Neutral Citation Number: [2023] EWHC 290 (Comm)

Case No: CL-2021-000188

IN THE HIGH COURT OF JUSTICE
KING'S BENCH DIVISION
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
COMMERCIAL COURT

Royal Courts of Justice, Rolls Building
Fetter Lane, London, EC4A 1NL

Date: 13/02/2023

Before :

MR JUSTICE BRIGHT

- -

Between :

MILLBROOK HEALTHCARE BIDCO LTD (formerly known as CAIRNGORM ACQUISITIONS 9 BIDCO LIMITED)	**Claimant**
- and -	
(1) PAUL CROLL	
(2) COLIN CROLL	
(3) MARK CROLL	**Defendants**

- -
- -

BEN WOOLGAR (instructed by **Gowling WLG (UK) LLP**) for the **Claimant**
SIMON JOHNSON (instructed by **Paris Smith LLP**) for the **Defendants**

Hearing dates: 16th, 17th, 18th, 19thM and 24th, January 2023

- -

Approved Judgment

This judgment was handed down remotely at 10am on 13 February 2023 by circulation to the parties or their representatives by e-mail and by release to the National Archives.

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MR JUSTICE BRIGHT

Mr Justice Bright :

Introduction

1. This judgment follows the trial of the claim of the Claimant ("**Bidco**") against the Defendants ("**the Sellers**") arising from the Claimant's purchase of the entire issued share capital of MHCDC Ltd ("**MHCDC**"). The claim arises under an Agreement for the Sale and Purchase of the Entire Issued Share Capital of MHCDC, dated 22 July 2019 (the "**SPA**").

2. Bidco was represented by Mr Ben Woolgar. The Sellers were represented by Mr Simon Johnson. I am very grateful to both counsel for the dedication and skill with which they represented their clients, but also for the courtesy and good nature with which they conducted their dealings with each other and with me.

3. The transaction completed on the SPA date, 22 July 2019. The price paid comprised Initial Consideration of £28,032,500 and a Total Stamp Duty Escrow Amount of £375,000. Bidco's case is that the Sellers were in breach of various warranties contained in the SPA.

4. Bidco is controlled by Cairngorm Capital Partners LLP ("**Cairngorm**"), a private equity investment manager. MHCDC, the subject of the SPA, owns a number of companies (collectively referred to as "**Millbrook**"). The only relevant subsidiary is Millbrook Healthcare Limited ("**MHL**").

5. MHL is in business providing healthcare equipment, including wheelchairs, to various NHS Clinical Commission Groups ("**CCG**"). The claim concerns two of MHL's contracts, referred to by the parties as "**the East Sussex Contract**" and "**the Somerset Contract**" (on the basis of the NHS CCGs with which they were concluded).

6. Bidco's case was that MHL had agreed to vary the East Sussex Contract, and had agreed to waive its right to recover the accrued debt under a specific invoice issued under the Somerset Contract, in respects that were not consistent with the financial information provided to Bidco. Bidco said that each of these matters put the Sellers in breach of various warranties under the SPA.

7. The Sellers denied that the variation of the East Sussex contract was material, or that MHL had agreed to waive its rights under the relevant Somerset Contract invoice. In any event, they denied that the relevant matters put them in breach of warranty, and asserted that Bidco was itself in breach of one of the warranty provisions (giving rise to a contingent counterclaim, to be set off against Bidco's claim).

8. There were also substantial issues between the parties in relation to quantum.

The witnesses

9. Bidco called the following factual witnesses:

    i) Mr Amit Thaper. Mr Thaper originally qualified and worked as a doctor, before moving into management consultancy and private equity investment. He was a director of MHL from July 2019 to December 2019, before becoming a

Managing Director of Cairngorm. He led Bidco's acquisition of MHCDC and was also involved in some of the subsequent events.

ii) Mr Charles Skinner. Mr Skinner was Chief Financial Officer of MHL from July 2019 to March 2021.

iii) Mr Phillip Campling. Mr Campling has been employed by MHL since 2008, i.e., before the acquisition. Immediately prior to the SPA, his role was Managing Director. Following the SPA, he was appointed Chief Executive Officer of MHL from July 2019 and remained in that role until December 2022.

10. The Sellers' factual witnesses were as follows:

i) Mr Paul Croll. Mr Paul Croll qualified as a chartered accountant and worked in that role for some years. He joined Millbrook in 2002 and was the de facto Finance Director of MHL until 2006, when he was formally appointed as Finance Director.

ii) Mr Colin Croll. Mr Colin Croll is the father of Mr Paul Croll and was largely responsible for expanding Millbrook's business from the 1960s, and in particular for developing its healthcare interests from 1995 onwards.

11. Both parties also called expert evidence, from their respective expert valuers, Mr Andrew Grantham and Mr Doug Hall.

12. Neither party called evidence from Mr David Lock. At the time of the SPA, Mr Lock was Commercial Director of MHL. He worked for MHL for many years prior to the SPA and was trusted by the Sellers. He then continued to work for MHL after the SPA, until July 2020, when he was dismissed. Each side suggested that the other could and should have called him: Bidco suggested that the Sellers should have, because they had known him longest and had stated their intention to call him in their Case Management Information Sheet, in August 2021; the Sellers suggested that Bidco should have, as they had employed him most recently, including the period after his activities in relation to the East Sussex Contract and the Somerset Contract had come to light. However, the reality is that it would have been difficult for either side to call him, let alone to commend him to me as a reliable witness, for reasons that I discuss below.

The SPA

13. The main body of the SPA included the following provisions:

> "8 WARRANTIES AND EXCLUSIONS
> 8.1 In consideration of the Buyer entering into this Agreement the Sellers warrant to the Buyer:
> (a) (subject to clause 8.3) in the terms set out in schedule 4 on the date of this Agreement; and
> (b) that any statement in schedule 4 which is qualified as being made "so far as the Sellers are aware" or "to the best of the knowledge, information and belief of the Sellers" or any similar expression has been so qualified after due diligent and careful enquiries by the Sellers of the other Sellers and of Phillip

Campling, Lee Davies and David Lock and so that the awareness, knowledge and information of each of the Sellers shall be imputed to each of the other Sellers PROVIDED THAT this clause 8.1(b) shall not apply to any such statement which refers to the actual awareness of the Sellers, in which case only the actual awareness of any of the Sellers shall be deemed to apply.

…

8.3 Except as provided in clauses 9.3(b) and 8.10(f), the Warranties are qualified to the extent, but only to the extent, of those matters fairly disclosed in the Disclosure Letter, provided that the provisions of this clause shall not apply to the Special Warranty.

8.4 Each of the paragraphs in schedule 4:

(a) shall be construed as a separate and independent warranty; and

(b) except as expressly provided otherwise in this Agreement, shall not be limited by reference to any other paragraph in schedule 4 or by any other provision of any Agreed Document, and the Buyer shall have a separate claim and right of action in respect of every Relevant Breach.

8.5 Subject to clause 17.3, the rights and remedies conferred on the Buyer under this Agreement are cumulative and are additional to, and not exclusive of, any rights or remedies provided by law or otherwise available at any time to the Buyer in respect of any Relevant Breach (including the right to damages for any loss or additional loss suffered by the Buyer).

…

8.6 All claims by the Buyer for damages or compensation in respect of any Relevant Breach and (to the extent specified therein) any Tax Covenant Claim and any Indemnity Claim shall (subject to clause 9.3(b)) be subject to the provisions for the protection of the Sellers in schedule 5.

…

17 ENTIRE AGREEMENT

17.1 The Agreed Documents constitute the entire agreement between the parties in relation to the sale and purchase of the Sale Shares and other matters covered by them and supersede any previous agreement, arrangement or understanding between the parties, whether written or oral, in relation to those matters, which shall cease to have any further effect.

17.2 The parties acknowledge that the Agreed Documents have not been entered into wholly or partly in reliance on, nor has either party been given, any warranty, statement, promise or representation by the other or on its behalf other than as expressly set out in the Agreed Documents.

17.3 Each party agrees that the only rights and remedies available to it arising out of or in connection with any warranties, statements, promises or representations will be for breach of contract and irrevocably and unconditionally waives any right it

may have to any claims, rights or remedies including any right to rescind this Agreement which it might otherwise have had in relation to them.
17.4 All warranties, conditions, statements, terms and representations not set out in the Agreed Documents whether implied by statute or otherwise are excluded to the extent permitted by law."

14. Schedule 4 included the following provisions:

"3 ACCOUNTS
…
3.2 The Accounts give a true and fair view of the assets, liabilities (including contingent
unquantified and disputed liabilities whether for Tax or otherwise), capital commitments and state of affairs of each Subsidiary as at the relevant Accounts Date and of the profits and losses of each Group Company for the financial period to which the Accounts relate and in particular (in each case, to the extent required by Accounting Standards in force at the relevant Accounts Date):
(a) do not overstate the value of any asset of each Subsidiary as at the relevant Accounts Date;
(b) include full provision for all actual liabilities and bad debts;
(c) include proper provision (or full disclosure) in accordance with Accounting Standards in force as at the relevant Accounts Date for all contingent liabilities; and
(d) include provision on the basis fairly disclosed in the Disclosure Letter for all doubtful debts and so far as the Sellers are aware that provision will be adequate.
…
3.8 The Management Accounts:
(a) do not materially misstate the assets and liabilities, and do not materially misstate the profits or losses, of the relevant Group Company as at the applicable dates and applicable periods to which the Management Accounts relate;
(b) have been prepared with reasonable care, on a basis consistent with the previous twelve months of Management Accounts up to the Accounts Date;
(c) have been prepared on a consistent basis from month to month; and
(d) contain no material errors or omissions, it being acknowledged that the Management Accounts have not been audited.
…
4 POSITION SINCE THE ACCOUNTS DATE
…
4.3 Since the relevant Accounts Date, no Subsidiary has:
…

(b) disposed of any of its assets except in the ordinary and normal course of business at the full market values of the assets concerned;
…
5 LOCKED BOX
5.1 The Locked Box Statements:
(a) have been prepared on a basis consistent with the Accounts;
(b) do not materially misstate the assets and liabilities of the relevant Group Company at the relevant Locked Box Date; and
(c) contain no material errors or omissions.
…
7 DEBTORS AND CREDITORS
…
7.4 No indication has been received by any Group Company or any Seller that any debt due to any Group Company is bad or doubtful.
7.5 No book debt has been duplicated or otherwise incorrectly recorded in the Accounts or the Management Accounts
…
17 COMMERCIAL CONTRACTS AND JOINT VENTURES
17.1 Complete and accurate copies of each of the Contracts listed in schedule 12 (and all other documentation which is supplementary to, varies or amends those Contracts) are contained in the Data Room."

15. Schedule 5 included the following provisions:

"1 FINANCIAL LIMITATIONS AND WARRANTY AND INDEMNITY INSURANCE
…
1.4 The Sellers shall be under no liability to make any payment in respect of any Non-Insured Warranty Claim (other than a Special Warranty Claim) unless:
(a) the amount of the Non-Insured Warranty Claim or series of Non-Insured Warranty Claims in respect of the same matter (excluding interest, costs and expenses) exceeds £45,000 ("Qualifying Warranty Claims"); and
(b) the amount of all Qualifying Warranty Claims (excluding interests, costs and expenses) exceeds £450,000, in which event the Sellers shall (subject to the other provisions of this schedule) be liable for the whole amount and not only the excess.
…
4 SPECIFIC LIMITATIONS
4.1 The Sellers shall have no liability in respect of any Warranty Claim to the extent that:
…
(e) it would not have arisen but for any act, omission, transaction or arrangement carried out after Completion by the Buyer or any Group Company or any of its or their respective directors, employees or agents or successors in title other than at the prior

written request of the Sellers or under a legally binding commitment of the Company that existed before Completion or in the ordinary course of trading of the Company.

