

As adjusted on behalf of the Council on 11 May 2018

Edinburgh Tram Inquiry

Submissions on behalf of City Edinburgh Council

As revised following exchange of submissions

11 May 2018



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INTRODUCTION

1.1 These Submissions are made on behalf of City of Edinburgh Council (hereafter “the Council”) following the conclusion of evidence before the Edinburgh Tram Inquiry (“the Inquiry”). The principal purpose of the submissions for the Council is to seek to identify the causes of the difficulties which occurred in the course of the Edinburgh Tram Project (otherwise “the Project”) with particular reference to the terms of reference of the Inquiry. The Council's submissions have been adjusted following receipt of the submissions made on behalf of other core participants on 27 April 2018. Where a specific point in those submissions has not been addressed in the Council's adjustments, it should not be taken as agreement by the Council.

1.2 The aims and terms of reference of the Inquiry which were set out by the Scottish Ministers (“the terms of reference”) are as follows:

“The Inquiry aims to establish why the Edinburgh Trams project incurred delays, cost more than originally budgeted and through reductions in scope delivered significantly less than projected. The official terms of reference for the Inquiry are to:

- *Inquire into the delivery of the Edinburgh Trams project (“the project”), from proposals for the project emerging to its completion, including the procurement and contract preparation, its governance, project management and delivery structures, and oversight of the relevant contracts, in order to establish why the project incurred delays, cost considerably more than originally budgeted for and*

delivered significantly less than was projected through reductions in scope.

- *Examine the consequences of the failure to deliver the project in the time within the budget and to the extent projected.*
- *Review the circumstances surrounding the project as necessary, in order to report to the Scottish Ministers making recommendations as to how major tram and light rail infrastructure projects of a similar nature might avoid such failures in future.”*

1.3 These aims and terms of reference were amplified by a list of issues which it is not necessary to repeat but which have guided the approach to the gathering and examination of evidence for the purpose of addressing the terms of reference.

1.4 On behalf of the Council, it is submitted that the range of aspects arising from the terms of reference can be summarised in three questions:

1.4.1 What was the principal (or proximate) cause of why the Project cost substantially more than budgeted for, was subject to delay and did not result in all of the proposed route being constructed?

1.4.2 What were the consequences, financial and practical, of the fact that the Project has delivered only a part of the route proposed and in doing so required work to be carried out on the streets and elsewhere in Edinburgh for an additional period of a number of years?

- 1.4.3 What were the other factors which contributed to difficulties arising in the course of the Project which were not the principal cause of its difficulties but which nevertheless can provide indications of how such similar infrastructure projects might be carried out and managed better in the future?
- 1.5 For the Council, it is submitted that the evidence has demonstrated that the answers to each of these questions can be readily identified and that the report of the Inquiry will be able to address each in a way which satisfies the terms of reference.
- 1.6 The Council submits that the principal or proximate cause of "*why the project... cost considerably more than originally budgeted for*" (as quoted from the first point in the terms of reference) is to be found in the contract entered into on 14 May 2008 between TIE Limited (normally shortened to "TIE" in contemporaneous records but referred to hereafter as "TIE"), and the contractors Bilfinger Berger (UK) Limited ("BB") and Siemens plc ("Siemens") (and referred to together as "BBS"). This was described as the "Infraco Contract" and was referred to in various of its provisions as "this Agreement". The parties to the Infraco Contract were referred to as the "Parties". At the same time, TIE entered into the tram supply contract with Construcciones Y Auxiliar De Ferrocarriles SA ("CAF") for the provision of the tram vehicles required to operate the first part of the proposed Edinburgh Tram Network (or "ETN") and which contract has been referred to as the Tramco Contract. The consortium formed to complete the Project therefore comprised BB, Siemens and CAF (referred to together as "Infraco").

1.7 TIE was one of a number of arm's length companies set up by the Council and its origins, purposes and operations are discussed elsewhere in these Submissions. In particular, it was the meaning and effect of the Pricing Assumptions in Schedule part 4 (the "Pricing Assumptions") and the change mechanism in clause 80 (the "change mechanism") which brought about the situation where the works were not completed at the cost originally envisaged or within the expected time frame. In summary, the combination of these elements resulted in a situation where the Consortium was able to obtain substantially higher payments for work carried out and to delay or discontinue works until increased payments had been established. As a consequence, this is "*why the project incurred delays*" and, as a result of the increased costs, "*why the project... delivered significantly less than was projected through reductions in scope*" (as each of these is also quoted from the first point in the terms of reference). This is the subject of the first question set out above and it forms the most significant aspect of what the Inquiry is required to address by the terms of reference. It is the subject of chapter 1 of these Submissions and this chapter is intended to address the first point in the terms of reference.

1.8 The second aspect concerns the consequences of how the Project developed and this will address the second point in the terms of reference which is to "*Examine the consequences of the failure to deliver the project in the time within the budget and to the extent projected.*" This is the second question set out above and will be the

subject of chapter 2 of these Submissions which is intended to address the second point in the terms of reference.

1.9 The result is that consideration of the principal cause and its consequences can fulfil the first and second points in the terms of reference leaving the other subsidiary, but nevertheless important, aspects to be considered by reference to the third question identified above, and in respect of the third point in the terms of reference which is to *“Review the circumstances surrounding the project as necessary, in order to report to the Scottish Ministers making recommendations as to how major tram and light rail infrastructure projects of a similar nature might avoid such failures in future”*. This aspect will be the subject of chapter 3 of these submissions.

1.10 There is a final aspect which is significant to the Council. The Council itself wishes to learn from what occurred in the Project and to some extent, and with respect to whatever conclusions the Inquiry may reach, to set out its own views as a local authority and corporate body of where matters of this sort can be dealt with better in the future. This is significant not least because of the intention of the Council to continue with the procurement and construction of the remainder of Phase 1a of the Project to Leith and Newhaven and the possibility of future implementation of other parts of the Edinburgh Tram Network for which parliamentary powers were obtained which are seen by the Council to be in the best interests of Edinburgh and in the public interest irrespective of the undoubted failures and difficulties which occurred in the construction of the Project thus far and which are the direct subject

of this Inquiry. This aspect does, of course, relate to the third point in the terms of reference but it is intended to provide a wider perspective which to some extent will relate to the aspirations and policy options of the Council in the future rather than what has occurred in the past. This final aspect will be the subject of chapter 4 below.

- 1.11 In presenting these Submissions, the Council has noted the list of issues set out in the Note by Chairman for Core Participants concerning closing submissions dated 15 March 2018. The Council has addressed all of these issues in the course of Chapters 1, 2 and 3 of these Submissions.

CHAPTER 1

2. Introduction

2.1 This chapter begins with a consideration of the meaning and effect of the Pricing Assumptions and the change mechanism. It will then address how these came to be part of the Infraco Contract and how the operation of the Pricing Assumptions and the change mechanism caused the disruption to the Project and finally who bears responsibility for that.

Schedule part 4 – Pricing Assumptions

2.2 In order to address the significance of the Pricing Assumptions and their part in bringing about the increased costs and delays in the Project, this chapter begins with a legal and practical analysis of what is contained in the Schedule part 4 to the Infraco Contract (referred to in this chapter as “Schedule part 4”).

2.3 A number of defined expressions are provided in Section 2.0 of Schedule part 4 as follows:

“2.2 The “Base Case Assumptions” means the Base Date Design Information, the Base Tram Information, the Pricing Assumptions and the Specified Exclusions.”

“2.3 “The “Base Date Design Information” means the design information drawings issued to Infraco up to and including 25th November 2007 listed in Appendix H to this Schedule Part 4.”

“2.4 The “Base Tram Information” means information contained in Tram Suppliers technical response in relation to the Employers Requirements...”

“2.8 A “Notified Departure” is where now or at any time the facts and circumstances differ in any way from the Base Case Assumptions save to the extent caused by breach of contract by the Infraco, an Infraco Change or a Change in Law.”

“2.10 “Specified Exclusions” means items for which Infraco has made no allowance within the Construction Works Price as noted in Section 3.3 below.”

2.4 In relation to the definition of “Base Date Design Information” just quoted, it may be noted that Appendix H to Schedule part 4 did not contain any list of design information drawings. It merely states:

“All of the Drawings available to Infraco up to and including 25th November 2007.”

2.5 In other words, the definition of “Base Date Design Information” in paragraph 2.3 is essentially circular as Appendix H added nothing to the definition itself. This suggests that although the drafting of paragraph 2.3 implied that there would be a detailed Appendix H, those responsible for the list which was to be included simply failed to create that list. This suggests a degree of complacency at the least on the part of those responsible because in a substantial works contract, with a

supposedly fixed and firm price as discussed below, the obvious need for a definitive list of the drawings.

2.6 The expression the “Contract Price” is defined in paragraph 2.5 as comprising capital expenditure and revenue expenditure as set out in a table following. For present purposes, it is necessary only to note that amongst the specified items against which prices were stated, the first is the “Construction Works Price” which was given as a sum of £238,607,644.

2.7 The expression “Value Engineering” was used in Section 5.0 which provided in part:

“5.1 The parties have agreed Value Engineering opportunities/savings as Noted in Appendix C.”

2.8 It is not necessary to quote from Appendix C nor to repeat any of the other provisions of Section 5.0 which deal with the identification and implementation of Value Engineering opportunities.

2.9 A number of other expressions which are relevant are defined in the Schedule part 1 to the Infraco Contract by reference to clause 1.1. These include:

““Dispute Resolution Procedure” means the procedure set out in Schedule Part 9 (Dispute resolution Procedure)”.

““Employer’s Requirements” means the specifications set out in Schedule Part 2 (Employer’s Requirements) and any modifications

thereof or addition thereto as may be made from time to time in writing by tie or tie's Representative in accordance with this Agreement"

It is not necessary to quote the detailed provisions of the Dispute Resolution Procedure (or "DRP") provided in Schedule part 9 which may be summarised as providing an escalating mechanism for the resolving of disputes through the Chief Executive, adjudication and court proceedings. It is also not necessary to quote the provisions of Schedule part 2 as its title is self-explanatory and the detailed mechanisms are not material.

"“SDS Agreement” means the agreement between the SDS Provider and tie... set out in Schedule Part 22 (SDS Agreement) as may be amended by the SDS Novation Agreement entered into in accordance with Clause 11.1 or from time to time with the approval of tie in accordance with this Agreement"

"“SDS Novation Agreement” means the agreement entered into by the Infracore and the SDS Provider on the same date as the Agreement and included as Schedule Part 23".

Once again, it is not necessary to quote from the provisions of Schedule part 22 or Schedule part 23. The expression "SDS Services" was defined as those services to be provided by the "SDS Provider", which was in turn defined as Parsons Brinkerhoff Limited.

2.10 The following definitions in Schedule part 1 relate to changes:

“Mandatory tie Change” means any addition, modification, reduction or omission in respect of the Infraco Works instructed in accordance with Clause 80 (tie Changes) which this Agreement specifically states will be a Mandatory tie Change”.

“tie Notice of Change” means a notice service [sic] by tie pursuant to Clause 80 (tie Changes) setting out the matters referred to in Clause 80”.

- 2.11 The “Infraco Works” were defined as essentially the works required to complete and maintain the Project *“all in accordance with this Agreement and the Employer’s Requirements”*. In that context:

“Infraco Proposals” means the Infraco’s proposal for implementation of the of the Infraco Works included in Schedule Part 30 (Infraco Proposals) as amended from time to time in accordance with this Agreement”.

As before, it is not necessary to quote from Schedule part 30.

- 2.12 The detailed provisions relating to the Construction Works Price were given in section 3.0 of Schedule part 4. This provided insofar as relevant:

“3.1 The Construction Works Price is a lump sum, fixed and firm price for all elements of work required as specified in the Employer’s Requirements as Schedule Part 2 and the Infraco Proposals as Schedule Part 31 and is not subject to variation except in accordance with the provisions of this Agreement.”

2.13 Paragraph 3.2.1, which followed Section 3.1, will be referred to below. Section 3.3 specified a series of “*Specified Exclusions from the Construction Works Price*” which may be summarised as (a) certain utilities diversions, (b) public realm works in St Andrew Square, (c) ground conditions works that could not reasonably have been foreseen by reference to ground conditions reports previously provided, and (d) public realm works in Bernard Street. Section 3.3 concluded:

“3.3.1 *In the event that the Infraco is required to carry out any of the Specified Exclusions, this shall be a Notified Departure.*”

2.14 The Pricing Assumptions themselves were specified in Section 3.4. The critical parts of that paragraph stated:

“3.4 *Pricing Assumptions are:*

1 *The Design prepared by the SDS Provider will not (other than amendments arising from the normal development and completion of designs):*

1.1 *in terms of design principle, shape, form and/or specification be amended from the drawings forming the Base Date Design Information (this except in respect of Value Engineering identified in Appendices C or D to this Schedule Part 4);*

1.2 *be amended from the scope shown on the Base Date Design Information and Infraco Proposals as a consequence of any Third Party Agreement*

(except in connection with changes in respect of Provisional Sums identified in appendix B); and

1.3 be amended from the drawings forming the Base Date Design Information and Infraco Proposals as a consequence of the requirements of any Approval Body.

For the avoidance of doubt normal development and completion of designs means the evolution of design through the stages of preliminary to construction stage and excludes changes of design principle, shape and form and outline specification.

2 Design delivery by the SDS Provider has been aligned with the Infraco construction delivery programme as set out in Schedule Part 15 (Programme).

3 The Deliverables prepared by the SDS Provider prior to the date of this Agreement comply with the Infraco Proposals and the Employer's Requirements;

4 That the Design Delivery Programme as defined in the SDS Agreement is the same as the programme set out in the Schedule Part 15 (Programme).

5 ...”

2.15 The Pricing Assumptions just quoted were the first four of a total of forty-three Pricing Assumptions which it is not necessary to quote and which described a range of factors relating both to the infrastructure works to be carried out and the interests of third parties and to technical tram track and vehicle specifications. The first of the Pricing Assumptions quoted above was the most significant in contributing to the additional costs which were incurred in the carrying out of the Project (and it will be referred to hereafter as “Pricing Assumption No. 1”).

2.16 Following all of these Pricing Assumptions, it was stated:

“3.5 The Contract Price has been fixed on the basis of inter alia the Base Case Assumptions noted herein. If now or at any time the facts or circumstances differ in any way from the Base Case Assumptions (or any part of them) such Notified Departure will be deemed to be and Mandatory tie Change requiring a change to the Employer’s Requirements and/or the Infraco Proposals or otherwise requiring the Infraco to take account of the Notified Departure in the Contract Price and/or Programme in respect of which tie will be deemed to have issued a tie Notice of Change on the date that such Notified Departure is notified by wither Party to the other..”

2.17 Without proceeding further at this stage, it is submitted that the following conclusions may be drawn from what has been quoted and described by reference to the provisions of the Infraco Contract just

referred to. Although the Construction Works Price is stated in paragraph 3.1 to be “a lump sum, fixed and firm price for all elements of work required as specified in the Employer’s Requirements”, such a reference to a “fixed and firm price” is not consistent with all that succeeds it and may be said to have given a misleading impression as to the certainty of the Construction Works Price, and thus to the overall Contract Price, at the time that the Infraco Contract was being entered into. At its most basic, that so-called fixed and firm price was stated explicitly to depend upon “Pricing Assumptions” which by definition were uncertain and assumed for the purpose of ascertaining the Construction Works Price but no further. The word “*assumption*” is defined for present purposes as “*The taking of something for granted as the basis of argument or action*” and as “*That which is assumed or taken for granted; a supposition, postulate*”¹.

2.18 The assumptions made for the purposes of the Construction Works Price were just that. An “assumption” is something taken for granted; it is not established or agreed fact. If what were described as “assumptions” by Infraco at the time that the Infraco Contract was entered into had been described otherwise than assumptions but as facts which Infraco had agreed as the description of the works which it had agreed to carry out and upon which it had provided its price, and had described the price as a fixed price which it would charge for constructing the tram infrastructure in order to achieve all of the elements which were required, then the situation whereby changes in

¹ Oxford English Dictionary, Second Edition, Volume 1, page 723

the Pricing Assumptions could then result in Notified Departures could not have come about. One need hardly go further than that in order to identify why the price of the Project increased as much it did. Infraco did not agree to a fixed price based upon the works which it agreed to do; but rather it agreed to a price fixed upon the basis of a series of assumed but uncertain factors which were likely to change.

2.19 That this was the true nature and effect of the mechanism provided by way of the Pricing Assumptions is described in the Infraco Contract itself. Paragraph 3.2.1 of Part 4 stated:

“3.2.1 It is accepted by tie that certain Pricing Assumptions have been necessary and these are listed and described in Section 3.4 below. The Parties acknowledge that certain of these Pricing Assumptions may result in the notification of a Notified Departure immediately following execution of this Agreement. This arises as a consequence of the need to fix the Contract Price against developing factual background. In order to the Contract Price on the date of this Agreement certain Pricing Assumptions represent factual statements that the Parties acknowledge represent facts and circumstances that are not consistent with the actual facts and circumstances that apply. For the avoidance of doubt, the commercial intention of the Parties is that in such circumstances the Notified Departure mechanism will apply.”

- 2.20 It was the evidence of Mr Laing that paragraph 3.2.1 was included at his initiative because he wanted the logic of the pricing mechanism to be clearly understood and because he was not getting a response from TIE². This is referred to again later in dealing with the evidence.
- 2.21 An analysis of paragraph 3.2.1 demonstrates this precisely. TIE formally agreed that “*certain Pricing Assumptions represent factual statements that the Parties acknowledge represent facts and circumstances that are not consistent with the actual facts and circumstances that apply*”. In other words, the Infraco Contract, with TIE’s express agreement, provided for a Contract Price which was based upon, and was acknowledged to be based upon, statements of assumed fact which were known not to be actual facts which would apply to the construction of the Project. However one might characterise that situation, it meant that the factual basis assumed to be the case for the purpose of fixing the Contract Price was known at the time not to be correct. Furthermore, TIE acknowledged that the uncertainty of the assumptions meant that “*certain of these Pricing Assumptions*” could be the subject of one or more Notified Departures to be given immediately after the execution of the Infraco Contract. Paragraph 3.2.1 may be said to be an unusual term in a formal and substantial works contract but its meaning and effect are clear. The manner in which a “*fixed and firm price*” was agreed meant that that price, both the Construction Works Price, and thus the overall Contract Price, were not actually fixed or firm.

² Transcript of oral evidence of Ian Laing 23 November 2017 pages 43-46

2.22 This is the essence of why it is that the terms of the Infraco Contract led to substantially increased costs and, when taken along with clause 80, to delay and a shortened route.

Clause 80 – the change mechanism

2.23 The nature of the mechanism provided by the Pricing Assumptions, in particular Pricing Assumption No. 1, and the ways in which they would bring about a situation where the Consortium became entitled to payment of substantially greater sums was not by itself the reason why the Project took so long to compete. The critical effect was the fact that a Notified Departure resulted in a TIE Change and in turn resulted in the application of clause 80 of the Infraco Contract by virtue of clause 79.1.1.

2.24 Clause 80 is entitled “TIE CHANGES” and insofar as relevant provided as follows:

“80.1 Unless expressly stated in this Agreement or as may otherwise be agreed by the Parties, tie Changes should be dealt with in accordance with this Clause 80 (tie Changes). If tie requires a tie Change, it must serve a tie Notice of Change on the Infraco.

80.2 A tie Notice of Change shall:

80.2.1 set out the proposed tie Change in sufficient detail to enable the Infraco to and calculate provide the Estimate in accordance with clause 80.4 below;

80.2.2 subject to Clause 80.3, require the Infraco to provide tie within 18 Business Days of receipt of the tie Notice of Change with an Estimate...

80.4 As soon as reasonably practicable, and in any event within 18 Business Days after having received a tie Notice of Change (or such longer period as may have been agreed by the parties, pursuant to Clause 80.3...) the Infraco shall deliver to tie the Estimate..."

"80.9 As soon as reasonably practicable after tie receives the Estimate, the parties shall discuss and agree the issues set out in the Estimate...

80.10 Subject to Clause 80.15, if the Parties cannot agree on the contents of the Estimate, then either Party may refer the estimate for determination in accordance with the Dispute Resolution Procedure."

"80.13 Subject to Clause 80.15, as soon as reasonably practicable after the contents of the Estimate have been agreed tie may:

80.13.1 issue a tie Change Order to Infraco; or

80.13.2 except where the Estimate relates to a Mandatory tie Change, withdraw the tie Notice of Change...

Subject to Clause 80.15, for the avoidance of doubt, Infraco shall not commence work in respect of a tie Change until

instructed through receipt of a tie Change Order unless otherwise directed by tie.”

“80.15 Where an Estimate has been referred to the Dispute Resolution Procedure for determination, but is deemed by tie (acting reasonably) that the proposed tie Change is urgent and/or has a potential significant impact on the Programme, subject to Infraco’s right to refuse to carry out a tie Change under Clause 80.12 and save where such proposed tie Change includes work by the SDS provider and where the valuation of such work is not agreed, tie may instruct Infraco to carry out the proposed tie Change prior to the determination or agreement of the Estimate by issuing a tie Change Order to that effect.

80.16 Where tie issues a tie Change Order under clause 80.15, Infraco shall implement the tie Change, and prior to determination of the Estimate shall be entitled to claim info goes demonstrate costs in implementing the tie Change...”

2.25 Reference may also be made to clause 34 of the Infraco Contract which provides in part:

“34.1 The Infraco shall construct and complete the Infraco Works in strict accordance with this Agreement and shall comply with and adhere strictly to tie and tie’s Representative’s instructions on any matter connected therewith (whether mentioned in this Agreement or not) provided that such instructions are given in

accordance with the terms of this Agreement and will not cause Infraco to be in breach of this Agreement...

The expression “*tie’s Representative*” is self-explanatory for present purposes. Clause 34.3 provides a mechanism which is to operate where Infraco incurs delay as a result of such an instruction. Such a situation is deemed to be a “Compensation Event” under clause 65 which once again it is not necessary to address for present purposes.

The relationship between the Pricing Assumptions and the change mechanism

2.26 The critical relationship between Pricing Assumption No. 1 and the change mechanism depended upon the qualification which was stated in that Pricing Assumption No. 1. That may be identified by repeating the following from Pricing Assumption No. 1:

“The Design prepared by the SDS Provider will not (other than amendments arising from the normal development and completion of designs)... be amended from... the Base Date Design Information...”

2.27 The precise terms of the individual elements in paragraphs 1.1 to 1.3 are not material as each incorporates the wording just quoted. The qualification in parenthesis is reflected in the final words of Pricing Assumption No. 1:

“For the avoidance of doubt normal development and completion of designs means the evolution of design through the stages of preliminary

to construction stage and excludes changes of design principle, shape and form and outline specification.”

2.28 Whatever uncertainties may have existed in individual circumstances as the Project proceeded (and certain of these were the subject of the adjudications to be discussed below), the critical element in Pricing Assumption No. 1 was there was scope for dispute in each individual circumstance as to whether an alteration to what had been designed by the SDS Provider and which was included as part of the Base Date Design Information (or “BDDI”) represented no more than “*normal development and completion of designs*”, that is to say “*the evolution of design through the stages of preliminary to construction stage*”, or alternatively represented an amendment of the BDDI because it amounted to a “*change... of design principle, shape and form and outline specification*”. In the case of the former, the price based on Pricing Assumption No. 1 would remain; in the case of the latter, Pricing Assumption No. 1 would not apply.

2.29 At the stage of entering into the Infraco Contract, the outcome of any particular dispute on the application of Pricing Assumption No. 1 was not the issue. What was important at that time was that the Construction Works Price, and thus the Contract Price, was dependent upon each and all of the designs completed as part of the BDDI being developed into the final designs which were Issued for Construction (or “IFC”) without there being any change which went beyond “*the evolution of design through the stages of preliminary to construction stage*” because

it amounted to a “*change... of design principle, shape and form and outline specification*”.

2.30 The critical relationship between the Pricing Assumptions, in particular Pricing Assumption No 1, in Schedule part 4, and the change mechanism in clause 80, is generally acknowledged in the submissions initially exchanged for most Core Participants. It is thus not an issue about which there is any significant dispute. In the submissions for Siemens at paragraph 75 and 76, reference is made to a process such as the change mechanism in clause 80 and it is stated that:

"This process was wholly appropriate for a client seeking to control changes to price and programme. However, what tie seemed not to appreciate was the operation of these provisions where changes arose as a result of the deeming provisions in Schedule Part 4 rather than as a client decision to modify the Infraco Works..."

2.31 This observation appears to the Council to be a reasonable one. Where the situation was that TIE wished under the Infraco Contract deliberately to make a change between BDDI and IFC then the result would properly be a TIE Change and it was logical that Infraco should have some protection as to increased costs as provided by the change mechanism. But what the relationship between Schedule part 4 and clause 80 did was to bring into operation the change mechanism every time Infraco claimed that there had been a Notified Departure as a result of a particular IFC design.

- 2.32 At the very least, the consequences of the relationship between Schedule part 4 and clause 80 were a matter of uncertainty at the point when the Infraco Contract was entered into and the nature of that uncertainty meant that the Construction Works Price would be subject to alteration each and every time an IFC design or drawing was provided which went beyond the scope of normal evolution of design. At the stage of entering into the Infraco Contract in May 2008, it was known that the design development had moved from what was Version 26 (“v26”) at BDDI on 25 November 2007, to Version 31 (“v31”), and that the design was still not complete. This was, or ought to have been, an obvious possibility to those who were required to advise on the terms of the Infraco Contract before it was entered into with the clear consequence that the sum which was stated to be the Construction Works Price would be subject to increase in a way which was not predictable in either amount or the number of times that it would occur.
- 2.33 Aside from that, the nature of how Pricing Assumption No. 1 would operate would by itself give rise to disputes about whether a particular IFC design was or was not consistent with Pricing Assumption No. 1, and such disputes would by themselves have consequences whatever the ultimate result in an individual case.
- 2.34 These considerations would give rise at the least to uncertainties about the nature of the Construction Works Price and, depending upon the facts and circumstances in each individual case, to the need to identify a price for works which were carried out and were beyond what was assumed in Pricing Assumption No. 1. This leads to a consideration of

what would take place where there was a dispute about the application of Pricing Assumption No. 1 and that was the subject of the change mechanism.

- 2.35 In a situation where a particular IFC design or drawing differed from what was assumed in Pricing Assumption No. 1, that would amount to a departure from the Base Case Assumptions, as defined in Schedule part 4, paragraph 2.2, either because it differed from the BDDI or because it differed from the Pricing Assumptions, or both. In that event, the difference amounted to a Notified Departure, as defined in paragraph 2.8. The resulting Notified Departure was deemed to be a Mandatory TIE Change by Section 3.5, and TIE was deemed to have issued a TIE Notice of Change. By the definition in Schedule part 1, a TIE Notice of Change was a notice served by TIE pursuant to clause 80. The provisions of clause 80 therefore became engaged each and every time an IFC or other design was issued which went beyond what was described in Pricing Assumption No. 1 as “*normal development and completion of designs*”. Just as importantly, it became engaged every time Infraco alleged that an IFC design went beyond what was described in Pricing Assumption No. 1.

The adjudications

- 2.36 It is not intended to deal at length with the nature and result of the various adjudications which took place in the course of the Project. This is not least because they comprised *ex post facto* proceedings in which the meaning and effect of the critical parts of the Infraco Contract were

determined. What is more critical is what was done at the time when the Infraco Contract was entered into and which lead, once the Parties were contractually bound, to the consequences which arose from the contractual rights and obligations which had been agreed. In other words, the critical issue is how TIE came to be bound by these rights and obligations, in a situation where it ought to have been aware that the terms of the Pricing Assumptions and the change mechanism had the potential to lead to dispute, and to increased costs and delay.

2.37 Furthermore, what has just been said about the meaning and effect of Pricing Assumption No. 1 along with clause 80 does not depend upon the ultimate decision in any adjudication. What has just been said depends upon a consideration of the particular terms and conditions of the Infraco Contract at the time that the decision was made to enter into it and what ought to have been foreseen by a reasonable adviser who had a duty to advise upon it. As already said, the problem was not just that Pricing Assumption No. 1 provided a mechanism by which in due course Infraco would become entitled to increased charges for work which had departed sufficiently from the BDDI designs but also that Pricing Assumption No. 1 inevitably meant that there would be likely to be disputes as the Project continued as to whether a particular IFC design or drawing did or did not represent a departure from the Base Case Assumptions and the likelihood of such disputes by itself gave rise to an uncertainty because of the potential to increase the Construction Works Price. In addition, the likelihood was that such

disputes would give rise to delay, in particular having regard to the mechanism provided in clause 80.

2.38 The provisions of clause 80, and its relationship with the provisions of Schedule part 4, were the subject of certain of these adjudications. Specifically, there was controversy in relation to the question of whether, on the wording of clause 80.13 of the Infraco Contract, Infraco was obliged to proceed with work in circumstances where there was a dispute about the existence of a Notified Departure. This controversy was particularly acute in circumstances where the terms of Pricing Assumption No. 1 led to a number of disputes in relation to whether specific changes to, or development of, the design constituted a Notified Departure.

2.39 The earliest adjudications in which the operation of Pricing Assumption No. 1 was in issue were two Decisions of John Hunter dated 16 November 2009 (“the first Hunter Decisions”) concerning Carrick Knowe Bridge and Gogarburn Bridge. Although these Decisions are not identical in form, they were nevertheless addressing the same arguments and may be considered together. It is also not intended to set out these or the other relevant adjudication decisions at any length but the following may be noted. As well as having to construe the Pricing Assumptions, the Adjudicator responded to an argument for TIE that the obligation of Infraco was “*simply to meet the Employer’s Requirements*”: paragraph 7.13. The first two Hunter Decisions said as follows:

“7.17 My finding is that Schedule Part 4 was included because the design was incomplete and therefore some unknowns existed that were beyond the capabilities of [Infraco] to include within their price. In other words how the BDDI was to be developed to IFC could be known in respect of certain factors but not all factors and the unknown or insufficiently developed elements were captured by the provision of the wording Schedule Part 4.

7.18 The parties are at one that the risk for normal development to completion of design lies with [Infraco]. This is other than where that risk has been transferred to [TIE] under one or more of the pricing assumptions set out in Schedule Part 4 pricing.

7.19 My finding is that whilst the occurrence of a Notified Departure is a question of fact I concur with [TIE] that the onus is on [Infraco] to demonstrate that which they claim falls within the exceptions set out in the contract

7.20 My finding is that this position is best summed up as follows. The risk which ought properly to be transferred to [TIE] is where development and completion of designs is outside of the normal course of development of the detail shown in the initial design ie the Base Date information, into the detail needed to construct the works as described all to meet the Employer’s Requirements. I would go one step further and clarify that the Employer’s Requirements have to be sufficiently well developed within the BDDI procedure as a baseline for proceeding in such a manner. I

include this further step as it is clear to me that the Employer's Requirements have in terms of the price for the works been limited by the BDDI and the Schedule Part 4 agreement in respect of the agreed price. I find that to arrive at any other conclusion would, in my view, make Schedule Part 4 meaningless.

7.21 My finding is that the matters that will become Notified Departures are matters that fall outwith normal design development that could be construed from the information available to the Contractor contained within the BDDI. These matters may have been alluded to in the Employer's Requirements as an obligation but because of the lack of complete design had not been sufficiently developed in terms of specification to become part of the price."

2.40 The general thrust of the first Hunter Decisions was that the price was not fixed, not least by reference to the Employer's Requirements. Where a detailed IFC design was outside of the normal course of development of the detail shown in the BDDI, then a Notified Departure was the result. These Decisions were confirmation that in general terms the Construction Works Price would be subject to change where the IFC design went beyond what was provided in the BDDI. In other words, the first Hunter Decisions confirmed at the very outset of the DRP process that the price was not firm or fixed.

2.41 The next adjudication Decision was that of Alan Wilson dated 4 January 2010 (“the Wilson Decision”) which concerned the Russell Road retaining Wall Two in respect of which IFC drawings had been issued. Infraco had issued to TIE an Infraco Notice of TIE Change (“INTC”) no 146. The IFC drawings showed a substantially altered foundation design from “L” shaped gravity structures to almost entirely cantilever walls on piles. The Adjudicator considered the effect of Pricing Assumption No. 1 in section 3.4 of Schedule part 4 (and in doing so, he referred to the individual paragraphs as 3.4.1.1 etc).

2.42 The Wilson Decision is a lengthy one. At paragraph 100, and in construing Pricing Assumption No. 1, the Adjudicator concluded that *“something has gone wrong with the language of Section 3.4.1.1 as, on the face of it, on a literal reading some part must be redundant to give it meaning.”* At paragraph 139, the Adjudicator found that INTC No 146 *“is restricted to notification of a Change arising under Section 3.4.1.1”*. At paragraph 142, it is recorded that TIE accepted that it had *“issued a [tie] Change Order under the Mandatory tie Change provisions which, by definition, must be one of the Notified Departures in Schedule Part 4”* although TIE denied that the assumption in paragraph 1.1 of Pricing Assumption No. 1 applied and it reserved its position on paragraph 1.3. In The Adjudicator found (in substance) that the change to the foundations was outwith paragraph 1.1 of Pricing Assumption No. 1 and in doing so he said as follows:

“146 The Change between the BDDI and IFC is significant. Adopting applying the definitions above

- i) *'Design prepared by the SDS Provider will undergo the normal development and completion of design and will not in terms of design principle, shape, form and/or specification be amended from the drawings forming the BDDI (except in relation to Value Engineering),'*
- ii) *'Normal development and completion of design means those changes that an experienced contractor and his engineer can expect in providing full construction information.'*

I do not consider that the Change from an L shaped wall to a piled cantilever wall is what an experienced contractor would expect in providing full construction information. It is clearly an amendment of what is shown in the BDDI drawings. On this analysis, it follows that the Change is outwith Pricing Assumption Section 3.4.1.1

147. In the alternative, applying the definitions of the exclusionary words adopted above

- i) *The design principle has changed fundamentally from an L shaped gravity wall to cantilever wall on piled footings*
- ii) *The shape, being the total effect produced by the outline has changed from L shaped to vertical*
- iii) *The form, being the external appearance has changed, including the below ground 'appearance'*

iv) The specification, being the nature and quality of the work has changed insofar as piles are added

On this analysis also, it follows that the Change is outwith Pricing Assumption Section 3.4.1.1.

148 By definition at Section 2.8 a Notified Departure is qualified 'save to the extent caused by a breach of contract by the Infraco, an Infraco Change or a Change in law, Changing.' No evidence has been advanced to suggest that any of these savings apply and I conclude that they do not.

Conclusion

149 I conclude that the Change to the Foundations being outwith Pricing Assumption Section 3.4.1.1 and not being the subject of any of the saving provisions is a Notified Departure properly notified by INTC no 146..."

2.43 At this point, it may be observed that as a result of the first Hunter Decisions and the Wilson Decision, it was or ought to have been apparent by January 2010 that, as a consequence of the mechanism contained in Pricing Assumption No. 1, the Construction Works Price was not firm or fixed and that the approach of TIE to the construction of the Pricing Assumptions was not being supported by Adjudicators.

2.44 The next adjudication Decision in sequence which is relevant was again by John Hunter dated 18 May 2010 ("the second Hunter Decision") which related to Tower Place Bridge. The second Hunter Decision

concerned the Pricing Assumption in paragraph 19 of Section 3.4 of Schedule part 4 and both TIE and Infraco accepted that a Notified Departure had occurred. The issue was therefore one of valuation. The dispute turned as a matter of fact on exactly what drawings had been available to Infraco at BDDI in particular by reference to a “data room” which had been set up and to which Infraco had access electronically.

2.45 At paragraphs 7.17 and 7.19 of the second Hunter Decision, the Adjudicator found that he was “*unable to establish that the BDDI drawings upon which [TIE] relies were available to [Infraco]*” on a particular date prior to 25 November 2007 for reasons which he then set out. The Adjudicator also commented:

“7.18 Further, at the hearing with the parties I was able to establish that both parties were rather unclear as to why appendix H had not been populated with a definitive list of drawings or a reference to the data room.”

2.46 The next adjudication Decision is that of T Gordon Coutts QC dated 24 May 2010 (“the Coutts Decision”) which concerned “Section 7A Track Drainage”. In the Coutts Decision, the Adjudicator found that a Notified Departure had occurred and in doing so he considered an argument for TIE which was that:

“... if the work had not been specified in the BDDI drawings then possession of information for other areas of Section 7 could not constitute or form the basis of an amendment of the design. A thing cannot be amended it was said, “if it not first showing” and, further, that

an amendment does not and cannot include additions to or additional detail within a drawing or any development of it.”

2.47 The Adjudicator found in favour of Infracore and he rejected that argument for TIE “so far as it is founded upon construing the word “amend” in Pricing Assumption 3.4.1.1.” He also commented on the situation where drawings or schedules were missing (as he found to be the case in the particular circumstances) and said:

“It would appear to me that it was to cope with such problems that parties adopted a Notified Departure mechanism to which para 3.2.1 refers and which stated that the commercial intention of the parties was that in the circumstances outlined in 3.2.2 the Notified Departure Mechanism would apply.”

2.48 There is also an adjudication Decision by Bryan G Porter dated 22 September 2010 in connection with Depot Access Bridge 32. In that Decision, the Adjudicator found that Notified Departures had occurred in respect of permanent and temporary works and he determined valuations for these. It is not necessary to consider the details of that Decision.

2.49 These are the adjudication Decisions which have a direct bearing on the meaning and effect of the Pricing Assumptions in Section 3.4, in particular Pricing Assumption No. 1. There are also Decisions which related to the meaning and effect of clause 80.

2.50 The principal of those was the Decision of Lord Dervaird dated 7 August 2010 (“the Dervaird Decision”) in which the issue was whether or not Infraco was obliged to comply with an instruction by TIE contained in a letter dated 19 March 2010 and which required the carrying out of works identified in an Infraco Notice of TIE Change which was INTC No 109. The Adjudicator set out the background and referred in particular to the provisions of clause 80 and to the obligation of Infraco in terms of clause 34.1 and 34.3 to comply with instructions given by TIE “*provided that such instructions are given in accordance with the terms of this Agreement*”. Having addressed the particular provisions of clause 80 in some detail, the Dervaird Decision continued:

“15. Against that background, the issue for determination in this adjudication is whether the letter from tie to Infraco dated 19 March 2010 constitutes an instruction which obliged Infraco to carry out the works referred to in INTC No 109, it being common ground that at the time that letter was issued there was no agreed Estimate for these works. It is also common ground that the subject matter of the works constituted a Notified Departure, defined as a situation where the facts and circumstances differ in any way from the Base Case Assumptions. Such Notified Departure is deemed to be a Mandatory tie Change: and tie is bound to pay to Infraco where appropriate in respect of an Estimate made by Infraco in respect of the tie Notice of Change that tie is required by Clause 80.1 to serve on Infraco.”

2.51 The critical issue was therefore whether, in a situation where an Estimate had been provided but had not been agreed or its value determined, TIE could oblige Infraco to carry out the works in question by the issuing of an instruction under clause 80.13. At paragraph 21 of the Dervaird Decision, the Adjudicator listed the characteristics of clause 80.13 and in particular he noted that “*The Clause expressly empowers tie to act after the contents of the Estimate have been agreed*” but that “*The final sentence “for the avoidance of doubt” provides that Infraco shall not commence work in respect of a tie Change until instructed through receipt of a tie Change Order...*” The Dervaird Decision then continued:

“22. *It may be argued that this is an unduly restrictive view in that it is dependent upon Infraco having put forward an Estimate Only if that is agreed is tie able to instruct work to commence in the ordinary case, with the exception of Clause 80.15 cases of urgency. It is, however to be observed in either case the Parties are protected in respect of financial consequences. In the case of the agreed Estimate the matter either goes ahead (80.13.1) or tie withdraws any Notice of Change which is not a Mandatory tie Change (18.13.2). In the latter case tie will in any event be deemed to have issued a tie Change Order, but again only after a lapse of time after the contents of the Estimate are agreed or determined. Matters are different under Clause 80.15 but (a) that is for tie to take the risk of financial uncertainty where it considers the matter urgent (b) it must act reasonably in taking that*

approach and (c) Infraco has some protection in its right of refusal under Clause 80.12.

23. *Clause 80.16 is of relevance in this context. It provides that where tie issues a tie Change Order under 80.15, ie before an Estimate, referred to the Dispute Resolution Procedure for determination, has yet been determined, Infraco shall implement the tie Change, and shall be entitled, prior to any such determination, to claim its demonstrable costs in implementing the tie Changes calculated in accordance with Clause 80.6. Infraco is thus protected in respect of the financial consequences of having to carry out work under 80.15. There is no such provision in respect of Clause 80.13 and that is appropriate given that 80.13 is only operable after an Estimate has been agreed.*

24. *The above analysis leads to the conclusion that as an Estimate had not been agreed in respect of the relevant works at the time that the letter dated 19 March 2010 was written by tie, tie was not empowered under Clause 80.13 to issue an instruction in respect of those works. The letter bears the heading "Clause 80.13 Instruction." Accordingly insofar as it bears to proceed under Clause 80.13 it is not a valid instruction and Infraco was not under any obligation to comply therewith."*

2.52 It may also be noted that the Wilson Decision addressed the obligations arising under clause 80 and in particular a complaint by TIE that Infraco had failed to provide a timely Estimate which provided all of the

information which was necessary and a dispute as to whether TIE had agreed to accept a “*part Estimate*”. This issue is not material for present purposes but it may be noted that at paragraph 118 of the Wilson Decision the Adjudicator found that the Infraco Contract did “*not provide a quality standard for Estimates*” and that TIE could not reject an Estimate “*simply because it says it is poorly executed.*” Clause 80.10 provided that if the Parties could not agree on an Estimate it might be referred to the Dispute Resolution Procedure.

2.53 The effect of clause 80 was also referred to in a Decision by Robert Howie QC dated 26 July 2010 but that concerned a claim by Infraco for extensions of time as a result of delays to the MUDFA Works and is not material.

2.54 As has been said above, the significance of these adjudication decisions is that they confirm what ought to have been apparent in respect of Pricing Assumption No 1 and its relationship with the change mechanism at the time that the Infraco Contract was entered into. Not only did these give rise to potential dispute on every occasion that an IFC design was issued leading to a claim by Infraco it departed too far from the BDDI design, but it also gave rise to disruption and delay in a situation where an Estimate had neither been provided nor agreed. In a situation where a Notified Departure had occurred, the Dervaird Decision determined that TIE could not issue an instruction requiring the work to be recommenced in terms of clause 80.13 and that is what gave Infraco the ultimate ability to cease to carry out works pending the determination of outstanding disputes.

2.55 In those circumstances, Infraco took the view that the wording of clauses 80.13 and 80.15 meant that TIE would only be entitled to instruct Infraco to proceed where either a TIE Change Order had been issued or an Estimate in relation to a Notified Departure had been referred to the Dispute Resolution Procedure, but neither of those would apply where TIE disputed that a Notified Departure had occurred. No decision was ever issued on this point (and the matter remained in dispute at the point at which the Settlement Agreement was concluded between TIE and Infraco). It was never determined whether TIE could issue some other form of instruction requiring Infraco to resume work on a particular aspect in a situation where the existence of the Notified Departure was in dispute.

2.56 The last point to note is that the meaning and effect of Pricing Assumption No. 1 and the change mechanism was never the subject of determination by a Court. The circumstances of this were dealt with in the evidence but it is submitted that what was provided in the various adjudication decisions was sufficient determination to justify an acceptance that in the event of a Notified Departure, or a claimed Notified Departure, Infraco could delay the carrying out of the relevant works until the Dispute Resolution Procedure had determined that issue. That, again is a result of what was in Pricing Assumption No. 1 and the change mechanism in the Infraco Contract.

3. **Legal advice: DLA**

Summary

- 3.1 TIE and the Council were joint clients of DLA; DLA owed a duty of care to the Council. There was a commonality of interest between TIE and the Council.
- 3.2 Senior officers at the Council took the decision, after careful consideration of the issues, to rely solely on the advice of DLA in relation to, amongst other things, the Infraco Contract. DLA was recognised as a major international law firm with relevant and specialist expertise, and had an existing knowledge of the Project.
- 3.3 Because DLA was engaged to provide advice to the Council, the Council's internal legal team did not carry out a review of the Infraco Contract, including the terms of Schedule part 4.
- 3.4 The Council relied on the advice provided to it by DLA in relation to, amongst other things, the risk allocation in the Infraco Contract. DLA was well aware of this reliance.
- 3.5 A significant aspect of the risk allocation in the Infraco Contract was Schedule part 4, and DLA was involved in the development and finalisation of Schedule part 4. The terms of the Wiesbaden Agreement were not non-negotiable in the context of agreeing Schedule part 4.
- 3.6 DLA gave written advice to the Council in relation to, amongst other things, the risk allocation in the Infraco Contract in a series of letters

issued between December 2007 and May 2008. That advice in those letters is not complete and/or accurate, in that it does not refer to the risk allocation created by Schedule part 4, and in particular Pricing Assumption No. 1. The letters do not take account of the evolving position in relation to risk allocation in Schedule part 4 as it changed between December 2007 and May 2008.

- 3.7 In particular, by the time that DLA issued their letter of 12 May 2008 immediately prior to contract close, the terms of Pricing Assumption No. 1 were such that the risk of changes from BDDI to IFC sat with TIE (and therefore the Council), rendering the concept of "*normal development and completion of design*" which TIE considered to be Infraco's responsibility all but empty of meaning.
- 3.8 Andrew Fitchie gave evidence that, although he understood them, he gave no advice whatsoever to the Council in respect of the implications of Schedule part 4 or Pricing Assumption No.1. DLA's advice letters to the Council were not qualified by any reference to oral advice said to have been given to TIE.
- 3.9 Andrew Fitchie also gave evidence that no advice was given to TIE in writing in this respect, but that it was given orally to officers of TIE. The evidence of TIE officers was that no such oral advice was given. Mr Fitchie accepted that in the course of the dispute resolution proceedings concerning the meaning of Pricing Assumption No. 1, he made no reference to having given advice prior to contract close of that meaning.

- 3.10 Mr Fitchie gave evidence that the terms of the DLA Report on Infraco Contract Suite (both a draft in March 2008, and the final document in May 2008) were inaccurate in respect of risk transfer, but he did not advise the Council of this.
- 3.11 Mr Fitchie also gave evidence in relation to the Close Report that, knowing that it contained inaccuracies and was not true, he allowed it to be provided to the Council in conjunction with DLA's letter of 12 May 2008.
- 3.12 The evidence of the TIE witnesses was that their understanding prior to contract formation was that the risk of normal design development sat with Infraco. They could not recall any advice from Andrew Fitchie specifically, or DLA generally, to the contrary; they did not, therefore appreciate the risks inherent in Pricing Assumption No. 1. Had that advice been given, Andrew Fitchie would have been asked to present it to the Tram Project Board and the procurement process would in all likelihood have been stopped. The terms of the Close Report therefore reflected the understanding of the relevant officers of TIE.
- 3.13 Witnesses on behalf of the Council gave evidence that their understanding at contract close was that the risk associated with design development lay with Infraco. Had advice been given by DLA that this was not the case, it would have been raised at a senior level in the Council.
- 3.14 The consistent evidence of TIE officers was that they had no recollection of being informed by Andrew Fitchie of a conversation that

is said to have taken place with Richard Walker of BB in December 2007 of an additional £80m in the Infraco price. Similarly, Willie Gallagher gave evidence that he had not had a direct discussion with Richard Walker in this respect.

DLA's duty and standard of care

3.15 DLA was appointed by TIE in terms of a letter of appointment dated 25 November 2002³ and accepted by DLA on 29 November 2002⁴. The appointment was subject to TIE's General and Financial Conditions of Appointment⁵, which contained the following at paragraph G3.1(a):

"On or as soon as is reasonably possible after the Start Date, the Consultant [i.e. DLA] shall start and progress the Appointment Work with due expedition and without delay to achieve timeous completion of the Section of the Appointment Work in question exercising a high level of professional care, skill and diligence as is to be expected of a properly qualified consultant carrying out work, similar in size and complexity to such Section of the Appointment Work" [underlining added].

3.16 This duty of care was extended to the Council in 2005. In his letter of 23 June 2005, Andrew Fitchie of DLA wrote *"We are happy to extend to*

³ CEC00031181

⁴ CEC00031180

⁵ CEC01710537

*CEC the same duty of care we owe to tie*⁶. That letter enclosed a draft letter⁷ which stated, amongst other things:

"We refer to our appointment as legal adviser by tie Limited (the "Appointment") as confirmed by your letters of 25 November 2002 and 7 March 2003 in connection with the Project.

You requested on 21 June 2005 that in respect of our work on the Project pursuant to the Appointment we acknowledge a duty of care owed to the City of Edinburgh Council ("CEC"), your corporate parent entity, such duty of care to be the same as the contractual duty of care we owe to you.

This letter confirms that as from December 5th 2003 onwards, DLA Piper Rudnick Gray Cary Scotland LLP has owed and owes the same contractual duty of care to CEC as owed to tie Limited pursuant to Clause G.3.1(a) of the General Conditions governing the Appointment on condition that:-

DLA Piper's primary responsibility has been and is to advise tie Limited and DLA Piper may at all times and for all purposes rely upon tie's instructions given to us under the Appointment as being identical to CEC's instructions as if emanating from CEC itself and as taking into account CEC's objectives and best interests...

⁶ DLA00006301

⁷ DLA00006300

This letter is a formal amendment to our Appointment pursuant to GC7.15 (Entire Appointment) and shall be governed by and construed in accordance with the laws of Scotland.

In order to put this undertaking into effect, please arrange for the enclosed copy to be signed by duly authorised officers of tie Limited and CEC and returned to us, for the attention of Andrew Fitchie."

3.17 It is accepted by DLA that "*parties plainly continued to engage after the issuing of the letter, and it is accepted by DLA that the express terms of the duty of care letter applied and that a duty of care, on the terms set out in the letter dated 23 June 2005, has existed since 23 June 2005, but back-dated to 5 December 2003*"⁸.

3.18 In the summer of 2007, the Council and DLA revisited the formalisation of the duty of care letter. On 16 August 2007, Andrew Fitchie emailed⁹ a proposed draft letter¹⁰ to Gill Lindsay, which closely followed the terms of the letter dated 23 June 2005, referred to above. DLA proceeded on the basis of this email and letter, which are addressed in the oral evidence of Gill Lindsay¹¹. Andrew Fitchie gave oral evidence that he was willing to sign letters on the terms of those referred to above in 2005 and 2007¹².

3.19 When it agreed this duty and standard of care to the Council, DLA was well aware that the Council would rely on the advice from DLA in

⁸ Paragraph 36 of written submissions of DLA dated 27 April 2018

⁹ CEC01711054

¹⁰ CEC01711055

¹¹ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 23:14 onwards

¹² Transcript of oral evidence of Andrew Fitchie 10 October 2017, page 25:1- 23

authorising execution of the project contracts, including the Infraco Contract, and entering into the Council guarantee of tie's liabilities under the Infraco Contract.

3.19.1 Reference is made to the oral evidence of Gill Lindsay, in which she stated *"My recollection of those tender documents was that the Council's position was clearly stated in them as being the ultimate person and the owner of the infrastructure. So when DLA were appointed, they knew that at all times they owed a duty of care to the Council in terms of the quantity of work which they had accepted... [TIE's] objectives were not in any way divergent from the Council's in terms of closing those contracts...there was a common objective of securing adherence to the Business Case...we [i.e. the Council] were relying on DLA who were the project's advisers..."*¹³

3.19.2 The letter of 17 December 2007 from DLA to the Council was acknowledged by DLA *"as enabling Council officers to recommend Full Council authorisation for tie to enter into the ETN contract suite"*¹⁴.

3.19.3 The letter of 12 March 2008 from DLA to the Council¹⁵ states on page 1: *"We have commented in this report on those elements of the procurement documentation and central contractual papers which when complete are viewed by tie as enabling Council officers to recommend Full Council authorisation for tie to enter into the ETN Contract Suite"*.

¹³ Transcript of oral evidence of Gill Lindsay 27 October 2017, pages page 25:10 to 28:3

¹⁴ CEC01540815

¹⁵ CEC01347797

- 3.19.4 DLA was well aware that its letter of 12 May 2008¹⁶ was intended to be used as a legal report, as part of a package of report documents prepared by TIE and DLA for the purposes of obtaining the Council's approval for the execution of the relevant project contracts¹⁷.
- 3.19.5 DLA was also well aware that the Council was to be the guarantors of TIE's liabilities under the Infraco Contract. The Council guarantee is referred to at section 9 of the letter of 12 March 2008 and section 9 of the letter of 12 May 2008, both referred to above.
- 3.20 Andrew Fitchie has sought to suggest that DLA provided "*information*" rather than "*advice*" to the Council¹⁸. This is wholly inconsistent with the terms of the duty of care which DLA owed to the Council and advice letters which DLA issued between December 2007 and May 2008, both of which are referred to above. Furthermore, Gill Lindsay gave unequivocal evidence to the Inquiry that Andrew Fitchie provided advice and not merely "*information*" to the Council: reference is made in this respect to her oral evidence, which she stated that any suggestion that DLA was not providing advice to the Council is "*wholly incorrect*", and "*There is no question that Mr Fitchie advised me as such. Through looking at my own papers, it's quite clear that there's a constant reference to advice, providing advice, and there is correspondence just after contract close which...confirms that the final sign-off letter, and indeed all letters, have been legal advice provided to both tie and to*

¹⁶ CEC01372309

¹⁷ See for example page 1 of the email from Graeme Bissett dated 12 May 2008 and page 1 of the Close Report at CEC01338846 and CEC01338853

¹⁸ Witness statement of Andrew Fitchie TRI00000102, at paragraph 2.206, page 36, at paragraph 4.60, page 52 and at paragraph 11.38, page 329

CEC...*Most certainly advice...*"¹⁹. DLA now concedes that it was DLA's responsibility to make tie and the Council aware of the relevant risks, including the risks associated with the Pricing Assumptions²⁰. Reference is further made to the email chain at CEC01709800, in which Gill Lindsay wrote to Andrew Fitchie on 4 September 2007 that she required DLA to address:

"The total and individual legal risk exposure for both Tie and the Council, and that which is and is not covered in terms of OCIP insurance or otherwise, with any reasoning for the exposure, ie necessary or commercial expectation, cost issues re bidding and whether or not risks are prudently insurable...

I would also wish your advice on whether these contracts can reasonably be recommended for acceptance to the Council and of any particular risks which require to be brought to Council attention whether due to their financial scale, likelihood, impact etc."

This request was repeated in Gill Lindsay's email to Andrew Fitchie of 9 October 2007 in the same email chain. It was seeking advice having regard to the "*particular risks*" faced by the Council. That must have included the particular financial risk to the Council as the actual funder of the Project (beyond the Scottish Government's contribution) but as just referred to, there is no evidence that DLA in general, or Andrew Fitchie in particular, ever addressed their minds to this issue.

¹⁹ Transcript of oral evidence of Gill Lindsay 27 October 2017, pages 42:20 to 44:14

²⁰ Paragraph 18 of the written submissions of DLA dated 27 April 2018

- 3.21 Senior officers at the Council relied upon the involvement of DLA: Tom Aitchison gave evidence that "*tie had behind them in the contract DLA...That again was, if you like, one of the almost quality assurance checks that the Council had to ensure that tie were giving satisfactory advice*²¹..."*I was given to believe by colleagues that...the advice being...given by tie supported by DLA was...moving towards a satisfactory conclusion*".²²
- 3.22 In its written submissions, DLA asserts that it assumed that "*Gill Lindsay and her team would take steps to read the contract*"²³. As acknowledged by DLA, Gill Lindsay's evidence was that it was important that she understood the contract²⁴. This understanding was specifically what Gill Lindsay had asked DLA to advise on in her email of 4 September 2007 referred to above. DLA having taken on the provision of that advice, it should have been accurate and complete, which it was not. Ms Lindsay's evidence was that she could not be expected to review Schedule part 4 herself, but accepts that she would have done had she "*received true and fair advice from DLA*"²⁵
- 3.23 In his oral evidence, Tom Aitchison confirmed his view that he did not consider that there was a need for independent assurance of the risks for the Council.²⁶ In his witness statement, Mr Aitchison stated that "*TIE*

²¹ Transcript of oral evidence of Tom Aitchison 28 November 2017, page 37:15-20

²² Transcript of oral evidence of Tom Aitchison 28 November 2017, page 76: 9-13

²³ Paragraph 102 of the written submissions of DLA dated 27 April 2018

²⁴ Transcript of oral evidence of Gill Lindsay 27 October 2017 page 10:23; paragraph 102 of the written submissions of DLA dated 27 April 2018

²⁵ Transcript of oral evidence of Gill Lindsay 27 October 2017 page 149:10-16

²⁶ Transcript of oral evidence of Tom Aitchison 28 November 2017, page 77:7-12

was supported by DLA (one of the largest legal firms in the UK) and that was considered to be sufficient²⁷.

Reliance by the Council on DLA

3.24 Consideration was given to the question of whether it would be appropriate for the Council to obtain legal advice from a firm other than DLA; the views of those who considered that this would be appropriate were taken into account, but the decision was taken by the Council that the better course of action would be for the advice to be provided by DLA²⁸. This decision was taken at the appropriate level: "*The matter was considered at IPG, considered with Tie, considered by Council senior officers and agreement was reached on the position.*"²⁹ Reference is further made to the witness statement of Gill Lindsay at pages 14 to 16, and to the transcript of the oral evidence of Gill Lindsay given on 27 October 2018 at pages 12:19 to 16:1.

3.25 In her oral evidence, Gill Lindsay confirmed that it would best provide protection for the Council's position for DLA to give advice to the Council on the terms and conditions set out in the draft letter, and that she "*had a telephone call with Mr Fitchie, and that we agreed that those words relating to joint client would be inserted, that it would be clear that the Council was able to receive information and advice from DLA directly.*"³⁰

²⁷ Witness statement of Tom Aitchison TRI00000022 at paragraph 171, page 58

²⁸ Transcript of oral evidence of Gill Lindsay 27 October 2017, see for example page 12:19-23; pages 13:19 to 14:3; pages 29:2 to 32:16; pages 38:2 to 41:8

²⁹ Witness statement of Gill Lindsay TRI00000160, page 16

³⁰ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 40:7-21

3.26 Gill Lindsay further addresses this point in her witness statement as follows:

*"In considering how to arrange external legal advice, the strategic decision was taken to ensure that the Council was regarded by DLA and Tie as a Joint Client. The relevant Directors within the Council together with the Monitoring Officer and Tie agreed this course of action. DLA confirmed that no conflict of interest arose and, on the contrary, DLA had always been required to consider and have proper regard to the position of the Council as owner of the Company, sole shareholder and owner of the infrastructure. This action provided the Council with the ability to receive legal advice directly to it at no additional cost, avoided what would have been a damaging if not impossible delay to the timetable and, importantly, required DLA who were working closely in the bidder negotiations and preparing all contract documentation, to be required to have an equal regard for the Council in a more formal way and for the Council to rely on their advice. The Council both sought and relied on their advice... DLA owed CEC as Joint Client an equal duty of care, could provide legal advice directly to the Council and the Council could rely on it."*³¹

3.27 There were a number of factors which were relevant to the decision to proceed on the basis of advice from DLA.

³¹ Witness statement of Gill Lindsay TRI00000160, pages 13-14, see also page 4 of the statement

- 3.28 DLA had significant relevant expertise: they were "*an international legal firm with specialist and expert skills in projects and financing*"³² and "*an international major law firm with a specialist practice in projects and finance*"³³. DLA further were the "*absolute experts in terms of light rail systems*"³⁴ and "*the experts were DLA*"³⁵.
- 3.29 DLA had been involved as "*legal adviser to the tram projects for a long period of time.....they had themselves been involved in determining the procurement, the procurement structure and strategy. They had worked with Partnerships UK to do so...they were involved at that point in what I would call a live procurement in terms of an EU Negotiated Procurement Exercise.*"³⁶
- 3.30 This involvement was in contradistinction to the position that a different law firm would be in, as "*any separate external agent could not advise if contracts properly detailed matters from live procurement negotiations they were not a party to and not aware of the result of developing commercial negotiations in a highly complex project.*"³⁷
- 3.31 Oral evidence was given to the Inquiry that "*to consider another firm of solicitors to come in to a live procurement, my view is it would have been virtually impossible as they wouldn't have known the original contract documents. They wouldn't have understood the contract suite. They wouldn't have known on which way the preferred bidders were*

³² Witness statement of Gill Lindsay TRI00000160, page 4, see also page 12 of the statement

³³ Witness statement of Gill Lindsay TRI00000160, page 14

³⁴ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 13:15-16

³⁵ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 14:15-16

³⁶ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 13:10-18

³⁷ Witness statement of Gill Lindsay TRI00000160, page 14

being chosen or had been chosen....there was really no possibility of bringing in another firm of solicitors into a live procurement exercise".³⁸

3.32 Timescales were also a related factor: *"One overriding factor at that time was that as a Council, and certainly as a Legal Division, we had been given exposure and brought into this project at a time where there were only a matter of weeks, I understand four weeks, before we were required to advise that all matters were ready to be closed. So we had an extremely short time between August, and we were advised 21 September, to ensure that we were then in a position to agree that those two full-time members may take that decision".³⁹*

3.33 However, oral evidence was given by Gill Lindsay that time was not the only factor: independent legal advice was "*not necessary*"⁴⁰. That was because of the arrangements referred to above in terms of which DLA was the adviser to the Council, as well as to TIE⁴¹. Gill Lindsay's oral evidence was that if she had considered that an independent legal review was required adequately to protect the Council's interests, she would have given advice to that effect, even if that involved delay⁴². It was considered that the concerns that had been raised by certain officers of the Council, such as Nick Smith and Colin Mackenzie, had been sufficiently addressed⁴³.

³⁸ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 14:4-13

³⁹ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 12:24 to 13:8

⁴⁰ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 15:25

⁴¹ See for example the transcript of oral evidence of Gill Lindsay 27 October 2017, page 18:6-9

⁴² Transcript of oral evidence of Gill Lindsay 27 October 2017, page 32:10-16

⁴³ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 30:13-18

3.34 Gill Lindsay summarised the position in relation to the Council relying on advice from DLA as follows, and her disagreement with the views of Nick Smith and Colin Mackenzie as follows:

*"I disagreed because we...were coming in at a very, very late stage to the project. I knew that the Council would be determining this matter in October, and there was no question politically that the matter would be delayed. We had taken a number of steps to agree this position with a range of senior officers. We had put the arrangement in place. And there was no other alternative arrangement at that time. I also...disagreed with it [the view of Colin Mackenzie in relation to legal advice from a firm other than DLA] as there was no practical example which Colin could even himself consider, and Colin's wish was that effectively the Council disengage from DLA and brought in another firm of solicitors who would have no knowledge of any of the procurement, of the history, of the...complexity of contract suite, and I did not consider that disengaging DLA and bringing in an entirely new firm who knew nothing about it was in any way consistent with the timetable. I also think their advice would have been so heavily caveated, it would simply been a range of information, and I considered that if DLA were required to consider more formally the Council's interests as they were drafting and negotiating, then that was the best way to protect the Council's interests."*⁴⁴

⁴⁴ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 31:6 to 32:5

3.35 Donald McGougan's evidence was that it was his "*understanding that Duty of Care from DLA would be sufficient for CEC purposes given the alignment of interests between TIE and CEC*"⁴⁵.

3.36 Mr McGougan also stated that "*CEC were not in a position to shadow TIE. CEC could not duplicate TIE's activities and responsibilities. CEC relied on the advice of TIE and the legal advice of DLA when attempting to understand the complexities of the Financial Close negotiations and the proposed finalised contract position*"⁴⁶.

3.37 Donald McGougan gave evidence that he was happy to proceed on the basis of Gill Lindsay's view in relation to legal advice, and therefore for the Council to rely on advice from DLA:

"...my overview was that the Council should be able to rely to a large degree on the advice from tie and from their legal advisers, given that we had secured a duty of care from DLA to the Council that they would have regard to the Council's interests in development of the contract. Beyond that, I was aware that the Council Solicitor, as I think it says in this email⁴⁷, that the Council Solicitor was of the view that the contract was still under development at this stage. It wasn't a completed suite of contract documents that someone could come in and look at. But the city's solicitor was of the view that another firm of lawyers, external lawyers, coming in to work beside DLA, working for tie and for the Council, would confuse the issue and could lead to delays and be

⁴⁵ Witness statement of Donald McGougan TRI00000060, page 20

⁴⁶ Witness statement of Donald McGougan TRI00000060, page 53, paragraph 138

⁴⁷ CEC01560815

damaging. I was happy to take the city's solicitor's view in regard to this proposal....What we were asking for was -- well, it's an analysis of the retained risk from the contract, and I think I was of the view that the responsibility that DLA had to the Council was sufficient in that...there was consultation with or between departments about the need for an independent legal analysis of the contract, and the city's solicitor was clear that she felt that that wasn't required. And...I was prepared to go along with that"⁴⁸ ...

But we did have, and I think we were entitled to rely on due diligence in tie and the written information from DLA, together with the discussions that our legal section were having with DLA, to take the view that the changes in risk that had happened in the run-up to contract close had been understood in terms of the overlapping elements of design construction; and that a provision had been made for them in the risk register....DLA had a duty of care to the Council and we expected them to properly undertake that duty of care and alert the Council to any areas where the final contract negotiations had changed the transfer of risk balance"⁴⁹.

3.38 Mr McGougan also gave evidence in relation to the commonality of interest of tie and the Council:

⁴⁸ Transcript of oral evidence of Donald McGougan 29 November 2017, pages 138:17 to 140:12

⁴⁹ Transcript of oral evidence of Donald McGougan 29 November 2017, page 150:5- 19

"I expected there to be full commonality between the Council and tie in relation to the planning and execution of contracts for the delivery of the tram project on time and on budget..."⁵⁰

I felt that there was no reason at all for there to be a departure between tie's interests and the Council's interests in relation to the delivery of the project..."⁵¹

I can't recall an experience where there was a divergence in terms of commonality of interest"⁵².

3.39 The evidence of Nick Smith and Colin Mackenzie was that they were not involved in reviewing Schedule part 4 prior to contract close, and accordingly the Council relied on DLA, as DLA was aware. Reference is made by way of example to the following passages from the evidence of Nick Smith and Colin Mackenzie respectively:

3.39.1 Nick Smith: witness statement⁵³, answers 54(a), 54(b), 59(b), 67, 68, 69 and 70(c); transcript of oral evidence on 14 September 2017, pages 3:18-22, 4: 6-14; page 4: 23 to page 5: 1.

3.39.2 Colin Mackenzie: witness statement⁵⁴ page 28; transcript of oral evidence on 26 October 2017, pages 45:16 to 46:17, 47:21 to 48:5;

DLA's involvement in Schedule part 4 and Pricing Assumption No.

