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Mediation – 8 March 2011

Sue Bruce - Opening Statement

final
as issued

In this Statement I will start with some personal background - and a brief overview of the project from the perspective of the City of Edinburgh. - I will then look at some of the history and disappointments. Whilst not wishing to dwell on these unduly - they are important because they will inform you of the rationale behind some of our thinking and of our lines. They also establish the starting point and direction of travel over the next few days. Both parties have an army of advisers here who have detailed knowledge and understanding of this project - and I do not intend to trespass into specialist areas or detailed history. But I will set out in terms that I - and you - will understand - what are the key areas for us, and for me as the decision-maker, if this mediation is to be successful, together with suggestions as to how we move forward if we can clear those key areas.

I took up the position of Chief Executive of City of Edinburgh Council on 1st January this year. Prior to this I was Chief Executive at Aberdeen City Council for two years and prior to that, Chief Executive at East

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Dunbartonshire Council for four and a half years. In our line of work every pound we spend is the taxpayers pound – so in this case – the delivery of the tram – every pound we collectively spend and argue over is the taxpayers pound – and in Edinburgh the taxpayer is suffering – that is the personal taxpayer and the business taxpayer – the local and the global business taxpayer. They all know about this impasse and they all know how much it's hurting them and Edinburgh – hurting the Capital City. In the public sector I have a strong and positive reputation as someone who can deliver a turnaround . I would be the first to recognize that turnaround cannot be achieved single handedly – it requires leadership, partnership, teamwork, honesty, integrity, and humility. My experience of Major Construction and Engineering projects is limited, particularly projects of this length and scale. Notwithstanding, my interest in construction started at an early age through the work of my father who worked in association with Liebherr, a long established and respected German company. I have had responsibility and accountability for delivering in the public sector school estate construction projects, housing developments, other public realm including roads, civic buildings, developments in association with waterways, and developments both new and restorative in heritage terms. I am not a construction professional but I do know about delivery in the public sector, spending public money and

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being publicly – and politically accountable. You will understand that from operating in the political environment a huge part of my role is to establish consensus and create satisfactory working arrangements so that policies and objectives can be delivered. My own personal style is optimistic, I prefer to focus on the art of the possible and my day job is underpinned by leadership, negotiation, mediation, support and challenge. This team and I , approach these next few days determined to reach an agreement which will deliver the tram system between the Airport and St Andrew Square, on terms that are fair and reasonable to the City and the wider stakeholders. I have made this approach clear not only to my team, but also in meetings with members of the consortium.

From the mediation Statements you have the core details of the Tram project. From my perspective, and that of my predecessors, this is an iconic project which heralds a significant leap in the development of City of Edinburgh. Its intention is not only to improve transport links in an environmentally responsible manner, but also it is a statement that Edinburgh is a World Class city with the latest facilities. Edinburgh is a Capital City - parts are a UNESCO World Heritage site - it is the seat of the Scottish Government. We have a world focus – with 32 Consular

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offices representing Governments the world over - right here in Edinburgh – all watching what is happening - or not happening – on the streets of the Capital. This City hosts more festivals than any other city – with a huge influx of tourists year round – all watching what is happening. This tram Project was due to be up and running by July this year, now we are looking at September 2013 for a truncated project, if this, in the Consortium's own words, "challenging", timetable is met.

Look at the streets - Look at the impact. Just look at one example – Haymarket Yards. As a City we have suffered from the global banking crisis. We need to maintain and attract financial institutions. Tesco are a global brand. We have the relatively new Tesco Bank operation at Haymarket virtually road blocked by the streetworks where the Consortium ceased work in October. We have the Convention of Scottish Local Authorities – who moved last week from the office at the Haymarket site to an office next door currently lined with Heras fencing – why did they move – because the rental offering was rock bottom – in an office that couldn't be let because of the stopped dead unfinished work at Haymarket. Every Political Leader and every local authority Chief Executive in Scotland passes that site every month and sees with disbelief what is happening. Whether they are businesses, council taxpayers, commuters or tourists, their frustration is translated into vocal

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criticism and opposition which is damaging the very future of this project, as well as the reputations of the council and each of the consortium members.

