THE GRAND RIVER VETERINARY HOSPITAL: A MERGER DECISION

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ACADEMIC ABSTRACT

The Grand River Veterinary Hospital (GRVH) is a two-doctor small animal veterinary clinic owned by Dr. Lauren Hudson. Dr. Hudson has found that her practice has outgrown its existing building and must decide whether to merge with a three-doctor veterinary clinic nearby. The current trend in veterinary medicine is to consolidate practices to increase operational efficiency and help pay for expensive medical equipment. Deciding to merge with another clinic involves considering the financials, the other clinic’s culture, how it will affect the staff, and whether the current clientele will follow Dr. Hudson to a new, larger practice.

EXECUTIVE SUMMARY

For the past ten years, Dr. Hudson has owned the Grand River Veterinary Hospital (GRVH), a two-doctor small animal veterinary clinic. Her practice has differentiated itself from many other veterinary clinics by providing clients and their pets with high quality medicine and personal attention in a small clinic atmosphere. The GRVH’s business model has been so successful that the clinic has outgrown its current building. In addition, the veterinary technology Dr. Hudson wishes to provide her patients is too expensive to attain on her own. Consequently, Dr. Hudson was deciding whether to merge the GRVH with a larger clinic nearby.

A breakeven analysis and comparison of the advantages and disadvantages indicate that Dr. Hudson should cautiously pursue the merger with Eastwood Veterinary Clinic (EVC). In doing so, Dr. Hudson needs to figure out how to go forward with the merger in a way that keeps her key staff and clientele on board. She also needs to make sure that she is able to maintain a similar level of quality of care and personal attention at the larger facility.

This case provides an opportunity for students to analyze a merger decision in a service-based field. They are able to use breakeven analysis to focus on the financial aspects of the merger. Students are also able to consider non-financial issues that are vital to a merger decision: preservation of the company’s culture, continuation of its competitive advantage, and motivating staff and clients to move to a new environment. The case allows students to utilize operations management concepts, such as quality management and operations strategy, as they consider how the merger will affect efficiency, quality, and productivity. Students will also use marketing concepts as they consider how to promote a merged company.
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INTRODUCTION

“This building has served me well,” Dr. Lauren Hudson, owner of the Grand River Veterinary Hospital, thought to herself as she sat in her office one day in 2006. “It was a good place to start my own practice. Its smallness has allowed me to give my patients the high quality, personalized care the clinic is now known for. It was also a good investment; I was able to purchase the clinic on my own and revenues have grown tremendously over the past ten years.” As she reminisced on the past decade, she also thought about what needed to change about the clinic in order for it to continue to grow in the future.

“The building is simply too small for my current practice and is not set up for the type of care I would like to provide in the future. There is no room for additional equipment, the treatment and surgery areas are cramped, there is no meeting room for my staff to gather, and the flow of the building isn’t very efficient. I cannot provide the wide variety of procedures I would like to due to space constraints. I believe that the only way for the practice to continue to grow and to provide the best quality pet healthcare is to move to a new building.”

Dr. Hudson decided to look into building a new facility, but found that the cost of doing so would require her to bring in another partner. Also, the only locations available to build on were located only miles from at least four other veterinary hospitals. This meant more competition and duplicate services. She then turned to the idea of merging with an existing practice that had room to grow. She knew that mergers were difficult, especially in the field of medicine, because clinics tended to work independently of one another and in competition, rather than in cooperation and coordination. Also, even if another clinic provided a similar level of quality of care, it would be difficult to find one with a similar culture and management style.

On the other hand, she knew that merging would mean that her practice and another could consolidate their equipment, utilize the same location without competing against each other, and share the costs of upgrading the combined practice to lessen the financial burden on each of the owners. Dr. Hudson thought of a colleague she had known for years who owned a clinic in the area she was looking to relocate to. The clinic, Eastwood Veterinary Clinic, offered more space, a larger array of services and equipment, and provided similar high quality healthcare - but would it be a good match for the Grand River Veterinary Hospital?

