VETERINARY SERVICES FOR HOUSEHOLD PETS

Appendix C: Financial and profitability analysis

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Competition & Markets Authority

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The Competition and Markets Authority has excluded from this published version of the final report information which the inquiry group considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by [✂]. Some numbers have been replaced by a range. These are shown in square brackets. Non-sensitive wording is also indicated in square brackets.

Contents

Tables

Figures

Summary

1. This appendix sets out our assessment of the following:

   (a) Scope of our analysis – timeframe (five years to 2024 for the purposes of economic profits, and generally six years to 2025 for the purposes of ROCE analyses), and focus of the profitability analysis (UK clinical veterinary services, split as to local clinics, referral centres and standalone OOH)[1]; and

   (b) The ROCE approach – whereby a return on capital employed is compared with an estimate of the cost of capital. This approach requires that the capital employed figure is valued appropriately, and we have looked at each of tangible and intangible assets in turn:

      (i) Tangible assets:

         (1) We have made adjustments to the value of leasehold properties and fixtures & fittings / clinical equipment. For the latter we carried out a bottom-up analysis of the recent costs of fitting out a sample of greenfield clinics to arrive at a cost per square foot and extrapolated it across each LVG's estate.

         (2) We did not make adjustments to the value of freehold property, vehicles or working capital.

      (ii) Intangible assets:

         (1) We considered whether we should include customer relationships, skilled workforce, reputation/brand, software, and goodwill, and if so, at what value these should be included in the capital employed figure.

         (2) We included customer relationships, skilled workforce, national branding and software, and exclude reputation and goodwill.

         (3) We considered two approaches to asset valuation: the cost-based approach and the start-up losses approach, and included the value of intangible assets under the cost-based approach. In our sensitivity analysis we included the value of intangible assets under the efficient start-up losses approach.

   (c) Financial performance analysis of independent veterinary businesses – we conducted operating profit margin analysis for two sets of independent firms;

[1] For the purposes of the profitability analysis, 'local clinics' relates to all veterinary clinic activity, including that undertaken by farm, equine and mixed practices, apart from that activity undertaken by RCVS-specialist led referral centres ('referral centres') and by IVC's Vets Now ('standalone OOH').

a smaller sample of firms sourced by the CMA and a second larger dataset provided by a third-party

2. We included the results of the ROCE analysis for all six LVGs' local clinic operations, as well as the results of our analysis for the referral centre operations of Linnaeus. We compared the results of the ROCE analysis with the cost of capital estimate (9.0% per year midpoint, range 7.5% to 10.5% per year). Our analysis for the estimate of the cost of capital is set out in Appendix D: Cost of Capital. For the OOH operations of Vets Now (owned by IVC) we set out its operating margins but neither ROCE nor economic profits (see below).

3. We also set out the results in terms of economic profits. Economic profits are the profits earned in excess of cost of capital, which is equal to operating profit, or EBIT, less the capital employed multiplied by the cost of capital (we call this deduction 'capital employed opportunity cost'). In other words, we subtract the profit expected from a (normal) market-based return on the net assets deployed from operating profit figures. The resulting measure of profitability (economic profits) is, therefore, based on the same building blocks as ROCE and simply expresses returns above or below the mid-point for the cost of capital in absolute amounts.

4. We received submissions about how we should prepare and interpret this analysis over the course of our investigation.[2] We have reflected on the points made to us, updating the analysis where we consider warranted. Over the six-year period of this updated analysis, we note the following points:

LVGs: Base case

5. In the first instance we modelled a base case in which we:

   (a) valued the clinic fit-out element of tangible fixed assets across all LVGs using the same cost per square foot averaged across a sample of recent LVG clinic fit-outs.

   (b) modelled asset values on the basis that the clinic fit-out element of tangible fixed assets had a weighted average useful economic life of 16 years

   (c) determined the value of each LVG's intangible fixed assets on the basis of the cost incurred by each LVG respectively on certain, separable intangibles, namely customer list, training and national brand.

[2] Parties have had the opportunity to feedback on: the Profitability Approach Paper 1 November 2024, a working paper sharing our initial results shared with LVGs on 1 May 2025 and with independent veterinary firms on 4 July 2025 and our Provisional Decision Report October 2025.

6. We also then modelled 5 sensitivities to:

   (i) use the (lower) clinic fit-out costs per square foot incurred by a sample of independent firms (hence lowering the value of these assets and the related depreciation charges);

   (ii) apply a 25% uplift to the clinic fit-out cost asset values (hence increasing the value of these assets and the related depreciation charges);

   (iii) lengthen the expected useful life of the clinic fit-out cost assets from an average 16 years to 20 years (and hence lowering the value of these assets and the related depreciation charges); and

   (iv) shorten the expected useful life of the clinic fit-out costs from an average of 16 to 12 years (and hence increasing the value of these assets and the related depreciation charges).

   (v) value intangible assets on the basis of using the efficient start-up losses approach to valuing intangibles rather than the cost-based approach for assets that are separable from the general running of the business.

7. We first discuss the results according to our base case and for the five-year period to 2024.

8. There is a wide variation in levels of profits and returns. However, for the local clinics, four of the six LVGs have consistently earned returns above the cost of capital, that is to say earning economic profits, across the five-year period to 2024: [✂],[3] [✂], [✂] and [✂]. [✂] has the highest average ROCE of [✂]%, with [✂], [✂]'s and [✂]'s average ROCEs [✂]%, [✂]% and [✂]% respectively,[4] compared with our mid-point cost of capital estimate of 9%.

9. In line with ROCE, there is a similar pattern in terms of economic profit: four of the six LVGs have consistently earned substantial amounts of economic profit across the five-year period: [✂], [✂], [✂] and [✂].[5]

10. [✂] and [✂] earned average ROCE of [✂]% and [✂]% respectively across the five-year period to 2024. [✂] did not earn economic profits over the period, and inconsistent earnings from [✂] result in a small economic profit over the same period.

[3] With the exception of [✂].
[4] In this sub-section we compare ROCE to the cost of capital over the five years to 2024 (as set out in Table 1.1 in Part A: section 7), rather than the six years to 2025. This is because our assessment of the cost of capital covers the five year period to 2024. In Table 1.1 below, however, we present ROCEs over a six year period to 2025 as we have updated our ROCE information to include 2025.
[5] With the exception of: [✂].

11. For the non-local clinic operations:

(a) Linnaeus' RCVS-specialist led referral centre operations earned average ROCE over the five-year period to December 2024 of [✂]%, and economic profits [✂].

(b) Vets Now OOH and referral operations earned EBIT margins of [✂]% on average across the six years to September 2025. As Vets Now OOH utilises the capital employed of host clinics to a significant extent (which are not necessarily IVC local clinics), and therefore utilises a low base of tangible fixed assets of its own, we do not present ROCE results for Vets Now OOH.

Variation over the six-year period to 2025

12. All the LVGs have experienced, to varying degrees and timing, an increase in profitability as shown by ROCE from 2020 into the middle of the six-year period analysed, followed by a decline into 2024, and then stabilising in 2025 (with the exception of [✂]).[6]

13. Reflected within these numbers is the impact of LVG-specific factors such as permanent local clinic closures that all of the LVGs made across the period. For some LVGs these clinic closures were concentrated in certain periods: for example, Pets at Home closed over 30 clinics in FY2020. Also reflected within these numbers is the financial impact on certain LVGs of dealing with the CMA, such as the costs of legal and economic advice. More recently, in 2024 CVS was impacted by a cyber-attack which significantly disrupted its operations.[7] Also reflected in some periods within these numbers are the costs that PE-owned LVGs have incurred in obtaining professional advice related to the restructuring / refinancing of their wider corporate groups. These costs can be material to the profits earned in these periods, understating our profitability figures relative to the cost of capital.[8]

14. We subsequently analysed financial information for each LVG for the 12-month period ending in the calendar year 2025, calculating ROCE for this period as shown in the tables below. We found that the level of ROCE persisted for each of the four LVGs generating economic profits materially above the mid-point of the cost of capital over the period to 2024.

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[6] [✂].
[7] See CVS Group plc Annual Report and Financial Statements for the year ended 30 June 2024, Note 6 Exceptional Items, page 122, and Financial KPIs, Adjusted EBITDA, page 24, for quantification of the estimated impact.
[8] These costs appear to be costs directly relating to the re-raising of funding. An efficient level of such costs could be treated as an element of the (forward-looking) cost of capital and, as such, their efficient level would be recovered across a period longer than one year. We, however, have not included such costs in our assessment of the level for the cost of capital..

Summary of results for individual LVGs

15. The table below summarises the results of the analysis for all of the LVGs' local clinic operations for the six-year period to 2025 in the case of ROCE and the five year period in the case of economic profits, and the second table summarises the results of the analysis for Linnaeus' referral centre operations and the third table Vets Now OOH operations (operating profit margins analysis only).

Table 1.1 ROCE (% per year) and economic profits (£m) for each LVG's local clinic operations (base case), 2020-2025

		Year in which each LVG's financial year ends					
		2020	*2021*	*2022*	*2023*	*2024*	*2025*
CVS (June)	ROCE (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Economic profits (£m)	[✂]	[✂]	[✂]	[✂]	[✂]	na
IVC excluding Vets Now (September)	ROCE (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Economic profits (£m)	[✂]	[✂]	[✂]	[✂]	[✂]	na
Linnaeus (local clinics) (December)	ROCE (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Economic profits (£m)	[✂]	[✂]	[✂]	[✂]	[✂]	na
Medivet (April)	ROCE (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Economic profits (£m)	[✂]	[✂]	[✂]	[✂]	[✂]	na
Pets at Home (March)	ROCE (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Economic profits (£m)	[✂]	[✂]	[✂]	[✂]	[✂]	na
VetPartners (June)	ROCE (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Economic profits (£m)	[✂]	[✂]	[✂]	[✂]	[✂]	na

Source: CMA analysis based on information provided by the LVGs. Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

Table 1.2 ROCE (% per year) and economic profits (£m) for Linnaeus referral centre operations (base case), 2020-2025

		Year to December					
		2020	2021	2022	2023	2024	2025
Linnaeus (December)	ROCE (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Economic profits (£m)	[✂]	[✂]	[✂]	[✂]	[✂]	na

Source: CMA analysis based on information provided by the Linnaeus.
Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

Table 1.3 EBITDA and EBIT margins (in £m) for Vets Now OOH operations, 2020-2025

	Year to September						
	2020	*2021*	*2022*	*2023*	*2024*	*2025*	*Total*
Revenues	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
EBITDA	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
EBITDA margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
EBIT margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on information provided by the IVC. See Vets Now subsection within Annex B to this appendix for further detail about how this information has been analysed.

Constraints on our analysis

16. We note that there are a number of constraints on the information we were able to gather and therefore limitations to our analysis which include the following:

    (a) We estimated the value of tangible fixed assets within the local clinics, comprising leasehold improvements, equipment and fixtures and fittings (which we call fit-out costs) based on the cost of the available sample of the LVGs' greenfield fit-outs. Because the LVGs have generally grown by acquisition and not greenfield openings, this was limited to 29 sites across the LVGs' total portfolios. For sensitivity analysis purposes we also modelled the impact of using the fit-out costs of a further nine independent greenfield sites opened in the last five years. The average fit-out costs per square foot for this sample was significantly lower than that of the LVGs (£204 compared to £329 for the LVGs' in 2024). We also analysed the fit-out costs of [✂], an independent group who opened [✂] clinics in the last five years. While we did not model any sensitivity analysis on these sites we note that their fit-out costs per square foot were also significantly lower than the LVGs ([✂][9] compared to £329 in 2024).

    (b) We estimated the cost of creating the relevant intangible assets on a per clinic basis using cost information obtained from the LVGs and used that per clinic estimate to generate our estimate for the aggregate value of these assets for each LVG.

    (c) For sensitivity analysis purposes, we estimated the value for intangible assets under an alternative approach (based on efficient start-up losses) based on a limited available sample of greenfield openings by Pets at Home, given that in the period of analysis only Pets at Home established new sites for local clinics for which we could obtain full information.

[9] [✂]

17. Other points to bear in mind when interpreting the results set out above include:

    (a) For simplicity, we used CPI in order to update fit-out cost figures at each year end for cost inflation.

    (b) Although we have revalued the fit-out cost assets of each LVG using CPI on the balance sheet to take account of cost inflation across the period of review, we did not reflect the resulting increase in value of existing fit-out assets in the individual LVG profit and loss statements. Were we to do so this would result in a credit to the profit and loss statement and hence increase profitability. Our profitability results for LVGs will therefore be understated in this respect and the effect may not have been immaterial over this period of high inflation.

    (c) We discuss from paragraph below how we carried out a simple extrapolation across the estates of the LVGs of our estimate for the efficient level of start-up losses for a representative greenfield site.

18. Some allowance has been made for these factors through the use of sensitivity analysis, which we set out in the following section, together with the results of that analysis.

LVGs: Sensitivities carried out on local clinic results

19. Our profitability assessment has required an extensive revaluation of the fixed assets of the LVGs. For this we have used information from a number of sources, to extrapolate across each LVG's total portfolio of clinics to arrive at our asset valuations. We have conducted a number of sensitivities on these asset valuations in order to understand the impact these have on the results of our profitability analysis for the LVGs' local clinics.

20. In revaluing fixed assets, we need to make some adjustments to reflect better the economic performance as opposed to accounting performance. We have sought and received input from the LVGs and their advisers in relation to these assumptions and have carefully evaluated this input. We have consistently sought to be balanced in our methodology. Nevertheless, we acknowledge some assumptions are unavoidable and this is exacerbated in businesses such as certain LVGs where a significant proportion of the value of their tangible fixed assets were not recorded in their accounts. In addition, the intangible assets we sought to value are not reported on at all.

21. Accordingly, we have carried out the following sensitivity analysis to:

    (a) use the (lower) clinic fit-out costs per square foot incurred by a sample of independent firms (hence lowering the value of these assets and the related depreciation charges) (Sensitivity A);

(b) apply a 25% uplift to the clinic fit-out cost asset values (hence increasing the value of these assets and the related depreciation charges) (Sensitivity B);

(c) lengthen the expected useful life of the clinic fit-out cost assets from an average 16 years to 20 years (and hence lowering the value of these assets and the related depreciation charges) (Sensitivity C); and

(d) shorten the expected useful life of the clinic fit-out costs from an average of 16 to 12 years (and hence increasing the value of these assets and the related depreciation charges) (Sensitivity D).

(e) value intangible assets on the basis of using the efficient start-up losses approach to valuing intangibles rather than the cost-based approach for assets that are separable from the general running of the business (Sensitivity E).

22. We set out in the table below in tabular form the results of our sensitivities on our base-case ROCE, which we have averaged over the six years to 2025, and sensitivities on our base-case economic profits, which we have totalled over the five years to 2024. At Table 1.5 we have totalled economic profits over the five years to 2024 because our estimates for the cost of capital (which ranges between 7.5% to 11.5% per year with a mid-point of 9.0% per year) only covers the period 2020 to 2024 inclusive.

Table 1.4: Summary of sensitivities based on average ROCE for each LVG's local clinics over the six-year period 2020 to 2025 inclusive (percent per year)

	CVS	IVC	Linnaeus	Medivet	Pets at Home	VetPartners
Scenario						
Base case	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Higher ROCE scenarios						
a Value the clinic fit-out element of tangible fixed assets (and related depreciation charge) based on the clinic fit-out costs of independent firms	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
c Lengthen expected useful life for fit-out costs (and related depreciation charge)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Lower ROCE scenarios						
b Increase valuations for fit out costs by 25% (and related deprecation charge)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
d Shorten expected useful life for fit-out costs (and related depreciation charge)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
e Adopt efficient start-up losses approach to valuation (asset value not amortised)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source CMA analysis based on information supplied by LGVs.

Note 1: Average ROCEs have been computed by the aggregate of individual year EBIT figures over the aggregate of average capital employed figures for each year

Note 2: Individual LVGs have financial year ends end in different months ranging from March to December, so these 6-year averages cover broadly the same period.

Table 1.5: Summary of sensitivities based on aggregate economic profits for each LVG's local clinics over the five-year period 2020 to 2024 inclusive (£ millions)

	CVS	IVC	Linnaeus	Medivet	Pets at Home	Vet Partners
Scenario						
Base case	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Higher economic profit scenarios						
a Value the clinic fit-out element of tangible fixed assets (and related depreciation charge) based on the clinic fit-out costs of independent firms	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
c Lengthen expected useful life for fit-out costs (and related depreciation charge)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Lower economic profit scenarios						
b Increase valuations for fit out costs by 25% (and related deprecation charge)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
d Shorten expected useful life for fit-out costs (and related depreciation charge)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
e Adopt efficient start-up losses approach to valuation (asset value not amortised)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source CMA analysis based on information supplied by LGVs.
Note 1: Average ROCEs have been computed by the aggregate of individual year EBIT figures over the aggregate of average capital employed figures for each year.
Note 2: Individual LVGs have year ends end in different months, so these figures cover broadly the same period.

23. Applying sensitivities introduces a range of outcomes. Every scenario has the same four LVGs' earning profits more than WACC based on the five years to 2024.

    (a) Basing valuations for fit out costs on those of independent firms (and related depreciation charge) (Sensitivity A) has the effect of increasing average ROCE (by 5-11 percentage points per year across each of the LVGs);

    (b) increasing the fit-out costs by 25% (Sensitivity B) has the effect of reducing average ROCE (by 2-5 percentage points per year across each of the LVGs).

    (c) lengthening the expected useful life for fit-out costs (and related depreciation charge) (Sensitivity C) also has the effect of increasing average ROCE (by 1-2 percentage points per year across each of the LVGs);

    (d) shortening the expected useful life for fit-out costs (and related depreciation charge) (Sensitivity D) has the effect of reducing average ROCE (by 2-3 percentage points per year across each of the LVGs); and

    (e) using the efficient start-up loss approach to valuing intangibles (Sensitivity E) has the effect of reducing average ROCE (by 1-6 percentage points per year across each of the LVGs).

LVGs: Efficiencies and synergies from [✂] business model

24. We note that [✂] has a significantly higher average ROCE than the other LVGs'. A significant factor driving this is [✂]. As set out below, [✂].[10] [✂].[11]

Financial performance of independent veterinary businesses

25. Our initial analysis for independent veterinary firms focussed on EBIT margins of a randomised sample of 36 independent firms covering 133 FOPs over the period of 2021 to 2023. This analysis showed that there was a wide distribution of EBIT margin for the independent firms in our sample. The firms in our sample had a range of EBIT margins of between negative 9%[12] and positive 34%, with a weighted average EBIT margin for the three-year period of positive 11%. The basis of preparation adopted here was designed to help ensure a degree of comparability of the EBIT margins across the independent firms and differed in some important respects from that adopted for the LVGs.

26. There are differences in the basis of preparation for the margin figures between those for the LVGs and the independent firms; the analysis of the independent datasets related to only those firms who traded over the period whereas the LVG analysis accounted for all clinic closures; and we have not assessed the differences in the way tangible fixed assets within capital employed, and therefore depreciation charges, have been measured between independent firms and LVG local clinics.

27. Furthermore, the differences in operation of independent firms and the LVGs lead us to interpret any comparison between the independent firms' and the LVGs' operating profit margins with caution.

28. In addition to our analysis of a sample of the 36 independents, we analysed a dataset received from an accountancy firm specialising in the veterinary sector covering 157 firms across 306 FOPs. The financial data spanned the years 2021 to 2025. Out of these 157 firms, 35 were start-ups. We identified and excluded data from these 35 firms that fell within their first three years of operation.

29. By removing those startups, we identified a range of net operating profit from negative 23% to positive 36% over the years 2021 to 2025 with a weighted average margin of 11% of the remaining firms.

30. Further datasets have been received; however, the data points were insufficient to be able to draw any reliable conclusions. For example, another [✂] firm

[10] [✂] response to the financial analysis and profitability working paper, paragraphs 4.1 to 4.12.
[11] [✂] response to the CMA Profitability WP at page 19 and Annex 002.
[12] The range previously included a firm with an EBIT margin of -51%, however, we found this firm was not a local clinic but instead a mobile vet conducting home visits and was therefore been removed from the sample.

specialising in the veterinary sector submitted a dataset of [✂] small animal veterinary firms, with only 27 datapoints in the most recent year.[13] Another dataset received from a specialist veterinary business consultancy, included only operating margins for one financial year.[14]

[13] [✂].
[14] [✂].

1. Introduction and purpose of this appendix

1.1 This appendix sets out how we have assessed the profitability of local clinics providing veterinary services and presents the findings from our financial and profitability analysis.

1.2 On 1 November 2024, 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.

1.3 We considered parties' comments on this proposed methodology carefully. We subsequently produced a working paper titled 'Financial and profitability analysis' (the **Profitability Working Paper**) setting out how we assessed the profitability of local clinics providing veterinary services and presenting the findings from our financial and profitability analysis to that point.

1.4 Over the course of May and July 2025, we shared the **Profitability Working Paper** with the LVGs, other main parties and independent veterinary practices from whom we requested financial information. The supporting Excel workbooks with the LVG analysis (but not the analysis for the independent firms) also went into a confidentiality ring with the LVGs' economic advisors. We have considered parties' comments on the Profitability Working Paper carefully.

1.5 We subsequently published our PDR, to which the provisional version of this appendix was published in October 2025 and further responses were received. This appendix sets out how we have taken those responses into account in carrying out our analysis and assessment of the profitability of local clinics providing veterinary services. However, we have not repeated here the detailed methodological discussion set out in our previous Profitability Approach Paper.

1.6 In performing our analysis, we have considered two main groups of veterinary services providers:

(a) The six largest veterinary groups, CVS, IVC, Linnaeus, Medivet, Pets at Home, and VetPartners (the **LVGs**);

(b) Independent veterinary businesses, comprising:

(i) The five veterinary businesses with ten or more practices, being [✂] (the **Mid-Tier independent businesses/**the **Mid-Tier independent firms**); and

(ii) A group of small businesses with fewer than ten practices (the **Small Independent Veterinary firms**.

1.7 The appendix is structured as follows:

(a) first, we set out the scope of our profitability analysis, in terms of our coverage of the market for local clinic veterinary services and the time period we have considered;

(b) second, we describe how we have applied the return on capital employed (**ROCE**) methodology in analysing the profitability of the LVGs, taking into account the submissions from parties in response to our Profitability Approach Paper and the information that we have collected;

(c) third, we show the results of our financial and profitability analysis of the LVGs, which we present as ROCE as well as economic profits in monetary terms;

(d) fourth, we provide some views on how we interpret the results of our analysis; and

(e) fifth, we present the results of the financial analysis we carried out on two sets of independent veterinary firms.

2. Scope of our analysis

2.1 In the Profitability Approach Paper, we proposed to carry out financial analysis on:

(a) The six largest LVGs, which have an estimated combined market share of first opinion practices (**FOPs**) of almost 60%;

(b) A sample of 50 Small Independent Veterinary firms in the remaining 40% of the market, which is composed of small veterinary practices, and some larger independent veterinary firms with ten or more practices.[15]

2.2 We then requested further financial data from third parties in order to extend our analysis of the independent veterinary sector. We received a dataset of 157 independent firms, comprising both mid-tier and small independent veterinary firms.

2.3 In terms of the time period for the analysis, we proposed to consider the five most recently completed financial years for LVGs and then as the investigation progressed extended this by one year to include the most recent financial data available during our investigation. The period of review for the independents firms was 2021 to 2023 for the independent firms. We subsequently received a dataset which provided financial data for the years 2021 to 2025.

2.4 We received a range of views from parties in response to our Profitability Approach Paper, which we consider below.

Timeframe

2.5 In the Profitability Approach Paper, we stated that we proposed to gather financial information covering a five-year historical period, which was an expansion from the three years' financial information which we had initially collected from the LVGs.[16]

2.6 IVC stated that a five-year period was still a relatively short period of time in order to address the challenges associated with market fluctuations and the economic cycle; it stated that this was particularly the case given that the time period considered was heavily affected by a number of 'once in a lifetime' events, such as Brexit, the COVID-19 pandemic and the high inflationary period leading to the largest reduction in living standards in the UK since World War II.[17] It

[15] When we published the Profitability Approach Paper, we had identified four Mid-Tier firms. Following publication, we refined our list of independent veterinary businesses and identified a further Mid-Tier firm.
[16] Requested in RFI 6.
[17] IVC response to the profitability approach paper, paragraph 3.23.

acknowledged that, in practice, collecting this data would be burdensome for IVC, particularly given the change in accounting standards during this period.[18]

2.7 Linnaeus told us that it agreed with us that it was necessary to examine profitability over a sufficiently long period to provide a representative picture of profitability, and that in theory, a five-year lookback period was an appropriate time period. It also noted, however, that even using the last five years may not be sufficient to achieve a stable view of the industry profitability going forward given the significant changes seen over this period, and referenced the specific issues we noted in the Profitability Approach Working Paper (the COVID-19 pandemic, increased labour costs).[19] [✂].[20]

2.8 Medivet told us that two additional years of financial information were not representative due to the impact of the COVID-19 pandemic and its associated restrictions which heavily distorted both demand and the ability to supply veterinary services. Medivet also cited [✂] in supplying an additional two years of data and [✂], and told us that the CMA should not place any weight on results derived from any such data.[21]

2.9 Pets at Home told us that it had concerns about the incremental benefit of collecting a further two years of financial information because it did not cover the full life cycle of a FOP.[22]

2.10 VetPartners told us that it might not be feasible to provide data for the two earlier years on a comparable basis with the later three years. It also told us that the COVID-19 pandemic took place in the time period in which we proposed to focus; this had long-term impacts due to the spike in pet ownership, which increased demand in the post-pandemic years, and which continues to affect demand, as puppies and other young animals purchased during the pandemic moved into a stage of their lives that typically required less intervention. VetPartners also told us that, although we had acknowledged the recent disruption, it was concerned that using the time period proposed by the CMA would not provide an accurate picture of profitability due to these factors; the expected fall in revenues as the post-covid spike in demand ends, combined with higher costs following fiscal changes announced in the government's recent autumn budget might well result in lower industry profitability than has been seen in recent years.[23]

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[18] IVC moved from UK GAAP to IFRS from FY22 onwards. IVC response to the profitability approach paper, paragraph 3.24.
[19] Linnaeus response to the profitability approach paper, paragraph 16.
[20] Linnaeus response to the profitability approach paper, paragraph 15
[21] Medivet response to the profitability approach paper, paragraphs 7-10. [✂].
[22] Pets at Home response to the profitability approach paper, paragraph 3.6.
[23] VetPartners response to the profitability approach paper, . VetPartners told us that the pandemic surge in demand for dogs resulted in [✂]; post-pandemic the number of new dogs declined, returning to pre-covid levels. [✂].

CMA assessment

2.11 We considered the views which have been put to us on the timeframe of our analysis.

2.12 We considered that it would not be appropriate to look further back than five years, for two reasons. First, we thought it would be very difficult to obtain the necessary data to carry out that examination without placing a disproportionate burden on parties. Second, we did not think looking back further than five years would show a representative picture of the LVGs' businesses as they had grown significantly (whether by acquisition or organically) over the last five years.

2.13 We also considered whether looking back as far as five years was too long a time period in the context of COVID distortions. We noted that the earliest year in the five-year time period covered some trading pre-COVID: for example Medivet's financial year ending 30 April 2020 covered ten months of trading pre-COVID, and CVS and VetPartners' financial year ending 30 June 2020 covered eight months of trading pre-COVID. We decided that, although some of the additional two years' financial information we had requested covered some of the pandemic conditions for some of the LVGs, it was nonetheless important to examine as long a time period as possible.

2.14 We therefore considered that five years was an appropriate period over which to understand the profitability of veterinary services, with a focus on the post-pandemic years 2023 and 2024. The results indicated for some LVGs that they might be experiencing a decline in profitability in 2023 and 2024 from the peak in around 2021 and 2022 in the wake of the post Covid pandemic boom in pet ownership. In the light of the submissions received with regards to that then apparent trend in profitability for some LVGs, we extended the ROCE analysis for all LVGs to include the most recent reporting period ending in the 2025 calendar year. Inclusion of the FY2025 results enables us to take into account any significant recent changes to ROCE that would affect our assessment of whether profitability was persistent in the case of each LVG.

2.15 We however did not update our cost of capital analysis (assessed as being 9.0% per year (mid-point) throughout the 5 year period to FY2024) to match this extra year of analysis of ROCE. We therefore present 6 years of ROCE but for the purposes of comparing a measure of average ROCE over a multi-year period we compare the 5 year period average to FY 2024 with our cost of capital covering the same period.

2.16 With regards to the independent firms, the proposed timeframe of 2021 to 2023 for the CMA dataset was based on the years in which complete data was available for the responsive set of firms. For the third-party dataset received, the data covers the years 2021 to 2025 however the number of observations per year varies. As

the dataset is much larger than the sample of firms we obtained ourselves, we considered that the variation between the number of observations per year to be of limited significance.[24]

Level of disaggregation

2.17 In our Profitability Approach Paper we stated that we proposed to assess the profitability of the veterinary services operations of each LVG, without seeking to (i) exclude revenues and costs from farm/equine services, or (ii) assess separately the economic profitability of the different types of veterinary services. We said that this was due to the following:

(a) the ways the LVGs have told us they segment their businesses and record balance sheet information;

(b) that in some cases it is not possible to separate each of the in-scope activities of each LVG; and

(c) the considerable complexity involved in reliably separating such activities even in cases where it may be possible.

2.18 CVS told us that it saw the logic in our approach of focussing our analysis at the level of UK veterinary services (including not only small animal FOPs, but also farm/equine practices and out-of-hours services (**OOH**), as well as referral centres, diagnostic laboratories, and crematoria) given data availability, and particularly the challenges of meaningfully allocating capital across these activities. However, it noted that it would limit the extent to which profitability could be meaningfully compared across firms.[25]

2.19 IVC told us that it disagreed with the CMA's proposal to assess the profitability of all of the veterinary services for each LVG in aggregate. Instead, it considered it reasonable to assess profitability of LVGs' clinical veterinary services in aggregate (ie combining FOP, referral centres and OOH), but non-clinical veterinary services must be excluded from this.[26]

2.20 IVC told us that it was necessary to distinguish between clinical veterinary services and non-clinical veterinary services and exclude non-clinical veterinary services from our economic profitability analysis because:

(a) these were fundamentally different businesses to clinical veterinary service, with different assets, cost structures and supply and demand characteristics. It gave the example of online pharmacy, which was a retail business, where

[24] The number of observations are as follows: 67 in 2021; 91 in 2022; 106 in 2023; 115 in 2024; 94 in 2025.
[25] CVS response to the profitability approach paper, Annex, paragraph 1.2a).
[26] IVC response to the profitability approach paper, paragraph 3.4.

the main physical asset was the warehouse and there were very few intangible assets; and stated that clinical services in contrast required specialist premises and equipment and relied heavily on intangible assets; IVC's crematoria business predominantly served B2B customers, while clinical services were customer facing.

(b) It limited comparability both across LVGs and between LVGs and mid-tier firms and independent veterinary firms, and to ensure comparability, profitability should be assessed based on activities which were most common across the sector. The LVGs were active in different ways across non-clinical services.

(c) It would make interpretation of the economic profitability analysis very challenging and was unlikely to meaningfully assist the CMA in its diagnosis of the market, because one aggregate profitability figure would not tell the CMA about where competition was or was not working.[27]

2.21 IVC also told us it was more straightforward to split out non-clinical veterinary services, both from an economic perspective (because the assets were distinct and standalone) and from an accounting perspective (reflecting on how many of the LVGs currently reported on their businesses). IVC told us that it reported separately on its pet crematoria business (separate P&L and balance sheet); IVC's online pharmacy had a separate P&L, and while there were some shared central costs and no separate balance sheet, it would be possible to make sensible and pragmatic assumptions to address this.[28]

2.22 IVC told us that, accordingly, with sensible assumptions it was practical to separate out non-clinical services to a sufficient degree of confidence, and it was important to do so given the risks associated with not doing so; and by contrast, attempting to distinguish and separate out activities within clinical services was highly complex, and economically inappropriate.

2.23 Linnaeus told us that it broadly agreed with the CMA's proposed scope for our profitability assessment, and in particular agreed that, given the limitations of the data available, the complexities of separating out the various in-scope activities, and the difficulty of comparing these across the various LVGs and independent veterinary services practices, it was likely not feasible to assess the economic profitability of the different types of veterinary services. However, Linnaeus noted that in order to ensure the robustness of the analysis it would be advisable for certain activities, namely pet cremation services and the online pharmacies to be removed from the overall results for veterinary services to the extent possible. It stated that while these were not provided by Linnaeus itself, it considered that

[27] IVC response to the profitability approach paper, paragraph 3.5-3.10.
[28] IVC response to the profitability approach paper, paragraph 3.8

these activities were likely to have a significantly different business model, with different cost and profitability structures, and therefore risked skewing the overall profitability results for the market.[29]

2.24 Medivet agreed that it would be excessively time consuming and complex to attempt to segment the LVGs' businesses into different lines of business for which Medivet's management accounts and internal reporting did not already offer such segmentation. Medivet told us that it segmented its business into [✂].[30]

2.25 Medivet told us that while assessing profitability at the group level would be appropriate for Medivet – given that the vast majority of its business was FOP – this was not necessarily the case for other LVGs, who offered services such as pet cremation and online pharmacy services, and Medivet considered that the CMA should adjust its approach to separate at least these services to prevent any distortions to profitability assessments.[31]

2.26 Medivet told us that further segmentation would not be reflective of the realities of the industry. It gave the example of regulation requiring FOP practices to arrange for OOH services of their patients, although this might be from the same clinics that offer FOP services; therefore, FOP and OOH should not be considered separately.[32]

2.27 Pets at Home told us that, given the complexities of analysing FOP markets, Pets at Home was concerned about our proposal to aggregate FOP activities with other veterinary services provided by the LVGs. Pets at Home told us that it understood our concerns about the challenges of allocating costs and capital within the LVGs, but that looking at economic profitability in LVGs in aggregate would deliver distorted and unreliable results for the FOPs segment of the market in which most vets operate. It cited examples of entry barriers, capital requirements, and competitive dynamics for FOPs which were fundamentally different to those of other veterinary services such as specialist animal hospitals and referral centres, OOH provision, and cremation service provision, and these differences would mean that looking at the aggregate profitability of a LVG would reveal little about the dynamics of the FOP market. Pets at Home's view was that this approach risked the CMA not being able to diagnose where problems (if any) in the sector were actually being caused, and saw a significant risk that frontline FOPs might be unfairly caught up in discussions of excessive profitability because of inflated profits in activities which these frontline vets did not themselves provide.[33]

[29] Linnaeus response to the profitability approach paper, paragraphs 13-14.
[30] [✂], paragraph 13-15.
[31] Medivet response to the profitability approach paper, paragraphs 16-17.
[32] Medivet response to the profitability approach paper, paragraph 21.
[33] Pets at Home response to the profitability approach paper, paragraphs 2.3, 2.4, 2.5.

2.28 Pets at Home told us that an approach of aggregating financial data across various veterinary segments operated by LVGs presented significant challenges in accurately assessing the profitability of frontline FOPs.[34]

2.29 It told us that the aggregation of financial data from various veterinary service segments into a single profitability metric obscured the distinct economic characteristics of each segment, which would impede the CMA's ability to identify any specific areas of concern within the veterinary sector, potentially leading to misguided conclusions about the competition dynamics and profitability drivers in the market.[35]

2.30 It also told us that the inclusion of potentially high-margin segments alongside FOPs might inadvertently inflate the perceived profitability of FOPs; segments such as OOH services or referral centres often operated with different cost structures and profit margins compared to FOPs; by not disaggregating these segments, we risked presenting a distorted and biased view of FOP profitability, which did not accurately reflect the operational realities faced by frontline FOPs.[36]

2.31 Pets at Home told us that in the first instance, a segmented profitability analysis that isolated the financial performance of individual business activities within FOPs was necessary and preferable; if this was not feasible, an alternative might be to collect information from specific upstream providers (for example, pet cremation service suppliers) that were not affiliated with the LVGs; in that instance, we should pay close attention to its segment margin analyses and be cautious in interpreting or communicating the LVGs' overall economic profitability results (and any resulting customer detriment) as reflective of FOPs excessively charging frontline customers.[37]

CMA assessment

2.32 We considered the views which had been put to us on the level of disaggregation and thought there were two issues to consider. The first related to the veterinary services provided by the LVGs, and the second related to the type of animal receiving the veterinary services.

(a) First, we agreed with the LVGs that it would be time-consuming and complex to attempt to segment their businesses into different lines of business where segmentation did not already exist, and agreed that we should assess the profitability of LVGs' clinical veterinary services in aggregate (ie combining all their clinical operations whether carried out in a FOP or a referral centre, but excluding any non-clinical veterinary services. The LVGs told us that they

[34] Pets at Home response to the profitability approach paper, paragraph 3.7.
[35] Pets at Home response to the profitability approach paper, paragraph 3.8.
[36] Pets at Home response to the profitability approach paper, paragraph 3.9.
[37] Pets at Home response to the profitability approach paper, paragraph 3.10.

were able to provide this level of disaggregation to exclude non-clinical activities. We were also able to break out the OOH services provided by IVC's Vets Now business (profit and loss statement only[38]) and the referral centre services of Linnaeus from these LVGs' UK clinical veterinary services.

(b) Second, regarding the type of animal receiving the veterinary services, none of the LVGs disagreed with our approach we set out in the Profitability Approach Paper of not disaggregating the revenues, costs and assets relating to veterinary services provided to household pets, from those relating to farm, equine and mixed practices (ie combining all their clinical operations including those relating to farm, equine and mixed practices where relevant).[39] Accordingly, the analysis we present later in this appendix includes veterinary services provided to farm/equine by the LVGs to varying degrees.

2.33 Given the distribution of revenues across different types of sites as shown in Table 2.3 (Breakdown of UK clinical veterinary revenues for each LVG), had the affected LVGs been able to reliably separate out their small animal FOP services from their other clinical activities, it is unlikely that our profitability results would have been materially different.

[38] Please see Notes on preparation of adjusted financial information for Vets Now (paragraphs 1.48 to 1.57) in the annex to this appendix to explain why we didn't also produce a balance sheet for IVC's Vets Now business.
[39] Please see the Table 2.3 Breakdown of UK clinical veterinary revenues for each LVG in Part A: section 2 at paragraph 2.44 where we give an indication of the materiality of these non-household pet services and also IVC's Vets Now OOH operations to each LVG's total UK clinical activity.

3. ROCE analysis for the LVGs

Approach to ROCE analysis

3.1 We set out the overarching conceptual approach to return on capital employed (**ROCE**) in our Profitability Approach Paper.

3.2 ROCE is calculated as earnings before interest and tax (**EBIT**) from clinical veterinary services as a percentage of the capital employed by the LVGs to provide clinical veterinary services.

3.3 As set out in section 4 of the Profitability Approach Paper, we are guided by the following principles in carrying out our analysis:

(a) Return on capital employed compared with the weighted average cost of capital (**WACC**) is our primary means of measuring profitability.[40]

(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 clinical veterinary 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 profit and loss and the balance sheets for the operating units of the firms that undertake the relevant activities, and then make adjustments to arrive at an economically meaningful measure of profitability.

(d) Where a firm undertakes other business activities in addition to those which we are reviewing in the market investigation, we require a share of common cost and assets to be allocated to those businesses under analysis.

3.4 As noted in the Profitability Approach Paper, 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 net replacement cost of the asset in its condition at the relevant balance sheet dates.

[40] 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 using the ROCE framework, we may also consider it relevant to calculate economic profits and economic profits/cost-plus as alternative points of comparison across firms which may have different capital structures. Fundamentally, these represent the same approach but allow data to be presented in different ways.

3.5 We assessed the financial information and considered the submissions and responses to our requests for information on the adjustments necessary to update the LVGs' financial information to reflect replacement cost.

Identification and valuation of capital employed

3.6 This subsection sets out our approach to:

(a) identification of the operating capital employed required to provide clinical veterinary services; and

(b) valuation of those assets.

3.7 The main categories of assets and liabilities recorded on the balance sheets of the veterinary services businesses are:

(a) tangible fixed assets, such as leasehold and freehold properties, refurbishment/fit-outs, diagnostic and operating equipment, and vehicles;

(b) intangible fixed assets, such as goodwill, brand/trade names, customer lists and software;

(c) working capital, which comprises operating current assets such as inventory (including medicines and prescription drugs), trade debtors, other debtors and VAT, and operating current liabilities such as trade creditors and other creditors;

(d) other current assets such as cash;

(e) other current liabilities such as intercompany balances; and

(f) operating provisions.

3.8 This subsection proceeds as follows:

(a) We first examine tangible fixed assets.

(i) We consider freehold property, leasehold property, refurbishment/fit-outs, and diagnostic and operating equipment, vehicles and working capital.

(ii) In respect of refurbishment/fit-outs, and diagnostic and operating equipment, we discuss various alternatives to accounting values as a means of estimating VTB: second-hand valuations, insurance valuations, and recent costs of fitting out greenfield practices.

(b) We then consider intangible fixed assets. We assess the value of customer relationships, the workforce and software assets, and explain why we have

excluded from our analysis other categories of intangible fixed assets put forward by the LVGs.

Tangible fixed assets

3.9 Most tangible fixed assets tend to be valued on the balance sheet at historic cost less any depreciation charged against the asset over its useful life. This is known as the net book value (**NBV**) of the asset.

The appropriateness of accounting NBVs in determining the economic value of assets

3.10 We asked the LVGs to confirm whether the NBV was a good approximation for the cost of replacing assets, and if it was not, to provide an explanation as to why this was not the case and an estimate of the replacement cost of that asset, with supporting evidence.[41]

3.11 The LVGs told us that the NBVs on the balance sheet were unlikely to be representative of the economic value of the assets used in their veterinary business, due to the following:

(a) The NBV of the tangible fixed assets on the balance sheet was likely to significantly understate their value to the business on an economic basis.

(b) A significant portion of tangible fixed assets were not recognised on the balance sheet and hence the omission of these would result in the economic capital being understated.

3.12 All LVGs told us that the accounting life of their tangible fixed assets was significantly less than their economic life.[42] Many LVGs also noted that they had some tangible fixed assets still in use in their business that had a book value of zero or close to zero.[43] In most LVGs' view the main reason why assets had a lower value for accounting purposes was due to accounting policies being very conservative resulting in assets being depreciated well below their current economic value.[44] [✂].[45] [✂] also noted that inflation and supply chains impacted the replacement values of tangible fixed assets and the impact of these were not reflected in accounting values.[46]

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[41] See Questions 1 and 2 of the CMA's s174 request of 23rd of September 2024.
[42] [✂] para 1.14, [✂], paragraph 25 and [✂] response to the profitability approach paper, [✂], paragraph 5, [✂] [✂] response to the profitability approach paper, Annex, [✂], page 11, [✂] response to the profitability approach paper, [✂] page 11 and [✂] response to the CMA s.174 Notice RFI 7 of [✂] para 1.1 page 3-4, [✂].
[43] [✂] and [✂], page 1, [✂] 11.
[44] [✂] response to the profitability approach paper, [✂], paragraph 38, [✂].
[45] [✂] response to the profitability approach paper, [✂], paragraphs 38 and 40, [✂].
[46] [✂] response to RFI 7 [✂] para 1.1 page 3. [✂].

3.13 [✂] noted that the maximum accounting life for its tangible fixed assets (excluding property and leasehold improvements) was five years whereas many of these assets had useful economic lives ranging from seven to 15 years.[47] It also stated that it had 26 clinics where the total NBV of the tangible fixed assets on the balance sheet was less than £1.[48] [✂] told us that 78% of assets on the fixed asset register still in use in FOPs had been fully depreciated from an accounting perspective.[49]

3.14 In respect of assets not being included in the accounts, some LVGs told us that many of the smaller practices they had acquired had not fully recorded all their assets on the fixed asset register and hence they were not included within the tangible fixed asset values in the accounts.[50] Some LVGs told us that from an accounting perspective these assets were instead included as goodwill on acquisition. This resulted in the value of goodwill being higher and tangible fixed assets lower in the accounts than would have been the case had the assets been properly identified.[51] [✂] told us while many of the tangible fixed assets would be physically checked during the due diligence process for these acquisitions, a full examination of the fixed asset register was not undertaken as the businesses were valued by reference to profitability metrics and not on an asset basis.[52]

3.15 [✂] provided an analysis of a sample of clinics which showed more than half (by number as opposed to value) of tangible fixed assets had not been recorded in the fixed asset register.[53] It also provided analysis showing a wide variation in the number of assets recorded in the fixed asset register in each clinic with some clinics having a very low number.[54] [✂] view was that generally it was tangible fixed assets of a small or medium value that were missing and while the individual values were relatively small, the cumulative effect was significant.[55] In support of this it provided internal analysis of a physical verification of assets in a sample of clinics showing some high value items missing but also a large volume of medium and low value items absent.[56]

CMA assessment

3.16 We considered that, for a large majority of the tangible fixed assets, the NBV of these assets in the accounts was unlikely to be representative of their replacement value, for the reasons submitted by the LVGs. We therefore considered various alternatives to accounting values as a means of estimating VTB, and we set out

[47] [✂] Economic Profitability Analysis' submission [✂].
[48] [✂] Economic Profitability Analysis' submission [✂].
[49] [✂] Response to RFI7 para 1.21. [✂].
[50] [✂] Economic Profitability Analysis' submission [✂] and [✂], page 11, [✂].
[51] [✂] response to the profitability approach paper, [✂], paragraph 51, [✂], [✂] and [✂].
[52] [✂] Economic Profitability Analysis' submission [✂] 14. [✂].
[53] [✂].
[54] [✂].
[55] [✂].
[56] [✂].

these alternatives in the following sections for each category of tangible fixed asset.

3.17 In considering potential adjustments to accounting values as a means of estimating VTB, we were mindful of only making adjustments to financial information supplied to us where it was likely to make a material difference to our assessment (as stated in our Profitability Approach Paper).

Freehold property

3.18 As most LVGs' clinics are based in leasehold properties there are only a small number of freehold properties used in the provision of veterinary services by LVGs. [✂] has the most freehold properties with 14 (representing 3.5% of its total estate (in terms of clinic numbers) in 2024 with a NBV of £19.4 million in 2024),[57] [✂] has 13 (3.0% of its estate with a 2024 NBV of £4.4 million),[58] [✂] has three (1.5% of its total estate with a NBV of £6.3 million),[59] [✂] and [✂] have one[60] (0.02% (2024 NBV £0.4 million) and 0.02% (NBV 2024 £0.15 million) respectively) and [✂] has none.[61]

3.19 The LVGs told us that freehold property was likely to be significantly undervalued on the balance sheet as it was recorded at its historical rather than current value, and that these valuations should be adjusted to reflect market value.[62] [✂] provided specific examples of freehold properties within its estate whose value was significantly below recent reinstatement estimates.[63] [✂] suggested such revaluations were most practically done through property agents.[64] In their response to our Profitability Working Paper both CVS and Linnaeus stated that by not revaluing freehold property their assets would be undervalued.[65] [✂], however, also acknowledged that the revaluation of these assets would only make a 'small difference'.[66] [✂] subsequently reiterated this point.[67]

CMA assessment

3.20 We noted a very small proportion of properties in the LVGs' portfolios were freehold. Furthermore, we note that [✂], who have the most freehold properties, stated that any revaluation would only have a minor impact. We therefore consider

[57] [✂] response to RFI. [✂].
[58] [✂].
[59] [✂] response to the CMA's s174 request paragraph 31.6 and footnote 12. [✂].
[60] [✂] response to the CMA's RFI request [✂] at page 24. [✂] and [✂] Response to RFI 13 of [✂] at pages 28. [✂].
[61][✂].
[62] [✂] response to the profitability approach paper, [✂], paragraph 38, [✂] 38 and [✂] response to the profitability approach paper, Annex, [✂], page 13, [✂].
[63] [✂] response to the profitability approach paper, [✂], paragraph 44, [✂] 44.
[64] [✂] response to the profitability approach paper, Annex, [✂], page 13, [✂].
[65] CRA Response on behalf of CVS to the Profitability Working Paper of [✂] page 12, [✂], Linnaeus response to the Profitability Working Paper Page 2, [✂].
[66] [✂] to the Profitability Working Paper of [✂] 12, [✂].
[67][✂] response to the PDR Annex 2, page 8.

that any adjustment we could make to the value of freehold property to reflect replacement value would not make a material difference to our assessment. We therefore did not adjust the NBVs of the LVGs' freehold properties.

Leasehold Property

3.21 The vast majority of LVG veterinary clinics operate from leasehold properties. Most LVGs told us that these properties were treated as right of use assets and capitalised under IFRS 16 on their balance sheet.[68]

3.22 IFRS 16 specifies how an entity will recognise, measure, present and disclose leases.[69] The standard requires lessees to recognise assets and liabilities for all leases unless the lease term is 12 months or less, or the underlying asset has a low value. The standard specifies that future contractual lease payments are discounted back to their current value using the entity's relevant incremental borrowing rate. By treating lease payments under IFRS 16, the LVGs will have recognised the current value of future contractual right of use property lease payments as an asset.

