westerleigh response to PDR, page 38, paragraph 124

⁹⁷ Westerleigh response to PDR, page 38, paragraph 125

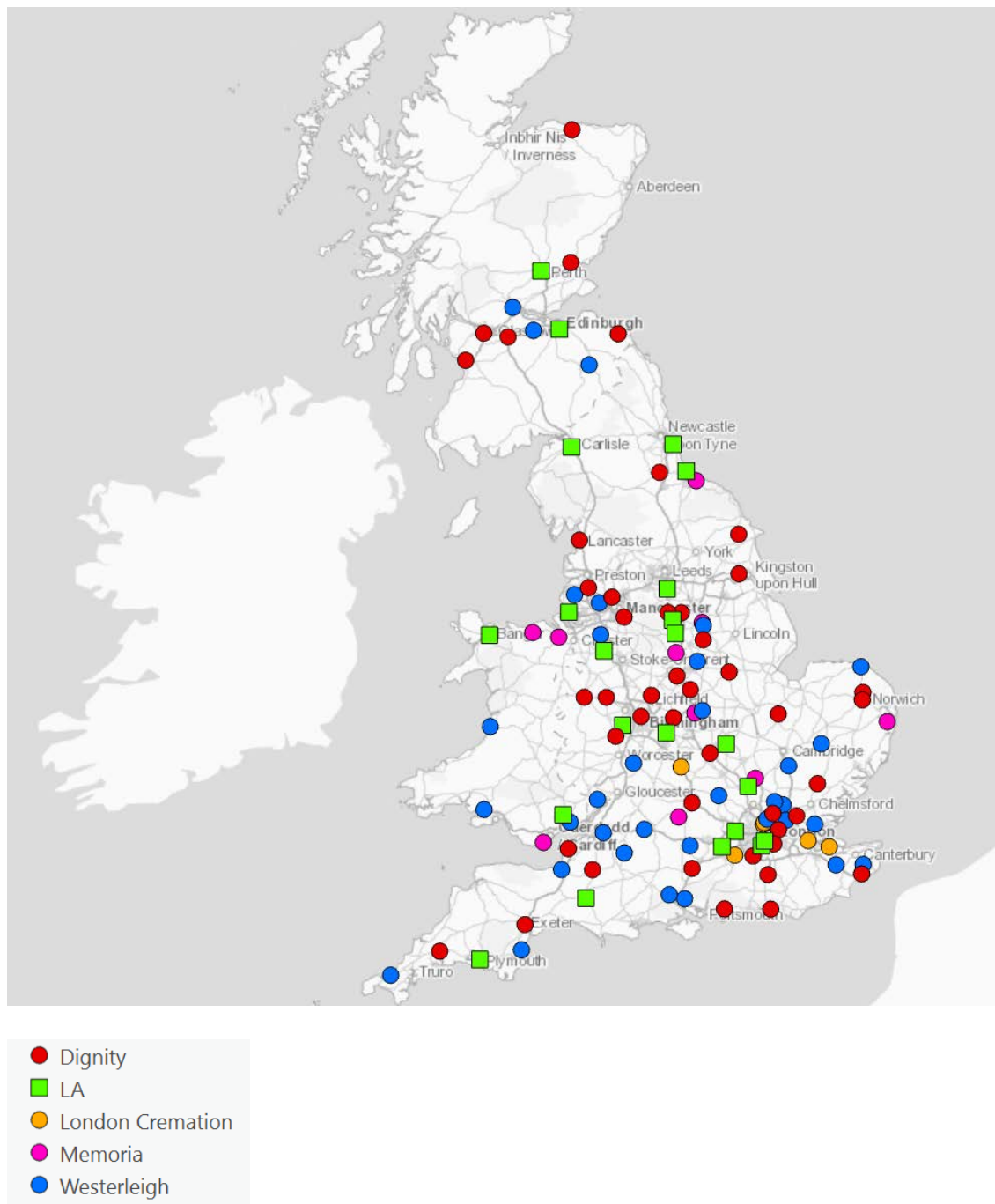
Our approach

Market coverage

264. We note parties' views on coverage and their arguments that we should extend its analysis to a greater proportion of the sector in general, and the local authority providers in particular.
265. The provision of crematoria services in the UK is highly fragmented, with the four largest firms accounting for around 26% of the sector by volume.⁹⁸ In carrying out our analysis, therefore, we must balance considerations of coverage with practical concerns regarding the collection of robust financial data from a large number of parties.
266. We note that our current approach means that our analysis covers 117 out of approximately 300 crematoria in the UK, which is just under half the total number of crematoria. With regards to the fragmented portion of the sector (around 70% of cremations by volume), we consider that our 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 that part of the sector as a whole. We note that our sample of local authority crematoria has broad geographical coverage as well as a mix of larger and smaller urban areas, and rural locations. See Figure 6 below.
267. Regarding analysis of sampled local authority crematoria revenue compared to the Pharos report 2019, we do not agree that LCC's analysis of our sample shows a material skew towards higher charging crematoria. We note that when all twenty-two crematoria are considered, only eight of the sampled local authorities have a fee greater than the average presented. As noted in the paragraphs above we consider that our sample is likely to provide information that is statistically representative and so do not propose any change to our approach.

⁹⁸ CMA analysis of the Cremation Society data

Figure 6: Map of coverage of crematoria and key



268. In this context, we do not believe that extending our sample would have provided significant additional insight into the financial performance of the crematoria sector. Furthermore, we note carrying out a full profitability analysis on 26 crematorium operators (both large and local authority crematorium operators combined) is resource intensive and that increasing the number of parties further would have created practical challenges in terms of completing our analysis, robustly, within the timeframe of our investigation,

without adding significant benefit. As such we chose not to extend the sample size.

269. However, we have supplemented our analysis by also reviewing and analysing the data prepared by the Chartered Institute of Public Finance & Accountancy ('CIPFA') on the financial performance of local authority crematoria. This dataset comprises information on the financial performance of 79 crematoria in 2014/15 and 69 crematoria in 2015/16. We have considered how the margins of these crematoria compare with those of the firms for which we have undertaken a full profitability analysis and how this information should be interpreted in the context of our overall analysis. See Annex 1 for further details.