GRAND RIVER VETERINARY HOSPITAL: AN OVERVIEW

The Grand River Veterinary Hospital (GRVH) was a two-doctor practice (Dr. Hudson is the owner and Dr. Johnson was a salaried associate) with a support staff of fourteen: one practice manager, two receptionists, three licensed veterinary technicians, three veterinary assistants, and five part-time kennel attendants. It was a small animal practice, which meant that the doctors saw household pets: dogs, cats, and the occasional “pocket pet” (rabbits, guinea pigs, hamsters, etc.). The building had been used as a veterinary clinic for over forty years, with Dr. Hudson

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1 This case (disguised) is based on discussions and e-mail correspondence with Dr. Lauren Hudson during the summer of 2007.
becoming its third owner in 1996. Over the past ten years, the GRVH had seen considerable growth in revenues, from $240,000 in gross revenues in 1996 to $685,000 in 2007. Dr. Hudson noted that most of this growth was due to providing new services and increasing prices. Patient growth had remained quite steady, rising only about three percent since 1996.

The 1,600 square-foot practice had a waiting area, two examination rooms, a pharmacy/lab, treatment area, small surgery and x-ray areas, and an office that was shared by the veterinarians and practice manager. It also had an 800 square-foot basement that was used as a small kennel facility. The kennels held about twenty dogs, most of which were boarded in cages, and brought in about $40,000 in revenues annually. The price structure at the GRVH was comparable to other clinics in the area that provided a similar level of care. Compared to all clinics in the area (disregarding level of care), its shopped fees (i.e., office calls, vaccines, routine surgeries and procedures) were in the upper twenty-five percent. Dr. Hudson noted that it was difficult to compare non-shopped fees (i.e., non-routine surgeries, specialized medicine) because there was so much variability in what clinics provided and in how they charged for those services.

The clinic had about 1,350 active clients and was open six days a week, many days until 7 p.m. to provide clients with convenient appointment times. Dr. Hudson maintained that the clinic competed by providing quality patient care with a high level of client contact. When clients brought their pets to GRVH, they met personally with either Dr. Hudson or Dr. Johnson, both of whom knew them and their pets very well. Both veterinarians also made sure to spend sufficient time with clients to answer all their questions and explain any needed procedures thoroughly, thereby reassuring clients that their pets would receive the best care available. The clinic also considered itself a patient advocate, meaning that the staff worked to get the pet whatever it needed, even if that meant referring the client to another practice because the GRVH did not possess the necessary equipment to treat it properly.

In addition to providing excellent client and patient care, the GRVH also worked on several community service projects. The clinic staff visited elementary and preschool classes to educate young children on bite prevention. The clinic was also known for its kitten adoption program; the waiting area contained an enclosed area for stray kittens to stay while the clinic tried to find them homes for them by advertising on their exterior sign. Over the years, the clinic had placed hundreds of cats in loving homes.

When asked what the management style was like at the GRVH, Dr. Hudson explained that it was “semi-open book.” Employees provided feedback and worked together to perform scheduling tasks, and helped to hire new team members. The staff met every three weeks to make decisions regarding the clinic and to work on continuing education. Dr. Hudson said that although she liked to involve her staff in decision-making, she reserved the right to make significant decisions on her own.

THE VETERINARY MEDICINE INDUSTRY

Dr. Hudson’s decision to look into merging with an existing veterinary practice was a fairly common topic in the field of veterinary medicine in 2007. Although the size of the industry has remained steady over the past decade, technology had changed the industry dramatically,
resulting in more procedures being performed and more money being spent on pet care than ever before. Veterinarians were now regularly using technology that was once reserved for human use, such as lasers, endoscopes, ultrasounds and digital radiology. However, offering these technologies involved large capital outlays that many small clinics either could not afford or could not justify from a profitability standpoint. This made it difficult for smaller practices to keep up with technological advancements in the field.

While the tendency was previously for doctors to operate their own practices individually, or run a two-doctor practice, this had led to considerable market congestion. Particularly in suburban environments, there were often several small animal practices within a few miles of each other, each providing a similar level of care. The owners of these small one- or two-doctor practices also were often under considerable stress from having to work seventy-hour workweeks to cover the extended schedule many clients desired, and from trying to cover a large amount of fixed costs on their own.

More recently, the trend had been to consolidate practices to create economies of scale, reduce workloads, increase productivity, provide better technology, and increase profits. A consolidated practice could share fixed costs and overhead, thus reducing the amount each owner was responsible for and, thereby, increasing profits. A consolidated practice could also provide more capital, making it easier to acquire the high-tech equipment they wished to own to provide their patients with cutting-edge healthcare. For instance, two two-doctor practices may not each be able to afford $100,000 digital radiology equipment (and be able to justify its cost), but if those two practices merged, the four doctors, jointly, may be able to afford to buy one set of the equipment and share it. More doctors under one roof also meant more flexibility so doctors could cut down on their hours and take vacations more easily without having to hire a relief veterinarian.