3.23 [✂] told us that while all leasehold assets were now treated as right of use and capitalised, it only formally adopted IFRS 16 between financial years 2021 and 2022. Prior to this the rental payments were treated as an expense in the profit and loss account and therefore not capitalised on the balance sheet. However, it also told us that it had restated its accounts for financial years 2020 and 2021 to show leasehold assets capitalised for comparison purposes.[70] Linnaeus told us that all leasehold assets were now capitalised as right of use assets and that it could provide estimates for the financial years 2020 and 2021.[71] Medivet stated that all its tangible fixed assets under leases were currently treated as right of use assets and capitalised under IFRS 16.[72]

3.24 [✂] told us that it had [✂] of leased property assets:

(a) [✂] leases in which the premises were used for veterinary services and the lease asset was capitalised under IFRS 16;

(b) [✂]; and

(c) [✂].[73]

[68] [✂] Response to RFI 13 dated [✂] at paragraph 62, [✂].
[69] See https://www.ifrs.org/issued-standards/list-of-standards/ifrs-16-leases/ for full details of the standard.
[70] [✂].
[71] Linnaeus response to RFI 13.
[72] Medivet response to RFI 13 at page 23.
[73] [✂] response to s.174 notice RFI 13 at paragraph 31.2.

3.25 We note that while [✂].[74]

3.26 Pets at Home told us that the total store lease (including the area for retail activities) for in-store FOPs and the leases for group owned FOPs were capitalised in the group accounts under IFRS 16. However, for standalone FOPs which are Joint Ventures (whereby the FOP is jointly owned by Pets at Home and a separate entity) the lease was not capitalised, as these entities were not consolidated in the group accounts and therefore the leases were not required to be capitalised under the accounting standards that apply to these entities.[75] However, Pets at Home told us that it could calculate proxy IFRS 16 values for those assets by calculating a capitalised figure for 2024 with an adjustment to the rental charge to arrive at the corresponding right of use asset depreciation charge. It told us that this would be accurate for all leases except a relatively small number that had been renewed during the period. It also suggested that the value of its store leases capitalised in its group financial statements could be pro-rated between its retail activities and its FOPs on the basis of floor space.[76]

3.27 We set out our intention to capitalise operating leases for leasehold properties in the profitability approach paper and most LVGs welcomed this.[77] CVS stated that the value of these leases under IFRS 16 was a reasonable approximation to replacement cost.[78] Some LVGs, however, raised the following concerns as to the appropriateness of IFRS 16 to calculate the value of these assets.

(a) [✂] told us that even when leasehold assets were capitalised there was still likely to be a significant variation in ROCE when compared to FOPs which operate from their own freehold property. It noted that under IFRS 16 only the remaining lease period was included despite the FOPs often leasing the property indefinitely. In its view this would result in a much lower capital asset being included compared to the value of any freehold property.[79] Pets at Home told us that as IFRS 16 asset valuations were calculated by reference to the remaining duration of the lease, this might unduly favour newer FOPs, because newer FOPs were at the beginning of longer lease agreements whereas older FOPs would be either part way through their original lease (and hence have a shorter duration remaining) or have moved to shorter rolling lease agreements.[80]

(b) [✂] stated that as some leases may either not be subject to rent reviews or rent reviews that happen every two-five years, the rental values on which the

[74] [✂].
[75] Pets at Home Response RFI 13 at pages 24-25.
[76] Pets at Home Response RFI 13 at pages 25.
[77] See CMA's Working paper on Profitability at para 4.47, Pets at Home response to the profitability approach paper, paragraph 3.27, [✂].
[78] CVS response to the profitability approach paper, Annex, page 13, [✂].
[79] [✂].
[80] Pets at Home response to the profitability approach paper, paragraph 3.27, [✂].

IFRS 16 capitalised assets were based may be significantly lower than current market rates and hence the IFRS 16 values would not reflect the true replacement costs.[81] VetPartners also stated that for right of use assets such as leasehold properties, the replacement costs of these assets were likely to be higher due to current market rental rates being higher[82] with [✂] also noting contractual lease payments were likely to be lower than current market rates.[83]

(c) [✂] told us that leasehold properties which were impaired and had a capitalised value of zero (that is, properties which were currently vacant but for which rental payments were still made) should be included using the same IFRS 16 calculations applied to unimpaired assets. It told us that these properties continued to be part of its portfolio and part of the economic capital employed in its veterinary business[84] and to exclude them would result in survivor bias in recognising only the assets of successful practices.[85] [✂] reiterated this point in its response to the working paper itself.[86]

(d) In its response to our Profitability Working Paper, [✂] stated that the remaining lease term through which the leasehold asset was calculated under IFRS 16 was arbitrary and the economic reality was that it would be required to operate from the property in perpetuity.[87] It noted that there was some divergence in the leasehold asset/revenue ratios amongst the LVGs despite all LVGs operating largely from leasehold premises.[88] As an alternative it proposed calculating the value of leasehold properties by reference to the historic cost per square foot of freehold property extrapolated across the leasehold estate.[89]

(e) In contrast CVS told us that it saw the use of IFRS16 values as uncontroversial as that approach would give a reasonable approximation to replacement cost.[90]

CMA assessment

3.28 We considered the submissions from the LVGs in the context of the appropriate valuation to be included in our profitability assessment in respect of leasehold properties.

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[81] [✂].
[82] VetPartners response to the s.174 Notice RFI 7 of 23.09.24 para 1.1 page 3. [✂].
[83] [✂], response to CMA Econometrics and Profitability Working Paper, page 30. [✂]
[84] [✂] Response to RFI7 para 1.16. [✂].
[85] [✂] to RFI7 para 1.16. [✂].
[86] [✂] response to the financial analysis and profitability working paper, page 3 and paragraph 2.2.
[87] [✂].
[88] [✂].
[89] [✂].
[90] [✂] to the financial analysis and profitability working paper, paragraph 2.3.3.

3.29 We considered that leasehold properties should be valued based on the approach under IFRS 16 for the purposes of our profitability analysis. We therefore asked the LVGs to provide us with the values of their leasehold property portfolio for each financial year using the approach under IFRS 16.[91]

3.30 We note the following:

(a) We did not take any account of potential additional rental periods which are not recognised under IFRS 16 methodology as we considered these to be too uncertain.

(b) We did not adjust the value of the right of use assets and associated depreciation charge (which are derived from, among other things, the value of the agreed contractual rental payments) to reflect the current market rate. We considered that the rental rates were set by both parties reflecting an expected market rate for the duration of the whole lease, not at the beginning of the lease.

(c) We did not add back the values of leases which had been impaired (and thus written off). Impaired leases relate to vacant properties, which by their nature are not required in the business, and as we were concerned with estimating a replacement cost for only those leasehold properties required, we did not add back the values of any leases which had been impaired. We instead reflected the amounts written off on right of use assets in the period in which these leased assets were impaired.

(d) We did not adopt [✂] suggestion of an alternative method of valuing leasehold properties by reference to the accounting values of freehold properties. As set out above, the accounting values of freehold properties may not necessarily reflect their economic value. We also note that LVGs could choose a business model in which they operate from wholly owned properties rather than the current model in which they operate from leasehold properties. We consider that they chose the latter in part because in their view it is more suited to the needs of their businesses, enabling some degree of flexibility as to choice of premises and less initial capital outlay (although in some instances we also appreciate from a practical perspective there may also be more suitable rental properties available). From a capital perspective, LVGs are only obliged to pay the contractual value of the lease rather than the full value of the property. In our view therefore to equate the value of leasehold properties to freehold properties would significantly overstate the capital employed in the business and would not reflect the business models employed by the LVGs nor reflect the assets they have.

[91] RFIs 12 and 13.

(e) [✂][92] suggested that we should assume within our analysis that LVGs owned rather than leased their properties because they would continue to need to occupy such premises into the future. While this intention may well be the case, the value of their investment in leasehold properties properly should only reflect the extent of their commitment at the balance sheet date to leasing such properties in future. To account for these assets as they were freehold properties would reflect a commitment that the LVGs have not in fact made and as a result overstate the extent of their investment.

(f) We refute any suggestion of survivorship bias in our analysis. We included within the analysis all the additional costs and impairments associated with clinic closures incurred by the LVGs over the period of review. According to information provided to us by the LVGs for the purposes of estimating intangible asset values, they closed 345[93] of their clinics during this period. In relation to Pets at Home, the LVG who raised this point as a particular issue, it closed 34[94] of its clinics in FY2020 as part of its Project Light and the impact on operating profits was fully reflected within our analysis of its profitability for that year.[95]

Refurbishment/fit-outs, and diagnostic and operating equipment

3.31 The LVGs provided views on the valuation of these assets, including their submissions on the appropriateness of various alternatives to accounting values as a means of estimating VTB, as follows:

(a) second-hand valuations;

(b) insurance valuations; and

(c) recent costs of fitting out greenfield practices.

Second-hand valuations

3.32 Four of the LVGs told us that replacement values of assets were unlikely to be derived from valuations in the secondary market as there was no liquid and comprehensive second-hand market for veterinary equipment.[96] Both [✂] and [✂] stated that they did not sell or buy equipment on the secondary market in any material volumes[97] and VetPartners stated the purchase of sophisticated equipment second-hand could risk pet welfare.[98] [✂] noted that its insurance

[92] [✂].
[93] [✂].
[94] Pets at Home response to RFI 16 [✂].
[95] For further detail, see 'Notes on preparation of adjusted financial statements for Pets at Home' in the annex to this appendix.
[96] [✂].
[97] [✂] and [✂].
[98] VetPartners response to CMA Profitability Working Paper at para 6.2.

policies were on a ‘new for old’ basis due to the lack of a reliable second-hand market.[99]

Insurance valuations

3.33 Three of the LVGs told us that insurance valuations were unlikely to be suitable proxies for the replacement costs of assets.[100] The reasons for this were primarily due to assets being either undervalued or omitted from insurance values. [✂] told us many of its clinics’ insurance policies were legacy policies from acquisitions which had not been updated and that assets were missing from coverage. In support of this it provided its own internal analysis showing a wide variation in clinic insurance values, some of which it stated were implausibly low.[101] It also told us that, as claims were generally for individual items and not the whole clinic, [✂].[102] CVS told us its insurance [✂].[103] Pets at Home stated its insurance was at the (retail) store, not clinic, level and hence was unsuitable for determining replacement cost.[104] Linnaeus stated that insurance values could be used as proxies for the replacement value of tangible assets [✂][105]. IVC also noted that insurance policies generally provided for new assets so a reduction may have to be applied to reflect the age of the original asset.[106]

Recent costs of fitting out greenfield practices

3.34 Five of the six LVGs suggested using the refurbishment or ‘fit-out’ costs of greenfield practices as a proxy for some tangible fixed asset valuations,[107] by which an average cost per square foot of fitting out greenfield clinics would be calculated and then extrapolated to the whole estate based on the total size of the estate. This would then serve as a proxy for the replacement value of the assets. A reduction would also be applied to reflect the age of the assets to arrive at depreciated replacement cost.[108]

3.35 In terms of scope, [✂] suggested this would be a good ‘starting point’ although it noted that it would exclude motor vehicles and leasehold properties.[109] CVS stated that this would be suitable to determine the values of assets such as leasehold improvements, fixtures and fittings, tools and equipment. It noted other tangible

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[99] [✂].
[100] [✂] Economic Profitability Analysis' submission [✂], [✂], Pets at Home response to the profitability approach paper, paragraph 3.27, [✂] at para 3.27 and CVS response to the profitability approach paper, Annex, page 15. [✂].
[101] [✂].
[102] [✂].
[103][✂] Response to CMA Profitability Working Paper page 15.
[104] Pets at Home response to the profitability approach paper, paragraph 3.27.
[105] Linnaeus response to the profitability approach paper, paragraph 6, [✂].
[106] [✂].
[107] See [✂] Consolidated Response to RFI7 para 1.15, [✂], VetPartners response to the profitability approach paper, paragraph 6.1, [✂].
[108] [✂] and [✂] response to the CMA's Profitability Working Paper para 67 to 70 and [✂]. Consolidated Response to RFI7 para 1.15
[109] [✂].

fixed assets such as leasehold and freehold properties and operating leases would have to be calculated separately.[110] [✂] stated that, as the fit-out costs did not include motor vehicles or IT equipment, these would have to be calculated separately.[111]

3.36 In terms of methodology, some LVGs noted that a distinction should be made between smaller, less complex, clinics which were likely to have a lower fit-out cost per square foot and larger, more complex, clinics which were likely to have a higher cost per square foot, and some noted that there was a difference in cost between more and less recent clinic openings:

(a) [✂] suggested that clinics should be categorised between normal and large (over 12,000 sq feet) with the latter having significantly higher fit-out costs due to their complexity.[112]

(b) Linnaeus noted that the cost per square foot varied between FOPs and referral centres.[113]

(c) Pets at Home also stated that the mix of its recent clinic openings was not reflective of its estate mix as it included a higher proportion of lower cost in-store clinics.[114]

(d) CVS told us that for fit-out costs relating to clinics newly established in the last few years, an inflationary uplift should be applied to reflect the current cost of replacing the assets.[115]

3.37 Many LVGs told us that if asset values were based on the fit-out costs of new clinics then some adjustment would be required to reflect the age and remaining useful life of the assets across their estate, that is, to calculate a depreciated replacement cost.[116] IVC and [✂] suggested a reduction of 50%.[117] [✂] told us that as this assumed that its assets were [✂].[118] IVC, however, subsequently stated in its response to our Profitability Working Paper that while 50% was the most appropriate assumption in the absence of any data it was still unevidenced and uncertain.[119]

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[110] CVS response to the profitability approach paper, Annex, page 11, [✂] Response to CMA Profitability Working Paper page 11 and CVS response to the profitability approach paper, Annex, page 14, [✂] Response to CMA Profitability Working Paper page 14
[111] [✂], paragraph 6.1, [✂] response to CMA Profitability Working Paper at para 6.1
[112] [✂].
[113] Linnaeus response to the CMA's Profitability Working Paper para 68,69
[114] Pets at Home-Consolidated Response to RFI7 [✂] para 1.29
[115] CVS response to the profitability approach paper, Annex, page 14, [✂] Response to CMA Profitability Working Paper page 14.
[116] [✂] and Linnaeus response to the profitability approach paper, paragraph 67 to 70, [✂] response to the CMA's Profitability Working Paper dated para 67 to 70, [✂]. Consolidated Response to RFI7 para 1.15
[117] [✂] and [✂].
[118] [✂].
[119] [✂].

3.38 Pets at Home suggested a lesser reduction in the range of 31% to 39%.[120] This range was based on dividing the average asset life ([✂]) by the estimated range of the economic life of a FOP (20 to 25 years) leads to an estimated range of depreciation of 31-39%.[121] In its response to our Profitability Working Paper where a useful economic life of 16 years was used and a discount factor of 50%, Pets at Home stated that while the 50% discount assumption might be suitable for LVGs whose portfolio was at a steady state, as their portfolio comprised more new clinics a lower discount rate should be applied to them.[122]

3.39 Some other LVGs also stated in their response to our Profitability Working Paper that their estate was likely to have assets that were comparatively younger compared to other LVGs' and hence they should have a lower discount rate applied. [✂] noted that it had significantly increased its refurbishment expenditure from [✂]% of its revenue in the period FY2020 to 2022 to [✂]% of its revenue in period FY2023 to FY2024 which in its view suggested that a lot of its assets were likely to be newer compared to other LVGs'.[123] VetPartners stated that as it was established in 2015, an assumption that the average age of its assets covered by the fit-out methodology is eight years would appear too high.[124] Medivet noted that the assumptions on asset age and useful life were not based on information from it and therefore may not represent Medivet's asset base.[125]

CMA assessment

3.40 We found the LVGs' submissions on the lack of significant second-hand market for replacement assets compelling. We considered that even if such a market did exist, there would still be considerable difficulties in identifying any assets missing from individual LVGs' fixed asset registers across their respective portfolio of clinics before assessing these assets' value in the second-hand market. We did not pursue this avenue of investigation further.

3.41 Similarly, we found the LVGs' submissions on the limitations of the relationship between insurance coverage and the replacement value of the assets compelling, and we did not pursue this avenue of investigation further.

3.42 We considered that using the recent fit-out costs of greenfield clinics as a proxy for refurbishment/fit-outs and diagnostic and operating equipment was the most appropriate approach.

[120] Pets at Home-Consolidated Response to RFI7.
[121] Pets at Home-Consolidated Response to RFI7.
[122] Pets at Home response to the CMA Profitability WP page 17.
[123] [✂] to the financial analysis and profitability working paper.
[124] [✂] to the CMA's Working Paper on profitability analysis.
[125] [✂], response to CMA Econometrics and Profitability Working Paper page 30.

Fit-out methodology

3.43 Broadly, our approach was to analyse the fit-out and equipment costs of the LVGs' greenfield site openings[126] for the last five years and calculate an average replacement value per square foot to fit-out and equip a greenfield site for an LVG. We then extrapolated that value per square foot to each LVG's whole estate based on the total size of that estate and applied a reduction to reflect the extent of depreciation to arrive at a depreciated replacement cost. We set out in more detail each of the steps in this process below.

Data gathering

3.44 First, we asked each of the LVGs for the following information:

(a) the name of each veterinary clinic fitted out in the last five years;[127]

(b) the type of veterinary clinic fitted out (local clinic or referral);

(c) the date the quote was accepted for these works;

(d) the total cost of the fit-out including all leasehold improvements, equipment and fixtures and fittings;

(e) the total size of the area fitted out (in square feet);

(f) the type of fit-out undertaken (greenfield site, full or partial refurbishment of a site or relocation of a site); and

(g) the total size of its current estate for the services included in the profitability analysis in square feet split between local clinics and referral centres.

3.45 As set out above, some LVGs noted that fit-out costs per square foot were likely to vary with the complexity of the clinic. We have therefore calculated a separate cost per square foot for local clinics and referral centres. This reflects the likely increased complexity in referral centres due to their specialisms and potentially higher costs. We then applied these separate figures to the total square footage of the LVGs' local clinics and referral centres respectively to calculate the cost of the replacement assets.

3.46 In terms of the type of site to include in our analysis (as set out above) we initially focused on greenfield sites on the basis that these would require the purchase of all assets required to fit out a clinic. We did not include any fully or partially refurbished, or relocated sites in our dataset, because we did not consider that the

[126] This included the fit-outs of existing (/ relocated) sites for which the nature of the fit-out undertaken, so we were told, was the same as that would have in fact occurred had that site occupied a greenfield location.
[127] We limited the dataset to those sites for which a quote for works was accepted within the last five years.

fit-out and equipment costs of those sites would include all of the assets, which might risk undervaluing the replacement value. For example, while there may be new leasehold improvements and fixtures and fittings included in a relocation, some of the equipment may have been relocated from the previous premises and therefore excluded from the total fit-out costs for that site. We did not include any purely farm or equine sites in our dataset as we noted that not all LVGs provide these services.

3.47 However, we did ask each of the LVGs if any of their refurbishments or relocations would be akin to fitting out a greenfield site, in terms of the extent of spend on leasehold improvements, equipment and fixtures and fittings. CVS told us that only three of its relocation or refurbishment sites were akin to the fit out of a greenfield site.[128] [✂] and IVC told us that none of their relocations or refurbishments were equivalent to the fit-out of a greenfield site. They stated that neither required the same level of investment, as moveable assets were transferred during a relocation and refurbishments generally did not require the same level of structural work.[129] Linnaeus told us that all its fully refurbished sites included costs equivalent to those of a greenfield site.[130] While Pets at Home identified some extensions to existing practices that may be the equivalent of greenfield sites[131] it suggested that we should focus on its list of greenfield sites to understand the fit-out costs of local clinics.[132]

3.48 [✂], most of its new sites within a multi-site practice received a full fit-out with some exceptions.[133] In its response to our working paper, [✂] however noted that its fit-out costs appeared lower than the LVG average.[134] While [✂] acknowledged that it had described these sites as 'full fit-outs',[135] it then stated that most of these sites where either relocations, expansions or the costs of developing sites within multi-site practices. It also stated that in respect of sites which were relocations or expansions, existing assets or resources may have been utilised in its development. In the case of sites developed within multi-practices resources may be shared.[136] In its view this 'may partially explain' why the average cost per square foot of its sites is lower and on this basis it considers that it should be removed from the sample.[137] [✂] also noted that while its sites accounted for 37% of all sites, on a simple average based on the basis of total square footage (on which the average square foot calculation is based) it accounted for 47%.[138]

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[128] CVS response to Question 4 of RFI 16.
[129] IVC response to Question 4 of RFI 16 and [✂].
[130] Linnaeus response to Question 3 of RFI 16.
[131] Pets at Home response to Question 4 of RFI 16.
[132] Pets at Home response to Question 4 of RFI 16.
[133] [✂] response to Question 10 of RFI 16 at paragraph 10.3. [✂].
[134] [✂] to the CMA's Working Paper on profitability analysis page 14. page 14.
[135] [✂] to the CMA's Working Paper on profitability analysis page 14. page 14.
[136] [✂] to the CMA's Working Paper on profitability analysis [✂].
[137] [✂] to the CMA's Working Paper on profitability analysis [✂].
[138] [✂] to the CMA's Working Paper on profitability analysis page 18. [✂].

3.49 We have continued to include [✂] sites in our sample as we note that it initially said that it received a full fit-out. From its submission it does not appear it has specific evidence that would indicate these sites did not receive a full fit-out and rather that its concerns are driven primarily from its average costs per square foot being lower than the LVG average. In this respect we note that its average costs per square foot ([✂] in 2024) are higher than [✂] [✂], the Independent Clinics' (£204) and the sample of [✂]. Moreover, we note that the impact of its removal would be to increase average costs per square foot by 14%, within the range of the sensitivity set out below, where fit-out costs and associated depreciation are increased by 25%.

3.50 Within our dataset we have therefore included the non-greenfield sites characterised as akin to greenfield sites by [✂], [✂] and [✂] in our analysis.

3.51 In addition to the above, two LVGs suggested some greenfield sites may not be fully representative of the costs of fitting out a local clinic or referral centre.

3.52 Pets at Home noted that two greenfield sites (Bracknell and Coalville) were built in retail stores that had previously hosted local clinics and hence did not incur the full fit-out costs.[139] We considered that they may not reflect the full fit-out costs as some leasehold improvements may have previously been undertaken and hence not included in the fit-out costs provided. We therefore removed them from our dataset.

3.53 Linnaeus stated that two of its referral centres were not representative of the costs of fitting out a standard referral centre. One ([✂]) was a single disciplinary site specialising in eye care and hence [✂]. The other [✂].[140] As both these clinics meet the definition of a referral centre (which we note will include a range of clinic sizes and locations) we have included them in our analysis. We note that the net impact of excluding both would be to reduce the weighted cost per square foot used in our calculations for referral centres. CVS told us that one of its local clinics, [✂], also included a teaching facility and hence its cost per square foot was not representative of local clinic. We therefore removed this from our sample.[141]

3.54 Pets at Home told us that for its in-store clinics, the cost of enabling works to the store to accommodate the clinic which were capitalised at the group level in the accounts should be included, because third party operators would incur similar costs in the same manner that concessions in supermarkets operated.[142] Pets at Home noted that there are efficiencies from being located in store, such as more

[139] Pets at Home response to Question 4 of RFI 16 at paragraph 2.1, [✂].
[140] Linnaeus response to RFI 16 at paragraph 3.3. [✂]
[141] CRA Response on behalf of CVS to the Profitability Working Paper page 6. [✂].
[142] Pets at Home Response to RFI7 para 1.34, [✂] and Pets at Home response to the profitability approach paper, paragraph 3.53, [✂].

flexibility over the size of the clinic and also efficiencies from leveraging some of the store estate such as utilities, deliveries and logistics.[143] In Pets at Home's view the CMA should either[144];

(a) include these enabling costs in calculating the average cost per square foot; or

(b) gross up the size of Pets at Home's instore estate to reflect the larger average size of its standalone clinics

3.55 Following these submissions we have added the cost of enabling works to Pets at Home sites in our sample. In our view, as these costs are necessary to access the efficiencies set out above, then they should be included in the cost. In our view this is preferable to adjusting the size of instore clinics to reflect the size of standalone clinics as this would not reflect the reality of their actual operations.

3.56 Following the adjustments set out above our dataset consisted of the following mix of local clinics and referral centres from the LVGs set out in Table 3.1 below.

Table 3.1 Summary of Local Clinics and Referral Centres used in fit-out analysis by LVG

LVG	Number of Local Clinics	Total Square footage of Local Clinics (Sq Ft)	Number of Referral Centres	Total Square footage of Referral Centres (Sq Ft)
CVS	[✂]	[✂]	[✂]	[✂]
Linnaeus	[✂]	[✂]	[✂]	[✂]
Medivet	[✂]	[✂]	[✂]	[✂]
Pets at Home	[✂]	[✂]	[✂]	[✂]
VetPartners	[✂]	[✂]	[✂]	[✂]
IVC	[✂]	[✂]	[✂]	[✂]
Total	28	88,190	7	139,365

Source: CMA analysis based on data provided by the LVGs
Note 1: *[✂]* and *[✂]* and *[✂].*
Note 2: Linnaeus informed us shortly before we published the PDR that we hadn't made an update to the square footage for one of its local clinics used in the sample that it had previously informed us about. We subsequently assessed this update and found that Linnaeus's update made a minimal difference to the cost per square foot we have used to adjust the carrying value of LVGs fit out cost assets. We as a result did not update our model and therefore didn't update this table.

3.57 In their response to our Profitability Working Paper, some LVGs queried the extent to which reliable estimates of their assets could be obtained from this sample size.[145] IVC noted the sample of sites represented less than 1% of total LVG sites and queried the extent to which a sample of this size could be relied on.[146] IVC also raised issues on its reliability on the basis it was a mix of greenfield and

[143] Pets at Home [✂].
[144] Pets at Home [✂].

[145] [✂], [✂], on behalf of Medivet, response to Econometrics and Profitability Working Paper page 30. [✂].
[146] [✂] IVC Technical Response to the CMA's Profitability Working Paper Page 11

refurbished sites and queried whether LVGs would apply a consistent methodology in estimating the size and fit-out costs of the sites included.[147] Medivet stated that the sample only included [✂] Medivet sites which accounted for less than [✂] of its estate and that [✂].[148]

3.58 In our view the estimates provided by this sample are likely to over-estimate the value of the assets covered by this methodology. In calculating economic profitability, it is the most efficient operator we are concerned with not the average. In addition to the sites in the table above we also calculated the average fit out costs per square foot for a further nine independent veterinary firms and also [✂] greenfield sites opened in the last five years by [✂] (an independent veterinary group). These were approximately 38% and [✂] less than the average fit-out costs of the LVGs respectively (more detail on this is provided in the sensitivities section below). Therefore, in our view any asset valuations calculated on the basis of the average costs of this sample are likely to over-estimate the fit-out costs of the LVGs and in turn also overvalue the assets of the LVGs covered by this methodology.

Purchase of further tangible fixed assets following clinic opening

3.59 Pets at Home stated that a further uplift of 25% should be applied to the asset base of greenfield FOPs to reflect the asset base of mature clinics as clinics are normally opened with a 'basic' fit-out and then accumulate further assets and improvements over time. The 25% uplift was based on a comparative analysis of the assets of irs mature and new clinics.[149] This assumed that all assets relating to the initial fit-out (and provided in its submission on fit-out costs of greenfield sites) were included on its fixed asset register within the first three years of opening. It then examined FOPs opened since 2010 to understand the additional assets added after this three-year period. This showed that on average 22% of their assets were added after three years which was equivalent to an additional uplift of 25% of the initial fitout asset value.[150] FOPs opened since 2010 were chosen for this analysis on the basis that they were relatively new and had not started replacing their initial assets.[151]

3.60 We asked the other LVGs if they budgeted for new clinics to acquire additional assets as they matured (other than replacement assets). Each LVG told us that it opened new clinics with a full fit-out and did not budget for additional assets (other than replacement of assets).[152] [✂], however, stated that whilst it opens each site

[147] [✂] IVC Technical Response to the CMA's Profitability Working Paper Page 11. [✂].
[148] [✂], on behalf of Medivet, response to Econometrics and Profitability Working Paper, page 30. [✂].
[149] Pets at Home Response to RFI7 dated 28th para 1.31. [✂].
[150] Pets at Home Response to RFI7 para 1.31. [✂].
[151] Pets at Home Response to RFI7 para 1.31. [✂].
[152] [✂] response to Question 7 of the CMA's RFI 16, [✂], [✂] response to Question 10 of the CMA's RFI 16, [✂] response to Question 7 of the CMA's RFI 16.

with a full fit-out it also budgets for additional assets as the need arises.[153] Given that these practices initially open with a full fit-out, our view is that these assets are more likely to be replacement assets and hence we have not made any adjustment to [✂]'s fit-out costs. We therefore only adjusted Pets at Home sites in the dataset with a 25% uplift of additional assets as the clinic matured.

Adjustments for inflation

3.61 To expand our dataset, and to provide equivalent values as at each balance sheet date, we expanded our set of results to include each year in our five-year period under review by deflating / inflating (as necessary) the fit-out and equipment cost for each clinic within the dataset.

3.62 The first step in this process was to identify the date that most accurately reflected the point in time at which the fit-out costs had been established. We used the date on which the quote was accepted for this, because this would be the point in time at which materials and labour would be priced for the purposes of carrying out the work. We asked each of the LVGs to provide the approximate date the quote was accepted for the fit-out costs for each site.

3.63 [✂][154] and [✂][155] provided the approximate date on which the quote was accepted. [✂] noted it did not systemically record the date the quote was accepted and therefore was unable to provide this. Instead, it provided the date on which the Letter of Intent or Formal Instructions to carry out the work were issued which it stated was the closest date it had to this. [✂].[156] [✂] was unable to provide the approximate date on which the quote was accepted and instead provided the completion date of the work. It noted that quotes were received no less than three months before work commenced.[157] For the [✂] Medivet sites, we were provided with the date of opening as opposed to the date the quote was accepted. In respect of the LVGs from which we did not receive an approximate date on which the quote was accepted ([✂] and [✂]), we have assumed that a quote was accepted one and a half years prior to opening.[158]

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[153] [✂].
[154] [✂].
[155] [✂] response to Question 37 of RFI 13 at paragraph 37.1. [✂].
[156] [✂].
[157] [✂] response to Question 37 of RFI 13 at paragraph 22. [✂].
[158] We note that in Pets at Home's response to Question 7 of the CMA's RFI16 (in which the CMA requested the date that the quote was accepted for the fit-out works) it stated that work commenced six-eight weeks post quote acceptance prior to 2023 and three-six months post 2023. It then suggested that 'one approximate approach would be to apply the longer time lag to the 'New Practice 2019 to 2023' tab and the shorter time lag to the 'New Practice 2023 onwards' tab.' which are found on Annex 10 to the CMA's RFI13. We assume Pets at Home's intended meaning is to apply the shorter time lag to pre-2023 sites on the 'New Practice 2019 to 2023' tab and the longer time lag to the 'New Practice 2023 onwards' tab. In addition, we note that its response to RFI13 at paragraph 37.3 states that the dates on these tabs show the date on which the project was delivered as opposed to started. We have followed Pets at Home's guidance and applied the suggested time lag to those sites on the second tab (we have not adjusted the dates for the six to eight weeks for those sites on the first tab due to its immaterial impact). To the extent that this is based on project delivery dates rather than project starting dates this may result in an incorrect quote date being applied which in turn may

3.64 We then deflated / inflated as necessary the costs per square foot for each greenfield clinic based on the Consumer Price Index (**CPI**).[159] For example, if the quote for a greenfield clinic (the quote being the pricing point we have used for the cost of the fit-out as set out above) was received in March 2022 this would first be inflated using a quarterly inflation measure to provide a calendar year-end value for 2022. This value would then be deflated using CPI to provide an equivalent value for 2020 and 2021 and inflated using CPI to provide an equivalent value for 2023 and 2024. This provided us with inflation-adjusted costs for each of the five calendar years within the scope of our assessment. Then the total average cost per square foot for each calendar year for local clinics and referral centres (calculated as set out below) was adjusted for inflation to reflect the financial year end of each of the LVGs. For example, for Medivet for the calendar year 2024, total average costs per square foot would be adjusted to remove the impact of inflation from May 2024 to December 2024 to reflect its April financial year end.

3.65 For simplicity we used the CPI, and in our Profitability Working Paper we welcomed submissions on the appropriateness of this index. Medivet told us that inflationary pressures on the mix of assets will be impacted by a number of different indexes and that CPI is unlikely to accurately reflect this[160]. CVS, however, modelled the impact of alternative indexes, and in its view using other indexes such as the CPI Index for Veterinary Services, Dental Services CPI and the Medical Services and Product Equipment CPI would make no material difference to our calculations.[161] We therefore have continued to use CPI.

3.66 The full dataset of sites for local clinics and referral centres, including their inflation-adjusted values as at the end of each calendar year are set out in the two tables below.

Table 3.2 Dataset of local clinics showing inflation-adjusted values as at each calendar year end

				Inflationary adjusted fit out cost values at year end (£millions)				
LVG / Site name	**Fit out costs (£m)**	**Date of quote**	**Size (Sq Ft '000)**	**2020**	**2021**	**2022**	**2023**	**2024**
CVS								
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus								

underestimate the inflation to be applied to these costs. Our expectation is that were this the case, then any adjustment to be made as a result is likely to be immaterial.

[159] See CPI ANNUAL RATE 00: ALL ITEMS 2015=100 - Office for National Statistics.

[160] [✂] response to Econometrics and Profitability Working Paper.

[161] [✂] to the Profitability Working Paper of 1st May 2025 page 9. [✂].

[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Medivet								
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home								
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners								
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on data provided by the LVGs.
Note 1: For [✂] the original cost is shown in second column above while the figures for each calendar year are adjusted for both inflation and the 25% uplift in assets.
Note 2: Linnaeus informed us shortly before we published the PDR that we had not made an update to the square footage for one of its local clinics used in the sample ([✂]) that it had previously informed us about. We subsequently assessed this update and found that Linnaeus's update made a minimal difference to the cost per square foot we have used to adjust the carrying value of LVGs fit out cost assets. We as a result have updated this table but did not update the model.

Table 3.3 Dataset of Referral Centres showing inflation-adjusted values as at each calendar year end

				Inflationary adjusted fit out cost values at year end (£m)				
LVG / Site name	**Fit out costs (£m)**	**Date of quote**	**Size (Sq Ft '000)**	**2020**	**2021**	**2022**	**2023**	**2024**
CVS								
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
IVC								
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus								
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on data provided by the LVGs
Note 2: Linnaeus informed us shortly before we published the PDR that we had not made an update to the total costs for one of its referral centres ([✂]) used in the sample that it had previously informed us about. We subsequently assessed this update and found that Linnaeus's update made a minimal difference to the cost per square foot we have used to adjust the carrying value of LVGs fit out cost assets. We as a result have updated total fit out costs within this table but did not update the model.

Calculating average fit-out costs per square foot for local clinics and referral centres

3.67 To calculate an average cost per square foot for each calendar year for local clinics and referral centres we divided the total cost (adjusted for inflation) of all the sites in our dataset in that year by the square footage of all the sites in our dataset. This effectively weights the results by size with larger clinics having a bigger impact on the average than smaller clinics (as opposed to a simple average where all clinics would count equally regardless of size). The two tables below set out the average cost per square foot (weighted by size) for each LVG and the composite figure for all LVGs for local clinics and referral centres.

3.68 We note that in their responses to the Profitability Working Paper two LVGs, [✂] and [✂] told us that we should use an average cost per square foot based only on their clinics.[162] Both noted that their clinics in the sample had a higher cost per square foot than the LVG average and that this, in their view, reflected a higher quality of fit-out.[163] [✂] also told us that the average independent clinic was unlikely to have the same standard of fit-out as [✂] and any lower costs could reflect lower quality rather than efficiencies.[164] Furthermore, in response to the PDR, [✂] submitted that [✂].[165] [✂].[166]

3.69 We recognise that each firm has its own business model, which in turn accommodates variation in the nature and level of fit out across the portfolio of each LVG's clinics. Such an approach does not necessarily imply inefficiencies within any particular business.

3.70 We accept that there are limitations in applying a standard, average level of fit-out cost within our modelling. This means that the averages used may only approximate the fit-out costs of any one individual LVG. However, we took this step to make the analysis tractable. It would not have been feasible for us within the timescale for a market investigation to have done a more granular analysis, given the variation in fit-out across individual clinics within the same LVG and given that there would have been six separate LVGs to analyse (many of which

[162] [✂].
[163] [✂].
[164] [✂].
[165] [✂] response to the PDR, page 6.
[166] [✂] response to the PDR, page 4.

had poor accounting records for their clinics), at an individual LVG level. As a result, we have applied the average cost per square foot of all LVGs including to [✂] and [✂].

Table 3.4 Local clinics fit-out cost per square foot as at each calendar year end

LVG	Number of sites	Total Sq Ft ('000's)	Average cost per Sq Foot (£)				
			2020	2021	2022	2023	2024
CVS	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Medivet	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
All LVGs	28	88.19	268	275	299	321	329

Source: CMA analysis based on LVG data from RFI 13
Note: IVC had no new local clinics built in the period.
Note 2: Linnaeus informed us shortly before we published the PDR that we had not made an update to the square footage for one of its local clinics used in the sample ([✂]) that it had previously informed us about. We subsequently assessed this update and found that Linnaeus's update made a minimal difference to the cost per square foot we have used to adjust the carrying value of LVGs fit out cost assets. We as a result did not update our model and therefore did not update this table.

Table 3.5 Referral centres fit-out cost per square foot as at each calendar year end

LVG	Number of sites	Total Sq FT ('000's)	Average cost per Sq Foot (£)				
			2020	2021	2022	2023	2024
CVS	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
IVC	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
All LVG's	7	139.37	355	364	398	427	437

Source: CMA analysis based on LVG data from RFI 13
Note 1: Pets at Home has no referral centres. [✂] and Medivet had no referral centres built in the period.
Note 2: Linnaeus informed us shortly before we published the PDR that we had not made an update to the total costs for one of its referral centres ([✂]) used in the sample that it had previously informed us about. We subsequently assessed this update and found that Linnaeus's update made a minimal difference to the cost per square foot we have used to adjust the carrying value of LVGs fit out cost assets. We as a result did not update our model and therefore did not update this table..

3.71 In order to calculate the gross replacement cost of the assets we multiplied the weighted average cost per square foot (adjusted to reflect the LVGs' respective financial year ends as set out above) by the total square footage of each LVG's Local Clinic and Referral Centre estate respectively in that year, as set out in the table below. [✂] stated that, as it does not ordinarily record the square footage of its clinics, it had to provide an estimate of its total square footage which in its view was likely to be understated and hence any assets calculated on this basis were likely to be conservative. The main areas it cites as likely to result in underestimations are;

(a) An assumption that clinics open during the period but subsequently closed had a constant square footage with no additions during the period they were open.

(b) Due to a lack of data on [✂] clinics that are now closed but were open during the period, it has had to assume that these sites have the average square footage of sites open in this period.[167]

(c) In addition, it also stated that in its experience square footage may not be recorded on a consistent basis across clinics (with areas such as hallways, staircases and parking spaces possibly accounted for on a different basis).[168]

3.72 In response to this we note that it was for [✂] to provide an estimate of its square footage that in its view most accurately represented the total size of its clinics in each year. To the extent that, in its view, its current methodology understates the size of its clinics we would welcome a revised submission that in its view more accurately reflects the size of its estate. We also note that any assumption using an average square footage for the sites set out above could equally result in an overstatement of the size of its clinics (where they are below average size) as well as an understatement. In relation to the more general point about consistency of reporting we assume that when asked for total clinic size all LVGs have provided the total size of the clinic (inclusive of all relevant areas within the building).

3.73 In response to the PDR, Pets at Home submitted that 'co-location allows Pets at Home's in-store FOPs to operate using an optimised configuration and a smaller footprint. In our analysis of capital employed (using square footage as a key driver of the estimation), this results in a much lower capital employed being estimated compared to a 'standalone' FOP. However, to be clear, Pets at Home considers that it invests substantially in all its FOPs and that FOPs, including in-store FOPs, have state-of-the-art equipment and facilities.[169]

3.74 As we acknowledge above, the use of a common LVG wide fit-out cost per square foot to arrive at current values for each LVG's fit-out tangible fixed assets for its clinics may mean that the averages used only approximate the fit out costs of any one individual LVG. The use of this approach within our modelling leads to the value of capital employed being approximated for each individual LVG. That in turn means that less reliance should be placed on the modelled ROCEs and economic profit figures for any individual LVG than on the figures we have generated for LVGs in total.

[167] [✂].
[168] [✂].
[169] Pets at Home response to the PDR, paragraph 3.4.

Table 3.6 Total Square footage of LVGs

LVG	Total Square Footage (000' Sq Ft)				
	FY20	FY21	FY22	FY23	FY24
CVS					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Total	[✂]	[✂]	[✂]	[✂]	[✂]
IVC					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Total	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Total	[✂]	[✂]	[✂]	[✂]	[✂]
Medivet					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Total	[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Total	[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Total	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on LVG data from RFI 13.
Note: as explained in the notes to the preceding tables, we have not updated Linnaeus' figures for the minor updates to the information for one of its local clinics and one of its referral centres it flagged to us shortly before publication of the PDR.
Note: [✂] was unable to provide figures for 2020 and 2021 we have therefore assumed the same square footage as 2022 for these years

3.75 Finally, to estimate a total depreciated replacement cost for each LVG, we then adjusted the gross replacement cost to reflect the age of the assets across the estate and their remaining useful economic life. As noted above these fit-out and equipment costs comprise a wide range of assets each with varying economic lives, making it difficult to ascertain the average economic life of the group of assets as whole. We noted that IVC and Linnaeus proposed a reduction of 50% while Pets at Home proposed a reduction in the range of 39% to 31%. We decided that a reduction of 50% was appropriate.

3.76 We note the submissions from IVC, VetPartners, Medivet and Pets at Home on the appropriateness of the 50% assumption to their estate.

3.77 In respect of [✂] view that its increased refurbishment expenditure suggests it has younger assets and hence should receive a lower discount factor we note that the increase in its expenditure has only occurred over a few years compared to the estimated economic average life of assets of 16 years. Moreover, one reason for this increased expenditure could be to offset lower investment in previous years or an older estate. In respect of the latter, we note that [✂].

3.78 Furthermore, we note that despite this increased investment four out of the five other LVGs generated more revenue per square foot than [✂] in 2024 so it is unclear the extent to which this additional investment generates increased revenue or efficiencies or addresses previous underinvestment. We therefore do not propose adjusting the 50% for [✂].

3.79 In relation to VetPartners' view that as it was only founded in 2015 the 50% discount would appear inappropriate to it, we note that of more relevance is the date on which their clinics were established. In this respect we note that as VetPartners has grown by acquisition it is likely that many of its clinics predate its establishment in 2015. For Medivet, we note that there is no evidence to the contrary to suggest that the 50% discount is not appropriate to it. We therefore propose keeping the discount at 50% for both Medivet and VetPartners.

3.80 In relation to Pets at Home's submission that a lower discount rate should be applied to its assets as its estate is newer, we note that based on its own calculations its assets covered by the fit-out costs methodology are on average [✂] years old (see above). This would obviously mean that based on the useful economic life we have used of 16 years then these assets would be halfway through this useful life and hence a discount of 50% would be appropriate. Moreover, were we to adjust the calculation to reflect the asset age ([✂] years) and the useful economic life (21 to 25 years) suggested by Pets at Home then this would have limited impact on their ROCE calculation as an increase in asset value from the lower discount applied would be offset by a lower depreciation charge (and hence higher profits) from the longer economic life resulting in a small net negative impact on their ROCE. We therefore do not intend adjusting the discount rate applied to Pets at Home.

3.81 The total depreciated replacement cost values for each LVG are set out in the table below.

Table 3.7 Total replacement cost asset value for each LVG

LVG	Total replacement cost asset values for fit-out costs £m				
	FY20	FY21	FY22	FY23	FY24
CVS					

[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
IVC					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on LVG data from RFI 13
Note: [✂] was unable to provide figures for 2020 and 2021 we have therefore assumed the same square footage as 2022 for these years in calculating the tangible assets values above. These figures include the 50% reduction for the age of the assets.
Note: as explained in the notes to the preceding tables, we have not updated Linnaeus' figures for the minor updates to the information for one of its local clinics and one of its referral centres it flagged to us shortly before publication of the PDR.

Vehicles

3.82 CVS distinguished between leased motor vehicles which would be valued accurately under IFRS 16, and vehicles owned outright, which were likely to be undervalued due to NBV being below replacement cost.[170]

3.83 We noted that vehicles made up a very small proportion of the total net book value of each LVG's balance sheet and considered that, because each vehicle would be of significant value, it was unlikely that there would be missing vehicles in any LVG's fixed asset register.

[170] CVS response to the profitability approach paper, Annex, page 13, [✂].

3.84 We considered that any adjustment to reflect the prevailing replacement cost of each LVG's vehicle fleet would not make a material difference to our assessment and therefore we decided to use the unadjusted NBV in our capital base.

Depreciation

3.85 We also needed to consider the impact of including revalued tangible fixed assets on the associated depreciation charge.

3.86 For those assets where no adjustment was made to the value in the accounts we did not change the depreciation charged. For leasehold assets, as set out previously, we used IFRS 16 methodology in the valuation of these right of use assets. We also followed this methodology for the associated right of use depreciation charge for these assets.

3.87 To calculate the annual depreciation charge for the tangible fixed assets derived from the fit out costs methodology we divided the average of the opening and closing gross tangible asset values (pre the reduction set out above) by 16 (based on our estimation of the weighted (by value) average economic life of these assets.) The one exception to this was FY2020 where we had no opening position due to having no prior year closing position. We therefore used the closing gross asset values for this year.

3.88 Our assumption of a blended economic life of 16 years for these assets was based on the midpoint of [✂] estimate of an economic life of 10 years for these assets[171] and Pets at Home's economic life estimate of 20 to 25 years (as set out above). Only Pets at Home provided us with a full breakdown of fit-out costs. Based on this we note that the largest category of fit-out costs is leasehold improvements comprising [✂] of costs, followed by clinical equipment comprising [✂] and fixtures and fittings [✂].[172] In addition we also received a breakdown of the asset mix for its new greenfield sites [✂]. This showed [✂]% of fit out costs related to leasehold improvements, [✂]% to fixtures and fittings and [✂]% to equipment.[173] In our view given this asset mix and the likely economic life of these assets (with leasehold improvements likely to have a long economic life) this assumption of 16 years appears reasonable.

3.89 In our Profitability Working Paper we sought submissions on this. CVS stated that given the mix of assets it is difficult to ascertain the blended age and economic life of the assets.[174] It stated that its leases normally are for [✂] years (with a [✂] break clause) and leasehold assets and fixtures and fittings are normally

[171] [✂].
[172] CMA calculation based on the date received [✂] provided in response to Question 37 of the CMA's RFI 13 request to [✂] .
[173] [✂].
[174] [✂] to the CMA's Profitability Working Paper of 1st May 2025 page 11.

depreciated on this basis. It also noted though as leases can be renewed some assets will have a longer economic life than this while others such as equipment will have shorter economic life. Based on an estimate of the useful economic life of assets in five greenfield sites they suggested an economic life of 15 years or shorter should be applied and that sensitivities should be modelled on this given its impact on the results.[175] In response to the PDR, CVS submitted the following: 'CVS estimated that the weighted average UEL across different asset sub-classes (leaseholds, IT equipment, other equipment) for five CVS greenfield openings/refurbishments in the CMA's sample to range from [✂] years to [✂] years.'[176] Adding, '[t]herefore, whilst the CMA's choice of a UEL sensitivity of 12 years seems sensible based on CVS's data, the CMA's sensitivity C of lengthening the UEL to 20 years, would not reflect the average economic life of CVS's tangible fixed asset categories, and should not be relied on in relation to CVS.[177]

3.90 IVC's view was that the economic life of assets was independent from the discount factor applied and that the discount factor applied should only be revised when there is clear evidence of the actual age of the assets. In the absence of this in its view the assumption that the assets are halfway through their useful life should remain even if the economic life changes.[178] We note that our assumptions are based on a mix of high-level estimates and more granular estimates from Pets at Home whereby the actual age of the assets as well as the economic life is estimated. In the case of the Pets at Home example, clearly any change in the economic life (increasing or decreasing depreciation) would also serve to reduce or increase the asset base with a movement in one having an offsetting impact on the other.

3.91 In our view, our assumptions on the economic life of the assets remain appropriate. First, we note that (as set out in above) we have only received one additional estimate of the useful economic life which at 15 years is broadly in line with our estimate of 16 years. Furthermore, we note the asset mix as set out previously would suggest that the bulk of the fit-out costs relate to leasehold improvements which we would expect to have a longer economic life. We also note that were we to adopt the Pets at Home estimates of useful economic life and asset age this would increase ROCE values.

3.92 While we think that there is clearly a natural offset between depreciation and the discount factor used (as set out above) we have modelled as part of our sensitivities the impact of moving the economic life to 12 and 20 years respectively

[175] [✂].
[176] [✂].
[177] CVS response to the PDR, Annex 2, page 8.
[178] [✂].

while retaining the 50% discount factor. We chose the values for these alternative assumptions to test whether they made a material impact on our results.

3.93 We have used the average gross cost of these assets during the year to work out the depreciation charge. In our view a charge based on this average best represents the expected loss in economic value of the assets used during the year allowing for disposals and additions during the year.