270. We note LCC's response that a price premium may legitimately be charged by parties with newer crematoria. We consider that, to the extent that newer, private sites are justifiably more expensive, it is because those sites have a higher cost plus. That is only likely to be because they have newer, undepreciated assets, on which they need to make a return. However, since we are taking into account all operating costs plus a return on capital, we consider that we are allowing for differences in cost based on differences in quality (insofar as those differences in quality cost providers more to provide).
271. Finally, we disagree that profitability should be analysed by geography and local competitive dynamics. As can be seen at Section 7, concentration and price/quality outcomes, we have found that measures of concentration do not significantly affect price and quality outcomes.
272. In carrying out our analysis, we performed a number of checks on the data provided by Local Authorities, including sense checking the average revenue per cremation and cost plus per cremation.
273. As explained above at paragraphs 215 and 200, we excluded LA 17 and LA 11 from our analysis, in the first case because we found the overall financial information to be unreliable and in the second case because we concluded that the cost information may have been too low to be credible.
274. Further, LA15 was unable to provide a breakdown of overhead costs and the information it provided suggests that its overhead costs include such distributions. As such it is likely LA 15's profitability is understated due to the inclusion of distributions in overheads costs. We erred on the side of caution by including this crematorium's results, despite the likelihood that its profitability was understated.
275. In this context, we are satisfied that 19 out of 22 Local Authorities have provided us with reliable financial information. Furthermore, as this sample

was representative and we have been relatively conservative in terms of excluding/including Local Authorities where we had any doubt at all over their financials (ie we included LA15 where its profits are likely to be understated but excluding LA 11, where its profits are likely to be overstated), we are confident that to the extent that our findings are not fully representative of all Local Authority crematoria, they are likely to be under- rather than over-stated. As such, our conclusions regarding the high profits being earned are robust.

Time period

276. Next, we considered parties' representations regarding the timeframe for our analysis. First, we observed that, while five years is shorter than the lifecycle of an individual crematorium, our analysis covers a broad range of crematoria that are in different stages of the lifecycle. As such, we do not consider it necessary to extend the relevant period for our analysis in order to understand the profitability of crematoria over their lifecycle since this can be achieved on a cross-section basis.
277. We consider that 5 years is a sufficient period over which to understand the profitability of crematoria. While we agree that it would be helpful to include information on the most recent performance of the firms in the industry by obtaining 2019 data and future forecasts, this has not been practicable given the current climate and restrictions placed on data gathering as a result of COVID-19.