Other business models that were being used in the veterinary industry to increase operational efficiency were the wheel with spokes model, the hub, and the national practice. The wheel with spokes model allowed veterinary clinics to work together rather than as competitors by organizing themselves, and their spending on equipment, around a hub and spokes. The central hospital would contain the expensive, shared equipment, while the “spokes” acted as “wellness clinics,” capable of providing general care. For this to work, though, practitioners from different clinics needed to work collaboratively. The hub model also involved creating an extremely large facility where everything the patient needed was available under one roof, including specialty clinics such as dermatology and radiology. Though these large clinics offered everything the patient needed in one place, their size sometimes prevented them from providing the caring, personalized care many clients sought for their pets.

The national practice model being used was by a company called Banfield. The company created standardized clinics across the country, the United Kingdom, and Mexico. Veterinarians then worked for Banfield, rather than owning their own clinics. The standardization and streamlined technology allowed veterinarians to see more patients per day, work fewer hours, and still make about the same salary as private-practice veterinarians. Although this model was efficient, many veterinarians still preferred to own their own clinics.
MERGER RESEARCH

Once she had decided to consider merging with Eastwood Veterinary Clinic (EVC), Dr. Hudson knew that she had a bit of research to do before making a decision. She first learned more about EVC. She already knew that EVC was a three-doctor practice, located in a building much larger than the one she currently owned, and it was about three miles away from GRVH’s current location. The doctors at EVC practiced high quality medicine and kept up-to-date on changes in the field of veterinary medicine. She also knew that EVC saw a wider variety of species, namely birds and reptiles, and had a large boarding facility.

After taking a cursory look at EVC, she decided to delve more into seeing if the two practices were compatible. Both the GRVH and EVC, she felt, focused on providing the best quality pet healthcare and maintaining a good rapport with clients. The doctors at both clinics stayed up-to-date in their fields and wished to provide cutting-edge technology, but could not do so on their own due to its costs. EVC had a laser and an endoscope, while the GRVH had an ultrasound machine. Together, they would have use of all of the machines, plus have the capital to purchase digital radiography equipment. Consolidation of expensive equipment and (possibly) some staff positions could also increase profits. Currently, both practices saw profits in the six to ten percent range, but wished to increase this figure to between twelve and fifteen percent. Dr. Hudson noted that four to five percent of her current profits were being eaten up by paying her clinic manager’s salary. For a practice the size of GRVH’s, this was a major expense. EVC, on the other hand, did not have a manager, but this had also meant that one of its doctors spent a large portion of his time performing management tasks, rather than veterinary tasks. A clinic manager would certainly be necessary at a merged clinic, but because revenues would be higher, the manager’s salary would require a smaller portion of the clinic’s gross profits. A manager would also allow the EVC doctor currently performing management tasks at his clinic the ability to spend more time seeing patients, and generating revenue.

Although EVC’s three doctors had about the same number of active patients as the GRVH, its revenues were considerably higher, at $1,450,000. Currently the GRVH’s revenues were about $662,000. About $400,000 of EVC’s revenues came from their large indoor/outdoor boarding facility, which accommodated about 100 dogs. The EVC building was also much larger (7,600 square feet), which would provide ample room for both practices. She liked that the clinic wasn’t too far from the GRVH’s current location so that (hopefully!) most of her clientele would follow her. So far, EVC seemed like a good fit for the GRVH.

A large concern for Dr. Hudson, however, was making sure that the culture at both clinics meshed. She knew that one of the biggest challenges in mergers is clashing of cultures, so she wanted to make sure that management would all be on the same page. She met with the two EVC owners and they discussed several things that they would not compromise on. Dr. Hudson wanted to make sure that the doctors would all work together as colleagues rather than competitors. Another challenge would be combining the two staffs as seamlessly as possible and taking them into consideration as a result of the consolidation, as Dr. Hudson hoped to bring her entire staff with her. This meant speaking with key people at both practices to see if they were on board for the merger and working on a plan to integrate the personnel. (The staff at EVC was about twice as large as the staff at the GRVH). Dr. Hudson and the two EVC owners drew up a
list of goals, rules, and decisions for the potential merged practice, including its mission and how to implement a new culture (Exhibit I).