…

5 RECOVERY FROM THIRD PARTIES

…

5.2 If the Buyer recovers from some other person any sum in respect of any matter or event which could give rise to a Claim (other than a Claim relating to any Tax Warranty or under the Tax Covenant, in which case the provisions of the Tax Covenant shall apply) or Indemnity Claim any sum recovered will reduce the amount of such Claim or Indemnity Claim after deduction of all reasonable costs and expenses of recovery.

…

6 THIRD PARTY CLAIMS

6.1 If any member of the Buyer's Group becomes aware of any actual claim by a third party against any member of the Buyer's Group including any Group Company (a "Third Party Claim") which causes, or which is likely to cause, the Sellers to be liable for a Non-Insured Warranty Claim or Indemnity Claim, the Buyer shall (and shall procure, where relevant, that the relevant member of the Buyer's Group shall) at the Sellers' cost (but only in respect of related third party expenses incurred by the Buyer's Group):

(a) as soon as reasonably practicable give written notice of the Third Party Claim to the Sellers' Representative; (b) consult with the Sellers' Representative in relation to such Third Party Claim, supply the Sellers' Representative with such information and copies of documents relating to such Third Party Claim, and provide the Sellers' Representative with access to relevant personnel, in each case that the Sellers' Representative reasonably requires;

(c) keep the Sellers' Representative informed as to the steps which are being taken in connection with any Third Party Claim, in each case subject to not endangering legal privilege.

…

8 MITIGATION

Nothing in this schedule 5 will in any way restrict or limit the Buyer's or a Group Company's common law duty to mitigate its loss."

The process leading to the SPA

16. Having decided to sell MHL, the Sellers instructed Smith & Williamson LLP to represent them in relation to the sale and to market the business. Just after this, in early 2019, they were contacted by consultants representing Cairngorm. A meeting was arranged which took place at MHL's premises on 5 March 2019. After the meeting, Mr Colin Croll drove the Cairngorm representatives (including Mr Thaper) back to the railway station. Cairngorm wanted exclusivity. Mr Colin Croll said that the price would have to be well above £40,000,000.

17. Cairngorm first received management accounts on 11 March 2019, being the management accounts prepared as at 31 January 2019. MHL's accounts (like those of many if not all of the various Millbrook companies) were prepared on the basis of the year ending 30 June. The January 2019 management accounts accordingly contained actual figures for the months from July to January (i.e., 7 months) and projected figures for the remaining 5 months. The projected figures were taken from the budgets that had been prepared for each company at the start of the financial year, under the supervision of Mr Paul Croll.

18. Cairngorm also received a financial pack, prepared by or under the direction of Mr Paul Croll, covering the whole group of Millbrook companies ("the Financial Pack"). It encapsulated the most recent audited accounts for all the Millbrook companies and all the most recent management accounts, including those of MHL. The Financial Pack P&L summary was as follows:

P&L					
Year-end 30 June	**FY17**	**FY18**	**FY19**	**FY20**	**FY21**
£'000	**Actual**	**Actual**	**Outturn**	**Projection**	**Projection**
Gross revenue	89,413	115,394	122,238	119,899	130,674
Service delivered product	(47,718)	(65,878)	(66,559)	(62,269)	(68,423)
Net revenue	**41,694**	**49,516**	**55,679**	**57,631**	**62,251**
Staff costs	(22,304)	(28,382)	(30,972)	(31,076)	(33,814)
Non-staff costs	(14,836)	(16,254)	(17,977)	(19,485)	(20,984)
EBITDA	**4,555**	**4,880**	**6,730**	**7,069**	**7,453**
EBITDA adjustments	606	174	(117)	(137)	(174)
Adjusted EBITDA	**5,160**	**5,054**	**6,613**	**6,932**	**7,279**

19. The pro forma balance sheet summary was as follows:

Proforma balance sheet	
	At 31-Dec-18
£'000	**Actual**
Fixed assets	**7,571**
Stock	7,857
Trade debtors	15,751
Other debtors	6,292
Current assets	**29,900**
Overdraft	(2,172)
Trade creditors	(3,963)
Other creditors and accrua	(11,085)
Current liabilities	**- 17,219**
Net operating assets	**20,252**

20. In these tables, 'Actual' figures were taken from audited accounts. The 'Outturn' figures for FY2019 were taken from the figures in the most recent management accounts, being actual figures up to January 2019 and projected figures for the remaining months in FY2019. The figures for FY2020 and FY2021 were, of necessity, pure projections.

21. The EBITDA adjustments reflected Mr Paul Croll's estimates of the likely differences that would ensue after the Millbrook companies left the Sellers' ownership. They related to factors such as rent of premises.

22. Accordingly, the information given to Cairngorm, on the basis of management accounts, was that Millbrook was expected to generate EBITDA for FY2019 (i.e., to 30 June 2019) of £6,613,000. Mr Thaper gave evidence, which I accept, that Cairngorm treated this as £6,600,000 and applied a multiple of 6.8, which he described as appropriate, indicating an enterprise value of about £45,000,000. I note that treating £6,613,000 as £6,600,000 involves a slight rounding down, and that multiplying by 6.8 before settling on £45,000,000 then involves a slight rounding up.

23. This was reflected in Cairngorm's formal written offer, in a letter dated 25 March 2019, offering £45,000,000 cash. As well as stating that the cash total was derived from adjusted FY2019 EBITDA of £6,610,000 and a multiple of 6.8, the letter stated that it would be subject to adjustments as follows:

    i) An adjustment in respect of the surplus/deficit of cash over debts, to leave the 28 February 2019 balance sheet cash free/debt free.

    ii) An adjustment in respect of normalised net working capital. This was to be based on a locked box balance sheet and with a normal level of working capital, representing the average level of working capital in the management accounts (also referred to as the target working capital). If the working capital at the locked box date exceeded the target, any difference would be added to the price; conversely, any shortfall would be deducted.

    iii) A profit ticker adjustment, to take account of profits from the locked box date to completion.

24. This offer was accepted. There were then negotiations regarding the adjustments, which gave rise to the final SPA price of £28,032,500 plus £375,000, it having been agreed that these were the figures that resulted from the appropriate adjustments being applied to £45,000,000. This took until the date of the SPA, i.e., 22 July 2019. The adjustment in relation to working capital was £1,199,000 in the Sellers' favour, reflecting the positive surplus in the locked box working capital over the agreed target.

25. In the meantime, Cairngorm/Bidco received further management accounts for the Millbrook companies, including management accounts for MHL prepared as at 28 February 2019, 31 March 2019 and 30 April 2019. As each month passed, the figures for FY2019 were based more on actual figures, and less on projected figures in respect of the remaining months before 30 June 2019. The actual results of MHL for February, March and April were somewhat better than the projected figures had been, so each successive set of management accounts indicated somewhat higher figures for FY2019 than those in the January 2019 management accounts. However, because the parties had already landed on a figure of £45,000,000 in relation to enterprise value, and no doubt also because MHL was only one among several Millbrook companies, whose enterprise value was assessed and agreed on an aggregate basis (hence the total figure for 2019 EBITDA of £6,610,000), this was not revisited.

26. Mr Colin Croll gave evidence that, prior to the offer of £45,000,000, there had been an earlier offer of £43,000,000 cash plus £3,000,000 deferred consideration, which he rejected because he did not want deferred consideration. Later on, at a pre-contract signing meeting in July 2019, after several hours of discussions, Mr Thaper said that, because of outstanding debts in relation to the East Sussex Contract, Bidco wanted to hold back £1,000,000 in escrow until the debts were paid. Mr Colin Croll refused this and said he would not sell to Bidco if there was an escrow or the price was "chipped", following which Bidco relented. He explained in oral evidence that he had no confidence that any element that was deferred or held back would ever be received.

27. It was suggested in closing submissions that this showed that the Sellers would never have accepted less than £45,000,000 (with adjustments) and that, if any buyer had made an offer below that level, on account of the problems with the East Sussex Contract or the Somerset Contract, Mr Colin Croll would have refused. I do not view Mr Colin Croll's evidence as having that effect. If both sides had known from the outset of the problems with the East Sussex Contract and the Somerset Contract, the negotiations would have had a different starting-point. In particular, the FY2019 EBITDA would have been reduced, as I discuss later.

28. However, this evidence does show that, if properly informed about the East Sussex Contract and the Somerset Contract, both sides would have conducted their negotiations by reference to the enterprise value. In addition it that MHCDC's enterprise value would very likely have been assessed (at least on Cairngorm's/Bidco's side) by applying a multiple to FY2019 EBITDA.

29. It also suggests, that the parties worked on the basis of reasonably round numbers (at least in relation to enterprise value).

<u>The relationship between the SPA warranties and the Financial Pack</u>

30. In relation to MHL, the 'Accounts' for the purposes of the SPA warranty provisions were the audited annual accounts for MHL for the period ending 30 June 2018. MHL's management accounts were on a monthly or two-monthly basis from March 2018 to April 2019. The 'Management Accounts' for the purposes of the SPA warranty provisions included not only the MHL January 2019 management accounts provided to Cairngorm on 11 March 2019 and subsumed in the summary figures in the Financial Pack, but also subsequent MHL management accounts up to and including those for April 2019.

31. The significance of this is that only the actual figures in the management accounts were warranted. Projected figures were not. In the MHL January 2019 management accounts, the figures for July 2018 to January 2019 were warranted, but the figures for the balance of the FY2019 were not (i.e., February to June 2019). In the April 2019 management accounts, the figures for July 2018 to April 2019 were warranted and only two months were not warranted (May and June 2019).

32. Accordingly, in relying on the figures in the Financial Pack for Millbrook's FY2019 EBITDA, the only warranted information relied on by Cairngorm was in respect of figures up to January 2019, the balance being a combination of projections for the rest of FY2019 and estimates in respect of the adjustments. Cairngorm had to form its own

view as to whether the non-warranted information could reasonably be taken to support the figures in the Financial Pack for FY2019, and in relation to the adjustments.

33. However, it ultimately did so with the benefit of the April 2019 management accounts. These will have shown, for MHL and for all the other Millbrook companies, whether Mr Paul Croll's budget figures for the February, March and April 2019 had been reasonably reliable. That will have made it possible to infer whether the projected figures for May and June 2019 were also likely to be reliable.

34. Cairngorm evidently saw nothing in the later management accounts that cast doubt on the reliability of the figure provided in January and did not revise its view as to FY2019 EBITDA; and the Sellers did not suggest otherwise in the course of negotiations. At the trial I was not provided with the management accounts for the other Millbrook companies, so I am not in a position to assess this, but neither party sought to suggest that the figures in the Financial Pack did not appear to be supported by the later management accounts. I therefore proceed on the basis that the figures in the later management accounts did, in fact, appear to confirm the reliability of the FY2019 figures in the Financial Pack and it was reasonable for Cairngorm to operate on this basis.

35. Similarly, neither party sought to suggest that the EBITDA adjustments were not appropriate.

The East Sussex Contract

The terms of the East Sussex Contract

36. The East Sussex Contract commenced on 1 July 2015 for a term of 36 months, later extended to 60 months, i.e., 5 years. The important features of its terms, as originally concluded, were not ultimately disputed and I am told that they were typical of NHS contracts of this kind.