Working capital

3.94 Working capital comprises inventory, trade debtors and other debtors, current and non-current operating liabilities such as trade creditors and other creditors and operating provisions. These assets and liabilities are necessary for the provision of veterinary services and therefore we included them in our calculation of capital employed. Due to their current nature, we have not revalued these assets.

Summary

3.95 The table below shows the estimated depreciated replacement cost for the fit-out assets for each LVG as a result of our calculations. We compare this with the carrying value in each LVG's statutory financial statements and show the difference between the two values.

Table 3.8 Comparison of depreciated replacement cost for fit-out assets with carrying values as at each LVG's respective 2024 year end, £m

	CVS	IVC	Linnaeus	Medivet	Pets at Home	VetPartners
Carrying value in (adjusted) statutory financial statements	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Depreciated replacement cost	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Uplift Factor	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA Analysis based on LVG information provided in responses to RFI12 and RFI13

Table 3.9 Comparison of depreciation charge based on replacement cost for fit-out assets with equivalent book depreciation charge for each LVG in respect of their financial year ended in 2024, £m

	CVS	IVC	Linnaeus	Medivet	Pets at Home	VetPartners
Depreciation charge in (adjusted) statutory financial statements	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Replacement cost depreciation charge	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Uplift Factor	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA Analysis based on LVG information provided in responses to RFI12 and RFI13

Intangible assets

3.96 In this section we consider intangible assets. First, we consider which types of intangible asset should be recognised in the capital employed of the firms for the purposes of our profitability analysis. Then, we consider how the relevant intangible assets should be valued in the context of the 'value to the business' framework as set out in our Profitability Approach Paper.

Initial observations

3.97 We received substantial submissions from the LVGs on intangible assets in response to our Profitability Approach Paper and in response to our requests for information. In summary, the LVGs contended that various intangibles not normally treated as assets for accounting purposes were relevant and should be added into their capital base figures for the purposes of our economic profitability analysis. The submissions identified a consistent set of intangibles but differed significantly as to how they might be valued, and the degree of quantification.

3.98 The argument underlying these submissions was – to use a proposition from CVS's submissions – that costs incurred to support future demand should be capitalised.[179] A significant proportion of costs treated in the accounts as operating expenditure were, it was argued, costs incurred today in support of future demand and therefore should properly be treated as part of the capital base when assessing profitability.

3.99 Our Guidelines[180] set the criteria for consideration when determining whether or not to recognise an intangible asset for the purposes of profitability analysis. 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;

(b) this cost must be additional to those necessarily incurred at the time in running the business; and

(c) it must be identifiable as creating such an asset separate from any that arises from the general running of the business.

3.100 Clearly some costs treated as operating expenditure for accounting purposes are properly treated as expenses in the profit and loss account for our analysis, while others are properly treated as capital in nature, capitalised in the balance sheet and amortised to the profit and loss account based on their estimated lives.[181] In principle, we accept that the distinction rests primarily on the extent to which the costs are incurred for future benefit as opposed to current benefit (as set out above). The questions we need to address are first, the extent to which expenditure which has been treated as operating expenditure in the profit and loss but which relates to the creation of a future benefit to the business should be capitalised. Second, the extent to which intangible assets recognised on the

[179] CVS response to profitability approach paper, page 18.
[180] CC3 (Revised), Annex A, paragraph 14.
[181] Where assets have an indefinite economic life, they are capitalised but not amortised.

balance sheet for accounting purposes should be recognised and if so, how they should be valued.

Categories of intangible assets under consideration

3.101 The LVGs put forward the following categories of intangible assets for consideration:

(a) Customer relationships, otherwise referred to as a customer list.

(b) A skilled workforce, otherwise referred to as intellectual capital or knowhow.

(c) Reputation, otherwise referred to as a trade name or brand.

(d) Software and other IT development.

(e) Goodwill.

3.102 We consider each of the categories identified above in turn and identify which types of assets may require capitalisation as part of our analysis.

Customer relationships

3.103 Veterinary services providers incur costs in acquiring new customers in the expectation that these customers will purchase services (and products) from them over the life of their pet.

3.104 Customer acquisition costs typically comprise the cost of leafleting campaigns, online and other media campaigns and other similar promotional costs. Both UK Generally Accepted Accounting Principles (**GAAP**) and International Financial Reporting Standards (**IFRS**) require that firms expense such costs as they are incurred, such that the value of customer relationships is generally not reflected on the balance sheet of a firm except insofar as the firm has acquired the customer book from a third party. In this latter case, firms are permitted to recognise the value of the intangible asset on their balance sheet, as part of the process of allocating the purchase price to the fair value of purchased assets and the residual amount to goodwill.

3.105 We consider that customer relationships meet our criteria for recognition (as set out above), in that they represent investment with the aim of generating revenues in the future, the costs of developing customer relationships are additional to those necessarily incurred in running the business and they form assets that are separable from any arising from the general running of the business. This latter

point is demonstrated by the fact that customer relationships can be sold by one firm to another.[182]

3.106 We note that customer relationship assets were similarly recognised in recent market investigations, including Retail Energy[183] and Home Credit.[184]

Trained workforce

3.107 It was put to us that training of staff helps to create the asset of a skilled workforce, with costs incurred at one point of time generating returns at a later date.

3.108 Similar arguments have been considered in previous CMA market investigations, including in SME banking,[185] Home Credit,[186] and Retail Energy.[187]

3.109 The SME banking report considered the following:

> Some training may be viewed as maintaining skill levels among the workforce, to be viewed as a revenue cost of continuing to operate the business. Moreover, the individual bank does not have to carry out all training itself. It can also recruit staff that have already acquired much of the training needed, although this will perhaps involve increased recruitment costs. The cost of obtaining the necessary skills is then largely reflected in the salaries paid, which are an ongoing revenue cost to the company concerned. This is clearly not true for company-specific training, but some of this can be incurred over a number of years, with revenue being earned by the employee's efforts in the meantime. None of this prevents some forms of training being treated as a capital cost, but suggests that other such costs may properly be regarded as revenue costs, which is how they are typically treated in company accounts.[188]

3.110 The SME banking report also considered that that much of the expertise of employees is gained by 'learning-by-doing' and is necessary for the ongoing running of the business, rather than for a future investment. Put simply, it stated that a bank must be able to provide banking services and, though acquired over many years, 'training and similar activities [serve] to maintain rather than create

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[182] We are aware, for example, of Medi vet's two purchases of customer relationships in 2021 and 2022, as set out on page 65 of Hecate Holdco Limited's Annual report and financial statements for the year ended April 2023.
[183] CMA, Retail Energy Market Investigation, Appendix 9.10: Analysis of retail supply profitability – ROCE, paragraphs 64-77.
[184] CMA, Home Credit Market Investigation, Final Report: Appendix 3.6 - Provisional assessment of profitability, using return on capital employed, paragraphs 38-42 and 109-116.
[185] CMA, SME Banking Market Investigation, Chapter 2: The supply of banking services by clearing banks to small and medium-sized enterprises within the UK.
[186] CMA, Home Credit Market Investigation, Final Report: Appendix 3.6 - Provisional assessment of profitability, using return on capital employed.
[187] CMA, Retail Energy Market Investigation, Appendix 9.10: Analysis of retail supply profitability – ROCE.
[188] SME banking report, paragraph 2.252.

that ability'.[189] The report stated that 'expertise in dealing with SMEs was originally derived from, and is maintained by actually dealing with SMEs', rather than being separate from it.[190]

3.111 As a result, the broad principle applied was that 'though costs result in a future benefit as well as a current one, … this creation of the future benefit is incidental in that the costs have had to be incurred in order to supply the product at all, and for this reason the costs are treated for the purpose of economic and financial evaluation as revenue, not capital costs'.[191]

3.112 The same principles could be applied to veterinary services, in that much of the expertise of veterinary staff would have been gained through actually dealing with household pets and learning-by-doing.

3.113 The SME banking report did, however, recognise that some staff costs, which are incurred entirely for future rather than current benefit, may be more appropriate for capitalisation. These costs may include staff recruitment costs (for permanent staff) and both initial and subsequent formal training costs.

3.114 The same principles were adopted in the Home Credit report, where costs relating to recruiting and training new home credit agents and other staff were capitalised.[192]

3.115 We note that in other cases, for example in Retail Energy, arguments relating to the capitalisation of a skilled workforce have been rejected entirely on the basis that an asset separable from the running of the business is not created.[193]

3.116 In the present case, we note that the majority of LVGs ([✂],[✂],[✂] and [✂]) recognise the value of a 'workforce' intangible asset on acquisition, as part of the process of allocating the purchase price to the fair value of purchased assets and the residual amount to goodwill.[194] For example, on acquisition, [✂] calculates the fair value of workforce assets based on the costs incurred in recruiting and training employees and an allowance for 'new hire productivity loss' (based on compensation paid and the number of months typically required to move up the experience curve and achieve '100% performance').[195]

3.117 This evidence informs our view that some costs relating to the workforce of the LVGs should be capitalised, in accordance with the principles applied in the SME banking report and the Home Credit report. We consider it debateable whether the third criterion of our Guidelines is satisfied in this case (ie that the asset created be

[189] SME banking report, paragraph 2.268.
[190] SME banking report, paragraph 2.268.
[191] SME banking report, paragraph 2.270.
[192] Home Credit report, Appendix 3.6, paragraph 36.
[193] Retail Energy report, Appendix 9.10, paragraph 78
[194] See paragraph 3.221.
[195] See, for example, [✂] response to RFI3, Annex 39.11.

separable from those assets arising from the general running of the business), but in view of this evidence – which shows the LVGs commonly value the assembled workforce as a separate asset post-acquisition – we adopt a prudent approach and capitalise some costs related to the trained workforce of the LVGs.

Reputation

3.118 We considered the LVGs' submissions on the relevance of reputation, or brand value, as an intangible asset.

3.119 Having determined that a customer relationship asset and a workforce-related asset should be recognised as part of our analysis, the question is whether an additional 'reputation' asset should be included, separate from the categories of assets already considered.

3.120 We first note the LVGs have consistently stressed the importance of 'word of mouth' as a crucial factor in building reputation.[196] In our view, this indicates that much of the reputation of a veterinary services provider emerges directly from the ongoing operation of the business, rather than from incurring additional costs (ie over and above the costs of the general running of the business) aimed at establishing reputation.

3.121 We also concur with the view expressed in the SME banking and Home Credit investigations that 'brand value ultimately derives from the recruitment, training and skills of the workforce, and the marketing and sales activities carried out, which together provide the service and the customer recognition of it. Accordingly, […] if the costs of such activities are capitalised as appropriate, then no further capitalisation relating to brands is necessary'.[197] Such costs are to be considered as part of the LVGs' customer relationship and workforce-related assets. Further capitalisation of a 'reputation' asset is therefore unnecessary and would result in double counting.

3.122 We also note that – to the extent additional costs are incurred to build a reputation (in excess of costs necessarily incurred in running the business) – they are not likely to be material to our assessment. We reviewed documents provided by the LVGs in relation to the allocation of acquisition purchase prices to the fair value of purchased assets and note that:

(a) In all of the purchase price allocation (**PPA**) models provided by [✂], it ascribed a nil value to trade names. In several of the documents, [✂] stated that it had identified 'marketing related assets (trademarks, names and brands)' in addition to customer relationship and workforce-related assets,

[196] For example: CVS response to the profitability approach paper, Annex, page 16; Medivet response to the profitability approach paper, paragraph 42; VetPartners response to the profitability approach paper, paragraph 7.4.
[197] SME banking report, paragraph 2.267 and, Home Credit report, Appendix 3.6, paragraph 31.

but that the value of marketing assets was 'immaterial', and no formal valuation was carried out.[198]

(b) [✂] consistently identified intangible assets related to customer relationships and the workforce of acquired sites, but no separate assets for 'reputation' or 'brand names'.[199]

3.123 While our review of PPA documents shows that [✂] and [✂][200] did value brand names for certain (larger) acquisitions only, both parties adopted the relief from royalty method in valuing these assets,[201] rather than considering the costs incurred to generate those assets.[202] We note that high royalty rates may exist in markets where competition is ineffective. This means that, for our purposes, the method carries a risk that royalty rates from poorly functioning markets might be used to explain away any excess profits (because of the circularity issue). We maintain that the more appropriate method is to consider costs incurred and that, so long as costs related to the recruitment, training and skills of the workforce, and the relevant marketing and sales activities are capitalised – and from which reputation is derived – no further capitalisation relating to brands is necessary. This approach is consistent with that adopted in the SME banking report, the Home Credit report and the Retail Energy report, all of which recognised issues with capitalising the value of a brand as separate from other intangibles, such as customer relationships.

3.124 For these reasons, our view is that it is inappropriate to capitalise a separate intangible asset for the 'reputation' of veterinary practices.

3.125 We recognise that two of the LVGs – Pets at Home and Medivet – also operate national branding and submitted that national branding constituted a separate asset to the customer relationships of local clinics (and should be capitalised separately in our analysis).[203] We have considered this issue carefully.

3.126 Our view is that costs incurred in relation to national brands (and recognition of those brands by pet owners) are incurred with the aim of generating earnings in the future. Such costs are also additional to the costs incurred in running the business. On this basis, such expenditure meets two out of three of our criteria for recognition of intangible assets. With respect to the third criterion, ie that the asset

[198] [✂] response to RFI3, question 39.
[199] [✂].
[200] For completeness, we note that [✂] told us it had not undertaken a detailed PPA exercise in respect of recent acquisitions [✂] response to RFI3, question 39) and [✂] had completed only the acquisition of [✂], a telehealth business, in the last five years [✂] response to RFI3, question 39).
[201] The relief from royalty method may be used by valuation practitioners to determine intangible asset value based on the hypothetical royalty payments that are saved by owning, rather than licensing the asset from a third party.
[202] [✂] response to RFI3, question 39. [✂] response to RFI3, question 39.
[203] Pets at Home response to RFI7, paragraphs 1.73 to 1.75 and Medivet response to RFI7, page 6.

created be separable from those assets arising from the general running of the business, we considered that the evidence was less clear.

3.127 We are not wholly convinced that national branding meets our criteria for recognition, but we have adopted a cautious approach and included a portion of expenditure on national branding for both Pets at Home and Medivet as part of our analysis (taking care to capitalise only those costs that are additional to those incurred by individual practices to develop customer relationships, to avoid double counting).

Software

3.128 Veterinary services providers typically require IT systems to manage appointments, schedule staff and process bills and payments, among other activities. All of the LVGs capitalise the costs of developing software on the balance sheets.

3.129 We consider that software meets our criteria for recognition in that it represents investment with the aim of generating revenues in the future, the costs of developing software systems are additional to those necessarily incurred in running a veterinary business and they form assets that are separable from any arising from the general running of the business. We note there are a number of veterinary practice management software packages available to purchase off-the-shelf, similar to the way tangible fixed assets might be acquired.

Goodwill

3.130 Finally, we consider goodwill. Goodwill is the balancing figure between the purchase price paid in acquisitions and the fair value of the assets acquired. In other words, it is the unallocated element of an acquisition price remaining once all tangible fixed assets and intangible assets have been identified, fair-valued and set against the price paid.

3.131 In principle we agree that, when purchasing a business, at least some of the goodwill figure may represent the value of intangible assets not capitalised on the business's balance sheet. The approach we have taken is to consider those intangible assets that meet our criteria for recognition, regardless of whether these have been separately identified in the companies' balance sheets or are included in a balancing goodwill figure, but to exclude any remaining goodwill in line with our approach in previous market investigations. This approach ensures that only intangible assets that meet our criteria for recognition are included in the estimate of capital employed. It also avoids the risk of capitalising the value of any excess

profits that the business is able to generate, which may be reflected in the purchase price and hence goodwill.[204]

3.132 For these reasons, we do not include goodwill as part of capital employed.

Conclusion: categories of intangible assets to be included

3.133 Based on the above, we consider the following categories of intangible assets should be capitalised for the purposes of our economic profitability analysis:

(a) customer relationships;

(b) skilled workforce;

(c) national branding (for Medivet and Pets at Home); and

(d) software.

Valuation of intangible assets

Possible approaches

3.134 In this section, we consider how the relevant intangible assets should be valued in the context of the value to the business framework outlined in the profitability approach paper.

3.135 We explained in our profitability approach paper that we were considering two approaches to the valuation of intangible assets:

(a) Estimating the value of **individual** intangible assets based on costs incurred, for example, using marketing costs as a proxy for the value of a firm's customer relationships (a bottom-up approach); and

(b) Using start-up losses as a proxy for the investment required to build **all** of the necessary intangible assets in the start-up period (a top-down approach).[205]

3.136 We received substantial submissions from the LVGs as to which approach was to be preferred. In summary, the majority of the LVGs contended that a bottom-up approach based on costs incurred may understate the value of intangible assets

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[204] See OECD (2011), Policy Roundtables: Excessive Prices, page 395. Capitalising excess profits creates a circularity in the analysis. In extremis, if all future excess profits were capitalised as goodwill, it would not be possible to find excess profits under a ROCE versus cost of capital (WACC) framework. This is the case because excess profits would be capitalised as part of capital employed based on future cashflows discounted at the cost of capital. So, capital employed = excess profits/cost of capital (the formula for discounting into perpetuity) and therefore ROCE = excess profits/capital employed = cost of capital.
[205] CMA, Approach to Profitability and Financial Analysis, paragraph 4.61.

and that an approach based on start-up losses would likely yield the more accurate estimate.[206]

3.137 In response to our Profitability Working Paper however, representations received stated that both approaches as implemented by the CMA yielded results that were too low.[207] Pets at Home reiterated this in their response to the PDR. It told us that it was uniquely positioned to comment on the costs of investment having opened more greenfield FOPs in the UK than any other market participants. Pets at Home submitted that '[t]he actual investment costs associated with opening a new FOP and bringing it to maturity are substantial. The capitalised value of these costs is much larger than the CMA's 'bottom-up' approach of estimating an intangible asset.'[208]

3.138 At this point, it is appropriate to outline the principles underpinning each approach, starting with the bottom-up, cost-based approach.

Cost-based approach

3.139 Under a cost-based approach, the amount to be included for each category of intangible asset may be calculated in one of three ways:

(a) by dividing the annual spend in a category (for example, customer acquisition costs) by the number of units gained of the asset (for example, customers acquired), so as to calculate the value of asset in each unit, and then multiplying this number by the total number of units of the asset held by the company;

(b) by observing the typical annual spend on the asset in recent years and multiplying the typical spend by the number of years in the useful economic life of the asset; or

(c) by observing the spend on the asset in the initial years of operation, before a level of mature activity is reached.

[206] For example: CVS response to the profitability approach paper, Annex, pages 15 and 17; Linnaeus response to the profitability approach paper, paragraph 75; Medivet response to the profitability approach paper, paragraphs 43 and 46; [✂] response to the profitability approach paper; Medivet response to the profitability approach paper, Annex, paragraphs 2 and 20; VetPartners response to the profitability approach paper, paragraphs 7.1-7.4.
[207] For example, [✂] response to the financial analysis and profitability working paper, [✂], page 1. [✂] submitted that 'both these approaches result in an estimated intangible asset value per FOP that is far below what it would actually cost to establish the intangible assets associated with a new FOP.' The 'cost-based approach simply excludes most of the costs of building a new FOP'. Additionally, that the sensitivity based on a start-up losses approach fails to 'take account of any of the costs of building a thriving practice from scratch …and capping the extent of such costs arbitrarily at the level of accounting loss.'
[208] Pets at Home response to the PDR, paragraph 2.7.

3.140 In selecting the approach for each asset category, we have considered which option is likely to yield the most accurate estimate given the information available from the LVGs.

3.141 A bottom-up, cost-based approach guards against the risk of capitalising the value of any excess profits that the business is able to generate and allows us to consider explicitly – and to capitalise only – those costs that (i) relate to identifiable assets; and (ii) are additional to those incurred in the general running of the business, in accordance with our Guidelines.

3.142 A common criticism of a purely cost-based approach is that it carries a risk of understatement, due to the bottom-up nature of the calculations. This issue can, however, be alleviated by allowing for some headroom between our benchmark (WACC) and the returns made (ROCE), and sense checks can be carried out to assess whether the wedge between ROCE and WACC is sufficiently large for missing intangibles not to be a realistic explanation.

Start-up loss approach

3.143 The start-up loss approach estimates and capitalises the losses incurred in the first few years of a greenfield operation, with losses incurred acting as a proxy for the investment required to develop the necessary intangible assets.

3.144 We note that start-up losses have been considered in previous CMA Market Investigations, in particular in the Funerals Market Investigation (**Funerals MI**). In the Funerals MI, the CMA stated that, when estimating the start-up loss arising from opening a new site, the relevant costs were the incremental costs associated with the new site (in particular, it disallowed allocations of central overheads where new sites were opened by large groups).[209]

3.145 We recognise the logic in the start-up loss approach but, similar to the Funerals MI, we consider it must be applied with caution. In particular, we consider that the relevant costs must be carefully assessed, and it should not be assumed that all costs incurred during the start-up phase are to be included in the calculation. To do otherwise, risks including costs which are the result of inefficiency or poor management (for example, a business which over-recruited staff and then dismissed most of them would have a large intangible asset despite having very few staff).

3.146 A further point to consider as regards the start-up losses approach is the argument put forward by the LVGs that capitalised losses should include the 'insufficient returns' below the cost of capital that are experienced in the early years of

[209] CMA, Funerals Market Investigation, Appendix S, paragraphs 143-147.

operation.[210] In other words, the CMA should consider not only the quantum of losses reported for accounting purposes but should seek to recognise the opportunity cost associated with early-stage investment in a business (where the alternative would be to invest elsewhere and to earn the cost of capital).

3.147 We agree, that were a start-up losses approach adopted, it would be appropriate to adjust any estimate of capitalised losses upwards to take account of opportunity costs of financing,

3.148 In summary, while the start-up losses approach has the advantage of reflecting actual spend for future benefit and therefore reduces the risk of under-estimation, it also has the risk of over-estimation, as it may include costs that do not result in future benefits and would otherwise not be capitalised.

Cost-based valuation

The approach we used

3.149 In our base case we have used the bottom-up approach to valuation (based on costs incurred in creating the identified assets) as this most aligns with our guidelines as set out above (and also avoids the issues of circularity set out below, whereby if a market is not well-functioning, observed profits may be higher than the competitive level and estimating the value of intangible assets on the basis of these (higher) profits would be circular.) We note that a top-down approach using start-up losses (to proxy the value of all intangibles) effectively includes all excess costs regardless of whether they fulfil the criteria in the guidelines. This means that some costs could be included that do not even contribute to earning future profits (for example in the case of inefficiencies). Similarly, costs that do not contribute to an identifiable separate intangible asset or are necessary for the existing running of the business could also be included.

3.150 We have however included the approach using start-up losses in our sensitivities as set out below. In the following sections, we set out the submissions of the parties and our analysis of the value of intangible assets. We begin with the cost-based approach, before setting out our analysis of start-up losses.

Customer relationships

Submissions received

3.151 In response to our Profitability Approach Paper, all of the LVGs provided views on our proposal to use marketing costs to value customer relationship assets.

[210] For example, [✂]; [✂], Response to Profitability WP, paragraph 3.36.

3.152 IVC told us that it 'strongly supported' this approach (as well as the start-up loss approach)[211] and submitted an analysis of its cost of customer acquisition. IVC's analysis can be summarised as follows:[212]

(a) IVC used recent spend data from [✂] campaign to carry out a 'difference in difference' analysis. Spend data covered the period from June 2024 to September 2024.

(b) It tracked new customer numbers in the period before and after [✂], and compared this to a 'control group' of clinics which [✂].

(c) IVC told us it had spent [✂] on the campaign and acquired [✂] additional customers (vs the control group): a cost of £[✂]per customer.

(d) IVC applied this estimate to its [✂] active customers as of July 2024, which implied a total value for its customer relationships of [✂].

3.153 All of the other LVGs submitted that the cost based, bottom-up approach risked undervaluing intangible assets.[213] For example:

(a) Linnaeus submitted that [✂].[214]

(b) Medivet told us that customer acquisition was mainly driven by word-of-mouth and that building an 'organic word-of-mouth presence' required significant time and effort. It submitted that 'effectively, marketing costs become embodied in start-up losses which are required before a firm establishes its reputation'.[215]

(c) VetPartners – similar to Medivet – told us that word-of-mouth was the main means of establishing customer relationships and that the value of these assets was reflected in goodwill (and not accurately reflected by marketing costs).[216]

(d) IVC's[217] response to the Profitability Working Paper noted the small sample size of only nine clinics and therefore that this was unlikely to be representative of new start-ups. It also noted that as seven of the nine clinics are Pets at Home, some of whose clinics are integrated within its wider retail

[211] IVC response to the profitability approach paper, page 9.
[212] [✂].
[213] [✂] to the financial analysis and profitability working paper, [✂], page 15. Linnaeus response to the financial analysis and profitability working paper, paragraph 3.1 and 3.2. [✂] Medivet to the financial analysis and profitability working paper, paragraph 42. paragraph 95. VetPartners response to Profitability WP, paragraph 7.4.
[214] [✂] response to the financial analysis and profitability working paper, [✂], paragraph 3.2 b).
[215] [✂] response for Medivet to the financial analysis and profitability working paper, paragraph 113.
[216] [✂] response to Profitability WP, paragraph 7.4.
[217] [✂] on behalf of IVC, response to Profitability Working Paper, slide 19.

store, they were unlikely to reflect the marketing costs of a clinic opening on a standalone basis.

3.154 Pets at Home also submitted that its national branding constituted a separate asset to the customer relationships of local clinics and should be capitalised separately in our analysis.[218] Similarly, Medivet told us that the Medivet brand was a valuable asset that should be 'properly accounted for' in our assessment of the capital base.[219]

Assessment

Overarching principles

3.155 We first note that a number of the LVGs focused on the 'value' of their customer relationships. However, our concern is with the cost of acquiring the relevant assets, rather than their subsequent value to the company.

3.156 Second – as to the relevant costs to be considered – a number of the LVGs referred to the staff time required to establish customer relationships and the importance of word-of-mouth as a promotional tool. We considered these submissions carefully and, on balance, our view is that it is appropriate to capitalise a portion of employment costs incurred in the years immediately post-opening.

3.157 We recognise that practices may operate with (significant) spare capacity in the initial years of operation. We consider that employment costs incurred during this period can be conceptually separated between: (i) costs necessarily incurred in running the business (vet time spent serving current customers); and (ii) costs incurred primarily to obtain earnings in the future (vet time spent building the business).

3.158 We note that costs falling in the latter category are likely to cover a range of activities. For example, these could range from implementing internal processes, building the supplier base, recruitment and time spend on marketing activities to grow the customer base. It is not clear that all these activities would fulfil the criteria set out above to be recognised as an intangible asset. For example, time spent building internal processes and supplier bases would appear not to create an asset identifiable as separate from any that arises from the general running of the business and hence not fulfil the criteria above. However, some of these activities, such as time spent in building the customer base clearly would contribute to creating a separate identifiable asset (as set out in previously).

[218] Pets at Home response to RFI7, paragraphs 1.73 to 1.75.
[219] Medivet response to RFI7, page 6.

3.159 However, we have chosen to adopt a cautious approach and assume that costs relating to excess staff capacity meet the criteria for capitalisation set out in our Guidelines. Accordingly, we propose to capitalise a portion of veterinary employment costs incurred in the initial years of operation, as part of our valuation of customer relationship assets. Once a steady state of customers is reached, we consider that employment costs are necessarily incurred in order to supply the relevant services, and that the creation of any future benefit is incidental. Employment costs incurred from this point are, therefore, appropriately treated as operating costs for our purposes and not capitalised.

IVC's estimate of customer acquisition cost

3.160 IVC's approach is similar to that outlined above: it aims to estimate the cost of acquiring one customer and multiplies by the total number of active customers.

3.161 While a reasonable approach in principle, we have significant concerns about the analysis presented by IVC.

3.162 First, it is based on one campaign that appears to be only part-way through execution, reflecting costs incurred from June to September 2024 only. Such a short period cannot, in our view, be taken as a reliable estimate of the costs of acquiring new customers.

3.163 Second, IVC has provided information related to one campaign only. It is unclear whether outcomes from this specific campaign can be considered 'typical'.

3.164 Third, IVC has provided no specific information about the clinics in the 'live' cohort and the control group. It assumes all additional customers are the result of its [✂]. IVC's analysis does not control for the potential impact of, for example, population density, proximity to other group clinics,[220] and the number of competitors in the local area.

3.165 Fourth, IVC has not sought to make any adjustments for 'successful' marketing costs. Instead, all of the marketing spend is attributed to new customers. We note this implies that if large amounts were spent on marketing and very few customers were obtained, the customer acquisition asset could be extraordinarily high and – in extremis – in excess of the value of the customers acquired. An alternative argument might be that the marketing spend was simply not successful and is more appropriately treated as operating expenditure because it did not create a lasting asset.

[220] We understand that new customers might be sent to other, local group clinics to manage patient numbers. IVC told us this was the case for Rufford Vets (IVC response to RFI13, paragraph 25.5).

3.166 For the above reasons, we are not persuaded that IVC's analysis provides a sufficiently reliable basis for the value of its customer relationship asset.

The approach we took

3.167 In our view, the best available approach for estimating the cost of acquiring customer relationships is to consider: (i) the marketing costs of newly established practices; (ii) the portion of initial employment costs that are incurred to generate future business; and (iii) the costs associated with national brands (for Medivet and Pets at Home only).

3.168 As regards (i), we consider that the marketing costs incurred in the initial years of operation can be seen as investment in establishing the reputation of the clinic in its local area and acquiring sufficient customers to operate effectively. This approach also reduces the need to distinguish between those marketing costs incurred to maintain existing customers and the costs incurred to attract new ones. The early stage of the practice's life cycle implies that the majority of marketing costs are incurred in respect of the latter.[221]

3.169 We also agree with VetPartners that recent years' marketing costs might reflect the costs to maintain existing relationships rather than to build new ones,[222] and favour a focus on the marketing costs of new practices for this reason also.

3.170 We therefore obtained information from the LVGs on the marketing spend of any 'greenfield' sites opened in the last five years.

3.171 As regards (ii), we set out above why we consider it appropriate to capitalise a portion of initial employment costs. Publicly available information and data collected during the course of our investigation allowed us to calculate an average salary for vets and veterinary nurses, to which we added Employer NIC and pension contributions, to arrive at an estimated total employment cost.

3.172 As regards (iii), we explained above that we are not convinced that national brand spending meets our criteria for recognition as an intangible asset. However, we have adopted a cautious approach and included a portion of expenditure on national branding for both Pets at Home and Medivet as part of our analysis.

Analysis of marketing costs: greenfield practices

3.173 With the exception of Pets at Home, the LVGs have historically grown by acquisition, rather than by opening new sites (that is, preferring to 'buy' rather than to 'build'). Accordingly, the number of greenfield sites opened by the LVGs in the

[221] This is similar to the approach adopted in the recent Funeral Market Investigation (Appendix S, paragraphs 140 *et seq.*).
[222] VetPartners response to Profitability WP, paragraph 7.4.

last five years is relatively few, compared to the number of acquisitions. Within the last five years:

(a) CVS has opened three greenfield sites.[223]

(b) IVC has opened [✂] greenfield sites.[224]

(c) Medivet has opened [✂] greenfield sites, although it was only able to provide marketing spend for the [✂] sites which opened from [✂] onwards.[225]

(d) Linnaeus has opened [✂].[226]

(e) Pets at Home has opened 15 sites (the majority of which are co-located inside Pets at Home retail stores).[227]

(f) VetPartners has [✂].[228]

3.174 For the purposes of our analysis, we focussed first on those greenfield sites which had been in operation for at least five years, consistent with the LVGs' views on the typical period to maturity of a veterinary practice.[229] We note that these marketing costs are relatively modest even taking them over five years, which itself may be excessive given the likelihood of break-even in [✂] years as set out below. The Figure below shows the total actual marketing costs incurred by each of these sites over the first five years of operation.[230]

Figure 3.1: Actual marketing costs incurred by LVG greenfield sites (sites in operation for 5 years) (£)

[✂]

Source: I[✂] and [✂]responses to RFI13 and CMA analysis.

3.175 We note the broad consistency in the level of marketing costs incurred (other than [✂]) and calculated the average marketing spend across the first five years of new sites. Excluding [✂], which appears to be an outlier,[231] we calculated a median spend of £19,000 per site and a mean spend of £21,000 per site.

3.176 We also note that the population of LVG greenfield sites that have been open for at least five years is comprised mainly of Pets at Home sites: the population in the

[223] CVS response to RFI13, question 4.
[224] IVC response to RFI13, question 4.
[225] Medivet response to RFI3, question 40 and Medivet response to RFI13, question 4.
[226] Linnaeus response to RFI13, paragraph 4.1.
[227] Pets at Home response to RFI13, Annex 002.
[228] VetPartners response to RFI13, paragraph 2.1.
[229] See for example: CVS response to Profitability WP, page 17; IVC, Proactive submission on the approach to economic profitability analysis, page 40; Linnaeus response to Profitability WP, paragraph 84; and Pets at Home, Response to Profitability WP, paragraph 3.37.
[230] We note Pets at Home told us marketing spend for Romford also includes spend for its [✂] site. The figure presented for [✂] in Figure 3.1 may therefore be an overestimate.
[231] [✂].

Figure above comprises seven Pets at Home sites and two [✂] sites, and we note that Pets at Home submitted that its veterinary sites benefit from co-location in its retail stores with spending on the Pets at Home retail business conferring benefit to its veterinary services, in the form of increased footfall.[232] We therefore considered whether the marketing spend of Pets at Home's greenfield sites might understate the spend that would be incurred absent co-location (that is, whether standalone sites would need to spend more to establish a reputation/customer awareness in the initial years of operation).

3.177 Accordingly, we also considered the annual spend of those LVG greenfield sites (other than Pets at Home) which had been in operation for fewer than five years. We pro-rated the average annual spend figures for each site to cover a period of five years and compared the results against the median and mean figures outlined in above.

3.178 For the purposes of this analysis, we focused on the three CVS sites opened during the last five years, one [✂] site and the [✂] Medivet sites opened since [✂]. We excluded the additional [✂] site on the basis that the spend figures pertained to a specialist referral hospital and were an outlier among the available data points (the site opened in November 2023 and spent £[✂] on marketing in year one).[233] We also excluded [✂] for two reasons:

(a) First, [✂].

(b) Second, [✂].[234] [✂],[235] [✂][236]

3.179 The outputs of our analysis are summarised in Figure 3.2.

Figure 3.2: Pro-rated marketing costs incurred by LVG greenfield sites (sites operational < 5 years) (£)

[✂]
Source: [✂], [✂] and [✂] responses to RFI13 and CMA analysis.

3.180 We note from Figure 3.2 that only [✂] is projected (on a pro-rata basis) to incur marketing costs greater than the average calculated above: the remaining six sites are all projected to incur lower costs and, in some cases, significantly lower costs. The available data does not, therefore, support a view that the actual five-year marketing costs identified in Figure 3.2 above are understated (eg as a result of the population being skewed towards Pets at Home sites).

[232] Pets at Home response to RFI13, paragraph 2.3.
[233] [✂] response to RFI13, question 4.
[234] [✂] response to RFI13, paragraph 4.1.
[235] [✂] response to RFI13, paragraph 4.2.
[236] [✂] disagrees with the CMA's approach to dismiss them on the basis that they reflect budgets rather than actuals. [✂].

3.181 We therefore adopt the figures identified in paragraph 3.175 for our analysis. We favour the use of the mean marketing spend of £21,000 over the median spend (£19,000). Our view is that either measure could be considered appropriate, and we adopt the higher figure as a cautious approach.[237]

Analysis of employment costs to be capitalised

3.182 In order to estimate the proportion of employment costs that might be capitalised (per site), we noted that two inputs were required:

(a) An estimate of the average salary of vets and veterinary nurses, to which we can add Employer NIC and pension contributions to calculate total employment costs; and

(b) An estimate of the proportion of employment costs incurred during the 'start-up period' that are primarily aimed at generating future business.

3.183 As to (a), we first note that the SPVS 2024 salary survey states that the median annual salary package for vets in 2024 was £57,000.[238] We also collected information from independent practices on the 'market rate' for vets employed by recently opened practices. We calculated the average of these salary submissions was approximately £67,000.

3.184 Recognising that vets employed in the start-up phase of a new practice might reasonably be expected to have an above-average level of experience (in order to build the business) and, therefore, command a higher salary, we adopt the higher figure of £67,000 for the purposes of our analysis. We then added Employer NIC and pension contributions to arrive at an estimated total employment cost of approximately £80,000.

3.185 For veterinary nurses' salaries, we based our estimate on the figures provided in an Alan Jones and Associates Ltd (a specialised salary and benefit survey provider[239]) 2024 industry salary survey. This provided a median salary figure for a veterinary nurse of £30,182.[240] We then added employer NIC and pension contributions to arrive at an estimated total employment cost of approximately £37,000.

3.186 As to (b), there is limited evidence on which to base our assessment. Only CVS proposed a method for apportioning these costs (which is set out in more detail below). In summary, based on an analysis of a sample of their greenfield sites

[237] We also note that the inclusion of all sites identified in Figures 3.1 and 3.2 in the calculation of average marketing spend produces a median spend of £17,000 per site and a mean spend of £16,000 per site. Both of these figures are below the averages calculated in paragraph 3.149, further supporting that these figures are not understated.
[238] SPVS 2024 salary survey: https://spvs.org.uk/2024-salary-survey/.
[239] See https://www.alan-jones.co.uk/aboutus.php for more information.
[240] [✂] in response to the CMA's RFI of 11th July 2024.

opened in the last 10 years, CVS assumed it took [✂] years for a practice to reach maturity.[241] It then sought to calculate the proportion of current year costs in each of the [✂] preceding years required to run the business by reference to comparison of current year revenue to revenue at maturity in year [✂] and current year costs to costs at maturity in year [✂]. Then current year revenue as a percentage of revenue at maturity was divided by current year costs as a percentage of costs at maturity to calculate the proportion of current year costs used to run the business in that year. The remaining costs were then assumed to relate to future profits.[242] CVS then applied this methodology to employment costs in a sample of its greenfield openings over the last 10 years. Based on this methodology, [✂], [✂], [✂], [✂] and [✂] of employment costs were viewed as generating future revenue [✂] respectively.[243]

3.187 In our view applying this methodology is unlikely to identify accurately the staff costs in the early years of the clinic used to build the customer base. First, we note, the general issues with this methodology as set out in the paragraphs below in terms of determining 'steady state' profits. Our analysis set out below would suggest a more realistic timeframe for maturity of a practice is between two to three years. Furthermore, any 'excess costs' calculated under this top-down methodology could be determined by other factors rather than future profit generation such as inefficiencies or normal fluctuations in revenue. In the context of employment costs, we note that there could be productivity gains from technological or process improvements or from familiarity with clients and colleagues and hence any 'excess costs' calculated under this methodology do not necessarily relate to time spent on marketing activities to generate future profits.

3.188 Second, we note that LVGs have some ability to manage excess staff capacity and are able to recruit in stages as demand grows. Based on evidence from CVS the first point at which it recruits additional staff (presumably to meet increased demand) is in the [✂]. CVS states that while a clinic initially opens with [✂].[244] CVS provides the example of its [✂].[245] While we appreciate that LVGs are likely to recruit ahead of the demand curve, the recruitment of additional staff in the second year of the clinics' operation suggests by the end of the second year of operations clinics have already acquired sufficient scale to require additional staff. This also suggests that by the end of the second year the staff initially recruited to build the clinic have limited excess capacity to devote to growing the practice. While we note that there is likely to be some customer growth after this point it is not clear that this is directly attributable to staff time devoted to marketing activities

[241] CVS response to Profitability WP, pages 17-20.
[242] [✂] Response on behalf of CVS to the CMA's Profitability Working Paper page 24.
[243] [✂] Response on behalf of CVS to the CMA's Profitability Working Paper page 24.
[244] CRA Response on behalf of CVS to the CMA's Profitability Working Paper page 24.
[245] CRA Response on behalf of CVS to the CMA's Profitability Working Paper page 25.

and once the initial customer base is built you would expect additional growth from 'word of mouth' from these customers.

3.189 In the absence of any suitable methodology we have made our own assumptions based on the evidence available to us. First, we note there appears to be a wide range of staff numbers with which clinics open initially. CVS told us that it initially opens a practice with several vets, nurses and support staff[246] whereas some independent veterinary firms told us that they opened with one vet, one veterinary nurse and one receptionist.[247] [✂] submitted that 'the customer support team and nurses are critical to building lasting relationships with pet owners, which could result in future revenue' which would amount to [✂] FTE vets as well as the [✂] FTE for the customer support team and [✂] FTE for nurses.'[248] In our view the variation between these numbers is unlikely to be driven by the number of clinical staff devoted to marketing activities and rather by the size of the clinic and the number of vets required to drive expected demand. Moreover, were additional staff required for marketing activities it would appear more efficient (from both a cost and expertise perspective) to employ specialist marketing staff rather than have clinical staff perform this role. In our view this would suggest that it is likely only a proportion of the equivalent of one FTE's time for clinical staff that is spent on marketing activities. We have therefore allocated a portion of one FTE vet's time and one FTE veterinary nurse's time.

3.190 We also note as set out previously that in our view excess capacity used for marketing activities is likely to arise within the first two years of a clinics operation and decrease on a sliding scale as demand increases.

3.191 Therefore, we have assumed that approximately 50% of one vet and one veterinary nurse's time is spent on marketing activities in year one with an additional 25% in year two as the practice grows and current demand increases. We note, as set out above, that this spare capacity within a clinic is in practice likely to be spent on a range of activities not all of which will fulfil the criteria to be recognised as an intangible asset. However, while being cautious in our approach, we have decided to include all the costs associated with this as marketing costs.

3.192 To calculate the amount of employment costs that might be capitalised per site, we then multiplied our total vet and veterinary nurse employment costs of £80,000 and £37,000 respectively by 50% for year one of a clinics operation and 25% for year two of the clinics operation, Table 3.10 shows the results of this analysis.

Table 3.10: Estimate of employment costs to be capitalised

	Year 1	Year 2	Total

[246] CRA Response on behalf of CVS to the CMA's Profitability Working Paper page 24.
[247] [✂] response to question 1b, [✂] response to the CMA's RFI of 15th November 2024 response to question 1b.
[248] [✂] response to the financial analysis and profitability working paper, page 23.

Vets			
1.Vet Employment Costs	£80,000	£80,000	
2.Portion to be Capitalised	50%	25%	
Calculated as [1 multiplied by 2]	£40,000	£20,000	£60,000
Vet Nurse			
1.Vet Nurse Employment Costs	£37,000	£37,000	
2.Portion to be Capitalised	50%	25%	
Calculated as [1 multiplied by 2]	£18,500	£9,250	£27,750
Total capitalised			**£87,750**

Source: [✂] and CMA analysis.

3.193 In total, we estimate the costs incurred in acquiring customer relationships (at the local clinic level) to be approximately £108,750 per site (ie the sum of the £21,000 per paragraph 3.175 and the £87,750 calculated in Table 3.10).

3.194 In response to our Profitability Working Paper, we received the following responses from LVGs with regards to calculating this cost:

(a) [✂] submitted that it 'agrees conceptually with the CMA's approach, we consider that the foundational assumptions for this exercise, particularly on the employment costs, should be improved to more accurately reflect the cost of acquiring customer relationships, which extends beyond a portion of a single vet's time.'[249]

(b) IVC submitted that the estimates for proportion of initial employment costs to generate new business, are therefore based on hypothetical figures for employment costs, both on a hypothetical number of vets and hypothetical time allocations, and therefore demonstrate that the results are not robust. [250]

(c) Linnaeus stated 'It is reasonable to assume that all staff at the clinic will spend a proportion of their time in building business and should therefore be included in the CMA's analysis.'[251]

Analysis of marketing costs: Pets at Home and Medivet national brands

3.195 In addition to considering customer relationships at a local clinic level, we noted in paragraph 3.125 that Pets at Home and Medivet submitted that the value of their national branding should also be reflected in our analysis.

3.196 We considered these submissions in paragraphs 3.126 to 3.127. While it is not clear that national branding meets our criteria for recognition, we adopt a

[249] [✂] response to the financial analysis and profitability working paper, page 22.
[250] [✂] response for IVC to financial analysis and profitability working paper, [✂].
[251] Linnaeus response to the financial analysis and profitability working paper, paragraph 3.2(c)(ii).

conservative approach and include a portion of expenditure on national branding as part of our analysis.

3.197 There were, however, a number of limitations in the evidence provided by both parties as to the amount of company-level marketing spend that might properly be capitalised.

3.198 Medivet provided total company level marketing spend for the years since FY22 but was unable to break down this spend into more granular categories.[252] We are not, therefore, able to analyse how much of its company-level marketing spend was incurred in relation to:

(a) activities which would be expected to have an impact in year (for example PPC and other digital search advertising and/or direct marketing, where impacts are expected within a very short period of time[253]); and

(b) activities which primarily yield future year benefits.

3.199 Pets at Home was able to provide a more granular breakdown of company-level marketing activity, separating its spending as follows:

(a) '**Brand/campaign**' spending, which [✂].[254]

(b) '**Digital**' spending, which [✂].[255]

(c) '**Customer relationship management**', which [✂].[256]

(d) '**Community**' marketing, which [✂].[257]

3.200 From the descriptions provided by Pets at Home (outlined above), we consider that only brand/campaign spend is potentially eligible for capitalisation. The remaining spend categories are activities that would be expected to yield in-year impacts.

3.201 However, Pets at Home did not disaggregate between 'brand' spending – which may be eligible for capitalisation – and 'campaign' spending (where impacts are expected in the very short-term and thus not capitalised).

3.202 For the purposes of this appendix, we assume that the 'brand/campaign' cost information provided by Pets at Home is split equally between 'brand' spending

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[252] Medivet, response to RFI13, question 2.
[253] CVS response to RFI13, paragraph 9; IVC response to RFI13, paragraph 3.1(c); Medivet response to RFI13, question 3; and Pets at Home response to RFI13, paragraphs 3.3 and 3.6.
[254] Pets at Home, response to RFI13, paragraphs 2.6 and 3.3-3.5.
[255] Pets at Home, response to RFI13, paragraphs 2.5 and 3.6.
[256] Although not explicit in its response to RFI13, we assume Pets at Home considers this type of activity to be 'performance marketing' or 'ad-hoc' marketing, both of which Pets at Home told us were expected to convert to demand/sales almost immediately (if at all). Pets at Home, response to RFI13, paragraphs 2.5 and 3.3-3.7.
[257] Pets at Home, response to RFI13, paragraph 2.5.

and ‘campaign’ spending. We also assume (in our view, this may be generous as it may include some costs that would not meet the criteria to be capitalised) that all Pets at Home company-level brand spending can be capitalised. Therefore, we allow company-level marketing spend, as set out in Table 3.11 below, in our analysis of Pets at Home:

Table 3.11: Pets at Home allowable company-level marketing

	FY20	*FY21*	*FY22*	*FY23*	*FY24*
[1] Brand/campaigns (Pets at Home submission)	[✂]	[✂]	[✂]	[✂]	[✂]
[2] Brand spend estimate (CMA capitalised amount)	**[✂]**	**[✂]**	**[✂]**	**[✂]**	**[✂]**

Source: Pets at Home, response to RFI13, Annex 002 and CMA analysis.
Note: [2] calculated as [1] divided by two.

3.203 For Medivet, we allow a percentage of company-level marketing costs to be capitalised. We determined the relevant percentage by reference to the proportion of Pets at Home’s total company-level marketing costs that are capitalised in our analysis ([✂]%).[258] We therefore allow company-level marketing spend, as set out in Table 3.12 below, in our analysis of Medivet:

Table 3.12: Medivet allowable company-level marketing

	FY22	*FY23*	*FY24*
[1] Company-level marketing costs (Medivet submission)	[✂]	[✂]	[✂]
[2] Company-level marketing costs (CMA capitalised amount)	**[✂]**	**[✂]**	**[✂]**

Source: Medivet, response to RFI13, question 2 and CMA analysis.
Note [2] calculated as [1] multiplied by [✂]%

Consideration of useful economic life: customer relationships

3.204 Next, we considered the useful economic life of customer relationships (at the local clinic level). The parties provided a range of views as to how such an asset might be amortised (if at all):

(a) CVS told us that the benefits of such costs would materialise ‘over the entire duration of the customer relationship, which could be ten years or more’.[259]

(b) IVC submitted it was ‘reasonable to argue that the value of this intangible has an indefinite economic life and therefore should not be amortised’, on the basis that the customer base might be assumed to be in steady state over time (ie new customers replace old ones).[260]

[258] It can be seen from Table 3.11 that the total amount capitalised for Pets at Home across FY20-FY24 is £[✂] million. Pets at Home’s total company-level marketing spend was £[✂] million over the same period (Pets at Home response to RFI13, Annex 002). The CMA therefore calculates £[✂] million/£[✂] million = [✂]%.
[259] CVS response to RFI13, paragraph 11.
[260] IVC, Proactive submission on the approach to economic profitability analysis, page 39.