Dr. Hudson and the two EVC owners first considered building a new practice and selling the current EVC building, but found that the cost to build a new building would be over $2.0 million, much more than the national average of $1.3 million.² (See Exhibit II) It also would be impossible to recreate EVC’s kennel facility due to zoning restrictions. Instead, the three doctors decided to look into renovating EVC’s current location to add exam rooms, offices, and improve the flow of traffic throughout the clinic. The size of the kennels could be reduced to about seventy runs in order to make room for the additions without expanding past EVC’s walls. The owners anticipated that the renovation would cost $1.0 to $1.5 million and would take twelve to eighteen months to complete. If they decided to go ahead with the merger, the GRVH would remain in its current building until the renovation at EVC was complete. Meanwhile, EVC would have to work around the renovation in parts of the clinic while other parts were under construction. This inconvenience could cause a reduction in EVC’s revenues during the construction process and will certainly be hard on productivity and employee morale.

The next step was to review a budget for the two practices to estimate revenues and expenses for a merged practice. Dr. Hudson had read that new practices typically see a twenty percent growth in revenues when they open (or re-open after a large renovation), so she added a column to the budget to project this additional growth to the merged totals (Exhibit III). Dr. Hudson also wished to see how much the merged practice would have to increase revenues to pay for the merger and renovation. She could see three alternatives: (1) increase the average transaction price level by four percent per year; (2) increase the number of transactions by five percent per year; and (3) a “combination” of the two – increase the average transaction price level by two percent per year and the number of transactions by two and a half percent per year. She did a sample projection of price and transaction increases, which can be found in Exhibit IV. Still, she wondered, were there other alternatives to make the merger succeed?

After looking at all of the information she had collected, Dr. Hudson knew that it was time to make a decision regarding the future of her practice. The decision would not be an easy one. It would affect her financial future, staff, clients, and patients. Merging could help her provide better care for her patients and increase efficiency within her practice, ultimately bolstering profits. On the other hand, merging came with several costs and challenges. Dr. Hudson wondered what she should do.

ENDNOTES
Exhibit I: Owner Decisions/Consensus for Proposed Merged Practice

*Source: Company records.*

1. Pets come first (advocates for the pet’s well being)
2. Provide professional, modern, clean, and well maintained environment that is eco-friendly and regularly updated
3. Be willing to adopt new technologies and protocols that are proven effective
4. Trust and honesty are paramount with clients and with the work team and partners
5. Continuing education will be fundamental for all team members
6. Must be respectful to team members and clients
7. Employ mature, motivated, enthusiastic, and well-educated team members
8. Goal is to provide an environment where our team members can fulfill their passion to care for the pets and to serve their people
9. Our target market is well-educated pet-devoted clients that are looking for a family partnership with one-on-one service
10. Owner and team incomes are to be at or above state average
11. The practice must be large enough to provide excellent care and service, but small enough for a personal approach
12. Provide a welcoming environment
13. Provide consistent medical care with same patient going to same doctor, reception staff, and nursing staff
14. Provide access to leading specialists
15. Provide high quality boarding and day care facility
16. Provide unique services such as advanced endodontics and dental care, endoscopy, laser surgery video otoscopy, ultrasonography, etc.
17. Give back to the community with education and community service events
18. Provide behavioral counseling for dogs in conjunction with training
### Exhibit II: National Benchmarks for Practice Expansion Projects


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<tr>
<th>Project Type</th>
<th>Percent Planning</th>
<th>Average estimated project costs</th>
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<tbody>
<tr>
<td>Remodel current facility</td>
<td>13%</td>
<td>$316,000</td>
</tr>
<tr>
<td>Expand current facility</td>
<td>14%</td>
<td>$842,000</td>
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<tr>
<td>Build a new facility</td>
<td>8%</td>
<td>$1,325,000</td>
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### Exhibit III: Budget Estimate for Merged Practices

*Source: Company records.*

GRVH + EVC

(+ 20% revenue growth)