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⁵⁰ Transcript of oral evidence of Donald McGougan 29 November 2017, pages 165:23 to 166:1

⁵¹ Transcript of oral evidence of Donald McGougan 29 November 2017, page 166:10- 13

⁵² Transcript of oral evidence of Donald McGougan 29 November 2017, page 167:3- 5

⁵³ Witness statement of Nick Smith TRI00000071

⁵⁴ Witness statement of Colin Mackenzie TRI00000054

3.40 DLA was involved in the development and finalisation of Schedule part 4, and was well aware of its terms prior to contract close. Andrew Fitchie was involved in a number of email chains in this respect, and attended meetings⁵⁵. Reference is made in this respect to the submissions at section 5.

3.41 DLA's involvement in Schedule part 4 was also confirmed in evidence to the Inquiry. In response to a question in relation to "*discussions and negotiations in relation to Schedule 4*", Steven Bell states in his witness statement "*...During March there were a number of meetings that I attended...There would probably have been a couple of sessions per week, maybe more depending on what topics were being dealt with and that was, generally, working in a round-table type forum. There would be ourselves [i.e. representatives of tie], DLA (usually Andrew Fitchie), Pinsent Masons representing Billfinger (Ian Laing), Susan Clark and also Scott McFadzen who was the BBS Project Director at that time*"⁵⁶. In his oral evidence to the Inquiry, Steven Bell stated that Andrew Fitchie "*was the lead partner for our legal adviser who were fundamental to the drafting of and finalisation of Schedule 4...I became specifically involved in the Schedule Part 4 discussions from about mid-February, and that was at meetings with DLA, including Andrew [Fitchie], and some of his colleagues present, and generally they tended to be at the working sessions that we had with BBS to try and resolve these matters. So I consider them implicitly involved in providing*

⁵⁵ Witness statement of Andrew Fitchie TRI00000102, page 173 to 177 and transcript of oral evidence of Andrew Fitchie 10 October 2017, page 93:21 to 95:16

⁵⁶ Witness statement of Steven Bell TRI00000109, page 51

comment and advice from the point that I was involved in Schedule part 4 from....And certainly Andrew had a risk matrix document to prepare as part of the Final Business Case, and that was discussed as part of that conversation around Schedule part 4 and in finalisation of that risk matrix. So my view was that DLA and Andrew personally and some of these key team members, I think, Phil Hecht and Joanne Glover were a couple of the lawyers who were involved attended virtually all of those sessions, if not all of them, and they were certainly fundamental to any circulation of any working drafts and proposals...I remember asking how the Notified Departure mechanism would work, and he [Andrew Fitchie] gave verbal advice at that time which was the mechanism by which Schedule Part 4 would convert into a tie change ⁵⁷. In response to a request for comment on Andrew Fitchie's position that TIE wanted Andrew Fitchie and other lawyers to have minimal input into Schedule part 4 in the period between January and May 2008, and such input was minimal, Mr Bell responded "*That is definitely not my recollection. Mr Fitchie or his colleagues...were in attendance at the vast majority, is my recollection, of these reviews and meetings. And certainly were a core player in any circulation of proposed changes or amendments of finalising of the drafting of Schedule Part 4*"⁵⁸.

⁵⁷ Transcript of oral evidence of Steven Bell 24 October 2017, pages 41:17 to 45:6

⁵⁸ Transcript of oral evidence of Steven Bell 24 October 2017, pages 50:22 to 51:2

3.42 Reference is further made to Bilfinger's written submissions, where they state *"from Bilfinger's perspective...DLA were in attendance at meetings at which Schedule Part 4 was discussed"*⁵⁹.

3.43 Graeme Bissett gave oral evidence⁶⁰ in relation to the role of DLA by reference to an email sent by him on 25 March 2008⁶¹, which attached a document⁶² containing a table allocating responsibility for various actions to different parties, including DLA. Mr Bissett confirmed that finalisation of the Infracore Contract Suite was assigned to DLA⁶³, and described his understanding of DLA's role:

"A. ...I would have assumed the same as with any major firm of lawyers with whom I had worked in closing out a major contract, which is that the firm would have its own internal quality control procedures to make sure that all of the components of the contract were in existence. They had final read-throughs, potentially, and I don't know DLA's internal procedures, but possibly a review by an independent partner or senior person within the firm. That sort of thing..... In my experience, the firm takes responsibility for the final quality control over all of the legal documentation which they've obviously been involved in negotiating and advising on; and once they sign off, very often with a summary report in some form, obviously it varies depending on the circumstances, but a summary report which is in more of a, if you like, a commercial analysis

⁵⁹ Paragraph 79 of written submissions of Bilfinger dated 27 April 2018

⁶⁰ Transcript of oral evidence of Graeme Bissett 21 March 2018, pages 1:19 to 8:10

⁶¹ CEC01431194

⁶² CEC01431196

⁶³ Transcript of oral evidence of Graeme Bissett 21 March 2018, page 6:8-11

and summary for boards to feel comfortable that that part of the process has been executed. I think that is pretty well standard practice.

Q. I should say this document, as we have seen, was attached to the email, the first recipient of which was Andrew Fitchie at DLA. Can you recall getting any feedback from him about this or any indication he wasn't happy with the role that DLA were being assigned in this document?

A. No, none at all, and I think I would have remembered if there had been any difficulty.

Q. Would it have been significant if the solicitors had come back and said: no, we are not willing or able to undertake that particular role"?

A. I think it would have been very significant, yes⁶⁴.

3.44 The document referred to above⁶⁵ contained a schedule⁶⁶ which provided for DLA to carry out a full quality control review in relation to both the Infraco Contract and Schedule part 4⁶⁷.

3.45 Willie Gallagher gave oral evidence⁶⁸ about the role of DLA:

"We were...receiving... legal advice and having review of all documents by DLA throughout this whole process. And I think even if you look at all the circulation lists for all these emails, you will see that DLA are copied into them all. I think you must not believe that there was any plan to

⁶⁴ Transcript of oral evidence of Graeme Bissett 21 March 2018, pages 6:15 to 8:5

⁶⁵ CEC01431196

⁶⁶ CEC01431195

⁶⁷ Transcript of oral evidence of Graeme Bissett 21 March 2018, page 17:10-15

⁶⁸ Transcript of oral evidence of Willie Gallagher 17 November 2017, pages 128:13 to 129:14

*exclude DLA from any parts of the process. Indeed, that was the whole point of having Andrew [Fitchie] as part of the team, that he attended every meeting, that he had access to all the information that was available... We were hugely reliant on DLA and indeed the...professional procurement people who had been involved in procuring tram systems, because they had done this before. So they had produced -- in DLA's case, they had taken responsibility for the contract, the contract was their contract. They were involved in the evolution of the contract and they were -- involvement in the detailed evaluation and examination of all the clauses; and if at any point Andrew or the DLA team felt that this was not consistent with the outcome that we were intending to achieve, then they had the opportunity to write to us. They had the opportunity at Tram Project Board meetings or at internal meetings to state their position, and indeed, in the end of the day, I believe they produced a formal report to the Council which reflected their position"*⁶⁹

3.46 James McEwan gave evidence about the nature of DLA's involvement in Schedule part 4:

"Q. Did you have legal advice in negotiating Part 4 --

A. Yes, of course we did. Yes. We had DLA Piper providing the legal advice to the...team...

⁶⁹ Transcript of oral evidence of Willie Gallagher 17 November 2017, pages 128:13 to 129:14

Q. If it's suggested to you that a representative from DLA Piper was there only to mark up the draft agreement and not to give any legal advice, what comment would you have on that?

A. Nonsense.

Q. If it was suggested that there was a decision by -- within tie, amongst the people negotiating to shut out or exclude legal advice, what would be your comment on that?

A. Not to my recollection. Why would anybody do that?... I was certainly not involved in instructing anybody to prevent our lawyers coming to the meetings to discuss these things, no. Of course they were there to help mark up the documents, but I mean, cor blimey, we could get a secretary to do that. The bottom line was they were there as far as I'm concerned, in their legal capacity.

Q. If we see emails being sent to or copied to the solicitors, it may seem an obvious question, but why was that being done?...

A. ...To make sure that our legal representation was fully up to speed with everything that was going on. And to give us an assurance in that regard"⁷⁰.

3.47 Bob Dawson also confirmed the involvement of DLA in the drafting of Schedule part 4 in his oral evidence⁷¹.

⁷⁰ Transcript of oral evidence of James McEwan 18 October 2017, pages 116:1 to 117:18

⁷¹ Transcript of oral evidence of Robert Dawson 21 March 2018, pages 38:2-12 and 84:25 to 85:1

3.48 Andrew Fitchie accepted in his oral evidence that "*I did apply my mind to this particular language*"⁷² (namely, Schedule part 4).

Advice given by DLA

3.49 **DLA's letter of 30 November 2007 to the Council**⁷³

3.49.1 On 30 November 2007 (and therefore prior to FBCv2 being finalised), DLA issued a letter to the Council, under cover of an email sent on behalf of Sharon Fitzgerald of DLA to Gill Lindsay, and copied to Colin Mackenzie, Matthew Crosse and Andrew Fitchie. That letter stated, amongst other things:

"We are able to report the draft contract suite has been advanced to a point where there are no significant legal issues outstanding on the core terms and conditions which could be an obstacle reaching a contract close and signature as programmed by tie in late January 2008. Work remains to translate commercial and technical positions being settled currently into agreed detailed drafting...."

Risk allocation matrices for the Infraco and Tramco Contracts are up to date and accurately reflect the status of each of the Infraco and Tramco Contracts....

As reported in our letter of 22nd October, we consider that the contractual allocation of risk and responsibility between tie Limited and the competitively selected private sector providers remains broadly aligned with the market norm for UK urban light rail projects, taking into

⁷² Transcript of oral evidence of Andrew Fitchie 10 October 2017, page 132:18- 19

⁷³ CEC01512159

account: the distinct characteristics of the Edinburgh Tram Network, its technical and commercial state of readiness at ITN issue in October 2006 and the development of scheme engineering and data design since that date. Refinement will be needed on the contract suite between now and programme close to take account of the actual state of the Employer's Requirements and Background Information finally made available. This exercise is mapped and at present is not expected to either materially alter risk allocation or adjust the core contractual rights and responsibilities...

During the Preferred Bidder stage, there has been a predictable hardening of stance by the Consortium on matters where their position had been expressly reserved or outlined only either due to extreme time pressures of the programme on contract negotiation to Preferred Bidder appointment or due to paucity of technical information/incomplete due diligence. Two areas where, in our view, the desired CEC risk allocation may not be achieved are Consents and Third Party Agreements. The primary reasons for this - namely the Consortium's view that tie/CEC are best placed to manage risk associated with certain consents and full compliance with third party undertakings - are also the primary reason why adjusted responsibility retention by tie/CEC for these matters (which are essentially a project management and stakeholder interface function) may not be unpalatable. The Consortium does accept risk for execution of third party agreements we were instructed to include in the ITN draft Contract Suite."

3.50 **DLA's letter of 17 December 2007 to the Council**⁷⁴

3.50.1 DLA's letter of 17 December 2007 was issued before the Wiesbaden Agreement had been concluded, and before Schedule part 4 had been produced. It was also issued before the report to the Council in advance of its meeting on 20 December 2007.

3.50.2 Andrew Fitchie stated in his oral evidence to the Inquiry that he agreed with the proposition that the purpose of the letter of 17 December 2007 was "*to give reassurance to the Council that their officers could enter into this contract suite*"⁷⁵.

3.50.3 The letter states at pages 2 to 3:

"We remain of the view (as in both our earlier written reports to you) that the contractual allocation of risk and responsibility between the Limited and the competitively selected private sector providers remains broadly aligned with the market norm for UK urban light rail projects, taking into account: the distinct characteristics of the Edinburgh Tram Network, its technical and commercial state of readiness at ITN issue in October 2006 coupled with the development of scheme engineering and data design since that date. Refinement will be needed within the draft ETN contract suite between now and programmed close to take account of the actual final state of the Employer's Requirements, the matching Consortium's proposals and project specific and Background Information finally made available. This exercise is mapped and at

⁷⁴ CEC01540815

⁷⁵ Transcript of oral evidence of Andrew Fitchie 11 October 2017, page 12:13-19

present is not expected to either materially alter risk allocation or adjust the core contractual rights and responsibilities".

3.51 DLA's letter of 12 March 2008 to the Council⁷⁶

3.51.1 DLA's letter of 12 March 2008 was written at a point in time when Schedule part 4 was under negotiation, but was not yet finalised. DLA had by that point in time received a copy of Schedule part 4 in draft⁷⁷.

3.51.2 Section 1 of the letter states that *"in our view the draft agreements in their current state adequately capture the commercial position which tie has achieved, followed by a list of matters which require to be agreed for tie to issue a notification of intent to award"*.

3.51.3 Paragraph 5.1 of the letter states:

"Our view on the contractual allocation of risk and responsibility between tie and the competitively selected private sector providers remains that the Infraco Contract and the Tram Supply and maintenance Agreements are broadly aligned with the market norm for UK urban light rail projects, taking into account the distinct characteristics of the ETN and the attitudes of BBS and SDS to novation. The project's state of technical and commercial readiness has matured since Christmas. However, the fact that work still continues on the Employer's Requirements Schedule — the core project scope — at this very late stage (resulting in SDS requiring an instruction to align their designs with tie's Employer's Requirements and the Infraco

⁷⁶ CEC01347797

⁷⁷ CEC00592614

Proposals) means that technical ambiguity (and therefore delay/cost risk) may exist in the interplay between design, scope and method of execution. There is contractual mitigation available whereby (1) the Infraco is under a duty to bring any ambiguity in technical documentation to the attention of tie; (2) tie's authority to direct resolution of such issues; (3) the precedence of core terms and conditions over Schedules; and (4) the exercise of SDS now instructed by tie to align their designs with the Employers' Requirements and the Infraco Proposals so as to eliminate mismatches".

3.51.4 Neither the letter of 12 March 2008, nor the risk allocation matrix appended to it⁷⁸, make any reference to Schedule part 4. There is no reference in the letter or the risk allocation matrix to a change in the risk profile having occurred since the previous letter issued in December 2007, despite the Wiesbaden Agreement having been concluded during that time, and Schedule part 4 being under discussion in a form which effectively passed the risk for all changes from BDDI to IFC to tie, rendering the *"normal development and completion of design"* which TIE considered to be Infraco's responsibility all but empty of meaning.

3.51.5 The letter of 12 March 2008 is incomplete, in that it fails to refer to the ongoing negotiations in relation to Schedule part 4. It is also inaccurate. Section 1 of that letter refers to Annex A: *"a report by tie with input from ourselves on contractual matters [which] provides more detailed analysis of the draft contracts"*. However, the report at Annex A makes no mention of Schedule part 4 and states that *"in broad terms, the*

⁷⁸ CEC01347795

principal pillars of the ETN contract suite in terms of scope and risk transfer have not changed materially since the approval of the Final Business case in October 2007". As conceded by Andrew Fitchie in oral evidence, this was inaccurate (see below).

3.52 DLA's letter of 28 April 2008⁷⁹

3.52.1 DLA's letter of 28 April 2008 stated in relation to the "*Core Infraco Contract Terms*":

"The Core Infraco terms are closed as to all matters of contractual technical and commercial principle...No issues have arisen since we last reported which have resulted in an alteration (of consequence) to risk balance. As they stand, the terms and conditions represent a clear reflection of the positions which have been negotiated by tie and are competent to protect and enforce those positions"

3.52.2 Under the hearing "*Risk*", the letter stated:

"Following on from our letter of 12 March, we would observe that delay caused by SDS design production and CEC consenting process has resulted in BBS requiring contractual protection and a set of assumptions surrounding programme and pricing.

tie are prepared for the BBS request for an immediate contractual variation to accommodate a new construction programme needed as a consequence of the SDS Consents Programme which will eventuate, as

⁷⁹ CEC01312368

well as for the management of contractual Notified Departures when (and if) any of the programme related pricing assumptions fall".

3.52.3 Gill Lindsay gave evidence in the context of this letter that her "*clear understanding was that the only Notified Departure that would have been expected was the one relating to the version of the design programme*"⁸⁰. Gill Lindsay further stated that "*there's nothing here in these words which are telling me that the price will not still be the price plus the QRA*"⁸¹. The Risk Allocation Matrix produced by DLA constituted an overview of which party or parties were to bear a risk, but did not contain any information about the probability of a risk arising, or the value of such a risk⁸²: "*The Council were relying on DLA's advice...the risk matrix actually made no mention of Schedule 4, and I think it should have been very explicit in that risk*".⁸³

3.53 **DLA's letter of 12 May 2008 to the Council and TIE**⁸⁴

3.53.1 In her oral evidence, Gill Lindsay explained the purpose of this letter as follows: "*This letter was because we were advised that there had been a significant increase in price required by the consortium just at the point of the Council meeting, and there was...particular activity after that time in order for there to be a decision between tie and executive members of the Council as to whether...the deal would still go ahead,*

⁸⁰ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 146:21-23

⁸¹ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 147:18-20

⁸² Transcript of oral evidence of Gill Lindsay 27 October 2017, pages 151:22 to 152:8

⁸³ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 191:22-25

⁸⁴ CEC01372309

whether that sum was going to be paid, and then what import it would have in terms of that."⁸⁵

3.53.2 Paragraph 1.1 of DLA's letter of 12 May 2008 states: "*No issues have arisen since we last reported which have resulted in any adverse alteration (of consequence) to risk balance*".

3.53.3 This was inaccurate, in that it failed to mention the material change in risk exposure to TIE, and therefore to the Council resulting from Schedule part 4, and in particular the interaction among Pricing Assumption No. 1, Notified Departures, and clause 80.

3.53.4 Paragraph 1.1 of DLA's letter of 12 May 2008 also states:

"As they stand, the terms and conditions represent a clear reflection of the positions which have been negotiated by tie and are competent to protect and enforce these positions".

As referred to below, the terms and conditions did not reflect TIE and the Council's understanding of the position.

3.53.5 Paragraph 1.2 of the letter refers to the SDS design in the context of the finalisation of the Employer's Requirements. It does not refer to the SDS design in the context of Pricing Assumption No. 1. The letter is incomplete in this respect.

3.53.6 Paragraph 5 of the letter states: "*Following on from our letter of 12 March, we would observe that delay caused by SDS design production*

⁸⁵ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 155:14-22

and CEC consenting process has resulted in BBS requiring contractual protection and a set of assumptions surrounding programme and pricing, tie are prepared for the BBS request for an immediate contractual variation to accommodate a new construction programme needed as a consequence of the SDS Consents Programme which will eventuate, as well as for the management of contractual Notified Departures when (and it) any of the programme related pricing assumptions fail".

3.53.7 This does not highlight the particular risk arising from Pricing Assumption No. 1. It is also inaccurate. Notified Departures were not restricted to a situation where "*any of the programme related pricing assumptions fail*": Pricing Assumption No. 1 was not a programme related Pricing Assumption, but could (and did) trigger multiple Notified Departures. Furthermore, it was not a case of "if" the assumptions failed, but when. The letter is incomplete and inaccurate in this respect.

3.53.8 Similarly, at paragraph 11.3 of the letter, DLA wrote:

"The Pricing Schedule (Infraco Contract Schedule Part 4) has been extensively discussed over the past six weeks and is now settled as to its key assumptions, value engineering items, provisional sums and fixed prices. tie has assessed the likely financial impact of the assumptions not holding true and triggering changes".

3.53.9 This passage contains no reference to specific Pricing Assumptions and Pricing Assumption No. 1 in particular. The letter is incomplete, in that it

does not highlight the risk arising from the Pricing Assumptions and in particular Pricing Assumption No. 1.

3.53.10 Paragraph 10 of the letter of 12 May 2008 stated: "*In our opinion tie has worked extremely hard to retrieve a difficult situation and to ensure that value and significant risk re-balance has been secured from BBS*". This does not reflect the risk assumed by TIE (and therefore the Council) under Pricing Assumption No. 1.

3.53.11 DLA's letter of 12 May 2008 attached a risk allocation matrix⁸⁶. The risk allocation matrix did not address Schedule part 4, the probability of a risk event occurring or the potential impact should it occur.

3.54 Where Mr Fitchie did touch on the terms of Schedule part 4 in an email to TIE, he made no reference to the terms of Pricing Assumption No. 1. On 26 March 2008, Ian Laing had sought confirmation in relation to the Notified Departure relating to the Design Delivery Programme: "*As we discussed earlier today, the Design Delivery Programme that will be v28. The Pricing Assumption in Schedule 4 of the Infraco Contract assumes that the Design Delivery Programme will not change from v26. It follows that there is the possibility that there will be an immediate Notified Departure on contract execution. Given the unusual position that we are in, please can you confirm that this is understood and agreed by tie*".

3.55 In a further email on 31 March 2008, Iain Laing asked again for confirmation on the point, and James McEwan asked Andrew Fitchie for

⁸⁶ CEC01347795

advice: "Can you advise on a response to this please, what Ian is saying is factually correct albeit that we are working to minimise the impact and variance between critical path items. While we accept that the version change will be a notified departure we are concerned to ensure that there will be no gaming of this position by BBS, and that only where the change can be shown to materially change the Infraco programme critical path should we be liable for potential additional charges"⁸⁷.

3.56 In responding to the request for advice, Andrew Fitchie did not raise the issue of Pricing Assumption No.1, nor its interaction with clause 80:

"If the situation is that at this point SDS is unable to produce a design delivery programme which is reliable and static at V26 - and that is indeed the situation that SDS have articulated - and that this programme will need to be varied immediately post contract award, tie needs to endeavour to negotiate with BBS now the specifics of what is or is not to be permitted as a variation to the Infraco Contract and its master construction programme, otherwise the Notified Departure mechanism is too blunt and will permit BBS to include everything that they estimate is going to affect them to be priced and to be granted relief. That Estimate is bound to be all encompassing and conservative. The only approach open to tie, in my opinion, is a factual one, not a contractual one (since the mechanism for Notified Departure puts the advantage with BBS by creating an automatic tie Change): to capture as many identified key changes that tie knows will be required and to

⁸⁷ CEC01465878

attempt to fix them and agree their likely programme and/or cost impact with BBS prior to contract award, or at the least identify the reasonable range of programme and cost impacts. Tie can still monitor/evaluate what are the elements of this specific Notified Departure for which Infraco will assert claims for additional cost and time, but tie has no ability to prevent there being a tie Change, other than going to DRP. The optimal response to Ian would then be to acknowledge that V26 will need to varied to reflect v28 but that tie wishes to agree the principles and key facts around which the construction programme and any related financial impact will be assessed and calculated by BBS. This is one where Steven and Geoff must, I feel, have a better sense of how factually to restrict BBS's ability to exploit this. After this review, we might be able to go about trying to structure acceptable controls in the Infraco Contract⁶⁸.

Mr Fitchie did not follow up on structuring "acceptable controls".

3.57 Mr Fitchie gave evidence⁸⁹ about his understanding of the effect of Pricing Assumption No. 1:

"I didn't like any of SP4, but particularly PA 1 and the wording "For the avoidance of doubt normal development and completion of designs means the evolution of design through the stages of preliminary to construction stage and excludes changes of design principle, shape and form and outline specification". I made my views on this and what it

⁸⁸ CEC01466394

⁸⁹ Witness statement of Andrew Fitchie TRI00000102 paragraph 7.241

*had done to risk allocation clear to what I believed were the relevant TIE senior management and more than once as I explain*⁹⁰.

3.58 As will be explained, there is no evidence that Mr Fitchie did bring his concerns to the attention of the responsible TIE management but the important point is that Mr Fitchie has given written evidence that he claims to have been aware of the consequences of Schedule part 4 and the pricing assumptions all along, and he has confirmed that evidence under affirmation at the Inquiry.

3.59 Mr Fitchie gave evidence that:

*“At contract signature, TIE already knew that that number of important Assumptions were untrue, triggering BBS’s immediate right to claim under the contractual change mechanism. Pinsent Masons also flagged this direct to TIE. It was, in short, again, a fantasy to regard the Infracore Contract as fixed price post-Wiesbaden or at contract signature and TIE’s management were fully aware of this. In exchange for a heavily qualified construction price – not a fixed one – and a construction programme with assumptions and conditions, TIE’s most senior corporate executive and at least two members of its Project Directorate had agreed to the key principles of SP4 Pricing and then participated in the drafting and settling of its language.”*⁹¹

Once again, this is evidence that Mr Fitchie claims to have understood at the time the consequences of the pricing assumptions in Schedule

⁹⁰ Witness statement of Andrew Fitchie TRI00000102 page 175

⁹¹ Witness statement of Andrew Fitchie TRI00000102 page 183, paragraph 7.285

part 4 but nowhere does he explain the steps taken to bring that to the attention of CEC having regard to his duty of care to the Council even if he asserts that senior management at TIE were aware (and which the other evidence contradicts).

3.60 In his oral evidence, Andrew Fitchie conceded that he did not give advice about the risk allocation created by Schedule part 4 in writing:

"A. I made my views on this [schedule part 4 and particularly Pricing Assumption No. 1⁹²] and what it had done to risk allocation clear to what I believed were the relevant TIE senior management - and more than once as I explain."

Q. Did you ever record that in writing?

A. No."

3.61 Andrew Fitchie also gave evidence that he understood the implications of Pricing Assumption No. 1, but nonetheless did not advise on this by email, and was not sure whether he gave any advice about it at all:

"Q. ...was it your understanding of the effect of Schedule Part 4 that any development from BDDI would entitle them to seek a variation? What's your answer to that?

A. Yes. Yes, although the question comes up as to missing design. In other words, design scope -- design for scope that was not available to BBS at BDDI.

⁹² Transcript of oral evidence of Andrew Fitchie 10 October 2017, page 86:20- 25

Q. *What is the question about that?*

A. *The question about that is how does Schedule Part 4 actually tackle that.*

Q. *...Is that something on which you provided advice at the time to tie? At the time, I mean prior to conclusion of the contract.*

A. *I am not sure. That is my honest opinion. My honest recollection.*

Q. *...Are you able to point to a single email or minute of meeting in relation to the dispute resolution procedures that went on which records that you had given advice that it would present a risk to tie and the Council?*

A. *Pre contract?*

Q. *That you had given advice pre contract that it would present a risk?*

A. *I don't believe there is such an email...*⁹³

3.62 As referred to above, it is evident from the terms of DLA's written advice letters that written advice in relation to the risk allocation in Schedule part 4 and in particular Pricing Assumption No. 1 was not given by DLA. The evidence of witnesses from TIE and the Council, as referred to below, is that neither was it given orally.

3.63 In his oral evidence, Andrew Fitchie stated that the reference in the document headed "*Draft of DLA Report on Infraco Contract Suite*"⁹⁴ to

⁹³ Transcript of oral evidence of Andrew Fitchie 10 October 2007, pages 166:15 to 168:9; see also pages 170:8 to 174:14

the principal pillars of the contract suite in terms of programme, cost, scope and risk transfer not having changed materially since the approval of the Final Business Case in October 2007 was "*stretching it*" and "*inaccurate*"⁹⁵.

3.64 Mr Fitchie was also taken in oral evidence⁹⁶ to the updated version of the report circulated prior to contract close in May 2008⁹⁷, which contained similar wording to that referred to above, in that it stated that the principal pillars of the contract suite, in terms of scope and risk transfer only, had not changed materially since the approval of the Final Business Case in October 2007. Mr Fitchie was asked whether that did "*not cry out for some action on your part to make them [the Council] aware that a statement like this was being made to them*"⁹⁸. Mr Fitchie's answer was that "*the appropriate place to make the point about these reports was back to tie*"⁹⁹. There is no documentary evidence which shows that DLA or Andrew Fitchie raised any concerns about the statement in the report to TIE or the Council. Reference is further made to the evidence in relation to TIE's understanding of the position below.

3.65 Mr Fitchie's oral evidence on the point continued as follows:

"Q. ...Why had you done nothing for two months, knowing that this was going forward to mislead the Council about the terms of the contracts?"

⁹⁴ CEC01428734

⁹⁵ Transcript of oral evidence of Andrew Fitchie 10 October 2017, pages 178:1 and 178:6

⁹⁶ Transcript of oral evidence of Andrew Fitchie 10 October 2017, pages 181:22

⁹⁷ CEC01338851

⁹⁸ Transcript of oral evidence of Andrew Fitchie 10 October 2017, page 184:13- 15

⁹⁹ Transcript of oral evidence of Andrew Fitchie 10 October 2017, page 184:19- 20

A. I do not have an answer to that other than the fact --...The answer to your question as to why two months elapsed between the emergence of this document and the emergence -- re-emergence of this document again...you are levelling a direct criticism at me for not picking this up, and for not contacting the Council and saying tie is misleading you.

Q. I said, or at least to tell them that they needed to get independent legal advice on the matter.

A. I -- I'm not sure that the course for me at that point was to say: you need to get independent legal advice. I accept that this language stayed in the Infraco --this document. I'm not prepared to accept that I owed a duty to CEC to tell them that they needed independent legal advice.

Q. So it's okay just to go forward in the knowledge that there was a misrepresentation being made to them as to the basis of the contracts that were about to be concluded?

A. Well, I believed in fairness that CEC have a tremendous amount of information about what was going -- what was going through, and there were a number of documents that came through to me from tie indicating that there were direct discussions going on through this period between the Council and tie about the contract, about risk allowances, and so I have to say that at this stage I was relying upon tie to produce/provide the information to answer the questions from the Council being put to tie from the Council on risk.

Q. *Even if you didn't have a duty of care to the Council as a client or some other way, as a solicitor with a -- as a partner in a firm, a well-established firm, were you quite content for your client to be misleading a third party?*

16 A. *No. I was disappointed, and -- I was disappointed in myself at this point. I was pretty tired.*

Q. *CHAIR OF THE INQUIRY: What options would be available to you in that situation where you were a partner in a firm, you realise your client is misleading a third party with whom you had no contractual relationship?*

A. *I -- I could have -- I could have spoken to another partner and said: look, I need you to take a look at this, I need you to advise me what the right course of action is in a situation where one client appears to be reporting an internal document -- in closed documentation something which is not accurate....I did not do that¹⁰⁰.*

3.66 In its written submissions dated 27 April 2018, DLA suggests that the reason why Mr Fitchie made the foregoing comments was that he was "exhausted" and that "he was not shown all of the relevant documents together". This is said to explain why Mr Fitchie "gave quite different answers [to DLA's counsel] to those given to Inquiry Counsel"¹⁰¹. Mr Fitchie provided a written witness statement to the Inquiry on 14 July

¹⁰⁰ Transcript of oral evidence of Andrew Fitchie 10 October 2017, pages 185:24 to 188:4

¹⁰¹ Paragraphs 16 to 18 of closing submissions on behalf of DLA dated 27 April 2018

2017¹⁰² which ran to 364 pages and covered numerous documents, including those put to him by Inquiry Counsel during the course of his oral evidence. Mr Fitchie had seen those documents at the time of their creation in 2008. He had therefore had ample opportunity to consider all of the relevant documents together, and was not being asked to consider them for the first time during his oral testimony.

3.67 The document headed "*Edinburgh Tram Project Report on Terms of Financial Close (Close Report)*"¹⁰³ was also put to Mr Fitchie in his oral evidence. Mr Fitchie confirmed that the following passage was inaccurate¹⁰⁴:

"The increase in Base Costs for Infraco is a result of a negotiated position on a large number of items including the contractual interfaces between the Infraco, Tramco and SDS contracts and substantially achieving the level of risk transfer to the private sector anticipated by the procurement strategy."

3.68 A draft of this document had been available to Mr Fitchie since 10 March 2008¹⁰⁵. Mr Fitchie confirmed in his oral evidence that "*it was known by you and others that this report was to go to the Council and it was intended that it should be something that they relied upon for*

¹⁰² TRI00000102

¹⁰³ CEC01338853

¹⁰⁴ Transcript of oral evidence of Andrew Fitchie 10 October 2017, page 188:22 and 24

¹⁰⁵ CEC01450478 and CEC01450479

*allowing the contract to go forward and close*¹⁰⁶. He further stated that the relevant documents "*had been sent to me in March*"¹⁰⁷.

3.69 Various passages from the report were put to Mr Fitchie¹⁰⁸:

"Q. ...reading [those passages], even as an outsider, particularly with the heading "Price certainty achieved" they give no indication at all of the possibility of substantial additional cost arising from Part 4 of the Schedule, do they?

A. No, they do not.

Q. And to that extent, they rather misrepresent the financial exposure under the contract?...

A. Right. It does not contain a reference to the effect of Schedule Part 4.

Q. There's no indication of the additional costs that could arise there, is there? None at all...

*A. ...I agree with you*¹⁰⁹.

3.70 Further passages were put to Mr Fitchie¹¹⁰, in respect of which he gave the following evidence:

"Q. None of these [passages] note the risk that also arises from the overlapping design that's inherent in Part 4 of the Schedule.

¹⁰⁶ Transcript of oral evidence of Andrew Fitchie 10 October 2017, page 190:6-11

¹⁰⁷ Transcript of oral evidence of Andrew Fitchie 10 October 2017, page 190:15

¹⁰⁸ Transcript of oral evidence of Andrew Fitchie 10 October 2017, pages 191:5 to 192:11

¹⁰⁹ Transcript of oral evidence of Andrew Fitchie 10 October 2017, pages 192:17 to 193:15

¹¹⁰ Transcript of oral evidence of Andrew Fitchie 10 October 2017, pages 193:16 to 194:23

A. No.

Q. ...there's no mention here of any possible complication caused by Schedule 4.

A. You're right.

A. Did you not think that it ought to have been included, putting it another way?

A. I have to say that this is deep in a document which was not being produced by DLA Piper, and...I clearly overlooked in reading this the necessity to include in there a mention of the Schedule Part 4..."¹¹¹

3.71 During his oral evidence, it was put to Mr Fitchie that certain individuals at TIE "would have been aware at the time of the letters in May to the Council that the information being given to the Council was inaccurate" and that Mr Fitchie in May 2008 "would have been aware that they were knowingly providing false information to the Council". Mr Fitchie agreed that the information in the reports to the Council in May 2008 was "deficient", "not accurate" and "wasn't true"¹¹². Mr Fitchie also confirmed that he understood the legal significance of knowingly providing false information is fraud, amounting to a criminal offence¹¹³; he further confirmed that "I read those documents. They were provided to me. I had to form a view as to whether they were fit for purpose...Yes, I allowed that information to go the Council together with DLA Piper's

¹¹¹ Transcript of oral evidence of Andrew Fitchie 10 October 2017, pages 194:24 to 196:1

¹¹² Transcript of oral evidence of Andrew Fitchie 11 October 2017, pages 85:21, 85:23 and 85:25

¹¹³ Transcript of oral evidence of Andrew Fitchie 11 October 2017, page 86:5- 12

letter which we've discussed"¹¹⁴. As referred to below, however, the relevant passages reflected the understanding of officers at TIE of the position.

The understanding of TIE and the Council in respect of Schedule part 4

3.72 It is not controversial that TIE and the Council broadly speaking understood prior to formation of the Infraco Contract that Schedule part 4 contained Pricing Assumptions which if they did not hold true, might result in additional time and/or money being awarded to the Infraco¹¹⁵. However, it was the evidence of witnesses from TIE and the Council that their understanding prior to contract formation was that the risk of normal design development sat with Infraco.

3.73 In its written submissions of 27 April 2018, DLA asserts that "*DLA had made tie and CEC aware of the relevant risks, in particular, the risks associated with the Pricing Assumptions, risk of MUDFA delay and SDS design delay...both tie and CEC understood these risks*"¹¹⁶. Notwithstanding this assertion, DLA's written submissions contain no reference to any evidence to support the proposition that DLA made tie or the Council aware of the risks associated with, in particular, Pricing Assumption No. 1, or that tie and the Council understood those risks, other than the testimony of Mr Fitchie which is at odds in this respect with the evidence of the tie and Council witnesses referred to below.

¹¹⁴ Transcript of oral evidence of Andrew Fitchie 11 October 2017, pages 86:15 to 87:9

¹¹⁵ See for example page 41 of the witness statement of Steven Bell at TRI00000109

¹¹⁶ Paragraph 18 of the written submissions of DLA dated 27 April 2018

- 3.74 DLA also asserts in its written submissions of 27 April 2010 that "*The CEC legal officials who testified after Mr Fitchie (Lindsay and MacKenzie) broadly accepted that, if one reads the whole suite of documents, then one is left in no doubt about the risks being assumed by tie relative to the various pricing assumptions...Accordingly, it may be that, in the end, not much really turns on the criticisms levelled at Mr Fitchie*"¹¹⁷. DLA have not provided any references to specific passages in the oral testimony of Ms Lindsay or Mr Mackenzie, but DLA's "broad" summary of their evidence is not accurate.
- 3.75 DLA accepts that it was DLA's responsibility to make tie and the Council aware of the relevant risks, including the risks associated with the Pricing Assumptions¹¹⁸. Ms Lindsay's oral testimony was that the Council relied on DLA to provide advice about the risks being assumed by tie relative to the various pricing assumptions¹¹⁹, and as referred to above under the heading "*Reliance by the Council on DLA*". Mr Mackenzie's evidence was that "*the decision had been taken to use Andrew Fitchie and DLA*"¹²⁰. DLA's advice was inaccurate and incomplete, for example as referred to above under the heading "*DLA's letter of 12 May 2008 to the Council and TIE*". As referred to below, neither tie nor the Council understood the extent of the risks associated with Pricing Assumption No. 1.

¹¹⁷ Paragraph 19 of the written submissions of DLA dated 27 April 2018

¹¹⁸ Paragraph 18 of the written submissions of DLA dated 27 April 2018

¹¹⁹ See for example pages 20:18, 27:24, 191:23, 192:15-16, 195:2 of the transcript of oral evidence of Gill Lindsay dated 27 October 2017

¹²⁰ Transcript of oral evidence of Colin Mackenzie dated 26 October 2017, pages 48:24 to 49:9

- 3.76 In this context, DLA asserts that it "*was not DLA's place to second guess tie on commercial matters*" because "*Only tie could know the commercial significance of the risks that it had agreed to take on*"¹²¹. The issue is that, because of the inaccurate and incomplete advice that had been given by DLA, tie did not understand the risk that it was taking on through the operation of Pricing Assumption No. 1. tie would not evaluate a commercial risk that it understood to lie with Infraco. DLA had a duty to provide legal advice, and it failed to discharge that duty.
- 3.77 DLA also asserts in its written submissions that certain communications involving tie and the Council evidence that individuals at those organisations understood the risks associated with Pricing Assumption No. 1¹²². The communications relied on by DLA do not support such a proposition. By way of example:
- 3.77.1 DLA relies on a file note said to record the terms of a conversation between Andrew Fitchie and Geoff Gilbert on 11 March 2008, but which was apparently produced on 23 February 2011¹²³. That note states "*Discussed with GG: all risk with tie; tie need to be very sure what the BCA are*". The document was not produced in compliance with paragraphs 32 to 34 of the Inquiry's Direction No. 10. It was not mentioned in the evidence of either Mr Fitchie or Mr Gilbert. However, taking its terms at face value, it in no way supports the proposition that Mr Fitchie explained the risks associated with Pricing Assumption No. 1.

¹²¹ Paragraph 70 of the written submissions of DLA dated 27 April 2018

¹²² See for example paragraphs 77 to 84 of the written submissions of DLA dated 27 April 2018

¹²³ See paragraph 83 and footnote 116 in the written submissions of DLA dated 27 April 2018

- 3.77.2 DLA relies on a marked up revision of an early version of Schedule part 4, which subsequently underwent significant and numerous revisions, as demonstrating that Bob Dawson and Tom Hickman "*fully understood what this document and its legal consequences*"¹²⁴. That is plainly incorrect on a proper reading of that document.
- 3.78 DLA's written submissions also conflate, on one hand, the position in respect of the risks associated with Pricing Assumption No. 1, and on the other hand, risks associated with consents/approvals, or the rate of progress of the production of the SDS design.
- 3.79 By way of example, DLA relies on an email dated 29 January 2008 from Nick Smith to Gill Lindsay, copied to Colin MacKenzie¹²⁵ as support for the apparent proposition that "*the CEC lawyers, and officers from City Development, were well aware of the state of the SDS design and the potential for "serious risk of increased cost to the project" which were "unquantified". Mr Smith also acknowledges that it would be "impossible" to require all drawings to be approved before financial close*"¹²⁶. This section of DLA's submissions appears under the heading "*Schedule Part 4 and Pricing Assumption 1*". In fact, the email in question is headed "*Consents issue*" and relates to "*the consents and approvals issue*". DLA's submissions conflate the question of consents and approvals to be issued by the Council in its capacity as a local authority, with the question of the development of the design from BDDI

¹²⁴ Paragraph 77 of the written submissions of DLA dated 27 April 2008 and document CEC00592615

¹²⁵ CEC01395151

¹²⁶ Paragraph 76 of the written submissions of DLA dated 27 April 2018

to IFC as provided for by Pricing Assumption No. 1. The email makes no reference to the risk allocation issues addressed by Pricing Assumption No. 1¹²⁷.

3.80 Reference is further made to the written submissions dated 27 April 2018 on behalf of Selected Ex TIE Employees ("SETE") at pages 70 to 74 which support the Council's submissions in this respect.

TIE's understanding

3.81 A number of witnesses, formerly of TIE, gave evidence that their understanding at the point of formation of the Infraco Contract was that risk associated with design development was transferred to Infraco. They could not recall any advice having been given by Andrew Fitchie, or anyone else at DLA, to the contrary¹²⁸. In particular, evidence was given by the following witnesses, each of whom is dealt with in turn below:

3.81.1 Steven Bell

3.81.2 Willie Gallagher

3.81.3 Kenneth Hogg

3.81.4 Susan Clark

¹²⁷ See also for example paragraphs 107 and 113 of the written submissions of DLA dated 27 April 2018

¹²⁸ In his oral evidence, Mr Fitchie referred to advice having been given to Willie Gallagher, Steven Bell, Geoff Gilbert, Jim McEwan, Dennis Murray, and possibly also Graeme Bissett; Transcript of oral evidence of Andrew Fitchie 11 October 2017, page 77:25 to 78:5 – the evidence of each of these individuals, together with a number of others is addressed in this section of the submissions

3.81.5 Graeme Bissett

3.81.6 Geoff Gilbert

3.81.7 David Mackay

3.81.8 James McEwan

3.81.9 Stewart McGarrity

3.81.10 Dennis Murray

3.81.11 Brian Cox

3.82

3.83 **Steven Bell**

3.83.1 Steven Bell's evidence in relation to his understanding in respect of the risk allocation in respect of design development was that: "*Design development was the responsibility of the contractor in the construction contract and you would expect that to be the fine tuning of practical solutions and buildability changes. This was a contentious area on this project but it was clear at this point in time [December 2007, after execution of the Wiesbaden Agreement] that the design development TIE expected the contractor to complete would not attract any additional cost or time... If there was a fundamental piece of design that was not complete - Picardy Place, again, I would pick on because it required a major input from the Council and a change that was driven by a third party - that was clearly the client's responsibility and not the responsibility of Infracore. We would discuss with them what the effects*

*would be and there would be an appropriate price adjustment whether up or down depending on whether there was a deduction or addition in scope*¹²⁹. Steven Bell's understanding was that the principle of how incomplete design would be dealt with in the Infraco price "goes back to the Wiesbaden agreement. The principle was set out there and I would expect normal design development to continue from that point and to be part of the original price that was included. If there is a significant change in principle or if a third party requires a change then that is not the Infraco's responsibility. That is a TIE responsibility under the contract"¹³⁰.

3.83.2 This was confirmed by Steven Bell in his oral evidence to the Inquiry: in relation to clause 3.3 of the Wiesbaden Agreement¹³¹, Mr Bell stated "My reflection at the time was that that was intended clearly to - ensure normal design development in completion of design was the contractor's responsibility. If it was beyond normal design development, then that was likely to be a client change...The phrase...was read by me and my colleagues that if there were significant changes to design principle, or outline specification, it rightly would be beyond normal design development. The contract set out Employer's Requirements that SDS were producing a detailed design for. It wasn't all complete, as you've already said, and our expectation was that the experienced design and construction contractor would interpret the status of those, whether it was nearly finished or whether it was early in its development, expect to

¹²⁹ Witness statement of Steven Bell TRI00000109, page 31; see also page 48 of the statement

¹³⁰ Witness statement of Steven Bell TRI00000109, page 39

¹³¹ CEC02085660

*achieve the ERs, and if there was a change in principle, outline specification of significance, then that would be a change. If it was just the normal process of completing design, then we would expect that to be included within the price and we thought that was the language that was covered there. It has been tested at length after the fact, but certainly at that time that was our very clear understanding of the mechanics*¹³².

3.83.3 As referred to above, it is not controversial that TIE understood that the Pricing Assumptions might be engaged. However, TIE's expectation was not that this would be in respect of design development, and further that it would be of an order that could be contained within the risk allowance: reference is made to the witness statement of Steven Bell:

"...I was expecting some of those Pricing Assumptions not to be met, for example, we knew the design programme was different at that point because it was baselined at V26 and we were likely to be dealing with either a V29 or V30 around then so there would be an immediate Notified Departure associated with that. It was likely that the provisional sums would be a different number because the whole point is they are a provisional sum, they are only an assessment. They might have gone up or they might have gone down and that was one of the reasons for identifying them as such and understanding some of the risk items. I would have expected, subject to all parties delivering what they were supposed to in utilities, to have seen some re-sequencing that would have had some impact on the Infracore. I would have expected it to be

¹³² Transcript of oral evidence of Steven Bell 24 October 2017, page 30:6 to 31:13

*minor and containable within the overall risk allowance for delay. I would also have expected, if any third party stakeholder or the Council had come along saying they wanted to change the fundamental scope of works, for Infracore to do the works but it for that to come from a separate budget, not the tram budget*¹³³. It is notable that Steven Bell does not make reference to design development in terms of Pricing Assumption No. 1¹³⁴.

3.83.4 Steven Bell addresses his understanding of the meaning of Pricing Assumption No. 1 at pages 73 to 74 and 77 of his witness statement as follows:

*"As drafted and as per my email in April to Andy Conway*¹³⁵ *we had Base Date Design Information (BDDI) which was all the information that was known about and shared in November 2007. In some cases designs were complete at that point, in other cases they were part way through; in one or two cases they were quite early in their process. I would have expected the principles of the design were clear in each of those examples on how the design was to be concluded. They would have done an outline design principle statement in the first place, and it would set out how they would try to solve any problem. That would include detailed or outline drawings showing what it might look like. If that progressed to conclusion I would expect that to be normal design development and what we expected the design and construction contractor to complete within their construction works price. If, for any*

¹³³ Witness statement of Steven Bell TRI00000109, page 69

¹³⁴ See also pages 71 to 73 of Steven Bell's witness statement at TRI00000109

¹³⁵ TIE00017426

reason, the designer had to amend fundamentally their specification, shape or form we would expect that to be a change. The vast majority of what I expected from that design phase would be to continue under a normal design development. The Infraco had the chance, through the bidding period, from January 2007 right up to November 2007 to understand how matters were progressing. They had a clear understanding of exactly where the design was, they made comments about what they saw as completed detailed design, it was reasonably detailed design and they did not have a particular problem with that. Their fundamental issue was that it was not all complete so it did not allow them to be certain on the price. I thought we were dealing with that very fairly with the approach on normal design development. That was my clear understanding of the purpose of that language and determines the contract under Section 3.4.1 and Schedule Part 4. It came from the Heads of Terms written at Wiesbaden in December 2007 so it was no new language. It was the understanding and expectation that TIE and CEC had always discussed and anticipated. It certainly was not explicitly highlighted by the Infraco that they had an interpretation that meant any minor change was going to be argued as being beyond normal design development. For normal design development I want them to finish off the job and if they have got some fine-tuned tweaks that they can make it better or cheaper to build and still satisfy what we need, that would be a benefit they retained. Equally, I was not expecting them to come with their hand out for every penny "extra". Infraco interpreted the final version of this clause in such a way

that there was virtually nothing in their view that fell under the terms of normal design development and everything in their view was a TIE change. Therefore, they felt they were entitled to argue for additional time and additional money. This was one of the major areas of dispute between us and that emerged from probably late 2008 onwards. It was not evident to TIE and CEC when we signed the contract....

We certainly did not expect the level of Notified Departures via Clause 3.4.1 over design development that eventually arose. My expectation was they would not submit claims associated with what would be determined normal design development. Infraco clearly took a different interpretation to that"¹³⁶.

3.83.5 These matters were also addressed in Steven Bell's oral evidence¹³⁷ in the context of the period between March and early May 2008:

"I do recall then and thereafter that DLA's view was that our interpretation of Pricing Assumption 1 and normal design development meant that that risk was a matter for the Infraco, and when it went beyond that, it was a matter for tie; and that was supported as we prepared for emerging disputes that happened later in 2009 and beyond, or 2008 and beyond, after contract close...I believe DLA were clear around how we were interpreting it, and they supported our risk transfer and approach...They had -- as we'd gone through each of those drafting points and items, where Andrew and his team were clear

¹³⁶ Witness statement of Steven Bell TRI00000109, pages 73 to 74 and 77; Reference is also made to pages 95:15 to 97:24, 107:16 to 112:12 and 145:20 to 146:21 of the transcript of oral evidence of Steven Bell 24 October 2017, and page 87 of his witness statement

¹³⁷ Transcript of oral evidence of Steven Bell 24 October 2017, pages 45:23 to 50:12

that if there was another matter that caused them concern, they raised it with us. They – used a Notified Departure example. He said: are you quite clear at this point that you -- this gives you a statement of fact and deals with it that a change has occurred? Are you clear on that and therefore you then have to apply through the tie mechanism how that would be valued or any impact of it. So where he was clearly identified that there was an area of concern as we had gone through it, he raised those items. Those would be examples for me where he was specifically flagging a concern he had....I certainly recall in conjunction with some of my colleagues, and Andrew and others, the clear view that normal design development would be for the Infraco's risk. Beyond that would be for tie's risk. And that was the debate that we had at that time.... this is certainly an area I'm very clear that for a number of years, not just a number of months, DLA supported our -- as in tie's -- position in the interpretation of that pricing assumption through 2008/2009, and I don't believe it was -- alternative legal position was tested on that until 2010¹³⁸.

3.83.6 Steven Bell also gave oral evidence in relation to the assertions made in Andrew Fitchie's statement¹³⁹ in respect of Pricing Assumption No. 1:

"A. I recall receiving advice from Andrew around work beyond normal design development, but not that that drafting included normal design development...

¹³⁸ Transcript of oral evidence of Steven Bell 24 October 2017, pages 46:4 to 50:12

¹³⁹ TRI00000102

Q. So is it your position that Mr Fitchie is simply wrong when he says he gave you that advice?

A. That is certainly not my recollection. I believe that he's recalled that incorrectly...

Q. In paragraph 7.295 [of Andrew Fitchie's witness statement] we see "Steven Bell considered that with "normal design development" a contractor would expect and include for some elaboration of design in the journey to 'Issued for Construction' drawings. In the industry, he reasoned, this would rarely be considered to be design development of the sort that PA1 was written to capture. We identified there were different ways of reading the language on normal design development in PA1 and I gave my view that BBS were likely to exploit this." Do you remember him saying that?

A. In relation to this specific item, no. He did make some general comments around he believed that BBS were likely to seek to optimise any contractual opportunities available to them, but I don't recall it in the way that he's described it in his statement, no.

Q. Is it possible that Mr Fitchie advised you before contract close that BBS were likely to exploit the language of Pricing Assumption 1?

A. In that way, no.

Q. It's simply not possible he gave such advice?

A. I don't believe he did, and I don't recall any such advice on that specific point...

Q. Look, please, at the next paragraph, 7.296: "I was not in a position to gainsay Steven's view as 23 an engineer - but I knew that due to Germany's risk aversion that BBS were going to be adversarial in operating the contract and I said so." Did he say that to you?

A. He didn't -- I don't recall the word "adversarial". As I said to you a moment ago, I believe that he expected a robust application of the contract in the number of areas. I do recall him saying that. I can't remember if it was then or thereafter, but I do recall him saying that.

Q. The next paragraph, please. 7.297. This is later on, and I will come back to look at this email, but this refers to Mr Fitchie. He says: "I sent a specific email about SP4 to Jim McEwan on 31 March 2008." ...about four or five lines down, Mr Fitchie 15 says: "I had had a further discussion with Steven Bell at around this time concerning SP4 and SDS design development; this resumed after Rutland Square and I explained that we had secured agreement to remove certain limbs from PA1 but I still had serious misgivings about how post-BDDI SDS design development time and cost responsibility now sat squarely with TIE..." So to pause there, what Mr Fitchie is saying is that he had a conversation with you in March 2008 that he has serious misgivings about how post BDDI SDS design development time and cost responsibility now sat squarely with tie. So that's completely different to

tie's interpretation of Pricing Assumption 1 that you explained to us earlier, isn't it?

A. As Andrew stated, yes, his view as he stated there, I don't recall him having that discussion with me at that time. I do recall talking about design development time and the issue of an immediate Notified Departure between completion of SDS design packages, and that's where we discussed the Notified Departure mechanism....I certainly don't recall the language that Andrew has used there, and indeed, I think is part of some of the Rutland Square discussions. This issue around design development time touched on quality of submissions by SDS, and there was a specific acceptance in one of those agreements that that was a risk that BBS were prepared to take. So that resume is incorrect for me.

Q. So in short, Mr Fitchie's position is that in 24 February 2008, and again in March 2008, he has told you of his concerns in relation to Pricing Assumption 1 and that in fact that Pricing Assumption gives rise to serious risks for tie. That's his position....You are saying that neither of these discussions or conversations happened?

A. We had a discussion about the design development time issue, and we acknowledged that there was going to be a Notified Departure associated with that, and that was going to be an additional cost over and above the proposed contract works price at that time...

Q. But in relation to the risks more generally arising from Pricing Assumption 1 --

A. Absolutely don't agree with Andrew's point there, and this issue of cost responsibility and normal design development is one we've already touched on, but we were very clear, and I do not believe Andrew came back to me at that time with that particular point again.

Q. If we then please go to page 190....In paragraph 7.319, at the bottom, Mr Fitchie 3 states: "I discussed the effect of PA1 directly with TIE once more at the latest on 9 April 2008 (with TIE management personnel), after SP4 sessions finished on or around 20 March 2008, immediately after TIE had been confronted by a further serious price increase demand off the back of Network Rail immunisation works. I wanted to alert the responsible TIE managers again to the magnitude of the change in risk allocation plus the demand for more money ... I said that TIE should consider stopping the procurement. They understood what I was saying and I repeated that advice to a full TIE management meeting if not that day, 9 April, in the next TIE management meeting - probably Monday, 11 April." I take it, Mr Bell, you attended these tie

18 management meetings?

A. I attended, yes, a number of tie management meetings. I don't recall that particular session per se...

24 Q. So what Mr Fitchie is saying is that in April he again alerted tie managers to the magnitude of the change in risk allocation in relation to Pricing Assumption 1. Do you remember him saying that?

A. In that language, no, I do not.

Q. Well, in any similar language?

A. No¹⁴⁰.

3.83.7 This evidence contradicts the assertion made by DLA in its written submissions that there was no challenge of Mr Fitchie's evidence¹⁴¹ in relation to the meeting said by DLA to have taken place on 9 April 2008, and recorded in a file note dated 9 April 2010.

3.83.8 Furthermore, the understanding which Steven Bell has described in his evidence, as referred to above, was wholly consistent with TIE's strategy in respect of the transfer of risk to Infracore, and DLA was well aware of this. Reference is made to the oral evidence of Steven Bell, in which he said:

"The strategy of tie at this time was to pass to Bilfinger the risk for normal design development?"

A. Yes.

Q. And tie's understanding of what normal design development was, was it was everything apart from the unforeseeable?

A. Particularly matters that could be moved to completion from the current design status as viewed by an experienced design and build civil engineering contractor...

Q. Was that strategy one which DLA were well aware of?

¹⁴⁰ Transcript of oral evidence of Steven Bell 24 October 2017, pages 52:19 to 60:5

¹⁴¹ Paragraph 20 of written submissions of DLA dated 27 April 2018

A. Yes.

Q. *So was it therefore tie's strategy...that any changes additional to Base Date Design Information that were consequent upon Employer Requirements should fall to BBS as at their risk?*

A. *Yes, generally. Clearly if there's a specific example, BBS intimated that we would review that on the base of its individual facts, but generally you're correct.*

Q. *...At any stage did anyone at DLA say to you: you haven't achieved that objective of transferring risk for completing Employer's Requirements, effectively, to BBS?*

A. *No, that wasn't stated...*

Q. *Your understanding was that the strategy at tie was to transfer all of that risk for normal design development to BBS; is that correct?*

A. *That's correct...*

Q. *..."normal development and completion of designs means the evolution of design ... and excludes changes of design principle, shape and form and outline specification." That's exactly the opposite of the strategy that tie was trying to pursue, isn't it?*

A. *Yes...*

Q. *Did you notice this problem in the document when you read it at the time?*

*A. I read it understanding it to enact the transfer of risk that we identified for normal design development. I didn't read it in the way that was subsequently tested in a number of disputes, and highlighted the difficulty in reading it...*¹⁴²

3.84 **Willie Gallagher**

3.84.1 Willie Gallagher gave evidence¹⁴³ in relation to the question of advice given by Andrew Fitchie:

"Q. Andrew Fitchie says in essence that he gave you advice that this [Pricing Assumption No. 1] had the effect of transferring all the risk back to tie for design development. And that it gave rise to unquantified risks on the part of tie?

A. No, not the case.

Q. Did he give you that advice?

A. No. If Andrew had given me that advice, then Andrew would have been asked to give that advice not to me, but to the Board, and also, Andrew attended as DLA attended all the Tram Project Board meetings. He attended all the working sessions. And Andrew was asked to present at all times his considered and impartial view of where we were. There was no attempt to somehow fetter or water down whatever the view that Andrew had. Andrew was part of the team and Andrew was expected to contribute in that way. If Andrew had said: don't sign this contract; then that would have been listened to.

¹⁴² Transcript of oral evidence of Steven Bell 24 October 2017, pages 76:13 to 81:8

¹⁴³ Transcript of oral evidence of Willie Gallagher 17 November 2017, pages 114:8 to 115:22

Q. ...He says he advised prior to the actual signature of the contract in May that tie should pause and not sign until matters were clarified. Do you recall that advice?

A. No. And if he was giving that advice, he had the opportunity to give that advice not just to me. He would have had the opportunity to give that advice to the Board. I mean, my style of management is not to focus everything through myself. I expect the specialists who are responsible for their areas to take responsibility for their areas and speak up. We were hugely reliant in this process on DLA, and also on particularly Matthew, Geoff and Steven, because these were the people who had been involved in procuring systems like this before and also involved in the contractual side of this before. For the rest of us, this was our first tram project. So if our legal advisers or if our procurement advisers had raised even a hint of a red flag, then we would have listened"¹⁴⁴.

3.85 Kenneth Hogg

3.85.1 Mr Hogg's evidence was that at contract close his "*understanding was that the risk for what was termed normal design development transferred from tie to the consortium and specifically Bilfinger Berger...*"¹⁴⁵ He explained that by "*normal design development he meant "that the evolution of designs for the physical infrastructure for the project became the responsibility of the contractor with the exception of changes which would be deemed to be beyond...normal*

¹⁴⁴ Transcript of oral evidence of Willie Gallagher 17 November 2017, pages 114:8 to 115:22

¹⁴⁵ Transcript of oral evidence of Kenneth Hogg 13 December 2017, pages 98:24 to 99:2

*design development. So, for example, had tie decided to change the fundamental design of station stops or had tie decided that they wanted a different sort of bridge at the airport, those would -- those would clearly be developments beyond normal design, but normal design development in line with the scheme proposed that a signature would transfer -- my understanding was that that would transfer to the contractor*¹⁴⁶.

3.85.2 Mr Hogg's evidence was that the information in relation to the risk transfer having been achieved at contract close "*came from discussions and papers at the March, April and May tie Board meetings. Information that was provided by both the tie executive team and by the...lawyer involved in this from DLA Piper*"¹⁴⁷ provided to him as a Board member. He gave evidence that at the Board meeting in March 2008 "*there was a very thorough examination of the...deal on the table which had emerged from the Wiesbaden conversations and we developed subsequently. Particularly around risk and around the extent to which this was a fixed price contract. In that discussion I asked questions of both the executive team and directly to the lawyer from DLA Piper....Andrew Fitchie. As did other non-Executive Directors, about the...matters which we're discussing, including the extent to which this was a fixed price contract, what was excluded from that, and the extent to which design risk had been successfully transferred through the*

¹⁴⁶ Transcript of oral evidence of Kenneth Hogg 13 December 2017, page 99:5-17

¹⁴⁷ Transcript of oral evidence of Kenneth Hogg 13 December 2017, page 100:19-22

contract as agreed and discussed in the December discussions in Wiesbaden"¹⁴⁸.

3.85.3 Mr Hogg also addresses the meeting of 12 March 2008 in his witness statement, saying:

"My recollection is that at that meeting on 12 March 2008, myself and other non-executive directors specifically asked to what extent this was a fixed-price contract. The answer repeatedly given was 95 per cent fixed price and that was a view also endorsed by Andrew Fitchie, who was a partner in DLA Piper, the law firm who was advising the TIE board on this contract. One of the things the TIE Board was told was that the deal that was signed at contract close in May 2008 bought out additional risk in relation to design development compared to the initial version because the risk was novated to the Infraco contract, which should have been signed in January 2008 under the original project timetable...

My recollection of the discussion in that meeting is that I and the other non-executive directors, including Peter Strachan, specifically asked and pressed on to what extent this was a fixed-price contract. The answer repeatedly given was that it was a 95 per cent fixed price contract. That view was endorsed by Andrew Fitchie of DLA Piper who were the legal firm advising TIE and acting on behalf of TIE in drawing up and agreeing this contract"¹⁴⁹.

¹⁴⁸ Transcript of oral evidence of Kenneth Hogg 13 December 2017, page 101:4-20

¹⁴⁹ Witness statement of Kenneth Hogg TRI00000045, page 35 and page 69

3.85.4 Mr Hogg gave oral evidence of his understanding that the Infraco Contract price was 95% or 96% fixed:

"My view was that the price increases were a consequence of changes in the contract. So, for example, the GBP10 million increase in the price from GBP498 million to GBP508 million, which resulted from the December Wiesbaden discussions, delivered additional benefits to tie. Specifically...my understanding was it increased the fixed price element from 77 per cent of the overall value of the contract to 96 per cent; secondly, that it would provide for the transfer of normal design development risk to the contractor. And that therefore that GBP10 million increase was a price to achieve those elements..."¹⁵⁰

But I can't remember ever being told that the fundamental basis of our understanding for this contract, which was that it was a 95 per cent fixed price contract, negotiated through the Wiesbaden deal, and indeed reinforced in the final May negotiation when yet further risk was bought out, that that was fundamentally wrong"¹⁵¹.

3.85.5 Mr Hogg confirmed in oral evidence that he was not advised that the Pricing Assumptions transferred risk to TIE:

"Q. Was it ever suggested to you, either by the Executive or by legal advisers, that in fact the terms of Part 4 of the Schedule to the Infraco contract, and in particular the Pricing Assumptions that it contained,

¹⁵⁰ Transcript of oral evidence of Kenneth Hogg 13 December 2017, pages 105:4- 15

¹⁵¹ Transcript of oral evidence of Kenneth Hogg 13 December 2017, page 147:3- 9; see also paragraphs 81 and 85 of Kenneth Hogg's witness statement at TRI00000045

would have the effect of transferring risk back to tie and creating a very substantial liability?

A. No. That understanding was only made available to me in January of 2011, when I was in receipt of other legal advice which had re-examined those contractual provisions¹⁵².

3.86 Susan Clark

3.86.1 Susan Clark gave evidence in relation to her understanding of Pricing Assumption No. 1: on 16 April 2008, she wrote in an email to Andy Conway¹⁵³ "Normal design development is a BBS risk as described in Schedule 4 of the Infraco Contract". In her oral evidence, Susan Clark said:

"A. ...I would have written that email on the advice of the people who were negotiating those clauses of the contract....

Q. So that represented your understanding of the views of 4 those involved at the time?

A. Yes...

Q. ... Mr Fitchie has also given evidence that he said: "I discussed the effect of Pricing Assumption 1 directly with tie once more on or around 9 April 2008. I wanted to alert tie managers again to the magnitude of the change in risk allocation. I said that tie should consider stopping the procurement. They understood what I was saying, and I repeated that

¹⁵² Transcript of oral evidence of Kenneth Hogg 13 December 2017, page 101:21 to 102:5

¹⁵³ CEC01245274

advice to a full tie management meeting, if not that day, 9 April, then the next tie management meeting, probably Monday, 11 April 2008." Now, did you generally attend tie management meetings around that time?

A. I would, yes.

Q. Do you have any recollection of Mr Fitchie giving such advice at a management meeting around that time?

*A. No*¹⁵⁴.

3.86.2 This evidence contradicts the assertion made by DLA in its written submissions that there was no challenge of Mr Fitchie's evidence¹⁵⁵ in relation to the meeting said by DLA to have taken place on 9 April 2008, and recorded in a file note dated 9 April 2010.

3.86.3 Susan Clark's evidence in her witness statement in relation to her understanding of the meaning of Pricing Assumption No. 1 at the time of contract close was that "*At the time I understood this to mean that Infracore took the risk [of] normal completion of the base date design but not for changes to this (other than Value Engineering changes). However, this was tested extensively during the subsequent dispute process*"¹⁵⁶.

3.87 Graeme Bissett

3.87.1 Graeme Bissett's oral evidence in relation to the wording in Pricing Assumption No.1 relating to "normal design development" was:

¹⁵⁴ Transcript of oral evidence of Susan Clark 25 October 2017, pages 151:25 to 153:18

¹⁵⁵ Paragraph 20 of written submissions of DLA dated 27 April 2018

¹⁵⁶ Witness statement of Susan Clark TRI00000112, page 40

"A.... my reading is for normal design development, which would be understood by both parties that was a firm price, but if design development was not normal, then it wouldn't be a firm price, and then there were consents and approvals dimensions over and above.

Q. If it was suggested to you that tie management had been advised by Andrew Fitchie that this was not the case, and that the design risk had not been transferred, what would your response be?

A. That wasn't my understanding at the time.

Q. Had you given advice to you to that effect?

A. I don't recall any, no.

Q. Do you think it's likely that if it had been different, you would recall it?

A. I think I would have recalled it, yes"¹⁵⁷.

3.88 Geoff Gilbert

3.88.1 Geoff Gilbert gave oral evidence in relation to his understanding of Schedule part 4 in the period leading to contract close:

"Q. If you'd been given advice that this failed to effect a transfer of risk to the consortium and that the effect of it was that tie would retain the design risk, would that have been important advice to you?

A. It would have.

Q. Do you think it likely you would remember that advice?

¹⁵⁷ Transcript of oral evidence of Graeme Bissett 31 October 2017, page 176:9- 24

A. I think I would, yes.

Q. What would you have had to do if you had had that advice?

A. In the first instance, I would have discussed it with Matthew Crosse, Project Director, and others, and then gone back to Richard Walker and say: this is not the intent of the Wiesbaden Agreement.

Q. Would you just have carried on to negotiate the agreement in that form and then concluded it in that form?

A. I don't believe so; no"¹⁵⁸.

3.88.2 Mr Gilbert further gave evidence that he could not recollect any discussion with legal advisers about the exclusionary wording at the end of Pricing Assumption No. 1:

"Q. The effect of this wording is that there is now no exception really for normal development of design....Was that the subject of any discussion with legal advisers on tie's part?