Competitive benchmark

278. Regarding Westerleigh's submissions on the appropriate competitive benchmark, we disagree that firms need to earn a return in excess of their WACC in order to have incentives to invest. Provided that investors expect to earn a return equal to their cost of capital, they have sufficient incentives to invest in an industry. This is reflected in the CMA's guidelines, which state that:

'Firms in a competitive market would generally earn no more than a 'normal' rate of profit – the minimum level of profits required to keep the factors of production in their current use in the long run, i.e. the

rate of return on capital employed for a particular business activity would be equal to the opportunity cost of capital for that activity.⁹⁹

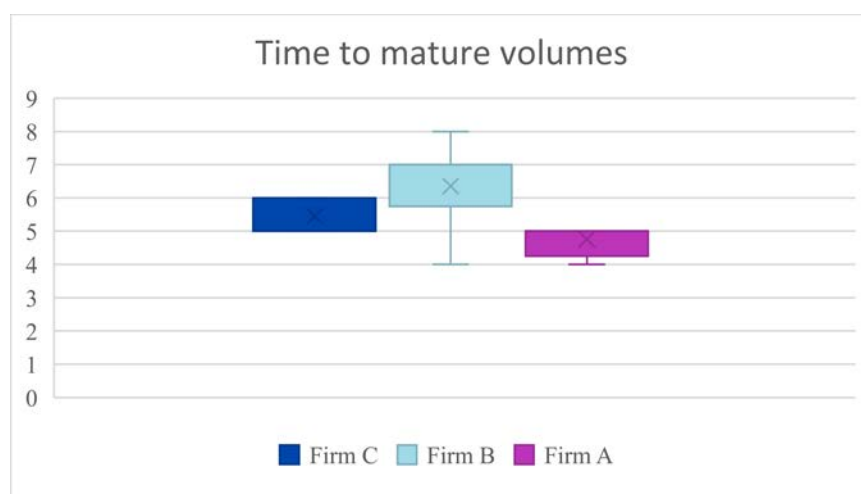
279. Further, we observe a tension in Westerleigh's position that a return in excess of the cost of capital is required in order to incentivise investment, that it plans to make further investments in the sector and that, at the same time, we are wrong to find that it is making returns in excess of its cost of capital.

Future profitability

280. We considered Memoria's and Westerleigh's submissions that there was no reason to believe that their profits would increase in the future. In particular, we have examined the evidence on growth in both crematoria volumes and cremator maintenance costs over time.

281. First, we reviewed the investment appraisals provided by [redacted], [redacted] and [redacted] [three of the large private crematorium operators] and considered the time taken to achieve steady state volumes. The results of this are presented in figure 7 below:

Figure 7: average time taken to achieve mature volumes as per investment appraisals



Source: CMA analysis

Notes:

- The chart above is a box and whisker chart.
- The chart above shows the average time taken to achieve mature volumes as per investment appraisals for [redacted], [redacted] and [redacted] [three of the large private crematorium operators].
- Firm C is shown in dark blue; Firm B is shown in light blue and Firm A is shown in purple.
- The chart shows that mature volumes were projected to be achieved after, on average, between five and six years.

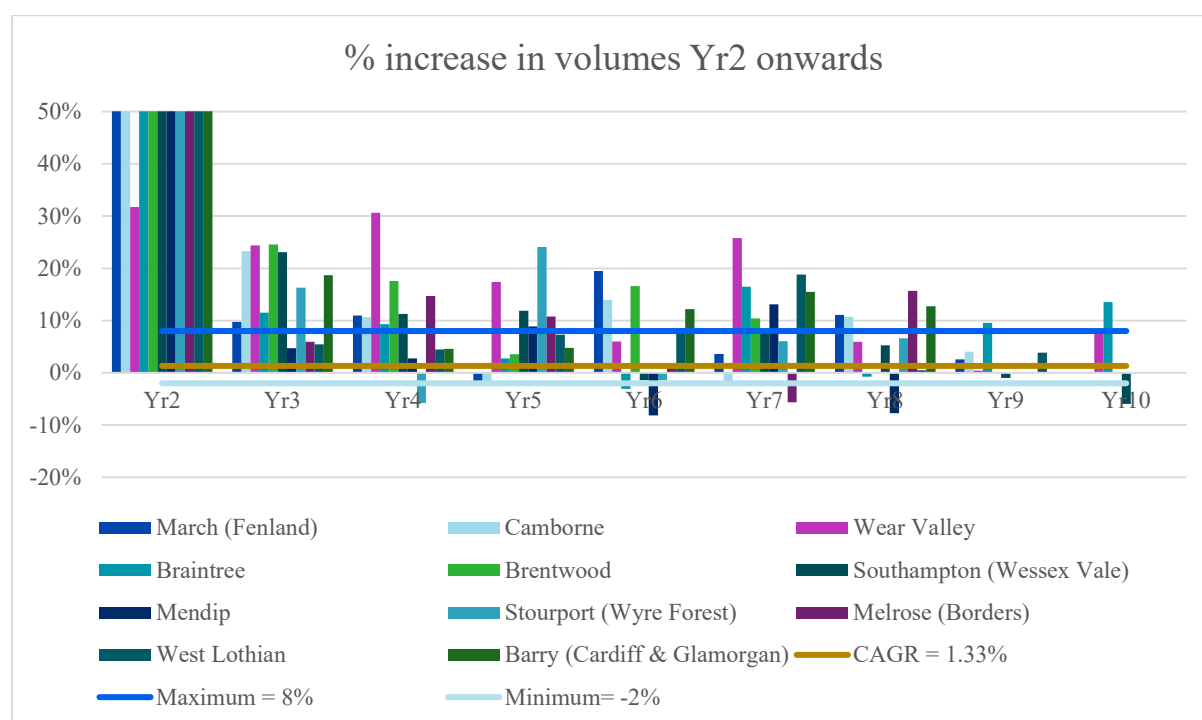
282. Figure 7 shows that mature volumes were projected to be achieved after, on average, between five and six years. In no cases were volumes projected to