(c) Linnaeus told us that [✂].[261]

(d) Pets at Home told us it did not estimate the useful life of marketing spend, but that the median tenure for its veterinary services clients was estimated to be seven to eight years.[262]

(e) Medivet and VetPartners told us they were unable to provide reliable estimates of the useful economic life of marketing spend.[263]

3.205 We first note the submissions of the LVGs that firms are likely to have to incur on-going marketing and other expenditure in order to avoid the decline of this asset over time. However, there is limited evidence on which to base our assessment of useful economic life. Therefore, our analysis treats this asset, once acquired, as having an indefinite life, ie the asset is not amortised. Consistent with that approach, we have also assumed that ongoing maintenance expenditure should be expensed (rather than capitalised) in the year in which it is incurred.

3.206 We note this treatment is, in substance, the same as that proposed by IVC. If we were to assume a steady state of customers has been achieved after five years,[264] then no adjustments to EBIT would be required. This is because the amount to be added back to EBIT (for ongoing relationship maintenance expenditure) would be equal to the amortisation charge on the replenished asset (thus there is no net effect on profit arising from an adjustment to the accounting data).

Consideration of useful economic life: Pets at Home and Medivet national brands

3.207 As regards the national brands of Pets at Home and Medivet, we are sceptical as to the extent to which impacts from media spending are realised in future years, rather than within the year in which the spend is incurred. Indeed, Pets at Home told us that the impact of media spending 'can be immediate'.[265]

3.208 In the absence of better information at this stage, we draw a parallel to the submissions received in the Funerals MI, where the large funeral services providers similarly advocated for the inclusion of company-level marketing costs (in addition to the capitalisation of site-level marketing), to reflect the value of operating under a single, national brand.

3.209 The Funerals MI expressed similar reservations about the capitalisation of such expenditure but took an approach which (i) capitalised 10% of company-level marketing costs, and (ii) wrote this asset off in the following year. This approach

[261] [✂], response to RFI13, paragraph 3.1.
[262] Pets at Home response to RFI13, paragraphs 3.2-3.8 and Table 2.
[263] Medivet response to RFI13, question 3 and VetPartners response to RFI13, paragraph 3.1.
[264] Consistent with IVC's Proactive submission on the approach to economic profitability analysis, page 40.
[265] See paragraph 3.199(a).

was based on evidence which indicated that any impacts from company-level media expenditure would materialise in years one and two only.[266]

3.210 We adopt a similar view for the purposes of this our analysis and write off capitalised company-level marketing costs in the following year.

Adjustments to the financial information provided

3.211 Based on the above, we adjust the LVGs' financial information in respect of both capital employed and EBIT.

3.212 As regards customer relationships at the local clinic level:

(a) **Capital employed**: capital employed is adjusted for each firm for each year by the value of £108,750 for each site operated by the LVG at year-end; and

(b) **EBIT**: for simplicity, we have assumed that the costs of establishing customer relationships would be incurred in the first year of operation. Considering the asset has been recognised on the balance sheet per the adjustment at point (a), we have added back £108,750 to EBIT in the year, for each greenfield site opened in that year. We note that these cost add-backs are only applied for sites which were opened organically rather than acquired.[267] We have also reduced EBIT by £108,750 for any sites closed in the year, to reflect the write-off of the asset.

3.213 As regards the company-level marketing adjustment for Pets at Home and Medivet:

(a) **Capital employed**: capital employed is adjusted to include company-level marketing costs per Tables 3.11 and 3.12 ([✂]% of Pets at Home brand/campaign spending and [✂]% of Medivet's total company-level marketing costs).

(b) **EBIT**: we have assumed that the capitalised portion of company-level costs are to be written off by the end of the second year. Accordingly, we have:

(i) added back the marketing cost figures in Tables 3.3 and 3.4 to EBIT in the years incurred; and

(ii) written off those costs in the following year.

[266] CMA, Funerals Market Investigation, Appendix S, paragraphs 148-153.
[267] Where sites have been acquired in year, we have included a customer relationship asset at a value of £88,200 per site, but we have not made any adjustment to EBIT.

Trained workforce

Submissions received

3.214 In response to our Profitability Approach Paper, four of the six LVGs (CVS, Linnaeus, Medivet and Pets at Home) submitted that the expertise of staff formed an important intangible asset for veterinary practices. Specifically:

(a) CVS submitted that its intangible assets included 'people, know-how… and training programmes'.[268]

(b) Linnaeus told us that [✂] (and thus met the CMA's definition of an intangible asset).[269]

(c) Medivet submitted that it incurred staff recruitment and training costs which should be taken into account as part of its capital employed.[270]

(d) Pets at Home told us that the ability of its vets to treat new and more complex conditions in-house was enhanced by training and experience in specialised clinical work, and this should be considered a human capital asset. It added that the value of this training and experience may not be properly captured by the ROCE/WACC framework.[271]

Assessment

Overarching principles

3.215 We set out in paragraphs 3.107 to 3.117 our view that some costs relating to the workforce of the LVGs should be capitalised. In summary, our view was that workforce-related costs that were incurred for future benefit should be capitalised, whereas those incurred in the general running of the business were appropriately treated as operating expenditure.

3.216 Costs that might be capitalised therefore include staff recruitment costs and both initial and subsequent formal training costs, such as the cost of accreditation and continued professional development (**CPD**). In this respect, we agree with the submissions of the parties which identified recruitment and training costs as eligible for capitalisation.

3.217 We also again emphasise that our concern is with the cost of acquiring the relevant assets – in this case, the workforce – rather than their subsequent value

[268] CVS response to Profitability WP, page 15.
[269] Linnaeus response to Profitability WP, paragraphs 106 and 107.
[270] Medivet, Annex to response to Profitability WP, paragraphs 7 and 22.
[271] Pets at Home response to Profitability WP, paragraph 3.23.

to the company. Our analysis therefore ascribes a value to the trained workforce based on the depreciated cost of recruiting and training them.

3.218 Other elements of staff costs – most significantly, their salaries and related benefits – are treated as operating expenditure (in line with the prior discussion) and fully included elsewhere in our analysis.

The approach we adopted

3.219 In principle, either of the approaches identified in paragraphs 3.139(a) and 3.139(b) could be applied to estimate the cost of recruiting and training the workforce. Having reviewed the information available from the LVGs, our view is that the approach identified in paragraph 3.139(a) is likely the most reliable approach in this case (that is, estimating the cost per staff member and multiplying by the total number of staff in each company).[272]

3.220 We obtained information from the LVGs which allowed us to estimate the cost of recruitment and training per staff member, by clinical role. We also gathered total staff number information to estimate the total amount to be capitalised for each party.

3.221 We supplemented the parties' data submissions with a review of internal documents. [✂]. In each case, the LVG considered the recruitment and training costs that should be taken into account in valuing the workforce. We consider this information highly relevant for our assessment and set out the relevant evidence from each LVG's PPA models as part of our assessment below.

3.222 We consider recruitment costs first, before turning to training costs.

Recruitment costs

Spend per staff member: LVG data submissions

3.223 We asked the LVGs to provide actual recruitment costs in each of the last five years and the number of staff recruited, split by clinical staff (veterinary surgeons and nurses) and non-clinical staff. The LVGs were able to provide information as regards the number of clinical staff recruited but were unable to separate recruitment costs between clinical and non-clinical staff.

3.224 While this prevents a more precise analysis of clinical staff recruitment costs, we were able to calculate the average recruitment costs per staff member (ie the

[272] Our view is that the approach identified in paragraph 3.139(b) cannot reliably be adopted in this case. The data received from the LVGs shows considerable variation year-on-year in both the total amount spent on recruitment and training and average costs. We find, therefore, that recent annual spending cannot be considered representative of 'steady state' recruitment and training costs and cannot be used in the way we describe in paragraph 3.139(b).

average across clinical and non-clinical staff) [✂] provided separate analyses aimed at estimating recruitment cost per clinical staff member. The data collected can be summarised as follows:

(a) [✂] average recruitment costs per staff member: [✂];[273]

(b) [✂] average recruitment costs per staff member: [✂];[274]

(c) [✂] average recruitment costs per staff member: [✂];[275]

(d) [✂] average recruitment costs per staff member: [✂];[276]

(e) [✂] estimated cost per clinical hire: [✂]for veterinary nurses and [✂] for veterinary surgeons;[277]

(f) [✂] estimate cost per clinical hire: £[✂] -[✂] ([✂]told us it was unable to split its estimate between veterinary nurses and veterinary surgeons).[278]

LVG PPA models

3.225 As above, we supplemented the LVG's data submissions with a review of the PPA models produced following recent acquisitions.

3.226 We note that [✂] and [✂] calculated recruitment costs per staff member, while [✂] and [✂] assumed that recruitment costs could be estimated as a percentage of employee salaries. This evidence is summarised below:[279]

(a) In the most recent model we have obtained from [✂] (produced February 2024), it assumed 'average recruiting expenses' per employee as follows:

(i) Director level veterinary staff: £1,400.

[273] Average recruitment costs calculated as the sum of FY20-24 recruitment spend divided by number of FTEs recruited in FY20-24. [✂] response to RFI13, Tables 5 and 6.
[274] Average recruitment costs calculated as the sum of FY20-24 recruitment spend divided by number of FTEs recruited in FY20-24. [✂] response to RFI13, Tables 2 and 3.
[275] Average recruitment costs calculated as the sum of FY20-24 practice-level recruitment spend and FY20-24 central-level recruitment spend, divided by the number of FTEs recruited in FY20-24. [✂] response to RFI13, Tables 3 and 4 and Annex 6.
[276] Average recruitment costs calculated as the sum of FY21-24 recruitment spend divided by number of FTEs recruited in FY21-24. [✂] response to RFI13, Tables 2 and 3.
[277] [✂] told us it had estimated the 'direct cost per head' using its recruitment budget. It told us it had used the total budget for the recruitment team, agency and marketing costs and allocated the budget across roles, with 60%, 25% and 15% allocated to vets, vet nurses and support staff respectively. This amount was then divided across the number of hires on a per person basis (as opposed to FTE). [✂] response to RFI13, paragraph 12.5 and Table 10.
[278] [✂] told us it had estimated 'Cost Per Hire' using spend incurred to recruit new staff in the last two financial years and its forecast recruitment spending for the next financial year. It told us that it had calculated Cost Per Hire including costs for the recruitment team, recruitment tools/systems, attraction and marketing (including any applicable advertising) and recruitment agency costs. [✂] response to RFI13, page 11.
[279] [✂] told us it had not undertaken a PPA exercise in respect of its recent acquisitions. [✂] response to RFI3, question 39. [✂] had not completed any acquisitions of FOPs/referral centres within the last five years. [✂] Home response to RFI3, question 36.

(ii) Senior veterinary staff: £1,400.

(iii) Veterinary nurses: £1,400.

(iv) Support staff: £750.[280]

(b) Following [✂], it produced a PPA model which assumed average recruitment costs of £6,500 for veterinary surgeons and £2,400 for veterinary nurses.[281]

(c) [✂]'s latest PPA model (produced December 2021) assumed that recruitment costs amounted to 12.5% of employee salaries.[282]

(d) [✂]' latest PPA model (produced FY23) assumed that recruitment costs amounted to 15% of employee salaries.[283]

Assessment

3.227 We summarise the data points outlined above in Figure 3.3 and Figure 3.4. Figure 3.3 shows the data points that relate to veterinary nurses only. Figure 3.4 shows the data that relate to veterinary surgeons and the LVGs' company-wide average recruiting costs (the latter are shaded in light blue). We have excluded [✂] high point estimate from Figure 3.4 as an outlier among the available data.

Figure 3.3: Veterinary nurse recruitment costs; summary of per staff data points (£)

[✂]

Source: LVG responses to RFI13 and CMA analysis.

Figure 3.4: Recruitment costs; summary of per staff data points (£)

[✂]

Source: LVG responses to RFI13 and CMA analysis.

3.228 Based on the Figures above, we adopt the following assumptions for the purposes of this appendix:

(a) For veterinary nurses: a recruitment cost of £1,400 per staff member. This figure reflects the mid-point of the estimates we received that were specific to veterinary nurses ([✂] estimate: £1,080; [✂] PPA documents: £1,400; and [✂] PPA documents: £2,400). We adopt the mid-point estimate rather than the high-point estimate as we are cautious about the extent to which costs

[280] [✂] response to RFI3, Annex 39.11 (tab 'workforce').
[281] [✂] response to RFI3, Annex 39.1, page 55. Recruitment costs are calculated as the sum of 'search cost' and 'interview cost'. The numbers presented are the average recruitment costs for veterinary nurses and veterinary surgeons (referred to as 'Residents' in Annex 39.1) across the sites acquired by [✂].
[282] [✂] response to RFI3, Annex VMI-000007401 'IVC Donnington Grove Draft PPA valuation', page 8.
[283] [✂] response to RFI3, Annex MI-0312 'Separately identifiable Intangible Assets – Valuation by Cohort FY23', tab 'Contributory Assets'.

related to [✂] may be considered representative of the costs that would generally be (efficiently) incurred in recruiting veterinary nurses.

(b) For veterinary surgeons: a recruitment cost of £6,500 per staff member. On balance, we consider this to be a reasonable (possibly generous) assumption, given that the majority of estimates we have obtained are below this level (and, in some cases, considerably so). In determining this figure we have had regard to (i) the estimates presented in Figure 3.4; and (ii) the fact that [✂] and [✂] assumed recruitment costs would amount to between 12.5% and 15% of salary costs in their PPA models. We note that a recruitment cost of £6,500 implies a salary of between £43,000 and £52,000, which we understand to be consistent with median 2024 salaries.[284]

Training costs

Spend per staff member: LVG data submissions

3.229 The LVGs submitted that various types of training activities were relevant to our assessment: CPD allowances; the cost of graduate/apprenticeship schemes; initial onboarding training and other learning and development that was not captured by formal CPD.

3.230 The LVGs submitted that their respective annual CPD allowances per staff member were as set out in Table 3.13.

Table 3.13: LVG CPD allowances (£)

	Director level / specialist vet	*Vet surgeons*	*Vet nurses*
[✂]	2,600	1,000	500
[✂]	2,500	1,750	600
[✂]	3,000-5,000	1,500	750
[✂]	2,000-2,500	1,500	300-500
[✂]	3,000	1,500	500-2,000
[✂]	2,000-5,000	1,250	550

Source: LVG responses to RFI13.

3.231 As regards other (non-CPD) training activities, the LVGs consistently told us that they also provided: (i) initial basic training; (ii) specific training for newly graduated veterinary surgeons; (iii) apprenticeship schemes; and (iv) a range of training activities through company-specific platforms.[285] The LVGs did not provide estimates of the costs incurred on these programmes on a per staff basis although in some instances did provide the total cost of some training programmes.

[284] See SPVS 2024 salary survey: https://spvs.org.uk/2024-salary-survey/.
[285] See for example: CVS response to RFI13, paragraphs 24 and 25. IVC response to RFI13, paragraphs 14.2 and 15.2. Medivet response to RFI13, page 13. Pets at Home response to RFI13, Table 3, Table 9 and Annex 006.

LVG PPA models

3.232 In this section, we set out the evidence we have obtained from our review of the LVGs' PPA models. In preparing these models, [✂], [✂], [✂]and [✂] each considered training costs as part of their assessment of the fair value of the assembled workforce (following recent acquisitions). Our review of these documents suggests that:

(a) [✂] considered the relevant costs to be the cost of CPD only. We note its most recent PPA model included assumptions for 'average training expenses' which match exactly those outlined in Table 3.13 above.[286]

(b) [✂] similarly considered annual CPD allowances to be the relevant training cost input.[287]

(c) [✂] assumed training costs per employee of £[✂] for both veterinary surgeons and veterinary nurses. The basis for these figures is not clear from the documents we have reviewed, but we note appeared to assume training costs that were lower than its CPD allowances.[288]

(d) In the latest [✂] model that we have reviewed, it considered training costs explicitly in assessing the 'workforce replacement cost' but determined that the number of weeks of required training was zero.[289]

Assessment

3.233 In considering the training costs to be taken into account as part of our analysis, we have given particular weight to the evidence from the LVGs' PPA models. This is because the PPA models represent the Parties' contemporaneous assessment of the relevant training costs to be considered in estimating the replacement cost of the assembled workforce. These documents were also prepared in a context other than for our investigation (which might confer incentives to be over-inclusive in the amount of costs included in the analysis).

3.234 The approach we adopt for the purposes of this analysis – guided by the LVGs' own approaches in the PPA models we have seen – is to capitalise the value of CPD training. Based on the data set out in Table 3.13 above, we include the following allowances for training costs:

(a) For veterinary surgeons holding the status of RCVS Specialist/Advanced Practitioner: an allowance of £3,000 per staff member.

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[286] [✂] response to RFI3, Annex 39.11 (tab 'workforce').
[287] [✂] response to RFI3, Annex [✂].
[288] [✂] response to RFI3, Annex 39.1, page 55.
[289] [✂] response to RFI3, [✂], page 8.

(b) For other veterinary surgeons: an allowance of £1,500 per staff member.

(c) For veterinary nurses: an allowance of £500 per staff member.

Consideration of useful economic life

3.235 If recruitment and training costs are to be capitalised, it is necessary to consider the useful economic life of recruitment and training. We sought representations from the LVGs as to economic life and received the following:

(a) IVC submitted that the useful life of training spend would correspond to the length of time the member of staff is employed by IVC. IVC did not provide the typical tenure of its staff but noted that referral specialists undertook a three-year residency programme [✂].[290]

(b) Linnaeus submitted that the useful life was the time over which staff remained with the business. It told us that:[291]

(i) Over 2022 to 2024, the average time with the business was [✂] for vets and [✂] for veterinary nurses.

(ii) As of January 2025, the average time that currently active staff had been with Linnaeus was [✂] for vets and [✂] for veterinary nurses.

(c) Medivet submitted this was difficult to estimate reliably and was likely to vary according to the type of training provided. It added that not all training was likely to correlate with future economic benefit in the form of improved sales (for example, training aimed at improving workplace safety).[292]

(d) Pets at Home told us it considered the number of years that staff remained with Pets at Home to be a 'useful proxy' for the economic life of the relevant assets. Pets at Home provided estimates of 'staff tenure', based on FY24 staff turnover data, as follows:[293]

(i) Vet tenure: [✂] years

(ii) Nurse tenure: [✂] years

(iii) Non-clinical tenure: [✂] years.

[290] IVC response to RFI13, paragraphs 16.1 and 16.2.
[291] Linnaeus response to RFI13, paragraph 16.1.
[292] Medivet response to RFI13, question 16.
[293] Pets at Home response to RFI13, paragraph 16.5.

3.236 Considering the representations of the LVGs, our view is that a useful economic life of five years, on average, appears reasonable. This is consistent with the staff tenure information provided by both [✂] and Pets at Home.

3.237 However, we also note that the LVGs would be required to incur ongoing expenditure to avoid the decline of this asset over time (assuming efficient staffing levels). We note that capitalising these ongoing costs would have an offsetting effect such that there is likely to be no net effect on profits (ie we would expect capitalised costs in any year to be equal to the amortisation charge, such that the workforce asset is replenished and maintained). Given there would be no net effect, it is not necessary to make adjustments in our analysis to reflect the amortisation charge and the offsetting capitalisation of ongoing maintenance expenditure.

Adjustments to the financial information provided

3.238 Based on the above, we adjust the LVGs' financial information in respect of both capital employed and EBIT, to account of the trained workforce asset:

(a) **Capital employed**: capital employed is adjusted for each firm for each year by the following values, using the number of clinical staff employed at year-end:

(i) For veterinary surgeons: £8,000-£9,500 (recruitment cost of £6,500 per staff member and training cost of £1,500-£3,000, with the higher allowance for staff holding the status of RCVS Specialist/Advanced Practitioner.

(ii) For veterinary nurses: £1,900 (recruitment cost of £1,400 and training cost of £500 per staff member).

(b) **EBIT**: Considering the asset has been recognised on the balance sheet per the adjustment at point (a), we have adjusted EBIT in the year to reflect the change in asset value from new joiners/leavers in that year.[294]

Total Value of intangible assets calculated under the cost-based approach

3.239 Table 3.14 below shows the total value of intangible assets for both the customer acquisition and workforce intangible assets for each LVG. Table 3.15 shows the average combined customer acquisition and workforce assets per clinic for each LVG. This is calculated by taking the total combined intangible asset for customer

[294] Note we do not have headcount information for FY19. This prevents us from calculating accurately the change in staff numbers and staff mix from FY19 to FY20. In calculating the adjustment to EBIT for FY20, we use the average annual staffing change across FY21 to FY24.

acquisition and workforce and dividing this by the total number of clinics at the year end. As the total workforce asset is determined by multiplying staff numbers, as opposed to clinic numbers, the combined average customer acquisition and workforce asset varies per LVG depending on the relative average number of staff per clinic.

Table 3.14 Total customer acquisition and workforce intangible assets for each LVG under cost-based approach (£m)

LVG	*2020*	*2021*	*2022*	*2023*	*2024*
CVS	[✂]	[✂]	[✂]	[✂]	[✂]
IVC	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus	[✂]	[✂]	[✂]	[✂]	[✂]
Medivet	[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home	[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis.

Table 3.15 Customer acquisition and workforce intangible assets for each LVG under cost-based approach expressed on a per clinic basis (£)

	2020	*2021*	*2022*	*2023*	*2024*
CVS	[✂]	[✂]	[✂]	[✂]	[✂]
IVC	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus	[✂]	[✂]	[✂]	[✂]	[✂]
Medivet	[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home	[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners	[✂]	[✂]	[✂]	[✂]	[✂]
Average	**143,820**	**146,675**	**148,395**	**149,315**	**150,697**

Source: CMA analysis.

Software

Submissions received

3.240 We received a number of submissions concerning the value of software and other IT systems from the LVGs. In summary, the LVGs contended that related license fees/operating costs should be capitalised and that NBV understated the true economic value of software assets:

(a) CVS told us that the depreciated value of its software assets (£[✂] as of FY23) did not reflect its recent transition to cloud services. It submitted that the cost of its third-party contract, which amounted to [✂] per year, should be capitalised.[295]

[295] CVS response to Profitability WP, page 21.

(b) Linnaeus told us it had incurred investments in various IT systems and software, which should be capitalised. It provided examples of investments made in its [✂] and told us that ongoing license fees (of around £[✂] per year) should also be capitalised.[296]

(c) Medivet told us that it had instructed an [✂] of its [✂]. It submitted that this [✂] could be used as the capitalised value [✂], with amortisation applied from that point in time and further investments added.[297] Medivet subsequently told us that there was an immaterial difference between the fair value of the asset and its carrying amount.[298]

(d) Pets at Home submitted that:

(i) Operating costs related to its PetCare app, its PMS and other software as a service should be viewed as investments and capitalised.[299] It estimated operating costs of around £[✂] in FY24.[300]

(ii) Historic IT costs would understate forward-looking costs, and it expected to spend £[✂] in relation to its PMS over the next two years.[301]

(iii) The 'vast majority' of assets held by its Vet Group related to software and licenses ([✂]). It proposed that 'for simplicity', the CMA should include all of the Vet Group assets in the software category.[302]

(e) VetPartners submitted that NBV was not a good measure of economic value for software because of a mismatch between accounting depreciation profiles and true economic life. [✂].[303]

Assessment

3.241 The submissions of the LVGs can be grouped into three broad reasons for considering NBV an unsuitable proxy for the economic value of software:

(a) First, NBV reflects the historic cost of software assets less accumulated depreciation. It does not reflect operating costs such as license fees which, according to some of the LVGs, should be capitalised.

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[296] Linnaeus response to Profitability WP, paragraphs 108 and 109.
[297] Medivet response to Profitability WP, paragraph 34.
[298] Medivet response to RFI16, question 20.
[299] Pets at Home response to RFI7, paragraph 1.55 and 1.56.
[300] Pets at Home response to RFI7, paragraph 1.59. Pets at Home also told us that these costs had previously been capitalised, before a change in international accounting standards in 2021. Pets at Home response to RFI7, paragraph 1.57 and 1.58.
[301] Pets at Home response to Profitability WP, paragraph 3.27(iii). Pets at Home told us this figure [✂].
[302] Pets at Home response to RFI7, paragraph 1.61.
[303] VetPartners response to RFI7, paragraph 1.1(g).

(b) Second, historic costs understate forward-looking costs, as evidenced by recent investments.

(c) Third, that the accounting depreciation profile results in assets being depreciated too quickly, producing assets values below the real economic value.

3.242 As to (a), we are not persuaded that license fees and other operating costs related to software and IT systems should be capitalised. The costs incurred appear to be for services rendered in year (not for future benefit) and are appropriately treated as operating expenditure.

3.243 As to (b), these submissions – in particular, those of Linnaeus and Pets at Home regarding recent investments – appear to us to amount to submissions that our estimate of replacement cost should reflect 'new for old' replacement of assets. We do not accept these arguments. Our view remains that the replacement cost of the asset in its current condition today (ie depreciated replacement cost) is the appropriate basis for determining MEAV, for the reasons explained in the Profitability Approach Paper.

3.244 As to (c), we first note that the value of software is expected to decline over time to the point where it no longer has any value. We would expect the LVGs to select an appropriate 'useful economic life' for their assets when applying depreciation to them and would expect that, on average, the NBV of assets such as these – for which the replacement cost is usually relatively straightforward to establish – should proxy the depreciated replacement cost.

3.245 For these reasons, we include software assets as recorded on the balance sheet in our calculation of capital employed.

3.246 We note our proposed approach is consistent with [✂] approach to considering the fair value of software assets acquired in recent acquisitions. In all of the acquisition papers we have reviewed, [✂].[304]

Start-up loss approach

3.247 In this section, we discuss an alternative approach to valuing intangible assets, based on efficient start-up losses.

3.248 Given that the LVGs generally advocated for an approach based on start-up losses (rather than the bottom-up approach set out above), we first set out the submissions of the LVGs in detail. We then assess the arguments put to us by the

[304] See for example: [✂] response to RFI3, Annex 39.22 to Annex 39.35.

LVGs and carry out our own analysis of the potential value of intangible assets, were we to follow the start-up loss approach.

Submissions received

3.249 We received substantial submissions from the LVGs on the merits of using start-up losses to estimate the replacement cost of intangible assets. The LVGs generally contended that an approach based on start-up losses was appropriate in this case, but differed in their application of the start-up loss approach.

3.250 We set out the submissions of each party in detail in this section.

CVS

3.251 CVS proposed two approaches to assessing the replacement cost of intangible assets using start-up costs:

(a) Modelling the start-up costs of a typical greenfield practice; and

(b) An 'opportunity cost' approach, which considered how much CVS should be willing to pay to avoid start-up costs.[305]

CVS – start-up costs

3.252 CVS told us it considered it inappropriate to focus solely on the period over which greenfield sites incurred losses, and the CMA should instead focus on the longer period of growth to maturity, which CVS considered a better approximation of the replacement cost of all intangibles. CVS told us the period to maturity was typically [✂] (based on its experience of opening greenfield sites).[306]

3.253 CVS set out a possible approach to capitalising start-up costs. It recognised that some operational costs during the start-up phase were incurred in order to serve current demand and generate current revenues (and therefore were correctly treated as operating expenditure) but submitted that some costs were incurred 'solely to support future demand'. It submitted that costs to support future demand were part of the costs of building intangible assets and should be capitalised.[307]

3.254 CVS submitted that these costs included costs incurred directly for future benefit (for example customer outreach, training staff, building up local know-how) and indirectly incurred costs, which were necessary practice running costs but were

[305] CVS response to Profitability WP, page 16.
[306] CVS response to Profitability WP, page 17.
[307] [✂].

only incurred to support future demand and without which a customer base and other aspects of a successful practice could not be built.[308]

3.255 CVS's approach was to consider the development of costs and revenues over time, compared to those of a mature practice. It described its approach in the following terms:

> *We calculate what the practice would hypothetically cost to run if it was solely serving current revenues, at the same productivity level that we would expect to see from a mature vet practice. Conceptually this is equivalent to assuming that the practice can flex costs (e.g. labour, buildings, equipment etc) so that it incurs only those necessary to serve current revenues – as opposed to allocating any staff time or other resources to building a larger future business. We allocate this adjusted hypothetical cost level to opex and allocate the difference between this hypothetical cost level and the actual cost they have incurred to capex.[309]*

3.256 CVS provided an illustrative example of how its approach might be applied, which it told us reflected its recent greenfield projects. In its example, CVS assumed a FOP reached maturity over [✂] years,[310] when it stabilised at revenues of [✂] and costs of [✂] per year. The results of CVS's illustrative example are reproduced in Table 3.16 below:

Table 3.16: CVS example: start-up costs creating assets vs driving current revenues

	[✂]	*[✂]*	*[✂]*	*[✂]*	*[✂]*	*[✂]*	*TOTAL*
Revenue (£'000)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	
Cost (£'000)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	
Revenue relative to maturity	30%	50%	70%	85%	95%	100%	
Cost relative to maturity	50%	65%	80%	90%	98%	100%	
Costs driving current revenues (£'000) [see note]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	
Proportion of costs generating current revenues	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	
Cost of developing future business, to be capitalised (£'000)	**[✂]**	**[✂]**	**[✂]**	**[✂]**	**[✂]**	**£0**	**£398**

Source: [✂].

Note: Calculated using the rate at which costs drive revenues in CVS's hypothetical mature business (ie 75% cost to revenue ratio). For example, if in Year one the practice was able to achieve the 75% ratio of cost to revenue that is experienced at maturity in this example, it would incur only [✂]: the remainder is the cost that CVS considers is incurred for future benefit (ie it is incurred to drive the growth of future revenues in a larger business).

[308] [✂].
[309] [✂]
[310] In its response to RFI7, question 2, [✂].

3.257 CVS's example produced total costs to be capitalised – per FOP – of around [✂],[311] with the majority of the asset value built in the first three years. CVS submitted this was to be expected and reflected that:

(a) The build-up of costs was faster than the development of revenues because staff costs – which make up the majority of practice costs – were used to build up relationships/new business and sign-up new customers, as well as to treat existing customers.[312]

(b) There was more spare capacity in the early years of a practice, so vets, veterinary nurses and other staff would spend more time and use more resources building new business, with these activities (and the spare capacity to conduct them) declining as the practice became more established.[313]

(c) Facilities needed to be scaled for the volume of business that could possibly arrive, rather than only for the initial expected volume of business.[314]

3.258 CVS added that its approach was 'clearly a simplification' and that, in practice, the size of intangible assets was likely to vary 'a great deal' from practice to practice, but considered its example showed that the value of intangibles could be significant.[315]

3.259 CVS also noted that the value of the intangible assets (including goodwill) recorded on its balance sheet in FY23 was £[✂], which was equivalent to around £[✂]per site. It submitted that the value of intangibles estimated under its start-up cost approach 'can therefore go a significant way to explaining the… intangibles on CVS's books'.[316]

CVS – opportunity costs

3.260 CVS's alternative method to assess the value of intangibles was to look at the opportunity cost associated with creating the asset (ie by building a greenfield site) compared to purchasing an existing veterinary practice of equivalent scale and nature. In other words, intangibles might be valued by looking at the foregone profits associated with building a practice from scratch rather than buying it.[317]

3.261 CVS recognised that this type of approach relied on a comparison of profits under two hypothetical scenarios and that, if prices were inflated due to market power,

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[311] CVS told us it considered this to be conservative estimate, as it considered financing costs should be added to the capitalised value of intangibles. [✂].
[312] [✂].
[313] [✂].
[314] [✂].
[315] [✂].
[316] [✂].
[317] [✂].

this could feed through to an inflated assessment of the opportunity cost of building rather than acquiring a new practice. However, it submitted that it '[did] not see clear evidence that this should be of concern… given that the market is characterised by the constant entry of new independent vets (as well as CVS greenfield projects, for example) and is relatively unconcentrated at a national level'.[318]

3.262 It added that, even if the CMA were to find evidence of market power inflating prices, it would still be possible to run an 'opportunity cost' assessment of the nature suggested by CVS, by replacing actual revenues with an estimate of what competitive revenue levels would be (for example by restricting the assessment to sites where local concentration levels are low).[319]

3.263 CVS told us subsequently that we continued to use a highly partial and unsubstantiated approach to value intangibles in our (cost-based approach) base case. We had provided no evidence to support key assumptions (particularly in relation to the very small degree to which staff costs were capitalised, and the complete lack of capitalisation of other start-up phase costs relating to premises, in particular).[320]

3.264 CVS also told us that under the cost-based approach we had introduced unnecessary complexity in trying to break down the intangibles of a clinic into different elements of "staff" or "reputation" or "customer list" – distinctions that were in CVS's view largely meaningless. In reality you could not develop a sound reputation and strong customer list without a happy and well-trained set of staff and could not have a happy and well-trained staff without a good and growing book of customers for them to serve. By ignoring this reality and trying to individually value selected components that make up its intangible asset base, we were forced to rely on arbitrary assumptions that substantially understated the true capital investment required to set up a new clinic.[321]

3.265 CVS told us that our estimate of start-up losses relied on those Pets at Home clinics that had been set up in recent years, and because that estimate of start-up losses had relied on those clinics' actual costs and revenues over that period, that estimate might well overstate the extent to which those clinics could have been expected to break even (as the revenues earned over that period and speed to maturity would have reflected the unprecedented increase in pet ownership post-Covid). As such, CVS explained, our estimate might well understate the actual cost of setting up a new clinic under more normal market conditions.[322]

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[318] [✂].
[319] [✂].
[320] CVS response to the PDR, Annex 2, pages 1–2.
[321] CVS response to the PDR, Annex 2, page 11.
[322] CVS response to the PDR, Annex 2, page 12

IVC

3.266 IVC submitted an analysis of the potential value of its intangible assets using the start-up losses incurred by a new practice it opened in 2019 ([✂]).[323]

3.267 IVC told us that its approach was to capitalise EBIT losses before [✂] had reached a 'steady state' and that 'steady state should represent a competitive and sustainable level of profitability'.[324] We note this approach is conceptually the same as the 'opportunity cost' approach proposed by CVS above.

3.268 In its analysis, IVC adopted an EBIT margin of [✂] as the steady state profitability [✂], reflecting its EBIT margin after five years. It assumed the same level of steady state profit in each year and calculated a 'capitalised loss' [✂] (or [✂] of 'steady state' revenues), as shown in Tabbelow:[325]

Table 3.17: [✂] (IVC) start-up loss estimate £

	Year 1	*Year 2*	*Year 3*	*Year 4*	*Year 5*	*TOTAL*
[1] Start-up EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	
[2] Steady state EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	
[3] Difference [1] – [2]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[4] Capitalised loss	**[✂]**	**[✂]**	**[✂]**	**[✂]**	**[✂]**	**[✂]**

Source: IVC, Proactive submission on the approach to economic profitability analysis, page 40.
Notes: Capitalised loss calculated as: $EBIT_t - EBIT_s \times 1+WACC_{s-t}$, *where* t = *current period and* s = *first period of "steady state" and WACC = [✂].*

3.269 IVC then extrapolated its analysis of [✂] over its estate in two ways:

(a) First, using the absolute start-up loss of [✂] and multiplying by the total number of IVC clinics. This gave a total value [✂] for IVC's intangible assets.

(b) Second, using the ratio of start-up losses to revenues of [✂] and applying to IVC's total revenues. This gave a total value [✂] for IVC's intangible assets.[326]

3.270 IVC noted that its analysis assumed [✂] was a representative clinic and stated that, ideally, a sample of multiple greenfield sites would be used to refine its approach.[327]

3.271 It added that its intangible assets arguably had an indefinite economic life and, accordingly, should not be amortised.[328]

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[323] [✂]
[324] [✂]
[325] [✂].
[326] [✂].
[327] [✂]
[328] [✂].

Linnaeus

3.272 Linnaeus submitted that the difference between the steady state level of profit of a mature practice, and the 'build' level of profit achieved by a greenfield site provided a 'direct estimate' of the level of intangible assets[329] (ie it proposed the same approach as IVC).

3.273 Linnaeus submitted an analysis based on P&L projections for its greenfield sites (Linnaeus told us that it did not have recent examples of greenfield sites that had completed a start-up cycle, but it had opened a greenfield site in 2024 and [✂]).[330]

3.274 Linnaeus told us [✂].[331]

3.275 Linnaeus used [✂].

Table 3.18: Linnaeus example: projected start-up losses for a greenfield site £

	Year 0	*Year 1*	*Year 2*	*Year 3*	*Year 4*	*Year 5*
[1] Start-up site EBITDA	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[2] Steady state site EBITDA	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[3] Difference [2] – [1]	[✂]	[✂]	[✂]	[✂]	[✂]	0
[4] NPV of Difference	[✂]	[✂]	[✂]	[✂]	[✂]	0
[5] NPV total	[✂]					
[6] Extrapolate across estate [✂]	**[✂]**					

Source: Linnaeus response to Profitability WP, pages 22 and 23.
Notes: NPV calculated using a discount factor of [✂] which Linnaeus told us was its pre-tax WACC as of [✂].

3.276 Linnaeus submitted that this analysis showed it 'would have been willing to pay a value of £[✂] more to acquire a site that can generate a steady stream of profits immediately, rather than having to invest in building up its book of customer business, brand etc, and reaching the steady state of profits in five years' time'.[332] It told us that this £[✂] therefore represented the total value of the intangible assets of the site.[333] Linnaeus then extrapolated this figure across its estate of 204 sites, producing a total value for intangible assets of approximately £[✂].[334]

3.277 Linnaeus told us this figure was [✂] than the £[✂] of intangible assets (including goodwill) capitalised on its balance sheet.[335]

3.278 Finally, Linnaeus stated that its methodology '[made] the implicit assumption that the projected EBITDA profit is achieved in a competitive environment and therefore does not reflect any excess profits'. It noted that the CMA may be

[329] [✂].
[330] [✂].
[331] [✂].
[332] Linnaeus response to Profitability WP, paragraph 86.
[333] Linnaeus response to Profitability WP, paragraph 86.
[334] Linnaeus response to Profitability WP, paragraph 87.
[335] Linnaeus response to Profitability WP, paragraphs 88-92. Linnaeus gave three reasons for this [✂].

concerned that, if the level of EBITDA profits was higher than the competitive level, estimating the level of intangibles on the basis of EBITDA may be circular.[336] As to this, Linnaeus submitted:

(a) [✂].[337]

(b) The CMA could still apply Linnaeus' framework, even if it rejected the notion that the estimates in its analysis reflected competitive conditions. In these circumstances, the CMA could use an alternative competitive benchmark that it considered consistent with a normal rate of profits (as the basis of the long run steady state profit) and perform the same calculations set out above.[338]

Medivet

3.279 Medivet provided information on the financial performance of [✂] greenfield sites since their establishment in [✂]. It told us that all [✂] sites had incurred [✂] in the first few months after opening, with [✂] revenues. It told us this reflected the need to establish a veterinary clinic with the capacity to attract and serve a significant customer base from day one, even though it would take time to build that customer base.[339]

3.280 Medivet stated that costs had [✂] across [✂] sites after the first few months of operation but that [✂].[340] As a result, [✂] of its greenfield sites [✂], while Medivet's [✂] greenfield site had [✂].[341]

3.281 Medivet considered the relative success of different sites [✂].[342]

3.282 Based on P&L information from these [✂] sites, Medivet told us it calculated an average [✂] per greenfield site of around £[✂].[343] Medivet explained it considered this figure a lower bound for the CMA's analysis because:

(a) [✂];[344] and

(b) Medivet had incurred upfront costs related to local marketing, staff recruitment and training, and software costs that were [✂].[345]

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[336] Linnaeus response to Profitability WP, paragraph 93.
[337] Linnaeus response to Profitability WP, paragraph 94.
[338] Linnaeus response to Profitability WP, paragraph 95.
[339] Medivet, Annex to response to Profitability WP, paragraph 8.
[340] Medivet, Annex to response to Profitability WP, paragraph 9.
[341] [✂].
[342] Medivet, Annex to response to Profitability WP, paragraph 12.
[343] Medivet told us that, for simplicity, it relied on a simple average of the [✂] across its [✂] greenfield sites. Annex to response to Profitability WP, paragraph 21.
[344] Medivet, Annex to response to Profitability WP, paragraph 21.
[345] Medivet, Annex to response to Profitability WP, paragraphs 7 and 22.

Pets at Home

3.283 Pets at Home told us that the start-up losses approach was a more appropriate way to estimate the value of the customer list intangible asset as the direct marketing costs included in the cost based approach will only capture a portion of the costs used in building a customer list and hence will understate the intangible asset.[346]

3.284 Pets at Home told us it had opened more than 200 FOPs over the past decade and had carried out modelling which suggested that capitalised start-up losses were 'likely material'.[347]

3.285 Pets at Home told us it had assessed the EBITDA profiles of its cohort of FOPs over the period FY20 to FY24, and that this analysis indicated a new FOP typically reached profitability (in accounting terms) in the fifth year of operation.[348]

3.286 However, Pets at Home submitted that it took between [✂] years for a new FOP to earn positive economic returns (which reflect economic depreciation and the cost of capital).

3.287 Pets at Home estimated the value of start-up losses as the difference between:

(a) the actual earnings for 'young' FOPs (using data from FY20 to FY24), adjusted for the effect of capitalised leases, economic depreciation and owner-operator salaries;[349] and

(b) the expected economic earnings per FOP (based on Pets at Home's estimate of capital employed per FOP and the relevant cost of capital).[350]

3.288 Pets at Home then accumulated the yearly differentials over a period of ten years to arrive at a total estimated start-up loss per FOP of over £[✂].[351] It added that its

[346] Pets at Home response to the CMA's Profitability Working Paper page 22 paragraph 5.4
[347] Pets at Home, Response to Profitability WP, paragraphs 3.29 and 3.37.
[348] Pets at Home, Response to Profitability WP, paragraph 3.32.
[349] The adjustments applied by Pets at Home were as follows: (1) Capitalised lease adjustment: It replaced yearly rental charges with a lower depreciation charge. (2) Economic depreciation adjustment: It adjusted depreciation charges because Pets at Home told us its accounting depreciation policy depreciated assets too quickly compared to the true useful economic life of its assets. (3) Owner-operator salary adjustment: It increased payroll costs, as it told us recorded costs may be too low if owner-operators took part of their compensation as dividends. Pets at Home, Follow-up Response on Start-up Losses, page 12. Pets at Home subsequently told us in their response the CMA's profitability working paper that there should also be an adjustment for management fees as the underlying costs to the Pets at Home Group will be less than the management fees charged. Pets at Home response to the CMA's Profitability Working Paper at P23 paragraph 5.7.
[350] Pets at Home, Follow-up Response on Start-up Losses, page 3.
[351] Pets at Home, Response to Profitability WP, paragraph 3.37 and Pets at Home, Follow-up Response on Start-up Losses, page 2. Pets at Home also told us it had specific financial arrangements for its joint venture practices (for example as regards interest and management fees) and it considered this created a favourable financial profile compared to FOPs operating outside of the Pets at Home network. Pets at Home, Response to Profitability WP, paragraphs 3.29, 3.33 and 3.37.

estimate of start-up losses would be higher had it assumed a cost of capital greater than 10%.[352]

3.289 Pets at Home further submitted it had used a sample of FOPs wider than those opened within the last five years for the purposes of its analysis. It told us it considered this approach would provide a more accurate view of start-up losses because the increase in pet ownership during the COVID-19 pandemic had meant that recently opened FOPs matured faster than expected, producing lower than typical losses.[353]

3.290 Pets at Home also submitted that focusing only on successfully opened practices would create survivorship bias and considered 'one way to try and correct for this is to capitalise losses from practices that have been closed'.[354] Pets at Home told us it considered it appropriate to include an additional £[✂] per FOP to account for start-up losses from unsuccessful entry attempts. Pets at Home explained it had calculated this figure by spreading the total losses associated with recent closures (£[✂] million) across its total FOP portfolio (447 FOPs).[355]

3.291 Pets at Home also submitted that it was possible for clinics to generate significant start-up losses and still earn its cost of capital over the lifecycle of the clinic. It provided analysis that it said showed [✂] and still earn returns in line with the cost of capital over its lifecycle.[356]

3.292 Pets at Home subsequently told us that our approach to valuing intangible assets materially underestimated the true investment costs of opening greenfield clinics. Pets at Home told us that it was uniquely positioned to comment on the costs of investment, having opened more new greenfield clinics in the UK in the past decade than any other LVG. The actual investment costs associated with opening a new clinic and bringing it to maturity were substantial. In its view the capitalised value of these costs was much larger than the values our cost-based approach generated. Our cost-based approach, Pets at Home continued, largely ignored the investment into new clinics. Instead, the cost-based approach simply tracked the ongoing costs of certain marketing and staff training costs (which primarily applied to mature clinics).[357]

[352] Pets at Home, Follow-up Response on Start-up Losses, page 4.
[353] Pets at Home, Follow-up Response on Start-up Losses, pages 11 and 12.
[354] Pets at Home, Response to Profitability WP, paragraph 3.26(iii). Pets at Home added it had closed over 30 [✂] FOPs in FY20 and a 'handful' of additional FOPs in the following years. Pets at Home, Response to Profitability WP, paragraphs 3.38-3.40.
[355] Pets at Home, Follow-up Response on Start-up Losses, page 21.
[356] Pets at Home response to the CMA's Profitability Working Paper pages 26 and 27
[357] Pets at Home response to the PDR, paragraph 2.7.

VetPartners

3.293 [✂].[358] [✂] provided submissions on the merits of considering start-up losses.

3.294 It submitted the following, appearing to consider that goodwill should be taken as a measure of intangible assets (including those generated in the start-up period):

3.295 *… when a new practice is established, a significant amount of cost is incurred before any revenue is generated. The practice will also take several years before it builds up the reputation necessary to attract the volumes that will allow it to reach an efficient scale. Throughout this time, it will be carrying fixed costs and generating economic losses. Losses incurred in earlier trading periods will not be recognised as assets in the balance sheet. The valuation of intangible assets at the time of acquisition is one way of reflecting the cost of developing these assets. Therefore, excluding intangible assets and goodwill from the profitability analysis would render any conclusions economically meaningless.*[359]

Assessment

Overarching principles

3.296 We note that the LVGs put forward a number of different methods to estimate a value for intangible assets using start-up loss information. The two key questions to consider are:

(a) what is the amount of start-up losses that may reasonably be capitalised for a greenfield site; and

(b) what is a reasonable approach to extrapolating greenfield losses across the estate of the LVGs.

3.297 We consider (a) first. We note that the submissions we received from the LVGs broadly identified different approaches, which can be summarised as follows:

(a) [✂]. This is the approach that Medivet appeared to follow in its submissions.

(b) Capitalise the differential between steady state profits and the profits of a greenfield practice. This is the approach proposed by CVS, IVC, and Linnaeus.

(c) Capitalise the differential between the profits expected in a competitive market (that is, cost of capital multiplied by capital employed) and the profits of a greenfield practice. This is the approach proposed by Pets at Home.

[358] [✂].
[359] VetPartners response to Profitability WP, paragraph 7.3.

3.298 Our view is that neither of the advocated approaches are wholly correct. Adopting approach (a) would fail to consider the opportunity costs associated with creating the necessary intangible assets.

3.299 As regards the approach (b), an analysis based on the "steady state profit" of LVG practices carries a circularity risk, as was also identified by CVS and Linnaeus (see above). Put simply, if the steady state profit is achieved in a market that is not well-functioning, observed profits may be higher than the competitive level and estimating the value of intangible assets on the basis of these (higher) profits would be circular.

3.300 CVS, Linnaeus and IVC[360] recognised this concern but submitted that, instead of rejecting such an approach entirely, the CMA could include its own estimate of the normal rate of profit (see above).

3.301 We have adopted an approach whereby a clinic is deemed to reach maturity when it is earning sufficient profits to both cover the required return on capital employed and also the opportunity cost of the cumulative losses to date (as set out in more detail below). Adopting this approach allows for both the opportunity cost of the capital employed and the funding costs of the initial losses. Furthermore, it provides a partial solution to the issue of circularity (discussed above) by determining the maturity of the clinic by reference to required returns of investors, through the cost of capital, rather than a 'steady state profit' that may be the result of inflated prices should the market not be functioning well.

3.302 Before we set out our analysis of the losses incurred by greenfield sites, we make three further observations regarding the submissions of the LVGs.

3.303 First, we note the wide range of estimates submitted to us, which are summarised in the table below, and that there is no consensus among the LVGs as to the amount of losses that might be included in our analysis.

Table 3.19: LVG greenfield start-up loss estimates

LVG	*Start-up loss estimate (per site)*
CVS	£400,000
IVC	[✂]
Linnaeus	[✂]
Medivet	[✂]
Pets at Home	[✂]
VetPartners	No data provided

[360] IVC response to Profitability Working Paper, [✂].

3.304 Second – and in addition to the circularity point above – we note that the estimates provided by [✂] and [✂] appear particularly high.

3.305 In the case of [✂], we note that its estimate is based on the experience of [✂], a site which [✂] told us had faced considerable difficulties post-opening, which had contributed to significant losses.[361] Our view is that the experience of [✂] is not likely to be representative of the experience of a typical greenfield FOP and produces an estimated loss that is unreasonably high. We note that adopting [✂] figures would produce a value even higher still.

3.306 In the case of [✂], we note that in its comparison of start-up profitability to mature sites profitability over five years as set in Table 3.19 above, it has compared the forecast profits over five years of a greenfield site opened in 2024 to the forecast profits of a mature site over this period (using the fifth year profits of the greenfield site as the profit level of a mature site in 2029). We note that to estimate the profits for the mature site in preceding years it has used a perpetuity growth rate of [✂]% (effectively reducing the 2029 profits by [✂]% each year to get the equivalent figures for 2024 to 2028). To the extent that this assumption was removed (or reduced) we note that this would increase the expected present value of the differential and to the extent it was increased it would reduce the expected present value.