I have tried to explore how we have reached this current impasse, not only to learn lessons so that we do not repeat them going forward in Project Phoenix, but also to see whether there is a means of extricating ourselves from this paralysis. There are many factors, judgments, actions and inactions which coalesce to produce this entrenched type of situation. Its not easy to unravel the strands. tie and City of Edinburgh Council must - and do - take responsibility for their part in this. From my perspective there are three areas at the root of the problems:

- the Design was not as advanced as perhaps had been understood, and that - together with differing understandings of the meaning of 'design development' in Schedule Part 4 - has led to a developing hostility - with the increasing uncertainty about price and time;
- the management structure of the contract has not been right to meet the circumstances that have developed; and

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- on the contract terms we signed - perhaps we have been naïve - particularly on the operation of Change Orders - but also elsewhere.

It is only right to point out that on all these matters tie took advice - and so it is frustrating. But I do also take a step back and ask serious questions as to the conduct and behaviour of the consortium.

tie was after all signing up to a Design and Build contract, where the consortium took on the responsibility to complete an integrated design in accordance with the Employers Requirements, to complete the project by July 2011, for what was expressed to be a 'Firm and Fixed Price'. In such situations the Clients contract management and administration is relatively light touch, as the Contractor gets on and delivers the project.

What is more, the contract conditions were designed to reflect that - not the situation now advanced and operated by the Contractor.

There are, however, many areas for which tie are not responsible. The consortium comprises three international contractors who assured City of Edinburgh Council and tie that they had the experience, expertise and capacity to manage and deliver this project. I have asked myself a series of questions:

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- if they were so aware of the incomplete state of the design at Contract signature in May 2008, surely they should have applied the necessary resource and management expertise to ensure the earliest completion of this task? So why do we still await so much of the design? I am told that up to 15% is still incomplete. To take an example in the bundle - In Section 5A - 50% does not have

‘Issued for Construction’ drawings. The tie team will tell you of numerous occasions when they were guaranteed or promised a completed design, but it is still not done. Richard Walker even told Donald McGougan and Alastair MacLean on 3rd December 2010 that they had a “completed design, fully costed and timed” for Airport to Haymarket. (you can read that in the minutes). So where is it?

- a cameo example which I have asked about is Gogarburn Retaining Wall. Three years later there is still no approved design, such that the consortium now want to exclude this £4m element from their price for Phoenix. The history of failing to pick up this issue with BAA - failing to include the relevant flood assessments - or more precisely submitting an out of date one - and producing a design which exacerbated the potential for flooding - seems to me to be culpable.

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- Where is the evidence of examples of best value engineering - where savings have been made - as provided under the Contract?
What has been the benefit of having these experienced International contractors running this project? I am told there are virtually no examples of value engineering. Instead I hear of areas of change for which we have had to pay for 'over' engineering or 'conservative' engineering;
- What conclusions do I draw from the Princes Street experience?
Mike, this is the street of Edinburgh, possibly the best known street in the UK. The track that has gone in there is to a design that has not been approved - there are serious design issues - workmanship defects - and even a suggestion that the City is to pay to put it right. - Surely any commercial organization would put up its hands – even apologise and put this right at its own expense as soon as possible? Instead we are still waiting - and in the meantime we get a claim for £2.3m. What conclusions should I draw about **their** behaviour and attitude?
- In October 2010 they downed tools and walked away. I have seen the whole route from Airport to Haymarket at first hand - and it is beyond argument that there is work to be done - and which can be done. The Contract terms at Clause 6 talks of partnering and

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working together. Do they really want to partner? Is this what partnering looks like – I don't think so!

A key part of partnering is mutual respect and we can work towards that by maintaining confidentiality and by keeping ourselves out of the media unless by mutual agreement.