"A. Not that I recollect"¹⁵⁹.

3.88.3 Mr Gilbert also gave evidence about the advice received from DLA in the context of the draft Report on Terms of Financial Close, version 6 dated 9 March 2008¹⁶⁰:

"Q. ... look at page 4 of this, please. If we look at the final paragraph on the page, we see: "In broad terms, the principal pillars of the

¹⁵⁸ Transcript of oral evidence of Geoff Gilbert 19 October 2017, page 141:1- 17

¹⁵⁹ Transcript of oral evidence of Geoff Gilbert 19 October 2017, page 189:18- 23

¹⁶⁰ CEC01463886

programme suite in terms of programme, cost, scope and risk transfer have not changed materially since the approval of the Final Business Case in October 2007. It is felt that the process of negotiation and quality control has operated effectively to ensure the final contract terms are robust and that where risk allocation has altered this has been adequately reflected in suitable commercial compromises." Dealing with ...the first half of the paragraph initially, the statement that risk transfer has not changed since October 2007, is that your view?

A. I don't recall my view at the time. But I think that on the basis of what we discussed in terms of transferring the design development risk, then broadly speaking, it was the same.

Q. Where did the design development risk lie in terms of the draft we've been looking at?

A. Do you mean at the time that the close report was prepared?

Q. Yes.

A. I believe that it lay with Infracore.

Q. You hadn't had any advice warning that it in fact lay with --

A. No.

Q. With tie...

Q. Did you understand there to be significant risks imposed on tie as a result of the wording of Schedule Part 4

A: No...

Q. So in terms of who bore the risk of design development, what do you think someone reading this would understand was the position? Where did that lie?

A. With the Infracore.

8 Q. Was that your understanding at the time?

9 A. I think it was¹⁶¹.

3.88.4 Similarly, in the context of an email dated 22 April 2008 from Dennis Murray¹⁶² and its attachment¹⁶³, which included Pricing Assumption No. 1 as it then stood, Geoff Gilbert stated in his oral evidence:

"Q. Even at this stage, did Andrew Fitchie provide any advice to you as to the effect of this?

A. Not that I recollect.

Q. Did he advise that this would expose tie to liability in the form of a number of Notified Departures?

A. Not that I recollect.

Q. Did he advise that you would be put on risk as to design changes would be paid for by tie?

¹⁶¹ Transcript of oral evidence of Geoff Gilbert 19 October 2017, pages 209:15 to 215:9. Similar comments are made in relation to the draft of the report dated 10 March 2008 (CEC01428734) at pages 215:20 to 217:2 of the transcript of Geoff Gilbert's evidence

¹⁶² CEC01374219

¹⁶³ CEC01374220

A. Not that I recollect.

24 Q. Would that advice have been material to you at the time?

25 A. I think it would.

Q. Is it likely that you would have recollected that if it had been said to you?

A. I think I would have, and if it was advice of that significance, then I would imagine it would have come in written form"¹⁶⁴.

3.88.5 Geoff Gilbert's evidence was that he could not recall any advice from DLA (or from Andrew Fitchie specifically) that it would be appropriate to put the Project on hold rather than proceeding with the Infraco Contract, in the context of the design not being complete¹⁶⁵.

3.89 **David Mackay**

3.89.1 David Mackay gave evidence that he was not informed by Andrew Fitchie that Schedule part 4 operated to transfer significant risk to TIE:

"Q. You can take it from me that there has been a suggestion made to the Inquiry that that Schedule effected a significant transfer of risk to tie away from the consortium. There was evidence also that that Schedule was negotiated certainly between January and May 2008, which would mean, if those were both correct, that there had been a material change in the allocation of risk in this period.

¹⁶⁴ Transcript of oral evidence of Geoff Gilbert 19 October 2017, pages 204:15 to 205:5

¹⁶⁵ Transcript of oral evidence of Geoff Gilbert 19 October 2017, page 77:10-18

A. I certainly did not appreciate a material change of risk.

Q. You said you had a presentation from Mr Fitchie?

A. Yes.

Q. I have to put it to you directly: did he say to you that in fact the effect of Schedule Part 4 was to transfer risk, a significant risk, to tie?

A. If Mr Fitchie had said that to me, I would be able to tell you that. He did not say that to me. May I add, he would not only -- if he was saying that, he wouldn't only say it to me. He would be saying it to other directors of the businesses....And, furthermore, I would have expected to see it in writing...

Q. So you really have very little chance to ask questions about this?

A. Yes. Nor did I appreciate the seriousness of...The Schedule 4 Pricing Assumption...

Q. What did you understand by "fixed price"?

A. That a large element of the contract was fixed price, but design changes would incur...further price movement, whether these came from tie, from the city, or from Transport Scotland.

Q. How likely did you consider it was that there would be such design changes?

*A. I had no appreciation whatsoever about how onerous that was going to be. None whatsoever. And if I had done, I would never, ever have agreed to proceed*¹⁶⁶.

3.89.2 David Mackay could not recall any advice being given to the TIE Board, the TPB or TEL that it would be unsafe or inappropriate to proceed in view of the state of the design: *"I think if Andrew Fitchie had told me or told the Board that it would be unsafe to proceed, then the Board would have taken heed of what he was saying"*¹⁶⁷.

3.89.3 Furthermore, in his witness statement, Mr Mackay stated *"If we had known the seriousness of the risk associated with the issues that might arise with Part 4 of the Schedule before, the contract would never have been signed. There was no way; however, those risks could have been anticipated standing the legal advice we had on the contract"*¹⁶⁸.

3.90 **James McEwan**

3.90.1 Mr McEwan's evidence was that *"Once novated, Infracore would bear the risk of normal design development...that was unequivocal from my perspective...From our perspective"*¹⁶⁹...

"Q. ...did you even consider the issue...of whether or not this contract would successfully pass the risk of design, normal design development, to the contractor.

¹⁶⁶ Transcript of oral evidence of David Mackay 21 November 2017, page 63:19 to 67:7

¹⁶⁷ Transcript of oral evidence of David Mackay 21 November 2017, page 47:21-23

¹⁶⁸ Witness statement of David Mackay statement TRI00000113, paragraph 221

¹⁶⁹ Transcript of oral evidence of James McEwan 18 October 2017, page 125:22 to 126:2

A. Of course. Yes. Our intention and our ambition was that that's exactly what it should be.

Q. That's your intention and that's your ambition. Did you consider whether the contract was going to achieve that intention and ambition?

A. Yes...that's entirely what we thought we had achieved...¹⁷⁰.

3.91 Stewart McGarrity

3.91.1 Mr McGarrity's evidence was that prior to contract formation, his understanding was that risk associated with completion of the design had been passed to Infracore:

"Q. Did you understand that the risk of a construction cost increase arising from completion of the design had been transferred to the Infracore?"

A. That is sure what I believed at this stage. I mean, much later, of course -- it's really important for me to tell you what I thought then, because the fact that contractual flaws meant that that didn't happen much later, it's what I believed then, at this time, that counts.

Q. So when you talk here in close report about substantially achieving the level of risk transfer to the private sector, you were meaning to include within that the risk of a construction cost increase arising in the completion of the design?"

¹⁷⁰ Transcript of oral evidence of James McEwan 18 October 2017, page 133:21 to 134:9

A. Yes, except to the extent it was something that didn't fall within the definition of the normal design development provisions or fell -- and also the Employer's Requirements, because when I wrote this¹⁷¹, I had no appreciation that legally the Employer's Requirements and the normal design development provisions could be -- that there was any wedge between them, which I think it's quite important in what happened later, that distinction. So yes¹⁷².

3.91.2 Mr McGarrity's evidence was that from the time of the Wiesbaden Agreement, risk in relation to design development had passed to Infracore:

"Q. ...in relation to the transfer of the risk of construction cost increases arising from completion of the design, what was your understanding of what had been agreed at Wiesbaden?"

A. That...all of the previous...provisionally priced sums had been taken ...into firm and fixed. So that was part of the changes in the price, the pricing make-up. And that we'd paid GBP8 million, and that substantively what we'd got for that GBP8 million was the contractor had explicitly taken the risk of taking the designs from where they were to completion, forming their view of -- as experienced contractors as to what would change between the designs that they had and when they would be complete.

¹⁷¹ The close report at CEC01338853

¹⁷² Transcript of oral evidence of Stewart McGarrity 12 December 2017, page 87:5 to 88:3

Q. *How much risk did you understand tie to retain in relation to construction cost increase arising from completion of the design?*

A. *None except insofar as it fell to be outwith normal design development.*

Q. *That understanding, did that come from the briefing you got from Geoff Gilbert?*

A. Yes¹⁷³...

"...the whole issue of incomplete SDS designs had -- as far as we understood, been quite significantly amended by the Wiesbaden Agreement... As far as we were concerned, the Wiesbaden Agreement, the contractor had agreed to take design development risk, had agreed to complete the designs, and that they would pay, or their new price included for any consequence of those designs being completed under normal design development conditions...the risk of incomplete SDS design is absolutely one of the risks that I believed had been very significantly removed as a result of the Wiesbaden Agreement"¹⁷⁴.

3.91.3 Mr McGarrity gave evidence that he was not aware of any advice having been given by Andrew Fitchie or anyone else at DLA about Schedule part 4, and specifically Pricing Assumption No. 1:

"Q. Was there any discussion within tie, for example, at management meetings about advice received from DLA about Schedule Part 4?"

¹⁷³ Transcript of oral evidence of Stewart McGarrity 12 December 2017, page 143:5 to 144:2

¹⁷⁴ Transcript of oral evidence of Stewart McGarrity 12 December 2017, page 107:1 to 108:3

A. I don't recall any, I'm sorry.

Q. If there had been specific advice about Schedule Part 4, which after all was about pricing and which you as the Finance Director had an interest in, would you expect to have been made aware of that advice?

A. Yes....especially if it was advice regarding the adequacy of achieving the risk transfer objectives that I understood it to be. I would absolutely expect to be told that, as would the rest...

Q. Were you aware of any advice emanating from Mr Fitchie or DLA more generally that Schedule Part 4 carried significant cost and programme risks for tie?

A. Absolutely not.

Q. Or that the language in Schedule Part 4 on design development was not free from doubt, but obviously transferred cost and time risks back to tie?

*A. No*¹⁷⁵.

3.91.4 Mr McGarrity gave evidence that he had no recollection of a meeting referred to in an internal DLA file note dated 9 April 2010¹⁷⁶, said by Andrew Fitchie to have taken place on 9 April 2008. The note refers to one of the attendees as having been "*Howard McGarrity*": Stewart McGarrity gave evidence that he was not aware of anyone called

¹⁷⁵ Transcript of oral evidence of Stewart McGarrity 12 December 2017, page 167:14 to 168:23

¹⁷⁶ DLA00006319

Howard McGarrity¹⁷⁷, and the reference in the note is therefore taken to be a reference to him. Mr McGarrity's evidence was that he could not "recall this meeting taking place at all"¹⁷⁸. This evidence contradicts the assertion made by DLA in its written submissions that there was no challenge of Mr Fitchie's evidence¹⁷⁹ in relation to the meeting said by DLA to have taken place on 9 April 2008, and recorded in a file note dated 9 April 2010. It will be a matter for the Inquiry to determine whether the DLA file note does relate to a meeting which did take place or not. Without identifying precisely how that file note came into existence, the position of the Council is that no weight should be attached to it and that the Inquiry should find that there has been no sufficient evidence of a meeting taking place on 9 April 2008 and that the testimony of Mr Fitchie that it did take place is not supported by any other evidence and is contradicted by the evidence of other witnesses.

3.91.5 Mr McGarrity further stated:

"Q. ..."AF: Advised that this represented a major procurement risk in the light of the very slim price differential at preferred bidder appointment in December. Also advised that Schedule Part 4 already contained numerous relief/compensation/arguable risk allocation points for BB(S) - on civils work especially. Biased for Infraco. Risk of BB exploiting Schedule Part 4." Now, in light of that, do you recall advice along those lines from Mr Fitchie?

¹⁷⁷ Transcript of oral evidence of Stewart McGarrity 12 December 2017, page 169:13- 15

¹⁷⁸ Transcript of oral evidence of Stewart McGarrity 12 December 2017, page 171:4- 6

¹⁷⁹ Paragraph 20 of written submissions of DLA dated 27 April 2018

A. No, I don't.

Q. If Mr Fitchie was to have given evidence that he did give advice on these matters, what would your response be to that?

A. ...I just don't recall it...I just don't think it happened. If the lawyer...had told that group of people that in his opinion there was substantial risk coming back to tie, we would have done something about it. It just -- it would not have happened. So I can't explain this file note at all.

Q. If Mr Fitchie's evidence was to the effect that he delivered this advice, but it seemed to him that he was delivering a very unwelcome message to the tie management, what would you say to that?

A. Well, if he ever had delivered this kind of message, we wouldn't have been happy, but we wouldn't have not done something about it.

Q. What would you have done?

A. Stopped and revisited the whole issue of Schedule Part 4 and what it achieved.

Q. When you say stopped, stopped what in particular? Well, stopped the procurement. Regardless of what the consequences of that would have been, we would not have individually or collectively have made a decision to proceed if we thought or had been advised by our lawyer that the contract had these kind of flaws".

Q. Was there concern within tie that further delay in the procurement would lead to tie incurring additional costs?

A. Yes, there was concern, but -- of course, but that -- under no circumstances would that lead this group of people to collectively say...we should proceed in any case with a contract which our lawyer is telling us has flaws in it....

*I think that...there were conditions attached to the government funding, and I think there always was a risk that the government funding would be pulled, but that would not under any circumstance -- that the imperative to secure the government funding would not overrule the imperative to make sure that we were looking after public money by signing a contract that we believed was effective*¹⁸⁰.

3.91.6 Mr McGarrity gave evidence that because of what he understood the contractual risk allocation to be, the QRA at financial close¹⁸¹ did not contain an individual risk allocation item for the risk of an increase in the Infraco construction costs arising from completion of the design¹⁸². Mr McGarrity stated "*...holistically the movement between the design and the Employer's Requirements, as they existed at preferred bidder stage, and the way that that was impacted by the fact that the design was not complete by financial close, was dealt with in the contract...there's a*

¹⁸⁰ Transcript of oral evidence of Stewart McGarrity 12 December 2017, pages 171:22 to 174:25

¹⁸¹ TIE00110802

¹⁸² Transcript of oral evidence of Stewart McGarrity 12 December 2017, page 118:11-20

*number of individual risks here which you can relate to incomplete design, but there was no single risk that said design not complete*¹⁸³.

3.91.7 Similarly, Mr McGarrity stated in his oral evidence:

*"We didn't have a risk allowance for design evolution. We thought...that what this clause¹⁸⁴ did was it transferred the risk of that evolution to the contractor...The changes in design principle, shape and form and outline specification, in my simple compartmentalisation, was that would be a design change that had to go through change control. So it's a change in scope. In other words -- sorry, I know I'm over-simplifying here, but a bridge is a bridge, and when it's moving from preliminary stage to completed design, it doesn't change -- I mean, I had no appreciation either at this time or at the time that we awarded the contract that those words could be interpreted to mean any change at all as a change. I had no appreciation that that's what those words in terms of a strict legal interpretation, that that's what they would mean"*¹⁸⁵...

A. I formed the view that as far as I knew, we were properly covered.

Q. So there was a conscious decision that no additional provision was required for risk?

*A. Yes*¹⁸⁶.

3.92 **Dennis Murray**

¹⁸³ Transcript of oral evidence of Stewart McGarrity 12 December 2017, page 119:8-16

¹⁸⁴ Clause 3.3 of the Wiesbaden Agreement at CEC02085660

¹⁸⁵ Transcript of oral evidence of Stewart McGarrity 12 December 2017, pages 149:24 to 150:24

¹⁸⁶ Transcript of oral evidence of Stewart McGarrity 12 December 2017, page 153:12- 16

3.92.1 Dennis Murray confirmed in his oral evidence that he could not *"recall getting advice from DLA to the effect that the terms of Schedule part 4 presented a substantial risk to tie"*¹⁸⁷

3.92.2 Mr Murray also gave evidence that he did not *"recall getting advice [from DLA] that it would be advisable to put the procurement on hold and wait until design and other matters had caught up"*¹⁸⁸ nor *"recall getting advice from any of the legal advisers to the fact that there would be a bar on getting a fixed price deal, because they [Infraco] simply weren't interested in doing that in all the circumstances"*¹⁸⁹.

3.92.3 Mr Murray's evidence was that *"It was my understanding that the designs would be developed and completed by normal design development. My understanding was that normal design development was the risk of BBS under the contract but anything beyond normal design development would be a notified departure and additional to contract price"*¹⁹⁰.

3.93 **Brian Cox**

3.93.1 Mr Cox gave evidence that his understanding of the position was that:

"Following the novation of the SDS contract to Infraco, Infraco would become responsible for all risks associated with normal design development, but changes to design and delays in consents and approvals would be at TIE/CEC's risk. The Board was assured that the

¹⁸⁷ Transcript of oral evidence of Dennis Murray 20 March 2018, page 124:22 to 125:1

¹⁸⁸ Transcript of oral evidence of Dennis Murray 20 March 2018, page 132:8- 12

¹⁸⁹ Transcript of oral evidence of Dennis Murray 20 March 2018, page 132:13- 17

¹⁹⁰ Witness statement of Dennis Murray TRI00000063, page 15

*contract was 95% fixed price, with the remaining 5% largely known and quantifiable and allowed for in the project budget, all this however being dependent on no changes to the project specification*¹⁹¹.

The Council's understanding

3.94 A number of witnesses from the Council gave evidence that their understanding at the point of formation of the Infraco Contract was that risk associated with design development was transferred to Infraco. In particular, evidence was given by the following witnesses, each of whom is dealt with in turn below:

3.94.1 Gill Lindsay

3.94.2 Tom Aitchison

3.94.3 Andrew Holmes

3.94.4 Philip Wheeler

3.94.5 Donald McGougan

3.94.6 Lesley Hinds

3.95 In its written submissions, DLA relies upon a passage from the oral evidence of Colin MacKenzie¹⁹² as evidencing the proposition that *"Undoubtedly, Mr Mackenzie read and understood Schedule 4"*¹⁹³. Nowhere in that passage does Mr MacKenzie refer to having understood the implications of Pricing Assumption No. 1 contained

¹⁹¹ Witness statement of Brian Cox TRI00000259, page 10, 13.2

¹⁹² Transcript of oral evidence of Colin MacKenzie 26 October 2017 pages 96:11 to 97:25

¹⁹³ Paragraph 103 of the written submissions of DLA dated 27 April 2018

within Schedule part 4. His evidence is that he recognised that there would be Notified Departures after contract close. That is not controversial; it is well trodden ground that it was understood that there would be a Notified Departure in respect of the change in the design programme from version 26 to version 28¹⁹⁴. It is entirely different from an understanding of the risks associated with the development of the design from BDDI to IFC.

3.96 Similarly, at paragraph 113 of its written submissions of 27 April 2018, DLA purports to rely on various passages from Colin Mackenzie's evidence that Mr MacKenzie understood what was being said in DLA's advice letters and was "*fully aware of the pricing assumptions and the expectation that there would be change and Notified Departures*". An awareness of the pricing assumptions and the likelihood of Notified Departures, in particular in the context of approvals and consents, does not correlate with an understanding of the risks associated with Pricing Assumption No. 1. The passages of Mr MacKenzie's evidence which are relied upon do not support DLA's position:

3.96.1 Page 112, line 22 and 113, line 18 of the transcript of Colin MacKenzie's oral evidence: Mr MacKenzie's evidence is that his recollection was that the matters which he considered to be risky for the Council and fully covered by the QRA were "*matters concerning the design risk...design and cost implications*". Mr MacKenzie goes on to explain what he means by "*design risk*", namely the risks associated

¹⁹⁴ See for example transcript of oral evidence of Gill Lindsay 27 October 2017 pages 146:25 to 147:6

with misalignment or "*mismatch*" in the context of prior and technical approvals. He does not refer to the risks associated with Pricing Assumption No, 1 in this respect¹⁹⁵.

3.96.2 Page 114, lines 5 to 19 of the transcript of Colin MacKenzie's oral evidence; Mr MacKenzie's evidence addresses the "*mismatch*" referred to above, and not the risks associated with Pricing Assumption No. 1.

3.96.3 Page 115, line 3 to page 117, line 9 of the transcript of Colin MacKenzie's oral evidence: Mr MacKenzie's evidence refers to the possibility of "*at least one*" Notified Departure in the context of reports "*submitted to the Internal Planning Group about the number of designs which had been approved or not approved*".

3.96.4 Page 134, line 4 to page 135, line 13 of the transcript of Colin MacKenzie's oral evidence: this passage largely consists of counsel to the Inquiry's reading of extracts from Mr Mackenzie's written statement. However, it relates to programme and "*mismatch*" delay, and not to issues associated with Pricing Assumption No. 1.

3.96.5 Paragraph 199 of Colin MacKenzie's statement: this set outs Mr MacKenzie's understanding that there would be more than one Notified Departure after contract formation. As referred to above, this is not controversial. It does not demonstrate an understanding of the risks associated with Pricing Assumption No. 1.

3.97 **Gill Lindsay**

¹⁹⁵ Transcript of oral evidence of Colin MacKenzie pages 112:22 to 113:18

3.97.1 Gill Lindsay summarised her understanding of Schedule part 4 in her witness statement as follows:

"My knowledge of this Schedule was as contained in the relevant Legal Advice letter provided to the Council by DLA, the external legal agents to the project, being DLA legal advice letter of 12 May 2008 (GL/2008/14a and GL/2008/14b). No matters of concern or comment for my attention or advice were raised to me by the in-house legal team of CMcK or NS, by the CEC finance team or any other team or by DLA. I understand the document was drafted by Geoff Gilbert, Commercial Director of Tie, Bob Dawson of Tie and Dennis Murray of Tie, reviewed by Stewart McGarrity, Finance Director of Tie, further reviewed by Steven Bell, Project Director/Manager of Tie and reviewed by DLA, legal advisers to the Project. The records contain a Financial Close Approvals Process paper for the Legal Affairs Committee of 7 April 2008 agreeing the approval and QC process to financial close. This 2-page paper and 2-page schedule details authors and approvers (GL/2008/1a and GL/2008/1b). In terms of my strategic role, even if this was not a finance schedule, I would not have expected to review it personally"¹⁹⁶.

3.97.2 Gill Lindsay also gave oral evidence¹⁹⁷ in respect of an email dated 15 April 2008¹⁹⁸ sent by Stewart McGarrity of TIE to Alan Coyle of the Council, copied to Andy Conway and Rebecca Andrew, both of the Council. One of the documents attached to that email was a

¹⁹⁶ Witness statement of Gill Lindsay TRI00000160, page 20

¹⁹⁷ Transcript of oral evidence of Gill Lindsay 27 October 2017, pages 128:15 to 144:25

¹⁹⁸ CEC01245223

document¹⁹⁹ which Stewart McGarrity described as follows "*Part 4 of the Schedule to the Infraco contract re Pricing - since it is where the numbers go in it's where all the last minute tweaking happens so there are still a couple of things to be incorporated which are being discussed and agreed today.*" That email, with its attachments, was forwarded to Gill Lindsay. Gill Lindsay gave oral evidence that she did not read the draft of Schedule part 4 at the time²⁰⁰ because this was one of "*of very many mails between [Stewart McGarrity and Alan Coyle] regarding QRA and workshops and I have simply just seen this as pricing, a financial analysis spreadsheet...I didn't have any indication from seeing that for information that that was an issue to do with risk*"²⁰¹. Gill Lindsay also gave evidence that had "*any particular matter...been flagged to my attention, I would have done anything to deal with it*"²⁰². Furthermore, "*...something as significant should not have been in a document that's provided over to a finance officer on the 15th. There was no visibility of this.*"²⁰³

3.97.3 As referred to above, DLA had not flagged the terms of the Pricing Assumptions, and in particular Pricing Assumption No. 1 to the Council or to TIE. Gill Lindsay's evidence to the Inquiry was that she "*would have expected it to be in the risk matrices very clearly in terms of the risks of Schedule 4, and very clearly explained through DLA and in fact through tie themselves*".²⁰⁴ As referred to above, that was not the case.

¹⁹⁹ CEC01245224

²⁰⁰ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 129:13-15

²⁰¹ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 131:5-15

²⁰² Transcript of oral evidence of Gill Lindsay 27 October 2017, page 134:20-22

²⁰³ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 140:6-8

²⁰⁴ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 144:6-9

The individuals involved at TIE were not aware of the risks associated with Pricing Assumption No. 1, and those risks were not flagged up by DLA.

3.97.4 Gill Lindsay further gave evidence that there was no discussion that she could recall amongst the Council's Legal team in relation to Schedule 4 before contract close.²⁰⁵

3.97.5 Had DLA drawn her attention to the relevant provisions, Gill Lindsay's evidence was that "*I think clearly I would have spoken to my own team about it, to understand what...did we know about this and what was the position. I think we would have had pretty much immediate contact with the Director of Finance, to understand what was his understanding. And probably what was the understanding overall in the Council, and also in terms of the TPB...there would have had to have been a very serious and significant matter about where in the QRA that could have been, and what the value of that would have been*"²⁰⁶. Gill Lindsay further confirmed in her evidence that she had been alerted to the relevant terms she would "*undoubtedly*" have escalated this to the highest level²⁰⁷, and regarded it as part of her duty to raise the matter with senior officers in the Council²⁰⁸.

3.97.6 Gill Lindsay's evidence in relation to the risks and uncertainties that were to be managed by TIE during construction was that these were: "*the risks which were accepted in the outline and Final Business Case,*

²⁰⁵ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 144:19-22

²⁰⁶ Transcript of oral evidence of Gill Lindsay 27 October 2017, pages 140:14 – 141:3

²⁰⁷ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 141:4-18

²⁰⁸ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 141:19-23

*which were probably largely MUDFA works and whether they would be complete...the issue of consents and approvals... [and] a range of other matters regarding other consents for TROs and the like".*²⁰⁹ Gill Lindsay did not include the risks associated with Pricing Assumption No. 1 as sitting with TIE at contract formation.

3.98 **Tom Aitchison**

3.98.1 The evidence of Tom Aitchison was that he was not aware of the terms of Schedule part 4²¹⁰, could not recall any discussion about it with the directors of City Development and Finance, or the Council Solicitor²¹¹ and had not seen a copy of it until being shown it by the Inquiry²¹². Tom Aitchison was unaware prior to contract award that there would be a Notified Departure or Notified Departures after contract award²¹³. He gave evidence that his "*clear understanding when the contract was going through the financial close phase was that it was substantially a fixed price contract. By that I mean there were various figures bandied around about 90 per cent, 95 per cent*"²¹⁴. Tom Aitchison accepted that it would have been beneficial for members to have been properly advised of Schedule part 4 and its contents, and necessary for members to be aware that the price was subject to a long list of Pricing

²⁰⁹ Transcript of oral evidence of Gill Lindsay 27 October 2017, pages 163:4-12

²¹⁰ Transcript of oral evidence of Tom Aitchison 28 November 2017, page 143:21-25

²¹¹ Transcript of oral evidence of Tom Aitchison 28 November 2017, page 145:2-6

²¹² Transcript of oral evidence of Tom Aitchison 28 November 2017, pages 151:23 to 152:9

²¹³ Transcript of oral evidence of Tom Aitchison 28 November 2017, page 146:18-22

²¹⁴ Transcript of oral evidence of Tom Aitchison 28 November 2017, pages 155:25 to 156:4

Assumptions, some of which were known not to be correct at financial close and would lead to a likely Notified Departure or Departures²¹⁵.

3.99 **Andrew Holmes**

3.99.1 Andrew Holmes gave evidence in relation to his understanding of the transfer to Infracore of risk associated with design. Mr Holmes was referred in his evidence to a PowerPoint presentation given by TIE (including Willie Gallagher and Stewart McGarrity²¹⁶) to the Tram Project Board on 19 December 2007²¹⁷, which concerned the agreement which had been reached at Wiesbaden. Mr Holmes stated that "*agreement had been essentially reached on de-risking elements that had been of concern...it was a question of premiums being applied to different elements in return for reduction in risk*"²¹⁸. As referred to in Mr Holmes' oral evidence, the PowerPoint presentation stated "*BBS taking detailed design development risk*"²¹⁹, and this accorded with Mr Holmes' recollection of what was "*said principally by Willie Gallagher, supported by those of his staff who had been involved in the discussion*"²²⁰. Mr Holmes confirmed that the reference in the presentation to "*Design development risk transferred to Infracore from this point on*" was "*at the core of my understanding of the outcome of the agreement*"²²¹.

²¹⁵ Transcript of oral evidence of Tom Aitchison 28 November 2017, pages 156:13 to 157:14

²¹⁶ Mr McGarrity gave evidence that his understanding of the position was based on "*if not the signed version, a very advanced version of the document and discussion with Geoff [Gilbert], and discussion with Willie [Gallagher]...*" see transcript of oral evidence of Stewart McGarrity 12 December 2017, page 148:6- 9

²¹⁷ CEC01483731

²¹⁸ Transcript of oral evidence of Andrew Holmes 29 November 2017, page 56:8- 16

²¹⁹ Transcript of oral evidence of Andrew Holmes 29 November 2017, page 56:19

²²⁰ Transcript of oral evidence of Andrew Holmes 29 November 2017, pages 56:24 to 57:1

²²¹ Transcript of oral evidence of Andrew Holmes 29 November 2017, page 57:15- 19

3.99.2 The minutes of the Tram Project Board at which the presentation referred to above was given²²² note that Andrew Holmes "*questioned how the risk of programme delays, specifically due to design delays, had been allowed for in the cost estimate. WG [Mr Gallagher] explained that a number of factors provided comfort in this matter: Normal design risk is passed to BBS through the SDS novation*"²²³. Mr Holmes gave evidence that he recalled this exchange, and understood "*that the design had effectively been de-risked*"²²⁴.

3.99.3 Mr Holmes' evidence was that when he left his position at the Council on 1 April 2008, his understanding was that the Infraco price "*was essentially fixed apart from...issues that might arise from the consents process, which I had assumed were manageable by the Council*"²²⁵.

3.100 Philip Wheeler

3.100.1 The evidence of Philip Wheeler, given in his witness statement and addressed in his oral evidence was that risk associated with design was to sit with Infraco:

"Q. ... look at page 21 of your statement... paragraph 58...third line:

"Design risk lay with TIE until such time as the novation was complete, but I cannot recall if this was discussed or if it was reflected in any risk registers. The lawyers were told by the TPB that the risk was to lie with

²²² CEC01363703

²²³ Transcript of oral evidence of Andrew Holmes 29 November 2017, page 58:25 to 59:5

²²⁴ Transcript of oral evidence of Andrew Holmes 29 November 2017, page 63:24- 25

²²⁵ Transcript of oral evidence of Andrew Holmes 29 November 2017, page 109:10- 13

the contractors in the contract." What risk are you discussing there, can you recall?

A. I think particularly that the risk that the design wouldn't be ready when required.

Q. Who was to carry the risk of that, as far as you were concerned?

A. That was my understanding, that there was novation discussions as part of the negotiation with the potential contractors for them to take on the risk of the designers....Or making sure that the designs were managed and delivered...The risk would be transferred to the contractors as part of the novation progress.

Q. Who was giving you that information, can you recall?

A. I'm sure that was information I was gleaning at the Board meetings from the senior officers of tie and those who were doing the negotiations...

Q. By the time you got to contract close in May, what was your understanding as to where that risk lay?

A. Well, that -- my understanding was that the novation was part of the contract suite, and therefore the risk for getting the designs finished had transferred as part of that suite of documents...

I cannot recall if I received a briefing from CEC legal officers, at any time, on the effect of the contract, including the pricing in Schedule 4. However, we did discuss it at TIE Board meetings or the TPB [Tram

Project Board]. *Some of those meetings were attended by DLA who probably explained it to us. At that stage I was still under the impression that the risks all lay with the contractor. That was what we were told by Willie Gallagher, Tom Aitchison and Gill Lindsay*²²⁶.

3.100.2 Mr Wheeler's evidence was that he had no recollection of relevant advice being given by Andrew Fitchie:

"Q. ...Did Andrew Fitchie of DLA give advice to the, TEL or the Tram Project Board that there was a weakness in the contract that would enable the [contractor] to claim additional monies?

A. I don't recall that.

Q. Had you been told that, do you think you would have been able to recall it?

*A. I'm sure if I had heard that someone like Mr Fitchie had questioned the robustness of the contract, I'm sure I would have remembered that*²²⁷.

3.100.3 Philip Wheeler stated that he did not recall any advice given in relation to whether or not it might be appropriate to pause, and said *"I'm sure I would recall it if I'd been aware of legal advice to that effect"*²²⁸.

3.101 **Donald McGougan**

²²⁶ Transcript of oral evidence of Philip Wheeler 2 November 2017, pages 53:1 to 60:13

²²⁷ Transcript of oral evidence of Philip Wheeler 2 November 2017, page 71:7-16

²²⁸ Transcript of oral evidence of Philip Wheeler 2 November 2017, page 51:17-24

3.101.1 Donald McGougan gave evidence to the Inquiry in relation to his understanding, at financial close, of the extent to which there were likely to be post contract changes that would increase the cost of the Project:

*"I think tie and CEC as client were very clear that they would not initiate any post contract changes that were going to impact on the programme or the cost. So the areas where there would be post contract changes would be in relation to the design where we had been assured that normal design development from BDDI to issued for construction was a risk for the contractor, and the areas of potential delay in relation to approvals and in planning and in the roads area, and the Council had supplemented the staff in both those areas to ensure that there was no delay once the contract drawings came to the Council"*²²⁹.

3.101.2 In his witness statement, Mr McGougan also gave evidence that his understanding of the position at or prior to contract close was that the risk associated with normal design development was transferred to Infraco²³⁰.

3.102 **Lesley Hinds**

3.102.1 Lesley Hinds gave evidence about the importance to the Council of Council's contribution of £45m not being exceeded: *"I would say it was pretty important because we had lots of other challenges...And therefore I would say that at that time, and we were given assurances that when the contract was signed, that it was a 95 per cent – it sticks in*

²²⁹ Transcript of oral evidence of Donald McGougan 29 November 2017, page 46:4- 15

²³⁰ See for example paragraphs 104, 112, 120,133 and 135 in the witness statement of Donald McGougan at TRI00000060

*my head very clearly, as I probably say quite often in my statement, 95 per cent fixed price, and therefore our assumption with putting in contingencies, et cetera, that we would not be asked for any more than the 45 million*²³¹. As referred to in her oral evidence, Lesley Hinds also gives evidence in her witness statement that the cost of the Infraco Contract was 95% fixed, and that it was crucial to achieve a fixed price²³². Lesley Hinds explained her understanding of the fixed price as meaning *"that the budget would be 95 per cent fixed cost, which would mean that the budget would be then including contingencies, but the 95 per cent was fixed cost, which meant all the designs were sorted out and the costs, then the budget would not exceed the 545 million. And that's my understanding and as I say, the 95 per cent is fixed in my head, that these were fixed costs so we would not go over the 545 million"*²³³.

3.103 Colin Mackenzie gave evidence in relation to his understanding of which Notified Departures he expected following contract close: he stated that *"The real concern about possible notified departures was likely to be INFRACO programme delays due to designs being late or inadequate and I noted that the issue had been discussed earlier about the bridge at Russell Road...if there was delay in the design production and the consenting process BBS would not be liable for delay to the construction programme"*²³⁴. It is not controversial that Colin Mackenzie

²³¹ Transcript of oral evidence of Lesley Hinds 6 September 2017, page 64:9- 20

²³² See for example paragraphs 156, 160, 211, 228, 272.2, 280, 350, 357 and 407 of the witness statement of Lesley Hinds TRI00000099

²³³ Transcript of oral evidence of Lesley Hinds 6 September 2017, page 68:10-17

²³⁴ Witness statement of Colin Mackenzie TRI00000054, page 87 to 88

(and others at the Council) understood that there would be Notified Departures following contract close (which is not controversial); however, this is not the same as an understanding of the full implications of Pricing Assumption No. 1.

Infraco's position in relation to Schedule part 4

3.104 The evidence of Matthew Crosse was that it would be incorrect to assert that Infraco's position at Wiesbaden was subsequently "non-negotiable". In his oral evidence to the Inquiry, Mr Crosse stated:

"Q. Were you ever told by Andrew Fitchie, the solicitor at DLA, that these principal terms of Schedule 4 were non-negotiable or that they had been all agreed at Wiesbaden and that was that?"

A. I don't recall being told anything like that by Andrew.

Q. Did you raise in the course of the Rutland Square negotiations any concern as to how Schedule Part 4 was being developed?"

A. No, I didn't. Not to the best of my knowledge. I can't recall that.

Q. If it is said to you that the reason you didn't raise any concern is because it simply reflected the discussions you had had while you were in Germany, what would your reply to that be?"

A. I would say it wasn't true because it -- more detail had been put around what we had discussed in Germany..."

Q. Q. Ian Laing who was representing the consortium, one element of the consortium, Bilfinger, said that Schedule Part 4 had been agreed by tie in Wiesbaden. It contained the rules to govern post contract signature, design, production and development, and that the consortium could not and was not prepared to absorb any cost or time risk at all, and that you didn't disagree with that?

A. That's rubbish. We would not have had a conversation like that in Wiesbaden. That was not what the meeting was about...

Q. If you had been told that the consortium was not prepared to absorb any cost or time risk at all, would you have agreed that that is what you discussed at Wiesbaden?

*6 A. No*²³⁵.

3.105 James McEwan gave oral evidence that the Wiesbaden Agreement was not non-negotiable:

"A. It clearly wasn't set in stone... I don't remember being told it was non-negotiable.

Q. Did you consider that you were negotiating terms such as the price and the responsibility for design risk?

*A. I think we were negotiating items which had the potential to impact price*²³⁶.

²³⁵ Transcript of oral evidence of Matthew Crosse 17 October 2017, pages 168:25 to 171:6

²³⁶ Transcript of oral evidence of James McEwan 18 October 2017, pages 119:23 to 120:5

3.106 In his evidence, Ian Laing also addressed the question of whether the Wiesbaden Agreement was "*non-negotiable*": he confirmed that the assumptions in Schedule part 4 "*changed or were developed over time to a significant extent*"²³⁷. Furthermore, Mr Laing agreed that "*even [his] first draft of the Schedule part 4 innovates quite markedly upon the Wiesbaden Agreement*"²³⁸. His oral evidence was that "*the Wiesbaden Agreement clearly is a record of agreements reached by the principals at a point in time. A number of things can have happened in that regard. The language of the Wiesbaden Agreement certainly is imprecise as one often finds in such documents. The legal teams were not involved in Wiesbaden, and therefore I would have felt it entirely appropriate to...interpret that in a way which gave greater certainty. But I have no recollection in particular of going back to the Wiesbaden Agreement from time to time and seeing it as something that we had to adhere to on an ongoing basis, not least because the factual circumstances were continually changing throughout the negotiation of Schedule 4*"²³⁹.

3.107 The written submissions made on behalf of Bilfinger confirm this position: at paragraph 44, they state "*Wiesbaden itself was merely a step in the process of negotiating the Infracore Contract terms. It was not a "final deal" that could not be opened up or negotiated further*".

3.108 Furthermore, the definition of what was to constitute "*normal design development*" remained an open issue in the months leading up to contract close. Ian Laing gave evidence that the meaning of what

²³⁷ Transcript of oral evidence of Ian Laing 23 November 2017, pages 8:24 to 9:1

²³⁸ Transcript of oral evidence of Ian Laing 23 November 2017, page 14: 9-12

²³⁹ Transcript of oral evidence of Ian Laing 23 November 2017, page 14:19 to 15:9

constituted normal design development "*mattered clearly because the parties needed to have a clear understanding of...what was normal in that context. I remember a number of times, at least in general terms I remember, asking technical people what was normal design development, and I don't remember ever getting an entirely consistent answer, and so it seemed to me important that there was a consistent view, and it was clearly defined so that the parties knew where the line was*"²⁴⁰.

3.109 Mr Laing also gave evidence in relation to a conversation that he had with Andrew Fitchie shortly before contract close in relation to Schedule part 4 following public reporting that that "*the contract was nearing finalisation and it was a lump sum fixed price contract. As matters had developed at that time, and although I can understand that phrase, I think there was a risk -- I thought there was a risk that that may be misunderstood. I spoke one to one with Andrew Fitchie. I expressed concern about the report to the Council, and I expressed concern as to what Edinburgh District Council knew as regards the mechanism within the contract. Andrew was always a polite man, but it sticks in my memory because he was somewhat irritated by my enquiry. He essentially told me it was none of my business what the Council were being advised by their legal advisers*"²⁴¹.

Discussions between Andrew Fitchie and Richard Walker

²⁴⁰ Transcript of oral evidence of Ian Laing 23 November 2017, page 23:7- 16

²⁴¹ Transcript of oral evidence of Ian Laing 23 November 2017, pages 47:21 to 48:10

3.110 Andrew Fitchie suggested in his witness statement and oral evidence that he was told by Richard Walker of BB in December 2007 that the Infraco Contract would cost an additional £80 million²⁴², and that he reported this to TIE. Mr Fitchie has not provided the names of any individuals to whom the report is said to be made (other than that he "may" have told Stewart McGarrity and/or Geoff Gilbert), nor has he provided a date for when the report was said to have been made, other than that it was in December 2007²⁴³. Mr Fitchie has confirmed that he did not make anyone at the Council aware of what Richard Walker told him: *"I am asked if I made anyone at CEC aware of my conversation with Richard Walker as described at 7.124 to 7.129. I did not..."*²⁴⁴.

3.111 There was no evidence from any TIE witnesses that they were informed of Richard Walker's comments.

3.112 There is no assertion by Andrew Fitchie that he sought to convey the information about the conversation to TIE or the Council in writing: *"I didn't feel the need to write this"*²⁴⁵.

3.113 David Mackay gave evidence had no recollection of being informed of the foregoing matters by Andrew Fitchie:

"With the caveat that I am being asked to recall something that is claimed to have been said approximately ten years ago, I do not think that Andrew Fitchie told me anything about this in 2007. As I said in my

²⁴² Witness statement of Andrew Fitchie TRI00000102, page 24 and transcript of oral evidence of Andrew Fitchie 10 October 2017, page 73:3 onwards

²⁴³ See paragraphs 2.115, 7.124, 7.129 in the witness statement of Andrew Fitchie at TRI00000102 and transcript of oral evidence of Andrew Fitchie 10 October 2017, page 73:3-16

²⁴⁴ Witness statement of Andrew Fitchie TRI00000102, paragraph 7.132

²⁴⁵ Transcript of oral evidence of Andrew Fitchie 10 October 2017, pages 74:25 to 75:1

*statement, I reacted with surprise and fury when Richard Walker said in February 2009 that Bilfinger were seeking a further £50-£80m to complete the work, and accordingly I do not think I had any prior warning of Walker's view on the "need" for this additional level of funding. I only had limited contact with Andrew Fitchie before I became interim Chair of TIE in November 2008. I had frequent contact with him once I was in post. It would be very odd for a matter of this significance to have been raised with me only in conversation and not in writing*²⁴⁶.

3.114 Steven Bell's clear oral evidence to the Inquiry was that he had no recollection of being informed by Andrew Fitchie that Richard Walker of Infracore had made reference of an increase in cost of £80m:

"Q. Do you have any recollection of it being reported to tie in early December 2007 that the Infracore Contract would end up costing about GBP80 million more than the price that had been offered by BBS?

A. Absolutely not.

Q. The reason I ask is that, as you may be aware, Andrew Fitchie has given evidence that Richard Walker of the consortium advised Mr Fitchie in early December 2007 that the contract would cost about GBP80 million or thereabouts more, and that Mr Fitchie had reported that conversation to tie management the same day. Do you have any awareness or recollection of that?

²⁴⁶ Additional questions for David Mackay TRI00000158, page 1

A. Not reported to me for sure. And I'm not aware of anybody in tie management that that was reported to. The first time I heard figures of that scale were in February 2009 when I met with Mr Walker and Mr Flynn.

Q. Given your involvement in the tram project in December 2007, if Mr Fitchie had reported that figure and that conversation with Mr Walker to tie management, is that something you are likely to have been made aware of?

A. I would have expected so, yes.

Q. Why do you say that?

A. Because it would have been a significant cost that was different from the values that everybody had been preparing and working through as part of the procurement process. That would be a very material change circa 22 to 25 per cent, perhaps more, depending on which end of the range to that price you've just described.²⁴⁷

3.115 Geoff Gilbert gave evidence that he did not recollect being informed of the conversation referred to above, and would have expected its content to be put to TIE in writing in any event:

Q. Now, the Inquiry has heard some evidence already that...Mr Fitchie, the solicitor at DLA advising tie, was told by the contractors and passed on to the senior management in tie in early December 2007 that the

²⁴⁷ Transcript of oral evidence of Steven Bell 24 October 2017, page 33:20 to 34:23

contractors had said it would cost GBP80 million more to build than the price that had been provided to that date. Were you aware of that?

A. ...I don't recollect it....If it had been something that BBS wanted to communicate to us, then I think it would have come in writing. Certainly should have. So that we could consider what they were proposing. Ad hoc comments to third parties -- not third parties, but ad hoc comments, perhaps just negotiation games....

Q. If it was suggested that there would be an increase of GBP80 million or some 40 per cent increase, would you expect that to have stuck in your mind?

A. I would have thought so. It would certainly give you pause for thought²⁴⁸.

3.116 Stewart McGarrity similarly gave evidence that he had no recollection of Andrew Fitchie informing him of a conversation with Richard Walker to the effect referred to above, and in any event would have expected such information to have been put in writing:

"Q. Were you aware around [early December 2007] that the cost of the Infracore works might turn out to be significantly higher than the GBP208 million then under discussion as the price?

A. No.

²⁴⁸ Transcript of oral evidence of Geoff Gilbert 19 October 2017, pages 79:21 to 80:21

Q. Were you aware of any suggestion that the figure might be GBP80 million or so higher than that?

A. Absolutely not.

Q. So not aware of any comments of that nature emanating from anyone in the consortium?

A. Nobody at all. I would have had a heart attack if I'd heard any such comments coming from anyone.

Q. Could we take it from that then that Andrew Fitchie of DLA, you do not recall him saying anything to that effect?

A. Absolutely not.

Q. If Mr Fitchie had given evidence that following a meeting he'd had with Richard Walker in 2007, at which Mr Walker had made comments to that effect, that he had then walked through the building and told you all about it, what would your response be to that?

A. No. Didn't happen. I would absolutely remember that. I have no such -- as certain as I can be that no such exchange took place with Andrew Fitchie.

Q. If Andrew Fitchie or anybody else had made a comment of that nature to you around that time, what would you have done with that information?

A. I would have taken it straight to Willie Gallagher and to Steven Bell and the entire team and said: we need to bottom this out; we can't continue any further with this procurement until we understand the context of that comment...

Q. Based on your knowledge of the way Mr Fitchie generally communicated with the tie management team, if he did have information to the effect that the consortium expected their final price for the works to be so much higher, how would you have expected Mr Fitchie to report that?

A. At the very least in an email. They're so important. It would have to at the very least be communicated in writing, I would have thought²⁴⁹.

3.117 Willie Gallagher referred in his oral evidence to the suggestion that he might have had a discussion with Richard Walker in respect of an increase in price being acknowledged in December 2007, and he categorically rejected this suggestion:

"Q. It has been suggested in evidence by others that at the Wiesbaden Agreement, and when you...had your discussions with Mr Enenkel and representatives of Siemens, you made it plain that you knew that wouldn't be the final price, that it would go up as soon as the contract was signed.

A. Absolutely not the case.

²⁴⁹ Transcript of oral evidence of Stewart McGarrity 12 December 2017, page 139:4 to 141:11

Q. You didn't say: this is not the real price, everyone knows it's going to go up.

A. No, of course not.

Q. It is suggested that not only at the Wiesbaden meeting, but a couple of times afterwards, at a meeting in late December and then again in January, you repeated the same thing, that everybody knew the price will increase after award?

A. No, who did I say it to?

Q. Richard Walker.

A. Absolutely not...why would I have discussions of that matter with Richard Walker? I've already said that I was very careful in terms of discussions with Bilfinger Berger in particular. But certainly -- and given that we are in the process of negotiating a contract, you know, why would I be so careless in terms of what was said? And more to the point, I didn't believe that at all. I stand by what I said earlier on, which was that we were hoping to achieve the price that was in the contract. If there were going to be changes to the price, it had to be approved through the contract, and we, ie the Council team, were going to work as hard as we can to secure the best price for the best outcome for the Council. And I guess -- I mean, it was a hard negotiation, and we negotiated hard to try and achieve that. But I didn't believe, and I certainly didn't communicate anything other than what I have just stated.

Q. It was suggested that you knew, because of the assumptions and the qualifications and the exclusions in their offer, the price was always going to go up once the contract started?

*A. No. No*²⁵⁰.

The evidence of Andrew Fitchie

3.118 In light of all of the evidence discussed above, it is submitted that the following conclusions may be drawn about the evidence of Andrew Fitchie.

3.119 In the first place, his evidence that he gave advice to officers of TIE as to the consequences of Schedule part 4 and the pricing assumptions, including Pricing Assumption No. 1, should be rejected, and the Inquiry should find that no such advice was given. He conceded himself that he gave no such advice in writing and his evidence that he did so verbally is contradicted by all of the TIE personnel who were involved at the time. Whether Mr Fitchie's evidence was deliberately false, or was perhaps the consequence after a period of time of his own mistaken belief that he must have given such advice, is a matter for the Inquiry. Such a finding would be justified by, and be consistent with, all of the evidence about what occurred between December 2007 and contract close in May 2008 which is considered in detail in the following sections of this Chapter.

²⁵⁰ Transcript of oral evidence of William Gallagher 17 November 2017, pages 97:14 to 99:4

3.120 Secondly, the evidence of Mr Fitchie that he was aware at the time of concerns about Schedule Part 4 and the pricing assumptions requires consideration. That evidence raises two possibilities. The first possibility is that that evidence may be accepted and Mr Fitchie be found to have been rightly concerned at the time. If that finding were to be made, however, it would have the consequence that Mr Fitchie clearly failed in his duties of care to TIE, and separately to the Council, because he did not articulate his concerns in any meaningful way to those to whom he owed those duties of care. If he was so concerned, then his failure properly and clearly to set out his concerns in writing to each of the parties to whom he owed a duty of care is unforgiveable, or at least incomprehensible. Any solicitor exercising a duty of care in such circumstances could not have failed to bring his concerns properly to the attention of clients to whom he and his firm owed duties of care.

3.121 The alternative view is that in claiming that he was aware at the time of the consequences of Schedule part 4, and of the pricing assumptions, as he has said in the passages in his witness statement quoted above, Mr Fitchie is not telling the truth. If that is the true situation, the position which he now claims may be the result of his belatedly giving proper consideration to the meaning and effect of the pricing assumptions in Schedule part 4, particularly Pricing Assumption No. 1, and that it is obvious that the progressing of designs from BDDI to IFC was inevitably going to lead to disputes and claims by Infracore for additional payments, and that at the stage of entering into of the Infracore Contract, that was or ought to have been obvious. The Council does not repeat the reasons

for this obvious conclusion which were explained at the outset of this Chapter 1.

3.122 The fact that Mr Fitchie did not truly appreciate the significance of the pricing assumptions in Schedule part 4 at the time would be consistent with other evidence. Most obviously, it would explain why he did not advise those to whom he owed duties of care of the fact that Pricing Assumption No. 1 in particular would be likely to lead to an unquantified and unquantifiable number of claims for additional payment, and that that would give rise to disputes and be likely to lead to additional cost. If Mr Fitchie did not truly understand the significance of Schedule part 4 at the time, then that would explain why he gave no such advice.

3.123 Likewise, it would explain why he continued to maintain during the DRP process in 2009 and 2010 which is discussed in Chapter 3, that the position of Infraco was not justified. An example is the Summary of Legal Interpretation dated 9 December 2009 in which the TIE position on the words “*normal development and completion of designs*” in Pricing Assumption No. 1 is stated to be:

*“The development and completion of designs showing in the initial design for part of the Infraco Works (Base Date Design Information) into the detail needed to construct that part of the works as described, all to meet the Employer’s requirements”.*²⁵¹

²⁵¹ CEC00651408, part 2.6

That view is stated to be the position of DLA but it was not supported in the first Hunter Decisions which had been issued on 16 November 2009.

3.124 It is difficult to understand how DLA could be maintaining that position if, as Mr Fitchie claims, he was aware all along that Pricing Assumption No. 1 would give rise to increases in cost because “important Assumptions were untrue”.²⁵² The position maintained by Mr Fitchie at the end of 2009 is not consistent with that.

3.125 It will be a matter for the Inquiry to determine which of those two possibilities regarding the evidence of Mr Fitchie is accepted. In either case, however, the critical fact is that neither Mr Fitchie nor DLA provided at the time complete and accurate advice to TIE and to the Council as to the likely effects of entering into the Infraco Contract containing Schedule part 4 in the form in which it was, including Pricing Assumption No. 1.

²⁵² Witness statement of Andrew Fitchie TRI00000102, page 183, paragraph 7.285

4. **Events of December 2007**

Summary

- 4.1 Final Business Case v2 ("FBCv2") was produced on 7 December 2007, and recommended that Phase 1a of the Project should proceed, with funding up to £545m committed to its delivery, against an estimated cost of £498m. There was a high degree of confidence in the estimates. The figures had been tested, reviewed and benchmarked in various ways.
- 4.2 There was no Optimism Bias allowance in the Final Business Case, because of the risk allowance based on the QRA, which gave a 90% confidence level, meaning that there was considered to be a 90% chance that costs would come in below the risk-adjusted level (P90).
- 4.3 The procurement strategy was to transfer a very significant number of risks to the private sector, including the design, construction and maintenance performance risks. It was recognised that there had been slippage in relation to the design, but steps were being taken to address this. The aim was to have a fixed price infrastructure contract. It was recognised that TIE would bear the risks arising from the utility diversion works not being completed before the Infracore works began.
- 4.4 Members received briefings in relation to FBCv2, and were given the opportunity to ask questions in relation to it.
- 4.5 Senior Council officers produced a report in advance of the Council meeting which took place on 20 December 2007. That report included

input from TIE. It had originally been intended that the report would recommend contract close, but because there were outstanding issues (including those referred to in a Briefing Note to Council directors), this was not possible.

4.6 The report instead recommended staged approval of contracts, subject to price and terms being consistent with the Final Business Case, and the Chief Executive being satisfied that all remaining due diligence was resolved to his satisfaction.

4.7 The evidence of one of the authors of the report was that it identified the unresolved key issues in summary form, and it would not have been appropriate to make public TIE's negotiating position, when negotiations were still ongoing. The other author gave evidence that the report explained the issues to the best of the authors' understanding at the time. The Chief Executive at the time, and others, gave evidence in relation to the factors which meant that the recommendations of the report were appropriate. However, members did give evidence that further information should have been provided at the time in relation to outstanding issues.

4.8 Against the foregoing background, Council granted approval to FBCv2, together with staged approval for TIE to enter into and manage contracts for the design, construction and maintenance of the tram network, the novation of the SDS Provider to Infracore and the supply of trams, on terms to be approved by TIE, and providing that remaining issues were resolved to the satisfaction of the Chief Executive.

- 4.9 It was recognised that the design was not complete in December 2007, notwithstanding the original intention. Consideration was given to pausing or slowing down the process, but ultimately this was not considered appropriate at this stage. However, evidence was given that there was no pressure or imperative to proceed, for example in the context of grant funding.
- 4.10 The Briefing Note referred to above had identified the possibility of paying a risk premium to BBS in order to pass risk. The evidence of former TIE officers was that their understanding was that this was what had been achieved by the Wiesbaden Agreement, in terms of which they considered that the risk of, amongst other things, normal design development had been transferred to Infracore for an additional cost of £8m. This risk transfer was reported to the Council by TIE officers.

Context to position as at December 2007

- 4.11 In high level terms, by the beginning of December 2007 the position in relation to the Project was as follows:
- 4.11.1 An OGC review had taken place which green lit the Project;
- 4.11.2 Funding for the Project from the Scottish Government in relation to the Project was capped at £500m, with the remainder to be met by the Council;
- 4.11.3 The Council had approved Final Business Case v1, noted at P90 (namely that there was a 90% chance that the final cost for phase 1a would be below the risk adjusted level);

- 4.11.4 Utilities works were ongoing;
- 4.11.5 A consortium of BB and Siemens had been appointed as Preferred Bidder in respect of the infrastructure works, and discussions were ongoing with them in respect of terms;
- 4.11.6 It was intended that the Final Business Case would be updated to reflect the ongoing negotiations, and presented to Council for its approval on 20 December 2007, in order to proceed to contract award in January 2008; and
- 4.11.7 It had been reported to the Tram Project Board on 26 September 2007 that 58-60% of the detailed design had been produced²⁵³.

"FBCv2

- 4.12 FBCv2²⁵⁴ was dated 7 December 2007. The executive summary stated:
- "The principal recommendation of this FBCv2 is that Phase 1a should proceed, with funding of up to £545m committed to its delivery. The FBCv2 sets out the full supporting analysis which leads to this recommendation"*²⁵⁵.
- 4.13 Paragraph 1.65 of FBCv2 stated *"Building on the detailed cost estimates prepared in November 2006, and incorporating the firm rates and prices received from bidders in 2007, the updated project cost estimates reflect the agreed scope for Phase 1a and a programme for*

²⁵³ CEC01507018

²⁵⁴ CEC01395434

²⁵⁵ CEC01395434, page 7

*delivery of Phase 1a by the first quarter 2011*²⁵⁶. The estimated cost for Phase 1a was £498m. Paragraphs 1.66 to 1.73 of FBCv2 stated " *There is a high level of confidence in these estimates. Approximately 99.9% of the costs included are based on the rates and prices for firm bids received for the main contracts (infrastructure, tram vehicle supply, utility diversions and design)... The overall level of confidence is reinforced by benchmarking against other tram schemes and the provisions for risk included in the estimate...The updated estimates comprise base costs and an allowance for risk and uncertainty. A rigorous Quantitative Risk Analysis (QRA) has been applied to identify project risks to derive a risk allowance to deliver a very high level of confidence (statistically at a 90% confidence level, meaning that there is a 90% chance that costs will come in below the risk-adjusted level). The level of risk allowance so calculated and included in the updated estimate represents 15% of the underlying base cost estimates for future Phase 1a costs at Contract Award. This prudent allowance for cost uncertainty reflects the evolution of design and the increasing level of certainty and confidence in the costs of Phase 1a as procurement has progressed through 2006 / 2007 and fixed priced bids for the infrastructure and tram vehicle supply contracts have been received...tie and CEC will continue to analyse, quantify and mitigate risks during the period through to final negotiation and award of the tram vehicles (Tramco) and infrastructure (Infraco) contracts and during construction with the objective of reducing or eliminating the impact of individual quantified risks and thereby the element of the allowance for*

²⁵⁶ CEC01395434, page 16

*risk which crystallises into actual costs...In summary, the cost estimate reflects substantial external validation from the procurement process for the major contracts and contains a sensible level of risk contingency...On 27th June the Scottish Government confirmed support for up to £500m funding for the Edinburgh Tram scheme. In January 2006, CEC made an in-principle commitment to make a contribution of £45m towards the capital cost of Phase 1, to be deployed initially on Phase 1a. Therefore, the benchmark total funding package is currently £545m. The updated cost estimates above reflect that Phase 1a, at a cost of £498m, is affordable within this level of funding, with 14% headroom over and above the 15% risk allowance provided for in the cost estimate...*²⁵⁷.

4.14 FBCv2 also makes reference to steps put in place to manage risk:

*"1.84 The Procurement Strategy, when fully implemented, will be effective in transferring a very significant number of risks to the private sector. However, as explained above, the strategy is also predicated on delivering value for money, and certain risks are retained in the public sector where they can be effectively managed. tie maintains a comprehensive register of all identified risks in relation to the project and has an active management and mitigation plan for each risk. Where these risks can be quantified they have been assessed and included in the risk allowance in the capital cost estimates..."*²⁵⁸

²⁵⁷ CEC01395434, pages 16 and 17

²⁵⁸ CEC01395434, page 19

11.3 *tie has developed a sophisticated approach to risk management. Central to this has been the appointment of a Risk Manager, and the establishment of a comprehensive risk management process including both a highly detailed risk matrix for the overall project, and detailed risk matrices for the individual contracts within the procurement strategy.....*

11.40 *The Project Risk Register has been developed since the instigation of the project. Each item in the risk register contains a probability of occurrence and the range of minimum, most likely and maximum financial impacts, where appropriate. The financial impacts are over and above costs included in the base estimate. This allows a quantitative risk analysis (QRA), using Monte Carlo simulation, to be undertaken.*

11.41 *Analysis showed that a ‘very high’ confidence that the outturn of the project costs will be derived from the inclusion of risk contingencies as shown below...¹²⁵⁹.*

4.15 It can be seen from the foregoing, that FBCv2 indicated that there was a high degree of confidence in the cost estimates, and that 99.9% of the costs were based on rates and prices in firm bids.

4.16 FBCv2 also set out the procurement strategy for the Project, namely that risk associated with design would be transferred to Infracore:

²⁵⁹ CEC01395434, page 178

"The Procurement Strategy followed by tie responds to feedback from the National Audit Office (NAO) in 2004 on the effectiveness of light rail schemes. The objectives of the Procurement Strategy are summarised as follows:

- Transfer the design, construction and maintenance performance risks to the private sector;*
- Minimise the risk premium (and / or exclusions of liability) that bidders for a design, construct and maintain contract normally include. Usually at tender stage bidders would not have a design with key consents proven to meet the contract performance obligations and, hence, they would usually add risk premiums for this...*

The Infraco will act as a "holding contract", with the intention that the design and vehicle provision (including maintenance contract) will be novated to the Infraco at the point of award. The entire strategy has been developed to help facilitate the speedy implementation and completion of the construction phase of the project and to remove uncertainty and, therefore, cost from bidders' proposals i.e. to deliver value for money...

In summary, the key attributes of the strategy are:

- Early commencement of design by the SDS contractor – To reduce scope and pricing risk in Infraco and Tramco bids and to reduce the overall project programme;*

- *Re-aggregation of the supply chain at the point of award – By novation of the SDS and Tramco contracts to Infraco, thereby creating single point responsibility for design, construction, commissioning and subsequent maintenance of the tram system, with consequential transfer of performance risk to the private sector²⁶⁰...*

The creation of the Infraco Contract as a lump sum contract transfers the pricing risk to the private sector. Finalisation of certain 'Edinburgh specific' elements, such as structures, of the Infraco contract price on the basis of SDS Detailed Design significantly reduces their scope and performance risk pricing premium that would otherwise be necessary under conventional design and construct or PFI approaches²⁶¹."

4.17 FBCv2 recognised that there had been slippage in relation to the production of the design:

"The original assumption was that overall design work to Detailed Design would be 100% complete when the Infraco contract is signed. Due to a number of delays, largely outwith tie's control, this is now not achievable. However, by identifying key risk areas and prioritising SDS activities, tie is completing several key elements of the Detailed Design in time to inform the Infraco bids on price-critical items. This has enabled the Infraco bidders to firm up their bids based on the emerging

²⁶⁰ CEC01395434, paragraphs 1.77 to 1.81 in the Executive Summary to FBCv2

²⁶¹ CEC01395434, paragraph 7.127(b)

*Detailed Design and thereby reduce the provisional scope allowances and design risk allowances that they would otherwise have included*²⁶².

4.18 In his evidence in relation to FBCv2, Donald McGougan notes the estimated capital cost of phase 1a of £498m and states:

*"That figure was based on consultant engineering reports, benchmarking and TIE input based on actual tender returns and prices. There was also the Cyril Sweett independent costing that was undertaken on behalf of Transport Scotland. Outside reviews described TIE as having a well-developed risk management process. Additional sums were added for land, TIE costs, costs of Council staff and legal fees. CEC reviewed the Business Cases and the estimates for capital and for revenue implications to ensure, as far as possible, that the process for arriving at the costs had been properly undertaken and was robust. CEC didn't seek to duplicate TIE effort. CEC didn't appoint our own consultant engineers because it was considered that TIE interests were 100% aligned with Council. It is also worth noting that, in any [case], Transport Scotland had commissioned an independent view of the engineering estimates and there were independent reviews of the project arrangements by the Auditor General and the OGC*²⁶³.

4.19 Tom Aitchison's evidence in relation to FBCv2 was that *"I was always clear that the aim was to have a fixed price contract with most of the risks transferring to the private sector, subject to the normal clauses in contracts relating to unforeseen circumstances. My understanding at*

²⁶² CEC01395434, paragraph 7.53

²⁶³ Witness statement of Donald McGougan TRI00000060, paragraph 312 and 313

*this time was that the risks were anticipated to be relatively small and those arising would be included in the risk allowances provision*²⁶⁴.

4.20 Mr Aitchison's understanding in respect of which party was to bear the risks associated with the incomplete design, was that final agreement had not yet been reached²⁶⁵. That was indeed the case until, on TIE's understanding, the position was addressed at Wiesbaden (which is addressed below).

4.21 In relation to other matters, Mr Aitchison's understanding was:

"...that TIE bore the risks arising from utility diversion works not being completed before the Infraco works commenced. A lot of analysis went into preparing the risk allowance for MUDFA and a high proportion of the overall risk allowance reflected that. I think something like 20% of the total risk allowance for the project was devoted to MUDFA. There was a clear understanding at the time that this was a specific risk area which would not transfer to the private sector (ie to Infraco) and would be retained by the public sector. The responsibility for dealing with consents within a prescribed timescale lay with the Council, providing the required quality standards were met by SDS. At the time, in December 2007, and before Financial Close in May 2008, the question of responsibility for design work and the novation of the SDS contract had not been fully resolved but the risk was thought, by TIE and Council colleagues, to be manageable. I accepted that advice from them. The Council was gearing up, in terms of capacity and expertise, to have the

²⁶⁴ Witness statement of Tom Aitchison TRI00000022, paragraph 68

²⁶⁵ Witness statement of Tom Aitchison TRI00000022, paragraph 69

resources in place to deal with the outstanding approvals and consents. I don't recall ever being advised that there was likely to be a major concern over the Council's ability to handle the approvals and the consents process. My understanding was that some of the then provisional prices and contract rates were being firmed up, with a positive impact on price "certainty". There was also a recognition that the risk allowance might change during the final contractual negotiations. Subsequently, as the estimated final price increased from £498m to £512m there was a compensating reduction in the risk allowance. At the time the view was that the MUDFA contract could be delivered on time and that the SDS work would be completed by the end of 2008. These two steps were considered to assist in managing outstanding risks and diminishing their impact²⁶⁶.