<table>
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<tr>
<th></th>
<th>GRVH + EVC</th>
<th>GRVH + EVC</th>
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</thead>
<tbody>
<tr>
<td><strong>Revenue</strong></td>
<td>2,400,000</td>
<td>2,880,000</td>
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<tr>
<td><strong>Variable expenses</strong></td>
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<tr>
<td>Drugs and medical</td>
<td>384,000</td>
<td>460,800</td>
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<tr>
<td>Outside services</td>
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<td>Diagnostic services</td>
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<td>Bank Charges</td>
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<td>Returns and Allowances</td>
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<td><strong>Total Variable</strong></td>
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<td><strong>Fixed expenses</strong></td>
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<td>Advertising</td>
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<td>Legal/accounting/consulting</td>
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<td>Payroll processing</td>
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<td>Office supplies</td>
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<tr>
<td>Travel and seminars</td>
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<td>Business promotion</td>
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<td>Dues and subscriptions</td>
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<td>Laundry and uniforms</td>
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<tr>
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<tr>
<td>Telephone</td>
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<td>Meals and entertainment</td>
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<td><strong>Total Fixed</strong></td>
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<td>714,000</td>
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<tr>
<td><strong>Facility expense</strong></td>
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<tr>
<td>Repair and maintenance</td>
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<tr>
<td><strong>Total Facility</strong></td>
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Total 1,700,720 1,833,240

Net operating income before veterinary compensation 712,800 1,059,840

Veterinary Compensation
Non-owner veterinarians 160,800 199,500
Owner veterinarians 240,000 299,000
Owner management 72,000 86,400
Relief DVM 2,000 2,400
Total DVM compensation 474,800 587,300

Total Expenses 2,175,520 2,420,540

Amount Available 224,480 459,460

Exhibit IV: Current figures for the GRVH and EVC
Source: Adapted from materials obtained from Dr. Hudson.

Average transaction: $126
Annual number of transactions: 12,054

Alternatives for Raising Revenues to Pay for Merger Project

Alternative 1: Increase average transaction price level by 4% per year

Alternative 2: Increase the number of transactions by 5% per year

Alternative 3: Increase average transaction price level by 2% and the number of transactions by 2.5%

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INSTRUCTOR’S MANUAL

Executive Summary

For the past ten years, Dr. Hudson has owned the Grand River Veterinary Hospital (GRVH), a two-doctor small animal veterinary clinic. Her practice has differentiated itself from many other veterinary clinics by providing clients and their pets with high quality medicine and personal attention in a small clinic atmosphere. The GRVH’s business model has been so successful that the clinic has outgrown its current building. In addition, the veterinary technology Dr. Hudson wishes to provide her patients is too expensive to attain on her own. Consequently, Dr. Hudson was deciding whether to merge the GRVH with a larger clinic nearby.

A breakeven analysis and comparison of the advantages and disadvantages indicate that Dr. Hudson should cautiously pursue the merger with Eastwood Veterinary Clinic (EVC). In doing so, Dr. Hudson needs to figure out how to go forward with the merger in a way that keeps her key staff and clientele on board. She also needs to make sure that she is able to maintain a similar level of quality of care and personal attention at the larger facility.

This case provides an opportunity for students to analyze a merger decision in a service-based field. They are able to use breakeven analysis to focus on the financial aspects of the merger. Students are also able to consider non-financial issues that are vital to a merger decision: preservation of the company’s culture, continuation of its competitive advantage, and motivating staff and clients to move to a new environment. The case allows students to utilize operations management concepts, such as quality management and operations strategy, as they consider how the merger will affect efficiency, quality, and productivity. Students will also use marketing concepts as they consider how to promote a merged company.

Teaching Objectives

The case focuses on a small veterinary clinic that wishes to grow by merging with another veterinary practice. The decision comes at a time when veterinary medicine costs are skyrocketing, the result of an increase in the use of expensive veterinary technology, while patient growth has remained stagnant. As a result, the current trend in veterinary medicine is to consolidate practices to improve efficiency and increase profit margins. The case is designed to provide a platform for students to discuss various business and operations management concepts, especially those relating to a merger decision. Though this case concerns a veterinary clinic owner’s merger decision, the issues could be applied to any service-based company’s merger decision.

Specific case objectives include:

1. Explore the issues and challenges involved in making a merger decision in a service-based industry.
2. Analyze a merger decision using breakeven analysis.
3. Develop marketing and promotional strategy recommendations for the merged clinic.
Courses and Levels for which the Case is Intended

The case is intended to be used in a course in which students analyze business strategy and operations. It would be suitable for use in upper-level undergraduate or graduate level courses in Operations Management, Strategic Management, Business Management, or Entrepreneurship. It would also be suitable study for veterinary students in conjunction with a Practice Management course.

The case is designed to help students critically evaluate a merger decision. Students are encouraged to analyze the pros and cons and make suitable recommendations as to what the owner of the veterinary clinic should do. They will use operations management and business strategy concepts in performing this analysis.

The case is intended to be discussed in one class session of approximately 90 minutes with three hours of external preparation.