37. Payment was dealt with in Schedule 3. This contained Expected Annual Contract Values ("**EACVs**"), which set out the expected total spend by category over the life of the Contract. The EACV for Year 1 (i.e., the year to the end of June 2016) was £2,267,599. The EACV for subsequent years was set to reduce slightly, year-on-year. 1/12 of the EACV value for each year was to be invoiced per month, on the 15th day of the month.

38. The EACV for each year was not, strictly, a fixed price. It was a cap. It was in effect an annual budget for the value of services and equipment to be supplied by MHL, as and when patients' cases were referred to it. For each patient referred to it, MHL would provide a wheelchair to a specification appropriate to that patient's needs, depending on the complexity of the patient's condition. For each wheelchair supplied, MHL would charge the price of that individual wheelchair, per a separate NHS tariff setting out the prices for various wheelchairs of different specifications. Thus, the total sum charged by MHL to the East Sussex CCGs in any contract year would depend on the number of referrals and the complexity of those referrals.

39. Furthermore, it is important to note that the NHS tariffs contained a profit element to MHL, in terms of the margin between the equipment prices paid by the East Sussex

CCGs and the equipment costs to MHL. It was common ground that this margin represented 9% of MHL's costs.

40. The page of Schedule 3 that set out the EACVs also stated the following:

> "Backlog values to be added in year when agreed as per Contract Variation.
>
> It has been accepted by both the Commissioners and Millbrook Healthcare that the above contract values are likely to represent a pressure on the budget and the ability to deliver the service in line with the service specification. The annual values will therefore be monitored on a monthly on the basis of the baseline as attached below in line with the trajectory documented in the indicative activity plan."

41. This text reflected the fact that, when the East Sussex Contract commenced, MHL was taking on an inherited backlog of cases already referred, which MHL was intended to reduce over time.

42. It also reflected the fact that, in the course of pre-contractual negotiations, MHL had insisted that the EACV figures would be inadequate to cover the total equipment cost for all the referrals likely to occur, and the CCGs had accepted this. Indeed, the Contract appended various documents including MHL's tender letter, which had stated "… we are offering to provide a fixed resource (and not an unlimited service)…"

43. It therefore was expected from the outset that, in order to deal with the cases likely to be referred, MHL would have to provide more equipment than the EACV allowed for, and so would incur sales to the CCGs in excess of the EACV.

44. I understand from the evidence of both parties' witnesses that it is in fact common in the sector for EACVs to be exceeded, with the CCG usually agreeing to pay the excess per the tariff prices (sometimes with a discount). The monitoring that the East Sussex Contract required could be expected to give rise to precisely this kind of discussion.

45. However, it was ultimately common ground that, in this situation, the CCGs would not be obliged to pay anything in excess of the EACV total for the year. Thus, when the EACV was exhausted, MHL would have to choose either (a) to continue to provide further wheelchairs, without a guarantee that the CCGs would pay for them, or (b) to stop providing wheelchairs in response to referrals, in which event the CCGs' patients' needs might go unmet and the backlog would go up rather than down and MHL would not receive the benefit of the 9% margin available to it on all equipment actually supplied.

46. I should add that Bidco's pleaded case was that it was agreed when the East Sussex Contract was tendered that £57,071 per month (excluding VAT) could be charged for equipment. The only basis for this was a reference in a report drafted by Mr Lock in August 2019 (referred to again below), which mentioned "the monthly equipment allowance of £57,071.00 (excluding VAT)". I suspect that this reflected either MHL's internal budgeting or something said in pre-contractual negotiations. There is no provision to this effect in the East Sussex Contract itself, including the various documents appended to it.

47. My impression is that the East Sussex CCGs (and, probably, CCGs in general) were more concerned with the finite sum payable to their provider within any financial/budgetary period, rather than how much of that total was incurred in respect of equipment or other costs. Having said that, if they had been told that, within the overall sum payable, the provider had incurred more in respect of equipment and less on overheads and other costs (i.e., reflecting efficiency savings), I find it hard to imagine they would have been displeased. In any event, I am sure that, if total sales amounted to the total EACV, the East Sussex CCGs would have paid that total, even if the equipment element had exceeded £57,071.

Performance of the East Sussex Contract, prior to the SPA

48. In due course the EACVs were indeed exceeded for all the East Sussex Contract years prior to the SPA (Contract Year 4 being the year to the end of June 2019), with MHL providing equipment substantially in excess of the contractual budget.

49. The person responsible for the commercial servicing of the East Sussex Contract was Mr Lock. While the EACV amounts were invoiced regularly (1/12 per month, as prescribed in Schedule 3), Mr Lock sometimes did not seek payment for overspends until very substantially after the relevant supplies had occurred. In March 2016, MHL received a payment of £875,000 referable to the inherited backlog and Year 1, in addition to the EACV for that year. In October 2017, it received a further additional payment of £330,170. However, by the end of Year 3 (ending June 2018), the total figure for equipment supplied, but not paid for, was £1,050,269.

50. MHL continued to make supplies in excess of the budget allowance in Year 4, because of the volume of equipment supplied. In the January 2019 management accounts, the total for sales up to and including January was already £1,622,100, meaning that the EACV was very likely to be exceeded in that year as well; the projected figure for the full year was £2,757,200. In the April 2019 management accounts, the total for sales up to and including April was £2,276,800 (i.e., already in excess of the EACV); the projected figure for the full year was £2,750,700.

51. The accounts for FY2018 did not suggest that there was any doubt over MHL's right or ability to recover the debts accrued as sales to the East Sussex CCGs prior to the end of June 2018. The management accounts recorded the sales referable to Year 4 of the East Sussex Contract as if they were accrued debts.

The Variation Agreement

52. In the course of 2018 – i.e., well before the conclusion of the SPA – Mr Lock had had discussions with the East Sussex CCGS which culminated in a variation agreement, dated 18 May 2018 and signed by East Sussex on 19 September 2018 and by Mr Lock on behalf of MHL on 4 December 2018 ("**the Variation Agreement**"). The relevant provisions were as follows:

> "The contract will be extended for two years from 02 July 2018 until 02 July 2020 (24 months).
>
> **SCHEDULE 3 PAYMENT – Ref 20150410_135838**

CCG	Year 4	Year 5
EHS	£804,527	£804,527
H&R	£722,155	£722,155
HWLH	£390,268	£390,268
Total Adults	**£1,916,950**	**£1,916,950**
EHS	£147,165	£147,165
H&R	£132,097	£132,097
HWLH	£71,388	£71,388
Total Children	**£350,650**	**£350,650**
Total (inclusive of VAT)	**£2,267,599**	**£2,267,599**

Annual payment terms
The payment terms have been revisited by CCGs and Provider. Agreed annual values are shown above and not subject to an annual price increase. Prices are inclusive of VAT.

Additional equipment budget
An additional budget has been agreed: £330,170 per annum

This is subject to the following:

Backlog: to be reduced to 476 open cases by the end of the contract.

Overspend: any over spend from previous three years must be recovered over the final 24 months of the contract as no additional payments will be made for this period.

Referrals (Rates and Complexity): there is no material change to either current referral rate or complexity of referrals; if a variance (up or down lift) of 10% or over is indicated, this will trigger a review by CCGs."

53. The figure in the table as the total for Year 4 and for Year 5 was the same as that originally agreed for Year 1.

54. There were some differences between the parties as to the meaning and effect of the entries below the table. However, when the Variation Agreement is read against the background of the original terms and with knowledge of the equipment supplies actually made in Years 1-3, the position is not open to any real doubt:

i) Extension: The first sentence set out above exercises the contractual option to extend the East Sussex Contract by 24 months, giving rise to its operation in Year 4 and Year 5.

ii) Annual payment terms: This refers to the figures set out in the table. It expressly characterises them as agreed annual figures, meaning that they are fixed. They include VAT. Net of VAT, the total agreed annual value was £1,889,666.

iii) Annual equipment budget: This provides for an additional allowance in respect of equipment only (i.e., no other costs). This too is expressly characterised as an agreed amount, meaning that the additional monies available to MHL in respect of equipment in either Year 4 or Year 5, once the annual limit in the table was exhausted, were capped at £330,170. I understand that this figure excluded VAT. It follows that the maximum figure that MHL could expect to receive in respect of sales in those years, excluding VAT, was £2,219,836.

iv) Backlog: This was a binding commitment, to be achieved within (and notwithstanding) the constraints arising from the annual payment terms and the additional equipment budget. The implication is that the parties agreed that this was, or should be, possible.

v) Overspend: The overspend from Years 1-3 – i.e., the sales supplied in excess of the EACV but not paid for, totalling £1,050,269 – could only be recovered over Years 4 and 5; but in the light of the previous provisions, this would only be possible if the sales actually supplied in Year 4 or Year 5 were less than the total of the (a) the agreed annual value and (b) the additional equipment budget – i.e., £2,219,836 in either year (excluding VAT). That is the only conceivable intention behind the words "… no additional payments will be made for this period."

vi) Referrals (Rates and Complexity): If referrals went up or down by 10% or over, this would trigger a review by the East Sussex CCGs. However, there is no indication as to the likely outcome of any such review. The CCGs might or might not agree to provide extra funds.

55. MHL remained under no obligation to provide equipment, beyond the limits set by the annual payment allowance and the additional equipment budget. It of course could do so, if it wanted. But, whereas previously MHL may have assumed (rightly or wrongly) that the CCGs would pay for additional equipment that was properly supplied on the basis of referrals, even if this meant exceeding the contractual monetary limits, this was now unlikely.

56. The clear terms of the Variation Agreement therefore should have made it apparent to anyone who read and understood it that:

i) MHL would not receive any payment in respect of the outstanding sales for Years 1 to 3, totalling £1,050,269, except in so far as sales in Year 4 or Year 5 might be less than £2,219,836 in either year.

ii) There would be no payment for sales in Year 4 or Year 5 in excess of £2,219,836 (excluding VAT).

iii) This was subject to the review process required if referrals went up or down by 10% or over, but that process did not guarantee that additional funds would be made available.

Mr Lock's failure to inform others

57. After the Variation Agreement had been signed, Mr Lock relied on it in order to claim money from the East Sussex CCGs, shortly before the SPA was concluded.

58. Mr Lock had a number of exchanges with Tracy Stickland, the CCGs' Senior Finance Manager, regarding two invoices which Mr Lock must have raised, each for £330,170 – i.e., precisely the amount allowed for under the Variation Agreement as the additional equipment budget for Year 4 and Year 5. Ms Stickland queried the text of the invoices as originally issued.

59. These exchanges began on 13 May 2019, when Ms Stickland noted that East Sussex CCGs had received two invoices dated 30 April 2019 which gave very sparse details, and she asked if they were for "the contract variation" and, if so if they could be re-issued stating this. In a subsequent email of 20 June 2019, she made it clear that the invoices should not use text that implied that relevant sums were "over and above the contract variation" – evidently because it would not be possible for her to authorise payment in excess of that contemplated by the Variation Agreement.

60. Mr Lock sent Ms Stickland both invoices in their final form on 20 June 2019 (although they were still dated 30 April 2019). As requested by Ms Stickland, each invoice characterised the relevant amount as relating to (respectively) "Contract Variation – Year 4" and "Contract Variation – Year 5". They were then paid by the East Sussex CCGs.

61. It is clear from the exchanges giving rise to these invoices that both Ms Stickland and Mr Lock understood that the invoices fell within the terms of the Variation Agreement, and specifically the provision for an additional equipment budget. Furthermore, Ms Stickland highlighted to Mr Lock that it would not be possible for MHL to be paid any monies that did not fall within the express provisions of the Variation Agreement.