4.22 Jennifer Dawe's evidence in relation to FBCv2 was that:

"It was a very detailed Final Business Case and again, as with all reports like this that came to the Full Council, we would have had briefings and the opportunity to ask any questions about any parts of it that concerned us. At the end of the day, we thought that the report was a reasonable one to support. I think that within the Council Officers' report we were told that DTZ Piedad (a consultancy) had been asked to look matters over. There was some kind of external assessment of the capacity of the Council to make the contribution that was going to be required. On those grounds it seemed to me that the ETP was worth supporting and any concerns that I might have had, or other members

²⁶⁶ Witness statement of Tom Aitchison TRI00000022, paragraphs 70 to 73

of my group might have had, would have been addressed by Council Officers before we actually went to the Full Council meeting....The DTZ Pidea report, in a way, gave some comfort that it was not just the view of GEC's Director of Finance, who was the main person who was advising on finances and the Council contribution. The fact that it had some external assessment probably gave us the feeling that it was a reasonable way forward. The headlines in these papers were about where the money was going to come from, and presentations showed us the amounts in sales of land, developers' contributions and the like. It has been noted that the DTZ Pidea report only related to the Council's financial contribution. That is correct but £45m, at the time, was a lot of money from the Council Budget. Obviously the bulk of the money was coming from TS, but we still had to be satisfied that we could actually bridge that gap if we had to....In terms of concerns about the FBC Version 2, I think any concerns we had at the time would have been satisfied before the meeting. Otherwise we would not have supported the project²⁶⁷ ...

"I must have felt comfortable with the FBC as I supported it. I must have felt that all our questions had been answered and that what we were being presented with was a reasonably argued case that was worth approving. All of the parties supportive of the ETP were in favour of the FBC²⁶⁸.

QRA

²⁶⁷ Witness statement of Jennifer Dawe TRI00000019, paragraphs 265 to 268

²⁶⁸ Witness statement of Jennifer Dawe TRI00000019, paragraph 282

- 4.23 As indicated above, FBCv2 referred to a QRA, or Quantitative Risk Analysis having been carried.
- 4.24 The QRA as it then stood was emailed on 3 December 2007 by Mark Hamill to Alan Coyle of the Council, copied to Steven Bell, Susan Clark and Stewart McGarrity of TIE²⁶⁹. The email attached a Risk Exposure Graph and a document entitled "*Edinburgh Tram Project Risk Allocation Report*"²⁷⁰ for the "*Current Period End 08-Dec-07*"²⁷¹.
- 4.25 The risks identified included the following:
- 4.25.1 Price certainty is not achieved: 50% risk, valued at £10m-£15m.
- 4.25.2 The SDS design is late and insufficiently detailed, meaning that Infraco do not have detail to achieve contract close without provisional designs. 94.5% risk valued at £3m.
- 4.25.3 Poor design and review processes mean that completion of the MUDFA Works is delayed leading to risk of additional time and money due to Infraco (plus potential claims from MUDFA Contractor). 50% risk valued at £0.4m to £4.8m
- 4.25.4 Poor definition of design and the ERs in Infraco tender documents – creates impact on the Infraco ability to develop its tender in terms of its pricing and supply chain. This will increase the time for BAFO, costs and bidder queries. 50% risk valued at £0.9m to £2.7m.

²⁶⁹ CEC01397535

²⁷⁰ CEC01397537

²⁷¹ CEC01397537

- 4.25.5 Utilities assets discovered and lead to redesign, delay and the requirement for additional works. 90% risk valued at £0.5m to £1m.
- 4.25.6 Delay caused by, amongst other things, Utilities or MUDFA Works. 40% risk valued at £1m.
- 4.25.7 The design requires to be re-worked after novation of SDS, meaning that bids will be higher than envisaged in the base estimate as Infracore will price for re-work. 75% risk valued at £0.5m. Infracore risk: utility connections cannot proceed as planned because of a failure to make arrangements with Utilities for the phasing of necessary connections. 50% risk; £0.5m.
- 4.26 The written submissions dated 27 April 2018 on behalf of certain tie employees refer at pages 57 to 62 to a manual alteration made to the QRA spreadsheet. For the avoidance of doubt, this manual alteration was not known to any officers of the Council at the relevant time. The matter was put to Donald McGougan during his oral testimony. Mr McGougan confirmed that this was the first time that he had been aware of this matter²⁷². He went on to say that "*My first reaction is great surprise, maybe even shock. I think if this is what it appears to be at first reading, and I can't think it's anything else, I think it's disgraceful*"²⁷³

Report for Council meeting on 20 December 2007²⁷⁴

²⁷² Transcript of oral evidence of Donald McGougan 30 November 2017 page 58:10 - 12

²⁷³ Transcript of oral evidence of Donald McGougan 30 November 2017 page 58:15 - 18

²⁷⁴ CEC02083448

4.27 The report was produced on 17 December 2007 and issued by Donald McGougan and Andrew Holmes, although input was obtained from various sources, and in particular from officers of TIE²⁷⁵.

4.28 It had originally been intended that the report would recommend contract close. However, because there were issues outstanding, that was not possible. Some of the outstanding issues were covered in a Briefing Note²⁷⁶ which had been emailed²⁷⁷ by Alan Coyle to Donald McGougan and Andrew Holmes on 3 December 2007, and which formed part of the papers for the Highlight Report to the Chief Executive's Internal Planning Group ("IPG") on 11 December 2007²⁷⁸. Mr McGougan states in his witness statement that "*Given these outstanding issues [raised in the Briefing Note] the position we had now reached meant that we could not recommend Contractual Close to Council at 20 December*"²⁷⁹. That was why the report at paragraph 1.2 recommended only staged approval of the contracts "*subject to price and terms being consistent with the Final Business Case, and subject to the Chief Executive being satisfied that all remaining due diligence is resolved to his satisfaction*". In addition, an action note²⁸⁰ was produced, which identified various deliverables to be taken forward²⁸¹.

4.29 Mr McGougan goes on to say:

²⁷⁵ See for example witness statement of Stewart McGarrity TRI00000059, answer 119, pages 104 to 105; witness statement of Donald McGougan TRI00000060, paragraph 78 and witness statement of Andrew Holmes TRI00000046, paragraphs 256-257

²⁷⁶ CEC01397539

²⁷⁷ CEC01397538

²⁷⁸ CEC01398245-

²⁷⁹ Witness statement of Donald McGougan TRI00000060, paragraph 66; see also transcript of oral evidence of Donald McGougan pages 170:7 to 171:13

²⁸⁰ CEC01391159

²⁸¹ Witness statement of Rebecca Andrew TRI00000023, answers 33(3) and 36, pages 35 and 37 to 38

"The briefing notes drew together a number of outstanding issues which indicated that we were not in a position to recommend Contract Close to the Council at that time (December 2007) which had been the intention in the previous timetable...It was clear that we would not be in a position in the report to Council to recommend Financial Close at that stage. The shape and content of the planned report would, therefore, would require to be amended to reflect the position as it now stood. Willie Gallagher was on the TPB and there were a number of meetings with him outwith the TPB over the course of the project. I had a number of meetings with Willie Gallagher and other TIE Executives and Andrew Holmes over the period. The subsequent report to Council on 20 December 2007... (CECO2083448) made clear that the Council sat behind TIE and ultimately carried all the contractual responsibilities. It noted that a guarantee was needed. Section 8 of that report set out on-going matters where work was continuing to ensure an acceptable outcome for the Council prior to Financial Close and allowed for all the risks that were remaining with the Council. My views on the matters set out in the briefing note attached to Alan Coyle's e-mail of 3 December 2007 were quite critical and it meant the project couldn't proceed to Contractual Close at that time. Basically my position was that if issues had been closed out then there was no point in detailing each issue which had been resolved. However, the Council had to be aware of the risks that were remaining in the project as we went forward. The final recommendation in the report to Council was to give delegated authority to the Council's Chief Executive to agree to contract closure once all the

issues had been bottomed out. The report to Council on 20 December 2007 therefore, ultimately, became a kind of holding report that recommended that powers be granted to the Chief Executive in relation to approving Contract Close. Ultimately the Chief Executive didn't feel comfortable with that level of delegation and I supported him on that. Prior to Contractual Close we came back to the elected members in May 2008. The risks that were still outstanding were included in the December report to Council. If there was a plan to resolve something with TIE then we wouldn't take the detail of each issue to the elected members until it had been resolved one way or another. The point is that there were outstanding issues which would require resolution prior Contractual Close. The report detailed the risks that were still outstanding at that stage of the project²⁸²...

...we were hoping, at one stage, that we would be able to recommend contractual close to the Council in December 2007. We went past that stage because there were still too many things to be resolved between TIE and the preferred bidder. That was a fundamental reason the report changed because we weren't now going to the Council with an idea of finalising contractual commitment. It became a recommendation that the Chief Executive be given delegated authority, however, he ultimately didn't think that that was appropriate given there were so many issues still to be resolved four months later. That is why the issue came back to the Council in May 2008²⁸³...

²⁸² Witness statement of Donald McGougan TRI00000060, paragraphs 66 to 69

²⁸³ Witness statement of Donald McGougan TRI00000060, paragraph 79

*The qualifications about price and the statement that the Chief Executive required to be satisfied in the joint report to Council (CECO2083448) were there because not all the issues surrounding diligence on the contracts had been completed. In particular, these were the issues that had been raised at the IPG in December. Those issues meant that we weren't in a position to recommend contractual close. The draft contract documentation between TIE and BBS was not complete. I understood it was still consistent with the Final Business Case and the information that was detailed to the TPB on 19 December 2007*²⁸⁴.

4.30 Mr McGougan's evidence was that the terms of the report made it clear to members that there were issues still to be resolved: *"I think they should have been aware from the contents of the report that indicated there were matters still under consideration, and the briefings that would no doubt take place round about the consideration of that report, and also the fact that the recommendation was such that there was still due diligence to take place, and that this delegated authority would only subsist if there was consistency with the Final Business Case. So that suggests very clearly, I would suggest, that there could be changes to the Final Business Case*"²⁸⁵.

4.31 Mr McGougan was asked in oral evidence whether it would have been better to delay seeking approval from members of FBCv2; Mr McGougan's evidence was that *"I don't agree that it was necessary....I*

²⁸⁴ Witness statement of Donald McGougan TRI00000060, paragraph 85

²⁸⁵ Transcript of oral evidence of Donald McGougan 29 November 2017, pages 174:21 to 175:3

*must have felt on balance that the advantages to submitting the Final Business Case Version 2 in December...outweighed the potential disadvantages...If members had considered that they hadn't enough time to properly digest the report, they could simply have continued it at the December Council for a month*²⁸⁶.

4.32 Mr McGougan also gave evidence in relation to paragraph 8.10 of the report²⁸⁷ which stated that *"The fundamental approach to the Tram contracts has been to transfer risk to the private sector. This has largely been achieved"*. Mr McGougan's evidence was that this could be said *"because by that stage the preferred bidder had bid on the basis of the outline design and the Employer's Requirements. And negotiations were going on to complete agreement about what happened to the design that remained to be developed, but it wasn't 100 per cent of the design work...on the Infraco"*²⁸⁸, and this is borne out by the opening sentence of paragraph 8.11 of the report which states *"Consistent with a project of this size and complexity, there are many different strands of work to be drawn together in the lead up to the conclusion of the main contract between tie, BBS and CAF"*²⁸⁹.

4.33 Mr McGougan's evidence was further that the report identified the unresolved key issues in the Briefing Note in summary form²⁹⁰ and that *"I don't think that it would have been wise to articulate in a public report at this stage, when negotiations were ongoing with the contractor, the*

²⁸⁶ Transcript of oral evidence of Donald McGougan 29 November 2017, pages 180:20 to 181:14

²⁸⁷ CEC02083448, page 6

²⁸⁸ Transcript of oral evidence of Donald McGougan 29 November 2017, pages 184:23 to 185:5

²⁸⁹ CEC02083448, page 6

²⁹⁰ Transcript of oral evidence of Donald McGougan 29 November 2017, page 187:8-12

issues that remained to be resolved and tie's position on them"²⁹¹. Mr McGougan did not accept the suggestion that members were not in a position to come to an informed decision "*because members were aware that timetable was that we were aiming at one stage to have contractual close certainly by maybe even before December 2007. So we were -- I think we were making them aware that there were still issues to be resolved, and that we didn't have full security over contract provisions at this time*"²⁹². Furthermore, he did not agree with the proposition that the reports to the Council generally on the Project were overly optimistic or under reported difficulties:

"...I would certainly not agree with that. I did check. There were 22 reports to the Council before contract close over the period of the project, and 15 after. And I think anyone who reads the whole suite of reports to the Council will be aware that in overall terms they were frank and gave the correct position, and said as much as we were -- it was prudent to say in the light of some commercial confidentiality issues. Now, I'm not saying to you that you can't go to some of these 35 or 37 reports and pick out individual lines or sentences that could perhaps now be regarded as over-optimistic. But I don't believe that the reporting to the Council was inaccurate over the period of the project before and after contract close"²⁹³.

4.34 The evidence of Andrew Holmes in relation to the report was that "*It explained them [the issues] to the best of our understanding at the time.*

²⁹¹ Transcript of oral evidence of Donald McGougan 29 November 2017, pages 187:22 to 188:1

²⁹² Transcript of oral evidence of Donald McGougan 29 November 2017, page 190: 7-13

²⁹³ Transcript of oral evidence of Donald McGougan 29 November 2017, pages 190:21 to 191:9

Whether our understanding was correct is another issue...Neither of us would have tried to suppress information from the members. I think I made the point about trying to present it in a concise version. We wouldn't have signed a report unless we actually believed the sentiments that were expressed within it"²⁹⁴...I accept that this particular report could have said more about the outstanding risks. It wasn't the intention to remove vast chunks of it. I think it was the intention to try and summarise the case as we assumed it at the time, that on the basis of the assurances in discussions that these issues had been dealt with. Otherwise the report wouldn't have gone up"²⁹⁵.

4.35 Whilst the evidence of Tom Aitchison was that in "*hindsight, it might have been better to have made more explicit reference in the report to Council to, at least, some of the issues raised in the Briefing Note*"²⁹⁶, his conclusion in oral evidence was that "*I think the report to the Council in December from my two colleagues was a fair report on the whole*"²⁹⁷.

4.36 Mr Aitchison also stated that:

"A. I thought it was appropriate to report to the Council. They had been advised an October report would be forthcoming. Clearly...behind paragraph 15.2"²⁹⁸ was a lot of discussion between the Director of Finance and his staff, Council Solicitor, and Director of City Development....They clearly believed it was appropriate to report. They

²⁹⁴ Transcript of oral evidence of Andrew Holmes 28 November 2017, pages 71:18 to 72:1

²⁹⁵ Transcript of oral evidence of Andrew Holmes 28 November 2017, page 74:16- 22

²⁹⁶ Witness statement of Tom Aitchison TRI00000022, paragraph 57; see also transcript of oral evidence of Tom Aitchison 28 November 2017, pages 85:19 to 86:1

²⁹⁷ Transcript of oral evidence of Tom Aitchison 28 November 2017, page 87:7- 8

²⁹⁸ Of the Briefing Note, at CEC01398245, page 96

put in the major caveat that they wanted it to be delegated to my good self to judge whether or not the contract could finally be signed, and that allowed a number of issues contained here to be taken forward. I think some months ago, I looked at the advice note that followed on from this particular meeting of the Internal Planning Group, and I think it did identify specifically named individuals to follow up on each of the reports, each of the points itemised in the report. So there did appear to me to be a management process under way to try and deal with the kind of issues that were being raised by...the B team.

Q. Did you think it appropriate to recommend that members approve the Final Business Case, given there were all of these outstanding issues?

A. Well, that was a judgment taken by my two colleagues. I'm not trying to divorce myself from my responsibility there. They were the two in charge of the project, and they clearly decided in due course that they had sufficient basis upon which to recommend moving ahead to the Council.

Q. What were your own views on whether it was appropriate to recommend at the meeting on 20 December 2007 that members approved the Final Business Case?

A. I was generally satisfied with that as a recommendation.

Q. Even against the background of all the concerns set out in the directors' briefing note we have just looked at?

*A. Yes, but I have never come across a project in senior management local government when every single aspect had been finally nailed down. There was not a question of going to contract close on 20 December. It was establishing a further process beyond which more information, more analysis could be undertaken, leading to an eventual final decision to go or not to go with the tram project*²⁹⁹.

4.37 The Briefing Note stated at paragraph 7.6³⁰⁰ that "*One option, should BBS remain concerned, would be to ask them to increase their costs by adding a "risk premium". Whilst making the project delivery perhaps more expensive, it would at least assure the members that the risk has been passed to BBS as originally intended*". This was precisely what TIE and the Council understood that they had achieved in terms of the Wiesbaden Agreement (see below in respect of TIE and the Council's understanding of the Agreement).

4.38 Furthermore, Tom Aitchison's evidence was that:

4.38.1 The report made it clear that approval was recommended "*subject to price and terms being consistent with the Final Business Case, and subject to the Chief Executive being satisfied that all remaining due diligence is resolved to his satisfaction*"³⁰¹;

²⁹⁹ Transcript of oral evidence of Tom Aitchison 28 November 2017, pages 97:6 to 98:24

³⁰⁰ CEC01397539, page 4

³⁰¹ CEC02083448, page 1 and witness statement of Tom Aitchison TRI00000022, paragraph 58

- 4.38.2 *"staff were working hard to try and ensure that, where there were significant issues to be addressed, they were being properly identified and followed through"*³⁰²;
- 4.38.3 *"TIE felt the issues that had not been dealt with at that point in time were capable of being dealt with"*³⁰³;
- 4.38.1 *"I placed reliance, in 2007 and early 2008 on the Audit Scotland view that TIE had procedures in place to actively manage risks associated with the project. Audit Scotland commended TIE for their approach to risk management and it seemed to be an aspect of the project that was under control and well managed. This, in turn, created confidence in the Council (in 2007/08) that TIE were well placed to manage risk"*³⁰⁴;
- 4.38.2 *"it was my colleagues' view that these [issues] were capable of being resolved"*³⁰⁵;
- 4.38.3 *"...there were certainly briefings behind that informally with councillors. I didn't attend all these briefings, but I do recall there being mention at the time of the fact that design was still to be complete...But the advice coming from my Council colleagues and from tie was that that was not of sufficient magnitude to cause the Council at its December meeting not to wish to proceed"*³⁰⁶.
- 4.39 Colin Mackenzie's evidence in relation to the report was that *"Risk contingencies and the final approved design were confidently said by*

³⁰² Witness statement of Tom Aitchison TRI00000022, paragraph 54

³⁰³ Witness statement of Tom Aitchison TRI00000022, paragraph 58

³⁰⁴ Witness statement of Tom Aitchison TRI00000022, paragraph 267

³⁰⁵ Witness statement of Tom Aitchison TRI00000022, paragraph 57

³⁰⁶ Transcript of oral evidence of Tom Aitchison 28 November 2017, pages 86:18 to 87:2

*TIE to be accommodated within the finding available. I did not have any concerns at that stage about this*³⁰⁷.

- 4.40 Andrew Holmes gave evidence in relation to earlier drafts of the report, and in particular the shortening of the report. Mr Holmes' evidence in this respect was that, although he could not remember the specifics,
- "...it's not a surprise. Producing reports, especially complex reports for the Council, was always an issue because you were trying to produce a report that people were actually going to -- this sounds rather blunt -- that the members were actually going to -- were going to read. Therefore it was always a question about making it clear. The clarity of the report, the length of the report, and covering...a lot of the information in appendices and background papers. The objective is not to try and obfuscate the issue, but to produce a report that the totality of members...can understand what it is that they're being recommended...to do. That was....not uncommon....in the typical week, I might be having 30 or 40 reports to different Council committees or Council going across my desk, and it was a common theme with a lot of them, the need to actually present the report in a clearer fashion so that members didn't have to wade through vast amounts...of paper. So that might well have been the reason behind the compression. I can't recall what the compression actually produced. It certainly wouldn't have been intended to try and suppress any vital information"*³⁰⁸.

³⁰⁷ Witness statement of Colin Mackenzie TRI00000054, paragraph 100

³⁰⁸ Transcript of oral evidence of Andrew Holmes 29 November 2017, pages 45:2 to 46:1

4.41 Rebecca Andrew also addressed this point in her witness statement, and in particular the removal of a reference to a contingency figure of £25m from an earlier draft of the report:

"There was no science to the £25m figure. I think Duncan [Fraser] included it to alert members of the issue and to provide an extra contingency against an unquantified risk. TIE did not want to include it for commercial reasons and because it increased the £498m headline cost of the project. While I did not support quoting an unrealistic cost, I could see why we shouldn't advertise the figure we had made available for contractor claims. At that point, we also had sufficient budget above the £498m, from which we could cover this risk"³⁰⁹.

4.42 Mr Fraser himself stated in evidence *"I did not have the full picture and hence the decision to remove them may have been based upon other information available to the Directorate to which I was unaware"³¹⁰*. The reference to *"them"* is a reference to an additional contingency of £25m for design changes and an appendix on risks.

4.43 Jennifer Dawe's evidence was that the reference in the report to the fundamental approach being to transfer risk (as referred to above) *"reflects what I remember being told about the FBC and contract, and the type of assurances we were given"³¹¹*. She notes that the report referred to the Council retaining certain risks, including agreements with third parties, utility delays and finalisation of technical and prior

³⁰⁹ Witness statement of Rebecca Andrew TRI00000023, paragraph 39(3)

³¹⁰ Witness statement of Duncan Fraser TRI00000096, paragraph 41(3)

³¹¹ Witness statement of Jennifer Dawe TRI00000019, paragraph 280

approvals, but that "*the advice that we had been given...[was] that this was reasonable*"³¹².

4.44 Jennifer Dawe's evidence was further that "*There were various issues raised in the report and we had to judge that through his [the Chief Executive's] professionalism and his use of Council Officers he would ensure that he was satisfied that they had been resolved. That is very common practice*"³¹³.

4.45 **Council meeting on 20 December 2007**

4.46 The report referred to above³¹⁴ was presented to Council by Donald McGougan and Andrew Holmes on 20 December 2007, seeking approval on FBCv2, which was granted, together with staged approval for TIE to enter into and manage contracts for the design, construction and maintenance of the tram network, the novation of the SDS Provider to Infraco and the supply of trams, on terms to be approved by TIE, and providing that remaining issues were resolved to the satisfaction of the Chief Executive.

4.47 Ewan Aitken gave evidence in relation to approval from Council being sought in October and December 2007:

"Councillor Henderson led for us on this and we went through it in real detail asking questions about income streams, capital receipts, risk levels and management. The answers we got gave us the confidence required to take it through the Council. As Leader I would not have let

³¹² Witness statement of Jennifer Dawe TRI00000019, paragraph 285

³¹³ Witness statement of Jennifer Dawe TRI00000019, paragraph 292

³¹⁴ CEC02083448

that happen, if I was not confident with all the answers. I believed, at the time, that the information I had was enough to make the judgement call. I knew there had been negotiations with pre-qualifying bidders and at least some of the information we were getting about the figures related to those conversations. Obviously we could not be part of them, but we were receiving assurances about the deliverability and cost frame and that there were bidders interested in making it happen. That is one of the key elements of knowing whether or not something has potential. I knew there was a considerable amount of work to be done before Final Close, but that is not unexpected on major infrastructure work. I certainly believed there was sufficient information for the business case to hold up"³¹⁵.

4.48 Mr Aitken also gave evidence that councillors received sufficient information, and could raise questions on specific points if they required further information:

"As a Councillor, I was kept informed of tram project developments through group briefings. We also got regular email briefings from TIE and from third party spokespeople who had separate meetings. We could also get specific information if we requested it which happened on a regular basis. We would find out information by asking questions, reading the papers, and just wanting to know more. We received a high level of information and it was very complex. To fully understand we (Councillors) needed to spend time unpicking it to make sure that we understood and could ask the questions that we needed to ask. I

³¹⁵ Witness statement of Ewan Aitken TRI00000015, paragraphs 36 to 37

*certainly feel that we had the right level of input into decisions that were our responsibility. The decisions that were our responsibility were making sure the case was made, that the communications were in place, and that finances were robust. We understood things like Optimism Bias, Risk Management and so forth. I do not recall ever being in a situation where I could not get enough information. If there were times when I needed to know more, I would know where to go to get it....If we received any information that was not clear and intelligible, or if I did not fully understand, then I would simply ask again*³¹⁶.

4.49 Reference is further made to the evidence of Jennifer Dawe in this respect: *"I never felt inhibited about asking for further information or further briefings. I do not ever remember actually asking for a briefing or a group briefing, but equally I do not remember ever having a request to discuss something coming up on the agenda refused. While I cannot recall any specific incidences where I asked for further information or briefings, I would remember if these had been refused"*³¹⁷. However, Ms Dawe also gave evidence that *"it would appear that the information that we got was not always as accurate as it should have been, particularly around the time of the contract closure (late 2007 and early 2008. Around that time, there were a lot of questions asked about risk and we were always given very general statements about how the risk level was perfectly adequate, compared favourably with other projects and that Audit Scotland thought everything was fine. It is quite possible that*

³¹⁶ Witness statement of Ewan Aitken TRI00000015, paragraphs 110 to 115

³¹⁷ Witness statement of Jennifer Dawe TRI00000019, paragraph 116

there was information that was available to some people at that time that was not imparted to us as members"³¹⁸.

State of design and MUDFA work

4.50 It had originally been anticipated that the design would be completed upon novation of the SDS Contractor to Infraco, but that did not transpire to be the case. Infraco had clarity in relation to the position from before December 2007³¹⁹. TIE's approach was a pragmatic one: "*we are where we are and we have to work our way through it*"³²⁰. Willie Gallagher sought to progress matters through liaison between Infraco and the SDS Contractor³²¹. However, the understanding of TIE was that the Infraco would take on the risk in relation to the design at contract close³²².

4.51 Brian Cox gave evidence that because the design was not complete " *a different way was found to solve that particular problem, which was to novate the whole thing within the context of a 95 per cent fixed contract*"³²³, and so the transfer of risk in respect of design development to Infraco was crucial from TIE's perspective. That was also the evidence of Jennifer Dawe³²⁴ and Lesley Hinds³²⁵.

4.52 Willie Gallagher's evidence in his witness statement is:

³¹⁸ Witness statement of Jennifer Dawe TRI00000019, paragraphs 117 to 118

³¹⁹ Witness statement of William Gallagher TRI00000037, paragraph 247

³²⁰ Witness statement of William Gallagher TRI00000037, paragraph 122

³²¹ Witness statement of William Gallagher TRI00000037, paragraph 122

³²² Witness statement of William Gallagher TRI00000037, paragraph 201

³²³ Transcript of oral evidence of Brian Cox 13 March 2018, page 151:21- 24

³²⁴ Transcript of oral evidence of Jennifer Dawe 5 September 2017, pages 96:16 to 97:16

³²⁵ Transcript of oral evidence of Lesley Hinds 6 September 2017, page 64:9-20

"I am asked why concerns about the state of the design were only emerging in December 2007. They weren't. There was clarity about where the design was. Part of the negotiating strategy for BBS was that they stated they understood the design would be complete. They were aware of where we were. They were aware of the programme to complete the design. They were aware that there would have to be agreement, as part of the process, as to where the baseline of the design was and how the remainder of the design would finish through...

This was part of their negotiating strategy. We were where we were with the designs. There were discussions taking place between all of the parties. There was prioritisation of areas which were important based on pricing and programme. I come back to the point that it wasn't that there was no design. It was just that there was further work which required to be done to finish the design. BBS had already quoted on outline design and we came to an agreement on price which included their view as to what would be needed to complete the design. There was as much information given to BBS as we could get to them. Where information wasn't available they were in discussions with PB. At the end of the day we got to a position where there was an agreement"³²⁶.

- 4.53 Matthew Crosse also addresses the question of the state of completion of the design in his evidence, concluding that the design was sufficiently advanced:

³²⁶ Witness statement of William Gallagher TRI00000037, paragraph 247

*"In an ideal world all of the design would have been completed before novation. However in practice that doesn't usually happen and on this project the design was never going to be perfectly complete by then. Our aim at novation was to have design sufficiently advanced in order that BBS felt comfortable with the risk to set a price and to accept novation. There was no need to pause the programme, we simply needed to get people to make decisions on design. There was no reason why the design could not be completed within the proposed timescale"*³²⁷.

4.54 Matthew Crosse also gave further evidence that he considered that pausing was not a realistic option:

*"Pausing the programme to allow design work to be completed was not a realistic option. The deadlines for this project had been made public and stated in the strategic business case upon which the project was approved. If we missed deadlines that would have affected the credibility of the organisations involved, the economic benefits contained in the business case and the affordability of the project. A slippage in the programme would have cost SDS money as the design contract was a fixed price contract. There was no interest in delaying the programme"*³²⁸.

4.55 David Mackay's evidence was that he could not recall any advice being given to the TIE board, the Tram Project Board or TEL by Andrew Fitchie that it would be unsafe or inappropriate to proceed in view of the

³²⁷ Witness statement of Matthew Crosse TRI00000031, paragraph 18

³²⁸ Witness statement of Matthew Crosse TRI00000031, paragraph 15

state of the design, and that *"I think if Andrew Fitchie had told me, or told the Board that it would be unsafe to proceed, then the Board would have taken heed of what he was saying"*³²⁹.

4.56 Mr Gallagher also addresses in his evidence the question of whether the Project should be paused or slowed down, but that approach was considered not to be appropriate:

"We did give consideration to whether we should slow things down. The problem was that, at that point, we had had the government change. We were burning money. TIE's running costs were about £1 million a month. I don't know what the consortium's costs were but the costs in terms of penalties for say a further three month delay would have been about £.15 million to £20 million. I think PB will say that BBS had enough information to be able to work. Also the priorities that BBS were looking for were already there. BBS were effectively saying that they weren't able to do this unless they had 100% of the design. That's not the case, they were never going to have 100% of the design. We did look at slowing things down. The reason we didn't was because that option was sub-optimal. The best option was to continue with the process we had. We had to try and get as much of the design as complete as possible... It's the principle that there was enough information to enable BBS to complete the process. Maybe BBS didn't agree with us as to how complete the design was but ultimately they must have taken a view because they signed up to the contract. I'm asked whether the pressure to carry on was purely financial. No, I

³²⁹ Transcript of oral evidence of David Mackay 21 November 2017, page 47:21-23

wouldn't say that. There were also logistical considerations. We had to consider what logistically would happen if we slowed the process down. From looking at all of the alternatives on the table, the best option was to drive this all to a conclusion"³³⁰.

4.57 Mr Gallagher clarified his point in relation to the cost of pausing or slowing down in his oral evidence:

"...the programme would have slipped, and in terms of cost of money, in terms of the amount of money that we would have needed to have funded that, just in terms of inflation, the price would have gone up....It wasn't penalties on the consortium. It was what was the total cost it was going to have to be to build it...what we looked at at that time was in terms of the cost of running the programme. What the cost of the...extension of the timelines on another six months or another year before the commissioning of the tram project would be, what the cost of financing that would be at a later time and date, what the impact on the Business Case would be by having a further delay on the Business Case coming through a bit later on. And I suppose being pragmatic about -- and would the situation and the negotiations we were having with the contractor or the Final Business Case actually improve significantly to make it all worthwhile...at that time we were also taking the view that there was significant design available....And I do think this was perhaps the precursor for going to Wiesbaden"³³¹.

³³⁰ Witness statement of William Gallagher TRI00000037, paragraphs 91-94

³³¹ Transcript of oral evidence of William Gallagher 17 November 2017, pages 47:2 to 49:2

4.58 Graeme Bissett also gave evidence in relation to proceeding with the procurement process:

"The overlap of the design process and the construction period, as a result of the Construction Contract not being delayed to allow SDS to catch up, was problematic. The planned position was that there should have been a completed design, properly documented, and then handed over. The concern was just to keep the programme moving along on the basis that more delay meant more cost...the general flavour was that the process installed to manage the design work that was outstanding should deal effectively with the involvement of the Bidder, or the Contractor by that stage, the designers and the Council's own interests in the final design. I recall a significant amount of work being done by TIE and Council people on this matter and I expect the final conclusion was that the risk could be contained and there was net benefit in proceeding with the procurement to maintain the overall programme and avoid further delays and cost exposures"³³².

4.59 Jennifer Dawe gave evidence that there was no specific imperative to proceed at this point, for example in the context of the grant funding: *"I don't remember there ever being an imperative saying: you must sign this today, or we are going to lose the 500 million; or something like that. I don't recall such an imperative"³³³.*

³³² Witness statement of Graeme Bissett TRI00000025, paragraph 108

³³³ Transcript of oral evidence of Jennifer Dawe 5 September 2017, pages 108:23 to 109:1

4.60 The status of the design was addressed in the report to the Tram Project Board for its meeting on 7 December 2007³³⁴; it was reported at paragraph 1.2.3 of the report³³⁵ that *"To 23rd November, of the 344 design deliverables, 236 have been delivered, representing 63% of the tram system design. 66% of Phase 1 A detailed design is now complete and it is expected that about 75% will be complete by the date of placement of the construction contract in Jan 2008. Some slippage occurred between V20 and V21 but the rate of progress has been recovered. This slippage is mostly due to the continuing impact of section 1 A delays"*. At the meeting which took place on 7 December 2007, Steven Bell provided an update by reference to the report³³⁶; the meeting in question was attended by, amongst others, Andrew Holmes and Donald McGougan of the Council³³⁷. Mr McGougan gave evidence that this was broadly in line with his understanding³³⁸, as did Andrew Holmes³³⁹.

Wiesbaden

Background

4.61 The background to the meeting between TIE and Infraco in Wiesbaden was a growing concern within TIE that there was not a firm price for the Infraco Contract, and the purpose of the meeting was, in the evidence

³³⁴ CEC01387400

³³⁵ CEC01387400, page 11 of 77

³³⁶ CEC01526422, page 4

³³⁷ Witness statement of Steven Bell TRI00000109, pages 26 and 29 and transcript of oral evidence of Steven Bell 24 October 2017, pages 26:16 to 27:6

³³⁸ Transcript of oral evidence of Donald McGougan 29 November 2017, page 157:16-21

³³⁹ Transcript of oral evidence of Andrew Holmes 29 November 2017, page 38:3-7

of Willie Gallagher, to obtain that firm price³⁴⁰, "*to agree the last few percentage points of costs that were outstanding*" and "*to try and achieve a target price or a fixed price*"³⁴¹.

4.62 Matthew Crosse also confirmed in his evidence the objective of achieving a fixed price at Wiesbaden:

*"At Wiesbaden the sole objectives were to get BBS to fix their price and get them to accept most of the risk of design completion. I do not think that a delay in contract close until design was complete would have made any difference"*³⁴².

4.63 This approach was consistent with the reporting to the Tram Project Board, and in particular the paper presented to it on 7 December 2007³⁴³.

4.64 There was a sequence of correspondence between the parties setting out their respective positions in advance of the negotiation that was to take place at Wiesbaden³⁴⁴.

Meeting at Wiesbaden and subsequent exchanges

4.65 TIE was represented at the Wiesbaden meeting by Willie Gallagher and Matthew Crosse. A considered decision was taken not to involve others, including lawyers because "*we wanted to speak at a senior executive*

³⁴⁰ Witness statement of William Gallagher TRI00000037, paragraph 245

³⁴¹ Witness statement of William Gallagher TRI00000037, paragraph 246; see also transcript of oral evidence of William Gallagher 17 November 2017, pages 52:20 to 53:11, 56:22-24 and 59:1-19; Witness statement of Matthew Crosse TRI00000031, paragraphs 106 and 111 and witness statement of Geoff Gilbert TRI00000038, paragraph 238

³⁴² Witness statement of Matthew Crosse TRI00000031, paragraph 84

³⁴³ CEC01023764 and witness statement of William Gallagher TRI00000037, paragraph 272

³⁴⁴ CEC01481843, CEC00547787, CEC00590611, CEC00547788 and CEC00547779

level". A legal advisor was not required as *"At that time we were not talking about the structure of the contracts or clauses"*³⁴⁵.

4.66 Willie Gallagher's evidence was that although the status of the design was discussed at Wiesbaden, *"the designs being behind schedule was not a key issue"*, but this would require to be reflected in their price (in other words, that Infraco would take the risk in relation to completion of the design)³⁴⁶.

4.67 It was TIE's understanding that the agreement reached transferred design risk from TIE to Infraco:

*"I'm asked what I consider was done at Wiesbaden in terms of design risk. We agreed a price for how it was going to transfer from being TIE's responsibility to BBS's responsibility...I am asked where the liability for development of designs lay after Wiesbaden. Once it was agreed and the contract was signed the responsibility for the completion of the final design lay with BBS... it was recognised that any further completion of design [after the baseline date of 25 November 2007] would not be a change of scope but just a, firming up of design. The further firming up of design was built into the baseline"*³⁴⁷.

4.68 The agreement reached at Wiesbaden was not considered by Willie Gallagher to be the final stage in the negotiations: *"I am asked whether, as far as I was concerned, Wiesbaden was not the final stage. No it wasn't, this is where I think the Inquiry is perhaps getting confused.*

³⁴⁵ Witness statement of William Gallagher TRI00000037, paragraphs 263 to 264

³⁴⁶ Witness statement of William Gallagher TRI00000037, paragraph 256

³⁴⁷ Witness statement of William Gallagher TRI00000037, paragraph 275

*Wiesbaden was a negotiation opportunity that we used knowing that there was a CEC meeting and knowing that BBS were very aware of CEC meeting dates. It was an opportunity to use that lever to try and help us get agreement not only from the directors but the senior directors as well*³⁴⁸.

4.69 Matthew Crosse's evidence in relation to the position achieved at Wiesbaden *"was that a price would be fixed on the basis of the design as it stood at 25 November 2007. It was known at Wiesbaden that the design would be changing but those changes would be relatively marginal. The few big problematic design areas, such as Picardy Place, were carved out of the Infraco contract but the substantive aspects of the design were in sufficiently complete enough state in order to fix the price. There was generally more design completed at this stage than typically on other previous tram schemes*³⁴⁹.

4.70 Matthew Crosse's evidence was that the stage that had been reached in completion of the design as at Wiesbaden, it would not be unreasonable to expect Infraco to fix their price:

*"In terms of them fixing the price, they have to take a view on it, and this is what constructors do, and it would not be unreasonable at this stage in the procurement, given what they knew about the design, and the prices that they got in*³⁵⁰.

³⁴⁸ Witness statement of William Gallagher TRI00000037, paragraph 276

³⁴⁹ Witness statement of Matthew Crosse TRI00000031, paragraph 112

³⁵⁰ Transcript of oral evidence of Matthew Crosse 17 October 2017, page 134:17- 21

4.71 Furthermore, it was not the case that the additional price agreed at Wiesbaden could be said to relate to relate only to fixing provisional sums. By reference to Infraco's letter of 12 December 2007³⁵¹, Mr Crosse stated:

"Q. ...If we look at the second page, we can see that the offer there is for fixed provisional sums, these specified provisional sums, in return for GBP8.12 million...f it was to be suggested that the GBP8 million was simply fixing these items and no others, what would your comment be on that?"

*A. I would say it was disingenuous....I don't think that was the intention*³⁵². Mr Crosse's evidence was that the various negotiating positions or statements made by Infraco in the period surrounding the Wiesbaden meeting and running up to the signing of the Contract Price Agreement was simply part of a tactical negotiating strategy, for example by reference to the email from Richard Walker dated 20 December 2007³⁵³ prior to the Contract Price Agreement being signed: there was exasperation with this approach:

"A. Well, they're basically resiling on their -- on the commitments they've made....It happened two or three times whilst I was in negotiations with them...I thought BBS's behaviour sometimes went too far....Again, it's - it's a managed negotiating strategy and they don't -- they can give back word all the time. I think we as public procurers stand by behind

³⁵¹ CEC00547788

³⁵² Transcript of oral evidence of Matthew Crosse 17 October 2017, pages 144:22 to 145:7

³⁵³ CEC00573351

what we say, and our approach always, but I think, you know, the constructors, right up until the point that they sign, played games with us.

Q. The suggestion there that the GBP8 million was in return for fixing items marked provisional, you would see that as the same?

A. Yes.

Q. It's game?

*A. Yes*³⁵⁴.

4.72 In relation to the same email exchange³⁵⁵, the evidence of Geoff Gilbert was that *"I am sure what Richard Walker meant was that the design would be sufficiently complete for Infracore to be able to define their responsibilities and therefore confirm their estimate for the cost of constructing the scheme. In other words, the design would be complete with the level of uncertainty as to shape, form and boundary of responsibility defined"*³⁵⁶. Mr Gilbert also explained he considered that Richard Walker's email *"was completely contrary to the agreement that we had, completely contrary to what had been agreed at Wiesbaden. Hence the exclamation marks"*³⁵⁷. In his oral evidence, Geoff Gilbert explained that the position *"was still being finalised, and there were ongoing discussions"*³⁵⁸.

³⁵⁴ Transcript of oral evidence of Matthew Crosse 17 October 2017, pages 157:4 to 158:22

³⁵⁵ CEC00573351

³⁵⁶ Witness statement of Geoff Gilbert TRI00000038, paragraph 47

³⁵⁷ Transcript of oral evidence of Geoff Gilbert 19 October 2017, page 108:14- 16

³⁵⁸ Transcript of oral evidence of Geoff Gilbert 19 October 2017, page 95:21-22

4.73 Subsequently, Geoff Gilbert circulated a revised draft of the agreement³⁵⁹ under cover of an email later on 20 December 2007 in relation to which his evidence was that "*I was trying to ensure that the intent of the Wiesbaden Agreement to fix the transfer of risk for the remaining design development to BBS was articulated*"³⁶⁰.

The Contract Price Agreement

4.74 The Contract Price Agreement, also known as the Wiesbaden Agreement³⁶¹, was executed on 20 and 21 December 2007. The Agreement provided, amongst other things:

"2.1 *The negotiated price for Phase 1a is £218,262,426. Details of the build-up to this price are set out in Appendix A.*

2.2 *The agreed Value Engineering items included in the price are set out in Appendix A3. These sums are fixed reductions save for the conditions listed in Appendix A3 under 'Key Qualifications'.*

2.3 *Provisional sums (previously normalisations) included within the price are as set out in Appendix A4. These allowances are provisional sums for the work described.*

2.4 *All other prices are fixed and firm, based on the Basis of the Price as set out below...*

³⁵⁹ CEC01495067

³⁶⁰ Transcript of oral evidence of Geoff Gilbert 19 October 2017, page 109:16- 18

³⁶¹ CEC02085660

3.3 *The BBS price for civils works includes for any impact on construction cost arising from the normal development and completion of designs based on the design intent for the scheme as represented by the design information drawings issued to BBS up to and including the design information drop on 25th November 2007. The price excludes:-*

- a) *Items designated as provision in the Appendix A4.*
- b) *Any material changes to the design resulting from the impact of the kinematic envelop of the CAF tram vehicle on the civils design.*
- c) *Excluded items, to the extent described in 3.4 below.*

In respect of footways, full reuse of existing kerbs and flags and minimal reinstatement behind kerb lines is assumed i.e. not wall to wall. Design must be delivered by the SDS in line with our construction delivery programme previously submitted.

For the avoidance of doubt normal development and completion of designs means the evolution of design through the stages of preliminary to construction stage and excludes changes of design principle, shale and form and outline specification³⁶².

TIE's understanding of the Agreement

³⁶² CEC02085660, pages 5 to 7

4.75 Steven Bell's evidence was that *"My reflection at the time was that that was intended clearly to -- ensure normal development in completion of design was the contractor's responsibility. If it was beyond normal design development, then that was likely to be a client change...If it was just the normal process of completing design, then we would expect that to be included within the price and we thought that was the language that was covered there. It has been tested at length after the fact, but certainly at that time that was our very clear understanding of the mechanics"*³⁶³.

4.76 James McEwan gave evidence in his witness statement that his understanding of the agreement was that *"BBS would absorb the risk for normal design development on novation of the SDS contract and would be well compensated for taking that risk onboard. The contract would provide standard change control mechanisms for anything regarded by the supplier as being outwith normal design development"*³⁶⁴.

4.77 Stewart McGarrity's evidence in relation to his understanding of the agreement³⁶⁵, and in particular clause 3.3, was that no risk allowance for design evolution was required because clause 3.3 *"transferred the risk of that evolution to the contractor"*³⁶⁶ and he agreed that *"there was a*

³⁶³ Transcript of oral evidence of Steven Bell 24 October 2017, pages 30:6 to 31:13

³⁶⁴ Witness statement of James McEwan TRI00000057, page 24

³⁶⁵ CEC02085660

³⁶⁶ Transcript of oral evidence of Stewart McGarrity 12 December 2017, page 150:1- 2

*conscious decision that no additional provision was required for risk*³⁶⁷.

Mr McGarrity's understanding of the exclusionary words was:

*"The changes in design principle, shape and form and outline specification, in my simple compartmentalisation, was that would be a design change that had to go through change control. So it's a change in scope. In other words...a bridge is a bridge, and when it's moving from preliminary stage to completed design, it doesn't change -- I mean, I had no appreciation either at this time or at the time that we awarded the contract that those words could be interpreted to mean any change at all as a change. I had no appreciation that that's what those words in terms of a strict legal interpretation, that that's what they would mean...I asked what that meant, and was given no indication that there had been any evolution of design that would fall out of this -- this description. And that none was expected"*³⁶⁸.

4.78 Mr McGarrity's understanding was further that an additional sum of £8m agreed for the risk transfer to Infraco: *"The resultant increase in the Infraco price, as I understand it recompense for making Provisional Prices firm and taking design development risk, was £8m"*³⁶⁹.

4.79 As referred to above, it was not considered that the agreement was the final stage in the negotiation process. Willie Gallagher's evidence was that *"the agreement became the new benchmark we were trying to achieve"*. However, reflecting the position in the eventual Infraco

³⁶⁷ Transcript of oral evidence of Stewart McGarrity 12 December 2017, page 153:14- 16

³⁶⁸ Transcript of oral evidence of Stewart McGarrity 12 December 2017, pages 151:22 to 152:16

³⁶⁹ Witness statement of Stewart McGarrity TRI00000059, answer 93, page 90 of 326

Contract "was now a very technical task that the right people with the right skills would have to achieve. It was Andrew Fitchie working with Matthew Crosse then Steven Bell who dealt with that"³⁷⁰....It was absolutely the case that follow up advice was sought as to the content of the deal. It would have been sought from Andrew [Fitchie]"³⁷¹. It was accordingly recognised by TIE that legal advice would be required in respect of the position achieved at Wiesbaden and the way in which it would be addressed in the contract documentation.

Reporting by TIE to the Council in December 2007

4.80 TIE reported to the Council in relation to risk, in terms of updated risk matrices which were issued to Donald McGougan, as confirmed in Stewart McGarrity's email of 14 December 2007³⁷². Stewart McGarrity's gave evidence is that those matrices reflected the position in relation to risk at the time³⁷³.

4.81 There was a meeting of the Legal Affairs Group on 17 December 2007³⁷⁴. At that meeting, Willie Gallagher reported to the Council that "the Infraco Contract is now at 97% fixed price with BBS taking on design risk"; this was Mr Gallagher's understanding of the position at the time³⁷⁵. Matthew Crosse also gave evidence that this "was a fair reflection of where we thought we were at that point. The number (97%) would have come from Geoff Gilbert and would have been based on the

³⁷⁰ Witness statement of William Gallagher TRI00000037, paragraph 284

³⁷¹ Witness statement of William Gallagher TRI00000037, paragraph 287

³⁷² CEC01509131

³⁷³ Witness statement of Stewart McGarrity TRI00000059, answers 84-86, pages 145 to 147 of 326

³⁷⁴ CEC01501051

³⁷⁵ Witness statement of William Gallagher TRI00000037, paragraph 201

*items in his pricing schedule and at Wiesbaden BBS had agreed to take on design risk*³⁷⁶.

4.82 A similar point was made at the Tram Project Board meeting on 9 January 2008 (whose attendees included Andrew Holmes and Donald McGougan on behalf of the Council)³⁷⁷, at item 5.4, where Mr Gallagher "*explained...Normal design risk is passed to BBS through the SDS novation*". Mr Gallagher also confirmed this in his oral evidence: "*...my understanding of the deal was that the design development risk had passed through*"³⁷⁸.

4.83 In respect of this meeting, Matthew Crosse's evidence was that "*The important thing is that BBS were pricing on documents they had seen and had agreed to a fixed price contract. The contractors had more design information than they would ordinarily done themselves by this stage*"³⁷⁹.

4.84 The evidence of James McEwan was that his understanding in relation to the matters discussed at this meeting was "*that it was proposed to novate the Design contract to Bilfinger and with the "Normal design risk" and that they would be compensated for absorbing this risk*"³⁸⁰.

4.85 A PowerPoint presentation was made by TIE (Stewart McGarrity, Steven Bell and Geoff Gilbert) to the Tram Project Board at the meeting

³⁷⁶ Witness statement of Matthew Crosse TRI00000031, paragraph 119

³⁷⁷ CEC01363703

³⁷⁸ Transcript of oral evidence of William Gallagher 17 November 2017, page 83:17- 19

³⁷⁹ Witness statement of Matthew Crosse TRI00000031, paragraph 116

³⁸⁰ Witness statement of James McEwan TRI00000057, page 23

on 19 December 2007³⁸¹, which reported on the agreement reached at Wiesbaden. The presentation reported that the "*Headlines of Deal agreed in Wiesbaden*" included "*BBS taking detailed design development risk*" and this was "*a good deal*" because "*Design development risk transferred to Infraco from this point on*". Mr Gallagher confirmed in his evidence that this reflected his understanding of the position at the time³⁸², as did Geoff Gilbert³⁸³ and Andrew Holmes³⁸⁴.

4.86 The papers for the Tram Project Board meeting on 19 December 2007³⁸⁵ included at pages 10 and 11 tables showing the change in cost, and in particular the additional payment of £8m for what TIE understood to be the transfer of design risk to Infraco³⁸⁶. The table on page 10 stated "*Current position is that 96.5% of the price is firm*".

4.87 Steven Bell's evidence of his understanding of the position at the point in time at which the Council was asked to agree Final Business Case v2³⁸⁷ was that "*Design development was the responsibility of the contractor in the construction contract*"³⁸⁸.

4.88 Stewart McGarrity's evidence of his understanding of the position at the time of the meeting and presentation was:

³⁸¹ CEC01483731

³⁸² Transcript of oral evidence of William Gallagher pages 85:8-10 and witness statement of William Gallagher TRI00000037, paragraph 281

³⁸³ Transcript of oral evidence of Geoff Gilbert page 89:16-17

³⁸⁴ Transcript of oral evidence of Andrew Holmes 29 November 2017, pages 57:18-19 and 58:18-21

³⁸⁵ CEC01526422

³⁸⁶ Witness statement of Stewart McGarrity TRI00000059, answer 101, pages 95-96 of 326, and answer 104, page 98 of 326

³⁸⁷ CEC01395434

³⁸⁸ Witness statement of Steven Bell TRI00000109, page 31

"A. That...all of the...previous provisionally priced sums had been taken...into firm and fixed. So that was part of the changes in the price, the pricing make-up. And that we'd paid GBP8 million, and that substantively what we'd got for that GBP8 million was the contractor had explicitly taken the risk of taking the designs from where they were to completion, forming their view of -- as experienced contractors as to what would change between the designs that they had and when they would be complete.

Q. How much risk did you understand tie to retain in relation to construction cost increase arising from completion of the design?

A. None except insofar as it fell to be outwith normal design development.

Q. That understanding, did that come from the briefing you got from Geoff Gilbert?

A. Yes³⁸⁹...

I believe this accurately reflected the commercial intent of the [Wiesbaden Agreement]...The basis for my own understanding was the [Wiesbaden] agreement itself and internal discussion which had taken place to assess the impact of the agreement on the overall cost estimate and risk profile³⁹⁰.

The Council's understanding of the position

³⁸⁹ Transcript of oral evidence of Stewart McGarrity 12 December 2017, pages 143:9 to 144:2

³⁹⁰ Witness statement of Stewart McGarrity TRI00000059, answers 107-108, pages 90

- 4.89 Tom Aitchison's evidence was that his *"understanding of the agreement was that the parties (TIE and BBS) had taken a number of important steps forward in relation to securing a positive outcome to the contractual negotiations, while there was still work to be done. There were no "red flags" flying saying there was likely to be a fundamental problem with the contract"*³⁹¹.
- 4.90 Donald McGougan's evidence of his understanding of the position *"was that an agreement had been reached on the principle of the transfer of design risk. This was only on the overall principle. It was not an agreement on the detailed contractual provisions. There was an update provided to the TPB about Wiesbaden on 19 December 2007"*³⁹².
- 4.91 Andrew Holmes evidence in relation to the position was that he was told *"That agreement had been essentially reached on de-risking elements that had been of concern...it was a question of premiums being applied to different elements in return for reduction in risk"*³⁹³.
- 4.92 Jennifer Dawe's evidence was that *"At that time, I probably thought that it was a fixed price contract unless there was a major change - for example, if the Council decided on a major change to the route (which was technically not possible because it was already defined in the Tram Acts) or they suddenly decided that there were to be a lot more tram stops. If there was a major issue or some fault of the Council which caused a great deal of expense, and*

³⁹¹ Witness statement of Tom Aitchison statement TRI00000022, paragraph 64

³⁹² Witness statement of Donald McGougan TRI00000060, paragraph 73

³⁹³ Transcript of oral evidence of Andrew Holmes 29 November 2017, page 56:8-16

that had not been written into the contract, then I think I always knew that might lead to additional costs. However, the headline phrase communicated to councillors always was that it was a 'fixed price' contract. I probably thought it was something like 95 or 98 percent fixed, and that the small element of variability was actually covered under the risk allowance that had been put into the project"³⁹⁴ ...

At this point, December 2007, it was obvious that the utility diversion work was not complete because there were signs of it throughout the city's streets. We definitely knew that that work had not been done, and it would also have been clear that you could not have contractors coming in to start working laying tram tracks while the road was still in upheaval. I knew that that would cause difficulties for contractors coming in. The design work is something I was not so familiar with. I knew it was not complete, but I did not know to what extent it was not complete. I suppose my assumption would have been that it had been completed to a stage that meant that the procurement process could have been gone through with a good understanding of exactly what was being asked for. As for the progress of approvals and consents, this again was in a way dependent on design, so I would have understood that that was not complete"³⁹⁵ .

Optimism bias ("OB")

³⁹⁴ Witness statement of Jennifer Dawe statement TRI00000019, paragraph 261

³⁹⁵ Witness statement of Jennifer Dawe TRI00000019; see also paragraphs 270-271 of Jennifer Dawe's statement and transcript of oral evidence of Jennifer Dawe 5 September 2017, page 127:23 to 128:10; in this context, reference may also be made to paragraph 633 of Jennifer Dawe's witness statement and that of Lesley Hinds TRI00000099 at paragraph 233

4.93 No OB allowance was made in the figures contained in FBCv2, because of the risk allowances in place. FBCv2 states that by the time of the draft Final Business Case (December 2006):

"By the time of the [Draft Final Business Case in December 2006], OB was effectively eradicated, as per the findings explained in the Mott MacDonald Review of Large Public Procurement in the UK. This was in view of greater scheme certainty and the mitigation of factors built into the procurement process, as well as project specific risks and environmental and external risks. Instead of using OB, TS and CEC adopted a very high confidence figure of 90% (P90) in the estimate of risk allowances to cover for specified risk, unspecified risk and OB. There are no proposed increased allowances for OB in addition to the above estimated risk allowances. The level of risk allowance represents a significant proportion of the project estimate value. In addition, there remains £47m headroom between the project estimate and maximum funding available. This provides comfortable headroom of 29% over base cost estimates for future costs of Phase 1a at Contract Award"³⁹⁶.

4.94 Donald McGougan was asked about this passage, and gave the following evidence:

"I am asked about the passage in the FBC that, instead of using Optimism Bias, Transport Scotland and CEC had adopted a very high confidence figure of 90% (P90) in the estimate of risk allowances to cover for specified risk, unspecified risk and Optimism Bias (para

³⁹⁶ CEC01395434, page 178, paragraphs 11.42-11.44

11.42). It must have been through my own staff. I think we were, quite possibly, taking the view that if Transport Scotland were happy, given their experience, and given the stage that the project was at, and then Optimism Bias, as such, was no longer an issue. I think, as I mentioned before, the issue was more around the level of contingency and risk built in rather than a blanket figure for Optimism Bias...This is back to my understanding of Optimism Bias being applicable in the early stages of the project and being overtaken by contingency and risk allowances later on. I am asked, when delays in the production of design and in obtaining statutory consents and approvals became evident during 2007, and when delays and difficulties became evident in carrying out the utility diversion works, whether any consideration was given to re-visiting the decision not to make any allowance for optimism bias in the estimated capital cost of the tram project, and/or to increase the risk contingency. My understanding at the time was, as I have said before, that Optimism Bias was a factor that gets applied in a fairly hefty chunk in the earlier stages of the project. I think that the risk contingency was visited and revisited throughout 2007, and it would appear from the various documents, that changes were made at various times, but the approach by TIE seems to have concentrated on reducing or controlling the risk contingency by appearing to transfer risk to the private sector. I would have expected that there would be some evidence from the minutes, to have questioned about the risk and the risk transfer and I must have been satisfied with the answers I was given³⁹⁷.

³⁹⁷ Witness statement of Andrew Holmes TRI00000046, paragraph 275 and 278

4.95 As referred to in the foregoing passage, evidence was given to the Inquiry in respect of the understanding of witnesses that the use of OB is applicable in the early stages of a project.

4.96 The evidence of Willie Gallagher was that in the early stages of building up a business case, a percentage in the order of 50% would be applied to cost. As the project matures, the OB percentage would reduce, as costs become firmer³⁹⁸

4.97 Mr Gallagher's view was that "*in an ideal world*", the levels of OB and risk built into the cost would have been higher, but this was not possible because of the funding cap. This in turn disadvantaged TIE in the negotiations with Infracore:

"The consortium used the fact that the funds were capped as a negotiating factor against us. They knew that that was all the money there was. It was a concern for them as to what would happen if the money ran out. As part of their negotiation strategy they made sure that they secured as much of the risk transfer and money as they could. If we had been a different position, where the funding cap hadn't been public knowledge, we potentially may have been able to negotiate a better deal. I am asked whether revealing that there was a funding cap resulted in PB and BBS de facto competing for as much of the funds as possible in the lead up to novation. I don't know if that was what was going through their minds but I do know that it was now a factor that wasn't there before. I think BBS found it strange that they were now

³⁹⁸ Witness statement of William Gallagher TRI00000037, paragraphs 206, 231

*bidding for a project that the government really didn't want to do. They were looking for additional guarantees on getting paid. They were concerned that the government may change their Mind on the funding again. I am asked whether I think that BBS were minded to secure the money sooner than later. I would say yes*³⁹⁹.

4.98 Geoff Gilbert gave evidence that he agreed with the approach taken in FBCv2:

"I do not think it was appropriate to apply Optimism Bias to an estimate that includes a P90 level of risk. A quantified risk assessment was undertaken and it is referred to in the estimate report that was sent to the Board in November 2006. Thereafter we applied a QRA at each stage. It is inappropriate to use Optimism Bias when one has a scheme where shape and form has been defined at preliminary design. Optimism Bias is largely for early stage estimating. By the time I arrived I thought that the designs were finished sufficiently to define shape and form. I thought they were because, in order to apply quantities, one needs to have drawings which show the different types of structures, the alignment and the general nature of the structures and work. The preliminary design drawings generally did show that. I had an awareness of Optimism Bias from previous projects before I started with TIE. However, I think it was relatively new in the 2000s. It was not a factor historically that had been applied prior to that date. There was no guidance provided to me regarding its use on the Tram Project. I believe OGC produced guidance on the use of Optimism Bias. It would

³⁹⁹ Witness statement of William Gallagher TRI00000037, paragraph 243

*all now be covered in the Treasury Green Book. Optimism Bias is gradually being superseded by more refined approaches*⁴⁰⁰.

4.99 Graeme Bissett's evidence in relation to OB was that it "*was part of the thinking in the early stages when the Tram Project was being considered. As a generality, it was driven by the Treasury arising from the background concern that public sector projects were prone to incur cost overrun. The experience seemed to be that when projects went wrong, typically the early cost estimate had been found to be very optimistic. Mott McDonald, who compiled the report proposing the use of Optimism Bias, suggested that the level of Optimism Bias was dependent on the stage of development. Basically if a project has a cost, it should have an Optimism Bias provision added to it. At the early stage, that might be 80% or 100%. Once the project has developed, this might reduce to 10/20 % or be replaced with a more specific risk provision. Optimism Bias was an addition to the estimated cost to reflect a risk the value of which could not be known at that stage*"⁴⁰¹.

⁴⁰⁰ Witness statement of Geoff Gilbert TRI00000038, paragraph 192

⁴⁰¹ Witness statement of Graeme Bissett TRI00000025, paragraph 180

5. **The events of January to May 2008**

Summary

- 5.1 During this period, as part of the negotiations to finalise the Infraco Contract, Schedule part 4 was developed using the Contract Price Agreement as a framework. TIE sought to maintain the position that had been agreed in the Contract Price Agreement in respect of normal design development, because their understanding was that the risk in this respect was passed to Infraco.
- 5.2 Despite DLA being heavily involved on behalf of TIE in negotiating Schedule part 4, TIE did not receive any legal advice from DLA of the risk that Pricing Assumption No. 1 would be interpreted in such a way as to mean that effectively the risk of design development sat with them (and reference is made to the submissions at section 3 of these submissions in this respect).
- 5.3 Infraco increased their price during this period, with agreement being reflected in the Rutland Square and Citypoint Agreements. From TIE's perspective, these agreements were intended to increase price certainty and transfer risk in return for the cost increase.
- 5.4 It was well known by all parties that the design was not complete at this stage. The Design Due Diligence report produced by BB in February 2008 was consistent with BB making enquiries in relation to the design for which it was taking responsibility and risk.

- 5.5 It was recognised that there were some issues of misalignment amongst the Employer's Requirements, the Infraco Proposals and the SDS Design, but these were to be addressed in workshops after contract close, which would yield Deliverables consistent with the Employer's Requirements. Infraco was responsible for this upon novation, and had priced for the misalignment.
- 5.6 TIE had risk management procedures in place. The QRA during this period moved from a P90 to P80 percentage likelihood that costs would come in below the risk adjusted level; P80 is more usual in large capital projects. Whilst there were concerns within the Council about whether the QRA provided for a sufficient risk allowance, it was reassured by TIE's belief that the risk for normal design development had been transferred to Infraco, the OGC position and the headroom within the funding envelope. Legal advice from DLA also reinforced that position (see section 3 of these submissions).
- 5.7 The Chief Executive authorised TIE to issue the notice of intention to award on 18 March 2008 on the basis of briefings from other senior Council officers, who gave evidence about the steps that they had taken to satisfy themselves in relation to the position. The authorisation memorandum contained a headline figure of £498m, with the risk contingency reduced from c. £49m to c. £33m as issues were closed out and resolved. There was risk to the Council in respect of delay by SDS in connection with consents and approvals, but TIE had reported that the best deal available had been achieved and the risk contingency was adequate. The risk was considered to be small and containable.

Reliance was placed on DLA's advice letter of 12 March 2008 (see the submissions at section 3 of these submissions).

The development of Schedule part 4

5.8 The background to the development of Schedule part 4 and related clauses was the Contract Price Agreement, referred to at section 4 of these submissions. The evidence of Steven Bell was that "*I considered the Wiesbaden Agreement was the frame that we expected to complete the agreement on*"⁴⁰²

5.9 Alan Coyle produced a tram briefing note which referred to the Contract Price Agreement, and which was subsequently put to the Tram Project Board, as well as the TIE and TEL boards. The briefing note reports on the Contract Price Agreement was follows:

"The discussion with BBS resulted in the signing of the "Agreement for Contract Price for Phase 1a" on the 21st December, essentially fixing the Infraco contract price based on a number of conditions. Key points of the agreement are:

- *Effective transfer of design development risk excluding scope changes to BBS;*
- *Construction programme to commence operations in Q1, 2011; and*

⁴⁰²Transcript of oral evidence of Steven Bell 24 October 2017, page 40:19- 20

- *Certain exclusion from the fixed price of items outside the scope of the tram project*⁴⁰³.

5.10 This accorded with the understanding of TIE officers, as reported to the Council in December 2007, as referred to above in connection with the events of December 2007.

5.11 The drafting and finalisation of Schedule part 4 took place between January and March 2008.

5.12 Initially, drafts passed between principals from TIE, BB and Siemens:

5.12.1 A draft was issued under cover of an email from Bob Dawson to Scott McFadzen and Michael Flynn as "*an outline framework*" in relation to which it was recognised that further work was required⁴⁰⁴;

5.12.2 A fresh draft was issued by Scott McFadzen to TIE on 4 February 2008⁴⁰⁵;

5.12.3 TIE issued a revised version of Infraco's draft on 19 February 2008, under cover of an email from Bob Dawson⁴⁰⁶.

5.13 It can be seen from the foregoing documents that TIE sought to maintain the position that had been agreed in the Contract Price Agreement in respect of normal design development, because their understanding was that the risk in this respect was passed to Infraco.

⁴⁰³ CEC01398233 and CEC01398234

⁴⁰⁴ CEC01447268

⁴⁰⁵ CEC01448377

⁴⁰⁶ CEC00592621

5.14 Subsequently, the parties' legal advisers became involved in the negotiation of Schedule part 4. As referred to at section of these submissions, TIE did not receive any legal advice from DLA of the risk that Pricing Assumption No. 1 would be interpreted in such a way as to mean that effectively the risk of design development sat with them.