3.307 Third, we note that none of the LVGs sought to identify costs which should be removed from the analysis (for example Group management costs or other central cost allocations, as described previously). Not doing so means that the LVGs' analyses include the maximum amount of costs, producing higher loss figures and, in turn, higher intangible asset valuations.

The approach we propose to adopt

3.308 Given the issues discussed above, we have carried out our own assessment of how the available start up loss information might be used to value intangible assets.

3.309 Accordingly, we obtained profit and loss information, for greenfield sites opened by each of the LVGs in the last five years. We also obtained profit and loss information from some independent veterinary firms who opened clinics within the last five years in the sample set out in Section 6 below. We also obtained profit and loss and balance sheet information from [✂], an independent veterinary group who have opened [✂] practices within the last five years.

[361] [✂].

Analysis of profit and loss information: LVG greenfield sites

3.310 As noted in paragraph 3.173, each LVG has opened greenfield sites as follows within the last five years:

(a) CVS has opened three greenfield sites.

(b) IVC has opened [✂] greenfield sites.

(c) Linnaeus has opened [✂].

(d) Medivet has opened [✂] greenfield sites, although it was only able to provide marketing spend for the [✂] sites which opened from [✂] onwards.

(e) Pets at Home has opened 15 sites (the majority of which are co-located inside Pets at Home retail stores).

(f) VetPartners has [✂].

3.311 As with our consideration of greenfield marketing costs, we focussed first on those greenfield sites which had been in operation for at least five years. This results in a population of seven Pets at Home sites and two [✂] sites (as in Figure 3.1 above).

3.312 We have chosen to exclude both [✂] sites from our analysis as we do not consider their experiences to be representative of a typical greenfield practice: [✂][362][✂].

3.313 We also note that Pets at Home told us it did not have reliable profit and loss information for [✂], which reduced the population to six Pets at Home sites.

3.314 We received representations from LVGs to our Profitability Working Paper, that this is not a representative sample. IVC submitted that 'The top-down approach is based on a sample of six clinics, which are exclusively Pets at Home sites. Again, Pets at Home sites have a completely different operating model to most FOPs in the market: given their joint venture model; being co-located with large retail pet stores and benefitting from retail footfall; and a well-known national brand.'[363] Similarly, Pets at Home stated that five of its six sites were in-store and therefore benefited from synergies that were not available to other clinics. Therefore, in their view the six sites may not be representative of the wider industry.[364]

[362] [✂]
[363] [✂], response to Profitability Working Paper, [✂]
[364] Pets at Home response to the CMA's Profitability Working Paper page 24 paragraph 5.11

3.315 Pets at Home also submitted that, these six sites were '[✂]'[365] and therefore are unrepresentative of the true start-up losses of a greenfield site. In support of this it states;

(a) Cumulatively, this cohort of sites outperformed their budget [✂] with [✂].[366]

(b) This sample of six clinics collectively [✂] compared to all clinics opened in this period based [✂] at the equivalent period of maturity.[367]

3.316 In its submission to the CMA, Pets at Home shows that adjusting for owner-operator salaries and economic losses (while correcting for factors that may cause the CMA's estimate to be too high) leads to an estimated SLA that is approximately [✂] per FOP. [368]

3.317 To assess the extent to which these six Pets at Home practices were likely to be representative of the start-up losses of a new clinic we compared their accounting losses to the information on the accounting losses of new LVG clinics and to the accounting losses of new independent practices.

3.318 Financial information provided by Pets at Home showed that these sites had incurred accounting losses as follows:

Table 3.20: Pets at Home greenfield site accounting losses

Site	*Loss period*	*Total loss*
Coalville	[✂]	[✂]
Whitstable	[✂]	[✂]
Heanor	[✂]	[✂]
Cumbernauld	[✂]	[✂]
Saffron Walden	[✂]	[✂]
Glasgow	[✂]	[✂]
Average	**[✂]**	**[✂]**

Source: Pets at Home response to RFI13, Annex 008.

3.319 We reviewed the information obtained from the other LVGs and noted:

(a) CVS had budgeted total accounting losses for its three greenfield sites of [✂].[369]

[365] Pets at Home response to the CMA's Profitability Working Paper page 6
[366] Pets at Home response to the CMA's Profitability Working Paper page 24 paragraph 5.10
[367] Pets at Home response to the CMA's Profitability Working Paper page 22 paragraph 5.10
[368] Pets at Home response to the CMA's Profitability Working Paper page 22
[369] CVS response to RFI3, question 40, Annex 40.3 ([✂]), Annex 40.4 ([✂]) and Annex 40.7 ([✂]). We note also that [✂], while CVS told us [✂]. The inclusion of budgeted losses for [✂] in our analysis would therefore be favourable to CVS and the LVGs. As regards [✂], CVS told us the site [✂] (CVS response to RFI13, paragraph 59).

(b) IVC had originally budgeted a total accounting loss of [✂].[370]

(c) The sites opened by Pets at Home are consistent with those opened by CVS, IVC and Medivet in terms of square footage, facilities (ie number of consultation rooms) and staff numbers.[371]

3.320 We consider the above suggests it is not unreasonable to read-across from Pets at Home's experience in opening greenfield sites to that of other LVGs, given consistency with the accounting losses expected by CVS and IVC,[372] [373] and the similarity in size, facilities and staff between Pets at Home's greenfield sites and those of other LVGs. We consider, therefore, that the profit and loss information obtained from those sites listed in Table 3.20 provides the best available basis for considering the typical start-up losses experienced by the LVGs. In any event, we consider it appropriate to consider the costs of experience, and thereby somewhat efficient, new entry and to avoid capitalising inefficiently incurred costs.

Start-up losses of independent veterinary firms

3.321 In addition, we compared the accounting losses from the six Pets at Home sites to the accounting losses from those independent veterinary firms in our sample in Section 6 below who had opened new clinics in the last five years and separately [✂], an independent medium-sized veterinary chain.

3.322 We asked independent practices about the losses they incurred when opening the practice. Of the 71 small independent practices we contacted, 12 provided information relevant to our consideration of start-up losses. Of those 12, we noted that two respondents provided mobile veterinary services. We excluded these responses from our analysis on the basis that they operated a different business model to that of the LVGs and could reasonably be expected to incur lower losses than a bricks-and-mortar veterinary practice would (their inclusion would therefore skew the results of our analysis downwards). One further respondent opened the practice in June 2024 and, therefore, had little information about actual losses over

[370] [✂].
[371] Pets at Home response to RFI3, question 40 showed the average square footage of the sites included in Table 3.14 was approximately 1,400 square feet. [✂] (Medivet response to RFI3, question 40). The same responses showed that Pets at Home sites had three to four consultation rooms plus one to two theatres, while CVS sites had [✂] consultation rooms, [✂], and Medivet sites had [✂] consultation rooms. Average FTE staffing numbers at the Pets at Home sites was: 5.3 in year one, 6.0 in year two, 7.1 in year three, 8.0 in year four and 8.7 in year five. These numbers compare favourably with the available information from the other LVGs: [✂], while Medivet told us its sites opened with only [✂]. CVS submitted the latest available staffing information for its sites which showed its [✂] site had [✂] FTE staff in year one and its [✂] site had [✂] FTE staff in year three.
[372] As regards the other LVGs: Linnaeus has [✂] in operation, which opened in November 2024. We exclude [✂] from our analysis for the same reasons as concern our analysis of greenfield marketing costs. Medivet was able to provide information relating only to [✂] opened since [✂] and combined monthly and yearly P&L data in compiling its response. We have concerns that this approach may have led to double counting and do not have sufficient confidence in the information provided to include it in our analysis. [✂]. [✂] both are specialised referral centres.
[373] We note the quantum of Pets at Home site losses will be affected by any management fee costs charged by the Pets at Home Group., We note however that the losses in Table 3.14 are in any event consistent with those expected by CVS and IVC, and greater than those of the independent practices from which we received start-up loss information.

the whole start-up period. We excluded this response from our analysis for this reason, leaving a population of nine responses.

3.323 We recognised that vets working in independent practices might receive (at least part) of their remuneration through profit-sharing rather than as salary payments and asked all respondents to provide the salary level equivalent to the role carried out by owners who worked in the business. In each case, we adjusted the P&L data provided to reflect market-rate salaries. On this adjusted basis:

(a) Two of the nine practices had generated profits in the first year of operation [✂].

(b) A further four practices had incurred losses in only the first year of operation [✂].

(c) One practice incurred losses in the first two years of operation only, [✂].

(d) The remaining two practices continued to incur losses, one having been in operation for two years and the other in operation for three years [✂].

3.324 In Table 3.21 below, we show the adjusted P&L information of each of the independent practices included in our analysis:

Table 3.21: Annual losses incurred by independent practices

	Year 1	*Year 2*	*Year 3*	*TOTAL*
Adjusted site-level P&L information:				
[✂]	[✂]			[✂]
[✂]	[✂]	[✂]		[✂]
[✂]	[✂]			[✂]
[✂]	[✂]			[✂]
[✂]	[✂]			[✂]
[✂]	[✂]			[✂]
[✂]	[✂]			[✂]
[✂]	[✂]	[✂]		[✂]
[✂]	**[✂]**	**[✂]**	**[✂]**	**[✂]**

Source: Independents responses to RFI and CMA analysis.

3.325 In addition, we also received information from [✂] on the practices it has opened in the last five years. [✂] opened [✂] in this period. As [✂] of these practices were opened in 2024 it is not possible to quantify their start-up losses and we have excluded them from our analysis. For the remaining five we have used the clinic's EBIT losses on an accounting basis in each year until the breakeven point. As this is an independent group, (as opposed to single or a small number of practices) we have not made any adjustment for owners working in the clinics. We have, however, adjusted EBIT to include an additional allocation of central management costs, based on [✂] of each clinic's annual turnover.[374]

[374] [✂].

3.326 The results of this are set out in Table 3.22 below;

Table 3.22: Actual losses for [✂]

	Year 1	*Year 2*	*Year 3*	*TOTAL*
Adjusted site level P&L Information				
[✂]	[✂]			[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]			[✂]
[✂]	[✂]	[✂]		[✂]
[✂]	[✂]	[✂]		[✂]
[✂]				[✂]

Source: [✂] responses to RFI of 2nd July 2025] and CMA analysis.
[✂]

3.327 As shown by Table 3.22 the average accounting start-up losses for the sample of independent veterinary firms are [✂] lower than those of Pets at Home. Table 3.22 shows that the accounting average start-up losses for [✂] greenfield sites are [✂] above the average losses of the six Pets at Home sites.

3.328 However, we also note that the fit-out costs (based on 2024 values) of the sample of independents and [✂] (as per paragraph 3.49) are [✂] and [✂] of the fit-out costs of Pets at Home (as per Table 3.4 above) on a per square foot basis. On this basis, in our view, it is likely that economic losses for these practices are likely to be lower than those of Pets at Home.

3.329 In summary, through our comparison of the accounting losses of the six Pets at Home clinics to those of other LVGs, independents and [✂] it is our view that these are representative of the start-up losses of efficient greenfield sites.

Economic start-up losses calculation methodology

Summary

3.330 To calculate the economic start-up losses for each of these six clinics we have taken their accounting Earnings Before Interest and Tax (EBIT) and made adjustments to the profit and loss to calculate their economic EBIT. In each year, we have then adjusted this figure to account for the opportunity cost of both the capital employed in the clinics and the cumulative losses to date. We then continue this until the point at which the clinics breakeven in year on this basis.

3.331 To do so a clinic must effectively generate sufficient EBIT to both cover both the expected return on its capital employed (so in effect earn a return equivalent to (or in excess of) the Cost of Capital of 9%) to which is added the opportunity cost of cumulative losses to date. We set out below in more detail each of the steps in this calculation.

Adjustments to EBIT

3.332 The starting point for our economic losses calculation for each clinic was the accounting earnings before Interest and Tax (EBIT) as per paragraph 3.2.

3.333 We then adjusted this figure to reflect the impact of Pets at Home's joint venture model with its 'practice owner' vets. Pets at Home stated that an adjustment should be made to reflect that, compared to a salaried practice lead, owner operator vets typically take a lower salary to invest in the business and earn dividends later.[375] Pets at Home suggested an adjustment of [✂] per clinic to reflect this.[376] However, as in our view, a JV owner starting a new clinic would not be earning the equivalent of a clinical director, we made an adjustment [✂] of £[✂].

3.334 Pets at Home also stated that an adjustment should be made to remove the [✂] and instead replace these with an allocation of central costs.[377] This reflects the fact that these [✂]. This adjustment was made on the basis of figures supplied by Pets at Home.[378] As Pets at Home did not provide the data for 2024 we have made no adjustment in this year for each of these clinics.[379]

3.335 We then made further adjustments to the EBIT to reflect the difference between economic and accounting profitability. First, we removed the rental cost in relation to leasehold properties and replaced this with the IFRS 16 amortisation charge (see paragraph 3.22) provided by Pets at Home.[380] [381] As Pets at Home did not provide the data for 2024 we have made no adjustment in this year for each of these clinics. As set out in paragraph 3.339 below and our assessment under the sub-heading 'Leasehold property' above, in our view, the economic value of leasehold assets is best reflected by valuing these leases according to IFRS 16 methodology. This adjustment therefore aligns the EBIT calculation with our calculation of the capital employed in the clinics.

[375] Pets at Home response to the CMA's Profitability Working Paper at page 24.
[376] Annex 002 to Pet's at Home's response to the CMA's Profitability Working Paper.
[377] Pets at Home response to the CMA's Profitability Working Paper page 22.
[378] Annex 002 to Pet's at Home's response to the CMA's Profitability Working Paper.
[379] Were we to apply the 2023 adjustments for leasehold amortisation and management fees to 2024 this would result in a 4% reduction to the start-up losses per clinic from £211,173 to £204,324.
[380] These figures were provided by Pets at Home in Annex 002 to Pet's at Home's response to the CMA's Profitability Working Paper.
[381] Annex 002 to Pet's at Home's response to the CMA's Profitability Working Paper.

3.336 Second, we removed the accounting deprecation in relation to fit-out costs and replaced this with our calculation of the economic depreciation for these assets. As set out in paragraphs 3.12 and 3.16 we agreed with the LVGs' view that the accounting life of many of their assets (including those represented by our fit-out methodology) does not reflect the economic life of the assets on their balance sheet which is likely to be much longer. As a result, from an economic profitability perspective, the accounting values of these assets are likely to be undervalued on the balance sheet and the depreciation charge (which is calculated based on the accounting life) correspondingly overstated in the profit and loss (assuming the assets are not yet fully depreciated). We have calculated an economic depreciation charge by depreciating the gross value of the fit-out costs and additions to the clinic on a straight line basis assuming an economic life of 16 years (see paragraphs 3.88 to 3.92 above). We have assumed that all of the depreciation charge in the profit and loss of the clinics relates to the fit-out assets. We therefore remove all the accounting depreciation in the EBIT and replace this with our calculation of the economic depreciation charge. Again, this adjustment aligns the economic EBIT calculation with our calculation of the capital employed in the clinics.

Opportunity cost of capital employed

3.337 To understand the opportunity cost of the capital invested in the clinic we first need to determine the value of the capital invested in the clinic each year. The capital invested in the clinic can be split into four categories

(a) **Tangible assets** Broadly this will include any leasehold improvements made to the clinic, fixtures and fittings and clinical equipment and most other assets that are not included in the categories below. Assets purchased on finance leases will not be included as generally these will not be capitalised in the accounts.

(b) **Leasehold property assets** All six clinics operate from leasehold properties. We therefore need to take account of the economic value of these leases.

(c) **Intangible assets** Clearly the purpose of the start-up losses approach is to calculate a value for the intangible assets. However, as the intangible assets are effectively represented by the losses, through calculating the opportunity cost of the cumulative losses (as per paragraphs below) we are in effect calculating the opportunity cost of the intangible assets invested in the clinic.

(d) **Other assets** This primarily consists of working capital

(e) We discuss each of these categories in more detail below.

3.338 For tangible fixed assets we have used the fit-out costs and capital expenditure in each year provided by Pets at Home[382]. To calculate the closing position at the end of each year we have taken the opening assets (or in the case of the first year the original fit-out costs) added any additions in the year and then subtracted the economic depreciation costs as calculated in paragraph 3.336.

3.339 For leasehold assets, as discussed in paragraph 3.29 above, in our view the economic value of these is assets is best reflected through their IFRS 16 values. We therefore used the IFRS 16 year-end values of the leases for each of these clinics provided by Pets at Home.[383]

3.340 The other assets of these clinics would largely comprise working capital and any assets held under finance leases that have not been capitalised by Pets at Home. We note as all the clinics operate from leasehold properties there are no freehold property assets. To provide a proxy for value of other assets in each of these clinics we took the total value of Pets at Home's other assets in 2020 to 2024 and divided this by the total number of Pets at Home's clinics in each year to provide an average value per clinic. [✂][384] [✂].

3.341 To calculate the opportunity cost of the capital employed in each clinic in each year we took a simple average of the opening and closing positions each year and applied the 9% cost of capital rate to this.

Opportunity cost of losses

3.342 Similar to capital employed, if the LVGs did not have to fund the losses in the early stages of the clinics start-up phase then they could instead invest their funds elsewhere (or return it to investors). LVGs would seek a return at least equivalent to their cost of capital. We have therefore included in our calculation of start-up losses an allowance for these forgone returns.

3.343 To calculate the opportunity cost of the losses in each year we must first determine which losses to include. For each clinic we have calculated the losses as follows;

(a) To reflect the average losses for the current year we have taken half of the Adjusted EBIT figure as per paragraphs 3.332 to 3.336. Our assumption is that the loss accrues evenly over the year hence the average loss (or funding requirement) for the year is half the total losses figure. We exclude the

[382] Pets at Home response to RFI13, Annex 008.
[383] Annex 002 - Calculations supporting Pets at Home Profitability WP response.xlsx to Pet's at Home's response to the CMA's Working Paper on Profitability.
[384] CMA Analysis of Pets at Home financial submissions.

opportunity cost of the capital employed in the year as this is calculated separately.

(b) We have then added the cumulative losses from prior years, being the adjusted EBIT losses plus the prior years' opportunity costs of capital employed and opportunity cost of losses.

3.344 Finally, similar to the capital employed calculation, we calculate the opportunity cost of the losses using the LVGs' cost of capital of 9%.

Total calculation of losses

3.345 The total loss for each year is therefore the sum of the following

(a) The adjusted EBIT (as per paragraphs 3.332 to 3.336 above).

(b) The opportunity cost of the capital employed (as per paragraphs 3.337 to 3.341 above).

(c) The opportunity cost of the cumulative losses (as per paragraphs 3.343 to 3.344 above).

3.346 For each clinic we then calculate the losses for each year until the point at which they breakeven based on the calculation directly above. To calculate the total losses to be capitalised we then take the sum of the average losses over each of the first five years of clinics. This average is calculated by taking the sum of the losses in each year and dividing by the total number of clinics (six).

3.347 Table 3.23 below shows how we have used this information to calculate the amount that might be capitalised for a greenfield site.

Table 3.23: CMA start-up loss estimate (Pets at Home sites)

	Year 1	*Year 2*	*Year 3*	*Year 4*	*Year 5*	*Total*
Actual site level P&L information						
(1) Coalville	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
(2) Whitstable	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
(3) Heanor	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
(4) Cumbernauld	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
(5) Saffron Walden	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
(6) Glasgow	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Average across all six sites	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: Pets at Home response to RFI13, Annex 008 and CMA analysis.

3.348 As shown in Table 3.23, based on the information of the LVGs, we calculate total costs to be capitalised of approximately [✂] for a greenfield site.

3.349 We note that Pets at Home had calculated an intangible asset of [✂] per clinic ,as set out in paragraph 3.316 above, applying the start-up losses approach to these six clinics. The primary difference between their calculation and ours is Pets at Home assumed an uplift of [✂] per year for the owner/occupier salary whereas we have applied an uplift of [✂] per year for the reasons set out in paragraph 3.333 above.

3.350 Pets at Home told us that the estimate that we had used for start-up losses per clinic in the PDR (the total in the above table) didn't reflect the costs of any of its enabling works.[385] Enabling works, Pets at Home explained, related to the costs incurred by it to enable local clinics to be placed within retail stores. Examples of enabling work costs included (but were not limited to): building mezzanine levels; installing extra plumbing and electrical work; and fitting out elevators.[386]

3.351 Pets at Home further explained that we had accepted that it was necessary to account for enabling works when estimating the fit out costs of its in-store local clinics and therefore it would be incorrect to omit the associated depreciation and opportunity cost of capital employed in respect of these enabling works when estimating clinic start-up losses. Pets at Home estimated that accounting for these elements of cost increased our estimate for the per clinic start up loss intangible asset by [✂] to [✂].[387]

3.352 We agree with Pets at Home that the cost of its enabling works should be included in our estimate for per clinic start-up losses, given the fact that this estimate is based exclusively on Pets at Home's clinic openings and five of the six openings used in our estimate are in-store clinics. Our estimate for the per clinic start-up loss is therefore now [✂].

Extrapolation across LVG estates

3.353 To ascertain the profitability of the LVGs as a whole, it is necessary to consider how to extrapolate the capitalised amount related to one greenfield site across the estates of the LVGs.

3.354 There are a number of approaches that might be considered, with varying degrees of sophistication and accuracy. The simplest (and least sophisticated) approach would be simply to multiply by the number of sites operated by each LVG in each

[385] Pets at Home response to the PDR, paragraph 4.4 (a).
[386] Pets at Home response to the PDR, paragraph 4.13.
[387] Pets at Home response to the PDR, Tables 4 and 5 at paragraph 4.15.

year. We note this is the approach adopted by CVS, IVC and Linnaeus.[388] While straightforward, such an approach is clearly an oversimplification.

3.355 A more sophisticated approach might instead consider how the LVGs have expanded historically and seek to mirror this in the extrapolation analysis. For example, we understand that veterinary groups might open sites in proximity to other group-owned sites, so that costs may be shared (including sharing of staff). The effect would be that additional sites incur lower costs and lower losses than the originally opened practices. Given this commercial reality, we believe it would be preferable to build out a more sophisticated start-up and expansion model as a means of extrapolating across the estate of each LVG.

3.356 We do not, however, have sufficient information to carry out such an analysis. We note that were we to do so, due to the possible synergies outlined above, it is likely that the intangible assets calculated under this methodology would be lower.

Consideration of useful economic life

3.357 We received limited submissions from the LVGs as to how intangible assets valued on the basis of start-up losses might be amortised (if at all). We note that only IVC addressed this point explicitly and submitted that intangible assets had an indefinite economic life and, in its view, should not be amortised.[389]

3.358 We note that the LVGs are likely to have to incur on-going expenditure in order to avoid the decline of these assets over time – whether that is marketing costs to maintain reputation, or recruitment and training costs to maintain staffing levels. Given this, and in view of the limited evidence on which to base our assessment of useful economic life, we treat these assets as having an indefinite life once acquired and do not amortise. Consistent with that approach, we have also assumed that ongoing maintenance expenditure should be expensed (rather than capitalised) in the year in which it is incurred.

Adjustments to the financial information provided

3.359 Based on the above, if we were to follow an approach based on start-up losses, we would need to adjust the LVGs' financial information in respect of both capital employed and EBIT as follows:

(a) **Capital employed**: capital employed is adjusted for each firm for each year by the value of [✂] for each site operated by the LVG at year-end; and

[388] CVS response to CMA Approach to Profitability and Financial Analysis working paper, page 20. IVC, Proactive submission on the approach to economic profitability analysis, page 40. Linnaeus CVS response to CMA Approach to Profitability and Financial Analysis working paper, paragraph 87.
[389] IVC, Proactive submission on the approach to economic profitability analysis, page 40.

(b) **EBIT**: for simplicity, we have assumed that the total capitalised costs would be incurred in the first year of operation. Considering the asset has been recognised on the balance sheet per the adjustment at point (a), we have added back [✂]to EBIT in the year, for each greenfield site opened in that year. We note that these cost add-backs are only applied for sites which were opened organically rather than acquired.[390] We have also reduced EBIT by [✂] for any sites closed in the year, to reflect the write-off of the asset.

Comparison of the intangible assets under the cost-based and start-up losses approach

3.360 The table below shows the comparison between the intangible assets per clinic calculated under the start-up losses approach and the cost-based approach. As discussed in paragraph 3.239 above, as the workforce intangible asset element of the cost-based approach intangibles is calculated by reference to staff numbers rather than clinic numbers, the total intangible asset per clinic varies between the LVGs. Taking the average difference each year of all the LVGs, the start-up losses approach shows intangible assets to be approximately £90,000 higher per clinic than under the cost-based approach.

Table 3.24: Comparison for each LVG of the estimate for the value of intangible assets expressed on a per clinic basis between the start-up losses based approach and the cost-based approach (£000s)

		2020	*2021*	*2022*	*2023*	*2024*
CVS	Start-up losses approach	[✂]	[✂]	[✂]	[✂]	[✂]
	Cost-based approach	[✂]	[✂]	[✂]	[✂]	[✂]
	Difference	[✂]	[✂]	[✂]	[✂]	[✂]
IVC	Start-up losses approach	[✂]	[✂]	[✂]	[✂]	[✂]
	Cost-based approach	[✂]	[✂]	[✂]	[✂]	[✂]
	Difference	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus	Start-up losses approach	[✂]	[✂]	[✂]	[✂]	[✂]
	Cost-based approach	[✂]	[✂]	[✂]	[✂]	[✂]
	Difference	[✂]	[✂]	[✂]	[✂]	[✂]
Medivet	Start-up losses approach	[✂]	[✂]	[✂]	[✂]	[✂]
	Cost-based approach	[✂]	[✂]	[✂]	[✂]	[✂]
	Difference	[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home	Start-up losses approach	[✂]	[✂]	[✂]	[✂]	[✂]
	Cost-based approach	[✂]	[✂]	[✂]	[✂]	[✂]
	Difference	[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners	Start-up losses approach	[✂]	[✂]	[✂]	[✂]	[✂]

[390] Where sites have been acquired in year, we have included intangible assets at a value of [✂] per site, but we have not made any adjustment to EBIT.

	Cost-based approach	[✂]	[✂]	[✂]	[✂]	[✂]
	Difference	[✂]	[✂]	[✂]	[✂]	[✂]
All LVGs	Weighted average difference	95	93	91	90	89

Source: CMA analysis based on information provided by the LVGs.
Note: Cost-based approach intangible asset relates to customer acquisition asset and workforce asset only ie doesn't include national brand asset.

Summary of our approach to intangible assets

3.361 In the preceding sections, we discussed two different approaches to valuing intangible assets and considered the adjustments that would need to be made to the LVGs' financial information in respect of each.

3.362 While representations received as part of the PDR, our view, taking into account the discussion above, is that the cost based valuation approach is to be preferred. We take this view because the cost based approach is more closely aligned with our Guidelines and, in particular, the need to identify assets that are separate from the general running of the business, and the costs incurred in creating them. Furthermore, the cost based approach aligns with accounting principles in only identifying those items as assets that meet certain criteria. We note that such an approach is consistent with an independent review of the Competition Commission's analysis in the SME Banking Market Investigation, where Sir Bryan Carsberg considered:

(a) *"…the Commission has been reasonable in insisting that the recognition of intangibles should be restricted to assets that are specifically identified and associated with costs incurred".*[391]

3.363 Furthermore, the cost based approach avoids the circularity issues described in paragraph 3.299, whereby if the market is not functioning well (which this analysis aims to help to determine) then profits could be inflated impacting any determination of intangible assets on a profit (or loss-making) approach.

3.364 We used actual costs and revenues to estimate the value of start-up losses, rather than those that might have been expected to arise given normal market trading conditions over the period of review, as that is the information we had to work with. Under our approach to asset valuation, the value ascribed to assets should reflect the value (using deprival valuation principles) the asset is expected to provide in future periods. The desirability of using those costs and revenues that would be expected in a competitive market rather than actual costs and revenues illustrates one of the inherent difficulties in estimating the value of intangible assets using a start-up losses approach.

[391] Report on Certain Issues Arising out of the Report by the Competition Commission on the Supply of Banking: a report for HM Treasury.

3.365 We do recognise, however, that the start-up losses approach takes a quite different approach, one that seeks to place a single all-in-one figure on the value of intangible assets associated with establishing a clinic in a new location, including that (efficiently incurred) expenditure that would not be capitalised under our three criteria asset recognition test. We show the results of the analysis had we instead determined to follow the start-up loss approach on the basis of the methodology set out above. This analysis is included as part of our sensitivity testing in Section 5.

Adjustments to the LVGs' financial information

Introduction

3.366 This section sets out the starting point and subsequent adjustments we made to the LVGs' financial information in order to estimate the ROCEs and economic profits of the UK clinical veterinary services of each LVG.

3.367 We first sought to identify the closest set of statutory financial statements prepared by each LVG that encompassed this activity. For some LVGs (IVC, CVS and VetPartners) these statements included activity relating to farm and equine as well as household pets.

3.368 While the starting point for our analysis for each LVG was different in terms of scope of the activities covered by that set of financial statements, the approach to adjusting that information was common in terms of what we were seeking to achieve.

3.369 For the first iteration of this analysis, we first asked each LVG to review and update the information we had extracted in terms of consistency in the detail and disclosure across the five financial years. We then made the following types of adjustments to that starting point financial information, relating to scope, relevance, and with the aim of generating meaningful economic profitability information, to the balance sheet and profit and loss statements of the LVGs as follows:

(a) We had invited each LVG to propose adjustments to align the scope of the activity that it had reported within its financial statements so that the adjusted numbers aligned with the scope of its UK clinical veterinary services. We took forward these adjustments into our analysis.

(b) For the balance sheet we did not take forward into the analysis those balances that were either financing items, or related to corporation tax. For the profit and loss we took forward all items up to and including operating profit before interest and tax. We then made adjustments, primarily relating to profit and loss items but also to associated balance sheet items, where we

judged the activity not to be relevant to our analysis or where adjustments proposed by the LVG were, in our view, wrong in principle.

(c) Finally, we made a set of adjustments, again to both balance sheet and profit and loss items, to update their values where necessary so that they reflected economic cost.

3.370 We set out each of these adjustments in more detail in turn in the following sections.

Focus on in-scope activities

3.371 For some LVGs the closest set of financial statements prepared by each LVG were group financial statements that not only included all its UK clinical veterinary activity but also out-of-scope activities. For other LVGs the closest set of financial statements were entity statements that related to their UK clinical veterinary activities, but which were but one entity in the wider corporate group. We asked each LVG to provide a methodology statement, including sources for input information used, to establish the quantum for each set of adjustments.

3.372 We asked the LVGs to exclude the following:

(a) The elements of any non-UK activities, whether veterinary services or not

(b) The elements of crematoria (but not the revenues received from, or the direct costs of, the retailing of cremations by local clinics).

(c) The elements of laboratory services (but not the revenues received from, or the direct costs of, the retailing of diagnostic tests by local clinics).

(d) The elements of retail online pharmacy (but not the revenues received from the sale of medicines via local clinics).

Focus on operating capital employed

3.373 We assess the profitability on a pre-interest and corporation tax basis. We therefore excluded any items which were related to financing or corporation tax. This approach meant we excluded the following items:

(a) loans, borrowings and lease liabilities;

(b) amounts payable to and receivable from branch partners;

(c) current and deferred tax assets and liabilities; and

(d) cash and cash equivalents (and any overdrafts) as this represents a means of funding the capital employed of the business rather than being an operational balance.

3.374 The focus of our analysis is on the profitability of the in-scope activities rather than the trading in the businesses which undertake those activities, and we therefore excluded balances relating to the acquisition and disposal of veterinary practices. This approach meant we excluded the following items:

(a) amounts payable in consideration of practice acquisitions, such as purchase consideration in all its forms, for example deferred consideration, earn-out costs, and business purchase and disposal transaction costs;[392]

(b) gains and losses incurred on disposal of practices;

(c) corporate restructuring costs stemming from change in ownership; and

(d) investment in subsidiaries (only relevant to entity financial statements) – balances relating to the funding of the purchase of businesses that undertake (out of scope) activities.

3.375 In response to our Profitability Working Paper, and noting that we had stripped out all cash balances, Pets at Home told us that we had adopted a very strong assumption and that it needed to hold a level of cash for its day-to-day operations. [393] We acknowledge that many firms choose to operate with balances in a current account, but it is also possible for them to operate with an overdraft too. It will also be the case that firms with many sites will also operate a treasury function to minimise use of current account funds. We therefore continue to implement the normal practice of the CMA here, which is to exclude all cash balances. This approach also ensures that we adopt a consistent approach across all LVGs in this regard, given that they will not all take the same approach regarding managing their current account alongside any surplus funds.

Adjustments by CMA to update values to reflect economic costs

3.376 Finally, we made a set of adjustments, to both balance sheet and profit and loss items, to update their values where necessary so that they reflected economic cost. We sought to take a materiality-based approach to this exercise whereby we revised only those values which a) were not likely to reflect current opportunity

[392] We would also ideally seek to exclude amounts payable to third parties associated with the acquisition and disposal of practices such as legal and consultant fees (including costs incurred in dealing with the CMA for merger control) but the LVGs did not provide us with this level of detail to enable us to do this. We expect that the amounts involved are relatively small and any adjustment would not make a material difference to our assessment.
[393] [✂].

costs (the costs that an efficient new entrant would incur) and b) whose adjusted value was likely to influence our results significantly. The following is of note:

(a) Leasehold buildings are one of the most significant elements of the LVGs' capital employed with almost all buildings leased, typically for 15 years with five year rent reviews. On the basis that leases are essentially the purchase of five-year fixes for property space, we retained the existing right of use valuations for leasehold buildings (see sub-heading 'Tangible fixed assets' – 'Leasehold property').

(b) We updated the values for clinic fit-out and equipment (in capital employed and depreciation charge) relating to both owned assets and right of use (leased) assets, using cost information provided by the LVGs on their new clinic openings in the past five years (see sub-heading 'Fit-out methodology').

(c) We excluded goodwill and associated impairment charges.

(d) We revalued other intangible assets, with the exception of software.

Approach taken to extending the analysis to include the results for FY2025

3.377 We asked each LVG to provide us with an Excel workbook with figures extracted from the relevant set of statutory financial statements for the financial year ending 2025 equivalent to those we had extracted from prior year financial statements. (We had used the figures we had thus extracted to populate an Excel workbook for each LVG, which we had then asked each respective LVG to review.) We also asked each LVG to provide any adjustments to these figures made on the same basis as previously requested and submitted in response.[394] We also asked that, to the extent that any figures previously provided in respect of financial year 2024 which had not been fully finalised when the LVG had submitted its response to our original request, to provide us with updated figures.

3.378 We then made the same set of adjustments for each LVG for FY2025 that we had made for FY2020 to FY2024 as described in paragraphs 3.376(b) to 3.376(d) above. In order to simplify the extension of the analysis to include FY2025, we, however, neither generated estimates of 'as at FY2025' values for 'fit out costs' tangible fixed assets (and associated depreciation) nor estimates of 'as at FY2025' values for intangible asset values for each individual LVG in the way we had generated these estimates for FY2020 through to FY2024. We instead we used the estimates for these two asset categories that we had used for FY2024. Where, however, the reported values from the financial statements for any individual LVG (both in terms of carrying values for balance sheet items and depreciation charges for profit and loss items) had increased between FY2024 and FY2025, we

[394] See subsection Adjustments to the LVGs' financial information.

increased the FY2024 current value by the same amount to generate the FY2025 estimates. In the case of Pets at Home, who had provided us with estimate for the value of right of use assets for its leasehold assets on an IFRS basis we used its FY2024 values.

3.379 This approach to implementation meant that we used estimates for the fit out costs (and related depreciation charges) and intangible fixed assets (both the cost-based approach and the start-up losses approach[395]) that were as least as high as they have been estimated for FY2024.

[395] As described previously, we did increase our estimate of the value of the start-up losses used in one of our sensitivities and that adjustment affects the results across all periods analysed.

4. The LVG profitability results

4.1 In this section we present the profitability results for the LVGs.

4.2 We used ROCE and economic profits in analysing the profitability of the LVGs. 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 cost of capital (we call this normal return 'capital employed opportunity cost'). Economic profits are calculated as operating profit, or EBIT, less the product of the cost of capital multiplied by capital employed. In other words, we effectively subtract the profit expected from a (normal) market-based return on the assets from the operating profit figures.

4.3 The resulting measure of profitability (that is, economic profits) is, therefore, based on the same building blocks as ROCE and simply expresses returns above or below the cost of capital in absolute amounts. We express economic profits in £millions.

4.4 We used a cost of capital of 9.0% when calculating economic profits, which is the mid-point of our pre-tax cost of capital range of 7.5% to 10.5%. We present ROCE results over the six years to 2025 and economic profits over the five years to 2024 as we had not extended the analysis for the cost of capital into a sixth year.

4.5 For completeness, we also present EBIT and EBITDA margins as percentages of revenues.

Results tables for the LVGs

4.6 In this section we set out the results of our analysis for each LVG in turn. The detailed calculations underlying the results are set out in Annex B, comprising tables showing summary adjusted balance sheets and adjusted operating profit and loss statements for each LVG. We present the results of the individual LVGs in the following tables.

UK veterinary services which are local clinics

CVS

Table 4.1: ROCE, economic profits and margins for CVS in the base case (all figures in £ millions except where expressly indicated)

	As at June / year to June	*2020*	*2021*	*2022*	*2023*	*2024*	*2025*	*Total*
ROCE	Closing / average capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Return on capital employed (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
ECONOMIC PROFITS	EBIT (as above)	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Cost of capital for period (% per year)	*9.0*	*9.0*	*9.0*	*9.0*	*9.0*	*na*	
	Capital employed opportunity cost	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Economic profit	[✂]	[✂]	[✂]	[✂]	[✂]	**na**	
MARGINS	Revenues	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on information provided by the LVGs.
Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

4.7 Our analysis indicates that CVS has [✂]. The average ROCE across the six-year period was [✂]%. It has earned [✂].

IVC

Table 4.2: ROCE, economic profits and margins for IVC excluding Vets Now in the base case (all figures in £ millions except where expressly indicated)

	As at September / year to September	*2020*	*2021*	*2022*	*2023*	*2024*	*2025*	*Total*
ROCE	Closing / average capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Return on capital employed (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
ECONOMIC PROFITS	EBIT (as above)	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Cost of capital for period (% per year)	*9.0*	*9.0*	*9.0*	*9.0*	*9.0*	*na*	
	Capital employed opportunity cost	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Economic profit	[✂]	[✂]	[✂]	[✂]	[✂]	**na**	
MARGINS	Revenues	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on information provided by the LVGs.
Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

4.8 Our analysis indicates that IVC has earned [✂] in the five-year period to 2024. The average ROCE across the six-year period was [✂]. It has [✂]. There is a similar pattern in terms of [✂].

Linnaeus

Table 4.3: ROCE, economic profits and margins for Linnaeus local clinics in the base case (all figures in £ millions except where expressly indicated)

		2020	*2021*	*2022*	*2023*	*2024*	*2025*	*Total*
ROCE	Closing / average capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Return on capital employed (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
ECONOMIC PROFITS	EBIT (as above)	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Cost of capital for period (% per year)	*9.0*	*9.0*	*9.0*	*9.0*	*9.0*	*na*	
	Capital employed opportunity cost	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Economic profit	[✂]	[✂]	[✂]	[✂]	[✂]	**na**	
MARGINS	Revenues	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on information provided by the LVGs.
Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

4.9 Our analysis indicates that Linnaeus has earned returns [✂].

Medivet

Table 4.4: ROCE, economic profits and margins for Medivet in the base case (all figures in £ millions except where expressly indicated)

		2020	*2021*	*2022*	*2023*	*2024*	*2025*	*Total*
ROCE	Closing / average capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Return on capital employed (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
ECONOMIC PROFITS	EBIT (as above)	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Cost of capital for period (% per year)	*9.0*	*9.0*	*9.0*	*9.0*	*9.0*	*na*	
	Capital employed opportunity cost	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Economic profit	[✂]	[✂]	[✂]	[✂]	[✂]	**na**	
MARGINS	Revenues	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on information provided by the LVGs.
Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

4.10 Our analysis indicates that Medivet has [✂] across the five-year period to 2024 for which we have determined a cost of capital, with the average ROCE across the six-year period to 2025 being [✂]. In line with ROCE, [✂].

Pets at Home

Table 4.5: ROCE, economic profits and margins for Pets at Home in the base case (all figures in £ millions except where expressly indicated)

	As at March / year to March	*2020*	*2021*	*2022*	*2023*	*2024*	*2025*	*Total*
ROCE	Closing / average capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Return on capital employed (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
ECONOMIC PROFITS	EBIT (as above)	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Cost of capital for period (% per year)	*9.0*	*9.0*	*9.0*	*9.0*	*9.0*	*na*	
	Capital employed opportunity cost	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Economic profit	[✂]	[✂]	[✂]	[✂]	[✂]	**na**	
MARGINS	Revenues	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on information provided by the LVGs.
Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

4.11 Our analysis indicates that Pets at Home [✂] in the five-year period to 2024. The average ROCE across the six-year period to 2025 was [✂]%. [✂]. In line with ROCE, [✂]. Pets At Home submitted that around [✂]% of the estimated economic profits '(nearly £[✂] over the last five years [to 2024], when expressed in pound terms) is simply driven by Pets at Home operating space-efficient FOPs'.

VetPartners

Table 4.6: ROCE, economic profits and margins for VetPartners in the base case (all figures in £ millions except where expressly indicated)

	As at June / year to June	*2020*	*2021*	*2022*	*2023*	*2024*	*2025*	*Total*
ROCE	Closing / average capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Return on capital employed (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
ECONOMIC PROFITS	EBIT (as above)	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Cost of capital for period (% per year)	*9.0*	*9.0*	*9.0*	*9.0*	*9.0*	*na*	
	Capital employed opportunity cost	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Economic profit	[✂]	[✂]	[✂]	[✂]	[✂]	na	
MARGINS	Revenues	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on information provided by the LVGs.
Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

4.12 Our analysis indicates that VetPartners has [✂] in the five-year period to 2024. The average ROCE across the six-year period was [✂]%. [✂].

UK veterinary services which are not local clinics

4.13 We analysed the profitability of two LVGs whose UK veterinary services business comprised a material amount of non-local clinic business: Linnaeus, which runs a number of RCVS-specialist led referral centres, and Vets Now, an operation owned by IVC which comprises standalone OOH services and three referral centres. For reasons explained in Annex B, we only present margins information on Vets Now.

4.14 We present the results for each of these operations in the following tables.

Linnaeus

Table 4.7: ROCE, economic profits and margins for Linnaeus referral centres in the base case (all figures in £ millions except where expressly indicated)

	As at December / year to December	*2020*	*2021*	*2022*	*2023*	*2024*	*2025*	Total
ROCE	Closing / average capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Return on capital employed (% per year)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
ECONOMIC PROFITS	EBIT (as above)	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Cost of capital for period (% per year)	*9.0*	*9.0*	*9.0*	*9.0*	*9.0*	*na*	
	Capital employed opportunity cost	[✂]	[✂]	[✂]	[✂]	[✂]	na	
	Economic profit	[✂]	[✂]	[✂]	[✂]	[✂]	na	
MARGINS	Revenues	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBITDA margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	EBIT margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on information provided by the LVGs.
Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable

4.15 Our analysis indicates that Linnaeus' referral centres business has [✂] in the five-year period to 2024.. The average ROCE across the six-year period was [✂]. The ROCE results over this period range from [✂].

Vets Now

Table 4.8: EBITDA, EBIT and margins for Vets Now (all figures in £ millions except where expressly indicated)

	As at September / year to September	*2020*	*2021*	*2022*	*2023*	*2024*	*2025*		*Total*
MARGINS	Revenues	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

EBITDA	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
EBIT	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
EBITDA margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
EBIT margin on revenues (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on information provided by the LVGs.

4.16 Vets Now has [✂] over the period of review ranging between [✂] of revenues, with an average of [✂] based on the draft financial statements received.

Sensitivity analysis

4.17 Our profitability assessment has required extensive revaluation of the fit-out tangible fixed assets of the LVGs and valuation of their intangible assets, using information from a number of sources. We have used certain metrics to extrapolate per clinic estimates across each LVG's total portfolio of clinics to derive estimates for these assets in total for each LVG. In summary, in our base case:

(a) We estimated the value in terms of replacement cost of tangible fixed assets within the local clinics, comprising leasehold improvements, equipment and fixtures and fittings (which we call fit-out costs) based on the cost incurred for the available sample of the LVGs' greenfield fit-outs;

(b) We assumed an average useful economic life for these fit-out cost assets of 16 years.

(c) We estimated the cost of creating the intangible assets we had identified as relevant using cost information obtained from the LVGs and used that as the asset value.

4.18 We have conducted a number of sensitivities on these asset valuations in order to understand the impact these have on the results of our profitability analysis for the LVGs' local clinics.

Tangible fixed assets

4.19 We set out under the heading 'Fit-out methodology' above how we estimated the depreciated replacement cost of refurbishment/fit-outs, and diagnostic and operating equipment using the LVGs' greenfield site costs.

4.20 We focused our sensitivity analysis on our use of fit-out costs of greenfield clinic sites as a proxy for various tangible asset values and associated depreciation. We modelled the following four sensitivities in relation to fit-out costs:

(a) Sensitivity analysis using the fit-out costs of greenfield sites opened by independent veterinary firms (Sensitivity A);

(b) Sensitivity analysis applying a 25% uplift to the average fit out costs per square foot for local clinics and referral centres (Sensitivity B).

(c) Sensitivity analysis lengthening the expected useful life of the clinic fit-out cost assets from an average 16 years to 20 years (Sensitivity C)

(d) Sensitivity analysis shortening the expected useful life of the clinic fit-out cost assets from an average 16 years to 12 years (Sensitivity E)

Sensitivity A: Fit-out costs of greenfield sites opened by independent veterinary firms

4.21 Sensitivity analysis of the fit-out costs of independent veterinary firms is informative as they provide additional evidence as to the level of investment in tangible fixed assets required to enter the market. We note that the fit-out costs of independent veterinary firms are significantly lower than the average fit out costs of the LVGs.

4.22 The sensitivity analysis using the fit-out costs of greenfield sites opened by independent veterinary firms was based on the information we received from the sample of 50 independent veterinary firms (see section 6). We asked a range of questions including details of any greenfield sites opened in the last five years. Within this sample there were nine independent veterinary firms who had opened clinics within this period.[396]

4.23 As these independent veterinary firms provided the opening date as opposed to the date the quote was received for the works (as LVGs had provided for their greenfield sites), we assumed that the quote was received a year and a half prior to opening, to align them with the assumption used for those LVGs who were unable to provide the date of quote acceptance.

4.24 We also assumed that all independent greenfield sites were local clinics rather than referral centres. We therefore only adjusted the LVGs' local clinic estate for the independent fit-out costs. For referral centres we continued to use the average fit out cost per the LVG greenfield referral centres.

4.25 The average fit-out cost per square foot for this group was calculated in the same manner as for the LVGs (as set out in section 3), broadly:

(a) We deflated or inflated the fit-out costs accordingly using CPI to give a data point for each year.

(a) We calculated a weighted average cost per square foot for each year by taking the total cost of all the fit-out activity and dividing this by the total size of all the greenfield sites. This provided values as at the end of each calendar year which were then adjusted for inflation to reflect the financial year end of each of the LVGs.

4.26 The results are set out in Table 4.9 to Table 4.11 below. These show that fit-out costs for independent greenfield local clinics are approximately 35% lower per square foot than the equivalent figures for LVGs. This is reflected in the change in Tangible Fixed Assets and Depreciation for the LVGs' local clinics portfolio with

[396] Independents responses to RFI.

both decreasing by approximately 35% when independent fit-out costs are used. The total impact on tangible fixed assets and depreciation will vary by LVG depending on their mix of local clinics and referral centres.

4.27 As the tangible asset values decrease this has a corresponding impact on depreciation, reducing costs and therefore increasing profits. Depreciation also reduces by approximately 35% for most LVGs.