62. Remarkably, however, Mr Lock appears to have negotiated, concluded and signed the Variation Agreement, and then conducted his exchanges with Ms Stickland regarding the two invoices dated 30 April 2019, without telling anyone within MHL about the Variation Agreement or explaining its significance.

63. How or why this came about is entirely unclear. However, Mr Paul Croll and Mr Colin Croll both said in evidence – and I accept – that they had no knowledge of the Variation Agreement, before the SPA. Furthermore, Mr Campling, who as I have already noted worked for MHL both before and after the SPA, and was called by Bidco, likewise said in evidence that he had no knowledge of the Variation Agreement before the SPA.

64. The significant amount of accrued income associated with the East Sussex Contract was raised between the parties shortly before the SPA concluded, at a meeting on 15 July 2019. This was the occasion when Cairngorm/Bidco suggested that part of the purchase price be held in escrow pending collection. As a result, Mr Colin Croll spoke to Mr Lock, who by chance was in a meeting with the East Sussex joint commissioner,

Sally Reed. At Mr Colin Croll's request, Mr Lock made a file note of what he claimed was the position that he reached with Ms Reed on that day, which Mr Colin Croll said reflected what Mr Lock told him by telephone:

> "The discussion was around the current outstanding equipment commitment of circa 1 million pounds.
>
> Sally confirmed that the East Sussex CCG's are fully aware of the outstanding monies. To date the CCG's have made a payment of circa 700k that was split across two invoices, from the original outstanding amount. The CCG's are working together to secure the balance of the outstanding monies due to Millbrook. Sally did suggest to potentially speed up the process Millbrook may consider putting together a detailed paper to demonstrate the overspend (some of the reasons behind it) and to show what work we have undertaken to control the current spend levels around, equipment procurement, recycling and refurbishment of equipment. Sally suggested that it may take a further 3 months to secure the additional funding
>
> Based on the conversation had, I remain 90% confident that we will secure the current outstanding monies within the next 3 months and 100% confident that we will recover the outstanding monies in full."

65. Mr Lock's file note is very difficult to reconcile with an email that Ms Reed sent to him on the following day, in which she said that she had spoken to Ms Stickland; that the CCGs would be looking for details of costs "for the last contract year" (i.e., Year 4, ending 30 June 2019); then said: "Once we have received this, we will review and may need to consider further audit to ensure clear understanding of where the pressures have arisen since the review at the end of contract year 2."

66. This indicates, first, that Ms Reed had checked with Ms Stickland, after the meeting with Mr Lock, before saying anything substantive; second, that she thought the discussion concerned overspend in Year 4; and, third, that she did not give an assurance of payment but suggested that, if suitable details were forthcoming for Year 4, this might give rise to the kind of review envisaged by the Variation Agreement, under the heading "Referrals (Rates and Complexity)".

67. In the light of Mr Lock's file note, and having heard the evidence from Mr Paul Croll and Mr Colin Croll, I have no doubt that the file note represents what Mr Lock told Mr Colin Croll. However, in the light of (a) the Variation Agreement, which Mr Lock had negotiated and signed the previous year, (b) Mr Lock's exchanges with Ms Stickland in May-June 2019 and (c) Ms Reed's email of 16 July 2019, I equally have no doubt that the account that Mr Lock gave Mr Colin Croll account bears no relationship whatsoever to the reality of the discussion that Mr Lock had with Ms Reed on 15 July 2019.

68. Not having received evidence from Mr Lock, it would be unfair for me to reach any settled view as to how, precisely, he came to give Mr Colin Croll the information that he did on 15 July 2019. However, in all the circumstances, it seems very unlikely that I would have felt able to treat any evidence from him as reliable.

After the SPA

69. Mr Skinner took up his position as CFO on 22 July 2019. On inspecting the purchase ledger, he discovered that debit balances were higher than he thought they should have been; that the overall debtor book was larger than he thought it should have been; and that the level of bad debt provision was much lower than he thought it should have been, given the large amount of debt. He therefore sought to reduce debtor days and collect old debts.

70. This process brought to light the large amounts apparently owed to MHL under the East Sussex Contract and under the Somerset Contract. In relation to East Sussex, Mr Skinner learnt in August 2019 that the historic debt had not yet been invoiced. His evidence and that of Mr Campling was that the East Sussex CCGs pushed back, when asked to clear that overspend, asking for explanations.

71. Initially, this task fell to Mr Lock. Under the direction of Mr Skinner, he prepared a draft report, which Mr Skinner and Mr Campling then checked and altered, in August 2019. Mr Lock then sent the finalised report to Ms Reed on 5 September 2019, explaining the financial pressure on MHL and justifying the overspend. She responded on 30 September 2019, relying on the Variation Agreement. Her response to him does not appear to have been forwarded by him to anyone else within MHL.

72. On 26 September 2019 MHL held a board meeting at which the East Sussex Contract was discussed as follows:

> "East Sussex (accrual not invoiced): £1.4m, c.£400k relating to years 1-3 possibly uncollectible. Current spend cut back to £51k pcm block fee to avoid increasing accrual. Waiting list growing as a result. Additional £57k pcm required in order to meet demand. PC and DS due to meet commissioner on 07 Oct to discuss payment of permitted overspend and secure additional funding to meet demand and clear waiting list. DS to investigate regarding a payment received in Apr-19 that could have been received in settlement of the disputed c.£400k."

73. It is apparent from this that those attending had not been briefed by Mr Lock and did not know about the Variation Agreement. Furthermore, they did not appreciate that the payments invoiced on 30 April 2019 did not relate to Years 1-3 but to Year 4 and Year 5 and had been justified by reference to the Variation Agreement.

74. Even without the benefit of the Variation Agreement, they were doubtful about the collectability of whatever unpaid sums related to Years 1-3. However, they do not appear to have appreciated that MHL's payment rights were limited to total of the EACV and the additional equipment budget. Nor did they appreciate that payments already received (under the invoices dated 30 April 2019) had exhausted the entire amount available under the additional equipment budget for Year 4 and for Year 5.

75. Emails from Mr Skinner in January 2020, expressing optimism about collecting substantial sums under the East Sussex Contract by the end of February 2020, again suggest that Bidco was still not aware of the problems that it faced by reason of the Variation Agreement.

76. At a board meeting on 26 February 2020, the existing debt was quantified at £1,450,000, and it was estimated that to hit the waiting-list target by the end of Year 5 there would be a further overspend of £350,00, making a total of £1,800,000. Mr Skinner was authorised to achieve either (a) settlement in full by 15 April 2020 (with a backstop of 31 May 2020) less a discount of £50,000 (or up to £100,000) or (b) settlement of £1,200,000 by 15 April 2020 (with a backstop of 31 May 2020) with the remainder paid over 12 months and no discount. This again suggests that Bidco was not yet aware of the Variation Agreement.

77. Mr Skinner corresponded with Ms Reed on the basis of these instructions, following which a meeting took place between them on 26 March 2020.

    i) Mr Skinner's report to the board concerning this meeting said that Ms Reed was to write, and that she would confirm that the East Sussex CCGs intended to pay but "in line with the contract" and that amounts to Year 3 might be irrecoverable.

    ii) When Ms Reed wrote on 1 April 2020, her letter in fact made it clear that the East Sussex CCGs were sympathetic, and there was a possibility of extra funds, but her letter expressed this in terms of undertaking "a full review of referrals, case-mix and expenditure from April 2019 to the end of contract year 5". It was explained that the fact that the review would take into account matters from April 2019, rather than from 1 July 2019 (when Year 5 began) was a concession that the CCGs were prepared to make because it aligned with their accounting year.

78. It therefore seems clear that, while Ms Reed may well have said that the East Sussex CCGs would pay "in line with the contract", she meant the East Sussex Contract as varied by the Variation Agreement (including the review mechanism provided for in the Variation Agreement). However, it also seems clear that this was not apparent to Mr Skinner, because he was not aware of the Variation Agreement. Nevertheless, what Ms Reed said at the meeting and in her subsequent letter obviously made Mr Skinner and MHL doubtful about the likelihood of recovering anything in relation to Years 1-3, albeit they remained more optimistic about Years 4 and 5.

79. The reality that MHL would not recover anything in relation to Years 1-3 was reflected in a further MHL board meeting on 28 May 2020, recording Mr Skinner updating the board in relation to East Sussex:

> "Current communicated intention is to reach a settlement on Y4-5 on 08 June in the region of c.£400k, with the residual £1.2M uncollectible. The Trust will provide detailed reasoning for the non-payment of the £1.056M (Assuming £400K paid)."

80. My interpretation of this record is that Mr Skinner was recounting the most recent communications with Ms Reed, which was that MHL would not recover more than £400,000. He had not yet received the CCGs' detailed explanation for not paying more, including why there would be no payment for Years 1-3.

81. Ms Reed tried to send Mr Skinner a copy of the Variation Agreement by an email of 5 June 2020, but the message appears to have failed. This was in advance of a meeting due to take place on 8 June 2020. It must have become apparent at the meeting that Mr

Skinner had not received the email of 5 June 2020, so Ms Reed re-sent it on 12 June 2020. I infer that she did so because she regarded the Variation Agreement as highly relevant to the ongoing discussions by which they were attempting to settle the position.

82. Prior to receiving the Variation Agreement (including in emails of 3 and 11 June), Mr Skinner was still ostensibly advancing the position that there was an accrued balance in MHL's books of nearly £1,600,000, and that the East Sussex Contract was one under which MHL was "entitled to be paid for the actual cost of services delivered" so that the CCGs had "always known [they were] liable to pay for excess on the contract value." It was in response to these assertions that Ms Reed sent the Variation Agreement.

83. Following receipt of the Variation Agreement, Mr Skinner and Ms Reed had a further meeting in July 2020, at which Mr Skinner appears for the first time to have expressly conceded that, for the sake of reaching agreement, MHL would put aside any claim in relation to Years 1-3 but was seeking payment in full for Years 4 and 5

84. Agreeing final terms on settlement took a few months longer. There were two significant meetings in November 2020 and January 2021, before a formal agreement was concluded on 14 January 2021 ("**the East Sussex Settlement Agreement**"). It provided for the East Sussex CCGs to pay MHL £354,000 plus VAT.

85. This not only resulted in MHL ultimately receiving more money than the Variation Agreement had provided for, but it also meant that MHL retained the full agreed value for Year 5 (including the additional equipment budget), despite the fact that actual sales in Year 5 had been substantially lower than the maximum amount allowed under the East Sussex Contract as varied. As I understand it, this was primarily because of the Covid-19 pandemic. The excess payment for Year 5 was £118,129.

Mr Skinner's evidence and his notebook

86. In oral evidence, Mr Skinner stated that he had found a version of the Variation Agreement, signed by Ms Reed but not by Mr Lock, much earlier than this – in October 2019. He said he found it by going through Mr Lock's emails. This was not mentioned in Mr Skinner's witness statement and seems very unlikely: all of Mr Skinner's inter-actions with Ms Reed, and his reports to the board, suggest that he was not aware of the Variation Agreement.

87. There is a manuscript note in Mr Skinner's notebook regarding a search, but I read this as relating to a search conducted after the event to check whether Mr Lock had sent the report that Mr Skinner had seen in draft in August 2019. The note records "Copy attached 5/9", before the words "No evidence sent to Sally. Search conducted." As I have noted above, there is indeed an email on record by which Mr Lock appeared to have sent the report to Ms Reed on 5 September 2019. I therefore believe that this notebook entry concerns a search conducted on Mr Lock's email account in relation to the 2019 report.