5.15 The exchanges between the parties, and in particular those which involved DLA, included the following:

5.15.1 On 6 February 2008, Andrew Fitchie received a draft of Schedule part 4. He noted that he had not seen it previously, but "*I am reading into it now*"⁴⁰⁷ and "*I have seen for the first time Schedule 4 (Pricing) plus assumptions this morning. It is assembled as a contract within a contract. I really need to understand this document to contribute meaningfully*"⁴⁰⁸. There was subsequently ample opportunity for Mr Fitchie to read and understand Schedule part 4;

5.15.2 Ian Laing issued a draft of Schedule part 4 on 22 February 2008 to Andrew Fitchie, Geoff Gilbert and Bob Dawson⁴⁰⁹. Iain Laing's comments included a note that "*The description of 'normal design development' is not satisfactory. Input will be required by the legal teams but it would be helpful to understand what is intended to be included in such 'normal development'*". In relation to clause 80, Mr Laing noted "*We are not clear why the drafting proposed by BBS has not been adopted here. Clause 80 contains a procedure which in*

⁴⁰⁷ CEC01513659

⁴⁰⁸ CEC01501176

⁴⁰⁹ CEC01449876

practice is unlikely to be appropriate for pricing assumptions. The reason is that clause 80 envisages a change mechanism and agreement as to the price of the change prior to the change being implemented. This, in turn, envisages that there may be circumstances where the change is then withdrawn. That would not be an option for a notified departure. If the concern is to link the valuation to the methodology set out in clause 80, the intention of the BBS drafting was to capture this principle. We will also require a discussion as to payment for actual costs as they are incurred in the event that there is a dispute as to the value of the impact of the notified departure. As has been discussed previously, BBS cannot assume the cash flow risk on notified departures";

5.15.3 On 6 March 2008, Bob Dawson issued a revised draft of Schedule part 4 to Pinsent Masons and others, including Andrew Fitchie⁴¹⁰;

5.15.4 On 10 March 2008, Bob Dawson issued revised wording in relation to what eventually became clause 3.5 of Schedule part 4 in relation to Notified Departures to Pinsent Masons and others, including Andrew Fitchie⁴¹¹;

5.15.5 On 13 March 2008, Pinsent Masons issued a revised draft of Schedule part 4 to Andre Fitchie and others, commenting *this document contains the "legal" drafting as discussed yesterday*⁴¹²;

⁴¹⁰ CEC01450309

⁴¹¹ CEC01450544 and DLA0006382

⁴¹² CEC01450765

- 5.15.6 On 20 March 2008, DLA circulated a revised draft of Schedule part 4 which had been agreed at a meeting that day, noting "*Please find attached Schedule 4 as agreed today on screen. Please note the various actions on both sides, as footnoted, to bring this document to a close. Thank you all for a productive session*"⁴¹³.
- 5.16 Many of the key terms contained in the draft of Schedule part 4 circulated by DLA on 20 March 2008 were not subsequently amended prior to contract close.
- 5.16.1 The description of the Construction Works Price is as in the finalised Infraco Contract;
- 5.16.2 The definitions of Base Case Assumptions, Base Date Design Information and Notified Departure was in all material respects as in the finalised Infraco Contract;
- 5.16.3 Pricing Assumption No.1 was in all material respects as in the finalised Infraco Contract.
- 5.17 There were provisions which were yet to be developed fully, specifically:
- 5.17.1 Clause 3.2.1 of Schedule part 4 was yet to be developed to explain the rationale behind the Pricing Assumptions, and that they might give rise to a Notified Departure immediately upon contract formation;
- 5.17.2 Clause 3.5 of Schedule part 4 was yet to be fully developed in relation to the way in which the Base Case Assumptions might give rise to a

⁴¹³ CEC00327764

Notified Departure, and the consequences of delay in TIE issuing a Change Order when a Notified Departure occurs.

5.18 Following the meeting and revised draft of 20 March 2008, there were further exchanges between the parties and their legal advisers, and a subsequent meeting on 25 March 2008. This led to further revised drafts being circulated as follows:

5.18.1 A revised draft was issued by Pinsent Masons on 27 March 2008, the recipients of which included Andrew Fitchie⁴¹⁴:

5.18.2 A further revised draft was issued by Pinsent Masons 2 April 2008, the recipients of which included Andrew Fitchie⁴¹⁵. This document contained provisions in relation to the explanation of the Pricing Assumptions in clause 3.2 and in relation to Notified Departure in clause 3.5 which were materially aligned with the provisions that were eventually executed in the Infraco Contract.

5.18.3 Subsequent drafts were exchanged and discussed during April 2008, although the changes did not relate in any material way to the question of risk allocation in relation to design development and Notified Departures⁴¹⁶.

5.19 At the request of TIE⁴¹⁷, DLA carried out a QA review of Schedule part 4; DLA's email of 22 April 2008 reported on the results of the review, and made no reference to the terms of Pricing Assumption No. 1: On 22

⁴¹⁴ CEC01451209

⁴¹⁵ CEC01451434

⁴¹⁶ See for example CEC01548431, CEC01541476, CEC01293878, CEC01293885, CEC01294194, CEC01294194

⁴¹⁷ CEC01374219

April 2008, DLA was asked by Dennis Murray of TIE to carry out a QA review of Schedule part 4: *"We have carried out a QA review of the Pricing Schedule. There are various inconsistencies with the main contract. We have tidied up some of the defined terms, however there are also numerous items with regard to which we have taken a view, given the length of time that it has taken to negotiate this Schedule"*.⁴¹⁸

5.20 The Council was not involved in the negotiations relating to Schedule part 4. It did, however, request a copy of Schedule part 4 from TIE prior to contract close: on 20 March 2008, Rebecca Andrew emailed TIE to say *"Could you also ensure that the Council gets a copy of Schedule 4 of the contract? – Donald [McGougan] and Andrew [Holmes] specifically requested this at the last IPG meeting"*⁴¹⁹.

5.21 A copy of Schedule part 4 was issued to the Council by TIE under cover of Stewart McGarrity's email to Alan Coyle of 15 April 2008⁴²⁰. This was circulated by Alan Coyle to others within the Council (Colin MacKenzie, Gill Lindsay, Steve Sladdin, Nick Smith and Andy Conway) on the same day⁴²¹.

Rutland Square Agreement

⁴¹⁸ CEC01293506

⁴¹⁹ The IPG meeting prior to the email being sent had been on 19 March 2008

⁴²⁰ CEC01245223

⁴²¹ CEC01245223

5.22 The Rutland Square Agreement⁴²² was entered into on 7 February 2008. It addressed Schedule part 4 of the Infraco Contract in high level terms only, stating:

"2.5 Schedule 4 (Contract Price Analysis) is to:

2.5.1 contain detailed bottom up price build up and description of scope for each element which is to be provided by noon on 13 February 2008 in the case of Siemens and noon on 14 February 2008 in the case of BB;

2.5.2 concept of draft limbs (n) and (o) (in the BBS Consortium draft presented on 6 February 2008) are not acceptable and are not to be included in Schedule 4 (Contract Price Analysis) or in the Infraco Contract or either of the novation agreements.

2.5.3 limb (c) is deleted;

2.5.4 notified departures are dealt with under Clause 80 (tie Changes) of the Infraco Contract;

2.5.5 value engineering will be dealt with in accordance with the Wiesbaden Agreement dated 20 December 2007..."

Accordingly, the Rutland Square Agreement did not deal specifically with Pricing Assumption No. 1, or the concept of design development.

5.23 The Rutland Square Agreement did not bring an end to negotiation in respect of Schedule part 4; reference is made by way of example to the email dated 12 February 2008 from Geoff Gilbert to Richard Walker⁴²³.

⁴²² CEC01284179

5.24 Steven Bell's evidence in relation to the Rutland Square Agreement was that it was intended to increase certainty in relation to price for an additional payment of £8.6m, and he referred to his with reference to his email of 10 March 2008⁴²⁴, and said:

"From a TIE perspective, Jim McEwan and I were concerned that there were a couple of assumptions or pricing variables that did not give TIE the certainty that we had expected. Some of these flowed over from the Wiesbaden Agreement that Willie Gallagher and Richard Walker had agreed back in December. We sought to take away the option for Infracore to argue for more money later on and before we went to a final agreed price with the Council".

5.25 Although the Rutland Square agreement provided that the price was not to be increased except under two circumstances to do with the misalignment of Employer's Requirements and the SDS residual design issue, Infracore did seek further price increases, which are addressed below.

Citypoint Agreement

5.26 A further agreement was entered into on 7 March 2008 known as the Citypoint Agreement⁴²⁵, which provided for a further cost increase of £8.6m.

5.27 Steven Bell gave evidence in relation to his email of 10 March 2008 reporting on the terms of the agreement to Geoff Gilbert and Jim

⁴²³ CEC00592619

⁴²⁴ CEC01463888

⁴²⁵ CEC01463888

McEwan that this cost increase was in return for, amongst other things "Acceptance by BBS of any SDS design quality risk and subsequent time impact". Mr Bell stated in evidence "The entry in here was around BBS accepting responsibility if the design provided was...not capable of being accepted by the approving authorities. So it was about the quality of that, and if it had to be reworked, they were very clear that that was a risk they were prepared to formally confirm and accept in this"⁴²⁶.

Base Date Design Information

- 5.28 It was settled for some time prior to contract close that Base Date Design Information was to be defined by reference to an Appendix to Schedule part 4, which provided that "*Base Date Design Information means the design information drawings issued to Infraco up and including 25th November 2007 listed in Appendix H to this Schedule Part 4*".
- 5.29 Infraco was to provide the information to enable a list to be provided in Appendix H, but failed to do so. In the absence of a list of drawings provided by Infraco, or any advice from DLA that this wording was not sufficiently precise, this wording was incorporated into the Infraco Contract.
- 5.30 The wording was to give rise to disputes after contract formation both in terms of which drawings had been issued or shared via the dataroom, and in terms of the proper interpretation to be given to "*available*": in high level terms, Infraco interpreted this as meaning the drawings which

⁴²⁶ Transcript of oral evidence of Steven Bell 24 October 2017, page 86:16- 22

had been transmitted to it. TIE interpreted the word as meaning the drawings to which Infraco could have had access had it requested the material.

- 5.31 Steven Bell gave evidence that "*It would have provided increased clarity*" if a schedule of documents had been provided⁴²⁷

Clause 80

- 5.32 Clause 30.5 of Schedule part 4 provides that Notified Departures are to be dealt with as a Mandatory TIE Change, and therefore are regulated by clause 80.

- 5.33 Earlier drafts of clause 80 provided that⁴²⁸ provided that "*for the avoidance of doubt, the Infraco shall not commence work until instructed through receipt of a tie Change Order*", with no further wording (other than in circumstances where there was a disputed Estimate). Subsequently, on 15 January 2008, DLA added the words "*unless otherwise directed by tie*" to the end of clause 80.13. This wording was in all material respects the final wording adopted in the Infraco Contract, so that the end of clause 80.13 provided:

"Subject to Clause 80.10.1 [which eventually became clause 80.15 in the executed contract], for the avoidance of doubt, the Infraco shall not commence work until instructed through receipt of a tie Change Order unless otherwise directed by tie".

⁴²⁷ Transcript of oral evidence of Steven Bell 24 October 2017, page 134: 14-18

⁴²⁸ See for example the email from Pinsent Masons to TIE, DLAP and others on 4 December 2007 at CEC01493840

5.34 The words which were introduced by DLA were to become a major area of controversy in the context of the disputes between TIE and Infracore in respect of whether TIE was entitled to require Infracore to proceed with work which was the subject matter of a disputed Notified Departure. This had a major impact on the progress of the work. Reference is made in this respect to the submissions at section 19 of these submissions.

Design

Design due diligence report

5.35 On 18 February 2008, BBS produced a Design Due Diligence Summary Report⁴²⁹.

5.36 Steven Bell's evidence in relation to the report was that:

"I agree TIE's original intention back in 2006/07 was to have a completed design but it had been clear since the summer of 2007 that the Infracore was not going to have the full completed design so there is some selective editing...In addition, circa 60% was considered as complete design and that included what SDS and TIE considered was the majority of the significant or critical design elements. That was clearly set out and covered accordingly. The idea that "the final concepts for these are unknown to us" might be their statement from December 2007 but it does not gel with me because most of those critical issues were discussed and shared. I would be surprised if there

⁴²⁹ CEC01449100

were critical locations that were not in that category. What they do say in their third paragraph is, "Where detailed design is available, it is mostly of an acceptable standard". I think my view would be that they had most, if not all, of the critical elements and, therefore, they understood the direction of travel and the material issues...It was my clear understanding that Infraco had accepted an element of design development and that that was their issue to resolve and that they accepted any things arising from their own systems proposals as being their responsibility as well" ...The principle was set out there [in the Wiesbaden Agreement] and I would expect normal design development to continue from that point and to be part of the original price that was included⁴³⁰.

Reference is further made in this respect to the submissions at sections 0 and 4 of these submissions in relation to the understanding of TIE and the Council in relation to the transfer of design risk to Infraco.

5.37 In his oral evidence to the Inquiry, Steven Bell agreed that *"if the consortium were going to accept any design risk, then carrying out a thorough due diligence on the design available would be an important aspect to them in deciding what design risk, if any, to accept"*⁴³¹. Accordingly, the production of the report was therefore consistent with TIE's understanding that risk had been transferred to Infraco; Mr Bell stated that *"It was clear that the procurement strategy to complete the design before novation was not going to be successful. We sought,*

⁴³⁰ Witness statement of Steven Bell TRI00000109, paragraph 25

⁴³¹ Transcript of oral evidence of Steven Bell 24 October 2017, page 71:5- 10

*therefore, to identify and clarify the basis of the price for the Infraco, and we firmly and clearly considered that that was based on what was known in the November 2007 baseline, and allowed for, in our view, very clearly normal design development to completion...So I think it was acknowledged that the original strategic intent of the completion of design prior to novation and contract award was not going to be the case. An appropriate protection for all parties we considered had been put in place. However, there clearly later emerged a difference in view as to what was transferred from normal design development risk and what was -- and what the Infraco considered that to be*⁴³².

5.38 Mr Bell also stated in oral evidence that "*there were elements [of the due diligence report] that were encouraging in that they noted specifically the design that had been completed was of acceptable or adequate quality. I think that was positive for all parties. It identified there were some significant areas that were not complete, and you've referred to things like some of the approvals. So those were known issues at the time, and I don't think it fundamentally changed the fact those were issues still to be addressed or were in the process of being addressed at the time, partly through the conclusion of the negotiations on the Infraco contract*"⁴³³.

5.39 It was put to Mr Bell that the report should have been sent to the Council. His view on that point was that the Council was already aware

⁴³² Transcript of oral evidence of Steven Bell 24 October 2017, pages 76:22 to 77:16

⁴³³ Transcript of oral evidence of Steven Bell 24 October 2017, pages 77:21 to 78:7

that the design was not complete⁴³⁴, and reference is made in this respect to section 4 of these submissions which does confirm that to be the case.

5.40 Willie Gallagher's evidence was that the motivation behind BBS producing the due diligence report was tactical, to gain commercial advantage. He stated that "*BBS had lost control of their supply chain. I think that they needed stalling tactics. It all became apparent when it actually came to signing the contract because they asked for more money. I think there were other factors at play. Stating the design was incomplete isn't exactly a red herring but it was a negotiating technique as part of a bigger strategy*"⁴³⁵. Mr Gallagher also made the point that "*I think the Inquiry must not buy into this theme that BBS were incapable of building the ETP in the absence of 100% of the design being complete on day one. The detailed design in certain areas still had to be completed but that was prioritised. The design that enabled BBS to firm up their price to something like 95% to 98% of the budget was in place. The SDS contract was always going to be novated, it's just the fact that PB didn't intend to work for a period of time under BBS. If their design had been complete then their work would have been complete*"⁴³⁶.

Alignment

⁴³⁴ Transcript of oral evidence of Steven Bell 24 October 2017, pages 78:17 to 79:18

⁴³⁵ Witness statement of William Gallagher TRI00000037, paragraph 121

⁴³⁶ Witness statement of William Gallagher TRI00000037, paragraph 173

5.41 Pricing Assumption No. 3 in Schedule part 4 of the Infraco Contract provided that "*The Deliverables prepared by the SDS Provider prior to the date of this Agreement comply with the Infraco Proposals and the Employer's Requirements*".

5.42 Steven Bell gave evidence that there were some areas of misalignment, but these could be addressed through planned workshops after contract close:

"I think SDS had warranted that their proposals would achieve those Employer's Requirements...There was amendments and alignments to the Employer's Requirements and confirming the SDS proposals were going to achieve those. As part of integrating Infraco proposals, there were planned to be workshops for that...And if there were minor changes to that, we would expect to deal with that beyond it, but there was no fundamental misalignments as I recall....I considered it [Pricing Assumption No. 3] to be correct, but there may have been found at these workshops examples where it was not aligned, in which case if there was an entitlement to change matters, then it could utilise the Notified Departure mechanism"⁴³⁷.

5.43 The SDS Novation Agreement⁴³⁸ provided at clause 4.6 that "*tie warrants that it has received a report from the SDS Provider... setting out the misalignments between the Deliverables completed prior to the date of this Agreement and the Employer's Requirements and that it has issued initial instructions to the SDS Provider in relation to*

⁴³⁷ Transcript of oral evidence of Steven Bell 24 October 2017, pages 147:9 to 148:7

⁴³⁸ CEC01370880

addressing all such misalignments. Upon completion of the work entailed to resolve the misalignments, the SDS Provider confirms to tie and the Infraco that such Deliverables shall be consistent with the Employer's Requirements".

5.44 In his evidence, Steven Bell agreed with the proposition that it had been recognised prior to close that there was a misalignment between the SDS design and the Employer's Requirements, and this misalignment would be addressed after close through a series of workshops, although work was already under way in this respect prior to close⁴³⁹.

5.45 Mr Bell also gave evidence that it recognised that it was likely that there would be Change Orders after completion in relation to aligning the design with the Employer's Requirements and the Infraco Proposals⁴⁴⁰.

5.46 Damian Sharp gave evidence in relation to the issue of alignment: *"There were three items to consider — the Employer's Requirements, the SDS Design and the Infraco proposals. The Employer's Requirements was what TIE had asked to be delivered by the Infraco. The SDS design was supposed to have delivered the Employer's Requirements and the Infraco was allowed to propose to deliver differently as long as the same outcomes were achieved. Inevitably the designer's design and what Infraco wanted to build would be different. The process was ongoing to work out whether some of the proposals from Infraco were acceptable and how to finish up with one design which was then going to be built on the ground. Ultimately by novating*

⁴³⁹ Transcript of oral evidence of Steven Bell 24 October 2017, page 161: 5 -13

⁴⁴⁰ Transcript of oral evidence of Steven Bell 24 October 2017, pages 163:19 to 164: 23

*SDS to Infraco design alignment became Infraco's problem and the contract should have led to Infraco managing design completion. All of that was taken into account in the actual contract wording for the design going forwards and it was highlighted that there were practical risks about what had to be achieved*⁴⁴¹.

5.47 As referred to above, Mr Sharp's understanding of the position was that after novation, alignment was at Infraco's risk:

*"I understood that BSC bore the liability for incomplete design; that BSC had priced for the fact that the design was incomplete and for outstanding statutory approvals and consents; that BSC had priced for misalignment and that TIE were only liable where the changes went beyond the normal design development, which was defined in the contract. That required to be followed through to agree the BDDI so that it could be determined if the final design had changed. The Notified Departures arose where there were changes that were not part of the normal design development...Whether any given misalignment was TIE's liability depended on why there was misalignment. Arguably if SDS had not designed something that was in accordance with the Employer's Requirements then that risk had to go to BSC*⁴⁴².

Novation

5.48 Willie Gallagher gave evidence in relation to the attitude of the SDS Provider and Infraco to novation, but concluded that the design was

⁴⁴¹ Witness statement of Damian Sharp TRI00000085, paragraph 199

⁴⁴² Witness statement of Damian Sharp TRI00000085, paragraphs 306 to 307

sufficiently complete: *"PB didn't want to novate to BBS. Conversely BBS never wanted PB working below them. They would always state that the design wasn't complete. The design was complete to a line which was certainly complete enough to allow BBS to tender against the job. The design was sufficient enough for BBS to be confident enough in terms of what they were going to do. It was sufficient enough for BBS to be confident in terms of their obligations under the contract"*⁴⁴³. Further, it was considered that *"there was no serious alternative to working with PB...Whatever way you looked at the risk or the cost, the most cost effective approach to take was just get this part of the design finished"*⁴⁴⁴.

5.49 In the event, the novation agreement was entered into⁴⁴⁵. The scope of work covered by the novation agreement as in 4 phases: (I) Requirements Definition; (II) Preliminary Design; (III) Detailed Design and (IV) Construction Support. Phases (I) and (II) were complete as at novation⁴⁴⁶. The status of Phase III was set out at Appendix part 4, clause 5 of the novation agreement⁴⁴⁷:

5.49.1 Detailed Design Packages: 296 out of 329 packages delivered, with 33 remaining to be delivered.

5.49.2 Prior Approvals: 22 out of 63 approved, with 41 remaining to be delivered.

⁴⁴³ Witness statement of William Gallagher TRI00000037, paragraph 85; see also paragraph 109 of the statement

⁴⁴⁴ Witness statement of William Gallagher TRI00000037, paragraph 86

⁴⁴⁵ CEC01370880

⁴⁴⁶ CEC01370880, page 84

⁴⁴⁷ CEC01370880, page 85 to 86

5.49.3 Technical Approvals: 30 out of 128 approved, with 98 remaining to be delivered.

Risk

5.50 There was evidence from witnesses that TIE's approach to risk management was effective. Graeme Bissett gave evidence that "*TIE had a well-developed risk management approach at the time, around 2008, involving Mark Bourke and also Mark Hamill as Risk Managers. Susan Clark and the Risk Managers were professional people and their roles were as dedicated professionals on the risk management case. I thought risk management, including how the risks in the risk register were translated into the quantified risk assessment in the budgets, was handled effectively*"⁴⁴⁸.

5.51 Mark Hamill was the Risk Manager for TIE for the period between May 2007 and May 2010⁴⁴⁹. In his witness statement⁴⁵⁰, Mr Hamill explained the risk management process used by TIE:

"The risk management process followed the ISO: 31,000 International Risk Management standards and also the guidelines for risk management provided within the Project Risk Analysis and Management (PRAM) guide by the Association of Project Management (APM). This process required the various teams within the project to identify and assess risks relevant to their respective areas. Facilitated by myself, the Risk Manager, these various teams were responsible for

⁴⁴⁸ Witness statement of Graeme Bissett TRI00000025, pages 30 to 31, paragraph 79 ; see also paragraph 179 of the statement

⁴⁴⁹ Witness statement of Mark Hamill TRI00000042, paragraph 1

⁴⁵⁰ TRI00000042

identifying risks and thereafter each team would offer support to and be responsible for the action plans designed to mitigate any risks Identified. Each risk and action plan was assigned an owner from within the project team and project directors. The product of this process was a Project Risk Register (PRR). The project used the risk management software Active Risk Manager (ARM). This is a recognised risk management tool, which acts as a database for recording and reporting risk information. The system provided an auditable record of all risk management information relevant to the project....Each element of the project had its own risk register and these combined would form the PRR⁴⁵¹.

5.52 Mr Hamill also explained the QRA and its use of the Monte Carlo Simulation:

"One definition of Quantitative Risk Analysis (QRA) is that it is the process of numerically analysing the effect of identified risks on project objectives. The Monte Carlo Simulation (MCS) is a recognised industry technique used to understand the impact of risk on a project. The project conducted cost QRAs using the MCS. When using MCS, uncertain inputs in a model are represented using a range of possible values, this is known as probability distributions. By using probability distributions, variables can provide different probabilities of different outcomes occurring. Probability distributions are a much more realistic way of describing uncertainty in variables of risk analysis. During an MCS values are sampled at random from the input probability

⁴⁵¹ Witness statement of Mark Hamill TRI00000042, paragraph 5

distributions. In the cost QRA exercise on the project the inputs were the percentage likelihood of each risk and a three point estimate of the financial impact of each risk. The three points were minimum, most likely and maximum. Each set of samples is called an iteration and the resulting outcome from that sample is recorded. MCS does this thousands of times resulting in probability distributions of possible outcomes. The output of this exercise would be a probabilistic range of values which informs senior management decisions on what we called the Project Risk Allowance (PRA)"⁴⁵².

5.53 As referred to at section 4 of these submissions, TIE had produced a QRA in December 2007. The document was subsequently updated in the period between January and May 2008.

5.54 During this period, the risk allowance which had been reported at P90 in FBCv2 (see section 4 of these submissions) was reduced to P80. This refers to the percentage likelihood that the costs will come in below the risk adjusted level. Mark Hamill gave evidence that P80 is more usual in large capital projects than P90⁴⁵³.

5.55 Prior to contract close, the QRA was circulated within TIE by Stewart McGarrity⁴⁵⁴. The spreadsheet attached to his email summarised the financial position in relation to the movement in the risk contingency as follows:

⁴⁵² Witness statement of Mark Hamill TRI00000042, paragraph 7

⁴⁵³ Transcript of oral evidence of Mark Hamill 19 October 2017, page 58:11-13

⁴⁵⁴ TIE00126754

5.55.1 As at the Contract Price Agreement in December 2007 the transfer required from the risk contingency to the price was £7.075m;

5.55.2 As at the Rutland Square Agreement on 7 February 2008, the transfer required was £11.406m;

5.55.3 As at May 2008, the transfer required was £17.806m.

5.56 Rebecca Andrew considered this document on behalf of the Council, and whilst she expressed some concerns, she noted the headroom available between project cost and available funding:

*"QRA provides insufficient cover for design risks (we are reliant on tie's project and risk management expertise to set an allowance at an appropriate level). We can take comfort from the fact that the OGC said the £50m at FBC stage was "about right" and would have expected this number to come down at final deal. We also have additional headroom between the project cost and available funding. Use of headroom, however, would make 1b even less affordable"*⁴⁵⁵.

5.57 On 4 March 2008, TIE gave a briefing to the Council in relation to the QRA (which is addressed above). Following that meeting, Rebecca Andrew issued an email to Stewart McGarrity and others at TIE and the Council which noted a number of actions for TIE, but concluded that *"we were reassured by your statement that the current level of the risk allowance (approximately £30m) as determined by QRA was sufficient,*

⁴⁵⁵ CEC01222041

based on your knowledge of the project and considerable experience of other major projects"⁴⁵⁶.

5.58 On 16 April 2008, Andy Conway raised a query in relation to whether a sufficient allowance had been made in respect of the design:

*"I've got a couple of specific questions, which I hope you'll be able to provide further info. As a general comment though, have tie identified costs for all items that will require BBS changes? The scope of the works related issues refer to the status of the design as of 25th November. Our concern is that if the design has changed, or at least developed, since then (and say a prior approval has been granted) then a change will need to be issued. Have tie undertaken an exercise to determine the extent and cost of changes that will be required since the design freeze in November?"*⁴⁵⁷

5.59 The responses of Steven Bell and Susan Clark to this email reflected their understanding that risk in this respect had been transferred to Infracore:

5.59.1 Steven Bell responded "*The logic behind the November "freeze" allows for all normal design development at no extra cost*".⁴⁵⁸

5.59.2 Susan Clark responded "*BBS are contractually obliged to construct to the designs that SDS produce and get consented. We have been identifying significant changes as design has progressed to ensure that we have made financial provision – e.g. Burnside Road. Normal design*

⁴⁵⁶ CEC01506128

⁴⁵⁷ CEC01355447

⁴⁵⁸ CEC01297322

*development is a BBS risk as described in Schedule 4 of the Infraco contract*⁴⁵⁹.

- 5.60 Tom Aitchison's understanding of the position in relation to risk (by reference to the period around March 2008) was that the position remained broadly as had been reported in FBCv2:

*"I had no information or advice at the time to lead me to believe that Infraco's price and terms had departed in any significant way from the Final Business Case. The percentage movement in costs was around 2%"*⁴⁶⁰...

*My understanding of the main risks retained by the public sector, including, in particular, any risks and liabilities arising from incomplete and outstanding design, approvals and consents, were regularly referred to in Council reports. The point was repeatedly made that the risks retained by the public sector were utilities, incomplete design work, third party agreements and approvals and consents. These were the main areas of risk. That is stated all the way through from the initial draft business case to final business case and in various Council reports beyond that*⁴⁶¹.

Notice of intention to award

- 5.61 It was against the foregoing background that Tom Aitchison authorised TIE to issue the notice of intention to award in terms of the document

⁴⁵⁹ CEC01335547

⁴⁶⁰ Witness statement of Tom Aitchison TRI00000022, paragraph 99

⁴⁶¹ Witness statement of Tom Aitchison TRI00000022, paragraph 103

dated 18 March 2008⁴⁶². The document was issued by Andrew Holmes, Donald McGougan and Gill Lindsay, and stated "*we consider that it is appropriate to accept tie's recommendation to you to authorise and permit them to immediately lodge the Notice of Intention to Award*". The document was countersigned by Tom Aitchison, under the endorsement "*I, Tom Aitchison, Chief Executive of the City of Edinburgh Council, having received the request from tie and the information detailed above, agree and confirm that tie Limited may immediately lodge the Notice of Intention to Award Contract*".

5.62 The document reported on the position in respect of proceeding to financial close and noted that

"The closure of due diligence issues have been progressing well as you aware. In essence, the position which is now closing at the Notice of Intention to Award stage, shows some adjustment in price and risk consistent with the further negotiations which have been undertaken since the period from financial close. In essence, as reported to you personally on 13 March 2008, the headline figure for the Project including costs and risk contingency in the final business case version 2 was £498 million as the best estimate to be put into the public domain. This was shown as being the estimate in the Report of 20 December 2007. Following closure of a number of issues and further negotiations and resolution of a number of issues, including the extensive issue relating to the SDS novation, the final contract price estimate is now, as advised by tie to us, the sum of £508 million. In approximate figures the

⁴⁶² CEC02086755

risk contingency within this has been reduced from £49 million to £33 million as part of the closure process. As discussed at our meeting yesterday in addition to this alteration to finance, the negotiations have required and provided for a 3 month extension to the programme and a range of adjustments to the risk allocations. Many of these adjustments to risk allocation are positive, reflecting the reduced risk contingency. There are some which do pass additional risk to the public sector. Of these, the most important is considered to be SDS. As you are aware, this has been a very difficult point for tie to negotiate and they have provided for the best deal which they advise us is currently available to themselves and the Council. In essence, the contractor BBS will accept the design risk for SDS to a high financial ceiling, whereas the Council and tie must remain financially liable for delay by SDS in relation to the provision by them of information for a range of consents and approvals. Both tie and the Council have worked diligently to examine and reduce this risk in practical terms and tie advises that the new risk contingency contains suitable adjustment for this residual risk. At our meeting of 13 March 2008 we advised that the outstanding matters related to obtaining clarification on SDS novation, further update and progress on Network Rail issues and the provision to the Council of a suitable letter of comfort from DLA, Legal Advisors to the Project. We can now advise that, following a further meeting with the Chairman of tie Limited this morning and a range of Officers within tie and the Council, the Chairman of tie has advised that he has now received sufficient assurances in relation to the SDS matter, the APA Agreement with

Network Rail has now finally been signed and DLA have today provided an updated letter, qualifying their earlier letter of 12 March. We were pleased to receive the qualifying letter from DLA today which details substantial progress on a number of outstanding and detailed financial, technical and legal issues present in the letter of 12 March..."

5.63 Mr Aitchison gave evidence in relation to the basis upon which he satisfied himself that it was appropriate to authorise TIE to proceed:

"There was a process going through the Internal Planning Group. There was briefings I had individually with the colleagues who were mentioned there. I also had a similar letter to this one from colleagues in tie. I set up what I thought was an appropriate management process in late December to get to this point where it was delegated to my three colleagues to go away and only come back to me when professionally satisfied that what was being proposed was in the best interests of the Council. So to a large extent I did rely upon their professional advice"⁴⁶³.

5.64 Mr Aitchison's evidence in relation to the risk being retained by the public sector in respect of SDS, which is referred to above, was that *"It seemed to be a relatively small risk that was containable...Plus the fact it had been flagged up in the Business Case report to the Council that design was incomplete, and could lead to some additional cost. So this seemed consistent with that ...earlier comment"⁴⁶⁴.*

⁴⁶³ Transcript of oral evidence of Tom Aitchison 28 November 2017, page 103:7- 19

⁴⁶⁴ Transcript of oral evidence of Tom Aitchison 28 November 2017, page 10-7:12- 17

5.65 Donald McGougan also gave evidence in relation to the steps that he had taken to satisfy himself that it was appropriate to issue the document relating to the notice of intention to award. Mr McGougan stated: *"we'd been immersed in...the project updates and the updates on contract negotiations. So through the Tram Project Board and other meetings, I was aware of the stage that that had reached. But in sending this to me, the Council Solicitor had confirmed that she'd had a meeting with the relevant officials and that she felt it was now appropriate to move to this stage....it was the iterations that had been done on the capital and indeed the revenue projections for the tram over...a number of times, the advice we were getting from tie and...DLA...the reviews that had been undertaken on the project by, I suppose, going back to Cyril Sweett under Transport Scotland's auspices before the summer of 2007, and also the OGC and Audit Scotland. The close report drafts were emerging by then, and they were indicating a position where nearly all issues with the contractor had been buttoned down and were ready for approval"*⁴⁶⁵.

5.66 Gill Lindsay gave evidence that, although she had not satisfied herself in relation to financial matters, she had satisfied herself *"Certainly in respect of the legal matters. I think there was sufficient certainty then..."*⁴⁶⁶ That included the advice that had been obtained from DLA, in relation to which reference is made to section 3 of these submissions. Furthermore, Ms Lindsay gave evidence in relation to the risks referred to in the document being consistent with the Final Business Case

⁴⁶⁵ Transcript of oral evidence of Donald McGougan 30 November 2017, pages 5:1 to 6:16

⁴⁶⁶ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 112:14- 15

"Insofar as the Final Business Case required a price and a QRA to fall within a certain price...My understanding was -- the Final Business Case was that it wasn't so much to do with individual risks, but it would be that the totality of the price and the QRA and the cost would be the delivery within the Business Case....I will have considered that provided, as we were told, it was in the QRA, then it would not have been inconsistent with it, and would therefore have been consistent....From my perspective, in terms of legally -- in terms of the actual numbers, how they work, I think that I wouldn't have considered it was inconsistent in a practical way, provided the costs were fully contained... my clear understanding at the date of the signing that was that legal matters had been closed, and there were sufficient certainties in other matters, and the Chief Executive, the Leader and the two Directors clearly wished the matter to proceed, and I didn't have any information that it was inconsistent with the Business Case"⁴⁶⁷.

IPG meeting on 16 April 2018

- 5.67 A Highlight Report was produced for the Chief Executive's Planning Group on 16 April 2008⁴⁶⁸.
- 5.68 Tom Aitchison gave evidence in relation to that report, and in particular the risk allowance of £3.3m in the QRA for design, stating: *"I recall it being discussed at the time, and again being reassured that the 3.3, if that's what it finally was, was sufficient....These designs were on ...the critical path for the construction programme. Had these been attended*

⁴⁶⁷ Transcript of Gill Lindsay 27 October 2017, pages 113:22 to 115:17

⁴⁶⁸ CEC01246992

to timeously, taken together with the fact the design was meant to be complete by August of that year, then it did seem to be that the risk had been identified and appropriate financial provision had been made for it... [Reassurance] came through in a second letter signed by colleagues and also...a company letter from tie at final contract close that they had a handle on the risk, they'd made additional provision for it, and they were satisfied that would be sufficient...I took that advice on board"⁴⁶⁹.

5.69 The further letters in the period prior to contract close to which Mr Aitchison refers are addressed in section 6 of these submissions.

5.70 The evidence of Donald McGougan in relation to report was that "*I don't think I was unduly concerned by this report at this stage*"⁴⁷⁰.

⁴⁶⁹ Transcript of oral evidence of Tom Aitchison 28 November 2017, page 114:1- 19

⁴⁷⁰ Transcript of oral evidence of Donald McGougan 30 November 2017, page 23:11- 12

6. **Decision to enter into the Infraco Contract**

Summary

- 6.1 It was anticipated that close would occur on 2 May 2008. On this basis, a report was produced by the Chief Executive of the Council for the meeting of the Council on 1 May 2008, reporting a headline cost of £508m. The report was produced on the basis of professional advice from Council and TIE officers.
- 6.2 BB re-opened negotiations on a last minute basis, seeking a price increase of £12m. There was annoyance and disappointment at BB's approach, but both TIE and the Council considered that they had no option but to enter into dialogue. Various options were considered; eventually an increased price was agreed with Infraco in return for further risk transfer. This resulted in a headline cost of £512m, which remained within the funding envelope. The Kingdom Agreement was entered into to reflect the position. Evidence from TIE and Siemens flatly contradicted the suggestion by Richard Walker that cost was allocated to Phase 1b artificially to reduce the cost of Phase 1a.
- 6.3 Agreed deliverables were produced by TIE with the involvement of DLA. These included the Close Report, the Report on the Infraco Contract Suite and the final deal paper. Those documents reflected TIE's understanding that risk in relation to normal design development had been transferred to Infraco. The only material change in the risk profile was reported as being the risk in respect of delay in design concerned with approvals and consents, which (as referred to above in section 5 o

these submissions was considered to be small and containable. Reference is made to section 3 of these submissions in relation to the legal advice given by DLA.

6.4 Following the price increase and production of deliverables by TIE, a further Council report was put to members at the Policy and Strategy Committee ("PSC") meeting on 13 May 2008, for them to approve the price increase, resulting in a headline cost of £512m. The Chief Executive took the decision to report to the PSC, which was composed on senior elected members, in order to bring the matter before members without delay.

6.5 The Chief Executive's recommendation to proceed to contract close was based on assurances from TIE and senior Council officers. Whilst some Council officers had concerns about the position, it was the view of senior Council officers that it was appropriate to proceed because of the processes that had been carried out, the understanding that the risk of normal design development lay with Infraco and the sufficient headroom within the funding envelope.

6.6 Authorisation was only given to TIE to proceed to contract close after this had been approved by members at the PSC, notwithstanding that the letter of authorisation was dated before the meeting.

Council report for meeting on 1 May 2008

6.7 It had originally been envisaged that the Infraco Contract (and other contracts in relation to the Project would be completed in January 2008.

This was incrementally pushed back, with issues remaining to be resolved between the parties throughout that period. It was eventually anticipated that close would occur on 2 May 2008, with the understanding being that all issues had been resolved at that point.

6.8 A Council report dated 23 April was produced for the Council meeting on 1 May 2008⁴⁷¹.

6.9 The report for the meeting on 1 May 2008 was signed on behalf of Tom Aitchison by Jim Inch. Mr Aitchison states in his witness statement:

"The report sought refreshment of the delegated powers previously given to the Chief Executive to authorise TIE to enter the contracts with the Infraco and Tramco bidders. The report noted: (1) the cost of the project was now £508m (comprising a base cost of £476m and a revised QRA of £32m), which increase was largely due to the firming up of provisional prices to fixed sums, currency fluctuations and the "crystallisation of the risk transfer to the private sector as described in the FBC" (para 3.5); (2) 95% of the combined Tramco and Infraco costs were fixed with the remainder being provisional sums which TIE had confirmed as adequate; (3) 'As a result of the overlapping period of design and construction a new risk area has emerged which has been the subject of extensive and difficult negotiation. TIE Ltd advise that the outcome is the best deal that is currently available to themselves and the Council. Both TIE Ltd and the Council have worked and will

⁴⁷¹ CEC00906940

continue to work diligently to examine and reduce this risk in practical terms" (para 3.10)⁴⁷².

6.10 The report of 1 May 2008 concluded:

"It is proposed that the Tramco and Infraco contracts should be awarded to CAF and BBS respectively, securing the best deal possible for the Council and Transport Scotland. The awarding of these two contracts will represent a significant milestone in the implementation of the Tram project. A significant level of risk has been assumed by the private sector considerably reducing the Council's exposure to future uncertainty"⁴⁷³.

6.11 Mr Aitchison's evidence was that his understanding of the position was based on advice which he had received:

"I accepted the professional advice given to me that the risk retained by the public sector in relation to design, approvals and consents was consistent with the statement that there had been a "crystallisation of the risk transfer to the private sector as described in the FBC". There did seem to be clarity about what colleagues considered to be the Infraco fixed price contract, ie what costs were provisional and what was being set aside for those responsibilities being retained within the public sector. By that stage the provisional prices had been firmed up. I remember seeing a table at the time, which I asked for, that showed the

⁴⁷² Witness statement of Tom Aitchison TRI00000022, paragraph 120

⁴⁷³ CEC02083359, page 3

various risk profiles. I recall meeting Finance staff and being taken through the table with the risks being explained"⁴⁷⁴.

- 6.12 However, in hindsight, Mr Aitchison's view is that there could have been more detail provided in the report of 1 May 2008: "*With the benefit of hindsight, I would have preferred it to have been a more detailed report, drawing out particularly issues associated with design and the reconciliation of design to the construction programme*"⁴⁷⁵.
- 6.13 However, on 30 April 2008, Infraco sought to re-open discussions by seeking a price increase of £12m. A period of negotiation ensued, and the Infraco Contract was eventually executed on 14 May 2008.
- 6.14 The evidence of Willie Gallagher was that Infraco's position in respect of a cost increase "*was right at the wire and right out of the blue. It was dreadful behaviour. I felt personally let down. I felt that the behaviour of BB here was disgraceful...it wasn't obvious at that point what the solution was going to be. I don't think S [Siemens] were aware until slightly before BB made me aware that there was a problem. This was not a S problem. This was a BB problem. After speaking with Richard [Walker], I had discussions with everyone to explain to them what had happened. I then had discussions with legal and S as to what options were open to us moving forward. I explored whether we could replace BB with S, whether we could replace BB with someone else and whether, from a legal procurement point of view, there were other options. In the timescales involved there really weren't any options other*

⁴⁷⁴ Witness statement of Tom Aitchison TRI00000022, paragraph 124

⁴⁷⁵ Transcript of oral evidence of Tom Aitchison 28 November 2017, page 128:1- 4

than going back and doing something which would have been another long drawn out process. I have to say that, at the time, I wanted to look anywhere else other than using BB. I couldn't just give money away just for the sake of it. In the end I asked for senior executives from BBS to come to Edinburgh to meet us. Originally I wasn't going to have any involvement from Richard. However, I felt that we needed to understand fully why the request had been made. The only person who could provide that was Richard. They came to Edinburgh and explained the position. They said that they were extremely sorry (or words to that extent). It didn't cut a lot with me. I said to them that we had a short period of time to see if we could resolve the issue. I made it clear but that there should be no illusion that we would just give them more money. We had agreed the position with all parties prior to that meeting. If we had to reach an agreement which resulted in BBS getting more money we had to receive something in return, whether that be a reduction of risk or further assurances on design work. There was an agreement by the parties that we had to find an agreement which provided value for money for public funds. If we could, then that may be acceptable to our stakeholders. We had to consider what the alternative would be if we couldn't reach an agreement. We had to investigate both options⁴⁷⁶.

6.15 Tom Aitchison's evidence in relation to the cost increases was that although they were concerning and "*smacked of brinkmanship on the part of the contractor*", ultimately "*I came to the view that the cost*

⁴⁷⁶ Witness statement of William Gallagher TRI00000037, paragraph 318; see also paragraphs 3.19 to 3.26 of the statement

*increase could be put forward to the Council for acceptance. It was annoying and concerning but I had to address what needed to be done and come to a view on whether or not to accept the increase. Colleagues reported back to me what lay behind the increase. The price increase against the business case estimate was now 2.4%. It was within the parameters that the Council were comfortable with in terms of price movement. The increase still left the projected costs for the project well within the risk allowance and the £545m ceiling set and could be contained financially*⁴⁷⁷.

- 6.16 The sequence of events relating to the cost increases is summarised in a briefing note produced by Alan Coyle and dated 14 May 2008⁴⁷⁸:

"A report on Financial Close and Notification of Contract Award went to Council on 1 May 2008. This report asked Council to note the imminent award of the Infraco and Tramco contracts and also asked the Council to refresh the authority given to the Council's Chief Executive to allow tie to enter into the contracts, previously given in the Council report of 20 December 2007.

Given the changes to programme and price from the 20 December 2007 report, the Chief Executive felt it was in the best interests of the Council to request that Council refresh the delegated powers given in the previous report as a result of a 5 month delay to programme and a £10m increase in price.

⁴⁷⁷ Witness statement of Tom Aitchison TRI00000022, paragraph 119

⁴⁷⁸ CEC01238382

At the point of the 1 May 2008 Council Report it was expected that Financial Close would be circa 2 May 2008.

On 30 April 2008 a request from Bilfinger Berger (BB) for a further £12m emerged.

BB's support for the price increase focussed around an admitted failure on their part to assess or control their supply chain prices with particular reference to increases in steel and fuel costs, £ / € movement and a claim for underwriting of central demobilisation cost which they had allocated to their bid for Phase 1b in the light of a more cautious view on the execution of 1b.

BB claimed their costs were actually £17m, but that they had reworked internally to arrive at £12m.

An additional payment of £1m has also been paid to SDS at Financial Close. This payment has been made out of contingency, therefore, no impact on the global price but has reduced the amount in the QRA by £1m.

On 5 May 2008 a meeting of tie senior management culminated in a proposal from tie that tie would:

- Absorb £3m of additional cost in return for tangible contractual and risk improvements;*
- Agree to meet BB Siemens (BBS) allocated demobilisation costs of £3.2m in event that Phase 1b does not proceed.*

A formal letter to BBS in the form of an ultimatum was needed to bring matters to a close. In addition to the continuing delay and attendant costs, and the unpalatable alternatives to concluding with BBS, there were concerns that Siemens, CAF and PB (SDS Contractor) may also seek price increases if BB were seen to be making inappropriate progress.

A combined meeting of the TPB and tie Board was held (as scheduled) in the morning of 7 May 2008. The meeting reviewed the position thoroughly and concluded that the approach which best protected the public sector's position would be to seek a conclusion with BBS within their demand for £12m.

Further negotiations were conducted from 7-9 May 2008 and an acceptable conclusion reached. The final terms negotiated reflect agreement by tie to increased consideration and contingent cost underwriting in return for early progress to contract signing, improvement in terms and capping of cost exposures.

The specific terms are as follows:

Financial amendments:

- *Incentivisation bonus – tie will pay a series of incentive bonus payments over the life of the contract on achievement of specified milestones. The aggregate cost will be £4.8m...*

The financial amendments were offset by the following improvement in terms.

- Immediate contract close on preferred terms - all of tie's preferred positions in the Infracore contract which were under query by BBS and their lawyers would be accepted. The documents concluded include the Review and Design Management Plan arrangements which assist management of the design and consents risk and which carries a £3.3m allowance in the QRA. The attempt by BB to revise the design process in a manner which would have created delay was also successfully rebuffed. Achievement of close also reduces extended legal and management costs....

In summary, the late price pressure from BB arising from their claimed supply chain pressure has been contained at £4.8m with a further potential cost of £3.2m if Phase 1b does not proceed....

[Clearly] the increased price of Phase 1a has impacted on the headroom within the overall budget and as a result the funding gap for Phase 1b now stands at £55.3m based on a price of £87.3m for Phase 1b.

An evaluation of tie's alternatives to negotiating the £12m demand from BB concluded that there was no commercial alternative which would better protect the public sector's interests given the current situation. tie had advised that flat refusal to pay BB would result in BB walking away from the deal.

The alternatives considered were:

- *Siemens to restructure consortium by incorporating a new civils contractor*
- *Tramlines re-introduced*
- *Full-scale re-procurement*
- *Project termination*

The first 3 alternatives would result in varying degrees of delay from 3 months to a year. Given the costs of any re-procurement, the rate of construction inflation and fuel prices as well as potential for differing contractual stand points of alternative bidders would in all likelihood be greater than the current price. Any subsequent delay would also impact on revenue generating operations.

The Quantified Risk Allowance (QRA) had reduced initially from £49m to £32m as a result of close out of procurement risks. The QRA has been further reduced to circa £30m based on a small amount of risk reduction as a result of final negotiations removal of £1m contingency for the additional SDS payment noted in paragraph 3.8...

Update on MUDFA (Contract for Utility Diversions)

Progress has reduced from that achieved in Period 13 with 70% of the planned diversions completed in the period. A total of 77% of the planned diversions have been achieved in total to date. The overall effect on the critical path remains at two weeks and implementation of the revised recovery programme actions is underway. Rescheduling of

key areas has been carried out to address resource peak demand and to prioritise critical interface areas with Infraco...

SDS (Systems Design Services Contract)

The SDS v31 design programme has been issued and incorporated into the final contract. To date, 16 Prior Approvals have been issued to CEC and 11 have been approved against a programme of 21 issued and 11 approved. Twelve Technical Approvals have been issued to CEC and none have been approved against a programmed 16 issued and 4 approved. A new taskforce composed of senior representatives from tie, CEC and SDS has been set up to ensure the approvals are granted promptly...

The QRA has reduced from £49m at FBC to £32m. The QRA has been reduced further at Financial Close to circa £30m.

tie Ltd have advised that the £30m QRA is adequate".

6.17 Accordingly, it was considered that the price increase was justified by a corresponding increase in risk transfer.

6.18 Willie Gallagher wrote to Infraco on 6 May 2008⁴⁷⁹ during the course of the last minute cost increases. That letter said, amongst other things:

"...In order to stabilise the ETN Procurement, and deal with the BBS Consortium's action in a transparent way, I see my authority to move forward with the BBS Consortium only as I have laid out in the attached

⁴⁷⁹ CEC01284033

paper. I am left with no option but to stipulate the precise terms on which tie will complete, with no further negotiation. The financial allowances in Conditions 1 and 2 are a final measure of goodwill by tie, which we are under no compulsion to offer. In making the proposal, tie must receive value for money. Accordingly the full set of Conditions 1-7 are a package, are not separable, and are integral to the InfraCo Contract itself."

6.19 The conditions that Mr Gallagher referred to included the following:

"Condition Two

tie shall pay the BBS Consortium an incentivisation bonus of £3 million, such sum to be paid as follows:

£500,000 at date of the first critical milestone completion date achieved by BBS Consortium

£2,500,000 at the date of issue of the Reliability Certificate

Condition Three

The InfraCo Contract Suite and all associated documentation is closed out on tie's preferred positions on all remaining open matters and there is no further discussion or negotiation on any core terms and conditions or schedules except for housekeeping and sense checking. This includes:

BBS Consortium withdrawing all points on the SDS Novation Agreement which were raised in week commencing 28th April 2008;

BBS Consortium accepts tie's preferred position on Schedule Part 14 Review Procedure, and the Design Management Plan and definition of Issued for Construction Drawings and the phased release of IFCs as allowed for in the Design Delivery Programme;

BBS Consortium delivering its collateral warranties and those of its subcontractors at Contract Close on the terms required by tie".

6.20 The change in the position was summarised by Graeme Bissett of TIE on 12 May 2008 as follows⁴⁸⁰:

"The net result is that the headline budget goes to £512m from £508m.

The components are somewhat complicated but boil down to:

- Full negotiated incentivisation bonus of £4.8m is included in the headline number*
- We have evaluated £4.6m of risk contingency savings but have reflected only £1.8m in the headline number*
- We have kept separate the £3.2m of contingent Phase 1B demob cost. This factor and the balance of unrecognised risk improvement effectively offset each other*
- A further £1m general risk provision has been added*

⁴⁸⁰ CEC01222120

This means that the supply chain pressure claimed by BBS which gave rise to the late negotiation has been met by milestone related incent bonus and in return we have bought out risk".

The Kingdom Agreement

6.21 The discussions referred to above in relation to cost increases resulted in what was known as the Kingdom Agreement⁴⁸¹, which provided for an incentivisation bonus of £8.4m, together with a payment of £3.2m in the event that phase 1b did not proceed.

6.22 Steven Bell gave evidence that this agreement "*dealt with...eight or nine points, some of which adjusted price, some of which clarified elements of risk or confirmed commitments to, I think, address matters associated with the Tramco Novation and the SDS Novation*".⁴⁸²

6.23 James McEwan's evidence was that TIE's position had been improved: "*BBS consortium agreed to accept the risk and any costs arising from changes relating to early release of IFC information subject to a cap of 1.5 million. So that would seem positive...from tie's perspective*"⁴⁸³.

6.24 The evidence of Stewart McGarrity in relation to the agreement was that:

"The agreement reflects the outcome of further detailed negotiations, following the BSC request for an additional £12m, resulting in this agreement to deliver a mix of contractual improvements in return for the

⁴⁸¹ WED00000023

⁴⁸² Transcript of oral evidence of Steven Bell 24 October 2017, pages 128:23 to 129:2

⁴⁸³ Transcript of oral evidence of James McEwan 18 October 2017, pages 113:24 to 114:3

aggregate £4.8m incentivisation bonus and the £3.2m Phase 1b payment. I'd highlight the following:

- *BSC withdrawing remaining negotiating points in relation to the SDS novation and Design Management Plan for the period post award.*
- *Capping of the tie/CEC exposure for the extent of roads reconstruction required to £1.5m (the pre-existing risk allowance was £2m) and capping the tie/CEC cost for delays relating [to] programme exposure for the extent of roads work as per pricing assumption 12 of Sch Pt3 to 8 weeks – assessed as £1.3m. This further mitigated general delay risk for which the pre-existing risk allowance was £6.6m".⁴⁸⁴*

6.25 The reason why TIE agreed to make a payment in the event that phase 1b did not proceed "was that BSC had or would incur costs in relation to the planning and preparation for Ph1b and that in the event Ph1b did not proceed then these costs, including the costs of demobilising resources and their supply chain assembled in expectation of delivering Ph1b would be abortive as they would not be recovered by them as part of their price for Ph1b"⁴⁸⁵.

6.26 Richard Walker suggested in his evidence that the "Kingdom Agreement wasn't really a compensatory or bonus payment, it was simply part of the price which was moved into a separate agreement so that tie could keep the price for Phase 1a of the Infraco Contract below

⁴⁸⁴ Witness statement of Stewart McGarrity TRI00000059, page 151, paragraph 99; see also paragraph 104 of the statement

⁴⁸⁵ Witness statement of Stewart McGarrity TRI00000059, page 151, paragraph 100

*a certain level*⁴⁸⁶, and *"was an attempt to mislead City of Edinburgh Council"*⁴⁸⁷. That was not supported by the evidence of any of the TIE witnesses. Furthermore, Michael Flynn gave evidence that *"I wouldn't accept that"*⁴⁸⁸ and that there was a rationale and logic to the arrangement.

Reporting by TIE and DLA

6.27 In early 2008, the Council had initiated a process in terms of which TIE was required to produce a number of deliverables⁴⁸⁹.

6.28 The principal deliverables that were produced by TIE in support of contract close were:

- (a) The Close Report⁴⁹⁰;
- (b) The Report on the Infraco Contract Suite⁴⁹¹;
- (c) A report on the final close process and record of recent events (also described as the final deal paper)⁴⁹²;
- (d) A report on the prospects of a procurement challenge⁴⁹³;
- (e) Approval letters.

These documents were all attached to Graeme Bissett's email of 12 May 2008⁴⁹⁴.

⁴⁸⁶ Witness statement of Richard Walker TRI00000072, paragraph 75

⁴⁸⁷ Transcript of oral evidence of Richard Walker 15 November 2017, page 107:1

⁴⁸⁸ Transcript of oral evidence of Michael Flynn 6 December 2017, page 89:7

⁴⁸⁹ CEC01397996

⁴⁹⁰ CEC01338853

⁴⁹¹ CEC01338851

⁴⁹² CEC01338847

⁴⁹³ CEC01338850

The Close Report

6.29 The Close Report was a document produced by TIE, with the involvement of DLA⁴⁹⁵. In an email dated 25 March 2008, Graeme Bissett stated that "*DLA will perform their own legal QC review on the full set of final documents and this will support and complement the review by tie/TEL people*"⁴⁹⁶. Andrew Fitchie marked up and commented on the draft document⁴⁹⁷. Reference is made to section 3 of these submissions in this respect.

6.30 The Close Report⁴⁹⁸ stated, amongst other things:

*"The increase in Base Costs for Infraco is a result of a negotiated position on a large number of items including the contractual interfaces between the Infraco, Tramco and SDS contracts and substantially achieving the level of risk transfer to the private sector anticipated by the procurement strategy... The increase in Base Costs for Infraco of £17.8m approximates closely to the allowance which was made in the FBC for procurement stage risks i.e. the increase in Base Costs which might have been expected to achieve the level of price certainty and risk transfer which has been achieved"*⁴⁹⁹ ...

⁴⁹⁴ CEC01338846

⁴⁹⁵ See for example CEC01448392

⁴⁹⁶ CEC01431196

⁴⁹⁷ See for example the email of 9 March 2008 at CEC01463884 (email) and CEC01463886 (mark-up)

⁴⁹⁸ CEC01338853

⁴⁹⁹ CEC01338853, page 4

the risks relating to the Infraco and Tramco contracts which have been identified as wholly or partly retained by the public sector beyond Financial Close...are:

- *The process for granting of approvals and consents;*
- *The process for granting of permanent TRO's*
- *The interface with the implementation of utility diversion works*
- *Delays to design approvals for reasons outside the control of the Infraco*
- *Stakeholder instructed design changes*⁵⁰⁰.

6.31 It can be seen from the foregoing that there is no reference in this list to the risk associated with the development of the design from the Base Date Design Information as provided for in Pricing Assumption No.1. However, the Close Report does also state:

*"Crucially the price includes for normal design development (through to the completion of the consents and approvals process – see below) meaning the evolution of design to construction stage and excluding changes if [sic of] design principle shape form and outline specification as per the Employers Requirements"*⁵⁰¹.

6.32 This provision was not highlighted as creating any risk for TIE, as a consequence of TIE's understanding that risk had been transferred to Infraco in this respect.

6.33 The Close Report also addressed the QRA and risk allowance:

⁵⁰⁰ CEC01338853, page 25

⁵⁰¹ CEC01338853, page 26

"tie's risk identification and management procedures as detailed in the FBC describe a process whereby risks associated with the project which have not been transferred to the private sector are logged in the project Risk Register. Where possible the cost of these risks is quantified by a QRA in terms of a range of possible outcomes, probability of occurrence and thereby the Risk Allowance which is included in the capital cost estimate for the project. The project Risk Register also details the "treatment plans" being followed to mitigate individual risks and thereby avoid all or part of the cost allowance⁵⁰²

The only material change in the Risk Allocation Matrices between Preferred Bidder stage and the position at Financial Close is in respect of the construction programme costs associated with any delay by SDS in delivery of remaining design submissions into the consents and approvals process beyond Financial Close. The Project Control Budget at Financial Close totals £508m (Final Business Case £498m) including a risk allowance of £32m (Final Business Case £49m). This change primarily reflects the closure of procurement stage risks on Infraco and Tramco including all the risks associated with achieving price certainty and risk transfer to the private sector as has been effectively achieved in the Infraco contract as summarised above. The risk allowance of £32m includes the following provisions for residual risks retained by the public sector during the construction phase of Infraco and Tramco.

- £8.8m in respect of specifically identified risks held by and to be managed by tie during the construction phase including adverse*

⁵⁰² CEC01338853, page 28

ground conditions, unidentified utilities and the interface with non-tram works and post close alignment of the Infraco proposals with the SDS design.

- *£2m in respect of the risk that conditions attaching to the VE items taken into the Infraco price may not be removed*
- *£3.3m in respect of post Financial Close consents and approvals risks which provides for the cost or programme consequences of imperfections which may arise in elements of the consents and approval risk transfer as described above.*
- *£6.6m to provide for the cost of minor Infraco / Tramco programme slippage of up to 3 months (other than as a result of delays to MUDFA which is provided for elsewhere in the risk allowance)⁵⁰³.*

6.34 The changes in the risk allowance between the Final Business Case and the Close Report are summarised by Stewart McGarrity in the table to be found at paragraph 133 of his witness statement⁵⁰⁴. From TIE's perspective, there was no requirement for a risk allowance in relation to normal design development because it considered that this risk sat with Infraco and had been allowed for in its price⁵⁰⁵.

6.35 Mr McGarrity also gave evidence that although the risk allowance reported in the Close Report in May 2008 was based on a QRA run which had been carried out on 1 May 2008, "*I don't think that should be*

⁵⁰³ CEC01338853, page 28

⁵⁰⁴ Witness statement of Stewart McGarrity TRI00000059, paragraph 133

⁵⁰⁵ Witness statement of Stewart McGarrity TRI00000059, page 173, paragraph 146

taken in any way to say that Steven [Bell] and the rest of the project team did not revisit all of this right up to the point where the contract was signed, and satisfy themselves that it was still valid. I don't think that -- my professional judgement is I don't think it should be -- a conclusion should be reached that because this was run on 1 March, that it wasn't still valid in all respects at the point of contract award...It certainly wasn't a case of: right, there's the QRA, put that to the side, and on we go. That's not the way that it happened at all....we could have [run the QRA again]. But if the inputs hadn't changed in terms of the values, and the percentage probabilities of the risk crystallising, it would have given the same answer"⁵⁰⁶.

- 6.36 The risk allowance was reviewed by TIE: Steven Bell gave evidence that *"We reviewed it on a number of occasions between January and May 2008, and certainly in the run-up to contract close in May 2008"*⁵⁰⁷. Steven Bell himself *"reviewed the consolidated numbers that were proposed for risk in total in May 2008"*⁵⁰⁸ and *"reviewed the Pricing Assumptions and the items I considered...had the potential to have a Notified Departure impact, and satisfied myself that I considered the total risk allowance was adequate...probably in the first or second week of May"*⁵⁰⁹. The conclusion of the review was that *"I think we'd considered that the adjustments that were being made were appropriate"*⁵¹⁰.

⁵⁰⁶ Transcript of oral evidence of Stewart McGarrity 12 December 2017, pages 36:14 to 37:12

⁵⁰⁷ Transcript of oral evidence of Steven Bell 25 October 2017, page 2:2- 5

⁵⁰⁸ Transcript of oral evidence of Steven Bell 25 October 2017, page 5:9- 16

⁵⁰⁹ Transcript of oral evidence of Steven Bell 25 October 2017, page 3:16- 17

⁵¹⁰ Transcript of oral evidence of Steven Bell 25 October 2017, page 6:19- 20

6.37 Mr Bell also confirmed in evidence by reference to the Close Report⁵¹¹ that the figure "*generated by the computer software*" in the QRA yielded a risk allowance of £27.937m, "*but then manually a human being or beings have come to a judgment that there should be additional sums added in relation to the non-delivery of value engineering, the risk of that, and also the risk relating to road reinstatement, and also unspecified risks*"⁵¹² which yielded a higher risk allowance of £32.3m. Mr Bell also agreed that it was generally correct that "*the QRA part of the risk allowance did not reflect any changes that may have occurred in the risk profile between 1 March and financial close*"⁵¹³.

6.38 The evidence of Tom Aitchison in relation to the Close Report is that, although it recognised "*that there were concerns over SDS*", these concerns had been addressed: "*A set of management actions were set out to improve the position. These actions included process improvements, prioritising critical work and finalising third party agreements and the like. The Close Report stated that there was a risk arising from the overlapping period of design on construction. TIE included an additional £3.3m in the risk allowance to cover that particular contingency*"⁵¹⁴.

The Report on the Infraco Contract Suite

⁵¹¹ CEC01338853

⁵¹² Transcript of oral evidence of Steven Bell 25 October 2017, pages 9:23 to 10:3

⁵¹³ Transcript of oral evidence of Steven Bell 25 October 2017, page 15:1- 5

⁵¹⁴ Witness statement of Tom Aitchison TRI00000022, paragraph 106

6.39 The Report on the Infraco Contract Suite is a document produced by TIE with input from DLA. Reference is made to section 3 of these submissions in this respect.

6.40 The report states:

"In broad terms, the principal pillars of the ETN contract suite in terms of scope and risk transfer have not changed materially since the approval of the Final Business Case in October 2007. The process of negotiation and quality control has operated effectively to ensure the final contract terms are robust and that where risk allocation has altered this has been adequately reflected in suitable commercial compromises..."⁵¹⁵.

6.41 In relation to price, the report states:

"A contract price has been agreed. The detailed contract price and pricing schedules for carrying out the Infraco Works is contained in Schedules to the Infraco Contract. A substantial portion of the Contract Price is agreed on a lump sum fixed price basis. There are certain work elements that cannot be definitively concluded in price and therefore Provisional Sums are included. A number of core pricing and programming assumptions have been agreed as the basis for the Contract Price. If these do not hold, Infraco is entitled to a price and programme variation known as "Notified Departure"⁵¹⁶.

6.42 There is no reference in the report to the specific provisions of Pricing Assumption No. 1, which reflected TIE's understanding of the position,

⁵¹⁵ CEC01338851, page 1

⁵¹⁶ CEC01338851, page 4

in the absence of legal advice to the contrary (see section 3 of these submissions).

6.43 In relation to "*contract changes*" (in other words, clause 80), the report states:

*"The Agreement contains a relatively conventional contractual change mechanism in relation to the management and evaluation of changes. Change rules depend upon the type of change instructed whether it is a tie Change, tie Mandatory Change (where an event occurs which needs to be dealt with) or an 'Infraco' Change"*⁵¹⁷.

This reflected TIE's understanding of the position, in the absence of legal advice to the contrary (see section 5 of these submissions).

The Final Deal Paper

6.44 The final deal paper was a TIE document which was "*a short novel on the evolution of the Infraco suite. It addresses the negotiation process, the detail behind the final changes since notification letters were issued, an assessment of value for money on the final deal, an examination of the alternative procurement options and an evaluation of the risk of procurement challenge*"⁵¹⁸. The increase in price is further addressed in section 5 of these submissions.

6.45 The final deal paper states:

⁵¹⁷ CEC01338851, page 6

⁵¹⁸ CEC01294645

"...underlying costs have been subject to the firming up of provisional prices to fixed sums, currency fluctuations and the crystallisation of the risk transfer to the private sector as described in the project's Final Business Case. The finalisation of the contracts required further amendment for similar reasons and supply chain pressure on the bidding consortium has been accommodated in the marginal increase over the most-recently reported cost estimate. Offsetting the increased cost is a range of negotiated improvements in favour of tie and the Council, in the areas of programme delay mitigation, cost exposure capping and more advantageous contractual positions. In addition, and as is normal in these circumstances, there is an imperative to bring the contractual matters to an efficient near-term close in order to mitigate against potential cost exposure and programme delay, which could represent a material risk. Tie has recommended that the final terms negotiated represent the best result achievable for the public sector and that the council should authorise tie now to proceed with the contract close"⁵¹⁹.

6.46 The final deal paper concludes that *"The project risk profile remains broadly in balance with the business case and the scope of works is unchanged. On this basis tie recommends that Close be executed"*⁵²⁰.

6.47 The evidence of Susan Clark in relation to the report was that the cost increase *"was an indication of the commercial approach BB took and their lack of partnering ethos and pointed to a contractually aggressive*

⁵¹⁹ CEC01338847, page 1

⁵²⁰ CEC01338847, page 11

*form of managing the contract to protect claims for additional fees and programme extension. I think we hoped that the increase now might remove some of the concerns Infraco had and so reduce the potential for further costs increases. This turned out not to be the case*⁵²¹. Ms Clark's view was that there were improvements in TIE's position as a consequence of the cost increases and "*These improvements included the capping of road re-instatement costs, capping road related prolongations and minimising risks of claims from works underway. This was meant to reduce these risks and I agreed with it at the time, albeit I did not agree with the manner in which BB had presented the last minute request*"⁵²².

6.48 As a consequence of the last minute discussions in relation to price, reflected in the Kingdom Agreement (referred to above), the risk allowance referred to in the final deal paper was reduced to £31.2m, from the previous level of £32.3m which had been provided for in the Close Report prior to the cost increases. Steven Bell addressed this reduction in his evidence: "*There were some explicit items that the agreement capped under the contract. So there was a GBP2 million allowance for roads reinstatement in our original risk allowance that was capped in the final agreement at 1.5. Therefore, we were able to remove the GBP0.5 million or make that element of the adjustment. That was an explicit item. There was adjustments to the Infraco budget in consequence, and we reviewed at the time the overall elements associated with the completion of the novation and the risk activities on*

⁵²¹ Witness statement of Susan Clark TRI00000112, paragraph 60

⁵²² Witness statement of Susan Clark TRI00000112, paragraph 62

*schedule, and concluded in overview that a net adjustment was merited in total...that needed to be reconciled to a final control budget*⁵²³.