Table 4.9: Difference in fit-out costs per square foot for greenfield local clinics between those based on independent veterinary firms and LVGs (£ per square foot)

Local clinics fit-out costs per square foot (£)	*FY20*	*FY21*	*FY22*	*FY23*	*FY24*
Independent veterinary firms	166	170	186	199	204
LVGs	258	264	287	308	316
Percentage decrease	*36%*	*36%*	*35%*	*35%*	*35%*

Source: CMA analysis based on financial information from the LVGs and the independents

Table 4.10: Change in local clinic tangible fixed asset valuations for fit-out costs for each LVG when using independent veterinary firm fit-out costs (£ million)

LVG	*FY20*	*FY21*	*FY22*	*FY23*	*FY24*
CVS					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
IVC					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus					
[✂] [✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Medivet					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home					
[✂] [✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on financial information from the LVGs and the independents.
Note: Medivet was unable to provide FY2020 and FY2021 information. We used FY2022 values for these years

Table 4.11 Change in fit-out costs depreciation charges for local clinics based on independent veterinary firm fit-out costs (£ million)

LVG	*FY20*	*FY21*	*FY22*	*FY23*	*FY24*

CVS						
[✂]		[✂]	[✂]	[✂]	[✂]	[✂]
[✂]		[✂]	[✂]	[✂]	[✂]	[✂]
IVC						
[✂]		[✂]	[✂]	[✂]	[✂]	[✂]
[✂]		[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus						
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]		[✂]	[✂]	[✂]	[✂]	[✂]
Medivet						
[✂]		[✂]	[✂]	[✂]	[✂]	[✂]
[✂]		[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home						
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]		[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners						
[✂]		[✂]	[✂]	[✂]	[✂]	[✂]
[✂]		[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on financial information from the LVGs and the independents.
Note: Medivet was unable to provide FY2020 and FY2021 information. We used FY2022 values for these years

Sensitivity B: 25% uplift to the average fit-out costs per square foot for local clinics and referral centres

4.28 In addition to modelling the impact of independent fit-out costs, we also modelled the impact of an increase of 25% on local clinics and referral centre fit-out costs. The purpose of this sensitivity was to show the impact a significant increase in fit-out costs and depreciation would have on our overall assessment. We chose this particular value (ie the 25%) for the percentage increase because Pets at Home had told us that in its experience additional investment in tangible fixed of assets of this magnitude occurred after the initial set-up phase of a new clinic.[397]

4.29 The increase in asset values and costs (through depreciation charges) from this sensitivity are set out in Table 4.12 and Table 4.13 below and show an increase in both tangible assets and depreciation charges of 25% in each year.

[397] As further explained under *Purchase of further tangible fixed assets following clinic opening*. As explained there, for the base case we factored this additional 25% into the assessed value of fit-out cost assets for Pets at Home only. In this sensitivity, however, we increase the value of fit-out cost assets for all LVGs (including Pets at Home) by a (further) 25%.

Table 4.12: Change in Fit-out costs Tangible Asset Valuations based on a 25% increase in fit-out costs (£ million)

LVG	*FY20*	*FY21*	*FY22*	*FY23*	*FY24*
CVS					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
IVC					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Medivet					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on financial information from the LVGs and the independents.
Note: Medivet was unable to provide FY2020 and FY2021 information. We used FY2022 values for these years

Table 4.13: Change in Fit-out costs Depreciation Charges based on a 25% increase in fit-out costs (£ million)

LVG	*FY20*	*FY21*	*FY22*	*FY23*	*FY24*
CVS					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
IVC					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Medivet					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home					

[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on financial information from the LVGs and the independents.
Note: Medivet was unable to provide FY2020 and FY2021 information. We used FY2022 values for these years

Sensitivity C: Lengthening the expected useful life of the clinic fit-out cost assets from an average 16 years to 20 years

4.30 As discussed in 'Tangible fixed assets – Depreciation', we have modelled the impact of changing the assumption on the economic life of the fit-out assets from 16 years to 20 years. In modelling this assumption, we have not adjusted our assumption on the average age of the assets and hence have retained the 50% discount applied to the gross values to calculate the depreciated replacement values. The only adjustment in this sensitivity is therefore to the depreciation charge with the movement shown in the table below.

Table 4.14: Change in fit-out costs depreciation charges based on a change from a useful economic life of 16 years to 20 years (£m)

LVG		*FY20*	*FY21*	*FY22*	*FY23*	*FY24*
CVS						
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
IVC						
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus						
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Medivet						
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home						
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners						
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on financial information from the LVGs and the independents.
Note: Medivet was unable to provide FY2020 and FY2021 information. We used FY2022 values for these years.

Sensitivity D: Shortening the expected useful life of the clinic fit-out cost assets from an average 16 years to 12 years (Sensitivity E)

4.31 As discussed in 'Tangible fixed assets – Depreciation', we have modelled the impact of changing the assumption on the economic life of the fit-out assets from 16 years to 12 years. In modelling this assumption, we have not adjusted our assumption on the average age of the assets and hence have retained the 50% discount applied to the gross values to calculate the depreciated replacement values. The only adjustment in this sensitivity is therefore to the depreciation charge with the movement shown in table below.

Table 4.15: Change in Fit-out costs Depreciation Charges based on a change from a useful economic life of 16 years to 12 years (£ million)

LVG	*FY20*	*FY21*	*FY22*	*FY23*	*FY24*
CVS					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
IVC					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Medivet					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners					
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on financial information from the LVGs and the independents.
Note: Medivet was unable to provide FY2020 and FY2021 information. We used FY2022 values for these years.

Intangible fixed assets

4.32 In addition to the sensitivities we applied to the values for the fit-out cost element of tangible fixed assets, we used our estimate for efficient per clinic start-up losses as the basis for a sensitivity on the value we had placed on intangibles using the cost-based approach. Under sub-headings 'Start-up loss approach' and 'Comparison of the intangible assets under the cost-based and start-up losses

approach' above we set out how we estimated the value of efficient start-up losses for each LVG.

Sensitivity E: Efficient start-up losses approach to valuing intangible fixed assets

4.33 Here we value intangible assets on the basis of using the start-up losses approach to valuing intangibles rather than the cost-based approach, an approach which seeks to place a value only on those assets that are deemed to be separable from the general running of the business.

4.34 We set out the impact of the two different approaches to placing a value on intangibles for each LVG on a per clinic basis at Table 3.24 above.

Results of the sensitivity analysis

4.35 In the following tables we set out the results of the sensitivity analysis. We first set out the base case, totalled for the six LVGs' local clinics to aid comparison with the sensitivity results in the following tables. We present ROCE results over the six years to 2025 and economic profits over the 5 years to 2024.

4.36 We then show:

(a) sensitivity analysis using the fit-out costs of greenfield sites opened by independent veterinary firms (Sensitivity A);

(b) sensitivity analysis applying a 25% uplift to the average fit out costs per square foot for Local Clinics and Referral Centres (Sensitivity B);

(c) sensitivity analysis changing the useful economic life of the fit-out assets from 16 to 20 years (Sensitivity C);

(d) sensitivity analysis changing the useful economic life of the fit-out assets from 16 to 12 years (Sensitivity D); and

(e) sensitivity analysis using the efficient start-up loss approach to valuing intangible assets (Sensitivity E).

Base case

Table 4.16: ROCE, economic profits and margins aggregated across the LVGs' local clinics in the base case (all figures in £ million except where expressly indicated)

		2020	*2021*	*2022*	*2023*	*2024*	*2025*	*Total*
ROCE	Closing / average capital employed	1,546	1,588	1,729	1,927	2,007	2,031	10,828
	EBIT	169	345	422	392	364	398	2,089
	Return on capital employed (% per year)	***11***	***22***	***24***	***20***	***18***	***20***	***19***
ECONOMIC PROFITS	EBIT (as above)	169	345	422	392	364	na	
	Cost of capital for period (% per year)	*9.0*	*9.0*	*9.0*	*9.0*	*9.0*	*na*	
	Capital employed opportunity cost	(139)	(143)	(156)	(173)	(181)	na	
	Economic profit	**30**	**202**	**266**	**218**	**183**	**na**	

Source: CMA analysis based on information provided by the LVGs
Note1: Average operating capital employed is, for 2021 to 2025, an average of opening and closing capital employed values, and for 2020, a year-end figure.
Note 2: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

Tangible fixed assets sensitivity results

Fit-out costs for local clinics based on those for independent local clinics

Table 4.17: Sensitivity A: Tangible fixed asset fit-out costs for local clinics based on those for independent local clinics (all figures in £ million except where expressly indicated)

		2020	*2021*	*2022*	*2023*	*2024*	*2025*	*Total*
ROCE	Closing / average capital employed (base case)	1,546	1,588	1,729	1,927	2,007	2,031	10,828
	EBIT (base case)	169	345	422	392	364	398	2,089
	Adjustment to capital employed	(324)	(348)	(381)	(423)	(441)	(441)	(2,357)
	Adjustment to EBIT	41	42	46	50	54	54	286
	Capital employed reflecting fit out costs of independent local clinics	1,222	1,240	1,349	1,504	1,566	1,590	8,471
	EBIT reflecting fit out costs of independent local clinics	209	387	467	442	418	452	2,376
	Return on capital employed (% per year)	***17***	***31***	***35***	***29***	***27***	***28***	***28***
ECONOMIC PROFITS	EBIT reflecting fit out costs of independent local clinics	209	387	467	442	418	na	
	Cost of capital for period (% per year)	*9.0*	*9.0*	*9.0*	*9.0*	*9.0*	*na*	
	Capital employed opportunity cost	(110)	(112)	(121)	(135)	(141)	na	
	Economic profits	**99**	**275**	**346**	**307**	**277**	**na**	

Source: CMA analysis based on information provided by the LVGs.
Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

Fit-out costs for local clinics increased by 25% over base case

Table 4.18: Sensitivity B: Fit-out costs increased by 25% over base case (all figures in £ million except where expressly indicated)

		2020	*2021*	*2022*	*2023*	*2024*	*2025*	*Total*
ROCE	Closing / average capital employed (base case)	1,546	1,588	1,729	1,927	2,007	2,031	10,828
	EBIT (base case)	169	345	422	392	364	398	2,089
	Adjustment to capital employed	217	234	259	288	300	300	1,598
	Adjustment to EBIT	(27)	(28)	(31)	(34)	(37)	(37)	(193)
	Capital employed reflecting values for fit out costs by 25% over base case	1,763	1,823	1,988	2,214	2,307	2,331	12,426
	EBIT reflecting values for fit out costs by 25% over base case	142	317	391	358	327	362	1,896
	Return on capital employed (% per year)	***8***	***17***	***20***	***16***	***14***	***16***	***15***
ECONOMIC PROFITS	EBIT reflecting values for fit out costs by 25% over base case	142	317	391	358	327	na	
	Cost of capital for period (% per year)	*9.0*	*9.0*	*9.0*	*9.0*	*9.0*	*na*	
	Capital employed opportunity cost	(159)	(164)	(179)	(199)	(208)	na	
	Economic profits	**(17)**	**153**	**212**	**159**	**120**	**na**	

Source: CMA analysis based on information provided by the LVGs.
Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

Weighted average asset life for fit out costs for local clinics based on 20 rather than 16 years

Table 4.19: Sensitivity C: Economic Life for fit out cost assets for local clinics based on 20 rather than 16 years (all figures in £ million except where expressly indicated)

		2020	*2021*	*2022*	*2023*	*2024*	*2025*	*Total*
ROCE	Closing / average capital employed (base case)	1,546	1,588	1,729	1,927	2,007	2,031	10,828
	EBIT (base case)	169	345	422	392	364	398	2,089
	Adjustment to capital employed	-	-	-	-	-	-	-
	Adjustment to EBIT	22	23	25	27	29	29	155
	Capital employed reflecting lengthened weighted average asset life for fit out costs (no change in asset values)	1,546	1,588	1,729	1,927	2,007	2,031	10,828
	EBIT reflecting lengthened weighted average asset life for fit out costs (reduced depreciation)	190	367	446	419	393	428	2,244
	Return on capital employed (% per year)	***12***	***23***	***26***	***22***	***20***	***21***	***21***
ECONOMIC PROFITS	EBIT reflecting lengthened weighted average asset life for fit out costs	190	367	446	419	393	na	
	Cost of capital for period (% per year)	*9.0*	*9.0*	*9.0*	*9.0*	*9.0*	*na*	
	Capital employed opportunity cost	(139)	(143)	(156)	(173)	(181)	na	
	Economic profits	**51**	**224**	**291**	**246**	**213**	**na**	

Source: CMA analysis based on information provided by the LVGs.
Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

Weighted average asset life for fit out costs for local clinics based on 12 rather than 16 years

Table 4.20: Sensitivity D: Economic Life for fit out cost assets for local clinics based on 12 rather than 16 years (all figures in £ million except where expressly indicated)

		2020	*2021*	*2022*	*2023*	*2024*	*2025*	*Total*
ROCE	Closing / average capital employed (base case)	1,546	1,588	1,729	1,927	2,007	2,031	10,828
	EBIT (base case)	169	345	422	392	364	398	2,089
	Adjustment to capital employed	-	-	-	-	-	-	-

	Adjustment to EBIT	(36)	(38)	(41)	(46)	(49)	(49)	(258)
	Capital employed reflecting shortened weighted average asset life for fit out costs (no change in asset values)	1,546	1,588	1,729	1,927	2,007	2,031	10,828
	EBIT reflecting shortened weighted average asset life for fit out costs (increased depreciation)	133	307	381	346	315	349	1,831
	Return on capital employed (% per year)	***9***	***19***	***22***	***18***	***16***	***17***	***17***
ECONOMIC PROFITS	EBIT reflecting shortened weighted average asset life for fit out costs	133	307	381	346	315	na	
	Cost of capital for period (% per year)	*9.0*	*9.0*	*9.0*	*9.0*	*9.0*	*na*	
	Capital employed opportunity cost	(139)	(143)	(156)	(173)	(181)	na	
	Economic profits	**(7)**	**164**	**225**	**173**	**134**	**na**	

Source: CMA analysis based on information provided by the LVGs.
Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

Intangible fixed assets sensitivity results

Intangible fixed assets valued on the basis of start up losses approach rather than cost-based approach

Table 4.21: Sensitivity E: intangible fixed assets valued on the basis of efficient start up losses approach rather than cost-based approach (all figures in £ million except where expressly indicated)

		2020	*2021*	*2022*	*2023*	*2024*	*2025*	*Total*
ROCE	Closing / average capital employed (base case)	1,546	1,588	1,729	1,927	2,007	2,031	10,828
	EBIT (base case)	169	345	422	392	364	398	2,089
	Adjustment to capital employed	253	256	253	255	245	245	1,506
	Adjustment to EBIT	(11)	(13)	(8)	(11)	(9)	(9)	(62)
	Capital employed reflecting efficient start-up losses approach	1,799	1,844	1,982	2,182	2,251	2,275	12,334
	EBIT reflecting efficient start-up losses approach	158	332	414	381	355	389	2,027
	Return on capital employed (% per year)	***9***	***18***	***21***	***17***	***16***	***17***	***16***
ECONOMIC PROFITS	EBIT reflecting efficient start-up losses approach as above	158	332	414	381	355	na	

Cost of capital for period (% per year)	*9.0*	*9.0*	*9.0*	*9.0*	*9.0*	*na*
Capital employed opportunity cost	(162)	(166)	(178)	(196)	(203)	na
Economic profits	**(4)**	**166**	**235**	**184**	**152**	**na**

Source: CMA analysis based on information provided by the LVGs.
Note: We have not computed economic profits for the year ending in 2025 because our assessment of the level of the cost of capital covers the period to 2020 to 2024 inclusive. We have therefore labelled the relevant cells 'na' ie not applicable.

Commentary on the sensitivity analyses

Sensitivity A

4.37 Reducing the tangible fixed asset fit out cost by around 35% to be in line with the figures for independent firms reduces the capital employed and increases operating profits (EBIT), which has the effect of increasing returns on capital employed and economic profits. Under this sensitivity, ROCE over the five-year period to 2024 across all LVG local clinics rises from 19% per year to 28% per year (and across the six year period to 2025 also rises from 19% per year to 28%).

Sensitivity B

4.38 Increasing the tangible fixed asset fit-out costs by 25% over base case increases capital employed and reduces operating profits. The purpose of this sensitivity was to show the impact a significant increase in fit-out costs and depreciation would have on our overall assessment. Under this sensitivity, ROCE over the five-year period to 2024 across all LVG clinics falls from 19% per year to 15% per year (and across the six year period to 2025 also falls from 19% per year to 15% per year).

Sensitivity C

4.39 Changing the economic life of the fit-out costs assets from 16 years to 20 years decreases the depreciation charge by 33%. This reduces costs and reduces profits. Under this sensitivity, ROCE over the five-year period to 2024 across all LVG clinics increases from 19% per year to 21% per year (and across the six year period to 2025 also increases from 19% per year to 21%).

Sensitivity D

4.40 Changing the economic life of the fit-out costs assets from 16 years to 12 years increases the depreciation charge by 33%. This increases costs and reduces profits. Under this sensitivity, ROCE over the five-year period to 2024 across all LVG clinics falls from 19% per year to 17% per year (and across the six year period to 2025 also falls from 19% per year to 17% per year).

Sensitivity E

4.41 Increasing the value of intangible assets to the value ascribed using the efficient start-up losses approach increases capital employed but operating profits are only reduced by a small amount (there is only a small adjustment to the profit and loss account because the value of the intangible assets for the most part is not amortised). Under this sensitivity, ROCE over the five-year period falls from 19%

per year to 16% per year (and across the six year period to 2025 also falls from 19% per year to 16% per year).

Conclusion on sensitivity analyses

4.42 Returns on capital increase when we base the fit-out costs on those of independent veterinary firms (Sensitivity A). Returns also increase when we lengthen the estimate for the weighted average life of fit-out assets to 20 years (Sensitivity C).

4.43 Even when we increase the fit-out costs substantially (Sensitivity B), shorten the estimate for the weighted average life of fit-out assets to 12 years (Sensitivity D) or change our approach to the valuation of intangible assets (Sensitivity E), resulting in an increase in capital employed (under Sensitivities B and E) or an increase in the depreciation charge (Sensitivities B and D), returns on capital over the five year period to 2024 are still materially above the cost of capital in aggregate.

Summary and assessment of the results

Summary

4.44 Over the five / six-year period of our ROCE analysis, we note the following points:

LVGs: Base case

4.45 There is a wide variation in the levels of profitability. However, for the local clinics, four of the six LVGs have consistently earned returns above the cost of capital across the five-year period to 2024: [✂],[398] [✂], [✂]and [✂]. [✂]% per year, with [✂], [✂] and [✂] ROCEs [✂]%, [✂]% and [✂]% per year respectively.

4.46 In line with average ROCE, there is a similar pattern in terms of economic profits: four of the six LVGs have consistently earned substantial economic profits across the five-year period: [✂], [✂], [✂] and [✂].[399]

4.47 [✂] and [✂] earned average ROCE of [✂]% and [✂]% per year respectively across the five-year period of our review.

4.48 For the non-local clinic operations:

(a) Linnaeus' referral centre operations earned average ROCE over the five-year to 2024 period of [✂]% per year, and [✂], which appears to be driven by the [✂] of its referral centres operations relative to its local clinics' operations.

[398] With the exception of 2020.
[399] With the exception of: [✂] earned [✂] economic profits in 2020; [✂] earned [✂] economic profits in 2020.

(b) Vets Now OOH and referral operations earned margins in each period between [✂] and [✂].

LVGs: Sensitivities carried out on local clinic results

4.49 Decreasing the fit-out costs to be those incurred by independent veterinary firms has the effect of increasing average ROCE (by 5-11 percentage points per year across each of the LVGs) over the six-year period to 2025. Lengthening the estimate for the weighted average asset life of fit-out costs also has the effect of increasing average ROCE (by 1-2 percentage points per year across each of the LVGs).

4.50 Increasing the fit-out costs by 25% has a small effect on reducing average ROCE (by 2-5 percentage points per year across each of the LVGs). Only [✂] and [✂] show average returns below the cost of capital, with the other four LVGs' average ROCE between 14% and 29% per year. Likewise shortening the estimate for the weighted average asset life of fit-out costs has the small effect on reducing ROCE (by 2-3 percentage points per year across each of the LVGs).

4.51 Using the efficient start-up loss approach to valuing intangibles has an effect on reducing average ROCE (by 1-6 percentage points per year across each of the LVGs). Only [✂] and [✂] generated returns on average below the cost of capital, with the other four LVGs' average ROCE between 15% and 28% per year.

LVGs: Variation over the six-year period

4.52 All the LVGs have experienced, to varying degrees and timing, an increase in profitability from 2020, into the middle of our five year period under review, and then a decline into 2024 and 2025 (with the exception of [✂] which continued to perform well into 2024 and 2025).[400] More general factors explaining this variation include the impact of the Covid pandemic depressing the market initially in 2020 due to vets being restricted to emergency work only during lockdown, then the ensuing boom in pet ownership and now subdued volumes in the face of the cost-of-living pressures.

Assessment of economic profitability

4.53 Our analysis of economic profitability indicates that, for four of the six LVGs ([✂], [✂], [✂] and [✂]), profits for local clinics over the five year period to 2024 were materially above the estimated cost of capital under the base case. Under each sensitivity, returns for those LVGs were 15% or more on average over the five-year period to 2024.

[400] [✂].

Substantial part of the market

4.54 In terms of share of the market, the four LVGs ([✂], [✂], [✂] and [✂]) generated [✂] revenues out of a total of £13.9 billion for all six LVGs' local clinics over the five-year period to 2024. The six LVGs are estimated to have a share of the total local clinics market (including independent veterinary local clinics) of 60%. Thus the four LVGs earning returns above the cost of capital make up [✂]% of the market (60% x [✂]/ £13.9 billion) - a substantial part of the market.

Persistent

4.55 All four LVGs which generated average ROCE across the five-year period to 2024 of more than the cost of capital have done so persistently: generating a ROCE in all five years in excess of the mid-point for our estimate of their cost of capital with regards to the base case.[401]

4.56 [✂].[402]

4.57 [✂] submitted that '[w]hile a period of higher profitability immediately post Covid is observed (understandably, as the veterinary services market adapted to a significant increase in the number of households caring for a pet), over the entire five-year period under review, profits have been in line with the cost of capital under reasonable assumptions.'[403]

4.58 [✂] queried the ability to extrapolate results based on an unrepresentative sample size, approximately one percent of the total population of clinics given there is a huge range in the size of clinics and services offered.[404]

4.59 [✂] told us it would be incorrect to interpret mechanically economic profit that arose from its innovative approach as 'customer detriment'. There could be legitimate reasons for firms – fiercely competing and innovating – to earn ROCE above their cost of capital even in the medium term. Evidence of some firms earning economic profits was precisely the stimulus for the growth and investment that the CMA were seeking to encourage in light of the Strategic Steer from the government.[405] [✂] added that recent [✂] from the Competition Appeal Tribunal had supported the view that revenues could legitimately exceed economic costs even in the long run.[406]

4.60 We set out previously at paragraph 2.5 onwards the LVGs' views on the particular circumstances of the timeframe of our analysis which covered a mixture of pre-

[401] [✂].
[402] [✂].
[403] [✂] response to the financial analysis and profitability working paper, p 1.
[404] [✂] response to the financial analysis and profitability working paper, p 2.
[405] [✂] response to the financial analysis and profitability working paper, p 2.
[406] [✂] response to the financial analysis and profitability working paper, p 3.

COVID trading, trading during the pandemic, and subsequently trading post-COVID, as well as other factors such as the impact of the availability of veterinary staff following Brexit, and latterly the increase in the cost of living. We examined what the LVGs told us about their financial performance since 2024 to put our findings over 2020 to 2024 into context. We subsequently analysed financial information for each LVG for the 12 month period ending in the calendar year 2025, calculating ROCE for this period as shown in the tables above. We found that the level of ROCE persisted for each of the four LVGs generating economic profits materially above the mid-point of the cost of capital over the period to 2024.

Assessment of potential inefficiencies

4.61 We stated in our profitability approach paper that we proposed to assess potential inefficiencies through an analysis of costs, as well as a review of internal documents, and we invited views from interested parties in our profitability approach paper on whether there were specific cost metrics which would be informative in this assessment.

Parties' views

4.62 CVS told us that it had not seen any evidence to suggest that there were material cost inefficiencies in the veterinary sector; indeed, the relatively unconcentrated nature of the market at a national level, and the strong competition for the acquisition of veterinary sites (on which the acquiring firm must then provide a return for its investors) would create strong incentives to operate in an efficient manner. CVS also told us that the fact that corporate entities had been increasingly likely to acquire independent veterinary practices in the UK over time may well reflect cost efficiencies that can be achieved through the complementarities and cost synergies that exist in a corporate structure (for example in relation to procurement, staff training and management, the provision of OOH and specialist services) compared to a fragmented and vertically non-integrated independent sector.[407]

4.63 CVS also told us that there were strong incentives to optimise costs in order to provide the services that customers want (and were willing to pay for) in a cost-efficient manner; while cost-inflation had been observed in recent years (not least in relation to veterinary professionals' salaries) this simply reflected the increased demand for high quality veterinary services and the resulting importance of hiring and retaining excellent veterinary staff. CVS stated that this could not constitute evidence of inefficiency or any lack of downward pressures on costs. [408]

[407] CVS response to the profitability approach paper, Annex, paragraph 1.2e). [✂].
[408] CVS response to the profitability approach paper, Annex, paragraph 1.2e). [✂].

4.64 CVS also told us that another critical factor in this market was the variation across business models, in particular, independent veterinary firms who were looking to build a practice and sell at retirement may also take their compensation in the form of dividends or rent rather than solely salary – deflating operating costs relative to those that would be seen for an equivalent business that was not owned by vets. CVS also told us that it seemed unlikely that any simple cost-comparison across businesses, sites or regions would provide much insight into the cost-efficiency of those businesses. [409]

4.65 IVC told us that it disagreed with our proposal to attempt to assess potential inefficiencies on both practical and theoretical grounds, and that one of the benefits of corporatisation within the veterinary sector was to increase efficiency.[410]

(a) Practically, given the complexities of the industry and company knowledge required, any efficiency assessment made by the CMA would be highly speculative and not likely to reflect the underlying drivers of cost metrics at a practice or group level;

(b) Theoretically, any competitive market will involve firms with a temporary efficiency advantage over rivals, and these firms should expect to be able to earn a return in relation to this competitive advantage.

4.66 IVC told us that, more generally, one of the benefits of corporatisation within the veterinary sector was to increase efficiency; IVC veterinary practices benefitted from central clinical and business support (for example HR and finance) which reduced the burden on individual clinics and allowed veterinary clinicians to focus on providing veterinary care; additionally, IVC veterinary practices gained access to the latest research and development (invested in heavily by IVC) as well as scale efficiencies for procurement; and these aspects both improved clinical outcomes and reduced costs.

4.67 IVC also told us that it had invested heavily in the salaries, benefits and development for professional staff in recent years in response to the systematic national shortage of veterinary surgeons and nurses in the UK, and to reflect recent high levels of economy-wide inflation, citing the example of IVC's Vet Academy, which provides additional clinical and business development, with the aim to help improve both the recruitment and retention of professional staff within the sector.

4.68 In terms of internal performance monitoring, IVC told us it used a Balanced Scorecard, which looked at clinical, client, people and financial KPIs, with some of the measures cost focussed, giving an indication of efficiency, but could not be

[409] CVS response to the profitability approach paper, Annex, section 6. [✂].
[410] IVC response to the profitability approach paper, paragraphs 7.1-7.5. [✂].

considered in isolation and may not be appropriate for the purposes of the CMA's analysis. It cited the example of payroll: payroll as a percentage of revenue showed how much a clinic was spending on staff costs proportionately, but it did not show the drivers of these costs; costs may be high for a clinic where illness cover is required and there is therefore a reliance on locums. IVC told that its management therefore used its understanding of the business to make judgements in interpreting these metrics and to what extent action was required operationally.

4.69 Linnaeus told us that comparing costs across firms was unlikely to be meaningful because different firms were likely to have different ways of measuring and accounting for costs, and in such a case it would be wrong to conclude that because there were significant variances between firms' costs, some firms must be inefficient. It also told us that such issues were likely to be particularly acute when comparing larger practices with smaller independent practices; smaller independent practices may have lower costs, but their costs were not directly comparable, with smaller practices having lower costs due to a number of reasons, such as lower payroll costs (because some payment might be made through profits ie dividends), [✂], or certain regulations not applying to businesses below a certain size (such as off-payroll tax rules relevant for locums). It told us that all of these factors would tend to result in independent veterinary firms having lower costs, even at individual site level, than LVGs, however, none of these differences provided evidence that the LVGs had inefficiently incurred costs.[411]

4.70 Linnaeus also told us that even within LVGs there could be cost differences that were not explained by inefficiencies; higher quality services (where consumers make informed decisions) and exogenous factors such as location could produce legitimate variations in costs, as well as mix of customer/pet types, services (for example FOP vs referral), treatment types, and size of practice; and corporate structure could also influence costs: for example certain inputs at lower prices due to economies of scope if those inputs were also used in the LVGs' other activities.[412]

4.71 Medivet told us that it saw no basis for any inefficiencies in its operations and incorporated rigorous operational oversight in its operations, and ensuring a high level of efficiency was a focus of its strategy. It told us that there was no reason to believe that it was incurring costs beyond what was strictly necessary for the operation of its business; [✂].

[411] Linnaeus response to the profitability approach paper, paragraphs 116-119.
[412] Linnaeus response to the profitability approach paper, paragraph 120.

4.72 Medivet told us that we should adjust for business conditions that influenced cost levels, and in particular take into consideration the geographical distribution of veterinary sites at each LVG and its comparators.[413]

4.73 Pets at Home told us that it believed any such comparison of costs to assess potential inefficiencies would be very difficult to conduct robustly as there were many legitimate reasons for costs to vary between FOPs (for example business models, regional mix, service/treatment mix etc) including higher costs for higher quality services, and exogenous factors such as locations. Therefore, controlling for all the legitimate reasons for cost variation was very challenging, even if the CMA could get sufficient representative data from a broad mix of market participants.[414]

4.74 Pets at Home also told us that it periodically reviewed the performance of its FOPs and often intervened to address underperforming FOPs, and therefore Pets at Home internal documents discussing underperforming FOPs was likely to be evidence of careful management and pursuit of improving efficiency, rather than a sign of poor performance in the market. It also told us that it closed or restructured many [✂] FOPs in FY20.[415]

4.75 Pets at Home told us that it sought to analyse cost differences between providers and it had assessed internally [✂]. It provided an internal analysis paper which [✂].[416]

4.76 VetPartners told us that any such analysis controlled for factors that drive costs, including factors such as location, size and maturity of practices, and differentiation in the quality of the services offered to clients, as well as an ability to recruit in the local area. It also told us that there were several factors that could result in LVGs running at higher costs relative to independent firms that were unrelated to inefficiencies, relating to IT security, health & safety and environmental standards, and regulatory compliance.[417]

CMA assessment

4.77 We considered the submissions of the LVGs very carefully and considered whether it would be possible to carry out a robust analysis of efficiencies.

4.78 We noted:

[413] Medivet response to the profitability approach paper, paragraphs 50-54
[414] Pets at Home response to the profitability approach paper, paragraphs 4.9-4.13
[415] Pets at Home response to the profitability approach paper, paragraphs 2.13, 2.14 [✂].
[416] Pets at Home response to the profitability approach paper, paragraph 4.14. [✂].
[417] VetPartners response to the profitability approach paper, paragraphs 10 and 11

(a) that all the LVGs had told us that they had seen no evidence of material inefficiencies in the veterinary sector in respect of themselves;

(b) the abilities for the LVGs to realise economies of scale and scope in their business models compared to the independents (for example, efficiencies in purchasing, central functions, staff training and management, provision of OOH services);

(c) that there was a wide variation across the LVGs in terms of a large number of factors, for which it would be very difficult to control: business models, quality of services, geographic location, mix of customer / pet types, services, treatment types, size of practice, and corporate structure.

4.79 For the above reasons we decided not to carry out an analysis of potential inefficiencies. We therefore do not make any adjustments for inefficiency within the profitability analysis of the LVGs.

Benchmarks

4.80 We stated in the Profitability Approach Working Paper that we considered whether broader price and/or profit margin benchmarking may provide useful insight into the extent to which the LVGs' prices and/or profits reflect those that one would expect to see in a well-functioning market. We stated that benchmarking was unlikely to yield robust conclusions, and we therefore proposed not to pursue this avenue of inquiry further. Nevertheless, we invited parties to make submissions on whether there were specific price/profit benchmarks from other countries that we should consider and the extent to which these were comparable with the supply of veterinary services in the UK.

Parties' views

4.81 Four LVGs[418] provided submissions on benchmarks, with the general view that such an analysis would have limited utility, given the difficulty in finding a comparable benchmark:

(a) CVS told us that it agreed with us that it was difficult to conduct truly 'like for like' comparisons against the profitability of FOPs in other countries, given the other respects in which these markets may vary.[419]

(b) Medivet told us that the CMA must adopt a robust methodology to account for country-specific difference, considering among others the following factors: veterinary labour markets, distinction between FOPs and farm animal

[418] Linnaeus and VetPartners did not provide comments on benchmarking in their responses to the profitability approach WP.
[419] CVS response to the profitability approach paper, Annex, . section 1.2

veterinary services, regulatory framework, demand (and any other supply) conditions.[420]

(c) IVC told us that it agreed with us that any price or profit benchmarking to other countries or sectors would face limitations in terms of comparability.[421]

(d) Pets at Home agreed that price and/or margin benchmarking based on firms operating in different countries or sectors was likely to have limitations in relation to comparability with firms supplying veterinary services in the UK.[422]

CMA assessment

4.82 None of the submissions from the LVGs disagreed with our view in the Profitability Approach Working Paper that we should not carry out benchmarking, and therefore we did not pursue this avenue of inquiry any further.

[420] Medivet response to the profitability approach paper, paragraph 66.
[421] IVC response to the profitability approach paper, paragraph 3.20
[422] Pets at Home response to the profitability approach paper, paragraph 4.24

5. The independent firms

Introduction

5.1 In this section we describe our work to understand the financial performance of independent first opinion practices providing veterinary services to household pets. Independent veterinary businesses (those other than the six LVGs) make up approximately 40% of the market and we estimated that there are 667 veterinary businesses, comprising 999 clinics.[423]

5.2 We set out below how we approached the task of understanding the financial performance of such a large and varied group of businesses. First, we adopted a sampling method, approaching 70 independent veterinary firms, to gather information of financial performance. We obtained complete financial data on 36 firms covering 133 FOPs over the period 2021 to 2023. We call this the **CMA dataset**.

5.3 Second, on the suggestion of independent veterinary firm owners we requested data from firms[424] which work closely with the sector. We did this in order to ascertain financial information for larger sample of firms in order to carry out further analysis. Out of the datasets received[425] one dataset contained comprehensive financial information across multiple years for 157 firms, covering 306 sites. We summarise our data gathering process of this **third-party dataset** in the annex at the end of this section.

Approach

5.4 In the Profitability Approach Paper we said regarding smaller independent veterinary businesses:

(a) It was not possible to do a comprehensive analysis of the portion of the market comprising independent veterinary businesses using publicly available data. This was due to the majority of them being small enough to meet small company reporting requirements and therefore filing only abridged or filleted accounts, in which there is no requirement to file a profit and loss account;

[423] Source: We obtained from the Royal College of Veterinary Surgeons (RCVS) a list of all practices in the UK, and checked the list to determine how many practices i) provide in-scope veterinary services and ii) are not owned by one of the LVGs.
[424] From [✂] firms that specialise in the veterinary sector.
[425] One dataset [✂] received contained only [✂] veterinary firms' data for one financial year end for each firm, however, this was across the years 2023 to 2025. A second dataset [✂] contained two financial data points for 88 firms for one year.

(b) Given the limited publicly available data and the fragmented nature of this portion of the market it was not feasible to assess the profitability of every independent vet. Therefore, we said we would take the following approach:

(i) Conduct profitability analysis of all four independent veterinary businesses with ten or more practices (which we call ‘mid-tier’ firms for the rest of this appendix); and

(ii) Adopt a sampling approach for the remaining independent veterinary businesses (which we call ‘small’ independent veterinary firms). This approach would comprise drawing a random sample of 70 small independent veterinary firms, to aim for a total of 50 eligible responses having taken into account non-responses and out-of-scope responses.

(c) Accounting data useful for our intended profitability analysis was generally more readily available and reliable at a firm rather than veterinary practice level. We therefore would analyse profitability at a firm rather than a practice level.

5.5 We also said in the Profitability Approach Paper that:

(a) The smaller veterinary businesses were owner-run, and may not have full-time accountants or bookkeepers, and as a result we considered that the information which we could reasonably collect from the smaller veterinary businesses in our sample was more limited than the information we could collect from the LVGs. We therefore did not attempt to collect asset valuation data from the smaller veterinary businesses, which meant that the information we obtained would be insufficient to calculate a robust ROCE;

(b) We would analyse profit margins of smaller veterinary businesses.

(c) EBIT margins would be used in the first instance, with consideration as to whether earnings before interest, tax, depreciation, and amortization (EBITDA) was more appropriate once we had data on the prevalence of different asset financing strategies and depreciation policies;

(d) To the extent that any smaller veterinary businesses cater to other animal classes such as equine or large animals we would:

(i) consider the need to adopt a de minimis approach (that is, a certain proportion of revenues generated by out-of-scope services) so that we do not exclude rural veterinary businesses disproportionately; and

(ii) take into account the potential impact of out-of-scope activities in our interpretation of our profitability analysis.

5.6 The Profitability Approach Paper also considered the need to achieve a 'like for like' comparison, in instances where:

(a) the vet was also the owner and was remunerated only or partly through their share of the profits; and

(b) FOPs differed in that they either lease assets and/or property for use in their business, compared to businesses that own these assets.

Responses to the Profitability Approach Paper

LVG submissions

5.7 Three of the LVGs provided submissions on the approach to our analysis set out in the Profitability Approach Paper.

5.8 CVS told us that it understood the CMA's desire to assess the profitability of mid-tier and independent veterinary businesses but noted that there were difficulties in assessing its capital employed accurately and it had doubts over how meaningful a simple comparison of margins was.[426]

5.9 Medivet told us that independent veterinary sites may not operate with the same capital intensity as the LVGs, as they may have lower asset bases, and it was therefore inappropriate to benchmark margins from independent veterinary sites against LVGs without the CMA first acquiring evidence on, and correcting for, relative levels of capital expenditure and asset bases. [427]

5.10 IVC noted that the same data challenges we referenced for independent vets were also relevant to LVGs and there was no conceptual reason why the CMA could not have estimated a ROCE for a smaller veterinary business using the same revaluation approaches it would adopt for LVGs. It also said that the CMA would need to make appropriate adjustments to ensure profits margins of smaller veterinary businesses were comparable to LVGs (for example, reflecting different accounting approaches).[428]

5.11 IVC also stated that the same asset valuation issues applied to independents as they did for LVGs.[429] It noted that if the CMA did assess profitability by comparing the margins of the independents to the calculated 'normal' margin required by the LVGs, it was vital the estimate for the cost of capital used as a benchmark

[426] CVS' response to the profitability approach paper, pp 25-26, [✂].
[427] Medivet's response to the profitability approach paper, p 11, [✂].
[428] IVC response to the profitability approach paper, p 39, [✂].
[429] Specifically, one of the main issues with IVC's asset register is that it has been inherited from independents who do not have processes in place to record data properly.

reflected the in-scope activities and the accounting approach used by independents was considered.[430]

CMA assessment

5.12 We considered that:

(a) an assessment of profitability based on returns on capital employed (i.e. ROCE) would need to reflect accurate understanding and valuation of capital employed, including expenditure and accounting treatment;

(b) to do so accurately would require a level of detailed information that independent veterinary businesses would be unable to provide to us within the response times necessary for our analysis;

(c) we would have been unlikely to have received a sufficient number of responses to such a detailed information request, and it would have been unlikely to have been sufficiently accurate and detailed; and

(d) requesting such an amount of detailed information would have been a disproportionate burden on those businesses given that our focus for the ROCE analysis was the six largest firms in the market.

Analysis of CMA dataset

Overall approach

5.13 We contacted 70 independent veterinary firms, and of these firms, three mid-tier[431] and 33 small independent veterinary firms[432] had available financial information over financial years 2021 to 2023 to analyse their performance.

5.14 For both mid-tier and small independent veterinary firms, we made the following adjustments to achieve a 'like for like' comparison. For each of the adjustments we made for the salary and rent costs, we based our estimate on the available data but acknowledge that there may be regional variations which we have not taken into account in our analysis.

[430] IVC response to the profitability approach paper, pp 39-40, [✂].
[431] After the publication of the Profitability Approach Paper we discovered that there are five mid-tier firms in the UK (according to our criterion of having ten or more sites), rather than the four mentioned in the Profitability Approach Paper. See Appendix A for details.
[432] 56 independent veterinary firms provided data, however, of these only 33 had available financial data over the period 2021 to 2023, with many being start-ups. We had previously analysed data from 34 independents in the Profitability Working Paper, however, we found that one of these firms was not a local clinic but instead conducted home visits and has therefore been removed from the sample.

Staff remuneration

5.15 We noted that it was often the case that where the vet was also the practice owner, the vet would not be remunerated by a salary, or would draw a lower salary alongside a share of the profits. This meant that the costs would be lower, and profits accordingly higher, than would be the case were the vet / practice owner paid a salary at market rates.

5.16 Pets at Home noted that an independent practice owner may not receive the same pay as they would within a corporate model, choosing to take the risk of 'pay' in dividends and ultimate exit value, rather than as a salaried senior employee. Pets at Home noted this was likely to have lowered the apparent labour costs in the P&L and to have overstated the practice-level profitability.[433]

5.17 Medivet said that our proposed approach was likely to underestimate the comparable salary of independent vets who own their clinics, as independent vets were free to choose how they are paid, and will receive tax advantages from taking pay in the form of dividends or capital gains rather than wages. It noted that this could overestimate both their efficiency and profitability compared to corporates, distorting any comparisons unless the CMA undertook appropriate adjustments. [434]

5.18 Linnaeus told us that, in its experience, one of the reasons smaller firms had lower costs is because they were often owned by one or more vet and these vets may prefer to have paid themselves through profits rather than a high salary.[435]

5.19 IVC noted that the CMA needed to appropriately account for the fact that many 'owner vets' paid themselves a below market rate salary and received their remuneration via dividends and/or capital on sale. It noted that this understated costs in the P&L so when splitting out any dividend payments, salary costs also needed to be adjusted.[436]

5.20 We recognised the need to adjust for independent vets taking remuneration through profit-sharing rather than salaries (or a mix of profit-sharing and low salaries) in our profitability approach paper. To adjust for this, we asked all respondents to provide the salary level equivalent to the role carried out by owners who also worked in the business. We calculated an average of these salaries, then added Employer NIC and pension contributions to arrive at an estimated equivalent cost to the business of approximately £80,000. Where an owner worked in an independent veterinary business but was not salaried (or had a very low

[433] Pets at Home's response to the profitability approach paper, para 3.11, [✂].
[434] Medivet's response to the profitability approach paper, p 11, [✂].
[435] Linnaeus' response to the profitability approach paper, p 30, [✂].
[436] IVC response to the profitability approach paper, p 39, [✂].

salary), this equivalent cost was added to their cost base for our assessment of profitability.

Rental costs

5.21 We noted that it was often the case that the practice owner personally owned the property from which the business was carried out, and did not charge rent to the FOP. This meant that the costs would be lower, and profits accordingly higher, than would be the case were the vet / practice owner to charge rental to the FOP at market rates.

5.22 To adjust for this, we asked all respondents for their rental costs and the size of their sites. Using this, we calculated an average annual rental cost per square metre of £149. For those independent veterinary businesses that owned their property, we added this average rental cost per square metre to their costs for each site that they owned.

Results of analysis

5.23 We calculated the adjusted EBIT margins for each of the firms for 2021 to 2023. The results are presented below.

Table 5.1: EBIT margins for each independent firm for 2021 to 2023

Firm	2021	2022	2023	2021-2023
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
Sextile 1			[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
Sextile 2				[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
Sextile 3				[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
Sextile 4				[✂]
[✂]	[✂]	[✂]	[✂]	[✂]

[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
Sextile 5				
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
Sextile 6	[✂]	[✂]	[✂]	[✂]
Weighted average	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based on review of responses received. [✂]

5.24 These results indicate that:

(a) At a range of negative 9% to positive 34% over the period 2021 to 2023, there is a wide distribution of EBIT margin achieved by independent firms; and

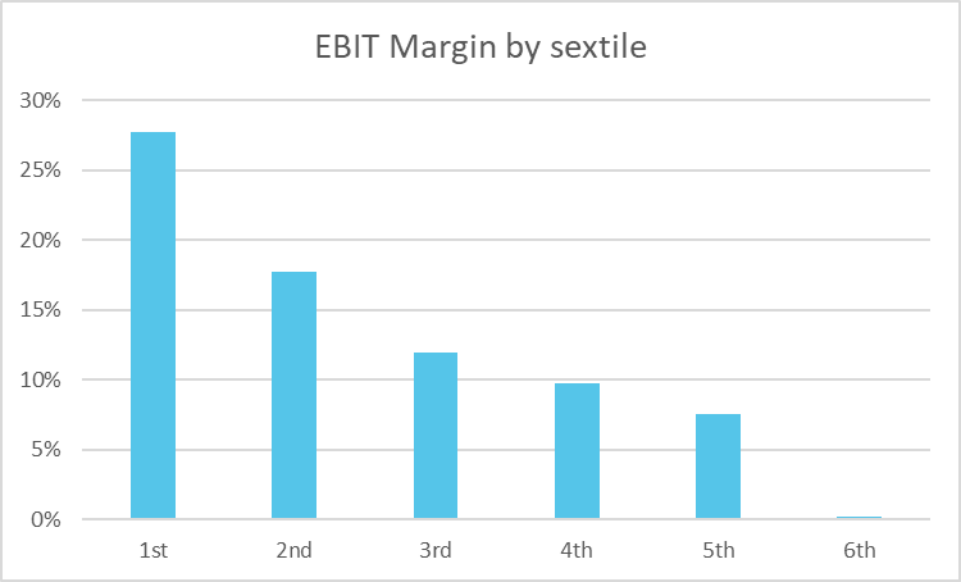
(b) The weighted average margin for the three-year period is 11%.

(c) The weighted average margin for independent firms declines over the period, from 15% in 2021 to 9% in 2023. However, we note that there is variability in this trend between firms; 24 of the firms (67%) have decreasing margins from 2021 to 2023, with 12 firms (33%) showing increasing margins.[437]

5.25 We then considered the distribution of EBIT margins across the sample, by grouping the 36 firms into sextiles and calculating the EBIT margin % for each grouping for 2021 to 2023. The result of this is shown below.

[437] Source: CMA analysis based on review of responses received.

Figure 5.1: EBIT Margin distribution by sextile, 2021 to 2023



Source: CMA analysis based on review of responses received. [✂]

5.26 We note that there is a wide spread of margins across the range, with the top sextile achieving margins of 28% across 2021 to 2023 and the bottom being 0%. This is in line with the large range of negative 9% to positive 34% shown above. We note that there is significant variation in performance across years with only nine (25%) of firms remaining in the same sextile throughout 2021 to 2023. However, this is not the case at the top and bottom of the distribution: three out of six (50%) of the firms in the top sextile remained there throughout 2021 to 2023, as did four out of six (66%) of the firms in the bottom sextile.

5.27 Overall this distribution indicates that there is significant variation in performance across independent firms, and the large range calculated in paragraphs 5.26 and 5.24(a) above reflects this variation in performance rather than highlighting outliers.

Comparison of EBIT margins with those of the LVGs

5.28 In this section we compare the results of our analysis of the financial performance of the independent veterinary firms in our sample with those of the LVGs. We noted in our profitability approach paper that we would interpret the results from our profitability assessment in the wider context of our market investigation, including our understanding of the broader competitive dynamics. We consider these contextual factors and other constraints of our analysis below.

5.29 We compared the EBIT margins of the independent firms in our sample with those of the LVGs over the same three-year period. We noted that the average EBIT margin of the independent firms in our sample was 11% and the average EBIT

margin of the LVGs was 14%, that is, the LVGs performed slightly better than the independent veterinary businesses in our sample.

5.30 We noted a number of reasons which might lead us to interpret our analysis with caution, which we set out in the following sections, supplemented with submissions from the LVGs:

(a) ensuring a like-for-like comparison of in-scope services;

(b) differences in the operation of independent firms and the LVGs;

(c) the smaller than planned dataset.

In-scope services

5.31 Medivet told us that, to ensure a like-for-like comparison:

(a) The CMA needed to target independent veterinary businesses that offered FOP services exclusively;

(b) We should ensure that we did not approach any veterinary practice for which farm animals and equine services represented a large proportion of their revenue, as there may have been differences in underlying levels of profitability and asset usage in these different markets; and

(c) This may imply that the CMA needed to carry out a pre-screening questionnaire to obtain an appropriate sample.[438]

5.32 IVC noted that most independents only provided clinical services, and for comparability purposes sector profitability should be assessed based on activities which were most common, that is clinical and non-clinical, in order to obtain any meaningful insights. [439]

Differences in the operation of independent firms and the LVGs

5.33 Linnaeus noted that different firms had different ways of measuring and accounting for costs and in such a case, it would be wrong to conclude that because there were significant variances between firms' costs, some firms must be inefficient. Linnaeus noted that these issues were particularly acute when comparing larger practices with smaller independent practices as independent practices may have lower costs, but their costs were not directly comparable. In Linnaeus' experience, smaller firms had lower costs because:

[438] Medivet's response to the profitability approach paper, p 11, [✂].
[439] IVC response to the profitability approach paper, p 39, [✂].