88. The notebook in which this appears covered the period from 14 August 2019 to 23 October 2019. This particular entry appears as the final entry that I have seen from the notebook – under the heading "Updated 23/8", on a page that comes after several entries that were undoubtedly made subsequent to 23 August 2019. I suspect that the search

was not conducted on 23 August 2019 but considerably later (possibly 23 August 2020, after Mr Lock had been dismissed and, I assume, no longer had control of his email account); and the entry was made in this particular notebook because Mr Skinner had gone over his old notes before conducting the search, and made the note towards the back of the relevant notebook. In any event, the terms of the manuscript are not consistent with it having been a search for, or which located, the Variation Agreement.

The settlement with the East Sussex CCGs

89. It follows that that the Variation Agreement can have had no effect on MHL's treatment of the East Sussex Contract prior to June 2020, in that no-one within MHL or Bidco knew about it – apart from Mr Lock. However, the Variation Agreement was significant in relation to the attitude of the East Sussex CCGs towards what they were prepared to pay. After June 2020, it was also significant to the attitude of MHL and towards what they were prepared to accept. Both sides negotiated as hard as one might expect, and both ultimately shaped their positions by reference to the Variation Agreement.

90. It was suggested by Mr Johnson that MHL might have done more to maximise the recovery achieved, but there is nothing to support this in the evidence. In particular, Mr Johnson suggested that MHL might have been affected by (a) the possibility of recouping sums from the Sellers, in this action, rather than from the East Sussex CCGs and (b) the desire to keep good relations with the East Sussex CCGs. While the board of MHL undoubtedly had in mind their possible rights against the Sellers, and quite reasonably wanted to preserve commercial goodwill, I see no indication that either of these factors affected the negotiations conducted by Mr Skinner.

91. On the contrary, it seems to me that, by recovering £354,000 (and retaining the excess sum for Year 5), MHL did as well as it reasonably could have done, in the light of the Variation Agreement.

The Somerset Contract

Terms of the Somerset Contract

92. The Somerset Contract commenced on 1 July 2015 and ran for 5 years, to 30 June 2020. Unlike the East Sussex Contract (and, I am told, most NHS contracts of this kind) it was not based on EACV. Somerset agreed to pay (on the basis of the NHS tariffs) for whatever equipment MHL provided. The contract permitted full monthly invoicing, but at Somerset CCG's request, MHL in fact invoiced fixed amounts each month, following by periodic reconciliations covering the outstanding balance.

Invoice 16150

93. Unfortunately, generating and issuing these reconciliation invoices was a task that fell to Mr Lock, who was neither prompt nor efficient. Significant outstanding sums were not covered by any reconciliation for long periods. This came to light when the October 2017 management accounts were completed, and Mr Paul Croll noticed that the accrued income balance had not been reduced by as much as he expected. Mr Lock checked his workings and (as he told Mr Paul Croll) realised he had missed a quarter's invoicing.

94. On 22 December 2017, Mr Lock generated and MHL issued invoice 16150. This purported to be a reconciliation invoice for the period July 2015 to March 2017, in the sum of £237,932.62 + VAT (a total of £285,519.14).

95. On its face, invoice 16150 did not relate to a single quarter but to the entire period from the inception of the contract until March 2017. Furthermore, Somerset CCG had already received invoices that (on their face) appeared to cover the period to March 2017 (indeed, invoice 15293, issued on 27 October 2017, was said to be "for services & products delivered up to the end of March 2017 less £60,000 accessories"). Mr Paul Croll suggested, both in contemporaneous emails and in evidence, that invoice 16150 probably related to the period April to June 2016. That may be correct, but the reality is that this is unclear even now (£285,519.14 seems a large amount for a single quarter, by comparison with the other invoices I have seen).

96. In these circumstances, it could not have been clear to Somerset CCG why this invoice had been issued or what it was supposed to cover. Mr Paul Croll suggested that the invoice would have been accompanied by a detailed spreadsheet and supporting documents which would have clarified the position, but the subsequent emails from Somerset CCG indicate otherwise.

<u>The exchanges re invoice 16150, prior to the SPA</u>

97. The CCG queried the invoice by various exchanges with Mr Lock, on the basis that (a) it had already received and paid reconciliation invoices for this period, (b) it had already finalised its accounting periods for 2015/2016 and 2016/2017, (c) the invoice was unacceptably late and (d) in any event an audit would be required. These points were ultimately set out in a formal letter from Somerset CCG dated 27 July 2018, sent by Alison Henly, the Chief Finance Officer.

98. This impasse continued for some time with no real progress. On 15 August 2018, Michael Carrington of Somerset CCG (one of MHL's main points of contact) cancelled a meeting with Mr Lock because of his failure to provide information required, noting:

> "...I understand we have had no response from you relating to the outstanding £285k invoice, which the CCG has declined to pay in full…the lack of communication from you is immensely frustrating and time consuming for us both chasing up responses."

99. Mr Paul Croll gave evidence that he attended a contract review meeting with Somerset on 11 September 2018, because he wanted to know when invoice 16150 would be paid and received the impression that it would be paid soon. There is no record of this meeting, and I found his evidence on this point somewhat vague. However, this is unimportant because whatever happened at that meeting was overtaken by subsequent exchanges between Somerset CCG and Mr Lock, over a few days in January 2019.

100. On 15 January 2019 at 15.48, Mr Carrington emailed Mr Lock in relation to email 16150, saying:

> "I can confirm the CCG would be able to authorise payment of the subject invoice to offset against any outstanding reconciliation payment due for the period December 2017 to December 2018. This would only happen following

> receipt of the balancing invoice which should clearly show the offset amount, and should also clearly state that no further payments remain outstanding for that period and represents full and final payment."

101. Mr Lock replied saying "Thank you, we will look to raise the additional invoice next week, this following the agreed reconciliation of the data for said period." Mr Lock thereby agreed to that solution.

102. Mr Lock then purported to forward the email he had received from Mr Carrington to Mr Paul Croll. However, in the version that he provided to Mr Paul Croll, he had removed all the text by which Mr Carrington had imposed a condition on this payment, which Mr Lock had accepted, to the effect that it would be offset against sums otherwise payable for December 2017 to December 2018.

103. At 8.46 on 16 January 2019, Mr Lock emailed Mr Carrington, saying:

> "Would you consider the below wording…:-
>
> Hello Dave,
>
> I can confirm the CCG would be able to authorise payment of the subject invoice of £258,519.14 to offset against any outstanding reconciliation payment due for the period December 2017 to December 2018. This would only happen following receipt of the balancing invoice which should clearly show the offset amount and should also clearly state that no further payments remain outstanding for that period and represents full and final payment."

104. Mr Lock then followed up at 9.15, amending the figure to "£285,519.14". He said: "*Correction below, typed the figure in wrong (sorry) I should have stayed in bed.*" Mr Carrington responded at 9.43, in precisely the terms requested by Mr Lock.

105. As before, however, when Mr Lock forwarded to Mr Paul Croll the confirmation received from Mr Carrington, he omitted the text relating to the offset.

106. By agreeing to offset the totality of invoice 16150 against sums expected to be payable in due course, Mr Lock was agreeing, on behalf of MHL, to forgive the totality of the invoice amount.

107. The arrangement that he and Mr Carrington arrived at assumed that the reconciliation amounts for the later period would exceed the amount of invoice 16150. This turned out not to be the case.

108. The Sellers suggested that this meant that Mr Lock's agreement with Mr Carrington (i.e., in reality, MHL's agreement with Somerset CCG) was ineffective. I disagree: it seems to me that Mr Lock and Mr Carrington must both have intended that, if the reconciliation amounts for the later period did not exceed invoice 16150, it would have to be offset by some other method. If an officious bystander had asked them in January 2019 whether this was what would have to happen, they would both have said "Of course".

109. In any event, the fact that the reconciliation amounts for the period to December 2018 would be insufficient became apparent rapidly: this was pointed out to Mr Lock by Mr

Carrington on 17 January 2019, and Mr Lock apologised (he appears to have forgotten that the Somerset CCG had already made a payment in November 2017).

110. On 21 January 2019, Jacqui Damant of Somerset CCG therefore said that the offset option was no longer viable and suggested that "this invoice is cancelled/credited."

111. There is no trace of an email from Mr Lock in response. However, it is inherently unlikely that he did not respond at all, not least because total silence would have provoked a chaser from the CCG – which did not happen. The next relevant email was not sent until 11 June 2019, when Mr Carrington sent an email to Mr Lock that addressed not only invoice 16150 but also another invoice in relation to which Mr Lock's paperwork had not been forthcoming as promised:

> "Hi Dave,
> I have still not received the credit note and part credit note for the subject invoices. Could you check status with your finance team please.
> Thanks
> Mike"

112. Mr Lock responded on 17 June 2019, apologising and promising to "… get copies of the credit notes and send over to you".

113. In the absence of evidence from Mr Lock or the Somerset CCG, it is impossible to be certain, but this strongly suggests that Mr Lock responded to Ms Damant's email promising that MHL would issue a credit note. That is the inference that I draw. In any event, the exchange between Mr Lock and Mr Carrington in June 2019 either confirmed a prior promise to issue a credit note or impliedly gave one at that stage.

114. Once again, however, Mr Lock did not reveal this to anyone else within MHL.

115. The result is that Somerset CCG did not regard itself as obliged to pay invoice 16150, and steadfastly refused to do so.

116. No credit note was issued for invoice 16150. Mr Carrington repeated that Somerset CCG was expecting "the agreed credit note" by an email of 9 July 2019. On 11 July 2019 he sent a further email, not to Mr Lock but to Annette Cairns of MHL (who had been chasing payment), stating that Somerset CCG was withholding payment of a separate invoice (no. 22708) pending receipt of the credit note for invoice 16150.

<u>MHL's decision to write off invoice 16150</u>

117. The dispute then escalated, shortly after the SPA. On 27 July 2019, Alison Henly sent a further formal letter, which referred to and repeated her letter of 27 July 2018 and stated that "… repeated assurances were given by your organisation that a credit note would be issued."

118. Mr Thaper withdrew the task of dealing with this invoice from Mr Lock. At a board meeting on 26 September 2019, the board agreed to write off invoice 16150. The minute is redacted (presumably reflecting legal advice). The relevant part reads as follows:

> "Somerset WCS (invoiced): £278k invoice (reconciliation invoice for long period ending Dec- 17). DL agreed payment of £278k in exchange for £278k credit against next payment in writing, however, next payment was less than £278k and so agreement fell away and Somerset have withheld payment of a £555k block payment of as a result. Previously labelled as quarterly payment missed. Narrowly missed referral of case to NHS fraud body. 25% provided for at Dec-18. [REDACTED] Additional £555k still being withheld though thought to be collectible in exchange for writing off the £287k. Board approved DS to write-off £278k in exchange for payment of £555k, including pushing to agree two-year extension."

(The reference to £278,000 appears to be a typographical error.)

119. The Sellers criticised MHL for writing off invoice 16150, but in my judgment MHL had no real alternative. The Sellers suggested that MHL took an inappropriately soft approach, because it was concerned to secure a fresh contract from Somerset CCG (a tender had been submitted and the board appears not to have known that it had been successful). The Sellers also suggested that MHL was unduly impressed by Somerset CCG's arguments about the lateness of the invoice and should not have paid attention to the threat of referral to the NHS fraud body.

120. None of these points has any weight. The simple fact is that Mr Lock had given an assurance that invoice 16150 did not have to be paid and had promised to issue a credit note. MHL was bound by this.