⁹⁹ CC3 Revised, paragraph 116.

reach steady state before the crematorium had been open for four years and, in some cases, steady state was not forecast until years seven or eight.

283. We then considered at the actual volume growth achieved at sites opened by Dignity, Westerleigh and Memoria since 2009. We took the first year with volumes to be Year 1 (Yr1) and then considered the % increase from Yr1 to Yr2 and so on for all sites. To aid comparability, we also considered the growth rate in cremation volumes in the UK as per the Cremation Society over this same period. We calculated that across the period 2009 to 2019 the minimum annual growth rate was -2% (ie a reduction of 2%); the maximum annual growth rate was 8% and the compound annual growth rate (CAGR) was 1.33%.¹⁰⁰ We reasoned that any individual crematorium could be considered to have reached steady state when its growth was approximately in line with the national average, taking into account that somewhat greater year-on-year volatility might be expected at the level of an individual site.

Figure 8: percentage increase in volumes from Yr2 onwards



Source: CMA analysis and the Cremation Society

Notes:

- The chart above is a compose bar chart.
- The chart shows the year on year percentage increase in volumes achieved at eleven sites from Year 2 onwards.
- The chart also shows the maximum, minimum and compound average growth rate of volume of cremations as per the CMA's analysis of the Cremation Society data.
- The chart shows that the majority of sites grew by more than the estimated annual growth rate of 8% until at least year 4.

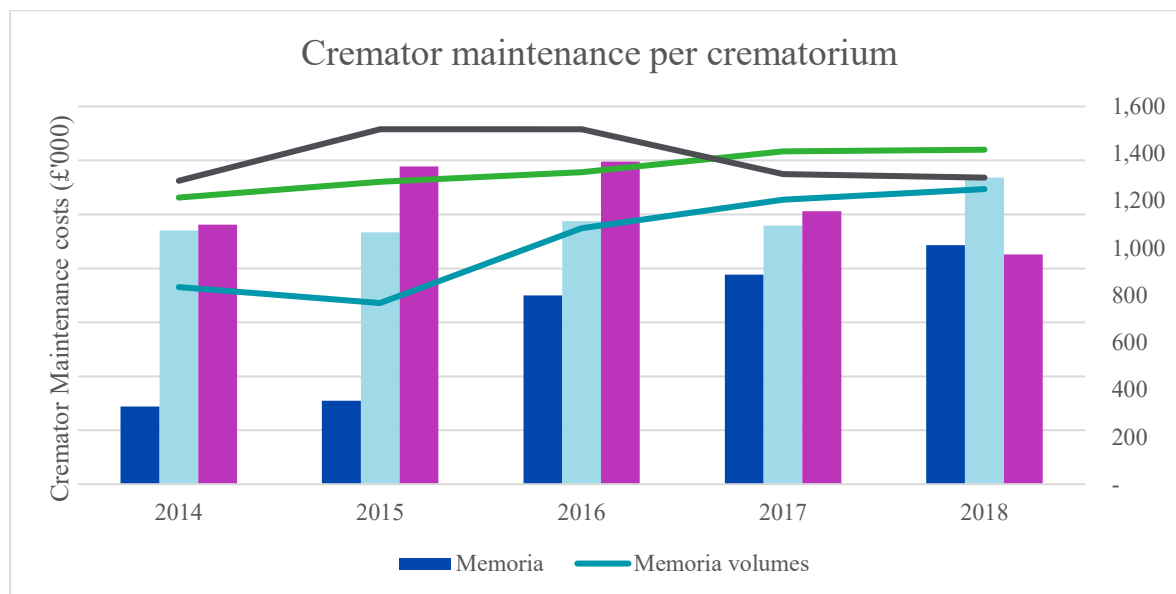
284. Figure 8 demonstrates that, while the results fluctuate each year, the large majority of sites grew by more than the Cremation Society's maximum annual