6.49 A TIE meeting was held on 13 May 2008, attended by amongst others, Mr Bissett, Willie Gallagher, Steven Bell, Susan Clark, Jim McEwan and Dennis Murray. Graeme Bissett gave evidence in relation to a note⁵²⁴ entitled "*Meeting of the tie management team to confirm readiness to proceed with completion of the Infraco contract suite*". Mr Bissett confirmed in his evidence that he believed the terms of the close report to be correct at the time, and that he considered he had adequate information as to whether there had been risk transfer since December 2007, and "*that the team who had negotiated that schedule were comfortable that those assumptions would hold true with the exceptions where there was a specific provision made*"⁵²⁵.

6.50 As well as the foregoing, TIE also carried out a quality assurance process in the period prior to contract close⁵²⁶.

The Council report of 13 May 2008

6.51 A report was produced for the PSC on 13 May 2008⁵²⁷ to take account of Infraco's cost increases. The report narrated:

"A report updating the Council on the imminent completion of the contractual negotiations for the ETN was submitted to Council on 1 May

⁵²³ Transcript of oral evidence of Steven Bell 25 October 2017, pages 16:16 to 17:13

⁵²⁴ CEC01319006

⁵²⁵ Transcript of oral evidence of Graeme Bissett 31 October 2017, page 201:21- 25

⁵²⁶ See for example the transcript of oral evidence of Graeme Bissett 31 October 2017, pages 1:15 to 19:11

⁵²⁷ CEC01247831, CEC01246115, CEC01891564

2008. Delegated authority, awarded to me by the Council on 20 December, was refreshed to allow tie Ltd to enter into contracts to deliver the ETN, subject to suitable due diligence and provided that any remaining issues were resolved to my satisfaction. While the contracts are now almost concluded and ready for signature, the final terms differ from those anticipated in my report to the Council on 1 May, with the estimated capital cost for phase 1a now standing at £512m, with a further contingent payment of £3.2m due, if phase 1b is not built, although this remains well within the available funding of £545m....⁵²⁸

There have also been some further changes to the commercial position of the consortium, following the publication of previous reports to Council. For this reason, details of the final position will not be released until contract closure is achieved. I reported to the Council on 1 May that, during contract negotiations, underlying costs were subject to the conversion of provisional prices to fixed sums, currency fluctuations, inflationary pressures and the transfer of risk to the private sector. The finalisation of the contracts required further amendments for similar reasons. Since then, tie Ltd has continued to work to ensure the competitiveness of the developing contract terms so that these continue to represent best value and are fully aligned with relevant regulations. Offsetting the increase in cost is a range of negotiated improvements in favour of tie Ltd and the Council in order to reduce the risk of

⁵²⁸ CEC01246115/USB00000357, paragraphs 2.1 to 2.2

*programme delays and minimise exposure to additional cost pressures, as well as better contractual positions...*⁵²⁹

*These changes increase costs by £4m to £512m, but have corresponding advantages by further transferring risks to the private sector. In addition, part of the package negotiated entitles BBS to an additional payment of £3.2m, should the Council decide not to construct phase 1b of the tram network...*⁵³⁰

*In return for the financial amendments, tie Ltd has secured a range of improvements to the contract terms and risk profile. Currently, these areas are regarded as highly confidential but, subsequent to contractual close, a more detailed report will be submitted to the Tram Sub-Committee*⁵³¹.

6.52 The report of 13 May 2008 was considered by the PSC on 13 May 2008. Tom Aitchison's evidence was that:

"It was my decision to report to the Policy and Strategy Committee. There had been a significant change and it was important that elected members and not Council officials approved the contract and revised price. I took the first opportunity possible to put the change in circumstances in front of elected members. The Policy and Strategy Committee was composed of senior elected members on an all-party basis. On that committee were the Leader of the Council, the Leader of the opposition, the Leaders of the political groups and other senior

⁵²⁹ CEC01246115/USB00000357, paragraphs 2.4 to 2.7

⁵³⁰ CEC01246115/USB00000357, paragraph 2.9

⁵³¹ CEC01246115/USB00000357, paragraph 2.11

elected members. Had the Committee been concerned about anything proposed at the meeting, they could have continued the matter to a special meeting of the Committee or referred the decision to the full Council for determination... I seldom put reports to committee at short notice. But the most important requirement was to get the information in front of elected members for determination as soon as possible. In the report I used the term "approve the increase" as I wanted it to be quite clear that it was the councillors who were being invited to take the decision. Ideally, it would have been preferable to have reported to a meeting of the full Council rather than the Policy and Strategy Committee. But, as already noted, a decision was urgently needed from elected members. Achieving financial close had taken much longer than originally anticipated and costs were being incurred as each week passed. In addition, "behind the scenes" many meetings took place between officers of the Council and the political leadership, political groups and individual councillors to keep them informed of developments"⁵³².

6.53 Tom Aitchison gave evidence that at the meeting of the PSC on 13 May 2008, *"There was a very lengthy spell of questioning of myself, Dave Anderson, Gill Lindsay and Donald McGougan as elected members scrutinised the proposals in the report"*⁵³³.

6.54 Mr Aitchison also addressed the issue of reporting to the PSC in his oral evidence. The report went to the PSC rather than a full meeting of the

⁵³² Witness statement of Tom Aitchison TRI00000022, paragraph 130

⁵³³ Witness statement of Tom Aitchison TRI00000022, paragraph 154

Council because *"I wanted to get the material in front of elected members as quickly as possible"*⁵³⁴. Now, clearly most of the major reports had gone through the Full Council, rather than a committee. But if you look at the composition of the Policy and Strategy Committee, they had the leaders of the various political groups on it. They had senior elected members on it...every month that passed, tie's costs were also increasing as well. So it seemed appropriate to use the first possible senior elected member vehicle into which I could report"⁵³⁵.

6.55 In terms of the substance of the report, Mr Aitchison stated:

"The recommendations that went to the Policy and Strategy Committee were based on the considered, and consistent, advice from TIE and senior Council colleagues. In my view it was now appropriate to proceed to Contract Close. There was written confirmation from TIE stating that "the final terms negotiated are materially consistent with the terms set out in the Final Business Case and confirm the value for money proposition demonstrated by the FBC and that it is now appropriate to conclude the contracts" (letter dated 13 May 2008 by Mr Gallagher⁵³⁶). I further had written confirmation from council colleagues in support of that position. The documents attached to Graeme Bissett's email [i.e. the Close Report, the Report on the Infraco Contract Suite and the final deal paper etc. as referred to above] were not made available to members before or at the meeting. However, members

⁵³⁴ The next full Council meeting was not until 29 May 2008 – witness statement of Lesley Hinds TRI00000099, paragraph 270

⁵³⁵ Transcript of oral evidence of Tom Aitchison 28 November 2017, pages 136:16 to 137:8

⁵³⁶ CEC01284042

would have been advised in private briefings on some of the content of these documents. Some of the content of the Financial Close documents was also commercially and legally sensitive and would not routinely have been publically reported".

6.56 The letter of 13 May 2008 from Willie Gallagher referred to by Mr Aitchison above provided Mr Aitchison "*with formal written assurance that in TIE's professional view as an organisation, it was appropriate to proceed*"⁵³⁷.

6.57 Mr Aitchison also received assurances from senior Council officers in relation to the report of 13 May 2008. Mr Aitchison refers in his witness statement to the following

"I note that on 13 May 2008 (at 07:49 hours) Gill Lindsay sent Donald McGougan and David Anderson an email (CEC01222437) attaching a short draft report (CEC01222438) for all three to sign to provide comfort to me as I closed the deal following the meeting of the Policy and Strategy Committee. The report was signed that day (CEC01244245). As previously noted, following the Council meeting in December 2007 a period of contract due diligence was entered into and I tasked the Directors of City Development and Finance and the Council Solicitor to undertake this on my behalf. I advised them that I would not consider approving the contract for signing until I had a written assurance from them that it was appropriate to do so. The purpose of the note was to fulfil that requirement. The note from senior colleagues was the

⁵³⁷ Witness statement of Tom Aitchison TRI00000022, paragraph 146

*culmination of a work programme extending over many weeks. I had discussed issues with them over this period, participated in briefings and been involved in discussion at the IPG. The note was discussed with colleagues but it also has to be viewed in this wider context*⁵³⁸.

6.58 The report to which Mr Aitchison refers in the extract from his evidence above⁵³⁹ is a memorandum dated 13 May 2008 and is headed "Edinburgh Tram Network Financial Close". It was issued by Donald McGougan, David Anderson and Gill Lindsay. The memorandum stated that its authors "*hereby advise and confirm that, taking into account all the circumstances, we consider it is appropriate to support and agree with tie's recommendation to you that there is now an imminent financial close to this project*".

6.59 Donald McGougan's evidence in relation to the memorandum was that "*I was signing this note after considerable work that had been undertaken in the period from the Final Business Case report in December 2007 to this date in May 2008. So this is an accumulation of all the activity and diligence that had gone in to the project in that process, both within tie and from the Council side*"⁵⁴⁰. Mr McGougan acknowledged that whilst some officers might have had concerns about the position, the position in relation to risk had been addressed: "*We'd been through a process of reviews of how risk was being dealt with, and the OGC and Audit Scotland had both confirmed that that was best practice in relation to what they'd found. Our own people had been*

⁵³⁸ Witness statement of Tom Aitchison TRI00000022, paragraphs 144 to 145

⁵³⁹ CEC01244245

⁵⁴⁰ Transcript of oral evidence of Donald McGougan 30 November 2017, page 42:22 to 43:3

involved in the review and the build-up of the QRA over a period of time, but there was a very complex set of contract documents and it was a very complex project. So clearly there would have been concerns about risk. There were risk allowances made against that risk which were felt to be adequate, and beyond that we were now at a position where I think the total costs including the risk allowance was 512 million. That left 33 million between that sum and the 545 funding envelope that was available for the contract. So that's the same again provision for risk that could have been needed in what we thought might be extremis...But I felt that the risk allowance in total and the headroom that was available beyond that should avoid any significant financial problems for the Council in taking the matter forward...tie and CEC as client were very clear that they would not initiate any post contract changes that were going to impact on the programme or the cost. So the areas where there would be post contract changes would be in relation to the design where we had been assured that normal design development from BDDI to issued for construction was a risk for the contractor, and the areas of potential delay in relation to approvals and in planning and in the roads area, and the Council had supplemented the staff in both those areas to ensure that there was no delay once the contract drawings came to the Council⁵⁴¹.

⁵⁴¹ Transcript of Donald McGougan 30 November 2017, pages 43:16 to 46:15

- 6.60 Dave Anderson's evidence in relation to the memorandum was that he relied upon the advice he had received from Willie Gallagher, Tom Aitchison, Jim Inch, Gill Lindsay and Donald McGougan⁵⁴².
- 6.61 Mr Anderson also gave evidence that *"it would have been advisable to complete a fresh options appraisal covering all the cost changes and outstanding risks so that Councillors could reach a more fully informed view"*⁵⁴³. Rebecca Andrew also considered that *"I do not think members had sufficient time to consider the terms of the report"*⁵⁴⁴. Steve Cardownie gave evidence that *"In hindsight, the increased price and authority to enter the contracts ought to have been considered by the full Council, unless there was a reason, such as if there had been a delay and they wanted to go directly to the Policy and Strategy Committee. The Policy and Strategy agendas should be discussed within groups as well but if that was an emergency report then it would be just the Policy and Strategy Committee members who would determine it and would have to vote according to the policy of their groups"*⁵⁴⁵. As referred to above, however, senior Council officers considered it appropriate to have the matter considered by members quickly at the PSC.
- 6.62 However, the evidence of Jennifer Dawe was that it was appropriate to have the matter considered at PSC: *"There was power to call special meetings of the Full Council but, as far as I can remember, there was*

⁵⁴² Witness statement of David Anderson TRI00000108, paragraph 28

⁵⁴³ Witness statement of David Anderson TRI00000108, paragraph 29(g)

⁵⁴⁴ Witness statement of Rebecca Andrew TRI00000023, paragraph 67(2)

⁵⁴⁵ Witness statement of Steve Cardownie TRI00000104, paragraph 76; see also witness statement of Lesley Hinds TRI00000099, paragraph 292

only one special meeting ever called regarding the ETP in 2011...What we were doing here was delegating power to the Council's Chief Executive. If matters changed dramatically or enough that he felt he had to come back and have that authority refreshed by the Full Council, then that is what he could do. He could also use the PSC to do that because it was cross party and had all the senior councillors on it. At this time, there would have been no suggestion that there would be a special meeting. We were still within the £545m. The key factor was the assurances that we were given that, no matter what happened with the risks and costs of the project, we were not going to be breaching that funding envelope"⁵⁴⁶.

- 6.63 Former Councillor Ewan Aitken gave evidence that "*Members of the Policy and Strategy Committee (Councillors) were briefed before all meetings in relation to the tram project. I know we did have briefings with spokespeople and group leaders, from officers and from TIE in the form of Willie Gallagher and others. I cannot say for certain whether the Tram Sub-Committee had started but we certainly had members on the TIE Board so we knew from them where we had got to. We certainly had lots of briefings. We (Councillors) would receive written and oral briefings from our representatives on TIE and from Council officers"*⁵⁴⁷.
- In relation to the PSC meeting itself, Mr Aitken stated "*I am certain the*

⁵⁴⁶ Witness statement of Jennifer Dawe TRI00000019 paragraphs 328 to 329; see also paragraph 379 of the statement

⁵⁴⁷ Witness statement of Ewan Aitken TRI00000015 paragraph 48; see also witness statement of Jennifer Dawe TRI00000019, paragraph 378

*tram proposal was subject to a proper discussion because that was what happened with the Tram Project*⁵⁴⁸.

6.64 The understanding of members in relation to the allocation of risk at contract close is addressed at section 3 of these submissions. In short, members understood that there had been a further transfer of risk to Infraco in return for an increased price, and the price was fixed in respect of the risks that Infraco was taking on⁵⁴⁹. Steve Cardownie gave evidence that *"I do not consider that I, and members of CEC were adequately briefed on the effect and risks arising from the contract including the Infraco Pricing Schedule 4. The members understood that it said that 95% of the costs were fixed but with a project of such a large cost, 5% can be a lot of money"*⁵⁵⁰. However, officers of both TIE and the Council gave evidence that the reporting reflected their own understanding of the position; reference is made in this respect to the submissions at section 3.

Financial close

6.65 Mr Aitchison authorised TIE to enter into the contracts in terms of his letter dated 12 May 2008⁵⁵¹. However, notwithstanding the date on the letter, Mr Aitchison's evidence was that it was issued after the PSC meeting on 13 May 2008: *"I can say, unequivocally, that I would have*

⁵⁴⁸ Witness statement of Ewan Aitken TRI00000015, paragraph 50

⁵⁴⁹ See for example witness statement of Ewan Aitken TRI00000015, paragraphs 53 and 54; witness statement of Jeremy Balfour TRI00000016, paragraphs 38 and 40; witness statement of Jennifer Dawe TRI00000019, paragraphs 347 and 248

⁵⁵⁰ Witness statement of Steve Cardownie see also for example witness statement of Jennifer Dawe TRI00000019, paragraph 633 and witness statement of Lesley Hinds TRI00000099, paragraph 280

⁵⁵¹ CEC00590620

*sent my letter to TIE after and not before the meeting of the Policy and Strategy Committee. One thing I am absolutely certain about is that I would not have signed a letter like that without the authorisation to do so by elected members*⁵⁵².

- 6.66 Jennifer Dawe's evidence was that at financial close "*we were satisfied that the requisite conditions had been met. But it should be borne in mind that our satisfaction was entirely based on what the Chief Executive reported to us. We, as councillors, did not go to TIE's offices and ask to see the contracts or question them in depth. That would be entirely outwith the remit of any councillor. When it came to the actual financial close, we were assured by the Chief Executive that proceeding with the contract was what we should do. In the end, all parties on the Council signed up to that at the time*"⁵⁵³.

The approach of Council officers

- 6.67 In the situation which is before the Inquiry concerning the events which occurred up to and including the entering into of the Infraco Contract, the evidence has demonstrated that DLA in general, and Mr Fitchie in particular, owed a duty of care to advise on the terms and consequences for the Council of entering into the Infraco Contract in the form proposed. For the reasons already discussed, that duty was not fulfilled with the result that the Infraco Contract was approved by the Council to be entered into by TIE including the critical pricing

⁵⁵² Witness statement of Tom Aitchison TRI00000022, paragraph 156

⁵⁵³ Witness statement of Jennifer Dawe TRI00000019, paragraph 290

assumptions in Schedule part 4 and in a situation where it was known that the SDS design process was incomplete to a substantial extent.

6.68 Neither the Chief Executive nor the other senior Directors of the Council was legally qualified, and Gill Lindsay explained why she felt able to rely on the performance of the requisite duty of care by DLA. In that situation, it is submitted that it would not be reasonable to expect that senior officers of the Council should themselves have carried out an analysis of the proposed Infraco Contract and themselves identified the critical terms which would lead to the difficulties which are the subject of this Inquiry. Put in simple terms, the Council submits that it was reasonable for the Council as a whole, and for its senior officers individually, to rely upon the expectation that a substantial firm of solicitors engaged specifically to advise on the proposed contract would properly exercise their duty of care to bring to the attention of the Council as their client the likely effect of the critical terms and conditions.

Conclusions on the principal cause

6.69 In light of all of the evidence referred to above, and having regard to the terms of reference and to the question posed at paragraph 1.4.1 above, the Inquiry is invited to draw the following conclusions:

6.69.1 The principal (or proximate) cause of why the Project cost substantially more than budgeted for, was subject to delay and did not result in all of the proposed route being constructed, was the inclusion in the Infraco Contract of the pricing assumptions in Schedule part 4, in particular

Pricing Assumption No. 1, which together with the change mechanism in clause 80, led in combination to unquantifiable increases in cost, to the emergence of disputes, and to the ability of Infraco to delay or discontinue works whilst disputes were resolved.

6.69.2 Had officers and members of the Council been made properly aware of the consequences of entering into the Infraco Contract in the form containing Schedule part 4 and the pricing assumptions in a situation where the SDS design process was substantially incomplete, then those officers and members of the Council would have taken that into account before agreeing to the entering into of the Infraco Contract in that form.

CHAPTER 2

7. Consequences

Summary

7.1 This chapter of the Council's submissions sets out a breakdown of the £776m expenditure in relation to the tram Project and gives an explanation of the other costs that could potentially be regarded as part of the Project but which are not included within that figure.

7.2 It is also explains how the Council intended to fund the extra £231m that was required. This was primarily through prudent borrowing with a repayment period of 30 years and interest rate of 5.1%. It is estimated that the additional revenue cost arising from this additional borrowing would be £15.3m *p.a.* A response to some of the potential criticisms of the Council's accounting for the Project is also provided.

7.3 This chapter also addresses the other consequences of overspend and delay of the Project including the consequences and additional indirect costs of the reduced scope of the tram line and the actions taken to try to mitigate the effect on businesses.

Introduction

7.4 The tram line from Edinburgh Airport to York Place was opened to the public on 31 May 2014. The final capital cost of the Project was reported as £776 million.

- 7.5 At a meeting of the Council on 20 December 2007, the Council's approval had been sought for the Final Business Case version 2 and the staged award by TIE of the Infraco and Tramco contracts. The Final Business Case stated that the estimated cost of phase 1a was £498 million, fixed prices had been agreed for that phase, and tram operations were expected to commence in February 2011.
- 7.6 Prior to contractual close TIE, produced a detailed project budget estimate totalling £508m and a quantified risk allowance of £29.7m on 15 April 2008⁵⁵⁴.
- 7.7 After the Mar Hall mediation a revised project budget of £776m was approved, comprising a base budget of £742m and a risk/contingency budget of £34m⁵⁵⁵.
- 7.8 On 25 August 2011 the Council was advised that the overall programme budget should be adjusted to £776 million. The budget represented a figure of £231 million above the approved budget of £545 million. The additional £231 million required to be funded by Council borrowing, which was estimated to represent an annual revenue cost of £15.3 million over a 30 year period. After a number of votes, the Council voted in favour of a line from the Airport to Haymarket as the first phase of a longer-term, strategic plan. As a result, Transport Scotland wrote to the Council indicating that it would withhold the remainder of the £500 million committed to the Project. On 2 September 2011, the Council re-considered its position and voted to complete the line to St Andrew

⁵⁵⁴ CEC01353027

⁵⁵⁵ Witness statement of John Connarty TRI00000153, paragraph 4.1

Square, subject to a number of qualifications. The Scottish Government then announced that the remainder of the grant would be paid and that a team of experienced project managers from Transport Scotland would fill senior roles in the new governance structure to help oversee the final delivery of the project.

7.9 On 25 September 2014 the Council was provided with a report from the Chief Executive⁵⁵⁶ which reported that agreement had been reached on the final account for the largest single contract, Infraco, in the sum of £427,238,356.15, which had been settled with no disputes or claims for contractor's entitlement made or outstanding. The Project remained within the revised overall project budget of £776 million.

7.10 An appendix to the report set out the main settled costs of items of work at that stage as follows:

Item	£'000
Infraco	427,238
York Place Direct Works	1,440
Utilities – Pre mediation	82,932
Utilities – Post mediation	20,734
Leith Walk Remedial Work	394
Tram vehicles (CAF)	64,694
Enabling Works	19,156
Third Party Contributions	- 7,453
Project Management, Land & Property,	

⁵⁵⁶ CEC02084099

Scottish Water, Network Rail, Stakeholders, Readiness for Operations, Design & Legal	166,865
TOTAL	£ 776,000

7.11 In John Connarty's witness statement⁵⁵⁷, he included appendices showing a detailed breakdown of the £776.6m revised approved budget expenditure (net of contributions and recharges) as at 31 March 2017⁵⁵⁸.

7.12 Mr Connarty also set out other costs associated with the Project that were outwith the £776m as follows⁵⁵⁹:

7.12.1 Parliamentary Costs: £16.852m for progressing the Bills - this was fully funded by a separate grant from Scottish Government.

7.12.2 An estimated £6.927m for additional infrastructure, public realm and reinstatement works (including £3.95m for reinstating works done on Leith Walk) (6.3). The Council agreed that works relating to reinstatement works beyond St Andrew Square/York Place would be carried out as part of a wider programme of wider public realm improvements, separate to the tram project itself. The expenditure on the wider public realm improvement programme has been classified as Infrastructure Assets on the Council's balance sheet and is measured at historical cost. In his oral evidence Mr Connarty confirmed these works had been charged to the Council's Capital Investment Programme and

⁵⁵⁷ TRI00000153

⁵⁵⁸ Witness statement of John Connarty TRI00000153, paragraph 5.1, Appendix 6

⁵⁵⁹ Witness statement of John Connarty TRI00000153, paragraphs 6.2 – 6.20

not included the £776m for the tram but could be seen as having been caused by the Project⁵⁶⁰.

7.12.3 Support for Business:

- (a) Business rates relief - an estimated £6.3m of rates were foregone but, as these are pooled by centrally by Scottish Government, that cost was met by it;
- (b) A hardship relief scheme of £85,469 of which 25% (£21,367) was paid by the Council and the rest by the Government was not included in the £776m.
- (c) By contrast a further sum of £1.697m for supporting small businesses was included in the £776m tram budget.
- (d) An allowance of £0.545m in 2011/12 and £0.445m in 2012/23 was allocated from the Council Revenue Budget for an “open for business” scheme

7.12.4 TIE redundancy costs of £2.561m were included in the £776m but the cost of winding up the TIE pension fund of £4.798m were not included (6.10)

7.12.5 £9.821m of tram revenue expenditure (including the cost of Council staff) which had previously been part of the Project budget were transferred to the Council revenue budget for 3 years 2012-2015 (6.13).

Consequences of exceeding the budget

⁵⁶⁰ Transcript of oral evidence of John Connarty 13 December 2017, pages 22:5 to 24:7

Additional Funding / Borrowing by the Council

7.13 Obviously the main consequence of the failure to deliver the Project within budget was that additional funds had to be procured to pay for the increased cost of the Project. The Scottish Government, as it had repeatedly intimated, was not prepared to exceed the £500m funding that it had originally agreed to make available to the Project. It therefore fell to the Council to try to find the additional funds to finance the increased budget.

7.14 According to the Finance Director of the Council's report to the Council on 25 August 2011, the Council "... were able to fund the Council's increased contribution through headroom in the long-term financial plan and revenue surpluses from the TEL business plan plus further prudential borrowing by the Council. That was all detailed in the August 2011 report... The increased borrowing was very much the lesser of two evils. By this stage our previously identified contingency planning and Treasury Management savings had already been realised. We had identified further savings that were capable of future realisation because of downward movements in long term interest rates. The stability of long term interest rates indicated that the affordability of the additional borrowing was comfortably within the Council's means. This was obviously not something that we would have wanted to put into the public domain or disclosed to BBS before the mediation"⁵⁶¹.

⁵⁶¹ Witness statement of Donald McGougan TRI00000060, paragraphs 272 and 300

7.15 *“Headroom in the Council’s long term Financial Plan arose from the opportunity to re-finance previous debt that had been incurred by the Council. That was due to be fully repaid over future periods. We were able, because of reduced interest rates, to replace the previous debt carrying higher levels of interest with borrowing at more competitive rates. That provided the headroom in the Long Term Financial Plan. In 2011 there was the prospect of Scottish Government grant changes since the way in which revenue grants for councils were calculated were also being reviewed. The change in the Scottish Government national revenue grant arrangement for local authorities was very favourable to both Aberdeen and to Edinburgh... In summary, a combination of the headroom created through borrowing cost savings and the additional Scottish Government grant supplemented our Long Term Financial Plan. The revenue resources were converted into capital through the workings of the Prudential Framework⁵⁶²”.*

7.16 A detailed summary of project costs and income as at 31 March 2017 was produced by John Connarty. He noted that based on the assumptions set out within the report to Council on 25 August 2011 (that additional borrowing of £231m would be required with a repayment period of 30 years and interest rate of 5.1%), it was estimated that the additional revenue cost arising from this additional borrowing would be £15.3m p.a. (comprising repayment of principal and interest) over a 30-year period. The additional annual revenue costs arising from the

⁵⁶² Witness statement of Donald McGougan TRI00000060, paragraph 316

additional borrowing approved by the Council for the Project were estimated to equate to approximately 1% of the Council's annual gross revenue budget in 2011/12.

7.17 Council borrowing is carried out on a programme basis through a consolidated loans fund, and not on a project-by-project basis. It is not therefore possible to specify the actual cost directly associated with the additional borrowing requirement of £231m. However, the marginal interest rate on the Council's external borrowing in 2011/12 and 2012/13 was around 4% compared to the prudent estimate of 5.1% which was assumed in the Council report of August 2011. Based on a lower marginal interest rate of 4%, the annual revenue cost arising from the additional borrowing requirement of £231m would equate to circa £13.4m p.a. (comprising principal and interest) over a 30-year period. Developer Contributions are within the Council contribution of £45m to the original budget of £545m. The Council budgeted to receive £25m in cash over 20 years. Developer contributions received to date total £9.5m with the current shortfall in contributions of £15.5m managed through additional prudential borrowing. Based on a lower marginal rate of interest of 4%, the annual revenue cost arising from this additional borrowing requirement of £15.5m would equate to £0.9m p.a. (comprising principal and interest) over a 30-year period.

7.18 The annual costs (principal repayment and Interest) arising from additional prudential borrowing arising from the Project are within the £15.3m estimate which was reported to Council in August 2011. Although the level of borrowing is higher due to the current shortfall in

developer contributions, this has been offset by lower marginal interest rates. Based on a lower marginal interest rate of 4%, the annual revenue cost arising from the additional borrowing requirement of £246.5m - the additional borrowing of £231m combined with the current shortfall in developer contributions of £15.5m - would equate to £14.3m p.a. (comprising principal and interest) over a 30- year period.

7.19 Mr Connarty agreed with Counsel to the Inquiry that the current estimated interest rate of 4% could increase or decrease in the future but the current projected total over 30 years was £429M of which £182.5M would be interest.

7.20 Several witnesses including Councillor Anderson⁵⁶³ noted that the increased financing of the Project would mean that the Council would have fewer resources available for provision of services in the city, especially in an era of Council tax freezes. Others acknowledged that it might have lead to the delay of other s projects planned but no-one, in particular Councillors Dawe, Henderson and Hinds, could not remember any particular project being delayed as a result of the Project⁵⁶⁴.

7.21 Mr Connarty provided the Inquiry with a breakdown of savings identified by the Council in its budgets from 2015 to 2018⁵⁶⁵. It should be noted that these were general savings identified by the Council to demonstrate the sorts of areas in which savings had been made to improve the Council's financial position. They demonstrated that the

⁵⁶³ Witness statement of Donald Anderson TRI00000117, paragraph 354

⁵⁶⁴ Witness statement of Jennifer Dawe TRI00000019, paragraph 1033; witness statement of Lesley Hinds TRI00000099, paragraph 744; witness statement of Ricky Henderson TRI00000020, paragraph 204

⁵⁶⁵ Witness statement of John Connarty TRI00000153, appendix 16

overall savings achieved by the Council in the period 2015 to 2018 were expected to be in the region of £144M. These savings would have been part of the Council's efforts to reduce costs to meet budget constraints. These were not cuts that were required directly because of the additional costs of the Project.

Criticisms of CEC's accounting

- 7.22 Insofar as Mr Fair's evidence is regarded as a criticism of the Council's accounting practice, the following comments and submissions are made.
- 7.23 In this context, Mr Fair's report was only received on 5 March 2018, shortly before he gave evidence, and the terms of his report were not put to Council witnesses and in particular Donald McGougan, Tom Aitchison and John Connarty.
- 7.24 Mr Fair appeared to suggest that the Council's Director of Finance placed undue reliance on the Director of Finance at TIE⁵⁶⁶. Reference is made to the evidence of John Connarty at paragraph 5.5 of his written statement⁵⁶⁷.
- 7.25 In particular it should be noted that TIE undertook detailed accounting and record-keeping until 2011. £509.2m of project expenditure was incurred and accounted for through TIE. Following handover of accounting and record-keeping, £267.5m of project expenditure was directly accounted for by the Council. Details of balances and

⁵⁶⁶ Transcript of oral evidence of Stuart Fair 22 March 2018 pages 182 - 190

⁵⁶⁷ TRI00000153

transactions (9,700 lines) accounted for through TIE were provided to the Council when responsibility for project accounting transferred to the Council.

7.26 The Council's Internal Audit partner, PwC, undertook a review of the project financial management and reporting arrangements and there were no material issues raised in this audit.

7.27 All balances have been included within the historical accounts of TIE and the Council, and have been externally audited, without qualification, by Geoghegans (TIE) and Audit Scotland (the Council).

7.28 In addition, full tracking of the Project was included in the Council's annual report and accounts. The results for TIE were consolidated into the wider group accounts within the Council's financial statements each year. The Foreword to the annual report and accounts included a summary of the latest position on the Project. The Council's financial statements were completed in accordance with relevant accounting standards and audited, without qualification, across the period of the Project.

7.29 Insofar as Mr Fair sought to criticise the lack of a separate detailed asset register it is submitted that it should be noted that the Council maintains a property asset register, and a register of expenditure on non-property assets. These are used as the basis for calculating impairment, depreciation, *etc.* in accordance with local authority accounting requirements. While balance sheet reporting is at a consolidated level across the relevant reporting categories such as

“Infrastructure Assets” and “Vehicles, Plant, Furniture and Equipment”, the underlying records hold details for individual projects.

7.30 The Council has provided details to the Inquiry on the value of Tram Assets reflected on the Council's balance sheet⁵⁶⁸. Information held on the Council's register of expenditure on non-property assets in respect of the Project is maintained at a level which is sufficient for local authority accounting requirements. Service areas are responsible for maintaining operational asset registers and Edinburgh Trams Limited has initiated a project to produce a detailed asset register to inform programmes for life-cycle maintenance and refurbishment.

7.31 The statement submitted to the inquiry represents the final account for the Project, subject to settlement of a small number of ongoing matters⁵⁶⁹. Outstanding issues include final settlement with Scottish Water for utility diversions. Estimates for settlement of these outstanding issues are reflected in the statement to the Inquiry and no material variations from these estimates are anticipated. The undertaking given when John Connarty presented his oral evidence to the Inquiry was to provide a further update to the Inquiry on these outstanding matters and any associated movement in the final account for the Project.

7.32 The Council's accounts have been externally audited, without qualification, across the period of the Project.

⁵⁶⁸ Paragraph 3.142 of Stuart Fair's report to the Inquiry at TRI00000264

⁵⁶⁹ Witness statement of John Connarty TRI00000153, paragraph 4

Failure to deliver the Project on time - consequences of delay

7.33 The Executive Summary for FBVc2 stated at para 1.65 that: *“Building on the detailed cost estimates prepared in November 2006, and incorporating the firm rates and prices received from bidders in 2007, the updated project cost estimates reflect the agreed scope for Phase 1a and a programme for delivery of Phase 1a by the first quarter 2011. If the option for Phase 1b was exercised within the window of opportunity to March 2009, it could commence revenue service in 2012.”*

7.34 Thus when the Council approved the Tram Project it was hoped that trams would come into service in 2011 if Phase 1a only was implemented. In fact they did not commence service until May 2014. The delay in the commencement of service was therefore approximately 3 years.

7.35 In addition to the extra costs incurred as a result of the delay, the delay had a number of other consequences. The main ones were:

7.35.1 Increased duration of MUDFA utilities works and the repetition of such diversions along the route including on Leith Walk before the scope of tram line was reduced.

7.35.2 Increased duration of disruption due to construction activities. In particular the duration of on-street works in Princes Street and Shandwick Place.

- 7.35.3 Increased duration of traffic diversions through New Town.
- 7.35.4 Increased duration of disruption to local traders.
- 7.35.5 Increased duration of the reduction in parking opportunities and revenue due to traffic diversions through the New Town, in particular on George Street.
- 7.36 In some cases it is difficult to separate the increased disruption from the amount of disruption that would have been required to be endured during construction in any event⁵⁷⁰. However it is clear that in cases where works were prolonged or workers required to return to repeat or remediate work already undertaken, the effect on the public and other stakeholders would have been especially unfortunate.

Mitigation

- 7.37 The Council/TIE were conscious of the effects the disruption had on businesses and members of the public and attempted to communicate with those affected and to minimise or at least reduce where possible the disruption and as far as possible. This was a major consideration in for example the decision to enter into the Princes Street Settlement Agreement to attempt to progress on-street works and minimise the effect of disruption arising from the near total closure of the city's major street. They also tried to ensure that works were carried out at a time that would minimise the impact on the city's tourist trade by avoiding

⁵⁷⁰ Witness statement of Colin Smith TRI00000143, page 102

works taking place during the Festival or over the Christmas and New Year periods⁵⁷¹.

Rates Relief

7.38 The Council sought to compensate for the disruption suffered by local businesses by implementing a rates relief programme⁵⁷². A rateable value scheme was applied for retail properties impacted during tram construction. This programme would have been shorter had the Project been completed in less time. The total reduction in rates payable is estimated to have been £6.3m. Rates are pooled centrally so that amount did not affect the Council or tram project budgets. The figure due to the delay as opposed to what have been incurred if the Project had run to time would have been considerably less.

7.39 As referred to above, a separate non-domestic rates Hardship Relief scheme was agreed for businesses severely impacted by the Project. 75% of the scheme was met by the Scottish Government and 25% by the Council. The total amount was £85,469 with the Council's 25% being funded by the Council. Again this would have been less had the Project been completed on time⁵⁷³. Calls were made to TIE to increase the level of compensation but these were subject to restriction on public spending.

⁵⁷¹ Witness statement of William Gallagher TRI00000037, paragraph 408; witness statement of David Anderson TRI00000108 page 128; witness statement of Tom Aitchison TRI00000022, paragraph 338

⁵⁷² Witness statement of Alan Coyle TRI00000028 pages 210-203; witness statement of Lesley Hinds TRI00000099 page 178; Witness statement of John Connarty TRI00000153, paragraph 6.4

⁵⁷³ Witness statement of John Connarty TRI00000153, paragraph 6.4

Other Support

7.40 An additional support scheme was also introduced for small businesses impacted during tram construction, provided for one-off lump sum payments. £1.697 million of expenditure was incurred under this scheme and this was accounted for within the £776 million Tram Project budget. In addition, a budget allowance of £0.545 million in 2011/2012 and £0.445 million in 2012/2013 was established by the Council to provide support for the *'Open for Business' scheme*⁵⁷⁴.

Liaison with public and affected organisations

7.41 Throughout the Project the Council sought to keep the public informed for example, through information leaflets, meetings and the “tram helpers” scheme to provide advice to those affected and inform them about the rates relief scheme. In addition, teams of helpers were organised to help shop owners whose access had been restricted and there was an *“open for business” campaign*⁵⁷⁵.

7.42 A more formal Stakeholder Forum was established as part of the revised governance model post mediation. The Stakeholder Forum was designed to allow the Council, as Project Sponsor, together with the contractors, to manage key relationships with stakeholders directly impacted by the Project, including organisations such as BAA

⁵⁷⁴ Witness statement of John Connarty TRI00000153 page 5 paragraph 6.8; witness statement of Alan Coyle TRI00000028, page 202

⁵⁷⁵ Witness statement of Ewan Aitken TRI00000015, paragraph 123; witness statement of William Gallagher TRI00000037, paragraph 396; witness statement of Gordon Mackenzie TRI00000086, paragraphs 558 to 567, 571; witness statement of Ricky Henderson TRI00000020, paragraphs 192 to 195

Edinburgh Airport, Henderson Global Investors (St James Centre), Forth Ports and other groups such as the Edinburgh Business Forum, Essential Edinburgh, the Federation of Small Businesses (Scotland) and the Edinburgh Chamber of Commerce, as well as representatives of local communities in areas impacted by the tram.

- 7.43 There were also regular meetings with business groups and these were attended by senior figures including Councillors Hinds, Dawe Mackenzie, Wheeler and Henderson, as well as Dave Anderson, Colin Smith and Mike Connolly of TIE⁵⁷⁶.

Consequences of reduced scope

- 7.44 The consequences of not completing the full intended tram line from Edinburgh Airport to Newhaven are twofold. There were costs incurred unnecessarily and there were benefits not fully realised.

Costs of Reduced Scope

Unnecessary Preparatory Works

- 7.45 As is well documented, a lot of work was undertaken, particularly on Leith Walk under the MUDFA contract to prepare it for tram construction works before the decision was taken to restrict the line to York Place. A large part of these works would have been unnecessary had the tram been intended to terminate at York Place. However some of the works have led to improved provision of utilities and have paved the way for

⁵⁷⁶ Witness statement of Lesley Hinds TRI00000099, paragraphs 727 to 740; witness statement of Philip Wheeler TRI00000092, paragraphs 184 to 5; witness statement of Ricky Henderson TRI00000020, paragraphs 192 to 195; witness statement of David Anderson TRI00000108, page 128

the tram to be extended down Leith Walk in the future if a decision is taken to do so.

7.46 As noted above, in his evidence Mr Connarty confirmed that a further £3.953m was spent on reinstatement works on Leith Walk undertaken after the decision to stop the tram at York Place as well as public realm works at St Andrew Square. Those funds were charged to the Council's capital investment programme rather than the £776m budget for the tram. He estimated there was a further £1.547m works required to complete reinstatement works on Leith Walk and Constitution Street which were being carried out as part of a wider programme of public realm works⁵⁷⁷.

Surplus tram cars

7.47 27 trams were purchased on the basis that the tram line would run from the airport to Newhaven. It is estimated that that had it been known that the line would only run from the airport to York Place only 17 trams would have been required. Therefore there were 7-10 trams purchased that are potentially surplus to requirements if the line to not extended. Attempts were made to dispose of the surplus tram cars. For example negotiations were commenced to lease them to the Croydon Tramlink or sell them back to, or through CAF, to other countries, but these were unsuccessful⁵⁷⁸.

Other Excess Equipment and Materials

⁵⁷⁷ Witness statement of John Connarty TRI00000153, paragraph 6.3

⁵⁷⁸ See for example Witness statements of Alan Coyle TRI00000028, page 195; witness statement of Colin Smith TRI00000143, page 103.

7.48 As part of the settlement agreement reached following the mediation at Mar Hall, all of Siemens' excess materials and equipment that were intended to be used on the tram line beyond York Place were transferred to the Council. During the Inquiry a number of witnesses were asked to what extent these could be utilised in a continuation of the tram line down Leith Walk in the future. The Siemens' witnesses' position was in general that they should be capable of being re-used. Some of the rails would be standard and some would be specifically pre-bent for the Project although, according to Axel Eickhorn some of the heavier materials had not in the end been delivered and credit was given in their place. It was generally agreed that any equipment that had been kept in storage would require to be checked before being re-used but should be in a suitable condition⁵⁷⁹.

7.49 It is submitted that the agreement to transfer title to the Siemens materials and designs was a sensible decision as part of the settlement agreement. In particular, the transfer of the design will be of benefit to the city if a decision is taken to extend the tram line down Leith Walk. It has not necessarily tied the Council into contracting with the consortium, has ensured the design is available and secured some of the more specialist materials required. It is however acknowledged that a number of utilities conflicts remain especially in Picardy Place and Leith Walk and that any materials retained would need to be carefully checked before being re-used.

Unrealised benefits of reduced scope of line

⁵⁷⁹ Transcript of oral evidence of Axel Eickhorn 7 December 2017, page 30:18- 23

Operating performance

- 7.50 Leith Walk was expected to be a significant trip generator for tram, especially at the foot of Leith Walk as it is a major public Transport interchange. The adverse impact on revenue of not extending the line down Leith Walk was estimated by Alan Coyle to be approximately £4m per annum⁵⁸⁰.
- 7.51 Various witnesses noted that it had been hoped that the presence of the tram line down to Newhaven might have acted as a catalyst or complementary factor to development and regeneration in the Leith and Newhaven areas⁵⁸¹.
- 7.52 Some expected developer contributions were lost as a result of the reduced scope of the tram line, although some of these were also lost because of the economic downturn following the recession of 2008 that reduce development in general⁵⁸².
- 7.53 In June 2011 the additional capital cost of completing the tram infrastructure to the foot of Leith Walk was currently estimated at £100 million and, to Newhaven, £160 million (based on a risk allowance of 100% and a Bill of Quantities priced against a Schedule of Rates). Intrusive studies would be required to achieve a more precise estimate. During the Inquiry the issue of the extent to which preparatory works

⁵⁸⁰ Witness statement of Alan Coyle TRI00000028, page 196

⁵⁸¹ For example witness statement of Donald Anderson TRI000000117, paragraph 349; witness statement of Jeremy Balfour TRI00000016, paragraph 95; witness statement of Alan Coyle TRI00000028, page 191; witness statement of Philip Wheeler TRI00000092, paragraph 190

⁵⁸² Witness statement of Ewan Aitkin TRI00000015, paragraph 128; witness of Jennifer Dawe TRI00000019, paragraph 1038; witness statement of Alan Coyle TRI00000028, pages 191 to 2; witness statement of Gordon Mackenzie TRI00000086, paragraph 582; witness statement of David Anderson TRI00000108, page 128

had been completed that would allow the tram line to be extended to Leith or Newhaven in the future was raised; reference is made in this respect to section 24 of these submissions.

Other Consequences

7.54 The cost over-run and delay also had other consequences. For example it was recognised by several witnesses that it had an adverse impact on the reputation of the Council and the city in general and potential economic damage to businesses as a result⁵⁸³.

7.55 A number of witnesses, while acknowledging the very significant problems experienced by the Project commented that they were proud of the fact that in the end a modern tram line had been installed and of the quality of the final product produced⁵⁸⁴.

7.56 Initial use of the trams has been in line or slightly higher than predicted⁵⁸⁵.

Conclusion

7.57 Unfortunately cost over-runs are not uncommon in publicly financed projects including light rails projects. Professor Flyvbjerg's evidence that a 52% over-run was not a statistical outlier. It was twice the median cost

⁵⁸³ E.g. Witness statement of Donald Anderson TRI00000117, paragraph 350; witness statement of Ewan Aitken TRI00000015, paragraph 127; witness statement of Jennifer Dawe TRI00000019, paragraph 1037; witness statement of Jeremy Balfour TRI00000016, paragraph 91; witness statement of Alan Coyle TRI00000028, page 194; witness statement of Jim Inch TRI00000049, paragraph 233; witness statement of Gordon Mackenzie TRI00000086, paragraph 582; witness statement of Philip Wheeler TRI00000092, paragraph 190; witness statement of Tom Aitchison TRI00000022, paragraph 339

⁵⁸⁴ E.g. Witness statement of Donald Anderson TRI00000117, paragraph 355

⁵⁸⁵ Witness statement of Jim Inch TRI00000049, paragraph 235

over-run of 25% but 23% of light rail projects had a greater cost over-run than the Edinburgh Tram Project⁵⁸⁶.

7.58 It is submitted that the tram line was delivered broadly in line with the budget agreed following the Settlement Agreement in September 2011. The cost increases were effectively crystallised at that point but they were caused by failings much earlier in the Project's life, most notably at the time the Infraco contract was entered into.

⁵⁸⁶ Transcript of oral evidence of Bent Flyvbjerg 22 March 2018, page 22:3 to 23:4

CHAPTER 3

8. Procurement Strategy

Summary

- 8.1 The procurement strategy was aimed at de-risking the main contract by undertaking design and utilities works to an advanced stage. This was intended to enable the main contract to be let at a more certain cost/terms. The initial contracts would then be novated as part of the main infrastructure contract.
- 8.2 The procurement strategy was the responsibility of TIE. However there were other bodies contributing to the strategy including the Scottish Executive, Partnerships UK, the Council, and DLA. A working group was established which included other professionals who provided their opinions and insight on procurement.
- 8.3 The rationale was to not only to reduce risk but also pass that risk to the private sector. The separate contracts also enabled specialists to be appointed for the discrete contracts.
- 8.4 The suitability of the procurement strategy should not be confused with the problems which arose in terms of the delays and cost overruns. The contract terms were not a consequence of the strategy but rather the execution of the contracts, in particular the provisions of the Infraco contract. Nonetheless the Council recognises that the strategy was not conventional and TIE may have lacked some of the skills required to manage the contracts.

The procurement strategy

- 8.5 The fundamental objective of the approach to the procurement was to complete the preliminary works to such an advanced stage that the main infrastructure works would be de-risked to enable the main infrastructure contract to be let at a more certain and lower sum than if the risk of design and utilities remained.
- 8.6 The principal elements of the procurement strategy and objectives are identified in the executive summary of the draft Final Business Case of November 2006⁵⁸⁷.
- 8.7 In short, the reasoning for the detailed design and utility diversions preceding the main contract was to enable a firm price bid. The substantial construction risk was to be passed to the private sector with the revenue risk being retained by the Council.
- 8.8 The strategy therefore required four separate contracts to be awarded at different stages as follows: (1) the SDS Contract (Design); (2) the Multi Utilities Diversion Framework Agreement (MUDFA) (Utilities); (3) the contract ("Tramco") for the supply and maintenance of the tram vehicles; and (4) the main infrastructure contract (Infraco).

When and How Procurement was Determined & Persons Involved

- 8.9 The history and development of the procurement strategy is discussed in the Interim Outline Business Case of May 2005⁵⁸⁸.

⁵⁸⁷ CEC01821403

⁵⁸⁸ CEC01875335

- 8.10 In September 2002 Turner and Townsend, on behalf of the Council and TIE, considered various procurement and funding options in a Strategic Review paper⁵⁸⁹. The review considered a number of issues including procurement and lessons from other similar projects. The various procurement models were variants of design and build contracts including Private Public Partnership options.
- 8.11 Donald McGougan's evidence was that due to the revenue risk of the Project it would not be attractive to the private sector in a PPP arrangement⁵⁹⁰.
- 8.12 In November 2002 TIE issued a press release⁵⁹¹. The press release indicated that various professional advisors had been appointed in relation to the Project. DLA was identified as providing legal advice on procurement and strategy. Grant Thornton was appointed to provide financial and business case advice. The remaining professional advisors appointed are not relevant in the context of procurement and related strategy.
- 8.13 TIE established a working group to consider procurement. On 13th December 2002 TIE's Procurement Working Group met. The objectives of the Procurement Working Group were:

⁵⁸⁹ CEC01868789

⁵⁹⁰ Transcript of oral evidence of Donald McGougan 29 November 2017, page 134:1- 5

⁵⁹¹ CEC00114235

“To ensure the development of a procurement strategy which enables the tram lines to achieve Royal Assent and be procured in the shortest possible time and with the minimum risk to successful operation”⁵⁹².

- 8.14 The working group comprised individuals from TIE, the Council, Grant Thornton, DLA, Partnerships UK, Mott MacDonald, and Faber Maunsell.
- 8.15 Geoff Gilbert was a member of the working group and explained in his evidence that consideration was given to a form of PPP but that would be unaffordable⁵⁹³. Similarly Alex Macaulay identified that a PFI arrangement would not be appropriate as you would need to buy the operator out and pay compensation if you wanted to build an extra tram line at a later stage⁵⁹⁴.
- 8.16 In July 2003 Grant Thornton prepared an evaluation of the procurement options⁵⁹⁵. The procurement options included variations of design and build contracts and partnering arrangements. The considerations included undertaking the utility works in advance of the main contract. The Scottish Executive and Partnerships UK endorsed the strategy of TIE appointing a private sector operator to assist during the development stages. The Council submit that it is clear that the (then) Scottish Executive was closely monitoring the progress and decisions being taken regarding procurement.

⁵⁹² CEC01853491

⁵⁹³ Witness statement of Geoff Gilbert TRI00000038, page 25

⁵⁹⁴ Witness statement of Alex Macaulay TRI00000053, page 25

⁵⁹⁵ CEC01868299

8.17 In November 2003 the STAG 2 appraisal was published by TIE in which Appendix E stated the advantages of advanced utility works⁵⁹⁶.

8.18 In May 2004 the Procurement Working Group identified that the preferred option was separate contracts for the tram vehicles and the infrastructure. The Scottish Executive was kept updated with all significant progress on the procurement discussions⁵⁹⁷.

8.19 Stewart McGarrity explains that:

*"The procurement strategy was developed in consultation with CEC, Scottish Executive, Partnerships UK, and Transdev in 2004"*⁵⁹⁸.

8.20 Donald McGougan states that:

*"Transport Scotland, with their experience from past projects, suggested that a design and build contract would result in the contractor building in significant sums for risk"*⁵⁹⁹.

8.21 Geoff Gilbert states:

*"There was quite a lot of external scrutiny of the project. During the early stages of the project there was support from Transport Scotland...oversight from Partnerships UK... (and)...an audit by Audit Scotland in mid 2007..."*⁶⁰⁰.

⁵⁹⁶ CEC00642726

⁵⁹⁷ CEC01880646

⁵⁹⁸ Witness statement of Stewart McGarrity TRI00000059, page 5

⁵⁹⁹ Witness statement of Donald McGougan TRI00000060, page 14

⁶⁰⁰ Witness statement of Geoff Gilbert TRI00000038, pages 3 to 4

8.22 Susan Clark was also involved in the procedural and process issues relating to the procurement of the Infraco contract⁶⁰¹ and explains that there was a design, procurement and delivery sub-committee established⁶⁰². The assertion that the SETE group was not involved in either the development of the procurement strategy nor Infraco process (page 23 of SETE's submissions) fails to recognise not only the direct involvement but the timing of appointments. With the exception of Mr Jeffrey and Mr Mackay all SETE employees were appointed prior to May 2008 and all had input into the assessment of either the strategy and/or Infraco.

8.23 As noted above DLA was instructed to act as solicitors giving advice on the procurement. It is therefore surprising that DLA's submissions (paragraph 26) indicate that neither DLA nor Mr Fitchie sought to assess whether the procurement strategy would be successful. This was integral to the advice and recommendations being provided. Sharon Fitzgerald of DLA confirmed in evidence that:

*"... there was very little involvement of the Council, and we were of course acting in accordance with the legal services agreement that we had in place with tie, which had been the subject of public procurement in 2002..."*⁶⁰³ DLA staff providing advice included Ms Fitzgerald and Andrew Fitchie, although there was also contact with DLA's head of UK

⁶⁰¹ Transcript of oral evidence of Susan Clark 25 October 2017, page 107:18- 19

⁶⁰² Transcript of oral evidence of Susan Clark 25 October 2017, page 108:10- 15

⁶⁰³ Transcript of oral evidence of Sharon Fitzgerald 22 November 2017, page 132:14- 18

transport Nick Painter who had been involved in other trams schemes in the UK⁶⁰⁴.

8.24 In terms of the procurement strategy Ms Fitzgerald confirmed her statement evidence as including:

“A number of elements in the procurement strategy for the tram project were developed on the basis of what was said in that NAO (National Audit Office) report. This was where the Partnerships UK team was effective. They brought forward their experience of what was regarded as UK best practice. Also Andrew (Fitchie), at that time, had been involved in another tram scheme in the UK”⁶⁰⁵.

8.25 The procurement strategy was scrutinised by KPMG.

8.26 Ms Fitzgerald confirmed that the NAO reports summarised the experience of other light rail projects and recommended:

“...early operator involvement, early design and also moving of the – doing utilities diversions in advance of the main construction contract being let.”⁶⁰⁶

8.27 In September 2005 TIE entered into the SDS (System Design Services) agreement with Parsons Brinckerhoff Ltd. This contract had three main phases, being the requirements definition stage (completed by the end of 2005), the preliminary design stage, and finally the detailed design stage.

⁶⁰⁴ Transcript of oral evidence of Sharon Fitzgerald 22 November 2017, page 142:20- 25

⁶⁰⁵ Transcript of oral evidence of Sharon Fitzgerald 22 November 2017, page 141:12

⁶⁰⁶ Transcript of oral evidence of Sharon Fitzgerald 22 November 2017, page 141:21- 23

- 8.28 In October 2006 TIE appointed Alfred McAlpine Infrastructure Services Ltd under the MUDFA contract to undertake the utility works. Those works were in 2 stages: (1) the pre-construction to refine scope and costs; and (2) the construction phase. It was intended that those works would be completed by the end of 2008 in advance of the main infrastructure works.
- 8.29 Tramco was entered into with Construcciones y Auxiliar de Ferrocarriles SA (CAF) which joined the BBS consortium.

Rationale

- 8.30 The Procurement Working Group produced a report on procurement in April 2004⁶⁰⁷. The April 2004 report noted:

“...the general view, given TIE’s own resources and experience (essentially a procuring body, rather than a major project management organisation) and the scale and complexity of the tram infrastructure scheme, was that we should be seeking to transfer a significant majority of the major project risk to private sector partners. In particular, key risks to be transferred (at an appropriate price) should include the majority of construction risk...”

- 8.31 In May 2005 TIE produced a draft Outline Business Case⁶⁰⁸. This was to contain what was ultimately pursued namely the separation of the works. The outline business case identified that the procurement would be disaggregated into direct contractual appointments for: (1) design;

⁶⁰⁷ CEC01853647 & CEC00380901

⁶⁰⁸ CEC01875336 & CEC01875335

and (2) utility works. This enabled specialists to be appointed and thereafter the contracts could be novated as part of the main infrastructure contract. The objective included the consequent transfer of design risk upon novation. It was also intended to reduce risk and consequent cost of the main infrastructure works if the utility diversions works were undertaken in a separate and earlier contract. Accordingly the outline business case supported this phased approach to the contracts.

8.32 Kenneth Hogg's evidence identifies that TIE's strategy was based on best practice from the experience of other light rail schemes in the UK and from evaluation by the National Audit Office. According to Mr Hogg this:

*"...highlighted the advantages in procuring separate contracts, whereby specialist contractors played to their strengths and undertook works that they were expert in rather than having a single contractor accepting the risk and responsibility for a wider range of works, not all of which they had expertise in. It also highlighted the advantages of a phased approach under which enabling works would be completed as far as possible before the actual construction work of the main project commenced."*⁶⁰⁹

8.33 Geoff Gilbert's evidence was that the "neat strategy" had been to de-risk the contract. Mr Gilbert had not experienced or read about any

⁶⁰⁹ Witness statement of Kenneth Hogg TRI00000045, page 75

such similar strategy having being adopted elsewhere⁶¹⁰. Mr Gilbert stated that the strategy had been:

“...created to bring certainty to the programme and project through designing out uncertainty and getting all the approvals in place at successive project stages”, but was “reliant upon things happening and decisions, whether they be design or approvals, being made at the right time in the design process to avoid delay”⁶¹¹. He correctly concludes that the strategy was not wrong simply because it had not been tested elsewhere.

8.34 Stewart McGarrity identifies the principal objectives in his statement⁶¹² as follows:

8.34.1 Early involvement of an experienced tram system operator under the Transdev contract. This was to enable an experienced operator of tram systems to be involved in the design and specification to give assurance on the operability of the trams.

8.34.2 Early design work through the SDS contract (Parson Brinckerhoff) with a view to having detailed design completed for the Infracore bidders to take into account when submitting bids. The logic was that the risk would be lower if the design was at an advanced stage.

8.34.3 Early utility diversions works under the MUDFA contract to mitigate against disruption which could be caused by the Infracore (main infrastructure) works being undertaken at the same time as the utility

⁶¹⁰ Witness statement of Geoff Gilbert TRI00000038, page 3

⁶¹¹ Witness statement of Geoff Gilbert TRI00000038, page 3

⁶¹² Witness statement of Stewart McGarrity TRI00000059, page 7

diversions. A further aspect to this was to avoid the additional costs for risk which would be likely to be included in the Infraco bids if these included the utility works. The early utility works was a key lesson from previous tram projects as recommended in a National Audit Office report from 2004.

8.34.4 Separate procurement of the tram vehicles (the Tramco contract) which was separate from the Infraco contract. The rationale was to enable TIE to select the tram vehicles best suited to the Edinburgh Tram Project.

8.34.5 Finally it was intended that there would be aggregation of the contracts by novation of the SDS and Tramco contracts into the Infraco contract. The objective and rationale of the novation was that one party/contractor was carrying most of the delivery risks.

Suitability

8.35 Clearly the suitability should not be assessed solely on the basis of whether the objectives were met but by considering the reasons for any failures.

8.36 Steve Reynolds had been involved in the Manchester Metrolink project. Unlike Edinburgh the project in Manchester had “...an *integrated management team*”⁶¹³. Mr Reynolds stated that he wondered if it was possible to have a collaborative culture given the separate contracts for design, utility, and infrastructure. Mr Reynolds concluded that you

⁶¹³ Transcript of oral evidence of Stephen Reynolds 11 October 2017, page 181:24- 25

would need to “...use different contract terms that promoted collaboration”⁶¹⁴. Accordingly one component which contributed to the failure was the poor working relationship between the parties as more fully considered in section 19 of these submissions. It is submitted that those poor working relationships could not reasonable have been foreseen during the strategy stages. A conventional design and build contract which comprised not only the infrastructure but also design and utility works may also have suffered from poor working relationships.

8.37 Graeme Barclay gave evidence that the utilities works were not completed when the Infraco contract commenced but that this did not prevent both contractors working together. Mr Barclay was of the opinion that the transferring of utility works to Infraco which “*worked reasonably well*”⁶¹⁵. This again reinforces the importance of the working relationships which failed.

8.38 Tony Rush was of the view that the TIE staff had the skills and competence to work on a normal design and build contract, but that the contact arrangements in the Project were “*exceptional*” and “*highly unusual*” meaning that those persons managing the contract needed additional skills and expertise⁶¹⁶. Mr Rush was of the opinion that the transfer of design and risk was “*not well undertaken*”⁶¹⁷ and therefore the risk came back to the client. The skills required to deal with such an usual contract were a “*...professional project management team*”⁶¹⁸.

⁶¹⁴ Transcript of oral evidence of Stephen Reynolds 11 October 2017, page 185:12- 25

⁶¹⁵ Transcript of oral evidence of Graeme Barclay 7 November 2017, page 11:25

⁶¹⁶ Transcript of oral evidence of Anthony Rush 9 November 2017, page 117:15 to 118:11

⁶¹⁷ Transcript of oral evidence of Anthony Rush 9 November 2017, page 118:20

⁶¹⁸ Transcript of oral evidence of Anthony Rush 9 November 2017, page 119:14

Accordingly the suitability of the contract has to be considered in the context of those persons administering the contract. Regrettably it is the Council's submission that the skills of those persons within TIE was not suited to meet the challenges that arose.

8.39 Geoff Gilbert highlighted that simply because the contract had not been used elsewhere that did not result in the strategy being wrong⁶¹⁹. However in hindsight he concluded that the procurement did not take into account the complexities such as working in a congested city centre, the number of stakeholders that needed to be consulted, and the approvals required⁶²⁰. Mr Gilbert explains that Infrastructure UK (now IPA) has:

*“...since developed tools (including the Procurement Route map) for understanding and defining the complexity of such projects. They have developed tools to allow a better assessment of the capabilities of both the team and supply chain, identify gaps and then adjust the strategy to deal with them...These tools did not exist in their current form at the time of the Tram Project...”*⁶²¹.

8.40 Accordingly it is conceivable that a similar strategy today may be successful, particularly where a collaborative working relationship exists.

8.41 Similarly Duncan Fraser identified that the Infraco Contract being used had not been used previously and accordingly had “*never really been*

⁶¹⁹ Witness statement of Geoff Gilbert TRI00000038, page 3

⁶²⁰ Witness statement of Geoff Gilbert TRI00000038, page 4

⁶²¹ Witness statement of Geoff Gilbert TRI00000038, page 4

tested⁶²². Mr Fraser was not directly involved in the procurement strategy but recognised that:

*“The aims of the procurement strategy were not fully met because the Infracore tender was put out prior to completion of MUDFA and design consents and approvals.”*⁶²³

8.42 For completeness Joachim Enenkel disagreed with the suggestion that the strategy was unusual stating:

*“The procurement strategy of TIE (phased approach) is a common approach including early investigation/relocation of utilities and the like.”*⁶²⁴

8.43 The Council submits that the contract was not a standard form and contained provisions which diverged substantially from the norm. The principal challenge was the Pricing Assumptions. The fact that design was not completed to the anticipated detail (for example) or that the working relationships were strained does not distract focus from the real cause of the difficulties which arose, namely the contractual terms.

8.44 As a number of witnesses identified a significant issue was timing. Geoff Gilbert stated:

*“The delivery of the strategy depended upon the right things coming together at the right time.”*⁶²⁵

⁶²² Transcript of oral evidence of Duncan Fraser 12 September 2017, page 9:12- 13

⁶²³ Transcript of oral evidence of Duncan Fraser 12 September 2017, page 10:25 to 11:2

⁶²⁴ Witness statement of Joachim Enenkel TRI00000150, page 9

⁶²⁵ Witness statement of Geoff Gilbert TRI00000038, page 25

8.45 Lesley Hinds stated that the design should have been nailed down before the Infraco contract was awarded. This is consistent with the evidence of Scott McFadzen (of TIE) who confirmed that

*“...the design would be completed and all necessary statutory approvals and consents would be obtained prior to the Infraco contract award. That was the big selling point for us.”*⁶²⁶

8.46 In conclusion the Council submits that the strategy of undertaking design and utility diversions was not flawed. There were obvious and clear advantages to such an approach. The difficulties which arose did not arise from the strategy. Indeed the difficulties did not arise principally because of the poor working relationships and failure to complete the design and utility works, though these undoubtedly exacerbated the problems. Had the design and utility works been completed clearly the scope for the additional sums sought by Infraco may have been cushioned. However the principal cause of the cost overrun was the contractual terms discussed under chapter 1, section 2. The contractual mechanisms entitled Infraco to make very substantial claims for additional time and money.

⁶²⁶ Witness statement of Scott McFadzen TI00000058, page 4

9. **Governance and project management**

Summary

9.1 The Council submits that the use of an arm's length company was appropriate. The Scottish Executive strongly encouraged the use of a company and the involvement of the private sector. The Council did not have an in-house capacity to manage the Project. Furthermore the Council's pay and grading structures would have restricted recruiting the staff required to manage the Project. An arm's length company had the ability to raise finance that was not available to a local authority.

9.2 The Council recognises that the governance of the Project was certainly not perfect, but in practice worked sufficiently well, a submission shared with SETE⁶²⁷. However the Council submit that the multiple bodies, whilst arguably cumbersome, operated in reaching decisions as required at both strategic and operational levels. To the extent that the membership of the various boards were duplicated acted as a check and balance and met the overall objectives. On no reasonable view could the governance structure be said to have caused or materially contributed to any cost overruns in the Project.

Decision to use an Arm's Length Company

9.3 In October 2001 the Council agreed to submit an application to the (then) Scottish Executive by May 2002 seeking approval in principle for the Integrated Transport Initiative for Edinburgh and South East

⁶²⁷ Page 9 of the written submissions made by SETE on 27 April 2018

Scotland⁶²⁸. At the same meeting the Council approved in principle the establishment of an arm's length company. Prior to the formation of TIE the support by the Scottish Executive for an arm's length company and involvement of the private sector was evident. On 28th February 2002 Wendy Alexander, the then Minister for Enterprise, Transport and Lifelong Learning wrote to the Council in which she explained the Ministers' views that

“As you know I firmly believe that the private sector has much to contribute to this process (the transport initiative) and I strongly support the principle of an off balance sheet company (ENTICO) to progress the Council's plans”.

9.4 The encouragement by the Scottish Executive was identified in the evidence of a number of former Council officers, for example Tom Aitchison⁶²⁹, and councillors, such as Ewan Aitken and Donald Anderson⁶³⁰.

9.5 Other than the support from the Scottish Executive there were other reasons for establishing an arm's length company, including lack of experienced personnel within the Council, inability to attract the required personnel and funding. Tom Aitchison identified that local authorities had lost a lot of technical and engineering capacities for large scale projects over the past 20 years⁶³¹. The Council had no similar experience of delivering on-street large scale engineering

⁶²⁸ USB00000228

⁶²⁹ Witness statement of Tom Aitchison TRI00000022, page 5

⁶³⁰ Transcript of oral evidence of Ewan Aitken 6 September 2017, page 140:7- 11. Transcript of oral evidence of Donald Anderson 6 September 2017, page 195:11- 15

⁶³¹ Transcript of oral evidence of Tom Aitchison 28 November 2017, page 28:12- 17

projects, and was restricted to road building⁶³². Alan Robertson's evidence was that a local authority did not have the strength in depth to deliver a £500m project. Alan Robertson stated:

*"The vast majority of projects of this size are delivered through significant existing authorities e.g. Network Rail, the Environment Agency and TfL. A local authority doesn't have that strength and depth of expertise to deliver (a) £500m or £1bn."*⁶³³

9.6 Mr Robertson noted that the situation would be equally true of another large city authority citing Glasgow City Council⁶³⁴. Local Government re-organisation in 1996 resulted in the retirement of a number of senior staff from the former Regional Councils and the experience those persons held. There was therefore a lack of in-house experience⁶³⁵. It was regarded as being too large a project to be handled in-house. Andrew Holmes' opinion was that not only could a local authority not deliver the Project but that there was scepticism of local authorities. This was a general (negative) perception by those outside the authority such as the Scottish Executive⁶³⁶. This scepticism arose in part due to the failure to deliver an earlier bus project for West Edinburgh⁶³⁷.