The MHL audited accounts for FY 2018 and management accounts

<u>The MHL audited accounts for FY2018</u>

121. The balance sheet in MHL's audited accounts for the year to 30 June 2018 reported debtors (amounts falling due within one year) in the sum of £21,795,000. Note 14 referred to an impairment loss of £84,000.

122. I understand it to be common ground that this included a bad debt provision in relation to the Somerset Contract invoice 16150 of £49,570. Accordingly, the accounts were prepared on the basis that the recoverable amount in relation this invoice was the balance of £188,362.62, plus VAT. On the basis of my findings, the whole of invoice 16150 should have been written off, David Lock's exchanges with Somerset CCG in January 2019 having preceded the date when the audited accounts were approved (on 13 February 2019).

123. Furthermore, the audited accounts reflected the full equipment costs that MHL had incurred, but had not yet invoiced, in relation to the East Sussex Contract in relation to Years 1-3 of that contract. In other words, the accounts did not reflect the Variation Agreement, despite the fact that the Variation Agreement was dated 18 May 2018 (before the close of the relevant accounting period) and was signed by both parties before the audited accounts were approved. This again affected the amount recorded for debtors on the balance sheet, very significantly (by about £1,050,000).

124. The result is that the relevant balance sheet entry should in fact have been £20,557,000.

125. However, the East Sussex Variation Agreement also affected the statement of income and retained earnings, because Year 3 of the East Sussex Contract falling within the year to 30 June 2018. The reported figures in the audited accounts included turnover of £114,360,000, gross profit of £16,516,000, operating profit of £1,234,000 and profit before tax of £1,059,000. On the basis of my findings, each of these figures was overstated. Bidco's figure for this overstatement (which I accept) was £817,000.

The MHL management accounts

126. The relevant MHL management accounts were not affected by the issues surrounding the Somerset Contract (which on any view related to sums arising before the period of the management accounts). However, the East Sussex Variation Agreement was highly relevant to the management accounts, because Year 4 of the East Sussex Contract covered the period from 1 July 2018, which coincided precisely with the period of these management accounts.

127. The January 2019 management accounts included figures for MHL's FY2019 sales as follows (these figures all in £000's):

Jul-18	Aug-18	Sep-18	Oct-18	Nov-18	Dec-18	Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19	TOTAL
22	**22**	**20**	**23**	**22**	**19**	**22**	**20**	**21**	**20**	**21**	**20**	**252**
9,958.4	10,385.7	10,333.8	11,212.0	10,511.7	8,985.7	10,808.8	9,755.9	10,086.2	9,032.6	9,370.9	9,147.3	119,589.1

128. The figures for months up to and including the figure for January 2019 were actual, those from February onwards were projected. The total for the year reflected both.

129. The sales figures for East Sussex were as follows:

Jul-18	Aug-18	Sep-18	Oct-18	Nov-18	Dec-18	Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19	TOTAL
22	**22**	**20**	**23**	**22**	**19**	**22**	**20**	**21**	**20**	**21**	**20**	**252**
244.7	273.2	220.0	210.1	251.0	228.9	227.2	220.4	220.4	220.4	220.4	220.4	2,757.2

130. On the basis of these figures, the depot contribution for the East Sussex Contract, for FY 2019, was projected to be £196,000. Adding back depreciation of £106,100, this indicated EBITDA referable to the East Sussex Contract of £302,100. The overall EBITDA of MHL projected for FY2019 was £3,875,400.

131. The final MHL management accounts received by Bidco prior to the SPA were those for April 2019. The equivalent figures for MHL's FY2019 sales were as follows (again, in £000's):

Jul-18	Aug-18	Sep-18	Oct-18	Nov-18	Dec-18	Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19	TOTAL
22	**22**	**20**	**23**	**22**	**19**	**22**	**20**	**21**	**20**	**21**	**20**	**252**
9,958.4	10,385.7	10,333.8	11,212.0	10,511.7	8,985.7	10,808.8	10,431.3	10,787.6	9,856.3	9,379.7	9,155.4	121,806.5

132. This time, all the figures for months up to and including April 2019 were actual. Thus, the FY2019 figures in these management accounts (including the figure for sales) were based on 10 months' actual figures, and only 2 months' projected figures.

133. The equivalent figures for the sales for East Sussex were as follows:

Jul-18	Aug-18	Sep-18	Oct-18	Nov-18	Dec-18	Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19	**TOTAL**
22	**22**	**20**	**23**	**22**	**19**	**22**	**20**	**21**	**20**	**21**	**20**	**252**
244.7	273.2	220.0	210.1	251.0	228.9	227.2	246.2	209.4	199.1	220.4	220.4	2,750.7

134. The depot contribution of East Sussex for FY2019 was projected to be £219,600. Adding back depreciation of £106,900, this indicated EBITDA referable to the East Sussex Contract of £326,500. The overall EBITDA of MHL projected for FY2019 was £3,817,400.

135. All these figures were incorrect, in that they did not take account of the fact that the effect of the Variation Agreement was to limit sales under the East Sussex Contract for FY2019 to a maximum of £2,219,836 (excluding VAT). Thus, the FY2019 figures for sales in the January 2019 management accounts should have been reduced by about £537,000, and those in the April 2019 management accounts by about £530,000. That would have resulted in identical reductions in the derived EBIDTA for FY2019, i.e., about £537,000 and about £530,000 (respectively) – i.e., the EBITDA figures for the East Sussex Contract would have been negative.

Breach of warranty

136. It follows that the Seller were in breach of the warranties in Schedule 4 of the SPA, paragraphs 3.2 (Accounts true and fair) and 3.8 (management accounts true and fair).

137. Bidco also asserted the breach of various other provisions in Schedule 4:

i) It asserted that Mr Lock's agreement to off-set or waive Somerset invoice 16150, and the East Sussex Variation Agreement, were disposals of assets other than in the ordinary and normal course of business at full market value, contrary to paragraph 4.3(b). I have not received evidence satisfying me that accommodations like these are not normal in this sector. In any event, the East Sussex Variation Agreement was not a disposal of a legal asset, given that MHL had no legal entitlement to be paid anything in respect of the historic overspend in Years 1-3, and the terms agreed for Year 4 actually increased the potential total sum payable.

ii) It asserted that the Locked Box Statements materially misstated the assets and liabilities of MHL, contrary to paragraph 5.1. This follows from my earlier findings.

iii) It asserted that no indication had been given that the sums reflected in the Accounts and management accounts in relation to East Sussex and Somerset included amounts that were bad or doubtful, contrary to paragraph 7.4. This follows from my earlier findings.

iv) It asserted that book debts had been incorrectly recorded, contrary to paragraph 7.5. This again follows from my earlier findings: Somerset invoice 16150 should have been treated as bad or doubtful or at least been the subject of comment in note 14; the historic East Sussex sums should not have been treated as debts at all, and the actual entries in the management accounts were overstated.

v) Bidco further asserted breach of paragraph 17.1, on the basis that the East Sussex Variation Agreement was not listed in schedule 12 to the SPA or contained in the Data Room. This was not disputed by the Sellers, but it caused no separate loss in addition to the breaches relating to the Accounts and management accounts.

Quantum: the principles

138. Both sides proceeded on the basis that the measure of damages for breach of warranty in a share sale agreement is the difference between the Warranty True value of the shares and Warranty False value: *Lion Nathan Ltd v C-C Bottlers Ltd* [1996] 1 WLR 1438, at p.1441; *Ageas (UK) Ltd v Kwik-Fit (GB) Ltd* [2014] EWHC 2178 (QB); [2014] Bus LR 1338, at [14].

139. I must assess the quantum of damages on the basis of a hypothetical, reasonable willing buyer and a hypothetical, reasonable willing seller, rather than being bound by the subjective views of Bidco or these Sellers. In *The Hut Group Ltd v Nobahar-Cookson* [2014] EWHC 3842 (QB), Blair J said at [180(2)] that, in both the Warranty True and the Warranty False context, the object is to arrive at:

> "The estimated amount for which an asset or liability should exchange on the valuation date between a willing buyer and a willing seller in arm's length transaction, after proper marketing where the parties had each acted knowledgeably, prudently, and without compulsion."

140. It is important not to be unduly affected by hindsight, i.e., events subsequent to the SPA that the parties could not have known about or anticipated at the date of the SPA: *MDW Holdings Ltd v Norvill* [2022] EWCA Civ 883, at [49].

141. All of that having been said, the thinking and conduct of both parties at around the time of the SPA can in principle be relevant to this inquiry. If and in so far as either Bidco or the Sellers can be taken to be reasonable commercial people, their assessment of the relevant commercial risks and opportunities may shed light on how the hypothetical reasonable willing buyer and seller might be expected to have approached matters.

142. Furthermore, while in principle quantum is to be approached by identifying the difference between the Warranty True value of the Company at the date of the SPA and the Warranty False value, this difference inevitably depends on the impairment to the Warranty True value that a hypothetical reasonable willing buyer would have established in negotiations, if such hypothetical reasonable willing buyer had known that the Sellers were in breach of warranty, but had nevertheless remained willing to buy. As long as the Warranty True value exceeds the impairment, the quantum of the impairment represents the quantum of the claim.

Warranty True

143. It is not unusual, in cases of this kind, to treat the price actually paid as the Warranty True value. Bidco pointed out that *Lion Nathan*, *Ageas* and *The Hut Group* were all cases where this approach was adopted. Indeed, in *Ivy Technology Ltd v Martin* [2022] EWHC 1218 (Comm), Henshaw J described this at [561] as "a general rule of thumb".

144. I accept that, in this case, the price actually paid represents the Warranty True value. I do so not blindly but because it resulted from an enterprise value that I accept was calculated by the entirely orthodox method of applying a multiple to the EBITDA. This was attested to by Mr Thaper, and it was also expressly stated in the offer letter of 25 March 2019.

145. The Sellers and their expert Mr Hall criticised this approach on a number of grounds, none of which has any force.

146. First, it was said that Bidco's assessment was based on unwarranted information, i.e., the projections in the management accounts (which were incorporated into the Financial Pack). However:

    i) Any reasonable buyer relying solely on the warranted figures (including the actual results in the management accounts) would have to value the company by using those warranted figures as the basis for forming an opinion as to the likely future performance of the business.

    ii) That is also the process followed by Mr Paul Croll when he approved the projections in the management accounts, as he explained in evidence.

    iii) The hypothetical reasonable willing buyer would have had to consider whether to accept those projections, or reject them and derive different forecasts on the basis of the actual figures.

    iv) In doing so, the hypothetical reasonable willing buyer would have taken into account Mr Paul Croll's deep knowledge of the business, the fact that (as Mr Paul Croll stated in evidence) the projections reflected budget figures prepared in advance for his use in managing the company (rather being figures intended to boost the price of any sale) and the fact that Mr Paul Croll is an intelligent businessman and competent accountant (as he demonstrated in his generally impressive evidence).

    v) I am satisfied that it is likely that the hypothetical reasonable willing buyer would have adopted the projections in the management accounts and that it was reasonable for Cairngorm/Bidco to do so.