¹⁰⁰ Cremation Society: table of cremations

growth rate of 8% until at least year 4, and that a number of sites experienced growth exceeding 10% in year 7. This evidence supports the finding that, on average, sites do not reach maturity until at least year 4, and often later than that. This is consistent with the forecasts used by the private operators in their investment appraisals.

285. Second, to assess Memoria’s claim that cremator maintenance costs would increase in the future, we calculated the average cremator maintenance costs per site for each of [redacted], [redacted] and Memoria for each year in the Historic Period.

Figure 9: cremator maintenance costs per crematorium



Source: CMA analysis

Notes:

- The chart above is a composite bar chart.
- The chart shows cremator maintenance costs and average volumes per crematorium for Memoria, [redacted] and [redacted] [two of the large private crematorium operators].
- The bar chart represents cremator maintenance costs.
- The line chart represents volume of cremations.
- Memoria cremator costs are shown in dark blue and volumes are shown in turquoise.
- Two of the large private crematorium operators' cremator costs are shown in light blue and purple, and volumes are shown in green and grey.
- The y-axis (cremator maintenance costs) has been left blank for confidentiality reasons.
- The chart shows that Memoria’s cremator costs increased significantly; [redacted] costs increased slightly and [redacted] costs increased to a peak in 2016 then decreased to 2018.

286. As can be seen at Figure 9, Memoria’s costs increased from c.[£5,000-10,000] to c.[£20,000-30,000] per site over the Historic Period, while [redacted] and [redacted]’s per-site costs suggest that around £25,000 to £30,000 is average for a mature portfolio.

287. However, we noted that Memoria's volumes are materially lower than [redacted] as of 2018 (by c.200 cremations per site) and [redacted] as of 2016 (c.250 cremations per site).¹⁰¹
288. As explained above, we find that crematoria generally do not reach maturity until at least their fourth year of operation and, in many cases, later than that. This is consistent with our observation that Memoria's average volumes have been significantly lower than those of [redacted] and [redacted] over the relevant period due to having a relatively recently opened portfolio of crematoria. Therefore, we consider that while Memoria's annual cremator costs may increase by a further £3,000 to £8,000 per site as these sites age, this increase in costs will be more than offset by the corresponding revenue earned with increased sales. (A further 10 cremations per year would comfortably cover these increased costs in the context in which Memoria's average volumes per site are around 200-250 lower than those of [redacted] and [redacted]).
289. Similarly, we expect [redacted]'s profits to increase in future years, potentially materially, given its relatively new portfolio of crematoria. Of its [redacted] sites, [redacted] and a corresponding drop in average volumes can be seen at Figure 9 in 2017. We expect the average volume to increase as these sites reach steady state.

Capitalising leasehold land

290. As discussed above, we do not agree that it is correct to capitalise leasehold land. However, even under Case Two plus capitalising leasehold land, Firm A earns returns in excess of its cost of capital and Firm B earns returns equal to its cost of capital. There is no impact on the results of Local Authorities as these all own their land in any case.
291. In a context in which, we believe that Case Two is likely to overstate average crematorium land values on a UK-wide basis and we find both Firm B and C's profits to have been suppressed over the relevant period due to opening a significant number of new sites, this sensitivity does not give us reason to alter our basic conclusions regarding the ability of crematorium operators in the UK to earn returns in excess of their cost of capital.

¹⁰¹ We have compared Memoria's volumes with Westerleigh's average volumes as of 2016 as in 2017 and 2018. Westerleigh opened a further 6 and 4 crematoria, respectively. We note that this will have reduced their average volumes per site in those years as these new crematoria would not have been operating at steady state. As Dignity has a large portfolio (46 crematoria) and opened only one new one over the relevant period, we consider that its volumes are likely to provide the best benchmark, albeit in a market where volumes are growing year on year.