9.7 Mr Holmes also notes that there were financial and funding reasons for the formation of a company:

⁶³² Witness statement of Tom Aitchison TRI00000022, page 5

⁶³³ Witness statement of Alan Robertson TRI00000070, page 5

⁶³⁴ Witness statement of Alan Robertson TRI00000070, page 5

⁶³⁵ Witness statement of Andrew Holmes TRI00000046, page 5

⁶³⁶ Witness statement of Andrew Holmes TRI00000046, page 5

⁶³⁷ Witness statement of Andrew Holmes TRI00000046, page 5

“...one was that it takes you out of the local government year on year budgeting restrictions...the company is able to be more flexible both in its spending and in how it raises its funding”⁶³⁸.

9.8 Accordingly TIE could obtain funding in the market which would not be available to the Council as noted in Mr Aitchison’s statement⁶³⁹.

9.9 An arm's length company also had the advantage of being:

“...more commercially focussed, with the ability to make quick decisions...”⁶⁴⁰.

9.10 There was no need for the Council (including political members) to make decisions. It was only where the costs exceeded £1m that the Council required to be involved in the decision making process.

9.11 The final principal reason, and advantage, of forming a company related to recruitment of staff. The Council had a particular pay and grading structure. The pay and grading has been subject of Union negotiations and equal pay disputes. TIE was not restricted to the pay and grading structures of the Council. Therefore the formation of TIE retained recruitment advantages over establishing an in-house function within the Council. Councillor Whyte identified that engineers for projects such as the Edinburgh Tram Projects:

“may be paid considerably more than a Council engineer...it allowed you to pay more to get the correct expertise”⁶⁴¹.

⁶³⁸ Witness statement of Andrew Holmes TRI00000046, page 4

⁶³⁹ Witness statement of Tom Aitchison TRI00000022, page 4

⁶⁴⁰ Witness statement of Malcolm Reed TRI00000066, page 45

9.12 Councillor Whyte also identified that “*if something went wrong and you had to wind it up...without having the worry of people on the Council payroll as well*”⁶⁴².

9.13 As a consequence of the views of the Scottish Executive and other advantages noted above in May 2002 the Council formed Transport Initiatives Edinburgh Limited (TIE) as an arm's length company to deliver the New Transport Initiative for the City of Edinburgh.

Bodies involved to 2009 and their roles and functions

9.14 Tram Project Board (“TPB”)

9.14.1 The TPB was set up as a decision-making forum which comprised representatives from TIE, TEL, and the Council (both councillors and Senior Officers including the Tram Monitoring Officer).

9.14.2 Tom Aitchison notes in his statement that:

*“the TPB was established in 2005 and was a key component in the governance structure for the tram project. I think it may have been a specific requirement set out by Transport Scotland. It was created as a high level project management body to oversee delivery of the tram project”*⁶⁴³.

9.14.3 Mr Aitchison further identifies that the role of the TPB included overseeing the execution of the delivery of the Project, approving

⁶⁴¹ Transcript of oral evidence of Iain Whyte 7 September 2017, page 47:14- 17

⁶⁴² Transcript of oral evidence of Iain Whyte 7 September 2017, page 48: 17-19

⁶⁴³ Witness statement of Tom Aitchison TRI0000022, page 104

funding requests and ensuring proper reporting to the TEL board and/or the Council⁶⁴⁴.

9.14.4 Willie Gallagher's evidence is that Transport Scotland insisted that the TPB was a sub-committee of TEL⁶⁴⁵.

9.15 Transport Edinburgh Limited ("TEL")

9.15.1 TEL was intended to have strategic oversight of the integration of Lothian Buses and the Trams in Edinburgh⁶⁴⁶. The aim was to:

*"Ensure the integration of bus, tram and potentially other public transport schemes in Edinburgh to provide a single integrated public transport system"*⁶⁴⁷.

9.15.2 Tom Aitchison identified that:

*"TEL was created in 2004, at a time when the Council had ambitious plans for transport improvements in and around Edinburgh. The think was that an overarching organisation could be formed to take forward transport policy development but with a strong operational and delivery aspect. That all changed after the road congestion charging referendum when TEL's role became much more specific and focussed on the integration of tram and bus operations"*⁶⁴⁸. The role of the TEL

⁶⁴⁴ Witness statement of Tom Aitchison TRI00000022, pages 104 to 105

⁶⁴⁵ Witness statement of Willie Gallagher TRI00000037, page 57

⁶⁴⁶ CEC01887027 at page 1

⁶⁴⁷ Witness statement of Kenneth Hogg TRI00000045, page 21

⁶⁴⁸ Witness statement of Tom Aitchison TRI00000022, page 107

board was focussed on statutory stewardship and overall responsibility to deliver an integrated transport network⁶⁴⁹.

9.16 **Transport Initiatives Edinburgh (TIE)**

9.16.1 Tom Aitchison identifies that TIE's role was "*getting the tram built*" and TEL's was "*public transport integration*"⁶⁵⁰.

9.16.2 TEL's membership included elected members and persons from the private sector, and Neil Renilson, the Chief Executive of Lothian Buses.

9.17 **Transport Scotland**

9.17.1 The Inquiry Statement of Main Events notes that following the May 2007 elections:

"Transport Scotland would relinquish its seat on the Tram project Board and would not attend meetings of the Tram Project Board in any capacity, and would, instead, receive regular confirmation from CEC that all grant conditions were being complied with."

9.17.2 Whilst the Council agrees that Transport Scotland remained informed, the Council submits that Transport Scotland's involvement post the 2007 election included being consulted and updated by TIE and the Consortium. This was in addition to being updated by the Council. Accordingly the Ministers were kept advised of matters and intervened during disputes e.g. John Swinney's involvement in the Princes Street Dispute (discussed under the Princes Street Dispute chapter of these

⁶⁴⁹ CEC01758865

⁶⁵⁰ Witness statement of Tom Aitchison TRI00000022, page 107

submissions). Mr Swinney was kept advised during the Mar Hall Mediation at which Transport Scotland was present. Similarly Mr Stewart Stevenson's involvement post dates the 2007 election. His evidence was that "*I did not deal with the Council very much in relation to the tram project*"⁶⁵¹. He had no regular meetings with the Council but met with TIE's Chief Executive on average every 2 months⁶⁵². Mr Stevenson states:

*"the two people I met most often were Willie Gallagher, and subsequently Richard Jeffrey"*⁶⁵³.)

9.17.3 Mr Stevenson also met with BB⁶⁵⁴.

9.18 City of Edinburgh Council

9.18.1 The Council was not a main body in the day to day operational matters relating to the Tram Project. However the Council established its Internal Planning Group ("IPG") for the purposes of internal oversight. More significantly the Council was represented on the boards of TEL, TIE and the TPB. In the written submissions made by DLA⁶⁵⁵, it is stated that the Council, the legal team, took a "*very hands off*" approach and might have taken more involvement in the "*day to day project management*". Whilst the Council recognises that it bore certain responsibilities in ensuring project delivery these were at a strategic level and not in the day to day operational matters. The intention, as

⁶⁵¹ Witness statement of Stewart Stevenson TRI00000142, page 17

⁶⁵² Witness statement of Stewart Stevenson TRI00000142, page 47

⁶⁵³ Witness statement of Stewart Stevenson TRI00000142, page 17

⁶⁵⁴ Witness statement of Stewart Stevenson TRI00000142, page 48

⁶⁵⁵ Paragraph 32 of the written submissions of DLA dated 27 April 2018

guided by the Scottish Executive, was that TIE would be responsible for the day to day matters relating to the Tram Project. Further DLA had been engaged to assist and any suggestion that the Council distanced itself from the Infraco Contract requires to be put in the context of what TIE was established to achieve and what DLA had been instructed to achieve.

Composition of Boards of TIE, TEL and TPB

9.19 TIE

9.19.1 The TIE board comprised paid full time executive directors involved in the day to day operational and strategic aspects of the Project. In addition there were non-executive Directors including Brian Cox and Kenneth Hogg, who brought experience from the transport industry. Finally the TIE board included councillors such as Gordon Mackenzie, Ricky Henderson and Philip Wheeler.

9.20 TEL

9.20.1 The board of TEL comprised executive and non-executive directors. The Council exercised some control of TEL via appointments to the board of TEL which included elected members and individuals from private industry. Tom Aitchison's evidence identifies that those persons from private industry included a range of rail experience and public policy experience⁶⁵⁶. The TEL board comprised senior Council officers such as David Anderson and Donald McGougan, and

⁶⁵⁶ Witness statement of Tom Aitchison TRI0000022, page 107

councillors such as Andrew Burns, Richard Henderson and Gordon Mackenzie. Individuals from Industry such as Brian Cox and Kenneth Hogg were also present. Senior officers in TIE such as Vic Emery, Willie Gallagher and Richard Jeffrey held positions during the existence of TIE. Neil Renilson was also a board member bringing his experience from Lothian Buses.

9.21 **TPB**

9.21.1 The TPB comprised senior personnel within from TIE, TEL and the Council. This was in addition to the political membership and senior officers of Transport Scotland (until summer 2007).

Changes to Governance in 2007 and 2009

9.22 **2007**

9.22.1 There were two principal changes to the governance of the Project in 2007. Firstly the role of Transport Scotland following the May 2007 election and secondly some general changes to governance in late 2007.

9.22.2 The role of Transport Scotland changed following the withdrawal of Transport Scotland. However despite the reduced role of Transport Scotland there remained oversight in respect of funding issues and progress of the works as evidenced by Ministers' involvement in the Princes Street dispute and Mar Hall.

9.22.3 The joint report to the Council on 20th December 2007 by Andrew Holmes and Donald McGougan sought new governance arrangements as shown in appendix 1 of the report⁶⁵⁷. The report identifies that the TPB would be formally constituted as a committee of TEL. Tom Aitchison notes in his statement that the operating agreement was amended before May 2008 so that it reflected that the TPB was noted as deciding on matters affecting the scope, cost and programme of the Project⁶⁵⁸.

9.22.4 The general changes are identified in the evidence of Tom Aitchison who explained that:

“In December 2007 the Council delegated general authority to the TPB for the tram project, working through TIE and TEL. The TPB formally reported to TEL”⁶⁵⁹.

9.22.5 The purpose was to reflect that the TPB was not a legal entity in its own right, and had no delegated authority prior to 2007.

9.22.6 It is submitted that the governance arrangements in 2007 merely formalised matters. Accordingly the absence of formally delegated powers did not prevent the TPB fulfilling its role.

9.23 2009

⁶⁵⁷ CEC02083448

⁶⁵⁸ Witness statement of Tom Aitchison TRI00000022, page 106

⁶⁵⁹ Witness statement of Tom Aitchison TRI00000022, page105

- 9.23.1 Tom Aitchison recognises that by 2009-10 the rationale for TEL was increasingly coming into question and that Lothian Buses could have fulfilled the role of integrating public transport provision in the city⁶⁶⁰.
- 9.23.2 It is submitted that this was a reasonable view to take at that time as there was only one transport initiative continuing to be pursued by TIE, namely the Tram Project.
- 9.23.3 Jim Inch explains in his statement that in 2009 the Council had identified a need to secure an “*improved governance grip*” as desired by the IPG⁶⁶¹. A report to the Policy and Strategy Committee on Governance in September 2009 sought approval for the new governance and operating arrangements⁶⁶².
- 9.23.4 In 2009 the main responsibilities of the Council, TIE and TEL were set out in the Memorandum of Understanding⁶⁶³. At that time TEL took on the ownership of TIE⁶⁶⁴.
- 9.23.5 Tom Aitchison also identifies that in December 2007 the Council delegated general authority to TPB for the Tram Project. The TPB formally reported to TEL⁶⁶⁵. The delegated authority recognised the fact that unlike TIE and TEL the TPB had no legal status, as noted above.

⁶⁶⁰ Witness statement of Tom Aitchison TRI00000022, page 108

⁶⁶¹ Witness statement of Jim Inch TRI00000049, page 89

⁶⁶² CEC00680472

⁶⁶³ CEC00690440

⁶⁶⁴ Witness statement of Kenneth Hogg TRI00000045, page 21

⁶⁶⁵ Witness statement of Tom Aitchison TRI00000022, page 105

In the joint report⁶⁶⁶ to Council on 20th December 2007 the authority was approved.

Role and Governance of TIE after 2009

- 9.24 As indicated above after 2009 TIE sat under TEL, although they remained two separate companies. From 2009 the TEL board further comprised the non-executive directors of TIE⁶⁶⁷.
- 9.25 As a result of the governance changes TIE reported to TEL, which in turn reported to the Council.
- 9.26 In the Council's submission, the distinction between TIE, TEL, and the TPB are, to an extent, artificial as the various personnel involved in the decision making and attendance at board meetings often were the same individuals and also included senior officers and members of the Council, as discussed below. The improvement and refinement of the arrangements did not have a material bearing on the governance other than to formalise matters.

The Effectiveness of the Governance Systems, the effectiveness of TIE as Project Managers and the reasons for failure in relation to these matters

9.27 General

- 9.27.1 The Council notes that the Inquiry seeks views on (1) the effectiveness of the governance systems; (2) the effectiveness of TIE as project

⁶⁶⁶ CEC01083448

⁶⁶⁷ Witness statement of Kenneth Hogg TRI00000045, page 13

managers; and (3) the reasons for failure in respect of (1) and (2). Before addressing the evidence relevant to these issues the Council wishes to make two general submissions. Firstly, the Council submits that whilst the governance was certainly not perfect that the governance was not the principal cause of any delay; cost overrun and/or reduced scope of the Project. Secondly, the changes to governance during 2007 and 2009 were not sufficiently significant that the earlier arrangements could be said to have caused the delays and cost overruns; or prevented the delays and cost overruns. Improvements to the governance arrangements during 2009 were of assistance but even if they had been completely appropriate and well functioning, they would not have provided a wholesale remedy to the deficiencies.

9.28 The effectiveness of governance systems and the reasons (if any) for any failures

9.28.1 Under this sub-chapter of submissions the Council candidly accepts that the governance arrangements were not a model of clarity but nonetheless were sufficiently effective.

9.28.2 Kenneth Hogg held non-executive directorships in TIE and TEL, had attended 45 of the 53 TIE board meetings and accordingly, it is submitted, had an informed view of the governance and reporting arrangements. In his evidence Mr Hogg explained the different functions of the bodies, explaining that TIE had overall responsibility for operational execution, whereas the TPB was concerned with operational execution Mr Hogg also reminded the Inquiry that the TPB

was a committee of TEL⁶⁶⁸. The Council recognises that there was a large element of cross membership of personnel on the various boards. Mr Hogg's view is that governance was effective and that cross membership of the bodies was beneficial⁶⁶⁹. Mr Hogg explained that meetings of the bodies took place on the same day in order that all relevant issues could be considered with all the relevant people available, describing the practice as "*sensible*"⁶⁷⁰. In this respect Mr Hogg's evidence is supported by Graham Bissett's evidence. Mr Bissett also reinforced that joint meetings took place to avoid duplication⁶⁷¹. Mr Bissett explains that the relationship between the bodies worked better than might appear on paper and that the responsibilities were clear to those involved⁶⁷².

9.28.3 Stewart McGarrity is of the opinion that:

*"...the project governance worked reasonably well throughout. I believed it was effective-but could be improved by reducing or focussing the number of reporting points..."*⁶⁷³.

9.28.4 The Council relies not only on the evidence of those witnesses but on independent review by external bodies such Deloitte in its review of the arrangements.

⁶⁶⁸ Transcript of oral evidence of Kenneth Hogg 13 December 2017, pages 55:22 to 56:23

⁶⁶⁹ Witness statement of Kenneth Hogg TRI00000045, page 5

⁶⁷⁰ Witness statement of Kenneth Hogg TRI00000045, page 14

⁶⁷¹ Transcript of oral evidence of Graeme Bissett 31 October 2017, page 119:14- 22

⁶⁷² Transcript of oral evidence of Graeme Bissett 31 October 2017, page 90:18- 19 and page 92:13- 22

⁶⁷³ Witness statement of Stewart McGarrity TRI00000059, page 318

9.28.5 Mr Richards described the relationship between the bodies as collaborative.

9.28.6 In the Council's submission any suggestion that all the bodies were required for effective governance is unlikely to be particularly convincing. The witnesses' reliance on cross-membership and back to back meetings does not assist justification. However the structure of governance did not cause the delay, or the cost overrun. In the Council's submission it cannot be reasonably shown that a single decision making body would have prevented the Pricing Assumptions to being agreed to, or indeed have ensured that any delays were not encountered.

9.28.7 It may be suggested that the governance was capable of being complicated, caused duplication/repetition in the decision making process and that there existed a lack of clarity as to the body responsible for decision making. Even if that were true those matters did not directly cause delay, cost overrun or otherwise had an effect on the extent of the route(s).

9.28.8 Complexity of itself does not lead to an absence of decision making. The cross membership of the groups and evidence of duplication of functions does not support any suggestion that decisions were not being made as required or that the decisions taken were bad decisions due to complex governance. In other words a poor decision may have been reached regardless. The important issue is whether or not critical decisions were being made. The Council submits that there was no

line of evidence that critical decisions were being overlooked or otherwise not being made due to the existence of the three different groups with cross group membership. The evidence also does not support a conclusion that the wrong decisions were being made by virtue of the existence of the three bodies. This logic is supported by the fact that the same persons would be making the decisions, where cross-membership existed. Duplication or repetition of decision making is undesirable as it may lead to irreconcilable or inconsistent decision making. In practice the cross membership acted as a safeguard to prevent such an occurrence.

9.29 The effectiveness of TIE as project managers and the reasons (if any) for any failures

9.29.1 In the Council's submission there are two separate issues. Firstly, the effectiveness of structure of the arrangement for delivering the Project, namely through TIE. Secondly, the experience and personnel within TIE.

9.29.2 There was a recognition by witnesses that TIE may have benefited from being a smaller and leaner organisation relying on external assistance. Willie Gallagher was of the opinion that a separate company was required to recruit the best staff but qualified his opinion in stating:

"...having a smaller delivery vehicle would have made more sense. I think if I was taking this thing forward again I would have had a small lean contractual delivery vehicle and I would contract the whole thing to

*private sector ...I wouldn't try and build up an organisation the size of TIE*⁶⁷⁴.

9.29.3 Alan Robertson, formerly of Alfred McAlpine, stated that a smaller, tighter knit organisation, rather than a client organisation would have been a far better way to deliver the Project. Mr Robertson explained that a bespoke organisation without past experience was a challenge from day one⁶⁷⁵. Mr Robertson stated:

*"TIE could have been a thin client rather than a thick client. Maybe TIE should have had no more than 20 people as opposed to, possibly, 200/300. Those 20 people would have then interfaced with a project management organisation..."*⁶⁷⁶.

9.29.4 Tony Glazebrook was of a similar view that the size of TIE was an issue as his opinion was that *"...the TIE organisation grew and became confused"*⁶⁷⁷.

9.29.5 Dave Anderson was of the view that:

*"it would have been much better (in the case of the Edinburgh Tram) to procure such support through a multi-disciplinary transport engineering company with an established track record and subject matter knowledge"*⁶⁷⁸.

⁶⁷⁴ Witness statement of Willie Gallagher TRI00000037, page 20

⁶⁷⁵ Witness statement of Alan Robertson TRI00000070, page 4

⁶⁷⁶ Witness statement of Alan Robertson TRI00000070, page 5

⁶⁷⁷ Witness statement of Tony Glazebrook TRI00000039, page 3

⁶⁷⁸ Witness statement of David Anderson TRI00000108, page 115

- 9.29.6 Accordingly the Council recognises that a smaller team outsourcing the work may have been a more suitable structure to deliver the Project. However this recognition is made in hindsight and it was not suggested, to the knowledge of the Council, that there was a body of resistance to the establishment of TIE.
- 9.29.7 The second issue is the experience within TIE. The construction industry was enjoying a period of growth prior to 2008 and accordingly construction professionals, including engineers were in particular demand. The evidence of Rebecca Andrew was that TIE had people with experience of procurement and “*perhaps the project management side*” but did not have the necessary operational experience⁶⁷⁹.
- 9.29.8 Mr Howell, the Chief Executive of TIE until 2006, recognised, and was surprised, by the lack of civil engineering experience⁶⁸⁰.
- 9.29.9 The lack of experience was recognised by Tom Aitchison in his evidence⁶⁸¹ but he stated that TIE was responding to this by “*employing a wide range of fairly prestigious management consultants*”⁶⁸².
- 9.29.10 The Council recognises that there was a lack of experience of constructing trams within a city centre. However this reinforces the proposition that the Project could not have been delivered in-house. The Council relied on the expertise of TIE and regrettably it fell short of what was required to deliver the Project.

⁶⁷⁹ Transcript of oral evidence of Rebecca Andrew 13 September 2017, page 63:2-16

⁶⁸⁰ Transcript of oral evidence of Michael Howell 26 September 2017, page 20:6- 10

⁶⁸¹ Transcript of oral evidence of Tom Aitchison 28 November 2017, page 34:13- 20

⁶⁸² Transcript of oral evidence of Tom Aitchison 28 November 2017, page 35:1-2

The Adequacy of Reporting

9.30 Information

9.30.1 The Council submits that the reporting for which it was responsible was adequate, namely the reporting to Council. In this respect the Council was largely satisfied with the sufficiency of the information being received or fed back from TIE and the boards above.

9.30.2 Mr Aitchison as former Chief Executive of the Council provided evidence was that he regularly briefed the Council leader⁶⁸³ and members were briefed on “...*significant developments and problems arising*”⁶⁸⁴. The frequency of the briefings would vary but could be as regular as weekly with the Council Leader. When the Council was seeking to resolve the dispute between TIE and Infracore the frequency of briefings increased. Mr Aitchison recognised that:

*“The need for commercial confidentiality and how to balance this against public reporting requirements was a constant problem. Reporting in public on details such as revised cost estimates being prepared by TIE or on legal advice which TIE was in receipt of, would have put TIE at a clear commercial disadvantage in its dealings with BBS”*⁶⁸⁵.

9.30.3 For these reasons a data room was established to ensure a balance was achieved between confidentiality and reporting to the political membership.

⁶⁸³ Witness statement of Tom Aitchison TRI00000022, page 102

⁶⁸⁴ Witness statement of Tom Aitchison TRI00000022, page 22

⁶⁸⁵ Witness statement of Tom Aitchison TRI00000022, page 103

- 9.30.4 Mr Holmes' evidence identifies that members were advised of development through a variety of measures including reports, weekly briefings, and presentations⁶⁸⁶.
- 9.30.5 In the submissions by SETE at Chapter 1(b) two issues arise which require clarification. First the implication that Council officers were intentionally concealing information from members. Secondly that the reporting by TIE improved later in the Contract.
- 9.30.6 The information to members requires to be considered in light of the following: (1) councillors were represented on the various governance bodies; (2) the Council was updating key councillors on developments and updating all councillors on significant developments and problems which arose⁶⁸⁷. Commercial confidentiality remained a problem and Mr Aitchison identified that more information was available to members in private briefings than made publically⁶⁸⁸. In their submissions SETE appear to imply that TIE was providing critical information which was not being relayed to Councillors. In the Council's submission this is simply not the case. There is ample witness evidence in respect of TIE failing to provide a full and frank disclosure of all relevant information, particularly during the period 2008 to 2010. This is consistent with the evidence of Bilfinger witnesses who were concerned that TIE was not properly informing the Council of matters relating to the Contract⁶⁸⁹. Separately Siemens also makes the submission that TIE failed to

⁶⁸⁶ Witness statement of Andrew Holmes TRI00000046, page 113

⁶⁸⁷ Witness statement of Tom Aitchison TRI00000022, page 102

⁶⁸⁸ witness statement of Tom Aitchison TRI00000022, page 103

⁶⁸⁹ Paragraph 133 at page 69 in the written submissions of Bilfinger dated 27 April 2018

provide stakeholders, such as the Council, with objective financial assessment to enable good decision making⁶⁹⁰ (Siemens' submissions at paragraph 17 on page 11). Siemens further reinforces its concerns that Tie were not reporting costs to the Council (Siemens' submissions at paragraph 330 on page 121). It is not clear what would have been achieved, or more significantly what may have been avoided, by senior Council officers relaying every memo or email containing information to all Councillors. For example on page 15 of the SETE Submissions there is apparent criticism of Councillors not being provided with a copy of the Contract. It is far from clear what would have been achieved, or what SETE assert would have been achieved, by making the Contract public. The Contract was available within the data room. The fundamental issues are (1) whether there was a failure to report relevant information by Council officers; (2) whether any alleged failure to report all relevant information was with the intent to mislead the Councillors, and (3) regardless of any such intent whether any failure caused or contributed to the delays and cost overruns. It is submitted that Council officers did not fail to report relevant information, that there was no intent to mislead and that in any event any failures did not cause delays or cost overruns.

9.30.7 The second matter arising from this Chapter of the SETE submissions is the assertion that the reporting by TIE improved after Willie Gallagher was replaced. Whilst this is a comparative assertion the Council is mindful of the manner and language by which the Adjudication results

⁶⁹⁰ Paragraph 17 on page 11 of the written submissions of Siemens dated 27 April 2018

were presented by TIE and Mr Hamill's "pockled" email. Accordingly whilst the Council's principal submissions do not detail all criticisms made of TIE's reporting the Council does not agree with the suggestion that the reporting by TIE improved as the Contract progressed.

10. **Scottish General Election (May 2007) and decision of Transport Scotland to change role**

10.1 The Scottish Parliament elections were held in May 2007. The SNP formed a minority administration. Cancellation of the Project formed part of the SNP manifesto⁶⁹¹.

10.2 On 27th June 2007 a parliamentary motion was passed in the following terms:

“The Parliament notes that the Edinburgh trams project and EARL were approved by the Parliament after detailed scrutiny; further notes the report of the Auditor General for Scotland on these projects and in light thereof, (a) calls on the Scottish Government to proceed with the Edinburgh trams project, within the budget limit set by the previous administration, noting it is the responsibility of Transport Initiatives Edinburgh and the City of Edinburgh Council to meet the balance of the funding costs”⁶⁹².

10.3 Transport Scotland subsequently withdrew from the Project and was no longer represented on the TPB.

10.4 Ainslie McLaughlin represented Scottish Ministers and Transport Scotland in the negotiation of the dispute(s) between the parties at the Mediation and was one of the 3 main negotiators⁶⁹³.

⁶⁹¹ Witness statement of John Swinney TRI00000149, page 2

⁶⁹² Witness statement of Stewart Stevenson TRI00000142, pages 2-3

⁶⁹³ Transcript of oral evidence of Ainslie McLaughlin 26 September 2017, page 176:7- 20

11. **SDS**

Summary

- 11.1 The SDS contract was entered into in September 2005. It contained a scheduled programme for development of the preliminary and then detailed design. For a variety of reasons that programme was not adhered to such that the detailed design was not complete by the time the Infraco contract was entered into as had been envisaged by the procurement strategy.
- 11.2 The detailed design was delayed in part by the time it took to obtain approvals and consent for both the utilities diversions and the construction design. This matter was complicated by the number of parties involved in the process and a lack of co-ordination and leadership.
- 11.3 The Council required to consider the consents and approvals processes in line with its statutory duties but accepts that it could have helped manage the consents and approval process more efficiently especially if it had been advised of the consequences of the delay in obtaining consents would have on the overall programme.
- 11.4 The failure to progress the detailed design to completion by December 2007 was one of the factors that led to the situation where the potential for change had to be properly considered and provided for in the Infraco contract.

Award of design contract

11.5 The “Draft Interim Outline Business Case”⁶⁹⁴ produced by TIE on 30 May 2005 noted *inter alia* that the letting of an SDS Contract early in the tender process was a key element in delivering TIE’s objectives and that TIE’s intention was to have a “*well advanced*” design by the time that bids were sought from the private sector for the vehicles and infrastructure. The SDS contract would be novated to the Infraco “*which will thereby take responsibility for the design obligations of the SDS*”. It was noted that TIE’s approach would result in “*all design risk being transferred to the private sector*” and reduce the overall risk to the Project. TIE would have “hold and review” points at each of the three main stages of design. An early conceptual design had already largely been completed by TIE.

11.6 It was envisaged that the initial task for the SDS provider would be to carry out the preliminary stage of design, with a completion target for the entire network of mid-2006. There would be a requirement for detailed design to have been completed on the sections where there were the most significant challenges, either technical or aesthetic. TIE had categorised the system into sections by criticality of the obtaining of planning consents e.g. the section from Haymarket to St Andrew Square was in the most critical category. At the forecast date of Royal Assent, around 25% of the detailed design for the entire network would have been completed, including a specific design for the significant utilities diversions (*i.e.* those which were currently intended to be under the track slab). Between Royal Assent and signing the Infraco contract

⁶⁹⁴ CEC01875336

the SDS provider would complete the process of designing the utilities diversions, further refine the design and provide input into the tender process to confirm design and pricing by the Infraco. Initially, tenderers would be provided with the preliminary design plus detailed design as available for critical areas. Design would continue while tenders were being evaluated and the bidders would receive a significant design update to price their Best and Final Offers.

- 11.7 It was anticipated that planning permissions for the core elements of the scheme (namely, Haymarket to St Andrew Square) would have been achieved by the time of signing the Infraco contract. The overall design process would take between 2 and 2.5 years and it was expected that *“the design work will be around 60-70% complete when the Infraco Contract is signed”*⁶⁹⁵.
- 11.8 It was anticipated that design and related activities would commence in June 2005, tenders for the infrastructure and tram vehicles contracts would be issued in April 2006, the Final Business Case would be delivered in September 2006, the infrastructure contract would be awarded in June 2007 and that trams would be operational by the end of 2009. That was recognised to be a *“challenging timescale”* which would require to be kept constantly under review.
- 11.9 Under “Other Survey Work”, it was noted that TIE had established a schedule of advanced works which would support/assist the SDS provider. It was noted that *“As part of the development of the utilities*

⁶⁹⁵ CEC01875336, paragraph 5.7.1

diversion and design relating to the overall scheme, tie plans to carry out extensive advance survey work ranging from ground penetrating radar, open cut ground investigations, structural surveys, topographical surveys and other surveys to help establish information needed to aid detailed design, such as virtual walk through surveys ... Some of these surveys will be carried out by the TSS Contractor but the majority will be within the scope of the SDS Contract”.

11.10 It was noted that a significant benefit arising from undertaking design early was that TIE could procure utility diversions early, *“thereby reducing programming and cost risk pricing by the infrastructure providers, and creating the best opportunity to minimise and maximise construction productivity”*. The majority of utilities work was scheduled for early 2006, which would *“result in significant utilities diversion works being completed prior to commencement of tram infrastructure works so potential conflicts between the utilities and infrastructure works will be minimised”*. It was intended to let the utilities contract towards the end of 2005, assuming the SDS provider had made sufficient progress with the design.

11.11 On 19 September 2005 TIE appointed Parsons Brinckerhoff Ltd (“PB”) under a System Design Services (SDS) agreement⁶⁹⁶ to provide design services for the Project. There were 3 main design phases (1) a Requirements Definition phase, (2) a Preliminary Design phase and (3) a Detailed Design phase.

⁶⁹⁶ CEC00839054

- 11.12 None of the witnesses from Parsons Brinckerhoff knew why there had been a delay in the award of the contract but the delay resulted in there being a rush to complete the Requirement Definition Phase by Christmas 2005⁶⁹⁷.
- 11.13 Michael Howell's recollection was that PB was awarded the contract on the basis that it was able to commit to meeting the schedule for the Infraco contract⁶⁹⁸. Trudi Craggs thought that the SDS contract may in fact have been let too early because it was entered into before the completion of Parliamentary approval and sign off in March/April 2006 and that could have led to changes in the tram route which would have to be reflected in the design and there would be limited work that could be done before the route was finalised⁶⁹⁹.

Scope of Services

- 11.14 SDS was required to produce a design that did not specifically reference specific manufacturer's components as these were being selected and procured by the contractor. In the case of the tram-stop shelter, SDS required to deliver a design for the tram-stops that showed generic tram-stop shelters that met the requirements of the Council, it had to be of a glass form and be of a particular size etc, but SDS did not select the specific shelter manufacture. SDS designed a generic track type that showed the broad shape of what it would look like and

⁶⁹⁷ Witness statement of Jason Chandler TRI00000027, page 10

⁶⁹⁸ Witness statement of Michael Howells TRI00000129, page 32, paragraph 98

⁶⁹⁹ Transcript of oral evidence of Trudi Craggs 6 October 2017, pages 130:3 to 132:25

the form that it needed to be, but the actual component selection for that track form was the contractors' responsibility⁷⁰⁰.

11.15 In relation to post-novation design, the contractor was to appoint and confirm the components that were being installed. The contractor was then to complete the design. There were various conditions around the approval of design. When SDS delivered the design up to the point of novation, the council approved the design with certain conditions attached which were to be resolved once the particular component selection had been completed. To overcome these conditions the contractor had to confirm what those particular components were.

11.16 SDS was to develop a detailed design for the entire infrastructure except the tram, the communications system and the power supply system, as these were dependent upon the particular component selection by the contractors. The Infraco consortium completed some of the track form design, so it added the detailed components to the track form design. Its systems design, the likes of the telecoms, Siemens completed based upon its component selection. It took certain key elements of the design that were very bespoke to its offer and completed those, SDS completed the more generic civil design. SDS was to support Infraco post-novation with the completion of the design, and support them to discharge outstanding approvals conditions.

11.17 The SDS agreement included a programme for producing the design⁷⁰¹. Preliminary Design for the "sectors" comprising phase 1a of the Project

⁷⁰⁰ Witness statement of Jason Chandler TRI0000027, page 8

(Edinburgh Airport to Ocean Terminal) would be approved by dates ranging from 30 November 2005 and 28 February 2006, with Detailed Design for these sectors to be approved by dates ranging between 30 March 2006 and 30 September 2006.

11.18 Clause 7.1. of the SDS Agreement "Progress" stated that "*The SDS provider shall progress the services with expedition ... to achieve timeous completion of the services ... and its other obligations under this agreement in accordance with the master project programme ...*" The master Programme was supposed to be updated from time to time but there was some confusion over whether or not this actually happened.

11.19 Trudi Craggs was concerned that there appeared to be no contractual penalty or remedy for missing a deadline other than to terminate the contract for breach of contract. That was not realistic. She thought "*SDS were churning out their programme month on month but did not adhere to it; and tie had their overarching procurement programme which they were bashing on with regardless of deadlines being missed, and it was not all being drawn together*"^{701A}. In addition there was no way of easily tracking slippage. The fact there was no penalty other than termination meant there was not really a stick to hit the contractor with. Andrew

⁷⁰¹ CEC00839054 SDS agreement (i) clause 7 (pages 30-31), (ii) Schedule 1, Appendix 2, "Programme Phasing Structure" (pages 111-112) and (iii) Schedule 4, "Programme" (at page 248 onwards)

^{701A} Transcript of oral evidence of Trudi Craggs 6 October 2017, page 128:16 – 20

Harper also had concerns about the lack of remedies short of termination available in the contract⁷⁰².

11.20 In terms of the contract TIE only had 20 business days within which to make comments on the preliminary design. The SDS preliminary design was submitted on 30 June 2006. No formal response comments were received from TIE by 28 July 2006. PB noted that *"any late review comments which result in the reworking of documentation will have a disruptive effect on the delivery of our main programmed works."*⁷⁰³

11.21 Clause 5.1 of the SDS Contract stated under "Consents", stated that: *"The SDS provider shall (at its own cost and expense): obtain and maintain in effect all consents which may be required for the construction ... of the Edinburgh tram network as is consistent with, required by or contained within the services. Clause 4.8 provided: "If it should be found that the deliverables do not fulfil the requirements of this agreement or the needs of any approval bodies, the SDS provider shall at its own expense amend the deliverable." 2.6.2.1 provided that: "The SDS provider shall ... produce the detailed design of the Edinburgh tram network ... such that the detailed design has full approval of the client and the relevant approval bodies."*⁷⁰⁴ TIE thought that the SDS Agreement placed the responsibility for designing utilities diversions and obtaining the necessary consents and approvals for them. This became controversial when the consents and approvals became more difficult to obtain than had been anticipated. Steve

⁷⁰² Witness statement of Andrew Harper TRI00000043, page 19, paragraph 564 to 65

⁷⁰³ CEC01794964

⁷⁰⁴ Transcript of oral evidence of Steve Reynolds 12 October 2017, pages 2:24 to 3:15

Reynolds of PB's position was that Paragraph 3.2 of Schedule 1 of SDS Contract was key to understanding SDS' obligations in relation to utilities and that PB was responsible for critical design but not for all utilities design⁷⁰⁵. He claimed TIE lacked understanding about the contract and that TIE was responsible for putting in place agreements with the statutory undertakers, whereas TIE seemed to consider that it could ask PB to do anything necessary to obtain an approval or consent.

Progress to December 2007, difficulties encountered, the reasons for these difficulties and remedial measures attempted

- 11.22 The Requirements Definition phase was carried out between September and December 2005. There were, however, difficulties and delays in progressing the Preliminary Design and Detailed Design according to the timescale set out in the original design programme.
- 11.23 In particular, a Preliminary Design package was issued by the SDS provider to TIE on 30 June 2006 but not agreed and the Detailed Design remained incomplete both at the end of 2007 and when the Infracore contract was entered into in May 2008.
- 11.24 Several witnesses said they thought PB initially failed to devote adequate resources to the Project and underperformed during the

⁷⁰⁵ Witness statement of Steve Reynolds TRI00000068, pages 13 to 14

course of the contract⁷⁰⁶. One of the concerns was whether the contractor would accept novation of the SDS contract⁷⁰⁷.

11.25 When PB submitted the Preliminary Design for the Project in June 2006. The Council was not very pleased with the preliminary design. The level of comments was so extensive that they could be accommodated in the review form procedure that had been envisaged and they were not submitted within the 20 days allowed for in the contract. A design approval panels was then tasked with the evolution of preliminary design 1, as it was then called, to preliminary design 2 (“PD2”), which allowed parties to discuss the design, add in their comments, and SDS to have another iteration in effect of the preliminary design⁷⁰⁸. The design approval panels got all the key stakeholders round the table to discuss their concerns with the preliminary design, and Council employees were also co-located within the TIE offices to improve communication and co-operation.

11.26 In the second half of 2006 “charrette” meetings were attended by SDS, TIE and the Council to try to ascertain the Council's preferences in relation to some key areas such as St Andrew Square and Picardy Place where public realm works were also planned and there were numerous options that required to be considered. Some witnesses expressed the view that one of the difficulties in obtaining approvals was that the approvals’ process contained an element of subjectivity in

⁷⁰⁶ E.g. witness statement of Michael Howell TRI00000129, page 34, paragraph 104; witness statement of Andrew Harper TRI000000043, page 15, paragraphs 52, 60

⁷⁰⁷ Witness statement of Andrew Harper TRI000000043, page 15, paragraphs 53 and 58

⁷⁰⁸ Transcript of oral evidence of Trudi Craggs 6 October 2017, page 137:20- 25

relation to the effect of a proposal in terms for example of its aesthetic value as opposed to its technical efficiency and designs that would work technically were sometimes not approved on the basis of aesthetics. Some witnesses thought that the charrette meetings contributed to the delay and complexity but Andrew Harper and others saw their value⁷⁰⁹.

11.27 There was also a lack of appreciation on the part of SDS that the Council acts in a number of different capacities such as roads authority and planning authority and it could not grant approvals or planning permissions just because it was the client in a project such as the tram. Trudi Craggs thought there was a failure both on the side of SDS and the Council to engage in relation to these matters earlier⁷¹⁰. To try to address, this weekly meetings were set up between TIE and the Council to discuss SDS design issues⁷¹¹.

11.28 The Council takes some responsibility for the delay that the difficulty in reaching decisions might have caused. On the other hand it is not clear what the significance of those decisions in terms of additional work caused given the general delay in producing acceptable designs. It is submitted that it was not properly appreciated the consequences of the changes in design might be causing because that was not properly appreciated by SDS or TIE and were properly reported to the Council by TIE or SDS.

⁷⁰⁹ Witness statement of Andrew Harper TRI00000043, page 21, paragraph 72

⁷¹⁰ Transcript of oral evidence of Trudi Craggs 6 October 2017, page 147:11- 13

⁷¹¹ Witness statement of Andrew Harper TRI00000043, page 20 paragraphs 68 to 70

- 11.29 This difficulty was also noted for example in the December 2006 Scott Wilson preliminary design review report⁷¹². It noted that *“the engineering aspects of the project seem generally to be on course with the structures a notable exception. These elements have been subject to recent interest and decisions are outstanding on certain design aspects. This is not something that SDS can be held wholly responsible for. Away from the hard engineering, a number of the softer issues would appear to be outstanding. It is clear that these will require to be addressed in early course given their impact throughout the project”*^{713A}. The report also suggested a qualified acceptance should be given to the preliminary design but noted that the design review process was in disarray^{713B}.
- 11.30 Another difficulty was the inter-relationship between the utilities diversion designs and the tram construction designs. Any changes in one would affect the other and sometimes statutory utilities companies would try to insist on a particular solution or on carrying out the works themselves even though the timing of that would not be related to the tram programme and may adversely affect it.
- 11.31 The Draft Final Business Case (dated November 2006)⁷¹³ noted, in relation to a discussion of the SDS contract that, *“The principal attributes of the procurement approach for this contract are: Scope – provision of design work up to detailed design stage including obtaining*

⁷¹² PBH00026782

⁷¹³ CEC01821403

^{713A} PBH00026782 page 5

^{713B} PBH00026782 page 7

all necessary approvals^{713C} ... *“It is expected that the overall design work to Detailed Design will be 100% complete when the Infraco contract is signed. However by identifying key risk areas and prioritising SDS activities, tie is seeking to complete the key elements of the Detailed Design prior to selecting the successful Infraco bidder in summer 2007. This will enable Infraco bidders to firm up their bids based on the emerging Detailed Design and thereby reduce the scope and design risk allowances that they would otherwise include*^{713D}; and *“The novation risk is mitigated by: Detailed design being largely completed prior to award of the Infraco contract*⁷¹⁴. A discussion on the procurement process to financial close noted, *“Due diligence by Infraco on key elements of the SDS detailed designs*⁷¹⁵. In relation to consents and approvals it was noted, *“Responsibility for the preparation and application for most necessary consents and approvals has been passed to the SDS provider and this risk will pass to the Infraco at the point of novation*⁷¹⁶. The Draft FBC also noted *“The programme is based on the assumption of ‘right first time and on-time’ delivery of activities with very little float within the programme ... The criticality of much of the design activities mean the need for on-time delivery is particularly true for SDS design work and the project team are currently actively pursuing improved performance in this area and critically reviewing these elements of the programme*⁷¹⁷.

^{713C} CEC01821403 paragraph 7.30

^{713D} CEC01821403 paragraph 7.53

⁷¹⁴ CEC01821403, paragraph 7.61

⁷¹⁵ CEC01821403, paragraph 7.118

⁷¹⁶ CEC01821403, paragraph 1.84

⁷¹⁷ CEC01821403, paragraph 11.3

- 11.32 The Project SDS contract report to 15 December 2006 noted that only 28.3% of the detailed design had been completed when 71.9% had been scheduled to have been completed⁷¹⁸. As at February 2007 there was a five month delay in the programme.
- 11.33 Another concern was that the Employer's Requirements, SDS and MUDFA contracts were misaligned. SDS was developing a design for the system and TIE was developing the Employer's Requirements which was sent to bidders to price against. The concept was that the SDS design was going to be novated to the contractor; if the Employer's Requirements and the design were not aligned the contractor would have two designs and would have a claim against TIE to make them align⁷¹⁹.
- 11.34 Part of the problem was that the Employer's Requirements were based on the preliminary design in late 2006 and were issued to the Infracore bidders; but at the same time as that procurement process was taking place, SDS was advancing and changing the design from the preliminary design. So there were two processes taking place, the SDS progression of its design and then the procurement exercise with the discussions and changes between the TIE procurement team and the Infracore bidders.
- 11.35 Attempts were made during 2007 to try to address this problem but it still remained in December 2007 and persisted into 2008 and there was

⁷¹⁸ TIE000040947

⁷¹⁹ E.g. Transcript of oral evidence of Jim Harries 6 October 2017, pages 5:23 to 6:4

a suggestion that TIE was changing the Employer's Requirements to accommodate the BBS offer as opposed to the design developed by SDS.

11.36 Richard Walker had some serious concerns over the standard of drawing information provided. This was an issue due to the information being lacking and incomplete, and the scope continually altering. These matters were never fully resolved. He said he thought the design around that time of contract negotiations was abysmal⁷²⁰. In late November 2007 BBS was provided with various discs containing the design as at that time. The design was changing so rapidly that BBS insisted on drawing a line in the sand that we could price against. This is what its price was based upon and in Richard Walker's opinion the detailed design was approximately 40% complete at this time,

11.37 From the PB perspective Alan Dolan identified the main problems as being difficulties with statutory utilities diversion designs because of the failure to secure timely agreement with third parties on designs and failure to secure timely agreement with statutory authorities for utility diversions⁷²¹. That was added to by an overwhelmed Client Team with little experience of Tram/LRT systems design leading to silo working of different fractions of a Client-base working against each other. HE also criticised TIE's management of the "Critical Issue" RFI clearances being afforded to the Tram Designer in order to achieve co-ordinated design completion.

⁷²⁰ Witness statement of Richard Walker TRI00000072, pages 7 to 8; CEC01625845

⁷²¹ Witness statement of Alan Dolan TRI00000101, pages 2 to 3

- 11.38 He also identified the problems caused by outside influences seeking changes to the design and the confusion and delay caused by informal and conflicting instructions from different parties within the Client Team. He felt there was a lack of understanding of Tram/LRT Systems issues by the majority of the Client Teams Officers and no ability on the part of TIE to provide a robust programme management/delivery plan which led to misaligned expectations by the TIE management team of the requirements for the designer.
- 11.39 He thought that SDS did not need TIE help or assistance in order to perform the SDS contract obligations but did need TIE to carry out the needed timely provision of information, communication and proper management, particularly of stakeholder interests and any change in requirements. However TIE was actually unable to manage the changing scene of design landscape outside the SDS contracted works. For example the number of charrettes called during the design period indicated that TIE as the client was not in control of the product that was being sought.
- 11.40 Overall the Failure to engage the statutory utility approval bodies early enough in order to assist TIE and SDS in technical discussions was damaging and the inability of TIE to secure the timely completion of Third Party Agreements and SU Approval body Agreements delayed the design process and prevented the Designer being able to carry out his obligations to prepare and deliver timely (correct to programme) contracted submissions. In May 2007 Parsons Brinckerhoff made a

claim against TIE for additional costs which was partly based on a failure on the part of TIE to update the master programme.

11.41 Alan Dolan accepted that matters were improved to an extent when TIE brought in a team to act on the lessons learned review exercise conducted by David Crawley in January 2007. The formation of an outstanding "Critical Issues List" and weekly or two weekly hit list against the Critical Issues until the blockage of "design holds" on the Project were opened up for the Designer to be able to prepare the Tram Infrastructure Design also helped.

11.42 Several witnesses recalled that David Crawley was brought in in January 2007 and conducted a review of the SDS design review process⁷²². He was brought into the Project by TIE and carried out a review to understand and identify issues with design progress. The issues he identified were poor leadership and a lack of working as a team.

11.43 A point raised by Jim Harries was that the discipline of change control should be enforced by which he meant that if something came along that causes a change to the design to be necessary it is vital that all of the consequences of the proposed change are understood before the change is agreed but there was at the time a lack of understanding of change both technically, commercially and in terms of programme and without the discipline of a proper process to assess change the risk was

⁷²² E.g. Transcript of oral evidence of Jim Harries 6 October 2017, page 1:13- 17

that the changes would not be for the better overall⁷²³. At the time there were too many people within the Council and different parts of TIE suggesting changes without understanding the full picture. In some instances there was not a common view on the proposed changes because people were working in “silos” and generally the organisation was not properly joined-up. TIE had a project delivery team, an engineering team, an approvals team and the teams did not always work well together⁷²⁴.

11.44 SDS Design programme continued to suffer slippage month on month, and it was readily identifiable that there was slippage greater than the elapsed days since the last provided programme⁷²⁵. David Crawley thought an estimate by BBS in its design due diligence report dated 18 February 2008⁷²⁶, that SDS design was still about 40% incomplete by December 2007 would be correct, as would a record that the latest available SDS programme version 23 indicated a slippage of more than a year compared to the programme in the SDS agreement and it scheduled the release of construction information from April 2008 to the end of 2008 based on an optimistic estimate of approval periods.⁷²⁷

Conclusions

11.45 It is clear that the design did not progress as quickly as envisaged by the original procurement strategy. SDS and TIE blamed each other and to an extent the MUDFA contractor and the Council for this. It is

⁷²³ E.g. Transcript of oral evidence of Jim Harries 6 October 2017, page 4:1- 11

⁷²⁴ E.g. Transcript of oral evidence of Jim Harries 6 October 2017, page 5:5- 9

⁷²⁵ E.g. CEC01625056, CEC01625058, CEC01625057, CEC01626309, CEC01626310

⁷²⁶ DLA00006338

⁷²⁷ Transcript of oral evidence of David Crawley 4 October 2017, page 97:23 to 100:4

submitted that each party should accept some blame for the delay although it is also likely that some delay was inevitable given the tight timescale envisaged and the complexity of the process which was not fully understood at the time. The design process was complicated by the need to modify it as utilities and other unexpected obstructions were found on the route. It was also complicated by the lack of appreciation that one proposed change, for example by one statutory undertaker, would have repercussions on other statutory utilities companies.

11.46 In its written submissions of 27 April 2018, Parsons Brinckerhoff seeks to place a large part of the blame for the delay in the designs being provided by SDS at the door of the Council. It is submitted that that is unwarranted. Whilst the Council accepts that the process of obtaining consents and approvals from the Council was a concern, and one for which the Council is partly responsible due to the number of comments made and the iterative process that was entered into, it is submitted that the failings on the part of SDS and others were more of a contributory factor to the delay. SDS presented applications in an incomplete and piecemeal fashion and failed to take on board comments from the Council that were intended to assist⁷²⁸. SDS should have been aware that the Council in its quasi-judicial capacity as planning authority or roads authority had a statutory duty to consider the applications on their merits in accordance with the required standards and independently of its role as the ultimate client in the tram project⁷²⁹. SDS as an experienced designer should have been aware that a local authority

⁷²⁸ Witness statement of Duncan Fraser TRI00000096 pages 6-9

⁷²⁹ Witness statement of Duncan Fraser TRI00000096 pages 66-67

would be bound to act independently and conducted its processes accordingly, especially as it was contractually responsible for obtaining the necessary approvals. Duncan Fraser's evidence was that CEC had sufficient resources to process the submissions and the majority of them were dealt with and comments provided within the 8 week period agreed with TIE and SDS⁷³⁰ and that they worked hard to process the submissions and provide comments that were reasonable and intended to assist the designers⁷³¹. The Council's role was to approve the design not to do the design⁷³². It is accepted that as Mr Fraser said, there was great intent by all the parties to try and complete the process but it is a complex matter fitting tram infrastructure into a city road and accommodating the competing interests both from a technical and a planning perspective⁷³³.

11.47 Again the Council submits that it was not the strategy or content of the SDS Agreement that was at fault but the failure to implement it timeously. The design process was obviously well behind its target programme and the fundamental problem arose from the way in which the Infraco contract tried to provide for and deal with the situation in which there was known to be an incomplete design at the time the contract was entered into.

⁷³⁰ Witness statement of Duncan Fraser TRI000000096 pages 6

⁷³¹ Transcript of oral evidence of Duncan Fraser 12 September 2017 pages 192-195

⁷³² Transcript of oral evidence of Duncan Fraser 12 September 2017 page 196: 6-7

⁷³³ Transcript of oral evidence of Duncan Fraser 12 September 2017 199: 4-9

12. MUDFA

Summary

- 12.1 Diversion and protection of the utility plant along the route of the tram, in advance of construction of the tram infrastructure was the first stage of the Project. The objective of MUDFA was to appoint a contractor to act as a single point of responsibility for the utility diversion works to clear the route in advance of the Infracore works.
- 12.2 In October 2006, TIE appointed Alfred McAlpine Infrastructure Services Ltd to undertake the MUDFA works. The MUDFA contract was in two stages. The first stage was the pre-construction phase, and involved the MUDFA contractor working with TIE and SDS to refine the scope and the costs of the second stage, the construction stage.
- 12.3 The MUDFA contractors experienced many problems. There were various criticisms of the MUDFA contractor's performance by TIE and others. However the main difficulties were caused by the delay in the provision of designs for the works by SDS which in turn were partly as a result of not knowing what was actually under the ground and the difficulties in agreeing designs between all utility contractors and obtaining approvals for a proposed solution. The planned programme for the MUDFA works quickly and continually slipped backwards to the extent that it was apparent that it would not be completed before the Infracore works were scheduled to commence.

Award of contract and scope of services

- 12.4 On 21 September 2006, the approval of the Council was sought for TIE to enter into the Multi-Utilities Diversion Framework Agreement (MUDFA). A report was provided by the Director of City Development⁷³⁴. It was noted that the first stage in the construction and delivery of the Edinburgh Tram Network was the diversion and protection of the utility plant along the route of the tram, in advance of construction of the tram infrastructure. The objective of MUDFA was to appoint a contractor to act as a single point of responsibility for the utility diversion works in relation to the tram network (subject to utility companies reserving the right to carry out works associated with high pressure gas mains, high voltage power cables and certain telecoms cabling works due to the technical complexity and sensitivity of these works).
- 12.5 The MUDFA contract was in two stages. The first stage was the pre-construction phase, and involved the MUDFA contractor working with TIE and its consultants to refine the scope and the costs of the second stage, the construction stage. Once these costs had been refined they would be fed into the business case which would be submitted to the Council for approval.
- 12.6 It was noted that it was not possible to finalise the scope of the work prior to the tender process and that would not be finalised until the MUDFA contractor had been appointed and the deliverables set out in the pre-construction stage were fulfilled. It was estimated, however, that the total value of the contract would be in the order of £50m and that the pre-construction stage would be in the order of £1m.

⁷³⁴ CEC02083472

12.7 In October 2006 TIE appointed Alfred McAlpine Infrastructure Services Ltd (“AMIS”) to undertake the utilities diversion works under the MUDFA⁷³⁵. The Programme for the MUDFA works was set out in Schedule 8 of the MUDFA contract⁷³⁶. Certain pre-construction services were to be undertaken between October and December 2006 with MUDFA construction works being undertaken between 2 March 2007 and 27 June 2008.

Progress to December 2007, difficulties encountered, the reasons for these difficulties and remedial measures attempted

12.8 A report provided by TIE’s Construction Director to a meeting of TIE’s Utilities sub-Committee on 4 April 2007 noted that AMIS had issued a draft MUDFA programme revision 04 which showed the main MUDFA works starting on 2 July 2007 (which was three months later than the previous programme and was driven by “design and Work Order requirements”) and showed the main MUDFA works on phase 1a, from Newhaven to Edinburgh Airport, completing by early January 2009 (which was six months later than shown on the previous programme)⁷³⁷. It was noted that, *“It has been recognised that the issuing of Utilities design at Section level is slowing the process of SUC approvals down. It is the intention of TIE to re-sequence the delivery of Utilities design in line with the approved MUDFA revised schedule. Issue of drawings and SUC approvals will be in smaller batches which align to the MUDFA construction worksites”*.

⁷³⁵ CAR00000300

⁷³⁶ CAR00005833

⁷³⁷ CEC01638569

- 12.9 A report to the Council's Internal Planning Group on 31 May 2007 noted that a pilot MUDFA site (at Casino Square, Ocean Drive, Leith) had been completed between 26 April and 4 May 2007⁷³⁸. Additional utilities had been uncovered at the pilot site that were not identified during the original survey works. It was further noted that the latest programme from AMIS, revision 05, showed a start date for the MUDFA construction works of 2 July 2007 (with works commencing in and around Forth Ports) and an end date for phase 1a of November 2008. The report included a diagram showing the dates for the MUDFA works in the different areas under revised programme 05 compared with revised programme 03.
- 12.10 Utility diversions work commenced under the MUDFA contract in July 2007. In February 2008 Carillion plc acquired Sir Alfred McAlpine plc.
- 12.11 A number of difficulties were encountered in relation to the progress of the MUDFA works. It was widely recognised that to achieve the dates being forecast in the SDS Design programmes would be a major challenge. This was subsequently proven with the continuous submission of SDS Design programmes indicating month on month slippage. Tom Hickman could not recall if there was ever a time that he was confident that a revised programme would be achieved as the utility diversions continued deep into the timescale of the Infrastructure programme. The main sections of the MUDFA programme were subject to continual slippage thus eroding any programme float that existed as

⁷³⁸ CEC01566088

a buffer between completion of utility diversions and commencement of infrastructure works⁷³⁹.

12.12 There were problems with the provision of utilities diversion designs from Parsons Brinckerhoff. John Casserly attributed these in part to late information from SDS and insufficient ground investigations having taken place. While Ground Penetrating Radar was used, it was not reliable and there were limited if any actual physical trial holes actually dug up along the route to test what was under the ground especially in the “on-street” sections⁷⁴⁰. When the ground was dug up significantly more utilities that required diversion were discovered. It had been anticipated that there would be in the region of 27,000m of diversions but in reality it was nearer to 60,000m. The contractor also uncovered unexpected subsurface obstructions such as cellars, basements, air raid shelters, tunnels, historic steam cable infrastructure beneath Leith Walk. All of these required changes to the detailed design.

12.13 Even more modern utilities were a problem as many of the existing the Council and SUC (Statutory Utility Company) drawings of underground services were not accurate, and existing services were not always installed to the correct depth. Richard Walker recognized that there were difficulties for the MUDFA works because the utility companies are generally “a law unto themselves” and did not keep accurate records of what is in the ground or all go in the same trench. In addition to that, in a historic city such as Edinburgh, there is often infrastructure built on

⁷³⁹ Witness statement of Tom Hickman TRI00000147, page 9

⁷⁴⁰ Witness statement of Casserly TRI00000111, page 3

top of infrastructure and built on top of infrastructure. He gave the examples of the cemetery site and underground toilets that Infraco came across, that did not appear anywhere on any drawings⁷⁴¹.

12.14 Several witnesses also suggested that the MUDFA works were adversely affected by poor performance by SDS and the time it took the utilities companies to sign off any changes even when agreements had been entered into with them.

12.15 There was an inter-dependency between the design and the MUDFA works and investigations. The utilities still requiring to be diverted would inhibit a completion of design, but also if it was unknown what the swept path utilities cleared, it was difficult, sometimes impossible, for the designer to complete the design for the overhead poles or indeed the track slab or services going into the track slab, because otherwise there would be a clash if they were to come across utilities as yet not removed.

12.16 There were some areas that were particularly complicated, especially at important traffic junctions such as Haymarket and Picardy Place. These areas took up a large amount of design time and negotiations with third parties were protracted. This led to attempts to convene joint meetings and charrettes to try to take into account the views of all parties, especially in relation to areas where the Council envisaged public realm works being undertaken in conjunction with the tram works. The impact of the charrette process on the design and therefore utility diversions

⁷⁴¹ Transcript of oral evidence of Richard Walker 15 November 2017, page 10:6- 19

design was thought by some to have further delayed the MUDFA works by holding up SDS utilities diversions designs.

12.17 From the point of view of the MUDFA contractor, Andrew Malkin thought that the principal difficulty during the utilities pre-construction phase was late availability of SDS drawings⁷⁴² and that SDS approved design drawings did not necessarily constitute a design that could be built in the streets, nor did they represent an acceptance or approval by the relevant SUC. Drawings arrived too late to allow AMIS to plan works properly and many technical decisions had to be taken on site.

12.18 For AMIS, among the main difficulties were that the out of sequence release of utility drawings resulted in changes to the consolidated works programme and led to conflict with restricted embargo dates imposed by the Council in relation to major events in the city. The scale and complexity of the inner city traffic and impact on the wider area road network had also not been adequately modelled which resulted in late agreement of road closures. The inadequate road closure notifications and late communication of work plans by TIE Communications team impacted on local retailers and communities and restrictions on work and consequent delay in progress.

12.19 AMIS refuted the suggestion that it had insufficient resources to undertake the work on schedule and even pointed out that AMIS undertook earthworks at Gogarburn Depot so not to waste resource when it was not able to proceed in other areas because of delay in the

⁷⁴² Witness statement of Andrew Malkin TRI00000056, page 10

design process. It claimed that any poor quality work resulted from poor quality SUC apparatus not form AMIS.

12.20 Mr Malkin also thought that TIE's MUDFA project team was initially disengaged but was refreshed in mid-2007 and he welcomed a more dominant client although the working relationship problems were not resolved during his time at AMIS/Carillion⁷⁴³.

12.21 Tom Hickman's understanding was that it was widely recognised that to achieve the dates being forecast in the SDS Design programmes would be a major challenge. This was subsequently proven with the continuous submission of SDS Design programmes indicating month on month slippage.

12.22 TIE's MUDFA Contract Review Report dated 17 December 2007 noted that of 4,903 planned metres of utilities diversions to date, 4,099 metres of diversions had been undertaken (and that of 21 planned chambers, 14 chambers had been undertaken⁷⁴⁴. An update was given of the works in the various sections. In section 1A (Newhaven Road to Foot of Leith Walk), it was noted that trial holes to inform construction had recently commenced. A total of 68 trial holes were planned (35 before Christmas and 33 in January 2008). In section 1D (Princes Street West to Haymarket), 45 trial holes to inform construction along Shandwick Place had been undertaken in the period and the remaining 31 trial holes would be completed in the next period. It was noted that a significant increase in the traffic management and construction works

⁷⁴³ Witness statement of Andrew Malkin TRI00000056, pages 15 to 16

⁷⁴⁴ CEC01452199

around Princes Street, St Andrew's Square and York Place were due to commence at the end of January 2008.

12.23 The Council recognises that the historic nature of the city of Edinburgh increased the complexity of the MUDFA works and the difficulty in predicting what would be found under the ground when work started. However the complexities were even greater than had been expected and the lack of collaboration and poor performance of TIE, SDS and AMIS in trying to combat them were less effective than would have been hoped for. The delay in progressing the MUDFA works had a detrimental effect on the progress of the Project as a whole and used up all the buffer that had been intended to ensure that the MUDFA works were completed before the Infraco works commenced. Again this brought into play the provisions of the Infraco contract in resolving the situation and it was a situation that should have and was predicted before the Infraco contract was signed and should have been adequately provided for in it. As can be seen elsewhere in the submissions, the consortium initially took a very hard line where it was perceived that the MUDFA works had not been 100% completed before it took occupation of an area of the tram route and that contributed to the delay and cost over-run of the Project.

13. **Infraco**

Summary

- 13.1 The tender process took place between the publication of the Prior Information Notice in October 2005 and the appointment of BBS as preferred bidder in October 2007.
- 13.2 Both bidders initially expressed concern about the requirement to accept novation of subcontractors and price on the basis of a lack of detailed design and suggested postponing the procurement process.
- 13.3 When the bids were received they contained caveats relating to the incomplete design.
- 13.4 TIE proceeded to appoint a preferred bidder with the intention of firming up the price during negotiations based on a more developed design before the contract was let.

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- 13.5 On 6 October 2005 a Prior Information Notice was published in respect of a proposed procurement of the infrastructure contract⁷⁴⁵.
- 13.6 The Contract Notice was published on 31 January 2006⁷⁴⁶.
- 13.7 On 6 March 2006, TIE produced a Memorandum of Information and Pre-Qualification Questionnaire in respect of the procurement of the

⁷⁴⁵ CEC01792891

⁷⁴⁶ CEC02085568

infrastructure contract⁷⁴⁷. The contract documents were due to be issued on 25 May 2006. BB pre-qualified as a civil works contractor and was asked to pre-qualify again, this time as part of a joint venture with Siemens plc. BB and Siemens duly formed an alliance or consortium (BBS) and pre-qualified as partners in July 2006.

- 13.8 A report on the findings of the Readiness Review team was issued to the Chief Executive of TIE on 25 May 2006⁷⁴⁸. The overall status of the Project was assessed as Red. It was recommended that the incoming Tram Project Director should lead a review of the procurement approach. Some of the prequalified bidders (of both Tramco and Infraco) had expressed concern at the requirements to accept novation of subcontractors: *“For example, there are reports that potential Infracos may not want to take on designers or charge a premium for full novation of the SDS contract”*. It was noted that it would be important to retain at least three (and two as an absolute minimum) robust and appropriately constituted bidders as far into the procurement process as possible to maintain competitive pressure. The project team was required continue to monitor the procurement strategy in light of the market situation. It was recommended that the ITN documentation must enable the implications of variations to the novation approach to be properly evaluated in respect of cost, time, quality and risk allocation.

⁷⁴⁷ CEC01781572
⁷⁴⁸ CEC01793454

- 13.9 A record of a meeting on 7 June 2006 between TIE and Infracore⁷⁴⁹ noted that TIE's intention was to issue the tender documents in late August/early September, with tender return by the end of December 2006, with a view to contract award by July 2007 and operational trams by the end of 2010.
- 13.10 In late June 2006 Parsons Brinckerhoff submitted the Preliminary Design for the project.
- 13.11 Three responses to the Pre-Qualification Questionnaire in respect of the infrastructure contract were received on 14 July 2006. One party subsequently withdrew for its own organisational reasons.
- 13.12 Richard Walker's evidence was that BB was pushed by TIE to work with Siemens. At this time BB wanted to work with Bombardier, but Laing O'Rourke had already approached Bombardier and TIE wanted someone different. He said that BB understood it was to be a 'build only' contract, fully designed by TIE's designer. The design would be complete before Infracore contract award. Scott McFadzen said that the fact that the design would be completed and all necessary statutory approvals and consents would be obtained prior to the Infracore contract award was the "*big selling point*" for BBS because it would provide certainty⁷⁵⁰. The majority of utility diversion works were also to be completed with the remainder being complete approximately six months in advance of scheduled construction. Richard Walker thought that TIE's programme was already slipping and delayed and the programme

⁷⁴⁹ CEC01800968

⁷⁵⁰ Transcript of oral evidence of Scott McFadzen ,14 November 2017 pages 5:23 to 6:7

was totally unrealistic as it was already delayed by four months but the end date had stayed the same⁷⁵¹.

13.13 On 3 October 2006 TIE issued Invitations to Negotiate (ITN) in respect of the infrastructure contract⁷⁵². The documents comprising the ITN were contained in 21 CDS and a set of hard copy drawings⁷⁵³. Tender submissions were required by 9 January 2007.

Extension of time for tenders

13.14 In his oral evidence Richard Walker explained that BBS came to meet with TIE on 12 October 2006 because it thought the tender documents were unsuitable⁷⁵⁴. By letter dated 13 October 2006⁷⁵⁵ Richard Walker advised TIE that BBS had a number of significant issues with the ITN (as listed in his subsequent letter dated 16 October⁷⁵⁶) which would preclude BSC from submitting a compliant tender and requested a three month extension to the period for submitting a tender return. He thought the complexity and magnitude that the tender deliverables in the ITN were such that BBS would be unable to work up any meaningful affordable prices by the required return date. He requested that consideration be given to extending the tender by three months. He also thought the first ITN was wholly unsuitable for working in an urban environment and no contractor would accept it⁷⁵⁷.