147. Second, it was suggested that, even if the figures for FY2019 EBITDA were acceptable in themselves (i.e., as figures for FY2019), they should not have been treated as maintainable EBITDA for valuation purposes. It was said that there was a declining trend.

    i) It is important to bear in mind that the relevant valuation was that of MHCDC, i.e., (in effect) all the Millbrook companies in the aggregate. It was not the valuation of MHL alone and certainly not the valuation of either the East Sussex Contract or the Somerset Contract. The relevant maintainable EBITDA was, therefore, that of MHCDC/the Millbrook companies as a whole (this being the figure to which Cairngorm/Bidco applied the multiple of 6.8).

    ii) It was not suggested to me that there was a declining trend in respect of the EBITDA of MHCDC and the Millbrook companies as a whole. On the contrary,

the Financial Pack indicated that the aggregate Millbrook EBITDA was increasing, year-on-year. However, so far as this point is concerned, all the Seller's focus was on MHL. For this reason alone, the point has no real force.

iii) Even in the context of MHL, there was no general decline in EBITDA, on the basis of the January 2019 and April 2019 management accounts. On the contrary, MHL's EBITDA was shown as increasing from FY2018 to FY2019. Once again, this makes it difficult to justify adopting a figure for maintainable EBITDA that was below the FY2019 figure for MHCDC/the Millbrook companies.

iv) In the specific context of the East Sussex Contract, EBITDA declined overall from 2018 to 2019 and was projected to decline further in FY2020 and then stabilise. However, it was not obviously declining in the 12 months leading up to the SPA; and the actual figures posted for February to May 2019 in the April 2019 management accounts were better than the projected figures in the January 2019 management. As Mr Thaper said in evidence, and Mr Woolgar repeated in submission, this confirmed it was acceptable, when concluding the SPA, to stick with the enterprise value arrived at on the basis of the January management accounts (via the Financial Pack) and set out in the offer letter.

148. Third, it was suggested that there was no justification for the use of a multiple of 6.8.

i) This is incorrect. Mr Thaper has great experience in this sector. In his first witness statement he said that 6.8 was used because he regarded 6.8 as appropriate.

ii) In his second witness statement, he expanded on this, saying that it was derived from comparable transactions and it took into account both features of the healthcare sector (e.g., growing population of wheelchair users) and features specific to Millbrook (the size of the business, management skills, funding sources, poor finance function, the fact that some contracts were coming up for renewal).

iii) None of this evidence was challenged. On the contrary, Mr Hall accepted in cross-examination that Mr Grantham's selected maintainable EBITDA figure of £6,610,000 was reasonable for MHCDC as a whole. He also accepted that the multiple of 6.8 was appropriate, if an EIBTDA x multiple approach were to be followed.

149. Fourth, and connected with the points already considered, it was suggested that it was inappropriate to arrive at enterprise value on the basis of EBITDA x multiple, and that it would have been better to use a DCF analysis.

i) This criticism loses all force when it is apparent that Bidco's case does not in truth rely on unwarranted information in relation to EBITDA, that it was proper to treat the FY2019 EBITDA in the management accounts as maintainable EBITDA, and that the multiple of 6.8 was justified.

ii) This point was not pressed on Bidco's expert Mr Grantham in evidence, nor was it pursued with much vigour in the Sellers' closing submissions.

iii) The EBITDA x multiple approach to valuation is in fact commonly used in transactions of this kind, as Mr Hall accepted in evidence. No proper objection to its use in this case was advanced.

iv) The Seller's other main point in this regard was their case on the risk of renewal. I address the merits of this point below. However, even had I been impressed by it, I understood to be confined, essentially, to MHL's contract with East Sussex. It therefore cannot provide a compelling reason to discard the EBITDA x multiple approach when valuing the MHCDC and the Millbrook companies in the aggregate.

150. Fifth, it was suggested that the East Sussex Contract, in particular, should not be treated as a source of maintainable EBITDA, even on a Warranty True basis, because it entered its final year on 1 July 2019 and its renewal was doubtful, plus the margins available to MHL were likely to be compressed.

i) I am sceptical that the hypothetical reasonable willing buyer would have adjusted the maintainable EBITDA by assessing the likelihood of a specific contract being renewed. Doing this would require the same scrutiny being given to all contracts (or, at least, all contracts up for renewal), and would be impossible to predict for any given contract.

ii) I would expect the risk of contracts not being renewed would be taken into account when selecting the appropriate multiple. Similarly, the risk of margin-compression must be applicable across the sector generally, and therefore to be considered in the context of the multiple. Mr Thaper's evidence confirmed that this was the case and that these points had been looked at in relation to the multiple.

151. I therefore accept that, on the Warranty True basis, the enterprise value was £45,000,000. The adjustments that led from this to the sale price of £28,032,500 (plus the Stamp Duty Escrow Amount) were mechanical and need no revision on the hypothesis that the warranted information was correct. The actual sale price therefore does represent the Warranty True value of Millbrook.

Warranty False: Enterprise value

EBITDA

152. The single most significant part of Bidco's case on quantum was in relation to EBITDA.

153. Bidco did not suggest that the problems associated with the Somerset Contract, i.e., invoice 16150, had any effect on EBITDA: they were essentially historic, and related specifically to poor management by Mr Lock (i.e., his failure to issue invoices promptly or efficiently). The reasonable willing buyer would not have considered these problems likely to affect the business going forward, or (therefore) have taken them into account when assessing the maintainable EBITDA for valuation purposes.

154. Bidco's case on maintainable EBITDA therefore was confined to the East Sussex Contract. Here, Bidco pointed to the adjustments that should have been made to the management accounts, specifically to the figures contributing to FY2019.

155. Bidco's expert Mr Grantham said that, if the Variation Agreement had been taken into account, the management accounts would have shown that the East Sussex Contract was unprofitable to MHL. When considering maintainable EBITDA, the East Sussex Contract therefore should have been ignored.

156. In fact, its contribution to the FY2019 EBITDA, as set out in the January 2019 management accounts, had been £302,100. If this were to be stripped out, the overall EBITDA for MHCDC/the Millbrook companies therefore would have been reduced by £302,000 – from £6,613,000 to £6,311,000. Bidco's case accordingly was that, on the Warranty False basis, Cairngorm/Bidco would have applied the multiple of 6.8 to £6,311,000, giving an enterprise value of £42,944,000.

157. I accept that, if the management accounts had been prepared so as to acknowledge the Variation Agreement, they would have had to reflect the fact that MHL's contractual entitlement to payment was limited by the Variation Agreement, as set out above. The management accounts would have shown the East Sussex Contract to be loss-making in FY2019, with negative EBITDA. My route to that conclusion is slightly different from Mr Grantham's, because he had been instructed to approach the East Sussex Contract on the basis that there was a specific monthly maximum sum allowed for equipment (per the comment in Mr Lock's report of August 2019), and I disagree with that assumption. However, this makes no practical difference. On either view, the FY2019 results for East Sussex would have been loss-making, with negative EBITDA.

158. However, the reason why MHL carried on performing the East Sussex Contract in a manner that led to inevitable losses is that its management was not aware of the Variation Agreement, Mr Lock having unaccountably kept its existence to himself. If it had been known within MHL that the company would not be paid for sales beyond the limits established by the Variation Agreement, the company would not have continued to make further sales, unless the East Sussex CCGs had agreed to make more funds available (possibly via the review process provided for in the Variation Agreement). The Sellers relied on this heavily.

159. The high-watermark of the Sellers' case on this was to argue that, even if Bidco had known of the Variation Agreement, it should have taken note of the fact that CCGs generally paid for equipment supplied irrespective of contractual limits and that this had been the case in Year 1 of the East Sussex Contract. I do not see that Bidco or any hypothetical reasonable willing buyer could properly have taken this hyper-optimistic approach.

160. Next, the Sellers argued that the outcome later achieved in the East Sussex Settlement Agreement was exactly the kind of outcome that should have been foreseen by Bidco or by the hypothetical reasonable willing buyer, and should have been factored into the assessment of maintainable EBITDA (in the context of East Sussex). Similar things were also said about the excess payment received, and retained, in relation to Year 5. I consider that, in both respects, this would have required unjustifiable optimism. These points are only made with the benefit of hindsight (cf. the reference above to *MDW Holdings Ltd v Norvill*). In July 2019, there would have been grounds to hope that negotiations might in due course be fruitful, but no reasonable buyer would have counted on this to the extent of factoring it into the assessment of maintainable EBITDA. Still less would any reasonable buyer have anticipated the Covid-19 pandemic or the £118,129 excess payment in respect of Year 5.

161. However, the point to which Mr Johnson devoted the most attention was that the losses incurred on the East Sussex Contract in FY2019 only arose because the management of MHL had not known about the Variation Agreement. The Sellers' case was that, if the management had been properly informed about the Variation Agreement and had understood its effect, they would have appreciated those losses could be avoided by restricting sales (in particular, equipment sales) so that they remained within the contractual limit.

162. Mr Johnson put this case to the witnesses, securing factual evidence to the effect (a) that the East Sussex Contract permitted MHL to restrict sales in this way and (b) that this is what the new management in fact did, in Year 5, once the existence of the Variation Agreement came to the board's attention.

163. He then put to Mr Grantham that, if this had been the relevant assumption in the context of maintainable EBITDA, the East Sussex Contract would not have been treated as loss-making but profitable. It would have been anticipated that, in Year 5, MHL would make the maximum sales consistent with the Variation Agreement, and in relation to these sales would profit on the basis of the 9% margin I have already noted. Mr Johnson said that the real difference between this hypothetical position and that anticipated in the January 2019 management accounts is that those management accounts anticipated a greater volume of sales in Year 5/FY2020, and a 9% profit margin achieved on that greater volume. The effective loss to MHL, on the basis of this case, was the loss of the 9% profit margin on the sales that would not be made. Mr Johnson put to Mr Grantham, and Mr Grantham accepted, that this amounted to only £38,000.

164. I accept that, if sales had been kept within the contractual limit, MHL's EBITDA in relation to the East Sussex Contract (and, therefore, overall) would have been reduced by this amount, as compared with the figures suggested by the management accounts. I also accept that any hypothetical reasonable willing buyer would have been able to do this, just as Bidco was in fact able to, in Year 5. What I do not accept, however, is that it follows that this is how the business should be valued, on the Warranty False basis.

165. The Warranty False analysis requires me to consider what the hypothetical reasonable willing buyer and hypothetical reasonable willing seller would have agreed – or how a reasonable objective valuer would have valued the business – knowing the true position, in July 2019. In these circumstances, the Accounts would correctly have recorded worse results in FY2017 and FY2018 (reflecting the losses made by MHL on the East Sussex Contract in Years 2 and 3), and the management accounts would have recorded (and, in part projected) losses being made on the East Sussex Contract in Year 4, and (therefore) worse results in FY2019. It therefore is inescapable that the FY2019 EBITDA of MHL, and therefore of the Millbrook companies in the aggregate, would have been £302,000 lower. This £302,000 difference would have been reflected in the Financial Pack.

166. The Sellers suggested in closing submissions that, with knowledge of the Variation Agreement, the East Sussex Contract would have been predicted to make a profit in Year 5, with sales restricted (as I have found, to £2,219,836) and with MHL making its 9% profit on the equipment sold. Crucially, they then contended that an objective valuation conducted in July 2019 would have adopted that position in relation to the East Sussex Contract, when assessing maintainable EBITDA: i.e., the fact that the East Sussex Contract was in fact loss-making in FY2019 would be ignored on the basis that

the position would be different going forward. Therefore, the Warranty False maintainable EBITDA must differ from the Warranty True maintainable EBITDA by only £38,000.

167. My difficulty with this argument is that it does not reflect the way that Cairngorm/Bidco in fact assessed enterprise value, or (in my view) how hypothetical reasonable parties would have done so. As I have already noted, the maintainable EBITDA that needed to be used was that of MHCDC, which was arrived at by aggregating the EBITDA within comparable accounting periods of all the Millbrook companies; and the period in question was that to the end of June 2019 (i.e. MHL's FY 2019). The Sellers' argument requires it to be assumed that an objective valuation would have used EBITDA to the end of June 2019 for all the other Millbrook companies, and for all of MHL's accounts except the East Sussex Contract; but that for this single contract, of one Millbrook company, a different figure would have been used – in effect, a corrected projection for FY2020 (being Year 5 of the East Sussex Contract). I consider this unrealistic.