(a) Linnaeus [✂] and

(b) Certain regulations, such as off-payroll tax rules (IR35), only applied to businesses above a certain size.[440]

5.34 CVS also noted that independent veterinary businesses were run differently from corporate veterinary businesses, for example they may suffer cost inefficiencies in relation to functions like procurement, staff training and complaint handling as well with raising finance which may make them seem less profitable and they would not benefit from vertical efficiencies. However, CVS noted that if independent veterinary businesses were being prepared for sale, they may have costs stripped out in ways that were not sustainable in the longer term (eg high caseloads for staff members) which may boost short-term profitability. The owners may also take a reduced salary, earning further compensation through dividends or rental income, which would give a skewed view of true profitability of these practices. CVS argued that these differences did not reflect any difference in competitive pressure faced by independent versus corporate veterinary practices, but may well result in quite different observed margins.[441]

5.35 [✂] told us that in some acquisitions, regulatory requirements and professional standards were not being met pre-acquisition. It noted that these incurred additional costs including, among other things, additional recruitment, salary increases, compliance with minimum wage legislation, working time regularisation, improved holiday policies, and refurbishment of facilities'.[442] [✂] encouraged the CMA to consider the different conditions in which these businesses operated compared to the LVGs. [✂] often had to make investments upon acquiring practices in order to improve IT security, H&S and environmental standards, and to ensure regulatory compliance. [✂][443]

Particular circumstances of two of the mid-tier firms

5.36 The evidence submitted by the mid-tier firms indicated particular circumstances for two of the mid-tier firms, which informs our interpretation of their profitability:

(a) [✂]; and

(b) [✂].

[440] Linnaeus' response to the profitability approach paper, p30, [✂].
[441] CVS' response to the profitability approach paper, [✂].
[442] [✂].
[443] [✂].

Dataset

5.37 Pets at Home questioned whether and how the CMA ensured that its sample of independent veterinary businesses was representative, given the wide range of different types of small chains and independent veterinary businesses (at different stages of the FOP lifecycle), and the variety of small local markets in which independent veterinary businesses operate (with their own different dynamics and underlying costs). Pets at Home also noted that a sample of 50 was so small as to raise significant risks of reliability.[444]

5.38 Medivet told us that our plan to issue information requests to 70 independent veterinary practices with an aim of 50 responses was unrealistic. To obtain a truly representative sample of independent veterinary practices, Medivet considered the CMA needed to contact significantly more than 70 practices.'[445]

5.39 IVC accepted that it was practical to consider profitability through a sample of independents, and noted that the sample of independents needed to be representative of the market.[446]

5.40 We consider that our sampling approach was appropriate given the need to accommodate resource constraints while obtaining sufficient evidence to analyse. We also note that we analysed every mid-tier firm.

5.41 However, in the course of our analysis we have had to adjust our sample by removing 19 firms due to the unavailability of financial information for all of 2021 to 2023 because they had not traded over the whole period and removed one firm's data as it is not a local clinic and instead conducts home visits. This has reduced the analysed dataset from 56 to 36 firms, below the 50-firm threshold we stated we would aim for in our Methodology Working Paper.

CMA assessment

5.42 We recognised the need to focus on in-scope services in our profitability approach paper and therefore focused on FOPs providing small animal services.

5.43 This resulted in all of our responses coming from firms providing small animal services. To confirm this, we asked respondents to highlight how much of their turnover (if any) came from services other than small animal. This resulted in two respondents (out of the 56 responses) telling us that they had a material portion of revenue from large animal services.[447]

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[444] Pets at Home's response to the profitability approach paper, para 4.15 – 4.22, [✂].
[445] Medivet's response to the profitability approach paper, p 11, [✂].
[446] IVC response to the profitability approach paper, p 39, [✂].
[447] These two were [✂] & [✂].

5.44 We stated in the profitability approach paper that we would consider the potential impact of out-of-scope activities in our interpretation of our profitability analysis. We excluded the two firms in question from our analysis to check how they impacted our results. Table 5.2 shows the weighted average EBIT margins of the independent firms in our sample, including and excluding firms with large animal services.

Table 5.2: Weighted average EBIT margins of small independent veterinary firms 2021-2023 (including & excluding firms with large animal services)

	2021	2022	2023	2021-2023
Including	15%	12%	9%	11%
Excluding	15%	12%	9%	11%
Difference	-	-	-	-

Source: CMA analysis based on review of responses received. [✂].

5.45 The inclusion or exclusion of these firms did not alter our results. We therefore did not consider their inclusion to require us to alter our initial conclusions, particularly as the firms did also provide small animal services.

5.46 We next turned to the differences in operation of independent firms and the LVGs, and considered that the particular circumstances of two of the mid-tier firms was consistent with the submissions of the LVGs regarding additional costs incurred following acquisition of independent firms.

5.47 We note that these submissions regarding explanations of performance variation between LVGs and independent veterinary businesses highlight factors that could cause both higher and lower margins.

5.48 The submissions from LVGs highlight the following to be potential reasons for independent veterinary businesses to have lower costs (and therefore higher margins) than LVGs:

(a) higher investment by LVGs;

(b) higher compliance costs for LVGs due to capture by taxation thresholds;

(c) higher compliance costs due to LVGs' superior adherence to compliance requirements and professional standards;

(d) temporary cost reductions at independent veterinary businesses as part of preparation for sale; and

(e) owner remuneration through profit-sharing rather than salaries.

5.49 The submissions from LVGs also state, on the other hand, that economies of scale in centralised services for LVGs are a potential reason for independent veterinary businesses to have higher costs (and therefore lower margins) than LVGs.

5.50 The differences in operation of independent firms and the LVGs, and our smaller than expected dataset, leads us to interpret any comparison between the independent firms' and the LVGs' EBIT margins with caution.

5.51 There are some potentially important differences between the analysis undertaken for the LVGs and the analysis undertaken for the independent veterinary firm analysis as follows:

(a) differences in what is accounted for:

(i) LVG analysis includes the financial consequences from clinic closures[448] whereas independent veterinary firm analysis relates to those which traded across all three years; so there will be a survivorship bias within the latter analysis.

(ii) LVG analysis will reflect their portfolio mix, in the main relating to mature practices, (all save Pets at Home established few / no new clinics during the period) whereas the results for each veterinary firm will relate to specifically where they are in that firm's life cycle; so it is to be expected that there will be wider dispersion in margins.

(iii) LVGs have higher levels of centrally incurred /charged out costs, all of which has been included in our analysis; independent firms will buy in support services from a range of suppliers, many of which focus on serving independent veterinary firms: were the different approaches to reflect materially different levels of costs for equivalent output, then the analysis would not reflect comparable levels of efficiency.

(iv) Three LVGs ([✂], [✂] and [✂]) have some farm, equine and mixed practices whereas our sample of independent firm were all small animal veterinary businesses.[449]

(v) We may not have fully accounted for the risk and effort undertaken by practice owners within the analysis whereas we can expect that to be fully reflected in the analysis for the LVGs.

(b) Differences in the basis of preparation of the financial information

(i) Independent firms' depreciation costs for tangible fixed assets (leasehold improvements, fixtures and fittings and equipment costs) are likely to reflect conservative accounting assets lives and the assets may

[448] Over the course of the period of review, LVGs closed 345 clinics permanently with the associated costs of closure included in the analysis. For the years FY2021 to FY2023 the total was 182. [✂].
[449] We included farm, equine and mixed practice activity because we needed these LVG balance sheets to align with their profit and loss accounts for the purpose of the ROCE analysis. Most of this non household pet activity in terms of turnover was undertaken by mixed practices (ie ones that did a mix of farm / equine and small animal).

be fully depreciated within their analysis;[450] for the LVGs those assets have been given values based on depreciated replacement cost and depreciation on those amounts reflected in their EBIT numbers;

(ii) EBIT figures for independent firms reflect the rental cost of their leases (FRS102 treatment), whereas EBIT for LVGs reflect depreciation on their right of use lease asset (IFRS16 treatment)

(iii) EBIT figures for the independent firms include any amortisation reflected within their accounts. For LVGs we excluded any amortisation that related to the write down of goodwill.

5.52 Regarding the level of centrally incurred costs, whether incurred directly or charged by another entity within the corporate group, we used the statutory financial statements as the starting point for our analysis. With the exception of CVS, however, we were not working from financial statements that related to the group as a whole, and even then not all activities undertaken were relevant to UK clinical veterinary activity, necessitating adjustments. At a minimum, this approach leaves scope for different approaches to be taken across the LVGs to determine the cost base for costs not incurred at the local clinic level.

5.53 A further point is that it appears that some independent firms carry on trading notwithstanding being loss making when all their costs are taken into account. In contrast, LVGs will close sites that they judge to be permanently loss making

5.54 These are all reasons why inferences from any comparison need to be made with caution. In particular, we cannot use this evidence to make definitive statements about the relative profitability of LVGs in relation to independent firms. We can, however, state that the top sextile of independent firms earned EBIT margins over 20% on the basis of assessment we used for this analysis.

5.55 Finally, we considered whether it was appropriate for us to draw conclusions on the analysis we carried out on the independent firms in our sample. As set out in our profitability approach paper we considered that determining the total number of independent veterinary businesses to sample (and issue with requests) involved a trade-off between the resources required, both within responding firms and the CMA, to collate and process the information, and the need to have a sufficient number of responses to meet the CMA's analytical and evidential needs. Taking these considerations into account, including that it would not have been practical nor proportionate to request, obtain and analyse financial information from every small independent veterinary firm in the UK, we considered that achieving 50 responses would be sufficient for our analytical and evidential needs. We therefore carried out our sampling as planned and followed up on non-responses. This

[450] This is set out in the section on Tangible fixed asset above.

resulted in us receiving 56 responses, with a spread across the four nations of the UK.

5.56 However, the responses we received from those 56 firms, while all complete in terms of covering what we had asked from them, did not all cover a common period, and in order to be able to analyse trends across the same period (FY2021 to 2023) we had to exclude 19 firms from our dataset. This resulted in a dataset of 36 firms which is smaller than we had originally planned. As a result we consider that we cannot draw robust inferences from the results we see in the sample of independent firms to the rest of the population of independent firms.

Responses to the initial working paper analysis

Non-LVG responses

5.57 We shared a version of the working paper with those independent veterinary firms which had responded to our information request.[451]

5.58 One veterinary firm owner questioned whether the EBITDA figures[452] for independent firms had been adjusted / sufficiently adjusted for the way owners sought to be renumerated by means other than via salaries. EBITDA levels of 34% suggested that might be the case.[453]

5.59 The same veterinary firm owner observed that the life stage of a single entity or small group of independent practices could show significant fluctuations in the EBITDA: a new practice would have negative or very low EBITDA whereas an established independent may well show 20%+ EBITDA before notional salaries. That variation due to life stage would be hidden with the LVGs as would show the aggregated total over their portfolio of sites.[454]

5.60 The same veterinary firm owner told us LVGs would have significant layers of overhead to run their business that would deflate the EBITDA total. Some of their local clinics, evaluated excluding non-locally incurred overhead would show an EBITDA 40%+ and certainly considerably above the 12% independent group average level. All the LVGs had a tier of well-paid senior management, [455] thereby incurring support costs that independent firms would not be incurring to the same extent. These additional support costs as well as transfer charges from other parts of the business deflated EBITDA, making the LVGs return levels appear to be on a par with those earned by independent firms. Based on their own personal

[451] Note not all those which responded were included in the sample the financial information of which we had used.
[452] In fact, EBIT figures were reported in the WP, not EBITDA. As the EBITDA metric excludes depreciation charges (and amortisation, which we had excluded if it related to goodwill or equivalent), the equivalent EBIT figures will be lower.
[453] Independent vet firm owner [✂] response to the financial analysis and profitability working paper.
[454] Independent vet firm owner [✂] response to the financial analysis and profitability working paper.
[455] For example, Chief Executive Officer (CEO) Chief Operating Officer (COO) Chief Financial Officer (CFO), Chief Technology Officer (CTO) Chief Marketing officer (CMO) and Head of Personnel (HOP).

experience of both working in LVGs and independent practice, corporate groups were run quite differently from independent practices.[456]

5.61 Another vet owner told us that the working paper reflected the priorities of corporate consolidators and private equity investors rather than the realities of how independents operated. Independent firms risked being sidelined in a process that measured success solely in financial return metrics despite the fact that most independent owners did not run their businesses with the same shareholder-driven outlook.[457]

5.62 The same vet owner, noting our need to rework their capital employed figures, thought that LVGs structured their accounts in ways that understated their true profitability, for example, through inflating central management fees: LVG reporting was opaque.[458]

5.63 Another veterinary firm owner noted the small sample size, undermining confidence in the reliability of the findings. The owner cautioned against drawing conclusions about the profitability of independents and specifically against using such findings to compare against the LVGs, given the methodological limitations. A broader and more inclusive dataset would be necessary to ensure that any findings were robust and reflective of the wider veterinary market.[459]

5.64 Another veterinary firm owner told us that the planned data set of 5% of independent practices was not representative. Each independent veterinary firm would have developed their own model of doing business based on what they judged would best serve their client and patient base in their geographical area. Observing the wide range in margins reported, the owner told us that, while some firms might not be charging enough and others overcharging, there were other obvious explanations for the wide range. The owner noted that it appeared that we had found no satisfactory way of comparing the profitability of veterinary practices. The owner told us that it was possible to have an efficient well-run practice that clients appreciated and be profitable without charging excessive fees. That approach also allowed the firm to at its discretion limit fees to clients who fell between the gaps.[460]

5.65 The owners of one veterinary firm noted that independent practices were recording staff costs as a percentage of revenue of less than 38%. Such figures seemed remarkably low and questioned whether a genuinely notional salary for owners working within the business had been reflected.[461]

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[456] Independent vet firm owner [✂] response to the financial analysis and profitability working paper.
[457] Independent vet firm owner [✂] response to the financial analysis and profitability working paper.
[458] Independent vet firm owner [✂] response to the financial analysis and profitability working paper.
[459] Independent vet firm owner [✂] response to the financial analysis and profitability working paper.
[460] Independent vet firm owner [✂] response to the financial analysis and profitability working paper.
[461] Independent vet firm owners [✂] response to the financial analysis and profitability working paper.

5.66 The same veterinary firm owners, noting that the LVGs had asserted that their level of investment brought veterinary practice to higher standards, told us that they could not see credible evidence to support that.[462]

5.67 The same vet owners, noting that we had included farm animal and equine services into an assessment of overall LVG UK clinical veterinary profitability, told us that was generally recognised that equine veterinary practice was much less profitable than that of companion animal (pet), and that farm could be very variable. Inclusion of these other services would most likely reduce the reported profitability of the LVGs.[463]

5.68 Two different veterinary firm owners told us that there were [✂] firms[464] which worked for a very large number of independent veterinary practices. They would have access to benchmarking data and would be well placed to support the CMA with a deep understanding of the financial workings of independent practice.[465]

LVG responses

5.69 We had previously shared a version of the working paper including the analysis of the profitability of independent veterinary firms with the LVGs' economic advisers. Only some LVGs commented specifically on the analysis of the independents and the inferences we had drawn as follows.

5.70 CVS told us that adjusting the salary of owners of independent practices to the market rate was insufficient to account for the costs incurred by a practice owner: a practice owner worked longer hours, took more risks, experiencing volatile income in ways a standard employee did not. That was consistent with its experience subsequent to it of acquiring practices, [✂]. An adjustment simply based on the market rate salary of a vet would result in a significantly lower estimate of the economic costs incurred.[466] The true profitability of these sites would be substantially below the figures suggested by our analysis.[467]

5.71 CVS also told us that while many independent FOPs might look similar to CVS or other LVG-operated FOPs, others will be significantly smaller and/or underinvested relative to those owned by CVS, and they will all have different models of financing and management (for example, in terms of how they access training, HR, etc – which CVS and it assumed most other LVGs would arrange centrally). The differences between these models needed to be taken into account

[462] Independent vet firm owners [✂] response to the financial analysis and profitability working paper.
[463] Independent vet firm owners [✂] response to the financial analysis and profitability working paper.
[464] [✂]
[465] Independent vet firm owners [✂] response to the financial analysis and profitability working paper, and independent vet firm owner [✂] response to the financial analysis and profitability working paper.
[466] CRA response for CVS to the financial analysis and profitability working paper, p 29.
[467] CRA response for CVS to the financial analysis and profitability working paper, p 38.

when assessing profitability of independents and/or attempting to compare margins across different players.[468]

5.72 VetPartners told us that it was not surprised by the wide distribution of earnings before interest and tax ('EBIT') margins for the independents. Given that VetPartners itself was a heterogenous collection of independent veterinary practices, the profitability level of different VetPartners' practices also varied. VetPartners' overall profitability would be impacted by the profitability of its individual practices.[469]

5.73 VetPartners also noted that, when comparing the distribution of EBIT margins across LVGs, LVGs sat within the range of independent firms' distribution. That suggested that LVGs' profitability did not stand out when compared to independent firms. Indeed, the CMA acknowledged that some independent firms could make similar profit to four of the LVGs.[470]

5.74 Medivet told us that, based on the analysis set out at above, there was no evidence that (i) LVGs were consistently more profitable than independents, given that EBIT margin ranges for LVGs and independents overlapped; or (ii) LVGs (or independents) consistently made supracompetitive profits.[471]

Responses to our PDR analysis

Non-LVG responses

5.75 We received many responses from independent veterinary firms, or firms representing groups of independent veterinary firms on the methodology of our PDR analysis or the outcomes of the analysis. We note that we did not conduct any profitability analysis of independent firms. Instead, we had sought to analyse the operating margins for a sample of independent firms based on responses to information requests that we had directly issued to the firms concerned. We, however, had drawn no conclusions on this analysis for a number of reasons including the small size of the sample of firms that we were able to analyse over a common time frame.

5.76 Some non-LVG respondents to our PDR felt that our analysis of the operating margins of independent veterinary practices was inadequate and some of these felt we should have assessed the profitability of independent practices.[472] One

[468] CRA response for CVS to the financial analysis and profitability working paper, p 38.
[469] VetPartners response to the financial analysis and profitability working paper, paragraph 2.2.
[470] Oxera response for VetPartners to financial analysis and profitability working paper, p 14.
[471] [✂] response for Medivet to the financial analysis and profitability working paper, paragraph 85.
[472] For example, Anonymous Respondent 27 ([✂]), response to the PDR, p 5;, Briar Vets Limited response to the PDR, p 8; Anonymous Respondent 12 ([✂]), response to the PDR, p 4; Individual, ([✂]), response to the PDR, p 1 ; Individual ([✂]), response to the PDR, pp 2 and 4; Individual ([✂]), response to the PDR,; XLVet UK Ltd response to PDR, pp 12-13]; Individual ([✂],) response to the PDR, p 5; Amwell Veterinary Practice response to the PDR, p 1 and Individual ([✂]), response to the PDR, p 1].

respondent said that we had done no profitability analysis for independent practices.[473] Some respondents said that around an operating margin of 10-15% of revenue was the accepted average for independent veterinary practices.[474] A small number of independent veterinary businesses cited their own operating margin which was below this range,[475] one of which felt this level of operating margin was not excessive and reflected the level of investment in staff, training and equipment.[476]

5.77 One respondent noted that when we had gathered data from independent practices in order to estimate their operating margins, we had not asked how much of this margin was paying off the loan to 'buy in' to the practice. That practice, this respondent explained, needed to make enough margin to pay these loans back and encourage future growth.[477] Another respondent noted that if directors/partners took below market rate salaries and were paying back personal loans used to invest in their practices then that would need to be taken into account in our analysis.[478]

5.78 Another respondent asked what comparators we had used when determining that veterinary practice operating margin was 'excessive' and whether, when estimating operating margins, we had considered that some practice owners took majority of their salary as dividends.[479] A small number of respondents questioned what operating margin levels we would consider to be reasonable.[480] One respondent had concerns that capping the level of operating margins would deter entry.[481]

5.79 Another respondent which had provided us with its financial information which had fed into our assessment of operating margins of independent veterinary practices said that the operating margins for independent practices, and LVGs, was not excessive, at 11% and 14% respectively.[482]

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[473] Anonymous Respondent 31([✂]), response to the PDR, p 1.
[474] Briar Vets Limited, response to PDR, p 8. Veterinary business or practice, [✂], response to the PDR, p 1. Anonymous Respondent 15 ([✂]) response to the PDR, p 1. veterinary business or practice ([✂]) response to the PDR, p 1.
Two respondents cited a wider range of profitability of 10-22%, veterinary business or practice ([✂]), response to the PDR, p 2. Veterinary business or practice ([✂]) response to the PDR, p 4.
Another respondent said that profit levels for independent practices are often as low as 5% and for those which are doing well, up to 20%, due often to the entrepreneurial nature of a practice-owner who is investing unpaid time and energy in building their own practice. Mounts Bay Veterinary Centre Ltd, response to the PDR, p 1.
[475] Priory Veterinary Group response to the PDR, p 8. Vet Well Soon Limited T/A Staveley Vets, Shirebrook Vets, Ravensdale Vets, response to the PDR, p 1.
[476] Priory Veterinary Group response to the PDR, p 8.
[477] Scott Veterinary Clinic response to the PDR, p 3.
[478] Hilltop Vets response to the PDR, p 1.
[479] Worcester vet group response to the PDR, p 11.
[480] Individuals, ([✂]), response to the PDR, p 2. Wrights Veterinary Services response to the PDR, p 3.
[481] Wrights Veterinary Services response to the PDR, p 3.
[482] Individual ([✂]) response to the PDR, p 1.

5.80 Another respondent said that many independent veterinary businesses 'have mortgages on the veterinary premises. These mortgage payments are not tax deductable [sic] (apart from the interest) but have to be paid from profit.'[483]

5.81 One respondent stated that 'all the evidence (personal discussions and external benchmarking) would suggest that most FOPs are not making excessive profits and are actually often overstating their profit by not including 'owned' property rentals costs or fully charging for partners time etc'.[484]

5.82 One respondent questioned whether our assessment of profitability had included practices making low levels of profit and those in 'low socio-economic areas'.[485]

5.83 One respondent noted that the financial data reviewed as part of our investigation reflected a 'distorted post-COVID period'. This respondent submitted that turnover and profitability had been temporarily elevated due to a backlog of cases, government grants, and furlough schemes. They said that these factors did not represent the prevailing financial reality for independent practices.[486]

LVG responses

5.84 Pets At Home 'is concerned that the CMA ha[d] not conducted meaningful profitability analysis for around 40% of the FOPs in the UK. Some of these independent FOPs may well earn profits above the cost of capital, but many will not be doing so.'[487]

5.85 VetPartners noted that the CMA is unable to comment on whether economic profits across independent practices are "sustained" given that the CMA's sample only covers the period 2021–2023 (i.e. it excludes one of the two years that the CMA said it will "focus" on).[488]

5.86 Medivet commented that '[f]or Independent Practices, the PDR has identified a wide range of EBIT margins, ranging from -9% to 34%, with a weighted average EBIT margin of 11%. This compares to a weighted average EBIT margin for LVGs of 14%, only slightly higher. Taking these findings together, the PDR has only been able to identify supernormal profits for providers accounting for [✂]% of the market. It is then clear that these profitability outcomes do not provide evidential basis for a market-wide AEC.'[489]

[483] Anonymous Respondent 8 ([✂]) response to the PDR, p 2.
[484] Anonymous Respondent 25 ([✂]) response to the PDR, p 5.
[485] Leith Vets, response to the PDR, p 2.
[486] Hilltop Vets, response to the PDR, p 1.
[487] Pets at Home response to the PDR, paragraph 2.9.
[488] VetPartners response to the PDR, paragraph 78.
[489] Medivet response to the PDR, paragraph 11 b). [✂]

Analysis of third-party dataset

5.87 As with the CMA dataset, we focused on FOPs providing small animal services and requested information as such, excluding the results for mixed practices where the information on household pets was not extractable, farm practices or equine practices. Some of the practices included incorporate dedicated OOH providers within the same veterinary business. This data is included within that presented.

5.88 Some normalising adjustments have been made to this dataset alongside their statutory data, thereby addressing some of the responses received, for example due to salaries and investment costs. The adjustments are:

(a) Notional Salaries for proprietorial input

(b) Notional Rent

(c) Tenants' improvements

(d) Capital losses on property improvement.

Notional Salaries

5.89 Proprietor salaries in statutory accounts may not correlate to the commercial value of input delivered to the business by the proprietor. As a result, an adjustment has been made to add back renumeration included in the statutory accounts. Subsequently a market rate notional salary is deducted so as to restate the figures to indicate the level of profit the business has generated, assuming all labour is employed.

5.90 The notional salary is based on LVG salaries for former proprietors, then added the employers National Insurance liability that would be incurred on this notional salary plus an auto enrolment pension cost.

5.91 Management time incurred by business owners, over and above clinical work, has not been adjusted for as part of this cost. We acknowledge that in owner managed businesses, there will be management activity required over and above the core business activities. We also acknowledge that management time will already be included within the costs of operating LVG-owned FOPs.

Notional Rent

5.92 Where we are comparing one practice to another, we need to normalise the cost to that practice of all properties that they occupy. Some practices will rent premises, whereas others will own the freehold.

5.93 The adjustments made in respect of notional rent are to add back all cost of finance relating to any funding taken to buy a freehold property and then deduct a market rent for the use of the premises.

Tenants' Improvements

5.94 Where a practice rents premises from a landlord, and undertakes works to that property, the value or cost of those works will be lost at the end of the tenancy period, unless there is some compensation clause included in the lease agreement.

5.95 For accounting purposes, the tenant's improvements are written off on a straight-line basis over the term of the lease to the profit & loss. That cost needs to be included within the adjusted profit figures to show the true cost to the practice of the premises they occupy.

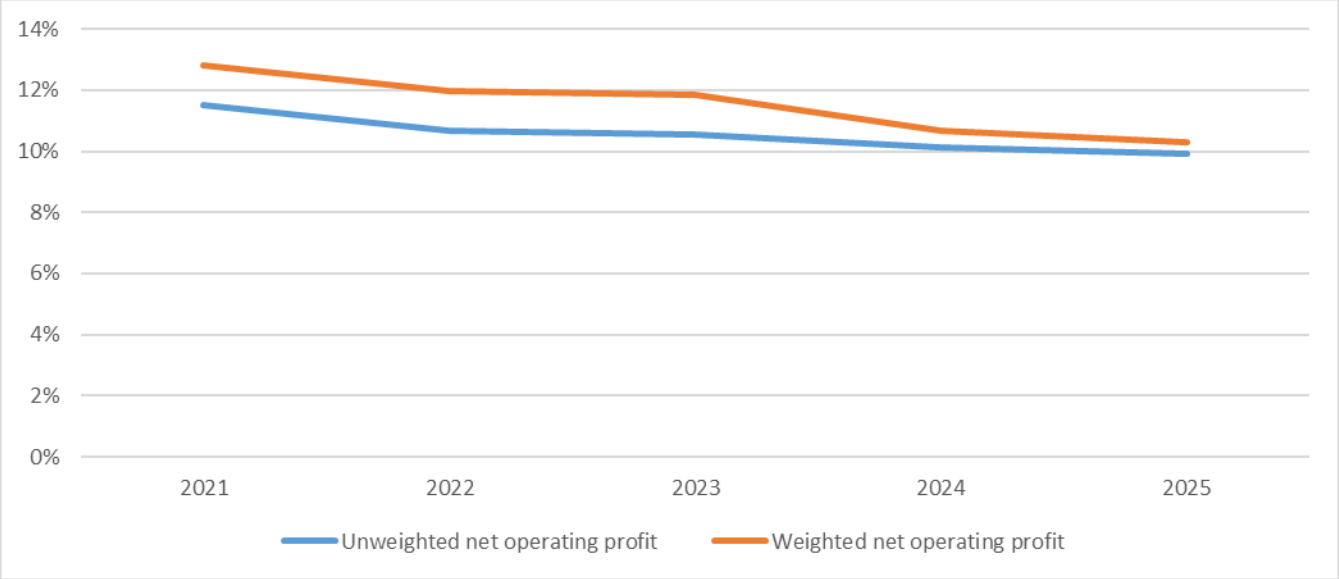
Capital Losses on Properties

5.96 Where practices buy premises and develop those premises, it is very common for the market value of the property, after the works have been undertaken, to be less than the cost of the premises, combined with the cost of the works undertaken. This capital loss can be significant due to the specialised nature of the build required for the veterinary practice to undertake their work. Therefore, the approach adopted is to quantify the capital losses at the point of completion in the works, most commonly through independent market valuations being undertaken, and depreciate those losses. These losses are depreciated on a straight-line period over an agreed term, typically 15-year depreciation period to give a realistic timeframe for recovering those costs through ongoing trading in the business.

Results of Analysis

5.97 In the graph below we show the average net operating profit margins over the years 2021 to 2025. In each year, the number of observations vary, this is listed in Table 5.3 below

Figure 5.2: Yearly average net operating profits for independent firms (%)



Source: CMA analysis of third-party dataset

5.98 Two measures of average net operating profit margins were produced, both unweighted and weighted.

(a) Unweighted averages treat each firm, regardless of their turnover, as identical and thus equally weight each datapoint over that year.

(b) Weighted averages sum the entire turnover across all firms' observations for that year and weights each firm's margin related to the proportion of turnover they are responsible for.

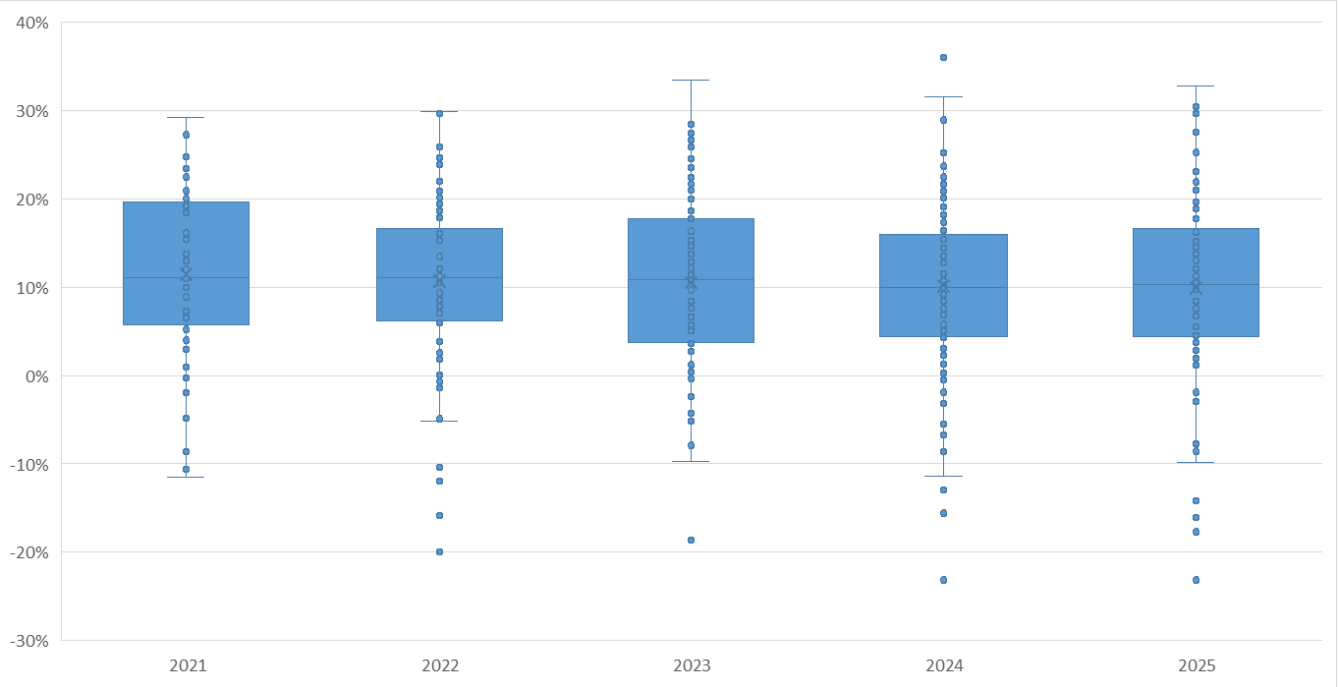
5.99 The range and values are presented in the table below.

Table 5.3: Descriptive statistics for net operating profits (NOPs)

	2021	*2022*	*2023*	*2024*	*2025*
Observations	67	91	107	117	97
Unweighted NOP	11.5%	10.7%	10.5%	10.1%	9.9%
Weighted NOP	12.8%	12.0%	11.8%	10.7%	10.3%
Min. Value	-11.5%	-19.9%	-18.6%	-23.1%	-23.1%
Max. Value	29.3%	29.9%	33.5%	36.0%	32.8%

Source: CMA analysis of third-party dataset.

Figure 5.3: Distribution of net operating profits for independent firms (%)



Source: CMA analysis of third party dataset.

5.100 We see from the results above that there is a wide distribution of net operating profit margins among the sample. The boxes in the chart above indicate 50% of the observations around the median point. While there are some outliers, at both ends of the distribution, around 85% of all the observations are positive in each reported year.[490]

5.101 In line with the results found in the CMA dataset, this distribution indicates that there is significant variation in performance across independent firms, and the large range shown in the table and charts above reflect this variation in performance rather than highlighting outliers.

CMA assessment

5.102 The third-party dataset as received contained the information of 157 firms over the period of 2020 to 2025 thus containing considerably more datapoints than the CMA dataset. However, we did make some exclusions for new start-ups, this is outlined below.

[490] CMA analysis of firm Ys data. Percentage of profitable firms varied from 85% - 90% over the period 2021 – 2025.

Start-ups

5.103 The dataset included 35 start-up practices, that is practices which have opened within the last five years. It was submitted that the three-year point was deemed to be the business viability milestone for new start-ups.[491]

5.104 Therefore we sought to assess the impact of including all of the start-up related observations or whether to only include data after the initial three-year period once viability had effectively been established. The 35 startup firms are split between observations within the first three years, which are excluded and those occurring thereafter. Of the 35 startup firms 12 have at least some data included and 23 are totally excluded.[492]

Table 5.4: Start-ups descriptive statistics

	2021	*2022*	*2023*	*2024*	*2025*	*Average*[493]
	Net operating Margin for the first three years of start-up operation					
Average margin	-31.4%	-2.9%	-11.9%	-7.4%	-12.9%	-10.79%
Min	-155.2%	-41.7%	-157.3%	-100.3%	-141.2%	-
Max	15.1%	29.5%	41.9%	40.4%	36.0%	-
Observations	4	8	16	21	16	-
	Net operating Margin for start-ups post three years operation					
Average margin	-	14.1%	12.3%	21.0%	17.5%	17.4%
Min	-	14.1%	0.1%	7.7%	-1.9%	-
Max	-	14.1%	21.6%	31.6%	32.8%	-
Observations	-	1	3	5	12	-

Source: CMA analysis of third-party dataset, averages provided are across all data points.

5.105 As detailed in Table 5.4:

(a) The data relating to the first three years of operation had a range of net operating profit margins from negative 157% at the lowest to positive 42% at the highest. The average margin across all years was negative 11%.

(b) Conversely the start-up data where it had been more than three years since start-up, had average margins across all years of 17% with a minimum value of negative 2% in just one year, with all other minimums being positive.

5.106 The information related to these firms shows the high level of costs in the initial years compared to the limited level of income that could be generated as the FOP builds its customer list. Or conversely, it may be that not all costs were fully

[491] [✂]
[492] Of the 23 excluded, 20 were excluded based on startup dates and 3 were excluded due those firms not reporting net operating margins.
[493] The average presented here was calculated by the average of all data points across years.

represented in the accounts, for example the management time taken to set up the practice.

5.107 Therefore, start-up data was included after three full years of operation, as the margins relating to the first three years of operation would otherwise skew the analysis and the resulting margins would not be representative of independent firms operating in steady state. This led to most start-ups being excluded from the dataset analysed.

5.108 Next, we sought to understand whether there were factors affecting the results of the margins analysis of the third-party dataset which would deem the results unrepresentative.

5.109 The submissions from non-LVGs highlight the following to explain why the CMA's margin analysis would not be representative of independent firm performance:

(a) Exclusion of loans and other forms of debt for the purposes of procuring the practice;

(b) Directors and partners taking below market rate salaries;

(c) Mortgage payments on veterinary premises;

(d) Firms in the dataset not being from low socio-economic areas; and

(e) The time period analysed being of an exceptional time period where COVID factors such as a back-log of cases, grants and furlough schemes may have an impact.

5.110 One accountancy firm commented that, any start-up business will require time input and commitment above a normal employee's working week and that it is common for the individual starting up the firm to not pay themselves a salary in the early years of trade.[494]

5.111 It was also submitted that a practice that started 5 years ago, may appear to be making reasonable profits in year 6 but that margin does not reflect the 5 preceding years of investment and therefore we should be wary of making conclusions based on margins.[495]

5.112 Another respondent to the PDR, added that the sample data may be less representative if data on multiple independent practices has been provided by e.g. the clients of which may demonstrate similar characteristics or adhere to particular

[494] [✂]
[495] [✂]

financial practices because of their contractual arrangement with a particular accountancy service.[496]

5.113 As acknowledged in this appendix we have not conducted a full profitability analysis of independent veterinary firms due to the burden it would place on those firms and the CMA in gathering the relevant data. As a result, we have not assessed the impact of debt and other forms of finance for independent firms.

5.114 We fully acknowledge that while normalising adjustments have been made to the third-party dataset to account for owner clinical activities at a market rate, that no adjustment has been made for management time. Whereas this type of cost would be accounted for within LVG data as part of its administration and centralised office costs. This could explain why some margins are extremely high in the first years of operation for a start-up firm, where clinical capacity wouldn't be fully utilised and there would be greater need for management and administration activities.

5.115 The third-party dataset has been provided by one firm and therefore, there may be some aligning characteristics to the firms in the dataset. We note however, that there was a geographical spread to the data and this aligns with the wide variation in net operating margins observed.

5.116 The dataset received also contained a significant number of observations across the period 2021 to 2025. We note that not each firm operated in each year of this period, however, given the number of observations and firms in the dataset we considered that this would not impact the observed margins. As a result, we did not restrict the timeframe to 2021 to 2023 as we did with the small sample of firms in the CMA dataset and therefore the margins cover a longer timeframe. We observe a stable average net operating margin over the period, notwithstanding the differing number of observations in each year.

Conclusions on financial performance of the independent firms as set out in the working paper

5.117 We have not completed a full profitability analysis of independent veterinary firms as explained previously and therefore our analysis does not incorporate the cost of financing the on-going operations and the investment in starting up these firms. These factors limit our ability to make definitive conclusions on the profitability of independent veterinary firms. We have also not sought to make comparisons

[496] Reader and Summers, Economic advisory report prepared for the PVA, 11 January 2026, p 3.

between the margins of the independent veterinary firms and LVGs due to differences in cost measurement and cost inclusion.

5.118 Our analysis of the CMA dataset for 2021 to 2023 showed that there was a very wide distribution of EBIT margin for the independent firms in our sample from loss-making to over 30%. The firms in the CMA dataset had a range of EBIT margins of between minus 9% and positive 34%, with a weighted average EBIT margin for the three-year period of 11%. Similarly, the third-party dataset had a range of net operating profit margins between negative 23% to positive 36% and an average weighted operating margin of 11%. The majority of firms had positive margins; 89% of firms had positive margins across all years in the third-party dataset, and similarly, 93% in the CMA dataset.[497]

5.119 We also noted that there was an approximately even distribution across the range of margins in the CMA dataset, with an average gap between each sextile's margin of 6%. In addition, we noted that there is significant variation in performance across years with the exception of those firms in the top and bottom sextiles. Only 10 (27%) of firms remained in the same sextile throughout 2021 to 2023, but four out of six (66%) of the firms in the top sextile remained there throughout 2021 to 2023, as did three out of six (50%) of the firms in the bottom sextile.

5.120 Overall, this distribution indicates that there was significant variation in performance across independent firms, and the large range of margins reflects this variation in performance rather than highlighting outliers. While there is variation in performance across years, those firms at the top and bottom of the distribution tended to remain there.

5.121 The analysis of both the CMA dataset and the third-party dataset resulted in similar observations. There are factors which could explain the variation in net operating profits, such as how each firm has accounted for staff costs, including management time, and differences in the levels of investment. We found there is a wide distribution of performance among independent veterinary firms, with some significantly higher margins than others. This evidence is consistent with our overall findings on the level of competition between veterinary businesses.

[497] In each year, 3 firms out of the 36 analysed had negative margins in the CMA dataset.

6. Annex A: Data gathering and responses received in relation to independent firms

6.1 In this section we summarise our data gathering process and the responses we collected.

CMA dataset of independent firms

Mid-tier firms

6.2 We sent an RFI to each mid-tier firm asking for information on size (site & staff numbers) and financial information.

6.3 After the publication of the Profitability Approach Working Paper we discovered that there were five mid-tier firms in the UK (according to our criterion of having ten or more sites), rather than the four mentioned in the Methodology Working Paper. We contacted all five, being:

(a) [✂] [mid-tier firm 1] ([✂] sites as of 5 November 2024);

(b) [✂] [mid-tier firm 2] ([✂] sites as of 5 November 2024);

(c) [✂] ([✂]) [mid-tier firm 3] ([✂] sites as of 5 November 2024);

(d) [✂] [mid-tier firm 4] ([✂] sites as of 5 November 2024); and

(e) [✂] [mid-tier firm 5] ([✂] sites as of 5 November 2024).

6.4 All five responded to our RFI providing at least three years of financial information (including 2024) where the firm had existed for that long, as well as answers to our questions. One firm, [✂], launched in [✂] through the acquisition of [✂] practices from four separate businesses and only had one full year of financial information in the form of management accounts, to [✂], and no audited accounts (the first set being prepared for the period to 31 December 2024). We therefore excluded it from our analysis on the basis that one year of financial information would not be particularly informative to our analysis. One firm, [✂], could not provide financial information for 2021 and was therefore excluded from our analysis of the 2021 to 2023 period.

Small Independent Veterinary firms

6.5 We selected at random a sample of small independent veterinary firms in the UK and sent an RFI to the 70 selected. The RFI asked for information concerning size (site and staff numbers) and financial information.

6.6 It was immediately apparent that one of the firms contacted was out of scope, and we therefore replaced it in the sample.[498] This means we contacted 71 firms. Of these, 56 responded.

6.7 The 56 responses from small independent veterinary firms have a geographic split across the UK with 84% in England, 11% in Scotland, 4% in Wales and 2% in Northern Ireland.

6.8 Of these 56, there were five incomplete responses including those where full or management accounts were not provided (only filleted accounts), only minimal responses were given (such as 'N/A'), or the firm had opened so recently that the first full year of financial information was not available. This left us with 51 firms.[499]

6.9 In order to strengthen our analysis, and capture yearly variations in performance, we focused our analysis on those firms that could provide to us financial information for each of 2021, 2022, and 2023. This reduced our analytical sample to 34 small independent veterinary firms.

Combined analysis

6.10 For this working paper, we analysed the performance of independents veterinary businesses as a whole for 2021 to 2023, including mid-tier and small independent veterinary firms. We have therefore been able to analyse 36 responses, being three mid-tier firms and 33 small independent veterinary firms. Together these 33 firms cover 133 sites and £121 million of 2023 revenue.[500]

6.11 The table below summarises the response and analysis process.

Table 6.1 The response and analysis process for the small independent veterinary firms

RFIs sent	**76**
No response	*(15)*
Responses received	**61**
Incomplete responses	(5)
Do not cover all of 2021-2023	*(19)*
Not in scope	*(1)*
Analysed responses	**36**

Source: CMA analysis based on review of responses received

[498] The firm in question ([✂]) was out of scope because it only supplied pet travel documents and did not provide veterinary services [✂]
[499] [✂]
[500] [✂]

Third-party dataset of independent veterinary firms

6.12 Requests for information were issued to [✂] firms operating in the veterinary market. Financial statements were requested for the independent small animal FOPs (thus excluding referral centres as well as equine and farm practices) that the firms dealt with.

6.13 The firms adjusted the financial statements using market rates for owner salaries and rent costs. These adjustments were applied to cases in which owners were not paying themselves salaries as well as if rent was not paid on property (and thus in both cases without adjustments profits may be overstated).

6.14 The properties of the data sets varied across the [✂] firms. The data set received from [✂] was limited. Due to these limitations the CMA has not placed weight on the data from this firm, instead conducting analysis on [✂] data.

(a) [✂] submitted a dataset containing 157 small animal veterinary businesses covering a total of 306 FOP sites. Including in this data set were 35 businesses that had started up recently. For each firm, financial statements were provided for all years on record. The dataset spans 2020–2025, though coverage is uneven; only two observations are available for 2020 and as a result the relevant period of review is 2021 to 2025 [501]

(b) [✂] dataset was limited in both size and breadth. The dataset covered [✂] firms in total across 75 sites, with only one datapoint per firm for the most recent year available, which was not the same year across all firms.[502]

6.15 Our analysis was conducted on [✂] data. EBIT data was not available and as a result we primarily analysed the independent firms' net operating profit margins.[503]

6.16 Once we had removed start-ups as well as a limited number of firms that had not reported net operating profits, the sample covered 127 firms across 264 sites. [504] This sample did include one large firm with [✂] sites.[505]

6.17 As the years each firm's financial statements covered varied, the sample size across the period also varied. Table 6.2 below presents the number of observations in each year.

[501] [✂] explanatory note.
[502] The data provided by Firm 1 covered: [✂] firms in 2023; [✂] in 2024; [✂] in 2025
[503] As opposed to EBIT which includes non-operating income.
[504] Total dataset 157 firms (306 sites). Removing 23 start-ups (including 3 with no operating profit data): 134 firms. Removing 7 firms with no operating profit data: 127 firms (261 sites). Data was also filtered out for the years 2020, this did not result in a firm being dropped from the data set.
[505] The distribution of firms by site number is as follows: 77 firms with 1 site; 26 firms with 2 sites; 11 firms with 3 sites; 5 firms with 4 sites; 2 firms with 5 sites; 3 firms with 6 sites; 2 firms with 7 sites and 1 firm with [✂] sites.

Table 6.2: Number of observations in each year

	2021	*2022*	*2023*	*2024*	*2025*	*Total*
Observations	67	91	107	117	97	479

Source: CMA analysis of third-party dataset

7. Annex B: LVG financial and profitability analysis

7.1 This annex sets out the adjusted individual balance sheet and profit and loss statements we have prepared for each of the LVGs for the five years to 2024 in line with the approach we set out in the financial and profitability analysis appendix ('Adjustments to financial information'). Under the set of statements for each LVG we give further information about what implementing that approach meant in their case, particularly in relation to items not covered in detail in the main section.

7.2 We therefore do not repeat here how we have adjusted for the treatment of tangible and intangible fixed assets as well as cash.

7.3 We begin this annex with generic points about accounting treatment issues that we have not already specifically addressed within the main part of this working paper, namely:

(a) Research and Development Expenditure Credits; and

(b) central support costs.

Research and Development Expenditure Credits scheme

Introduction

7.4 Several of the LVGs receive, or have received, credits from claims submitted under HMRC's Research and Development Expenditure Credits (**RDEC**) scheme. The RDEC scheme can be used by some companies (not limited to companies providing veterinary services) to claim a tax credit for relief on research and development (**R&D**) costs.[506] It can be used to pay a company's corporation tax liability, other tax liabilities such as VAT, and if there is any credit left over after paying the company's tax liabilities, it may be paid to the company. The tax relief is designed to support companies which work on innovative projects in science and technology.[507]

7.5 Under the RDEC scheme, the benefit is reported as an 'above the line' credit, as an element of profit before interest and tax within the firm's profit and loss statement.[508] Qualifying R&D expenditure is eligible for a 13% RDEC tax credit, and the credit is subject to corporation tax, resulting in a 10.53% benefit (£1,053 per £10,000 of qualifying expenditure).

7.6 Table 7.1 summarises the amounts included as RDEC tax credits within the financial statements provided by each LVG and shows that the amounts credited

[506] R&D expenditure credit for large companies and small and medium-sized enterprises - GOV.UK.
[507] Check if you can claim Research & Development (R&D) tax relief - GOV.UK.
[508] RDEC scheme - R&D tax relief explained | RSM UK.

to the LVGs' profit and loss statements for the six years to 2025 totalled £116 million. There has been a significant increase in the amounts being recognised in the respective financial statements of those veterinary business claiming RDEC, particularly in 2025 as disclosed in their statutory financial statements,[509] although in the case of CVS this in part reflects its increasing confidence that the full amounts claimed under the scheme will be reimbursed by HRMC.[510]

Table 7.1: Income from government R&D grants (RDEC) for each LVG over the six financial years (FY) to 2025 (£m)

	FY20	*FY21*	*FY22*	*FY23*	*FY24*	*FY25*	*Total FY20 to FY25*		*Total FY20 to FY24*
CVS	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
IVC	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Linnaeus	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Medivet	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Pets at Home	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
VetPartners	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Total	3.9	4.8	12.4	21.8	30.2	43.1	116.2		73.0

Source: LVG financial information (RFI 12 and RFI 21 financial template responses) and CMA analysis. [✂]
Note: The final column shows the total for income from government grants (RDEC) over the 5 years to 2024 as discussed in part A: section 15.

Parties' submissions

7.7 In response to the profitability approach working paper only CVS made submissions regarding an adjustment to the treatment of RDEC tax credits in our economic profitability analysis. It submitted that RDEC credits should be stripped out of the ROCE calculations, on the basis that although they were recorded as a negative cost due to accounting standards, in reality they were a tax credit.[511] [512]

7.8 [✂] told us that it did not receive the RDEC tax credit.[513] We note that [✂] only disclosed [✂] amounts of RDEC tax credit in 2020 and 2021 and [✂] for subsequent years (although it may be the case that [✂]), and [✂] (although again it may be the case that another group entity has claimed the credits). VetPartners disclosed RDEC in all years 2020-2024 totalling £[✂], and IVC disclosed RDEC in [✂] totalling £[✂].