My other question is how are they - the consortium, - managing this project between themselves? From my own observation from meeting them there is no clarity - no lines of authority. We deal with three heads - not one. That is clear from the Phoenix proposal - but it permeates the whole contract structure and administration.

I want to touch on one further area where I think we probably got it wrong - but it cannot be ignored in the analysis of Project Phoenix. It is that in good faith a substantial up front payment of £45.2m was paid to Bilfinger Berger and Siemens - £22.6m each - and there was generous front loading of preliminaries. This means that they have been overpaid this far, for the work executed. This has not been recognized in their

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figures - and we guess is a partial explanation as to why the costs to complete are so high. And indeed from the Lord Dervaird adjudication decision of last week we now know that they have been overpaid even on those front loaded preliminaries.

As I explained at the outset - these questions represent our reality - and the issues that underlie them shape my approach and priorities in this mediation. We have set out our objectives for the mediation in both the Mediation Statement at para 15.2, and at the beginning of our Project Phoenix Statement. I won't repeat them - but I will underline that by the end of this process I must have a plan - process - date and price that takes us from Airport to St Andrew Square. In many senses, when reading page 3 of the Consortium's Mediation Statement encouragement can be drawn from the commonality of the objectives. That is a welcome starting point. There is a huge amount of work to be done to arrive at any agreement but I am keen that we start this unusual mediation off by resolving some fundamental issues - before addressing specific areas or topics. In other words I need to know that we - the principals - are on the same page before the specialists in design, programming, engineering and so on, start their work.

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Let me spell out what I perceive to be these fundamental litmus tests, as to whether a Phoenix deal can be negotiated.

First and foremost I need to be satisfied that there is a genuine intent on the part of the consortium to manage effectively and professionally this project from their side - with clear leadership and decision making. This involves acknowledging that they have got things wrong. In my meetings with them - albeit friendly on the face of it - this is something that they have not overtly faced up to. The new management needs to be collaborative - in a partnering sense - with the ambition to meet their customers best interests as well - instead of purely their own. The words and assurances so far given are not reflected in the Phoenix proposal, which falls well short of giving me the comfort I need to proceed with this. I need to see change.

Secondly - this was and is a Design and Build Contract where the responsibility to design and deliver the tram system in line with the Employers Requirements lies with the Consortium. The Consortium has

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had two and a half years to complete the design. The Phoenix proposal perpetuates - and in some cases worsens - the vulnerability of the City of Edinburgh Council - by fixing the price to the existing drawings. This is how we got to this point of impasse - of price uncertainty and no completion date - and we are not repeating it. The design and designer is in their hands - under their control. It cannot be right that we pay for their delays - errors and omissions. Project Phoenix must proceed on the basis that it is a proper Design and Build contract - without erosion of responsibilities. If it takes more time to complete the design and clear the outstanding issues then so be it - and we will play our part in supporting this to achieve the earliest possible date. Appendix 4 simply does not provide the certainty in scope, price or timescale to which we could sign up.

Thirdly – the financials. We are a very long way apart. Look - I cannot go into the detailed make up of the costs of a Project - but I can ask for headline financial data in a form that I can understand - interrogate and communicate to others. These are some of the answers - broadbrush – yes - but for me, they still paint a picture:

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- The original bid for this project was £11.2m per km. We signed up after a lot of last minute increases to £12.9m per km. The Phoenix proposal is now up to £33.4m per km. If we include the Appendix 4 exclusions it is near enough £40m per km. It would be by some way the most expensive tram system of its type anywhere in the world. Just by way of example, Manchester is in the region of £12m per km.
- Project Carlisle in September was £348m - with about £212m to go - now Project Phoenix is £384m - so about £250m to go. An increase of £38m - or 18% in 6 months.
- In the limited time we have had the Exclusions and 'Clarifications' you propose to Haymarket amount to £30m associated with physical works - with a similar amount to be added in for time and risk.
- In this Proposal the price for Siemens has gone up from £68m to £136.5m - (which price also has huge exclusions – so is not a final price) - a 100% increase despite virtually no change. Why a doubling - and no justification and breakdown? We have received back up sheets from Bilfinger Berger - and information

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- concerning CAF and SDS - but why only one summary sheet announcing a doubling of the price from Siemens? This is not acceptable and reinforces my point about management - conduct and behaviour.
- Even where we have agreed a Schedule of rates under the contract to value Extension of Time costs - Bilfinger Berger are now attempting through this Phoenix proposal to increase them by 75%, at a time when the indexes are flat.