Summary

292. Two of the four large private crematorium operators have been persistently earning returns in excess of the cost of capital. Further, we note that average returns at two of the large private crematorium operators appear to have been reduced as the result of opening a large number of new crematoria which have yet to achieve maturity. As a result, these firms may be expected to earn higher returns in the future. Similarly, the majority of local authority crematoria that we have analysed have been persistently earning returns in excess of the cost of capital. As our sample was selected randomly, we consider that this finding indicates that a majority of local authority crematoria across the country are earn returns that are significantly in excess of the cost of capital.
293. Overall, therefore, our analysis indicates that firms comprising a substantial proportion of the crematorium market have been able to charge prices significantly above the level one would expect to see in a well-functioning market over an extended period of time (at least the five year period for which we have conducted this analysis).
294. In addition, we observe a trend of increasing profitability, on average, across the crematorium market. This trend is present among both local authority crematoria (see Figure 3) and the large private crematoria firms (see Tables 1 to 7).

Annex 1

CIPFA Dataset

295. Local authorities make up 90% of the smaller providers in the crematoria services sector. Separate financial statements for the operation of local authority run crematoria are not publicly available. However, the Chartered Institute of Public Finance and Accountancy (CIPFA) undertakes annual surveys of local authority operations; this includes requesting financial information on crematorium operated by local authorities. We have referred to this as the 'CIPFA dataset'.
296. We have analysed two years of this data (2014/15 and 2015/16) for the purpose of comparing it to the results of our profitability analysis.
297. For the 2014/15 CIPFA dataset the response rate was: 79 of 194 crematoria surveyed. For the 2015/16 CIPFA dataset the response rate was 69 of 194 crematoria surveyed.

Net margins

298. We used the data provided to CIPFA for net expenditure including capital charges¹⁰² and total income to calculate the net margin for each local authority crematorium.
299. Table 53 below shows the range of net margin values within the responses for each year. The local authority net margins range widely, particularly in 2014/15. In both years, much of this range is within the first quarter, influenced by two to three low outliers. The gap between the average and median values also reflects the skewing effect of these very low outliers.

¹⁰² Our review of the margins for the overlapping local authorities in the CMA and CIPFA datasets indicated that generally the capital charges declared to CIPFA were very similar to the depreciation and amortisation charges provided to CMA.

Table 53: Local authority net margins range, CIPFA data

	2014/15	2015/16
Minimum Value	-281.1%	-49.2%
1st Quarter	32.4%	30.1%
Median	46.8%	47.6%
3rd Quarter	57.1%	59.2%
Maximum Value	71.9%	75.8%
Average Value	37.7%	40.8%

Source: CMA analysis

300. Table 54 below shows the net margin of large crematoria in 2014/15 and 2015/16.

Table 54 Large crematoria net margins range

	2014/15	2015/16
Dignity	[REDACTED]	[REDACTED]
Westerleigh	[REDACTED]	[REDACTED]
LCC	[REDACTED]	[REDACTED]
Memoria	[REDACTED]	[REDACTED]

Source: CMA analysis

301. Over one quarter of the local authority crematoria generated higher margins than any of the four largest private providers in both years.

302. Figures 7 and 8, below, show the range of the local authority net margins plotted alongside the EBIT margins of the four largest providers in each year. This analysis indicates that, while there is significant variability in profit margins across the local authority crematoria included in the CIPFA dataset, the majority of local authority crematoria are earning margins in excess of those earned by [REDACTED] and [REDACTED] and broadly in line with those earned by [REDACTED] and [REDACTED].

Figure 10: Local Authority Net Margin Range Compared to the EBIT Margins of the Four Largest Providers for 2014/15

[REDACTED]

Source: CMA Analysis

Figure 11: Local authority net margin range compared to the EBIT Margins of the four largest providers for 2015/16

[REDACTED]

Source: CMA Analysis

303. In general, for the CIPFA dataset, the net margins increase slightly for those local authorities handling greater volumes of cremations and the costs per funeral reduce.

304. As previously noted, we have been unable to develop this analysis due to the COVID-19 pandemic. However, this analysis suggests that local authorities (more broadly than our sample) are earning similar profit margins to Firm A and Firm B and may, therefore, be expected to be earning returns in excess of our estimate of WACC for crematorium operators.