Conclusions: Discussion Questions and Answers

Q1. What is the Grand River Veterinary Hospital’s competitive advantage? How could the decision to merge with Eastwood Veterinary Clinic affect it?

The Grand River Veterinary Hospital competes on quality. The case revealed that the clinic is in the upper 25% of clinics in the area in terms of price, so it does not compete based on low price. The case also noted that the clinic is known for its quality of care and high level of personal interaction, two aspects that are very important in the field of medicine. More specifically, the clinic focuses on two particular dimensions of service quality, assurance and empathy. Assurance represents quality in employees’ knowledge, courtesy, and their ability to inspire trust and confidence. Empathy represents quality in how employees provide individualized attention to clients.

Quality is a difficult attribute to compete on because it is hard to define it. It is dependent on how a service matches up to a client’s expectations, thus it is highly subjective. As a result, it is difficult to know if the quality clients perceive at the Grand River Veterinary Hospital will translate over to Eastwood Veterinary Clinic. Some people may define quality in terms of how responsive the veterinary staff is to their pets. Will a larger clinic be streamlined enough to keep wait-times to a minimum? Others may define quality as being recognized by name and being able to see the same veterinary assistant and doctor each time they come in. Will a larger clinic and staff be able to provide this individualized attention? Dr. Hudson may wish to survey a random sampling of her clients to see what their definitions of quality are. This way she can focus on preserving quality in those areas if she decides to complete the merger.

It is very important that the Grand River Veterinary Hospital is able to replicate the quality its clients perceive in a new environment in order to maintain its client base. Clients may have even higher expectations than before with a new clinic. This means that the delivered bundle of benefits (i.e. perceived quality) needs to be higher as well in order to maintain the current level
of client satisfaction. Dr. Hudson and her potential business partners will need to consider how they will provide even better service quality to their clients.

**Q2. With the current state of the veterinary industry, why is merging possibly a better solution than building a larger practice?**

As noted in the case, the veterinary industry has had little growth in the number of patients, but tremendous growth in revenues due to increases in veterinary fees. Veterinary fees have increased mainly due to the demand for expensive medical technology. Even though fees have risen, they often are not high enough to justify purchasing some of this equipment because of the low volume of usage. Also, there are simply too many small animal practices providing the same services, creating unnecessary duplication and competition. Building a larger clinic would mean having to come up with a larger clientele while competing against even more practices. With patient growth rates relatively stable, the only way to increase revenue would be to take clients from other practices.

From an operations management standpoint, it makes sense for practices to consolidate in order to utilize scarce resources (i.e. capital and expensive equipment) most effectively. Alone, most small practices are unable to afford to keep up with advancements in the field. However, by joining forces with another clinic, both clinics have a larger pool of capital to draw from and can afford to purchase expensive medical equipment. Being able to provide this equipment gives a combined clinic an additional competitive advantage over smaller clinics. It makes a combined clinic more desirable to clients seeking the highest quality medicine, so it potentially could draw in a larger clientele than two smaller clinics who compete with one another.

Being able to share resources such as equipment and personnel also makes the combined clinic more efficient and productive. Many small clinics cannot afford to hire a manager, so the owner veterinarian spends up to half of their workday performing management tasks rather than seeing patients – and bringing in revenue. Small clinics that do hire a manager see 4-5% of their profits eaten up by the manager’s salary. A larger clinic would allow the veterinarians to do what they do best; see patients. Meanwhile, a manager could take care of non-revenue producing tasks, and cost less because now both clinics, as opposed to just one, would be paying the manager’s salary. Being able to see more patients in a day with the same level of input (staff hours) means that the merged clinic is more productive.

**Q3. What are the potential benefits associated with merging with EVC? What are the potential challenges?**

There are many potential benefits associated with merging with EVC. Merging would bring together more capital, allow both clinics access to cutting-edge technology, and create efficiencies that could increase productivity. The combined practice would be able to provide a wider variety of services under one roof and have better staffing to allow for more flexibility in scheduling. Merging would also create a more stable and more profitable business, as well as more opportunities for growth. Additionally, the merger would provide both clinics with the opportunity to reevaluate their strategies and provide input in designing the renovated clinic so that it suits both of their needs.
While there are many benefits to consider, a merger also brings about some challenges. First, the owners in the consolidated practice must be able to share control, which could be difficult if any of the owners care to work, or make decisions, independently. Also, it is vital that the owners share similar management styles, or at least are able to agree on a particular style to be used in the merged clinic. If the owners cannot agree on a form of management, or use two kinds, employees will become confused and frustrated. The same goes for clinic culture. The merged clinic needs to have a culture of its own, not a mishmash of the two clinics, to encourage unity and productivity among the staff.