7.9 CVS reiterated its position in its response to the working paper. It told us that on an accounting basis it was a tax credit (which was set against corporation tax that

[509] CVS Annual Report and Financial statements for the year to June 2025, p 116. VetPartners Group Limited Annual Report and Consolidated Financial Statements for the year ended June 2025, pp 35 and 43. Independent Vetcare Limited Annual report and financial statements for the year ended 30 September 2024, pp 42 and 71.
[510] CVS Annual Report and Financial statements for the year to June 2025, p 101.
[511] CVS response to the profitability approach paper, Annex, section 2.1. [✂]
[512] [✂]
[513] [✂]

was not included in the calculation, creating an asymmetry), and as such it was inconsistent to ignore tax liabilities but include tax credits. On an economic basis, it told us that achieving a higher RDEC value was not indicative of a failure of competition: there was no reason to believe that higher RDEC credits would make consumers worse off (given that they are not earned from consumers), or should be competed away (given they are a fixed credit earned from government, and not a variable cost saving). By including RDEC as part of its revenue calculations, CVS submitted, the CMA had significantly overstated the returns CVS earned from consumers, compared to its market reality.[514]

7.10 [✂] told us that it did not consider RDEC to be a core activity of its practices and it did not consider RDEC when assessing the performance of its practices.[515]

CMA assessment

7.11 We examined whether we should exclude RDEC on the basis set out by CVS, namely that they should be treated as a corporation tax credit and therefore out of scope of our pre-interest, pre-corporation tax analysis of profitability.

7.12 We first looked at the aims of the RDEC scheme. The scheme exists to encourage companies to invest in R&D projects which seek an advance in a field of science or technology. Companies are able to claim credits against allowable costs which relate to their direct R&D activity as well as on a wide range of indirect activities. Allowable costs encompass a wide range of costs including staff costs, consumable items, and software (the proportion claimed being the proportion of costs incurred in the R&D).[516]

7.13 We then looked at the mechanism by which the RDEC were claimed. First, a payable credit is used to discharge any corporation tax liability in the relevant period. Any remainder[517] is used to discharge corporation tax liabilities for any other period, and can be surrendered to another group company, as well as to discharge any outstanding liabilities to HMRC. Any remaining balance is payable as a credit.

7.14 We therefore considered that the substance of these credits was of a business incentive (government grant) in the nature of the costs allowed to be claimed against, as well as the mechanism under which the credits were paid, relating to the LVGs' operations rather than a tax credit. We also noted that the LVGs treated the RDEC in their financial statements as a government grant and not as a tax credit. As such, to the extent that amounts are owed by the government under the

[514] [✂]
[515] [✂]
[516] Check what Research and Development (R&D) costs you can claim - GOV.UK.
[517] The remainder is reduced by the tax rate, to give a net of tax amount, and the tax amount is carried forward for offset against future corporation tax liabilities. The remainder, once liabilities have been discharged for other periods, is capped at the total PAYE / NIC of R&D staff.

RDEC scheme to CVS, then these should be classified as ordinary assets and not excluded as tax assets, an approach we have sought to implement within our analysis.

7.15 A further point on consistency across our analysis is that we did not modify our approach to determining the cost of capital to take into account the rate of corporation tax CVS is 'paying' after deduction of this 'tax credit'. In our cost of capital analysis, we use the average standard corporation tax rate over the period of 21%.

7.16 We note CVS's point that income from RDEC may not directly scale with their operations in the shorter term but that is also true of other LVG's costs and revenues. We remain of the view that RDEC is income that LVGs derive from their activities as providers of veterinary services and it is the operation of the market over the longer term which determines whether the benefit of this income is competed away or not.

7.17 We therefore did not make an adjustment to the RDEC credits, and they remain included in the assessment of the profitability of operational performance of the LVGs' local veterinary clinics.

Central support costs

7.18 Noting that our profitability assessment focussed on a part, not the whole, of each LVG's wider business operations, we needed to understand how the LVGs had each allocated central costs, (including any management fees charged from other parts of their wider corporate group[518]) to their UK clinical veterinary services businesses when submitting their responses to our requests for financial information. We noted that these approaches differed between the LVGs which reflected both the starting point of the financial information provided as well as the relative importance of each LVG's clinical veterinary services in the UK, within the context of each LVG's wider business operations. We also noted that, because of reporting disclosure exemptions for statutory financial statements for transactions with related parties,[519] we did not necessarily see charges (possibly measured at cost) from related companies in the LVGs' financial statements.

[518] With the notable exception of CVS, the starting point for the profitability analysis for each LVG was either a set of entity or group financial statements that related to a subset of that LVG's wider corporate group. In the case of Pets at Home we asked it to aggregate the entity financial statements (profit and loss and balance sheet) of all the Pets at Home-branded clinics for each financial year. In the case of Linnaeus, we used as our starting point financial information used to prepare financial statements for Linnaeus' shareholders.
[519] Corporate entities which are subsidiaries within wider corporate groups may take advantage of an exemption to not disclose within that entity's statutory financial statements transfer charges between it and other subsidiaries in that wider corporate group and/or transactions with related parties, if a) those transfer charges or related party transactions are included within the group financial statements of that wider corporate group and b) that wider corporate group's financial statements are prepared in accordance with recognised group reporting standards.

7.19 CVS removed any incremental central costs that would not be necessary were their non-UK veterinary services (ie crematoria, labs and online retail business) not part of their business, that is, it carried out a decremental approach to cost allocation. CVS found the majority of central expenses would be incurred even in the absence of non-UK veterinary activities, however it did identify a small amount of non-UK veterinary specific expenses relating to time spent by finance and HR staff on these activities.[520]

7.20 IVC allocated central costs to UK veterinary services with the method of allocation dependent on the cost item: [✂].[521]

7.21 Linnaeus also adopted [✂].[522] [✂].[523]

7.22 [✂][524] [✂][525][✂].[526] [✂].

7.23 Medivet submitted that there was no allocation method for joint and common costs that was both robust and practical and as a result it [✂]. The exceptions to this were [✂], which were [✂]. It noted that there [✂]. IT costs were allocated by [✂]. It also noted that this allocation method [✂]. To reflect [✂]it stated it would require a bespoke system which would be disproportionately complex and resource intensive.[527]

7.24 Pets at Home allocated central costs (relating to office support such as procurement, marketing and HR) wholly to local clinics where these services were exclusively for its UK veterinary business, and on an apportionment basis where central costs (relating to executive and other central group teams such as finance and professional fees) were shared with the retail pet business. IT costs were allocated to local clinics on the basis of respective profit shares (which resulted in [✂]% of costs allocated to its clinical veterinary services business). Pets at Home submitted that:

(a) all joint venture local clinics paid management fees to Pets at Home Group in return for a bundle of business support services (eg negotiating with suppliers of pharmaceuticals / medicines / drugs, property management, IT, accountancy, secretarial, marketing);

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[520] [✂].
[521] [✂].
[522] [✂].
[523] [✂].
[524] [✂].
[525] [✂].
[526] Mars is, amongst other things, both a confectionary and pet food manufacturer. See Mars.com.
[527] [✂].

(b) the management fee was linked to the revenue rather than the profit of the local clinic, and whether the local clinic chooses to use certain additional services (for example additional marketing support); and

(c) the fees compensate Pets at Home Group for the costs of services it provides and a return on its investment in the local clinic portfolio (Pets at Home Group does not get dividends from the local clinics).[528]

7.25 We have removed the management fee from the profit and loss figures provided by Pets at Home and included in its place an allocation of central costs estimated by Pets at Home.

7.26 [✂] told us that it did not allocate central costs to its UK clinical veterinary services business in the ordinary course of business. For the purposes of this process, it used a cost allocation basis based on varying cost drivers such as FTE.[529]

7.27 Some owners of independent vet firms whose financial information had been the basis of our independent firm margin analysis commented on the significant level of central costs that would be being incurred by the LVGs. As noted in the financial and profitability analysis appendix, the variety of approaches that have been taken to determine these costs leaves scope for some lack of comparability across the LVGs in respect of costs not incurred at the local clinic level.

Results for each of the LVGs

7.28 In this section we present the adjusted balance sheets, and adjusted profit and loss statements, together with a summary of the adjustments we made, for each of the LVGs.

CVS

7.29 The balance sheet and profit and loss statements for CVS are set out below in line with the approach we set out in section 3 above under the sub-section 'Adjustments to the LVGs financial information'. We then set out further information about what implementing that approach meant in CVS's case.

[528] [✂].
[529] [✂] response to CMA's RFI 12, p 6.

CVS adjusted financial statements

Table 7.2: CVS adjusted balance sheet statement (base case) £m

		As at June / year to June					
		2020	2021	2022	2023	2024	2025
Fixed capital employed	Intangibles: customer acquisition & workforce based on costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Leasehold property (Right of Use) (ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Clinic fit out & equipment (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Other Tangible Fixed Asset (TFA) (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Software	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Working capital employed	Other non-current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Non-current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Provisions re P&L costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Split as to:	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Fixed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Working	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based in the first instance on the group financial statements of CVS plc and adjusted using supplementary financial information provided by CVS to the CMA. [✂].

Table 7.3: CVS adjusted operating profit and loss statement (base case) £m

			As at June / year to June					
			2020	*2021*	*2022*	*2023*	*2024*	*2025*
Cash Flow items	Revenue	Revenues	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	COS	Cost of sales	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	AE/O(O)I	Administrative expenses	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Board restructure	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	O(O)I	Grant income (Coronavirus)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Non cash flow items	TFA depreciation	Leasehold property (ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Clinic fit out & equipment (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Other TFA (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Software	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	Unexpected loss in value of TFA	Leasehold property (ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Clinic fit out & equipment (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Other TFA (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Software	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		EBIT before certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Income from government R&D grants (RDEC)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Cyber incident (April 2024) costs associated with Estimate of negative impact of cyber incident on FY2024 EBITDA	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Third party costs relating to CMA investigations	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Costs associated with the closure of 32 sites	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Costs associated with the careline call centre closure	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Total for certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		EBIT after certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Other noteworthy items	Included in above P&L	Value of CVS plc group's corporate costs eliminated	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

Not included in above P&L	Loss on disposal of businesses in lieu of Phase II reference	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Deferred / contingent consideration passing through P&L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Transaction costs related to practice acquisitions	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based in the first instance on the group financial statements of CVS plc and adjusted using supplementary financial information provided by CVS to the CMA. [✂].

Notes on preparation of adjusted financial information for CVS

7.30 The source financial statements for this analysis are those for CVS Group plc, the top holding company, for this AIM-listed veterinary services group. The base information has been extracted from CVS's group financial statements.

7.31 As CVS undertakes other activities other than UK clinical veterinary services it proposed adjustments as follows:

(a) To remove its Crematoria segment (summary information on this reporting segment along with the other reporting segments identified below is separately disclosed in the notes to CVS's group financial statements).

(a) To remove its Laboratories segment.

(a) To remove its Online Retail Business segment – this segment contains its online pharmacy business but also contains its other online retail offerings.

(b) To remove the non-UK element of its Veterinary Practices segment. CVS told us that, unlike for its other reporting segments, it was not straightforward for it to identify this adjustment. It did not provide us with any explanation of how it had gone about this.

(c) To remove that element of its Central admin segments costs that related to those of its activities that were not related to its UK clinical veterinary services. CVS asked us how it should go about this exercise, and we asked it to take a decremental approach ie identify those of its costs which related to the above elements. The impact of this adjustment is shown above.

7.32 When processing the Central admin adjustment CVS sought to price its (wholesale) Crematoria services into its UK clinical activities as the price that a third party would charge. In principle, this approach to pricing is correct as the provision of crematoria services falls outside our analysis.

7.33 In addition to the above 'scoping' adjustments, CVS proposed that we exclude the income it had earned from RDEC and the associated tax asset balances.

7.34 As explained in the introduction to this Annex, we regard RDEC to be a source of operational income and therefore reversed the adjustment that CVS had included as part of its adjustment to its Central admin segment costs and revenues.

7.35 We excluded CVS's FY2023 exceptional item: Impairment of the investment in Quality Pet Care Ltd. This related to the loss that CVS suffered when it accepted that it would divest this firm in lieu of a Phase II merger control reference. According to explanations provided in its annual report, due to the interim

measures that the CMA imposed it never acquired control of this business and so it never consolidated this business into its results.

7.36 As noted in the ‘other noteworthy’ items not included in the profit and loss analysis’ above, in all periods of the period of review there are significant level of costs going through the profit and loss that relate to the purchase and sale of veterinary practices. These have been excluded as they relate to the buying and selling of veterinary practices and not the net assets deployed within, and operational performance of, those veterinary practices.

IVC

7.37 The balance sheet and profit and loss statements for IVC are set out below in line with the approach we set out in section 3 above under the sub-section ‘Adjustments to the LVGs financial information’. We then set out further information about what implementing that approach meant in IVC’s case.

IVC adjusted financial statements

Table 7.4: IVC excluding Vets Now adjusted balance sheet statement (base case) £m

		As at September					
		2020	*2021*	*2022*	*2023*	*2024*	*2025*
Fixed capital employed	Intangibles: customer acquisition & workforce based on costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Leasehold property (Right of Use) (ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Clinic fit out & equipment (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Other Tangible Fixed Asset (TFA) (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Software	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Working capital employed	Other non-current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Non-current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Provisions re P&L costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Total operating capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Split as to:	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Fixed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Working	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based in the first instance on the entity financial statements of Independent Vet Care Limited and adjusted using supplementary financial information provided by IVC to the CMA. [✂]

Table 7.5: IVC excluding Vets Now adjusted operating profit and loss statement (base case) £m

			Year to September					
			2020	*2021*	*2022*	*2023*	*2024*	*2025*
Cash flow items	Revenue	Revenues	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	COS	Cost of sales	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	AE	Administrative expenses	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Administrative expenses (other identified items)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	O(O)I	Grant income (Coronavirus)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Management charges receivable	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		"Other" other operating income	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Non cash flow items	TFA depreciation	Leasehold property (Right of Use) (ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Clinic fit out & equipment (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Other TFA (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Software	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	Unexpected loss in value of TFA	Leasehold property (ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Clinic fit out & equipment (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Other TFA (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Software	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		EBIT before certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Income from government R&D grants (RDEC)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Restructure / reorganisation type items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		External advisory costs on implementation of group restructuring and reorganisation	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Implementing a new Target Operating Model	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Third party costs relating to CMA investigations	not included within info provided by IVC					
		Total for certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		EBIT after certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Other noteworthy	Included in above P&L	"Centralised management costs"	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

Not included in above P&L	Loss on disposal of businesses in lieu of Phase II reference	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Deferred / contingent consideration passing through P&L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Transaction costs related to practice acquisitions	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based in the first instance on the entity financial statements of Independent Vet Care Limited and adjusted using supplementary financial information provided by IVC to the CMA. [✂].

Notes on preparation of adjusted financial information for IVC

7.38 IVC seeks to include the results of all its UK veterinary practices within the legal entity Independent Vet Care Limited (IVCL). This is a set of entity financial statements. Note that Vets Now has its own set of statutory financial statements and has been separately analysed.

7.39 Vets Now has a different operating model to most other veterinary practices. Vets Now utilises host clinics (which are not necessarily IVC clinics) to offer its OOH service. [✂]. Vets Now operates on a standalone basis and uses separate financial reporting. [✂].

7.40 IVC set out its proposed adjustments to adjust for the following:

(a) [✂];

(b) [✂]; and

(c) [✂].

7.41 We made adjustments which included:

(a) removing balances described as 'Trade and other receivables (current) from other group entities' as, based on information given in the notes to the source financial statements, these balances appeared to be financing rather than trading balances; and

(b) removing the element of centralized costs that related to Vets Now by the estimate that IVC had used to estimate for standalone OOH in RFI6.

7.42 [✂]. We have therefore updated the information that IVC reviewed to reflect these items.

7.43 As noted in the 'other noteworthy' items not included in the profit and loss analysis' set out above in earlier periods of the period of review there are [✂]. These have been excluded as they relate to the buying and selling of veterinary practices and not the net assets deployed within and operational performance of those veterinary practices. [✂].[530]

7.44 [✂].[531] As a result, and in contrast to the other LVGs, our analysis for IVC does not include its costs [✂].

7.45 Included within IVC's operating costs are £59.2 million and £13.3 million of external advisory costs on implementation of group restructuring and

[530] [✂]
[531] [✂]

reorganisation', relating in part to costs incurred by the IVC wider corporate group.[532] We excluded a [✂][533] of upward revaluation of leased property assets, which IVC told us this represented a one-off correcting adjustment following the transition to IFRS accounting standards, which enabled a more precise calculation of lease-related assets.[534]

[532] Independent Vetcare Limited Annual report and financial statements for the year ended 30 September 2024, p 71.
[533] See IVCL's 2023 Annual Report and Financial Statements, Notes to the financial statements 16, the net of two figures for 'Remeasurements'.
[534] IVC RFI 20 response.

Vets Now

7.46 The profit and loss statements for Vets Now are set out below in line with the approach we set out in section 3 above under the sub-section ‘Adjustments to the LVGs financial information’. We then set out further information about what implementing that approach meant in Vets Now’s case.

Vets Now adjusted financial statement

Table 7.6: Vets Now adjusted operating profit and loss statement (base case) £m

			Year to September					
			2020	2021	2022	2023	2024	2025
Cash flow items	Revenue	Revenues	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	COS	Cost of sales	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	AE	Administrative expenses	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Restructure / reorganisation type items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Training income	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	O(O)I	Grant income (Coronavirus)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Research & development expenditure tax credit (RDEC) income	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		"Other" other operating income	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Non cash flow items	TFA depreciation	Leasehold property (Right of Use) (ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Clinic fit out & equipment (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Other TFA (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Software	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	Unexpected loss in value of TFA	Leasehold property (ROU)						
		Clinic fit out & equipment (Owned & ROU)						
		Other TFA (Owned & ROU)						
		Software						
		EBIT	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Other noteworthy	Included in above P&L	Redundancy of staff and general restructuring	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		"Centralised management costs"	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

Source: CMA analysis based in the first instance on the entity financial statements of Vets Now Emergency Limited and adjusted using supplementary financial information provided by IVC to the CMA.

Notes on preparation of adjusted financial information for Vets Now

7.47 Vets Now is a specialist OOH provider that IVC acquired in 2019, just before the period of review. Its business model for providing OOH services is predicated on host clinics (which are not necessarily IVC clinics) [✂]. As such Vets Now is capital light as it does not need to invest extensively in either its own premises or equipment.

7.48 However, there are three Vets Now hospitals / RCVS-specialist led referral centres, which were owned by Vets Now at the time of acquisition by IVC, of which Vets Now still retains operational management. Vets Now retains its own corporate identity and branding within IVC and maintains its own set of accounts.

7.49 For the above reasons we therefore decided at the working paper stage to analyse Vets Now separately from the rest of IVC's UK clinical veterinary operations.

7.50 We separately estimated the fit-out costs for the three hospitals / RCVS-led specialist clinics and the related depreciation charge.

7.51 Regarding intangibles, we did not consider that the 'customer acquisition' asset was as relevant to Vets Now in the same way as it is to local clinics. Before setting up an OOH service within a clinic, Vets Now will be negotiating on the one hand with a clinic where it is looking to host an OOH operation and on the other hand further feeder local clinics which are also seeking to outsource to Vets Now the provision of OOH services to their own clients. In such a model, the clients of the OOH clinic are directed to these clinics by their own local clinic. We therefore did not make an adjustment to include a 'customer acquisition' asset in Vet Now's capital base in the working paper and we acknowledged in that working paper that further thought on this issue was warranted.

7.52 In its response to the working paper where we presented both a balance sheet as well as a profit and loss statement for Vets Now, IVC told us that the balance sheet we had prepared was not at all reflective of the capital employed in providing the out-of-hours service due to its unique model of operating out of host practices.[535]

7.53 IVC highlighted that Vets Now had developed the following key intangible assets:

(a) [✂].

(b) [✂].

[535] [✂].

(c) [✂].[536]

7.54 Our view is that for tangible fixed assets any omission would relate to those tangible fixed assets which Vets Now brought into the host clinics but retained ownership of and also its IT and software assets and related depreciation charges. IVC told us that Vets Now invested in its own emergency-specific state-of-the-art equipment to give clients a wide range of treatment options in the OOH and Emergency and Critical Care (ECC) environment where cases could be more complex.[537]

7.55 However, we also acknowledge that we had not placed any value on its intangible fixed assets. We understand that Vets Now has grown organically over the many years since it was founded in 2001 and it has sought to lead the development of the specialist discipline of emergency and critical care in the UK using dedicated staff. Vets Now also seeks to attract both pet owners whose daytime clinic is not necessarily a registered partner practice and those who do not have a regular vet.[538]

7.56 Because of these omissions regarding its fixed asset base we only present our analysis for the profit and loss statement of Vets Now.

Linnaeus

7.57 The balance sheet and profit and loss statements for Linnaeus are set out below in line with the approach we set out in section 3 above under the sub-section 'Adjustments to the LVGs financial information'. We then set out further information about what implementing that approach meant in Linnaeus's case.

[536] [✂].
[537] [✂].
[538] [✂].

Linnaeus' adjusted financial statements

Table 7.7: Linnaeus local clinics adjusted balance sheet statement (base case) £m

		As at December					
		[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Fixed capital employed	Intangibles: customer acquisition & workforce based on costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Leasehold property (Right of Use) (ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Clinic fit out & equipment (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Other Tangible Fixed Asset (TFA) (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Software	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Working capital employed	Other non-current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Non-current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Provisions re P&L costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Total operating capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Split as to:	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Fixed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Working	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based in the first instance on the US GAAP internal financial statements of Linnaeus UK as [✂] and adjusted using supplementary financial information provided by Linnaeus to the CMA.

Table 7.8: Linnaeus local clinics adjusted operating profit and loss statement (base case) £m

			Primary Care					
			Year to December					
			2020	*2021*	*2022*	*2023*	*2024*	*2025*
Cash Flow items	Revenue	Revenues	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	COS	Cost of sales - materials and labour	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	AE	Administrative expenses - site costs	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Administrative expenses - non-site costs	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	O(O)I	Research and development tax credit [O(O)I]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Non-cash flow items	TFA depreciation	Leasehold property (ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Clinic fit out & equipment (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Other TFA (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Software and IT infrastructure	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	Unexpected loss in value of TFA	Leasehold property (ROU)						
		Clinic fit out & equipment (Owned & ROU)						
		Other TFA (Owned & ROU)						
		Software and IT infrastructure						
		EBIT before certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Income from government R&D grants (RDEC)			[redacted]			
		External advisory costs regarding financing / re-financing			[redacted]			
		Management fees levied by other parts of the Mars Inc group	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Third party costs relating to CMA investigations	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Costs associated with / impairments arising from clinic closures			[redacted]			
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Total for certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		EBIT after certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

Source: CMA analysis based in the first instance on the US GAAP internal financial statements of Linnaeus UK [✂] and adjusted using supplementary financial information provided by Linnaeus to the CMA.

[✂]

Table 7.9: Linnaeus referral centres adjusted balance sheet statement (base case) £m

		As at December					
		2020	*2021*	*2022*	*2023*	*2024*	*2025*
Fixed capital employed	Intangibles: customer acquisition & workforce based on costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Leasehold property (Right of Use) (ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Clinic fit out & equipment (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Other Tangible Fixed Asset (TFA) (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Software	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Working capital employed	Other non-current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Non-current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Provisions re P&L costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Total operating capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Split as to:						
	Fixed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Working	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based in the first instance on the US GAAP internal financial statements of Linnaeus UK as [✂]and adjusted using supplementary financial information provided by Linnaeus to the CMA.

Table 7.10: Linnaeus referral centres adjusted operating profit and loss statement (base case) £m

			Referrals					
			Year to December					
			2020	*2021*	*2022*	*2023*	*2024*	*2025*
Cash Flow items	Revenue	Revenues	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	COS	Cost of sales - materials and labour	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	AE	Administrative expenses - site costs	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Administrative expenses - non-site costs	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	O(O)I	Research and development tax credit [O(O)I]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Non cash flow items	TFA depreciation	Leasehold property (ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Clinic fit out & equipment (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Other TFA (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Software and IT infrastructure						
	Unexpected loss in value of TFA						[redacted]	
		Leasehold property (ROU)						
		Clinic fit out & equipment (Owned & ROU)					[redacted]	
		Other TFA (Owned & ROU)						
		Software and IT infrastructure						
		EBIT before certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Income from government R&D grants (RDEC)			[redacted]			
		External advisory costs regarding financing / re-financing			[redacted]			
		Management fees levied by other parts of the Mars Inc group	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Third party costs relating to CMA investigations	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Costs associated with / impairments arising from clinic closures			[redacted]			
		Total for certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		EBIT after certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

Source: CMA analysis based in the first instance on the US GAAP internal financial statements of Linnaeus UK [✂] and adjusted using supplementary financial information provided by Linnaeus to the CMA. [✂].

Table 7.11: Linnaeus cost items that relate to both local clinics and referral centres

		2020	2021	2022	2023	2024	2025
Included in above P&Ls	Third party costs relating to CMA investigations	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Administrative expenses - costs supporting both PC and R	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Administrative expenses - management fees supporting both PC and R	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based in the first instance on the US GAAP internal financial statements of Linnaeus UK as [✂] and adjusted using supplementary financial information provided by Linnaeus to the CMA. Note PC = Primary Care, Linnaeus' term for those practices it has acquired which are wholly or predominately local clinic. R = Referrals, Linnaeus' term for those practices it has acquired which are wholly or predominately RCVS-specialist led referral centres.

Notes on preparation of adjusted financial information for Linnaeus: local clinics and referral centres

7.58 Linnaeus is part of the Mars corporate group, a privately owned conglomerate that is headquartered in the US. Linnaeus prepares both its internal and external financial statements on a US GAAP basis, which is a similar basis of preparation to IFRS (International Financial Reporting Standards) and UK GAAP. Linnaeus prepares its financial statements both in UK £s and US $s. The information it provided to us was in UK £s.

7.59 Since FY2022 Linnaeus has been capitalising its property leases under ASC-842,[539] an approach to capitalising right of use assets that is similar to IFRS16 and it provided us with information on that basis. It provided us with estimates for the FY2020 and FY2021 for its property leases and the associated right of use asset depreciation.

7.60 Linnaeus provided us with a detailed profit and loss account and balance sheet for its UK veterinary operations. For internal reporting purposes it allocates the individual veterinary practices (each of which may well comprise many individual clinics) that it has acquired between its 'Primary Care' and 'Referrals' divisions. The former primarily relates to local clinics and the latter RCVS-specialist led referral centres.

7.61 Linnaeus' Referrals division expanded in FY2021 as the result of the acquisition of the five referral centres that had comprised Pets at Home's Specialist Division.[540] As a result, [✂].

7.62 As a result, Linnaeus was able to identify the revenues and costs (down to site costs) associated with the two 'divisions'. It also records separately the tangible fixed assets associated with the two divisions. Because [✂], we considered it was possible to generate estimates for the profitability of its Primary Care 'division' separately from its Referrals 'division'. However, this exercise did involve apportioning some costs that are shared between the two divisions and working capital. We apportioned these costs based on the respective divisions relative share of total cost of sales,[541] which was accounted for by Linnaeus separately, to avoid the circularity involved in apportioning costs on the basis of revenues or profit share.

7.63 This approach, while not a full accounting separation exercise (because it assumes that the shared costs on a standalone basis would be at the same level

[539] Leases (Topic 842), Financial Accounting Standards Board, July 2021.
[540] Pets at Home's Specialist Division joins Linnaeus family, Linnaeus press notice, 1 December 2020, and Pets at Home Annual Report and Accounts 2021, pp 8, 59, 164 and 199—200.
[541] Cost of sales in this case comprised materials and veterinary labour.

as they would be on an integrated basis), should nevertheless give us some insight on the relative performance of Linnaeus's two divisions.

7.64 Linnaeus also has [✂] amounts of non-site costs, those that are incurred in the UK by Linnaeus directly itself and [✂]. These elements of costs are set out in the table above.

7.65 Linnaeus told us that as [✂].[542,543, 544]

7.66 [✂].

7.67 [✂].[545]

Medivet

7.68 The balance sheet and profit and loss statements for Medivet are set out below in line with the approach we set out in section 3 above under the sub-section 'Adjustments to the LVGs financial information'. We then set out further information about what implementing that approach meant in Medivet's case.

[542] [✂]
[543] [✂]
[544] [✂]
[545] [✂]

Medivet's adjusted financial statements

Table 7.12: Medivet adjusted balance sheet statement (base case) £m

		As at April					
		2020	*2021*	*2022*	*2023*	*2024*	*2025*
Fixed capital employed	Intangibles: customer acquisition & workforce based on costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Leasehold property (Right of Use) (ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Clinic fit out & equipment (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Other Tangible Fixed Asset (TFA) (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Software	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Working capital employed	Other non-current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Non-current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Provisions re P&L costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Total operating capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Split as to:						
	Fixed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Working	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based in the first instance on the entity financial statements of Medivet Group Limited and adjusted using supplementary financial information provided by Medivet to the CMA.

Table 7.13: Medivet adjusted operating profit and loss statement (base case) £m

			Year to April					
			2020	*2021*	*2022*	*2023*	*2024*	*2025*
Cash Flow items	Revenue	Revenues	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	COS	Cost of sales	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Cost of sales (other identified items)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	AE	Administrative expenses	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Administrative expenses (other identified items)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	O(O)I	Income from Coronavirus Job Retention Scheme [O(O)I]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Loss/(gain) on disposal of other assets/liabilities	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Non cash flow items	TFA depreciation	Leasehold property (ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Clinic fit out & equipment (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Other TFA (Owned & ROU)						
		Software	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	Unexpected loss in value of TFA	Leasehold property (ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Clinic fit out & equipment (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Other TFA (Owned & ROU)						
		Software	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	Gains / losses due to Δ in cost of TFA	Leasehold property (ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		EBIT before certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Income from government R&D grants (RDEC)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Non-underlying items: Legal professional and compliance	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Third party costs relating to CMA investigations	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Restructuring costs	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Total for certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		EBIT after certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Other noteworthy items	Included in above P&L	Third party costs relating to CMA investigations	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		of which were settled by Medivet's majority shareholders					[redacted]	[redacted]

Not included in above P&L	Loss on disposal of businesses in lieu of Phase II reference	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Deferred / contingent consideration passing through P&L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Transaction costs related to practice acquisitions	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Costs associated with the legal reorganisation of Medivet on change of ultimate owners	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Impairment charge on goodwill	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based in the first instance on the entity financial statements of Medivet Group Limited and adjusted using supplementary financial information provided by Medivet to the CMA.

Notes on preparation of adjusted financial information for Medivet

7.69 The source set of financial statements is Medivet Group Limited. This is a set of entity financial statements. This is the set of financial statements into which Medivet [✂].

7.70 Medivet proposed only two adjustments to the information contained within these statements and then only for FY2024 as follows:

(a) [✂].

(b) [✂].

7.71 Medivet confirmed that the cost base for Medivet Group Limited included the total profit share for Medivet's branch partners.[546] [547] Medivet had previously told us that it could not easily ascertain what element of this total (£[✂]million for FY2024) would be an appropriate salary level for these branch partners. We therefore did not seek to make an adjustment to remove an estimate of the profit element. So, in this respect Medivet's profit is understated. (On the (arbitrary) assumption that 20% of this would be profit share, then one would have an adjustment that would increase EBIT by £[✂] million a year in FY2024. This would increase ROCE by [✂]% percentage points (ie from [✂]% to [✂]% over the period of review).

7.72 We excluded the £21.9 million loss on disposal of businesses that Medivet reported in FY2024 in lieu of a Phase II merger control reference.[548] According to the notes of Medivet Group Limited financial statements for FY2024 these disposals included a mix of disposing of practices and customer lists.[549]

7.73 We also excluded the £11.5 million of costs relating to the sale of Medivet Group Holdings Limited that were reflected in the Medivet Group Limited financial statements for FY2022.[550] In FY2022 Medivet was sold on to a new set of owners. These costs relate to the trading in Medivet as a business as a whole and we therefore excluded them as a non-operating item.

7.74 We have also excluded the impairments of certain tangible fixed assets that Medivet had included within its reporting for Medivet Group Limited during the period, including the £11.5 million impairment reported in 2022,[551] shortly after

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[546] Medivet's branch partners do not earn a salary as such, so this profit share will be a combination of salary and a return to the branch partner as an equity holder in the clinic(s) of which he or she is a branch partner.
[547] [✂].
[548] Please note that this loss figure is calculated on the basis of preparation in the financial statements and not on our adjusted basis. It for example includes write off of goodwill.
[549] Medivet Group Limited Annual report and financial statements for the year ended on 30 April 2024, Notes to the financial statements 15 and 32 and also p 7.
[550] Medivet Group Limited Annual report and financial statements for the year ended on 30 April 2022, Notes to the financial statements 11.
[551] Medivet Group Limited Annual report and financial statements for the year ended on 30 April 2022, Notes to the financial statements 16.

Medivet was sold on to new owners, [✂].[552] Our general approach is that we seek to value and depreciate all tangible fixed assets that are being used within the business on the basis of depreciated replacement cost rather than their book value. Were we to do otherwise, we would not be able to assess whether the firm was making an economic return or not on that basis.[553] This approach is also required to maintain consistency between what is reflected in the profit and loss in any one period and the values appearing in the balance sheet at the end of that period.

7.75 It is worth noting [✂], we have had to base certain FY2020 and FY2021 items on their values reported for subsequent years.

7.76 In three of the periods Medivet reported impairments on its goodwill, including most recently £53.6 million and £86.4 million in FY2024 and FY2025 respectively.[554] The FY2024 impairment was a result of upwardly adjusting the discount rate applied to assessing whether the carrying value for goodwill exceeded its recoverable amount. These impairments have all been excluded.

Pets at Home

7.77 The balance sheet and profit and loss statements for Pets at Home (PAH) are set out below in line with the approach we set out in section 3 above under the sub-section 'Adjustments to the LVGs financial information'. We then set out further information about what implementing that approach meant in Pets at Home's case.

[552] Medivet told us that it had only closed [✂] clinic(s) during this period. See Section 4 (Intangible assets) within Appendix C.
[553] Impairment losses are the mechanism by which firms recognise that their previous book carrying values are now overstated regarding these assets' future earning potential. The purpose of this analysis is, however, to reveal poor trading performance in subsequent periods.
[554] Medivet Group Limited Annual report and financial statements for the year ended on 30 April 2024, Notes to the financial statements 16. Medivet Group Limited Annual report and financial statements for the year ended on 30 April 2025, Notes to the financial statements 16.

Pets at Home adjusted financial statements

Table 7.14: Pets at Home adjusted balance sheet statement (base case) £m

		As at March					
		2020	*2021*	*2022*	*2023*	*2024*	*2025*
Fixed capital employed	Intangibles: customer acquisition & workforce based on costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Leasehold property (Right of Use) (ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Clinic fit out & equipment (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Other Tangible Fixed Asset (TFA) (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Software	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Working capital employed	Other non-current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Non-current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Provisions re P&L costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Total operating capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Split as to:						
	Fixed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Working	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based in the first instance on the entity financial statements of individual Pets at Home branded veterinary clinics and adjusted using supplementary financial information provided by Pets at Home to the CMA.

Table 7.15: Pets at Home adjusted operating profit and loss statement (base case) £m

			Year to March					
			2020	*2021*	*2022*	*2023*	*2024*	*2025*
Cash Flow items	Revenue	Revenues	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	COS	Cost of sales excluding PAH COGS management fee	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	AE	Administrative expenses	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		Income from Coronavirus Job Retention Scheme [O(O)I]						
	O(O)I	Research and development tax credit [O(O)I]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Non cash flow items	TFA depreciation	Leasehold property (ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		Clinic fit out & equipment (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		Other TFA (Owned & ROU)						
		Software and IT infrastructure	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Unexpected loss in value of TFA	Leasehold property (ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		Clinic fit out & equipment (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		Other TFA (Owned & ROU)						
		Software and IT infrastructure						
		EBIT before certain highly variable operational items	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		Impairments arising from clinic closures	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		Third party costs relating to CMA investigations	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		Total for certain highly variable operational items	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		EBIT after certain highly variable operational items	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Other noteworthy items	Included in above P&L	Pets at Home Central costs (50% of total)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		Pets at Home PetCare app (Polestar)(50% of total)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
		Pets at Home Software subscriptions (32% of total)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Notional additional practice owner remuneration (PAH estimate)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based in the first instance on the entity financial statements of individual Pets at Home branded veterinary clinics and adjusted using supplementary financial information provided by Pets at Home to the CMA.

Notes on preparation of adjusted financial statements for Pets at Home

7.78 Each local clinic that Pets at Home establishes is set up as a limited company. As such Pets at Home ensures that each company maintains and files at Companies House its own set of statutory accounts. Because these accounts only relate to a single local clinic, these accounts are prepared under the reporting regime for small companies and benefit from an audit exemption.

7.79 Pets at Home seeks to install a practice owner in each of its local clinics wherever it can find a suitable candidate. Practice owners are often veterinarians but may also be practice managers or veterinary nurses. These corporate entities are run on a joint venture basis between Pets at Home and the practice owner(s) of that individual local clinic. Because the set up of these joint ventures is such that the practice owner(s) owns the upside benefit should the local clinic become commercially successful,[555] Pets at Home does not consolidate the financial results of these local clinics into its group financial statements. Instead, Pets at Home accounts for the management and other fees it levies on these joint venture corporate entities for the services it (Pets at Home) provides to these joint venture entities.

7.80 However, where Pets at Home cannot find a suitable candidate to become the practice owner of a local clinic that it has established,[556] Pets at Home has full control of that local clinic and therefore is required to consolidate the results of that local clinic within its group financial statements.

7.81 We, however, are interested in the performance of the business of local clinics regardless of how each individual clinic is owned and managed. We therefore asked Pets at Home to aggregate the balance sheet balances and profit and loss classifications as reported in the individual entity accounts for all Pets at Home branded local clinics. That was the starting point for our analysis.

7.82 As with the other LVGs, we are looking at the performance of Pets at Home's clinics on a portfolio basis, a way of viewing the Pets at Home veterinary clinic estate that Pets at Home itself also adopts.[557]

7.83 Having aggregated the results of all the local clinics, we asked Pets at Home to substitute the management fees it had levied on those of its local clinics owned on a joint venture basis[558] with a measure of the underlying costs of supply to Pets at

[555] Practice owners are able to sell on their share in the local clinic to a successor, thereby releasing the equity for him or herself that the practice owner has been able to generate by operating that local clinic.
[556] [✂], Pets at Home manages the local clinic on its own until it can find a suitable practice owner to partner with it on a joint venture basis.
[557] Pets at Home Annual Report and Accounts 2020, p 60.
[558] Note that Pets at Home does not levy management fees on those local clinics that it controls, that it where there is no practice owner operating that local clinic on a joint venture basis with Pets at Home.

Home for the services that it renders to those local clinics. As a result, Pets at Home estimated the following types of costs to be included within our analysis:

(c) costs incurred by the Vet Group reporting segment within Pets at Home

(d) costs incurred by its Central reporting segment such as:

(i) IT infrastructure related to its in store veterinary practices and related depreciation not accounted for in the respective entity financial statements;

(ii) leasehold improvements related to its in store veterinary practices and related depreciation not accounted for in the respective entity financial statements;

(iii) IT costs;

(iv) central costs;

(v) costs related to the development of its PetCare app for its customer (Polestar); and

(vi) software subscriptions.

7.84 The costs referred to above relate to both the clinics that Pets at Home directly controls itself and those it operates on a joint venture basis with a practice owner. The intention is that the cost base for our analysis of Pets at Home's profitability should relate to the operation of the full portfolio of Pets at Home-branded local clinics.

7.85 Pets at Home also sought to include the interest costs it incurs in providing top up loans to those joint venture practices needing funding additional to that initially subscribed by the practice owner (£30,000) and Pets at Home itself (also £30,000) and that provided by the bank loan to the local clinic (up to £450,000). We however did not include this adjustment because this is a financing cost that is taken account of when determining the cost of capital.

7.86 Pets at Home also sought to include the (very significant) bank loan and other creditor write offs reported in the individual entity financial statements that it had paid off (in lieu of the entity defaulting on the loan). We did not include these amounts as they related to the financing, not the operation, of this business. We sought however to include any impairments that had been booked into the entity financial statements but found that there were none apart from an amount that was described to us as 'accelerated depreciation' in FY2020.[559] We thought that, as this depreciation charge related to clinics that had been closed down by Pets at

[559] [✂].

Home, that this item was in fact an impairment loss. We therefore estimated this amount and included this as an impairment loss within FY2020.

7.87 Pets at Home's management fees, however, are not intended to recover the costs of space utilised by those local clinics which are located within a Pets at Home store (which roughly two thirds of them are). For this cost, Pets at Home levies a sublease rental charge alike to both local clinics operated on a joint venture basis and those which it directly controls itself. This subleasing charge is based on the local clinic's percentage of floorspace (in square feet) that it occupies within the Pets at Home retail store within which it is located. The level of the subleasing charge is determined on an individual clinic basis.[560]

7.88 For our purposes however the accounting treatment within the individual entity accounts[561] for the cost of this instore space is different to the approach taken by the other LVGs for the same type of assets. There, assets utilised under property leases are accounted for as right of use assets. As a result, Pets at Home used the software it uses to generate values for its Pets at Home store right of use property lease assets as reported in its group financial statements to generate comparable right of use asset values and related right of use asset depreciation charges for the space occupied by in-store local clinics for use within our analysis.

7.89 Pets at Home also conducted a similar exercise to ascertain capital values and related depreciation charges for those property leases that are utilised by its standalone clinics which are operated on a joint venture basis. Pets at Home already had these right of use asset figures for those local clinics which it controlled at the respective balance sheet dates.

7.90 We therefore swapped out the rental charges reflected in the aggregations of the entity financial statements for the asset and depreciation charge estimates that Pets at Home had generated for us.

7.91 In our analysis we did not include the five specialist referral centres that Pets at Home operated up and until the point when it sold them all onto Linnaeus in December 2020. See above for further information. These referral centres have been accounted for within Linnaeus for the period FY2021 to FY2024.

7.92 Pets at Home told us that our analysis for it was subject to survivorship bias. It, Pets at Home explained, had undergone a major restructuring (Project Light) in 2019 in which it had closed underperforming FOPs, and so the remaining cohort were already carefully positioned for success. Pets at Home told us that it had incurred large impairment costs related to closing the underperforming FOPs. We

[560] [✂].
[561] All of Pets at Home local clinic entities fall within the definition of small companies and are therefore not obliged under the small company reporting regime to account for property leases as right of use assets.

however had focused on the period FY20 to FY24 where its portfolio no longer included those underperforming FOPs.[562]

7.93 We therefore looked more closely at how Pets at Home had accounted for the closure of clinics under the auspices of Project Light. Pets at Home decided to go ahead with a programme of clinic closures in its FY19, so it was in this period that it was required to come up with its then best estimate of the financial impact on the Pets at Home group and reflect that within its costs for the period. The financial impact of these closures, however, was only reflected within the relevant entity accounts when these closure costs actually happened. It was not until the end of May 2020 that clinic closures were fully complete. So, some closures occurred in FY19, around 30 occurred in FY20[563] and a few occurred in FY21.[564] So while it is the case that not all its Project Light clinic closures were included within our analysis a substantial number were fully reflected.

7.94 A more general point is that within our analysis we are seeking to reflect the costs associated with closing down a clinic when the closure actually occurs and not when the management take a firm decision to close a clinic. The taking of a firm decision is the trigger point within the accounting standards for group financial statements for requiring the recognition of losses. That, however, is not a meaningful approach for us to take here – the firm would end up continuing to earn profits on a zero capital base. What is more meaningful is for us to assess profitability on the unimpaired (ie full) value of capital employed until the clinic has closed down.

7.95 Pets at Home also told us that it would be more appropriate for us to reflect within our analysis the management fees it levies on its local clinics rather than the underlying costs of the business support services on the grounds that FOPs would have to incur the costs of these business support services themselves at a higher cost without the benefits of economies of scale and efficiencies from its business model.[565] This however misunderstands the basis on which we are conducting our analysis of Pets at Home's profitability: we seek to assess it on the basis of the performance of the clinics as a whole as though they were owned by a single firm. In consequence, we seek to substitute these transfer charges with the underlying cost of supply.

VetPartners

7.96 The balance sheet and profit and loss statements for VetPartners are set out below in line with the approach we set out in section 3 above under the sub-

[562] [✂].
[563] [✂].
[564] Pets at Home reported in its FY2020 annual report signed in May 2020 that this one-off recalibration was now complete, p 40.
[565] [✂].

section ‘Adjustments to the LVGs financial information’. We then set out further information about what implementing that approach meant in VetPartners’ case.

VetPartners' adjusted financial statements

Table 7.16: VetPartners adjusted balance sheet statement (base case) £m

		As at June					
		2020	*2021*	*2022*	*2023*	*2024*	*2025*
Fixed capital employed	Intangibles: customer acquisition & workforce based on costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Leasehold property (Right of Use) (ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Clinic fit out & equipment (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Other Tangible Fixed Asset (TFA) (Owned & ROU)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Software	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Working capital employed	Other non-current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current assets	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Non-current liabilities	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Provisions re P&L costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Total operating capital employed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Split as to:						
	Fixed	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Working	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based in the first instance on the entity financial statements of VetPartners Group Limited and adjusted using supplementary financial information provided by VetPartners to the CMA.

Table 7.17: VetPartners adjusted operating profit and loss statement (base case) £m

			As at June / year to June					
			2020	2021	2022	2023	2024	2025
Cash flow items	Revenue	Revenues	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	COS	Cost of sales	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	AE	Administrative expenses	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	O(O)I	Grant income (Coronavirus)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		"Other" other operating income	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Non cash flow items	TFA depreciation	Leasehold property (Right of Use) (ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Clinic fit out & equipment (Owned & ROU)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Other TFA (Owned & ROU)						
		Software						
	Unexpected loss in value of TFA	Leasehold property (ROU)						
		Clinic fit out & equipment (Owned & ROU)						
		Other TFA (Owned & ROU)						
		Software						
		EBIT before certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Income from government R&D grants (RDEC)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Non-financial element (such as legal fees) of debt refinancing costs	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Third party costs relating to CMA investigations	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Costs associated with / impairments arising from clinic closures			[redacted]			
		Total for certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		EBIT after certain highly variable operational items	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Other noteworthy items	Included in above P&L	Value of VetPartners Limited group's corporate costs eliminated	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

	Reorganisation and restructuring costs						
	Business transformation costs			[✂]			
Not included in above P&L	Profit on disposal of businesses (/in lieu of phase II reference)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Deferred / contingent consideration passing through P&L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	Transaction costs related to practice acquisitions	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis based in the first instance on the entity financial statements of VetPartners Group Limited and adjusted using supplementary financial information provided by VetPartners to the CMA.

Notes on preparation of adjusted financial information for VetPartners

7.97 The source set of financial statements for VetPartners is VetPartners Group Limited. This is a set of consolidated financial statements which contain all of its UK clinical activity but, unlike for CVS Group plc, VetPartners Group Limited is not the top holding company in the corporate group.

7.98 As VetPartners undertakes other activities other than UK clinical veterinary services it proposed adjustments as follows:

(a) to remove non-UK elements (veterinary and non-veterinary);

(b) to remove Laboratory activities;

(c) to remove Crematoria activities;

(d) to remove its Retail online pharmacy; and

(e) to remove the relevant element of Central admin that related to activities excluded.

7.99 For the latter adjustment VetPartners, like IVC, based it on previous analysis it had prepared when responding to a previous financial RFI, RFI6.

7.100 Note the analysis for the profit and loss presented above does not directly identify the significant amounts of exceptional items that are reported within the Strategic Report for VetPartners Group Limited. These exceptional items carry descriptions such as:

(a) reorganisation and restructuring costs;

(b) business transformation costs;

(c) acquisition and integration costs; and

(d) other non-recurring exceptional costs.

7.101 The original template of figures that we had extracted for VetPartners Group Limited for VetPartners to review inadvertently omitted these numbers entirely and, unlike for [✂], we cannot simply update our analysis for these omissions because at least some element of these exceptional items in some periods will relate to excluded activities.

7.102 VetPartners, however, did identify for us separately the gains and losses it made on disposing of practices in lieu of a Phase II merger control reference in FY2023

and FY2024. These gains and losses have been excluded as they relate to trading in veterinary practices. [✂][566] [✂].

7.103 In the penultimate period (FY2024) VetPartners reported an impairment on its goodwill and other intangible assets of £123.9 million (mainly relating to goodwill)[567] including £[✂] million[568] that related to UK clinical veterinary activity. According to information given in the financial statements for FY2024, the impairments of goodwill related to its equine and farm practices in the UK.[569] Impairments of goodwill are in any case excluded on principle.[570]

[566] [✂]
[567] VetPartners Group Limited Annual Report and Consolidated Financial Statements for the year ended 30 June 2024, Notes to the financial statements 12, p 47.
[568] [✂]
[569] VetPartners Group Limited Annual Report and Consolidated Financial Statements for the year ended 30 June 2024, p 49.
[570] VetPartners Group Limited Annual Report and Consolidated Financial Statements for the year ended 30 June 2024, p 49.