168. Maintainable EBITDA was in fact based, and always would have been based, on the EBITDA for FY2019 – initially, as taken from the Financial Pack, but also as indicated in the successive management accounts produced through to the April 2019 management accounts. The figures for FY2019 EBITDA were the foundation for Cairngorm/Bidco's assessment of enterprise value, and would have been the foundation for any hypothetical reasonable willing buyer, any hypothetical reasonable willing seller and any hypothetical objective valuer.

169. Information suggesting that MHL was likely to do better under the East Sussex Contract in Year 5 – i.e., FY2020 – would of course have been welcome. However, I have in mind that the Financial Pack P&L summary actually provided in March 2019 already showed the projected EBITDA of MHCDC rising by over £300,000, without this affecting maintainable EBITDA. I am sceptical that news that it should theoretically be possible to stem the losses under the East Sussex Contract would have had any real effect on the maintainable EBITDA of MHCDC. Nor do I consider that there would have been any real effect on the multiplier. However, it is likely to have affected negotiations in relation to some of the adjustments to the enterprise value, which I deal with later.

170. I therefore accept Bidco's case that, on the Warranty False analysis, the maintainable EBITDA of MHL – and, by extension, the maintainable EBITDA of MHCDC – would have been reduced by £302,000. This would mean using aggregate EBITDA of £6,311,000, rather than £6,613,000.

171. On the basis that the EBITDA x multiple approach is the most appropriate way of arriving at enterprise value, and on the basis that 6.8 is the most appropriate multiple, this means that, on the False Warranty basis, that would suggest an enterprise value of MHCDC of about £42,914,800.

172. Bearing in mind my earlier comment that the parties appear to have worked on the basis of reasonably round numbers, I suspect that this would have been rounded up to £43,000.000. I therefore find that, on the Warranty False basis, the enterprise value of MHCDC would have assessed at £43,000,000, and the SPA transaction would have

been proceeded on that basis. This differs from the enterprise value that the parties actually used by £2,000,000.

The working capital adjustment

173. As already noted, the offer letter of 25 March 2019 proposed a number of adjustments to the enterprise value, including one in respect of normalised net working capital.

174. It was common ground that the process actually followed by the parties in arriving at the SPA price included such an adjustment, and that such an adjustment is typical of transactions of this kind. Agreeing on the quantum of this adjustment primarily involved negotiations as to the 'target' working capital, meaning (in Mr Thaper's words) "the amount of working capital (or cash) that the business required to achieve the projected maintainable earnings."

175. Working capital included the debts owed to the company. On the Warranty True basis, it therefore included the historic debts shown in the Accounts and management accounts in relation to the East Sussex Contract (up to and including Year 4) and the Somerset Contract (invoice 16150). However, on the Warranty False basis, those debts could not count towards working capital, being write-offs.

176. Mr Thaper's evidence was that, if he had known about the Variation Agreement and the agreement to waive invoice 16150, this would not have affected the target working capital, which he would have wanted to keep the same, but it would have affected the locked box working capital, which would have been reduced accordingly.

177. Bidco's case (relying on the evidence of Mr Grantham) was that the locked box working capital fell to be reduced from £17,155,000 to £15,504,000, i.e., by £1,651,000. This would mean that the net working capital adjustment changed from adding £1,199,000 to the SPA price to reducing it by £451,000. However, a consequence of the receivables being written down would have been to generate a tax shield, which would have added back £314,000. Bidco's case as to the net effect of these changes to the working capital adjustment therefore was a reduction in the Initial Consideration of £1,366,000.

178. Critical to Bidco's case on this point is the premise that, on a Warranty False basis, the target working capital stays the same, even though the actual locked box working capital must change to reflect the true position. However, the Warranty False analysis requires me to consider what a hypothetical reasonable willing buyer and hypothetical reasonable willing seller would have done, in the knowledge that Accounts and management accounts were incorrect and that the relevant debts should be written off.

179. The hypothetical reasonable willing buyer would still have had to form a view, and negotiate with the hypothetical reasonable willing seller, in relation to the target working capital. Like the negotiations that actually took place between Cairngorm/Bidco and the Sellers, these negotiations would have focused on the working capital that the business required to achieve the projected maintainable EBITDA. However, on this counterfactual scenario, both sides would have known about the write-off, (and, in the case of East Sussex that the maintainable EBITDA was somewhat lower than in the January 2019 management accounts). They therefore would have appreciated that MHL had in fact operated its business, and produced this

EBITDA, without the benefit of the working capital attributable to the debts now treated as having been written off.

180. Mr Thaper's evidence on this point was founded on his view that "the business would have required the same level of working capital for its obligations and operations" – meaning, the same as on the Warranty True basis. This cannot be right. The Warranty False counterfactual requires me to consider how objective parties would have assessed the business's use of and need for working capital, if they had been presented with accurate Accounts and management accounts. Their computations would not have been the same as on the Warranty True basis.

181. Accordingly, notwithstanding Mr Thaper's evidence as to what he thought he would have done, it seems to me inevitable that both parties' approach to target working capital would have been different. The exercise of assessing the quantum of this point therefore requires not only the actual locked box working capital to be reduced (on Bidco's case, by £1,651,000); it also requires the target working capital to be reduced by the same amount. The Sellers noted that, in the course of the SPA transaction, Cairngorm/Bidco were advised by PWC, who contemplated precisely this outcome in an email sent a few days before the SPA concluded.

182. It was agreed that, on this approach, there would be no material difference to the working capital adjustment. I therefore reject this element of Bidco's claim.

183. I should add that Mr Thaper suggested in evidence that, if the target working capital were to be reduced, then the multiple should change. I received no evidence as to how the multiple should change. In any case, Mr Thaper's evidence as to how the 6.8 multiple was selected does not provide any real support for the suggestion that a reduction in the working capital of MHL by £1,651,000 would make any difference, especially bearing in mind (as always) that this multiple was to be applied to MHCDC/the Millbrook companies as a group. The primary factor identified in Mr Thaper's second witness statement concerned the sector as a whole (providing healthcare to a growing population of service users). After that, he identified "the business' growth prospects, recession proofing, management skills, size of the business, and funding sources." This suggests that, as long as the aggregate working capital of all the Millbrook companies was adequate – i.e., sufficient for MHCDC to achieve the maintainable EBITDA, which the agreed target working capital should be, by definition – it would be unlikely to affect the multiple.

Other adjustments

184. Bidco also argued that there should be changes to some of the other adjustments to the SPA price namely (a) an adjustment of £37,000 for indirect expenses relating to the East Sussex Contract between July and September 2020; (b) cash losses of £249,000 in respect of Year 5 of the East Sussex Contract, and (c) a £96,000 reduction in the profit ticker.

185. In his written closing submissions Mr Woolgar accepted (Mr Grantham having accepted this in evidence) that these all hinged on whether the East Sussex Contract would have been expected to make losses in Year 5, by hypothetical parties or by an objective valuer who knew the true position. In oral submissions he put this slightly

differently, saying that this would depend on the state of knowledge at the relevant time and how that affected each of these three components.

186. A hypothetical reasonable willing buyer would not have been able to alter MHL's conduct of its business between the locked box date and the date of completion. However, such a party should have expected to do so after completion, i.e., from July 2019 and onwards through FY2020.

187. I therefore find that Bidco succeeds in relation to the profit ticker, but not in relation to the adjustments in respect of indirect East Sussex expenses between July and September 2020 or in relation to cash losses in respect of Year 5 of the East Sussex Contract. This increases the claim by £96,000.

188. Conversely, Mr Grantham accepted, and Bidco accepted in its opening submissions, that a reduction in the enterprise value would have resulted in an associated reduction in the management bonuses (which were among the deductions made from the enterprise value when arriving at the Initial Consideration). Mr Grantham's evidence supported a reduction in the enterprise value of £2,055,501, which he calculated would lead to a reduction in the management bonuses (and thus an uplift in the Initial Consideration) of £104,667. I have concluded that the reduction in the enterprise value would have been slightly smaller, meaning that the reduction in the management bonuses and the corresponding uplift in the Initial Consideration must also be slightly smaller. I received no evidence about this but my best estimate is £100,000.

189. This means that the net effect of all changes to the relevant adjustments is to reduce the claim by £4,000.

Mitigation

190. Earlier in this judgment, I have rejected the Sellers' contention that, on the Warranty False basis, the payment received by MHL under the East Sussex Settlement Agreement should be treated as contributing to maintainable EBITDA. I did so on the basis that the Settlement Agreement was not concluded until 14 January 2021 and so was something the parties could not have known about or anticipated at the date of the SPA.

191. However, the East Sussex Settlement Agreement does come into play as successful mitigation. Bidco accepted this, while noting that the £354,000 payment was reduced by an associated tax liability of £67,000. The net effect of the East Sussex Settlement Agreement therefore is to reduce Bidco's claim by £287,000.

The Sellers' positive case and counterclaim

192. The Sellers asserted that Bidco was in breach of its obligations under Schedule 5 of the SPA. Specifically, they said that Bidco's claim would not have arisen but for decisions made after the SPA, in particular the Settlement Agreement with East Sussex and the writing-off of invoice 16150 under the Somerset Contract, and they relied on Schedule 5 paragraph 4.1(3). They also asserted that, in relation to these matters, Bidco failed to notify the Sellers of a Third Party Claim in breach of Schedule 5 paragraph 6.1.

193. I reject these assertions, in the light of my earlier conclusion regarding the effect of the Variation Agreement on the East Sussex Contract and of Mr Lock's agreement with the

Somerset CCG in relation to invoice 16150. In the circumstances, Bidco and the new management of MHL did as well as they reasonably could. Notifying or involving the Sellers would have made no difference. In any event, I do not accept that a CCG's legitimate refusal to pay an invoice or debt that is not in fact payable constitutes a Third Party Claim within the meaning of Schedule 5 paragraph 6.1.

Schedule 5, paragraph 1.4

194. The Sellers also asserted a right to rely on Schedule 5 paragraph 1.4. This does not arise in circumstances where I have found that Bidco's claim exceeds the limits under that provision.

Outcome

195. I find that the Sellers were in breach of warranty in relation to the East Sussex Contract and the Somerset Contract.

196. The breach in relation to the East Sussex Contract affected the perceived maintainable EBITDA of MHL, and thus the maintainable EBITDA of MHCDC. This had an effect on the price paid under the SPA and has caused loss to Bidco.

197. Otherwise, the breaches meant that the sums given for debtors in the Accounts and management accounts were overstated. However, these incorrect entries had no effect on the SPA price and so have caused no loss.

198. The effect of the breach in relation to the East Sussex Contract was that the price was negotiated and agreed with both sides assessing the enterprise value of MHCDC on the basis of maintainable EBITDA of £6,610,000 (or £6,600,000, after rounding), whereas in fact the appropriate figure for maintainable EBITDA was £6,311,000.

199. Adopting an orthodox EBITDA x multiple approach to valuation, and on the basis that the appropriate multiple was 6.8, the breach in relation to the East Sussex Contract caused Bidco to pay a higher price than if there had been no breach. The difference in price was £2,000,000.

200. This loss is reduced by the net amount of £4,000 in respect of other adjustments. It is then reduced again by the successful mitigation achieved by way of the East Sussex Settlement Agreement, which itself gives rise to a net reduction of £287,000.

201. It follows that Bidco's claim succeeds in the amount of £1,709,000.