Second, merging two practices could mean a reduction in staff. Though Dr. Hudson wishes to keep her current staff, it is possible that not all of their positions will be necessary at the merged clinic. Also, the merger will be hard on the employees at both practices, so greater than average turnover, and moments of poor morale, are to be expected. Plans need to be in place to thwart excessive employee turnover and to boost employee morale. (Note: Students might be asked to brainstorm various ways that this could be accomplished.)

Third, mergers can be expensive. Though the owners of the two clinics in this case project spending $1.0-$1.5 million on the renovation of EVC’s building, they must also consider (if they have not already) all of the costs involved in a merger. This includes the cost of valuing the two practices, various legal documents, consulting fees, and potentially lost income while EVC is under construction. Eliminating some of the boarding at EVC to make room for additional exam rooms will decrease boarding revenues to some extent. Also, the owners need to decide how they will obtain the funds to go through with the project, finding a suitable loan and interest rate.

Q4. Should the Grand River Veterinary Hospital merge with Eastwood Veterinary Clinic? If yes, how do you think revenues should be increased (i.e. which alternative in exhibit IV)?

Dr. Hudson’s decision to merge her practice with Eastwood Veterinary Clinic is a very important one. If she keeps her practice in its current location, she will not be able grow much more, nor will she be able to provide the kinds of medical services she would like to. If she decides to maintain her practice as sole owner, but move into a new building, she will be taking on a tremendous financial burden on her own. Dr. Hudson noted in the case that building a new clinic would require her to bring in another partner because she would not be able to bring in the revenues necessary to support such an investment. Merging with EVC would solve many of Dr. Hudson’s problems, but the decision certainly comes with its costs.

It appears from the case that Dr. Hudson has done some thorough research regarding her decision. Indeed, astute students might point out that she appears to be a very prudent, conservative decision-maker. Looking at Exhibit I, it is apparent that Dr. Hudson has put considerable thought into what the culture and management should look like at the merged practice. She has met with the owners of EVC and has tackled many of the concerns addressed in question 3. Looking at the budget, it appears that the merged clinic should produce enough in revenues to cover the extra expenses. Students may want to do some research to decide whether a 20% increase in revenue is attainable and how sustainable that kind of growth is. Astute students might also point out that the budget does not appear to take into account EVC’s lost
revenues during the construction period or from reducing their boarding facilities… and this merits consideration as well, particularly in the early stages of the GRVH/EVC merger.

Breakeven Analysis
Dr. Hudson indicates in the case that the total cost for the merger and renovation associated with it is expected to be between $1.0 and $1.5 million. Exhibit IV shows that the average transaction price for both clinics is $126. An average student should be able to take from Exhibit II that variable costs take up 22.4% of revenues for both clinics (645,120 / 2,880,000 = 0.224) and find that 22.4% of $126 is $28. This means that the contribution margin (price per transaction – variable cost per transaction) is roughly $98. A conservative estimate uses the $1.5 million cost figure to calculate breakeven point.

Breakeven point would then be calculated as follows:

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\text{BEP} = \frac{\text{Total Merger Costs}}{\text{Contribution Margin}} = \frac{\$1,500,000}{\$98} = 15,306
\]

This number represents the number of transactions (at the average price of $126 per transaction) the owners would need to perform to breakeven on their investment. Exhibit IV shows that together the two clinics currently average 12,054 transactions per year. The 15,306 transactions needed to breakeven would be in addition to the current transaction levels. For example, by increasing transactions by 10%, or to 13,259 transactions per year, the clinic would gain 1205 transactions per year. At the current average price per transaction, it would take the owners about 13 years to breakeven on their investment.

The case does not mention how much longer the owners plan to be in practice, but considering that Dr. Hudson has owned her current practice for ten years, she will most likely be working for at least 13 more years. As long as the owners plan to be in practice for at least this amount of time (or have a plan to have their interest bought out upon retirement), they should see a return on their investment.