Lets be absolutely clear that this is taxpayers money - and I will not get authority to sign up my Council or the Scottish Government on this basis.

There has to be accountability, and we all know that various bodies will crawl over these figures in the months and years to come - as they are doing even now. - So we need to see some realism in the form of financial explanations and transparency in these discussions. We need a breakdown of works costs, - distinct from historic claims. We need to see financial acknowledgement of the up front payments - of the inefficiencies and of intra consortium claims. I need to be satisfied that the pricing is fair and reasonable.

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So those are the litmus test items. - If I can see a genuine meeting of minds on these - actions not words - then we can move forward. Given the complexity and volume of what has to be agreed I propose - and this is up for debate - that we set up joint working teams to address the principal areas requiring agreement. - In general terms, I suggest that the teams identify what work needs to be done in order to reach agreement - the process - by whom - and by when. We will need to appoint a leader in each team responsible for delivering this process - and to escalate up the chain if there are blockages or problems. I will be at the top of the chain for us - I need to know who will be at the top of the chain for the consortium - and who speaks with full authority. I am not going to deal with three people collectively or individually.

The obvious workstreams - if we are to reach agreement - are:

1. Design and Risk Transfer. This is the most important working group - because these issues are at the heart of the divisions between the parties. Basically - the question to be answered is

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what steps need to be taken to complete the design and obtain all necessary consents and approvals to build from Airport to Haymarket - and then on-street to St Andrew Square? We need to understand - and have demonstrated to us - that there has been a value engineering exercise. We need a leader here who has a 'can do' approach - who will foster a team spirit - and sees these as engineering and approvals issues to be solved - rather than a battle-hardened veteran chipping away protecting their position. If this team does its job - then the risk transfer issues in Appendix 4 will largely evaporate.

2. Programme/Completion dates. - We want certainty on completion. Although the responsibility will rest under the Design and Build Contract with the consortium - we need to understand it more fully - that its achievable - and how it impacts upon the life of the City.

3. Financials/Pricing. - We want to reach agreement on the historic claims over these next few days. Otherwise it contaminates the

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process going forward - in terms of the pricing of the future works - and the need to build afresh the working relationships.

4. Management Structures. - We need to look again at how this project is managed - and I do mean on both sides. - We must get this right - and I will lead for us on this.

5. Terms and Conditions. - Both parties recognize the need to review certain contract terms - those relating to Change Orders and other Clauses. The lawyers will need to get together to draft some Heads of Terms to reflect what we have agreed at the end of these few days and what needs to be done over the coming weeks. They will also need to keep us right on Procurement law - warranties, bonds and so on.

That appears to us to be a sensible way forward. - When we get to that point - we can discuss them in detail - be more specific as to their respective briefs - and put names in there.

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In this Opening I have concentrated upon taking us forward on Project Phoenix - because that is where we are - and is the real purpose of next few days. - I am not going to posture on the alternatives - because we both understand the risks and damage of any other route - and like the consortium - if this cannot be negotiated at an acceptable level then we do not shrink or shy away from the consequences. - We are frustrated by what has happened - but are committed to this one last roll of the dice to see whether it is possible to restore sanity - before following the more draconian options.

Dr Keysberg (Jochen} , Dr Schnependahl (Joerg), and Snr Campos, (Antonio) - I am here - if necessary - until Saturday to hear your words - and witness your actions - to find out whether you really want to deliver this project for your customer - the City of Edinburgh - and to start to repair reputations so that we can - together - put this episode behind us.

Thank you.