A bright student should realize that the above BEP calculation is a very rough estimate as there are factors that may change it to an extent. First, it is unlikely that transaction levels will increase by 10% in the first year and remain at that level over time. It is more likely that transaction levels will increase at a smaller rate over a time span of years, rather than immediately spiking and staying at that level (similar to Dr. Hudson’s projections in exhibit IV). Also, the above calculation does not take into consideration any increases in price – it assumes that the average transaction price will remain the same over time. For instance, if the average transaction price rose to $141, the BEP would fall to 13,761 transactions.

Additionally, the breakeven analysis does not account for the increase in operating expenses that result from increasing the number of transactions. If efficiency does not increase substantially, a large increase in the number of transactions would mean that staff compensation and variable expenses would also increase. As a result, significantly more revenue would be needed to cover the expenses.
A growing practice does not want to attain all of its increase in revenues through increases in price; they want to increase the number of patients they see. Increasing transactions increases expenses, however. Because of this, the best solution for increasing revenues is probably alternative 3 – increasing fees and the number of transactions at a slower rate than would be used if just one or the other was increased. It should be noted, however, that over time expenses will increase due to increases in the cost of living. Any increases in prices to help pay for the renovation need to be above and beyond these cost-of-living increases.

Another alternative, of course, to generate additional revenue is vis-à-vis the types of services provided. It is entirely possible – indeed, it is even presented as part of the rationale for the merger, that a larger practice will be able to offer more sophisticated technologies and, therefore, surgeries, treatments, and so on, which (presumably) will be done at higher fees. If the instructor wishes to direct the case discussion along this line, including a more in-depth financial analysis, this would present an excellent opportunity to introduce topics such as interest rates, opportunity cost, etc. (i.e., additional tangible costs associated with a merger decision).

Finally, some instructors may want to use this as an opportunity to introduce SWOT analysis (Strengths-Weaknesses-Opportunities-Threats), or to invite students to brainstorm other alternatives to the merger (e.g., converting GRVH to a surgery/specialized center or kennel and using EVC as a routine/check-up clinic, or expanding either facility rather than building a new clinic).

Q5. How should Dr. Hudson promote the merger to her staff and clients? How should the merged clinic be marketed to the public?

Insights for managing the transition and adaptation process, should Dr. Hudson decide to proceed with the merger, can be drawn from the literature on human resource management, particularly power/conflicts, cultural adaptation, and so on. Additionally, students may have been in similar situations and can be asked to comment on what strategies worked (or were helpful) in the “real world” and what were less effective, or ineffective.

Moreover, it seems Dr. Hudson should be open with her staff about why she chose to merge her clinic with EVC. She should include them in discussions about the merger, honestly answer their questions, and assure them that they will be keeping their jobs. Some employees may have a difficult time with change, so Dr. Hudson should provide these employees with an outlet to discuss their concerns. It may help to have the staff at both clinics meet and to discuss what the new clinic’s culture will be like to prepare them for the change and know who they will be working with.

As for her current clients, Dr. Hudson should explain to key clients what her rationale was in deciding to merge her clinic with another. She will also want to reassure them that their pets will still receive the best care and that what they currently like about her practice will not change. She also may want to ask them what it is that they like best about her clinic to ensure that their expectations are met, or surpassed, at the new clinic. Dr. Hudson and the EVC owners may also want to consider having clients from their original practices see the veterinarian and support staff that they are used to, rather than having them go to a new doctor. Broader forms of
communication could be used with the rest of her clients. For instance, she could have a poster describing the merger progress hanging on the bulletin board in the lobby, or provide brochures answering commons questions regarding the move. It may also be helpful to provide a 3-D model of the proposed renovation available in the lobby for clients to see. A few months before the practice moves, Dr. Hudson should mail out postcards telling all of her clients when they will be moving and where their new location will be. She may also want to provide an “incentive” for either the client or the pet to move to the new location (e.g., free coffee or movie pass for the client, or free treat/ID tag for the pet).

The merged clinic should definitely be marketed to the public, not just current clients at both clinics because of the opportunity to grow the merged clinic’s client base. One way to do this is to hold an Open House that is highly advertised in newspapers, on the radio, etc. The Open House would allow potential clients, as well as returning clients, the opportunity to see the brand new, state-of-the-art facility. The Open House could include activities for children, offer coupons for various pet products, and offer an opportunity to have complementary businesses, such as groomers or the Humane Society, promote their products at the event. Providing clients with something tangible, such as seeing areas of the clinic that they normally would not, increases the sense of value clients perceive.

Special Thanks
We are grateful to Dr. Lauren Hudson for allowing the use of her practice for this case study, as well as for providing needed information.