⁷⁵¹ Witness statement of Richard Walker TRI00000072, pages 3 to 4

⁷⁵² CEC01794929

⁷⁵³ CEC01851927

⁷⁵⁴ Transcript of oral evidence of Richard Walker 15 November 2017, page 9:4-10

⁷⁵⁵ CEC01795260

⁷⁵⁶ CEC01795314

⁷⁵⁷ Witness statement of Richard Walker TRI00000072, pages 4 to 5

- 13.15 On 25 October 2006 BBS returned a mark-up of the Infraco Contract⁷⁵⁸ and Schedules and a document highlighting the key issues for BBS arising from the ITN documents⁷⁵⁹. Richard Walker said the purpose of this document was to show what was unacceptable to BBS and what would be acceptable⁷⁶⁰. Scott McFadzen attached a document, document⁷⁶¹ listing inconsistencies between the hard copy set of drawings, the electronic CD set, the drawing list attached with the documents and the Employer's Requirements. Richard Walker thought this indicated that the administration of the data was in disarray. None of the information was consistent, and was impossible to price. Appendix H, Schedule part 4, Base Date Design Information was an attempt to resolve the issue, but failed as the Appendix did not list anything.
- 13.16 Richard Walker said that meetings then took place between TIE and BBS on 8 November 2006⁷⁶² and 22 November 2006⁷⁶³ in relation to the design not being in a fit state to be priced, the documentation not being in a fit state to be understood, and the conditions of the contract being unresolved.
- 13.17 Geoff Gilbert's evidence was that TIE was aware that there was a lack of detailed information for the tender process at that time but TIE was trying to obtain an indication of whether the project was viable by

⁷⁵⁸ CEC01795913 and CEC01795947

⁷⁵⁹ CEC01795948

⁷⁶⁰ Witness statement of Richard Walker TRI00000072, page 3 paragraph 7

⁷⁶¹ CEC01823110

⁷⁶² CEC01794528

⁷⁶³ TIE00078323

running an initial bid based on the preliminary design⁷⁶⁴. TIE then intended to work with the bidders as design advanced to progress towards a more detailed design and firmer price before contract award.

13.18 In January 2007 TIE issued a Supplemental Instructions to Tenderers document⁷⁶⁵. The intention was to receive Proposals on 12 January 2007, after which further dialogue and negotiation would take place with a view to the submission of final Consolidated Proposals on 16 April 2007. BBS submitted proposals on 12 January 2007⁷⁶⁶. Geoff Gilbert's evidence was that a huge amount work went into reviewing the initial bids⁷⁶⁷.

13.19 During the period between 12 January and 16 April 2007 it was intended that Tenderers would be provided with further information including updated Employer's Requirements, significant development to the Preliminary Design (including surveys) carrying price or risk implications, updated traffic modelling, current programme for the MUDFA works and detailed design for key structures. After submission of the Consolidated Proposals it was proposed that a number of activities would take place, including the selection of a Preferred Bidder, the release of detailed design from SDS (after nomination of the Preferred Bidder), due diligence by the proposed Preferred Bidder on price and risk critical items in the SDS design and final negotiations to settle the agreed Infracore Contract package, including firm price and

⁷⁶⁴ Witness statement of Geoff Gilbert TRI00000038, pages 19 to 22

⁷⁶⁵ CEC01824070

⁷⁶⁶ CEC01533655

⁷⁶⁷ Witness statement of Geoff Gilbert TRI00000038, page 76

scope for Phase 1a. It was anticipated that Infracore contract award would take place in October 2007. Richard Walker's view was that BBS was provided with approximately 10 to 15 % of the information mentioned; he said that a firm or fixed price would only have been agreed if there was a complete design, the contract wording had been agreed and all the utilities had been moved. Mr Walker also said that he realised when he first received the Supplemental Instructions to Tenderers document in January 2007, that it would not work. He said that he suggested to TIE that the procurement process should be delayed to allow for the appropriate information to become available⁷⁶⁸. Scott McFadzen said he suggested that SDS should run two design teams – one to complete the detailed design and the other to give the bidders the information they needed to tender⁷⁶⁹.

13.20 In May 2007 BBS submitted its Tender⁷⁷⁰. The proposed price was £268m which was less than the £295m that had been estimated in January because of new information that had become available⁷⁷¹.

Initial comments on tenders

13.21 Negotiations continued and BBS submitted updated proposals in August 2007 with a Schedule of Clarifications⁷⁷². Where the information was incomplete, the price was qualified.

⁷⁶⁸ Transcript of oral evidence of Richard Walker 15 November 2017, pages 12:12- 13:13

⁷⁶⁹ Transcript of oral evidence of Scott McFadzen 14 November 2017, page 8:9- 16

⁷⁷⁰ CEC01656123

⁷⁷¹ Transcript of oral evidence of Scott McFadzen 14 November 2017, pages 20:24 to 21:14 and CEC00573745

⁷⁷² CEC01604676 and CEC01491869

13.22 In a letter dated 19 July 2007⁷⁷³, Geoff Gilbert set out the Activities to Deliver Contract Award Recommendation. It was noted: The strategy for the delivery of the Project included "*The de-risking of the price for the works by getting sufficient design done in advance of Infracore recommendation so that risk pricing by bidders for scope and performance is minimised*". The programme had been delayed by "*Delays to the design programme resulting in the outputs required for pricing due to their difficulty in obtaining decisions from Project stakeholders. TIE have intervened now to bring about clear decision making*". TIE intended to conclude tender evaluation and negotiations by 28 August 2007, to enable TIE to make a conditional contract award recommendation to its board by 25 September (with proposed contract award in October), which recommendation would be conditional on negotiations and design due diligence. To enable that timescale to be met, TIE required bids that met certain criteria including that bids "*Don't contain significant pricing uncertainty and risk allowances*" and "*Have a clear and agreed basis for adjustments in respect of: significant areas of design uncertainty e.g. roads, paving's and drainage; and significant quantity changes arising from completion of detailed design*". Bidders were required to update their bids for "*The further design information to be provided as the attached schedule*". TIE required "*Details of the items bidders believe are required to enable them to deliver design due diligence for the price and performance risk critical*

⁷⁷³ CEC01627004

issues". The purpose of this letter was to articulate TIE's intended process.

13.23 Richard Walker's view at that time was he did not think the design would be ready, but BBS had articulated a clear and agreed basis for adjustments. He did not think that the design was delayed, rather the tender process was started too early in relation to the design progress. BBS caveated its submissions on the basis that the design would be complete in sufficient time for it to have been able to give firm prices. It was told that TIE had intervened to bring about clear decision-making in terms of progressing the design, so was given some confidence that the design would be ready in adequate time for BBS to price. His understanding was that due diligence would be undertaken when it was concurrent with receipt of the design. It was envisaged and anticipated that all the design would be complete in sufficient time for BBS to price.

13.24 In an email dated 30 August 2007⁷⁷⁴, Geoff Gilbert sent a spread sheet⁷⁷⁵, noting that *"Taking things in the round it doesn't look like there has been much movement" and that "Heads up from the contract session this morning is that it has not gone at all well. We need [to] settle this this afternoon"*. Richard Walker believed the purpose of this email and spread sheet was to put pressure on the bidder to reduce the price by indicating what the other bidder was likely to accept.

13.25 On 20 September 2007 Parsons Brinkerhoff gave a presentation to both Infracore bidders, namely Scoop (i.e. the Tramlines consortium) and

⁷⁷⁴ CEC01642812

⁷⁷⁵ CEC01642813

Roley (i.e. BBS)⁷⁷⁶. Richard Walker expressed disappointment that BBS was not allowed to speak directly to the designers and he expressed his view that the tender process should be put on hold because of the state of the design⁷⁷⁷.

13.26 In an email dated 21 September 2007⁷⁷⁸ Scott McFadzen noted that TIE had stated that it was its intention to deliver a price that was within the £219 million budget for the Infracore works. Richard Walker and Scott McFadzen both felt like TIE was trying to dictate what the price should be because it had a budget to stick to⁷⁷⁹.

Appointment of preferred bidder

13.27 On 22 October 2007 TIE and BBS entered into an agreement relating to the Selection for Appointment as Preferred Bidder, document reference⁷⁸⁰. The purpose of this agreement was to try and articulate the areas that needed adjustment after award of preferred bidder where the design was not finalised. The main terms of this agreement was a payment mechanism and adjustment of prices for provisional and undesigned work.

13.28 The sum of £218.5m sum was noted in the agreement. Richard Walker had the impression that TIE had been trying to manipulate the numbers to get the price through this "gateway". TIE did not disclose to BBS what this figure was. It was simply aware that it was under pressure to

⁷⁷⁶ CEC00199336

⁷⁷⁷ Transcript of oral evidence of Richard Walker 15 November 2017, pages 17:6 to 19:7

⁷⁷⁸ CEC01602752

⁷⁷⁹ Transcript of oral evidence of Richard Walker 15 November 2017, pages 20:6 to 21:17;
Witness statement of Richard Walker TRI00000072, pages 10-11

⁷⁸⁰ CEC01497399

get the number below a set figure in order for this "business case" to be approved by the Council. The Agreement also referred to 'PB finalisation issues' and bidder due diligence of design to be undertaken was adequate to assess the status of the design.

13.29 Geoff Gilbert's evidence was that the bids were very close between the two consortia, and there were fractions of a percentage between the scores for the bidders and one of the main reasons why BBS was selected was because of its proposed track form and its constructability with the street environment⁷⁸¹. He also said that the reason why BBS was deemed the preferred bidder in October 2007 but a firm bid was not made until the next year was part of the negotiation strategy to negotiate with both bidders to get the best position based on the bid information including the available elements of detailed design to form a baseline form which to proceed to the next stage of adjusting from that baseline⁷⁸².

13.30 Further negotiations took place after BBS had been appointed preferred bidder up to contract close in May 2008. Joachim Enenkel said that during tender process the consortium found the communication open, fair and straight forward. After award, however, we noticed increasingly legal language, which meant that due to lack of leadership (or clear direction) in the project lawyers took control by trying to defend

⁷⁸¹ Witness statement of Geoff Gilbert TRI00000038, page 7 paragraph 16

⁷⁸² Witness statement of Geoff Gilbert TRI00000038, page 86 paragraph 226

traditional contractual understanding which was not reflected in the contract⁷⁸³.

- 13.31 The Council submits that the bid process and appointment of the preferred bidder did not of itself cause the delay or increase in the cost of the Project. The problems arose because the detailed design was not sufficiently completed before the contract was let and how the contract terms dealt with how changes from the design would be dealt with.

⁷⁸³ Witness statement of Joachim Enenkel TRI00000150, page 10

14. **Involvement of Audit Scotland and OGC Gateway Reviews**

Summary

- 14.1 The reports produced by OGC throughout 2006 and 2007 as well as the report of Audit Scotland in 2007 had some positive effect on the progression of the project. They showed a project which was evolving and becoming more robust. Members of the Council gave evidence that they relied on the Audit Scotland Review and the OGC Reviews. The positive assessments given by these two public bodies had the effect of creating confidence in the project and influenced their decisions in favour of the project.
- 14.2 The risks of the project were referred to in the OGC Reviews. However, members of the Council did not have the relevant experience or qualifications to assess the risks highlighted. The simplistic way in which the reviews were presented using a general indicator system was a risk in itself. The Council submits that the reviews were the not a principal cause of any difficulties with the project. The difficulties mainly arose as a result of the effect of Schedule part 4 and clause 80.
- 14.3 Witnesses on behalf of the Council gave evidence that they wanted to seek an independent review on risk by Turner & Townsend as this would have provided greater detail than the OGC Reviews. Officers of TIE resisted these suggestions. The Council recognise that an independent review could have provided a clearer assessment of risk. However, and this can be no more than speculation, it is likely that it

would not have had any effect on the inclusion of Schedule part 4 and clause 80 in the Infraco contract.

Audit Scotland and OGC

14.4 With reference to the involvement of Audit Scotland and the Office of Government Commerce (“OGC”) Gateway Reviews, it is submitted that although these had an effect in encouraging confidence in the procuring of the Project, they did not lead to or contribute to the additional costs, the delays or the reduction in scope. Other than in the sense that these reviews were a part of the picture which led to the decision to enter into the necessary contracts, they did not support the entering into of the Infraco contract which in particular contained Schedule part 4 and clause 80. As already discussed, it was these elements which led to the critical failings and there is no evidence that either Audit Scotland or the OGC Reviews played any part in their inclusion in the Infraco contract.

14.5 The relevant sequence of events is set out in the Statement of Main Documents and Events. The following events are particularly relevant for the purposes of this section of the submissions. After initial work, TIE published the STAG 2 Appraisal for the then Line One on 28 November 2003⁷⁸⁴ with Appendices⁷⁸⁵. The Appraisal was prepared with the assistance of TIE's technical advisors, Mott MacDonald, and was submitted to the Scottish Parliament with the Bill for Line One. It concluded that “*a strong case for Line One has been made*”. In December 2003, TIE produced a Preliminary Financial Case for the

⁷⁸⁴ CEC00632759

⁷⁸⁵ CEC00642726

then Line One and Line Two⁷⁸⁶. In January 2004, the Bills for Line One and Line Two were submitted to the Scottish Parliament. In July 2004, a further STAG appraisal was published⁷⁸⁷. In September 2004, an Update of the Preliminary Financial Case for Line One was produced⁷⁸⁸. The update had been prepared at the request of the Private Bills Unit of the Scottish Parliament to provide the Committee of MSPs considering the Bill for Line One with an update. The update was part of a sequence of reports and financial assessments carried out by or on behalf of TIE throughout the period in question. The Committee of the Scottish Parliament considering the Bills for Lines One and Two produced reports on each Bill⁷⁸⁹. In March 2006 the Edinburgh Tram (Line One) Act 2006 and the Edinburgh Tram (Line Two) Act 2006 were passed and received Royal Assent in April and May 2006.

- 14.6 Between 22 and 25 May 2006 a Readiness Review was carried out to provide an independent assessment of the project, including the extent to which the programme satisfied relevant criteria which were similar to those that would be assessed as part of an OGC Gateway 2 Review. The accompanying terms of reference explained that the review would be high level and strategic and would not be concerned with contract drafting or detailed provisions of the invitation to tender nor with the economic case for the project, but would focus on key issues which

⁷⁸⁶ TRS00000054 and TRS00000016

⁷⁸⁷ TRS00000041

⁷⁸⁸ CEC00630633

⁷⁸⁹ CEC00634674 and TRS00031163

underpinned successful procurements⁷⁹⁰. The overall status of the Project was assessed as Red (immediate action necessary).

14.7 Between 26 and 28 September 2006 a further Readiness Review was carried out on the instruction of the Chief Executive of Transport Scotland to reflect the criteria of an OGC Gateway 2 Review⁷⁹¹. The review found that there had been a considerable transformation in the organisation, attitude and effectiveness of the TIE team since the previous review with a common understanding of the requirements of the procurement process and the challenges faced. The overall status of the project was assessed as Amber (project should go forward with actions on recommendations to be carried out before the next review of the project).

14.8 On 21 December 2006, the Council was asked to approve the draft FBC dated November 2006⁷⁹². Following the change of Scottish Government in May 2007, John Swinney, the Cabinet Secretary for Finance and Sustainable Growth, requested the Auditor General for Scotland to carry out a high-level review of the Project (and of the Edinburgh Airport Rail Link project).

14.9 On or about 20 June 2007, Audit Scotland published its findings in a report⁷⁹³. It was concluded that the arrangements in place to manage the Project appeared to be sound although a range of key tasks needed to be completed before the final business case could be signed off. On

⁷⁹⁰ CEC01881455

⁷⁹¹ CEC01629382

⁷⁹² CEC01821403

⁷⁹³ CEC00785541

27 June 2007, the Auditor General for Scotland gave evidence in relation to the Project⁷⁹⁴ and later that day the Scottish Parliament voted in favour of a resolution calling upon the SNP administration to proceed with the Project within the budget set by the previous administration.

14.10 The OGC Gateway 3 review took place on 25 September and between 1 and 4 October 2007 and a report dated 9 October was delivered to the Chief Executive of the Council⁷⁹⁵. The overall status of the project was assessed as Green (the project is on target to succeed provided that the recommendations are acted upon). It was noted that the project was continuing to make good progress. It was further noted that all of the recommendations in the Gateway 2 report had been fully or substantially achieved at the time of the follow up review in November 2006. The report also noted concerns about the timelines of project delivery.

14.11 On 15 October 2007, the OGC review team produced a further report⁷⁹⁶. The report noted that a number of risks remained with the public sector, including the outturn price, the delivery programme of MUDFA works, and potential delay in the design and approvals processes. It stated that the TIE Project Management team needed to have a clear vision of what was required in terms of contract management. The report also noted concerns about the level of contingency provided for risk in the budget estimates.

⁷⁹⁴ SCP00000031

⁷⁹⁵ CEC01562064

⁷⁹⁶ CEC01496784

- 14.12 The above is no more than selected events during the course of the initiation, development and decisions to enter into the Infraco and other contracts which were carried out by TIE, the Council and others including appointed consultants. Overall, it is submitted that the progress of the OGC Gateway Reviews gave an impression of a project which during the course of its evolution was becoming more robust and thus more acceptable. The movement of the overall assessments in the Reviews from Red, through Amber, to Green may be said to have given that impression. Of course, each Review raised concerns which were considered in detail (and of which what is stated above is only the briefest flavour) but these concerns were addressed in detail in the individual Review reports and did not detract from the overall increasingly positive assessments.
- 14.13 The report of Audit Scotland in June 2007 may be said to have had the same positive effect, as did the evidence of the Auditor General himself to the Scottish Parliament. Not only could that give confidence to those in the Council and elsewhere who had to make the critical decisions to proceed with the Project but it also gave confidence to the Committee which advised on the Bills and the Parliament which passed them. Indeed, the passing of the Bills in itself may be said to have been a factor in favour of the financial and economic justification for the Project.
- 14.14 That the Audit Scotland and OGC Gateway Reviews did give such confidence is demonstrated in the evidence to the Inquiry, including evidence of those who were councillors at the time. Examples are the evidence of Jennifer Dawe who gave evidence that both the Audit

Scotland review and the OGC Reviews had influenced her in favour of the Project and she referred to the Red, Amber, Green sequence as having some bearing.⁷⁹⁷ Lesley Hinds said that members of the Council would have gained comfort from the Green status and she suggested that it indicated that the Project was “robust”.⁷⁹⁸ Similar evidence was given by Iain Whyte.⁷⁹⁹

14.15 The nature of the risks referred to in the OGC Reviews was known to officers. Duncan Fraser referred to them in an email dated 19 October 2007.⁸⁰⁰ Donald McGougan said that both the OGC and Audit Scotland had reviewed risk and with the risk allowance and the headroom he considered that this “*should avoid any significant financial problems*”.⁸⁰¹

14.16 The Council submits that the evidence has demonstrated that the fact that both Audit Scotland and the OGC had provided outwardly positive reviews as the steps towards implementation progressed did lead to a degree of confidence when it came to the critical decisions to be made by those responsible, most notably councillors of the Council, but also officers. The members of the Council had no particular qualifications or experience by which to judge the financial and economic viability of such a large project. The fact that they could see outwardly positive assessments from public bodies charged with fulfilling the relevant responsibilities was obviously something which would engender confidence when it came to approving the Project.

⁷⁹⁷ Transcript of oral evidence of Jennifer Dawe 5 September, pages 101 to 102, in particular pages 101: 20 to 102:3

⁷⁹⁸ Transcript of oral evidence of Lesley Hinds 6 September 2017, pages 71:20 to 72:9

⁷⁹⁹ Transcript of oral evidence of Iain Whyte 7 September 2017, pages 95:24 to 96:6

⁸⁰⁰ Transcript of oral evidence of Duncan Fraser 12 September 2017, page 56:7- 23

⁸⁰¹ Transcript of oral evidence of Donal McGougan 30 November 2017, pages 43:15 to 44:22

14.17 In that respect, it may also be the case that the way in which the relevant reviews were presented was a factor in giving unjustified confidence. Where a review report uses a generalised indicator system such as the Red, Amber and Green indications of the OGC Gateway Reviews, Green may be said to give too general a positive impression. These Reviews did, of course, contain considerable detail, much of it relating to cost and risk, but the fact that a project has reached Green status creates a much less nuanced immediate impression as to the pros and cons of the project. It may be said that to properly understand the reasons for that status, the reader needs to consider the whole report. But if that is the case, there is no need for the stark Red, Amber or Green categorisation which, as has just been said, by itself creates an unduly favourable impression.

14.18 There has been no detailed evidence on how such financial and economic reviews are conducted and reports written, but the Council would submit that for the future some thought might be given as to whether a simplistic system, such as the Red, Amber, Green one, does create the risk by itself that a project will be likely to be given approval in a situation where actually the risk element is greater than appears. This is not to suggest that the reliance by members and others on the Audit Scotland and OGC reviews was a principal cause of the difficulties with the Project because, as before, these came about as a result of the critical effect of Schedule part 4 and clause 80 of the Infraco contract, and these would not have been affected by any different form and presentation of review by the public bodies in

question. However, a more sophisticated method of representing risk may be an element in the lessons which may be learned for the future.

14.19 There is a further aspect relating to the OGC Reviews. In September 2007, officers of the Council had been seeking a separate independent review on risk and had prepared to instruct an additional review to be carried out by Turner & Townsend, but that was resisted by officers in TIE.⁸⁰² Duncan Fraser was concerned that the OGC advice was at too high a level and that the OGC referred to the risk element having been validated by DLA. Ultimately, he felt that the OGC report “*slightly underplayed the potential risk*”. He believed that Turner & Townsend would have gone into the risk assessment side in much greater detail.⁸⁰³ Jim Inch said that it would have been better to have obtained advice from Turner & Townsend rather than the OGC and he was not sure how the decision to remain with the OGC had come about.⁸⁰⁴ Susan Clark of TIE thought that the review should be done by OGC because it was already going to do a review; she was trying to save costs.⁸⁰⁵ Michael Heath, who had been involved in the OGC Reviews, thought that instruction of Turner & Townsend would have been beneficial because their review would have gone into “*much more detail*” than had the OGC Reviews.⁸⁰⁶

14.20 Amongst the senior officers of the Council, Andrew Holmes was in agreement with the proposal to instruct Turner & Townsend and felt

⁸⁰² Transcript of oral evidence of Rebecca Andrew 13 September 2017, pages 56:1 to 58:17

⁸⁰³ Transcript of oral evidence of Duncan Fraser 12 September 2017, pages 35:9 to 48:12

⁸⁰⁴ Transcript of oral evidence of Jim Inch 19 September 2017, pages 167:17 to 169:20

⁸⁰⁵ Transcript of oral evidence of Susan Clark 25 October 2017, pages 146:12 to 149:1, in particular page 147:12-17

⁸⁰⁶ Transcript of oral evidence of Michael Heath 21 September 2017, pages 92:17 to 94:7

with the benefit of hindsight that it would have been prudent to obtain independent advice on risk.⁸⁰⁷ In contrast, Donald McGougan supported the need of a review but was content for the OGC to do it. He did not consider that such a review would be too high level and he had confidence in the OGC.⁸⁰⁸

14.21 There was therefore some concern at the time about the adequacy of the OGC Reviews. Likewise, there could be said to have been shortcomings in the Audit Scotland review instructed in 2007. This was conducted in only 16 days which was a much shorter time than the normal nine months,⁸⁰⁹ and the instruction of this review had not been discussed with or explained to officials from Transport Scotland.⁸¹⁰

14.22 This evidence suggests that in 2007 there might have been advantages in the Council instructing a separate independent review beyond those of the OGC and Audit Scotland but also that there were seen to be good reasons why that was considered to be unnecessary, including issues of cost, and a further review at the time was carried out by the OGC. It may be that with the benefit of hindsight a review by Turner & Townsend could have provided a more robust and potentially challenging assessment on risk but that cannot be certain. It also cannot be certain what the outcome of such a situation could have been: whether it could have resulted in a pausing or even cancellation of the Project or, more likely, the taking of further steps to address risk.

⁸⁰⁷ Transcript of oral evidence of Andrew Holmes 29 November 2017, pages 23:17 to 31:18

⁸⁰⁸ Transcript of oral evidence of Donald McGougan 29 November 2017, pages 142:4 to 148:2

⁸⁰⁹ Transcript of oral evidence of Graeme Greenhill 21 September 2017, page 136:7 to 141:17 under reference to his Inquiry Witness statement

⁸¹⁰ Transcript of oral evidence of Damien Sharp 5 October 2017, pages 96:14 to 97:11

This can be no more than speculation but the one thing which is likely is that an independent review by Turner & Townsend would not have had any effect on the inclusion of Schedule part 4 and clause 80 in the Infraco contract.

14.23 The result is that in these respects lessons may be learned for the future, and the Inquiry may be able to give guidance about how formal reviews by Audit Scotland and the OGC, which are to be relied upon by lay persons such as local authority members, in the making of important decisions, ought to be carried out and presented. These may certainly be aspects of the lessons which can be learned for future projects but they are not a cause of the additional costs, delays and reduction of route of the Project.

15. **Approvals Committee**

Summary

15.1 This component of chapter 3 outlines the various reports in chronological order from the FBCv2 in December 2007 to the letter from Willie Gallagher to the Chief Executive of the Council on 13 May 2008 advising that TIE was of the view that the final contract terms were materially consistent with the terms of FBCv2 and that it was now appropriate to conclude the contracts.

15.2 The Approvals Committee was a committee of the TPB. TEL had ultimate responsibility as the TPB was its sub-committee.

15.2.1 Although the ultimate decision of the Approvals Committee was an intended part of the process leading to the entering into of the Infraco and other contracts, it did not truly represent an additional and separate stage in the events leading to contract closure.

15.3 Whatever the Approvals Committee may have been expected to do, and whatever deficiencies there may have been in its processes, such deficiencies made no difference to the outcome of the Project.

Decision to set up Approvals Committee

15.4 The decision to enter into the Infraco and other contracts was subject to the approval of a committee known as the Approvals Committee. The background to consideration by the Approvals Committee may be summarised as follows.

- 15.5 On 20 December 2007, the approval of the Council was sought for FBCv2 which had been prepared by TIE. This was supported by a report provided by the Director of Finance and the Director of City Development⁸¹¹ which recommended staged approval for the award by TIE of the contracts for the supply and maintenance of the infrastructure works and tram vehicles. The Council granted approval⁸¹².
- 15.6 On 18 March 2008 the Directors of City Development and Finance and the Council Solicitor provided a memorandum to the Council's Chief Executive advising that they considered that it was appropriate to accept TIE's recommendation to authorise and permit TIE to lodge the formal Notice of Intention to Award document⁸¹³. On the same date, notice was given by TIE of the intention to award the Tramco contract⁸¹⁴ and the Infraco contract⁸¹⁵.
- 15.7 On 18 March and 20 March 2008, DLA sent letters to the Council Solicitor advising on the draft contract suite as at 13 March 2008⁸¹⁶.
- 15.8 On 1 May 2008 a report was provided to the Council by the Chief Executive⁸¹⁷ giving information on negotiations, the assessment of risk and the estimated final cost of the Project. The Report concluded by proposing that the Tramco and Infraco contracts should be awarded to CAF and BBS respectively. The Council was asked to refresh the delegated powers already given to the Chief Executive to authorise and

⁸¹¹ CEC02083448

⁸¹² CEC02083448

⁸¹³ CEC02086755

⁸¹⁴ CEC01314422

⁸¹⁵ CEC01314423

⁸¹⁶ CEC01347796 and CEC01544970

⁸¹⁷ CEC02083359

instruct TIE to enter these contracts and to note that a Guarantee by the Council for the benefit of Infraco would be provided at Financial Close.

15.9 On 12 May 2008, DLA sent a further letter to the Council Solicitor and the Chief Executive of TIE advising on the draft contract suite⁸¹⁸. The letter attached an updated version of a document entitled "*Contractual Allocation of Risks in the Draft Infraco Contract*" as at 12 May 2008⁸¹⁹. Gill Lindsay met the Council Directors on 12 May 2008 and was certain that they would have confirmed that they were satisfied. She then signed the financial close recommendation⁸²⁰ on 13 May.⁸²¹

15.10 In the evening of 12 May 2008, a final set of internal approval documents was circulated among TIE and Council officers by email⁸²². These comprised a Financial Close Process and Record of Recent Events dated 12 May 2008⁸²³, a Report on Terms of Financial Close (the "Close Report")⁸²⁴, a Report on Infraco Contract Suite⁸²⁵, and an Assessment of Risk of Successful Procurement Challenge⁸²⁶ (the details of these documents are set out in the Statement of Main Documents and Events and are not material for present purposes).

15.11 On 13 May 2008, an updated letter from DLA was emailed to the Council Solicitor⁸²⁷. On the same date, the Policy and Strategy

⁸¹⁸ CEC01222442

⁸¹⁹ CEC01222439

⁸²⁰ CEC01244245

⁸²¹ Transcript of oral evidence of Gill Lindsay 27 October 2017, page 174:8 - 10

⁸²² CEC01338846

⁸²³ CEC01338847 and CEC01338848

⁸²⁴ CEC01338853 and CEC01338854

⁸²⁵ CEC01338851 and CEC01338852

⁸²⁶ CEC01338849 and CEC01338850

⁸²⁷ CEC01372309

Committee of the Council was provided with a report by the Chief Executive which advised the Committee of a changed commercial position in procurement negotiations and sought approval for the Chief Executive to instruct TIE to enter into contracts with the Infraco and Tramco bidders, subject to the satisfactory final conclusion of negotiations⁸²⁸. The report referred to the final estimated cost of phase 1a and recommended that the Committee approve that final estimated cost, authorise the Chief Executive to instruct TIE to enter into contracts with the Infraco and Tramco bidders in the context of the recent changes noted in the Report and refresh the Chief Executive's delegated authority to make any minor amendments in respect of the contracts. The report recommended that FBCv2 be modified to reflect the above position. The Committee provided the approval sought⁸²⁹.

15.12 In FBCv2 which was approved by the Council on 20 December 2007 it was proposed that the TPB would be constituted as a committee of TEL. The Approvals Committee was set up at a joint meeting of the TPB, TIE and TEL on 23 January 2008⁸³⁰. It consisted of David Mackay, Neil Renilson and Willie Gallagher.⁸³¹

15.13 A report to the TPB on 7 May 2008 gave an update on Infraco negotiations⁸³². At a meeting of the TPB on 13 May 2008, it was noted that approval had been received from the Policy and Strategy Meeting of the Council allowing the letter from the Chief Executive to be signed

⁸²⁸ USB00000357

⁸²⁹ CEC01891564

⁸³⁰ CEC01515189

⁸³¹ CEC01515189 and Transcript of oral evidence of Neil Renilson 14 December 2017, pages 4:16 to 8:4

⁸³² CEC00079902

and sent to Willie Gallagher giving delegated authority to sign the contracts and that "*Receipt of this letter allowed the Approvals Committee to approve final signature*"⁸³³.

15.14 By letter dated 13 May 2008, Willie Gallagher advised the Chief Executive of the Council that TIE was of the view that the final contract terms were materially consistent with the terms of FBCv2 and that it was now appropriate to conclude the contracts⁸³⁴.

15.15 The Approvals Committee met to confirm authority to proceed with the Infraco Contract on 13 May 2008⁸³⁵. David Mackay recalled that the members were given papers, probably over a period of time, and a verbal presentation possibly by Graeme Bissett. The evidence of David Mackay was not clear on just what had been provided and had been taken into account. Neil Renilson could recall a meeting of the three persons who were the members of the Approvals Committee but could not recall if there had been a formal meeting or a "*paper exercise*".⁸³⁶ Willie Gallagher described discharging his responsibilities as a member of the Approvals Committee by referring to a "*process*" whereby TIE and legal representatives were asked formally if they were recommending that the project should go ahead although he was not clear as to whether that actually depended upon the various formal decisions which had been made by those in TIE and other bodies.⁸³⁷ Ultimately, he accepted that the approval given by the Approvals

⁸³³ CEC00079774 and CEC00080738

⁸³⁴ CEC01284042

⁸³⁵ CEC01289240

⁸³⁶ Transcript of oral evidence of Neil Renilson 14 December 2017, page 7:12-17 and page 8:15- 20

⁸³⁷ Transcript of oral evidence of William Gallagher 17 November 2017, pages 135:8 to 141:6

Committee was “*simply a formal step*” to approve the other work that’s already been done and that there had been no further or independent review.⁸³⁸

15.16 At the time of entering into the contracts, Tom Aitchison said that he expected senior Council officials to satisfy themselves to trust their own judgment and do what they thought was right. They could rely on advice from DLA but ought to ask the hard questions on behalf of the Council.⁸³⁹ This was related to the Council’s decisions to authorise the entering into of the contracts but was not related to the Approvals Committee which did not include any Council representation.

15.17 It is not apparent that the Approvals Committee itself took any particular steps to satisfy itself as to the proper transfer of risk and Neil Renilson could not give detailed evidence of what exactly was taken into account when approval was given.⁸⁴⁰ Mr Hogg considered that the Approvals Committee had responsibility for risk.⁸⁴¹

15.18 The Approvals Committee was a committee of the TPB, and TEL had ultimate responsibility as the TPB was its sub-committee.⁸⁴² Neil Renilson was regarded as the senior responsible owner by Donald McGougan as he was chair of TEL.⁸⁴³ David Mackay agreed that the

⁸³⁸ Transcript of oral evidence of William Gallagher 17 November 2017, page 142:10-17

⁸³⁹ Transcript of oral evidence of Tom Aitchison 28 November 2017, pages 109:19 to 110:18

⁸⁴⁰ Transcript of oral evidence of Neil Renilson 14 December 2017, pages 9:16 to 22:10

⁸⁴¹ Transcript of oral evidence of Kenneth Hogg 13 December 2017, pages 103 to 4

⁸⁴² Transcript of oral evidence of Neil Renilson 23 November 2017, page 83:7- 17

⁸⁴³ Transcript of oral evidence of Donald McGougan 29 November 2017, page 123:5- 6

Approvals Committee was set up to “*provide a detailed scrutiny*”.⁸⁴⁴ He said that it was not a “*rubber stamping exercise*”.

15.19 In light of this evidence, it is submitted that although the ultimate decision of the Approvals Committee was an intended part of the process leading to the entering into of the Infraco Contract and other contracts, it did not truly represent an additional and separate stage in the events leading to contract closure even though it may have been intended as such a separate stage. There was no process whereby the three members of the Approvals Committee formally identified what they needed to take into account before giving approval, and no formal process whereby they met and decided to grant approval in light of their independent consideration. There appear to be no minutes of any such meeting and decision which was said to be unusual⁸⁴⁵.

15.20 In the circumstances, however, it is submitted that whatever the Approvals Committee may have been expected to do, and whatever deficiencies there may have been in its processes, such deficiencies made no difference to the outcome of the Project. As discussed in chapter 1, the principal or proximate cause of the additional cost, delay and reduction of the route was the entering into of the Infraco Contract which contained Schedule part 4 along with clause 80. The decision to enter into the Infraco Contract was effectively approved by the Council taking into account all of the information which had been provided in particular by TIE and DLA. The submissions already made are not

⁸⁴⁴ Transcript of oral evidence of David Mackay 21 November, page 51:4-6

⁸⁴⁵ Transcript of oral evidence of David Mackay 21 November 2017, pages 51:25 to 61:18

repeated. As summarised at the beginning of this section, the Council was fully informed of all of the circumstances leading up to the decision of the Policy and Strategy Committee on 13 May 2008. This included, most critically, such legal advice as had been tendered by DLA and which was deficient for all of the reasons already advanced. The Policy and Strategy Committee acted on all of the material provided to it by TIE and the TPB and this again depended upon the legal advice which had been received from DLA.

15.21 It is not apparent as to what additional scrutiny could have been provided by the Approvals Committee set up in the way that it was. The members of the Approvals Committee had no additional or independent sources of information or advice. In particular, they had no separate legal advice and it was never suggested that they should seek such advice. The members of the Approvals Committee were appointed as named individuals none of whom was appointed because of legal qualification or experience. Each of those members had already been able to form his own view as to whether the contracts should be entered into given that each held a position as an officer of TIE or TEL which was recommending that the Project should proceed.

15.22 It is therefore submitted that the device of appointing an Approvals Committee did not achieve anything of significance in the circumstances of the Project. It did not in practical terms result in any additional level of scrutiny and its members were not qualified or given the resources to do so. It may be seen as no more than one element in a sequence of events in which for all of the reasons already discussed

the Infraco Contract was entered into with the approval of the Council and that position would have been the same with or without the Approvals Committee as it was constituted.

15.23 It is fair to say that there may be a case for a suitably independent and resourced approvals committee to be set up in the case of a proposed major public infrastructure project such as the Project. There has been no evidence as to whether that has been done in other cases or how it might be done. For it to have any real value as a scrutinising committee, it would seem that it would need to be composed of individuals and resourced in a way which allowed truly independent consideration and decision-making. On the other hand, there may be good reasons why such a committee would not be a good idea given its potential to disrupt at the last moment the entering into of important contracts in a situation in which these contracts have already been scrutinised fully and properly by the bodies responsible. For these reasons, the Council presents no definitive submission on this aspect.

15.24 In the circumstances of the Project, however, the position of the Council is that the appointing of the Approvals Committee by the TPB had no material effect on the entering into of the Infraco Contract, neither positive nor negative, and it played no part in the events which led to the additional costs, the delay, and the reduction of scope of the Project.

16. **Events after Contract Close**

Summary

16.1 After contract close both the MUDFA Works and SDS design programme continued to fall behind schedule. The MUDFA contractor continued to discover unexpected obstructions under the ground and SDS struggled to produce detailed designs and re-design diversion works.

16.2 TIE complained that Infraco slow to mobilise and start the Infraco works. In the summer of 2008 Infraco did start some on-street construction works on Leith Walk despite the fact that the MUDFA works had not been completed in the area.

16.3 Infraco issued its first INTCs and claimed payment in relation to the changes in September 2008. TIE refused to make payments in October 2008 and after some discussion over the competing interpretations of the contract Infraco stopped work and relations between the parties started to deteriorate and head towards formal DRP procedures.

Difficulties in progressing the Infraco Works (and the reasons for these difficulties)

16.4 In May 2008, the Council requested information about potentially terminating the MUDFA contract. However it was considered that the failures to meet contractual obligations were not sufficiently material

and had been affected by other factors outwith AMIS' control, such as the obstructions found underground⁸⁴⁶.

16.5 Throughout 2008 and 2009, TIE produced four-weekly MUDFA Contract Review Reports. The review report for the period to 20 June 2008 noted that the latest construction programme indicated completion by November 2008 which conflicted with the Infraco works by 2 weeks⁸⁴⁷. The review report for the period to 20 July 2008 noted that significant focus had been placed on enabling works for both Haymarket and the Mound which were critical to the planned commencement of the Infraco works in January 2009 but that completion of the MUDFA works was predicted to be by March 2009, which potentially conflicted with Infraco in a number of areas. From that time on there was increasing concern in relation to the problems that might arise as a result of the potential overlap between the MUDFA and Infraco works.

16.6 The MUDFA works continued throughout the rest of 2008. TIE's MUDFA Contract Review Report for the period ending on 4 January 2009 noted that progress in the period had been affected by the embargos within the city centre and Leith Walk/Constitution Street and the two week shutdown for Christmas⁸⁴⁸. The overall performance for phase 1a was 58% of utilities diversions undertaken against 82.4% that had been planned by that stage.

⁸⁴⁶ Witness statement of John Casserly TRI00000111, page 37

⁸⁴⁷ CEC01302950

⁸⁴⁸ CEC01153420

16.7 In June 2008, TIE became concerned by Infraco's lack of mobilisation⁸⁴⁹. Steven Bell thought this was because Infraco had changed some of its supply chain and selected sub-contractors to do packages but also agreed that there was a legitimate issue that design information was not available⁸⁵⁰. Martin Foerder thought TIE misunderstood the lack of signing of formal contracts with sub-contractors for a lack of progress, when in fact Infraco had sub-contractors on board through letters of intent; it had not entered formal contracts because there was not enough work for them to start doing because a lack of agreed scope and programme as a result of the lack of detailed design drawings and continuing MUDFA works preventing access to the sites. Mr Foerder's view that what TIE was asking for by way of work to "*mitigate*" the potential consequences of the delay to the programme by undertaking works elsewhere (such as on the off-street section) not in accordance with Infraco's planned programme actually amounted to a request to "*accelerate*" the works not to "*mitigate*"⁸⁵¹.

16.8 In June and July 2008, Infraco issued a number of technical queries to SDS but commenced work on Leith Walk and tried to work around MUDFA contractor who was still on site⁸⁵². Richard Walker referred to these as "*goodwill works*" because he had agreed with Willie Gallagher that work would have to commence before TIE could go back to the Council and ask for any more money or time because of the changes

⁸⁴⁹ DLA00001673

⁸⁵⁰ Witness statement of Steven Bell TRI00000109, page 84

⁸⁵¹ Transcript of oral evidence of Martin Foerder 5 December 2017, page 183:6- 8

⁸⁵² Witness statement of Richard Walker TRI00000072 pages 50 to 52; transcript of oral evidence of Martin Foerder 5 December 2017, pages 23 to 127

from the contract that had become inevitable and without going through the change process under clause 80.13 of the Infraco contract⁸⁵³. Infraco complained that it could not progress without further information and drawings from SDS and there was a dispute about who was going to pay SDS for the redesigns⁸⁵⁴. It later decided to stick strictly to the terms of the contract and refuse to work if the MUDFA contractor was still on site or if there were disputed INTCs.

Notification of changes under the Infraco Contract

- 16.9 During the course of May, June and July 2008, Infraco issued approximately 50 Infraco Notices of Tie Change (INTCs) in relation to *inter alia* structural changes at Russell Road and Gogarburn and accommodation works at the Hilton car park. TIE rejected the INTCs⁸⁵⁵.
- 16.10 Issues in relation to the notification of changes under the Infraco contract commenced after Infraco intimated an application for payment in relation to various Notified Departures in September 2008.
- 16.11 In September 2008, Infraco suggested amending the Infraco contract to allow Infraco to implement urgent changes without going through the procedure set out in Clause 80 of the Contract. There were discussions in relation to this but nothing was agreed⁸⁵⁶.
- 16.12 In late September 2008, Infraco submitted an application for payment in relation to various claims for Notified Departures. According to Richard

⁸⁵³ Witness statement of Richard Walker TRI00000072, page 49

⁸⁵⁴ Witness statement of Richard Walker TRI00000072, page 54

⁸⁵⁵ Witness statement of Richard Walker TRI00000072, pages 49 to 50

⁸⁵⁶ Witness statement of Richard Walker TRI00000072, pages 50 to 52

Walker this primarily related to the work undertaken with and around the utility contractor in Leith Walk in a piecemeal fashion rather than doing it efficiently⁸⁵⁷. Infraco submitted a repeated application for payment for these works in October 2008. Mr Walker said that he informed Willie Gallagher that if this could not be resolved Infraco would have no alternative than to strictly abide by the terms and conditions of the contract, particularly in respect of the change control (Notified Departure) process⁸⁵⁸. Infraco's position was that the Notified Departure was justified because it was TIE's responsibility to the Infraco contractor to ensure that the MUDFA contractor was out of the way.

16.13 At about the same time Willie Gallagher resigned from TIE and David Mackay became interim Chief Executive of TIE. Richard Walker thought that relations between TIE and Infraco deteriorated after that point.

16.14 When INTCs were submitted, TIE complained about the delays in providing estimates for value of the TIE change notices by Infraco and Infraco had to ask for extensions of time to submit estimates from the time stipulated in the contract. TIE complained that the estimates provided were excessive and also lacking in specification. As matters progressed TIE and Infraco were exchanging hundreds of letters and the process was becoming unmanageable. TIE complained that Infraco was not progressing with work while the disputes were resolved but Infraco claimed that in terms of Clause 80 of the Contract it was

⁸⁵⁷ Witness statement of Richard Walker TRI00000072 pages 51 to 52

⁸⁵⁸ Witness statement of Richard Walker TRI00000072 pages 52 to 53

prohibited from doing so. This was the start of the disagreements that eventually led to the DRPs discussed at section 19.

17. **Princes Street**

Summary

- 17.1 The Princes Street Dispute (PSD) arose in early 2009. The PSD arose out of the parties' differing views on whether an instruction was required for works under the main (Infraco) contract. TIE was of the opinion that Infraco was obliged to undertake the works. Notably Infraco had undertaken other works without ceasing work. In the Council's submission Infraco awaited these high profile works before 'testing' the requirements under the Contract. In addition Infraco waited until the works were due to commence before refusing to undertake the works.
- 17.2 The ceasing of the works caused media attention and as a result the Council was forced into negotiations. It was suggested by Infraco that the dispute was restricted to works valued in the region of £1,500 however Infraco insisted upon a significant alterations in payment under a supplemental agreement which increased the cost of the contract considerably. The supplementary agreement required payment at a demonstrable cost basis plus an uplift of 17.5% which, unsurprisingly, were in excess of the agreed rates upon entering the Contract.
- 17.3 The Council's principal submission is that the PSD was an opportunistic and orchestrated attempt to secure additional monies available for the project. In addition the Council submits that the agreeing of a supplementary agreement, rather than creating a stable working relationship, was the catalyst or encouragement for further claims by Infraco.

Causes and Scope

- 17.4 The Princes Street Dispute (“the PSD”) arose during 2009 after contract works had been commenced. Infraco advised by email dated 18th February 2009 that it was not obliged to commence the works.⁸⁵⁹ This was due to Infraco insisting that it required an instruction to undertake the works. The assertion that an instruction was required was not brought to the attention of TIE until one week prior to the intended commencement of the works in February 2009⁸⁶⁰. TIE disagreed with the views of Infraco insofar as the works were part of the works under the contract, and accordingly did not require an independent instruction.
- 17.5 The principal issue in dispute between the parties was a change providing that the option of use of a westbound bus lane was required. TIE was firmly of the view that Infraco was required to undertake the works. Dennis Murray’s statement indicates that:

“There were many obstructions on the Princes Street Section of works and BDS considered that many would result in Notified Departures. My recollection is that BSC did not think that the works could be carried out without interruption and were not prepared to carry out the Princes Street works until an arrangement was in place to protect them.”⁸⁶¹

- 17.6 Accordingly the PSD arose due to alternative interpretations of the contract including the change mechanism and pricing. As noted

⁸⁵⁹ CEC00867153

⁸⁶⁰ Witness statement of James Donaldson TRI00000033, page 14

⁸⁶¹ Witness statement of Dennis Murray TRI00000063, page 32

above the PSD arose immediately before the works were due to commence and by which time:

“...a significant amount of the traffic management works and diversion preparations had been implemented.”⁸⁶²

17.7 Stephen Bell notes that the works to Princes Street were high profile works and had been prepared and enabled over a period of three months⁸⁶³. It is therefore submitted that the decision by Infracore to refuse to undertake the works was intentionally made at (or delayed until) a stage to maximise the pressure on TIE and jeopardise delivery of the project. This was a view shared by the political membership of the Council. Gordon Mackenzie highlighted that:

“...the contractor was trying to put pressure on TIE and Council particularly to cough up more money. The view being put across was that Princes Street was, you know, the foremost street in Scotland and this was an opportunity to put the Council under a lot of pressure...contractor trying to get a better deal than they were entitled to”⁸⁶⁴.

17.8 Alastair Richards identified that the tram lines were not being installed as Infracore

“...took the view that each and every time they would encounter a utility they would stop work and be entitled to compensation waiting whilst a local utility was designed and then undertaken. This was considered to

⁸⁶² Witness statement of Susan Clark TRI00000112, page 47

⁸⁶³ Witness statement of Steven Bell TRI00000109, page 107

⁸⁶⁴ Transcript of oral evidence of Gordon Mackenzie 1 November 2017, page 52:3-9

*be an opportunistic interpretation/exploitation of what they considered were their rights under the contract*⁸⁶⁵.

17.9 Richard Jeffrey's evidence was that:

*"...Princes Street had already been closed to traffic and converted into a building site..."*⁸⁶⁶.

17.10 Bilfinger's written submissions on the issue of the PSSA are found at pages 94 to 109. The submissions state that *"The Princes Street dispute arose relatively soon after the events in the summer of 2008..."*. It is submitted that if this were accurate in respect of the timing, this would only lend support to the suggestion that Bilfinger waited until the high profile works were to be undertaken before refusing to work under the Contract. It is suggested by Bilfinger that to commence the Princes Street works would have meant *"...taking on a huge commercial risk exposing itself to a very substantial financial liability..."*⁸⁶⁷. However any liability would accrue in a piecemeal fashion and not accrue as a lump sum. Rather, it is submitted that the timing was intentional, and reflected the attitude of Bilfinger, which is reinforced by Bilfinger's own submission that Infracore was not willing, to undertake the works, rather than being unable to do so⁸⁶⁸. Bilfinger cites the hostility of David Mackay as a reason which clearly is not a contractual issue or a matter giving rise to any financial liability. It is suggested by Bilfinger that the project should have been delayed. If Bilfinger's evidence that it was

⁸⁶⁵ Witness statement of Alastair Richards TRI00000116, page 22

⁸⁶⁶ Transcript of oral evidence of Richard Jeffrey 8 November 2017, page 24:12-13

⁸⁶⁷ Page 96 of the written submissions of Bilfinger dated 27 April 2018

⁸⁶⁸ Page 96 of the written submissions of Bilfinger dated 27 April 2018

entitled not to undertake works is to be accepted, then Bilfinger would have held the authority to have delayed works. The reality is that Bilfinger was content to undertake the works providing more sums were paid under the contract, which TIE agreed to reluctantly and under pressure⁸⁶⁹, as more fully discussed below. Siemens' submissions highlight that regardless of the dispute off street works could have been progressed by Bilfinger as an alternative to the Princes Street works⁸⁷⁰.

Attempts to Resolve

17.11 Stephen Bell of TIE was of the opinion that the failure to undertake the works was an attempt to obtain additional sums of between £50M and £80M. In his statement Mr Bell indicates that:

“...BB then announced they were not going to do the Princes Street work. They dressed that up, in argument, around particular instructions that they had not agreed, or otherwise, but it was certainly perceived by us that it was primarily related to the fact that they had just delivered this ultimatum around this significant price increase. It was just another key lever to intensify the focus on the project and on TIE to try and extract an agreement to pay these additional monies”⁸⁷¹.

17.12 Mr Bell's evidence is that TIE was prepared to meet the value of the change and indicated that Infracore was not entitled to refuse to undertake the works⁸⁷². As Mr Bell indicates in his statement “There

⁸⁶⁹ Page 100 of the written submissions of SETE dated 27 April 2018

⁸⁷⁰ Paragraph 118 on page 45 of the written submissions of Siemens dated 27 April 2018

⁸⁷¹ Witness statement of Steven Bell TRI00000109, page 106

⁸⁷² CEC00942802

*required to be demonstrable proven costs...*⁸⁷³. By email dated 19th February 2009 Infraco indicated it would undertake the works on the basis of being paid on a demonstrable cost basis. However the offer by Infraco was made as a gesture of goodwill rather than contractual obligation⁸⁷⁴. Infraco indicated by letter dated 23rd February 2009 that contrary to TIE's understanding the contract was not fixed price and that Schedule 4 made express provision for TIE's liability for changes⁸⁷⁵.

17.13 In an attempt to make progress Mr David Mackay wrote to Siemens on the understanding that Siemens was also "*fed up*" with BB by this stage in the contract. Mr Mackay did so in the hope that Siemens may wish to part company with BB⁸⁷⁶. This communication with Siemens was subsequently referred to by BB in their letter of 23rd February⁸⁷⁷. The Council submit that this episode of the PSD would clearly not have assisted the already volatile relationship between TIE and BB.

17.14 In contrast to the position above the evidence of Richard Walker of Infraco highlighted the failure of TIE to agree the sums of £1,500 in an estimate of works. As Mr Walker indicates in his statement⁸⁷⁸ Infraco viewed the failure of TIE to meet the cost of £1,500 as contractually entitling Infraco not to undertake the Princes Street works. In the Council's submission it is clear that the suggestion that the PSD was restricted to such a modest level of quantum is wholly lacking in candour when the agreed terms of the Princes Street Supplementary

⁸⁷³ Witness statement of Steven Bell TRI00000109, page 107

⁸⁷⁴ CEC00942802

⁸⁷⁵ CEC00942804

⁸⁷⁶ Witness statement of David Mackay TRI00000113, page 78

⁸⁷⁷ CEC01009884

⁸⁷⁸ Witness statement of Richard Walker TRI00000072, page 57

Agreement ("PSSA") are considered, in particular the extent of the agreed changes and sums.

17.15 Furthermore as Martin Foerder highlighted, the true concern of BB was:

*"Our concern was that if we proceeded to carry out all of these works without agreement on the impact of these changes we would end up in a very bad situation financially"*⁸⁷⁹.

17.16 Reinforcement of the true motives is exposed when consideration is given to Infraco insisting that without the PSSA the contract was unworkable, as stated by Mr Walker. Mr Walker states that clause 80.13 prevented the works being undertaken and not due to a refusal to undertake the works⁸⁸⁰. This is inconsistent with the practice of Infraco until February 2009 whereby works were undertaken. As indicated in the evidence of Dr Keysberg who indicated in his statement that:

*"...it would be a complete mess if we had to progress this (discovery of utilities) under the contract regime by raising a Notified Departure...this was the first occasion when we refused to carry out work..."*⁸⁸¹.

17.17 Accordingly it was not until a few days before the most significant on street works that Infraco chose to cease works, and therefore took advantage of a contractual mechanism/provision without notice and contrary to all prior works under the contract. In the circumstances it is submitted that Dr Keysberg's evidence that the only two options were

⁸⁷⁹ Witness statement of Martin Foerder TRI00000095, page 15

⁸⁸⁰ Witness statement of Richard Walker TRI00000072, page 58

⁸⁸¹ Witness statement of Jochen Keysberg TRI00000050, pages 18 to 19

ceasing the works or agreeing to the requirements of Infraco⁸⁸² is not an accurate statement. The work could have been undertaken as had been done previously.

17.18 The evidence of James Donaldson was that the project should have been delayed a year⁸⁸³. A delay was not pursued by either party and Infraco sought the additional costs ultimately agreed in the PSSA.

17.19 Infraco was aware that its failure to undertake the works after the closure of Princes Street was attracting a “*huge amount of media attention*”⁸⁸⁴.

Intervention by John Swinney

17.20 Mr David Mackay indicates in his statement that:

*“I had been sent for by the Deputy First Minister, John Swinney, and in very clear language I was told to get it sorted out. I spoke to him about our values and standards and my values and standards and the fact that we were charged with looking after the public purse. I told him the only way to break this impasse was to pay more and that we had already paid for Princes Street in the agreements. I was told to get it sorted out and to break the impasse”*⁸⁸⁵.

⁸⁸² Witness statement of Jochen Keysberg TRI00000050, page 20

⁸⁸³ Witness statement of Jim Donaldson TRI00000033, page 15

⁸⁸⁴ Witness statement of Martin Foerder TRI00000095, page 15

⁸⁸⁵ Witness statement of David Mackay TRI00000113, page 79

17.21 Mr Swinney acknowledges that he became aware of the PSD through briefings by Transport Scotland officials⁸⁸⁶. Mr Swinney describes how:

“...we would be pressing the Council and TIE to resolve these issues and we would be getting updates from TIE...A lot of time was swallowed up trying to resolve the dispute”⁸⁸⁷.

17.22 Mr Swinney indicates that TIE stated that it had “a strong position” however that Transport Scotland was providing a “less optimistic assessment”⁸⁸⁸.

Negotiations

17.23 All parties met to try and resolve the PSD, including TIE, BB, CAF and Siemens⁸⁸⁹. BB attended with Pinsent Masons to enable any drafting to be undertaken. Infracore sought to apply a series of percentages to the actual costs. TIE disagreed with this as being appropriate⁸⁹⁰ and the parties debated the issues at a mediation process.

17.24 A percentage based solution was achieved at a lower percentage than sought by TIE. DLA was advising the Council on the PSD⁸⁹¹.

17.25 Mr David Mackay (of TIE) was not prepared to meet the demands of a “65% premium on top of the preliminaries”⁸⁹². Mr Mackay discussed with Mr Aitchison the conversation he had with Mr Swinney. Mr

⁸⁸⁶ Witness statement of John Swinney TRI00000149, page 64

⁸⁸⁷ Witness statement of John Swinney TRI00000149, page 65

⁸⁸⁸ Witness statement of John Swinney TRI00000149, page 65

⁸⁸⁹ Witness statement of Martin Foerder TRI00000095, page 15

⁸⁹⁰ Witness statement of Dennis Murray TRI00000063, page 33

⁸⁹¹ Witness statement of Gill Lindsay TRI00000121, page 65

⁸⁹² Witness statement of David Mackay TRI00000113, page 78

Mackay did so as Mr Aitchison would ultimately be the authorising officer of any agreement with Infraco. Mr Mackay notes in his statement that Alastair Richards was the individual who “*raised the question of paying on the demonstrable cost basis supported by timesheets and material sheets*”⁸⁹³.

17.26 Alastair Richards was “*semi-independent of those directly involved (in the PSD)*”⁸⁹⁴. Mr Richards notes in his statement that he was engaged to take a view on, and support, the negotiations. Mr Richards notes that “*BBS effectively had tie and the City Council to ransom*”⁸⁹⁵.

17.27 Mr Mackay did not see any justification for paying but under instruction he contacted Dr Keysberg. Dr Keysberg disputed ever having said to Richard Jeffrey that the contract “*was a great contract for us, it allows us to hold the client to ransom*”⁸⁹⁶. However Dr Keysberg did think that he may have more likely stated “*if we don’t move on and find alternative scenarios for this contract, and we start working in the city, the city will be blocked for the mechanism I explained and the project will never be built...*”⁸⁹⁷.

17.28 In the Council’s submission the more significant issue for the Inquiry is the impact of what occurred as a consequence of the actions by Infraco rather than the particular words used, although the Council maintains that the motive of BB was opportunistically and cynically to use a high

⁸⁹³ Witness statement of David Mackay TRI00000113, page 79

⁸⁹⁴ Witness statement of Alastair Richards TRI00000116, page 22

⁸⁹⁵ Witness statement of Alastair Richards TRI00000116, page 22

⁸⁹⁶ Transcript of oral evidence of Jochen Keysberg 16 November 2017, page 50:7-18

⁸⁹⁷ Transcript of oral evidence of Jochen Keysberg 16 November 2017, page 51:4-8

profile location, at the last moment, in order to secure monies to which Infraco would not otherwise have been entitled to.

- 17.29 Donald McGougan's evidence is that it was necessary to consider the dispute not from the narrow view of the Council wishing to keep a bus lane open but rather by placing the PSD:

*"...into the context of the wider areas of dispute. This included the contractors' lack of mobilisation, the emerging lack of agreement over the contract conditions in relation to the responsibility for costs of design changes...In my view the contractor was able to use Princes Street to gain leverage in terms of other areas of the works across the whole project"*⁸⁹⁸.

Princes Street Supplemental Agreement

- 17.30 The dispute was resolved through the entering into of the Princes Street PSSA⁸⁹⁹. The PSSA was agreed by David Mackay (of TIE) and Dr Keysberg following discussions over a number of weeks. Ultimately the PSSA was agreed at a meeting on 20 March 2009. The initial agreement was subject of subsequent iteration to incorporate the comments of other parties such as Siemens and CAF⁹⁰⁰.

- 17.31 Mr Mackay indicates that the PSSA was achieved by agreeing to:

"put our senior teams and our lawyers into a locked room until they came up with a solution which we would either approve or reject in due

⁸⁹⁸ Witness statement of Donald McGougan TRI00000060, page 67

⁸⁹⁹ CEC00302099

⁹⁰⁰ Witness statement of Martin Foerder TRI00000095, page 16

*course. The process took a few days and Transport Scotland were kept updated. They did and having agreed a supplementary agreement, which we both signed, the Princes Street dispute was over and they started to work*⁹⁰¹.

17.32 It was agreed that Infraco would carry out the Princes Street works at demonstrable cost (plus overhead and profit percentages etc). Ultimately this was fixed at 17.5%. Stephen Bell identifies that the demonstrable cost plus overhead and profit percentages required Infraco:

*“..to demonstrate what resources and the weights and prices they were being charged by their sub-contractors, plus...an element of overhead in profit...”*⁹⁰².

17.33 Martin Foerder identifies that the PSSA provides that the work was to be carried out by the subcontractors at rates within the PSSA⁹⁰³ rather than rates under the Contract. It is submitted that this was but one of Infraco's attempts to erode what had been agreed in 2008.

17.34 It was reported to Transport Scotland that TIE did not anticipate additional costs arising from the PSSA. The daily bulletin report of 23 March 2009 states:

“The Supplemental Agreement does not involve paying Bilfinger any additional moneys but gives them greater reassurance and confidence that TIE is not going to be difficult about any additional costs caused by

⁹⁰¹ Witness statement of David Mackay TRI00000113, page 79

⁹⁰² Witness statement of Steven Bell TRI00000109, page 108

⁹⁰³ Witness statement of Martin Foerder TRI00000095, page 16

*unforeseen ground conditions....At this stage TIE doesn't anticipate that this will lead to grater costs*⁹⁰⁴.

17.35 This was not a view shared by Transport Scotland who thought TIE was being overly optimistic⁹⁰⁵. By April 2009 TIE was of the view that the PSSA was made at *"no extraordinary additional cost"*⁹⁰⁶.

17.36 The additional costs of the PSSA were expected to be included within the risk allowance as identified by Stephen Bell:

*"(the cost) would be greater than the basic sum but we would have expected elements of the risk allowance to address certain things in this area of work....we would have expected the overall liability to be higher in any event"*⁹⁰⁷.

17.37 TIE was satisfied with the appropriateness of the PSSA as identified by Stephen Bell in his statement:

"The obligations to deliver a tram system under the Infraco contract that complied with the Employer's Requirements still held. There was a change in the mechanism by which an element of the works are valued and paid...Therefore the Infraco were going to be entitled under the contract to a change in to the construction works price for that element of the work. We had reviewed that it and considered it appropriate.

⁹⁰⁴ TRS00005103

⁹⁰⁵ Witness statement of John Ramsey TRI00000065, page 22

⁹⁰⁶ TRS00005108

⁹⁰⁷ Witness statement of Steven Bell TRI00000109, page 108

*On balance, we thought it was an acceptable way to take it forward...*⁹⁰⁸.

17.38 Mr Richards notes that the costs were higher than the original Infraco price, but not as high as it would have been if Infraco had continued to sit and wait. Mr Richard Jeffrey's evidence was that "*I don't believe it was a good outcome*" and agreed that the cost was much more than had been anticipated. It is submitted that the days of negotiations were not an attempt to make the contract workable to enable Infraco to undertake the works as suggested by Mr Walker but rather to secure more monies not otherwise available under the Contract. If Mr Walker's assessment was correct there is no reason why a mechanism to undertake the works at the costs under modified change provisions could not have been agreed.

17.39 The Council submits that the suggestion that the PSSA was to resolve a dispute over payment of £1500 identified in evidence above, is wholly lacking in candour. David Anderson of the Council had expected "*the additional costs to be low single millions at worst*"⁹⁰⁹. Stewart McGarrity identified that it was also hoped that the PSSA would "...*help with fostering improved engagement*"⁹¹⁰. Therefore the PSSA was intended not only to avoid any further stalling by Infraco but also it was hoped to be the beginning of a better and improved working relationship.

⁹⁰⁸ Witness statement of Steven Bell TRI00000109, page 113

⁹⁰⁹ Witness statement of David Anderson TRI00000108, page 52

⁹¹⁰ Witness statement of Stewart McGarrity TRI00000059, page 231

17.40 Mr Jeffrey's understanding that the PSSA did not create risk is not what transpired⁹¹¹.

17.41 The Council submit that the PSD was an intentional and orchestrated attempt to re-negotiate terms of the contract. The reasons for reaching this view are the timing and the scope of the works. The timing, as noted above was immediately prior to the works commencing. Princes Street was arguably the most significant of all the on-street works.

⁹¹¹ Transcript of oral evidence of Richard Jeffrey 8 November 2017, page 68:3- 13

18. **Events in 2009 following PSSA**

Summary

18.1 Throughout 2009 similar issues persisted in relation to the Project as referred to in section 16 of these submissions. MUDFA works were behind schedule and were alleged to be impeding Infraco commencement of the Infraco works. In mid 2009 TIE decided to remove Carillion and re-let the remaining parts of the MUDFA works to other companies.

18.2 The issuing of SDS designs was also significantly behind schedule and remained so throughout 2009. This was accentuated by the number of changes for which re-designs were required and the contractual interpretation dispute between Infraco and TIE about this.

18.3 In late 2009 the issues in relation to the difference in interpretation of the Infraco contract started to come to a head after Infraco sought payment for INTC changes.

18.4 TIE considered its options and decided to pursue a strategy of enforcing the contract and then entering into formal DRP processes.

Progress of MUDFA (including reasons for difficulties) and Removal of MUDFA contractor

18.5 Similar problems persisted with the MUDFA contractor in 2009 as had been encountered previously. In March 2009, Carillion complained that it was paying its sub-contractors more than it was being paid itself

under the MUDFA contract and was therefore losing money. John Casserly believed that this was the case⁹¹². TIE settled a claim by Carillion in relation to delay and disruption for £1.2m and granted an extension of time to substantial completion date of the MUDFA works to April 2009 and a Longstop Date of 3 August 2009.

18.6 By May 2009 TIE had decided to try to close down the MUDFA contract by the end of July 2009 and transfer the remaining diversions to another utilities contractor because it thought Carillion had been losing money and was reluctant to plough further resources into completing the works under a challenging contract⁹¹³. Richard Jeffrey's evidence was that TIE had concerns about Carillion's performance, quality and cost but it was particularly concerned about Carillion's commitment and the decision to try to replace Carillion was more about trying to ensure the work was completed in a timely manner rather than trying to reduce the price of the contract⁹¹⁴. TIE ran a competition for other suppliers and Clancy Docwra and Farrans were appointed.

18.7 The TPB Minutes of 21 October 2009 referred to 98% of the Carillion works having been completed once sections 1 and 7 (at either end of the line) had been taken back by TIE to be re-let⁹¹⁵.

18.8 It is submitted that the decision to terminate the MUDFA contract and re-let the works to alternative contractors was largely successful. The new contractors completed the majority of the outstanding works

⁹¹² Witness statement of John Casserly TRI00000111 page 50

⁹¹³ Witness statement of Steven Bell TRI00000109 page 115

⁹¹⁴ Witness statement TRI00000097 of Richard Jeffrey page 13, paragraphs 64-65

⁹¹⁵ CEC00681328, page 7

although in some areas that were deemed too complicated, Infraco was later responsible for co-ordinating the final utilities diversion works in co-operation with sub-contractors.

Progress of SDS (including reasons for difficulties)

- 18.9 On 23 January 2009, Infraco intimated a claim to TIE for SDS' failure to issue Issued for Construction Drawings (IFC) by the dates identified in the programme⁹¹⁶.
- 18.10 It is submitted that the delays in SDS producing the requisite detailed designs continued to be a problem for the Project throughout 2009. This was intimately linked to the major dispute that had broken out between the parties about the interpretation of the Infraco contract and what constituted normal design development and how, when and by whom changes could be instructed.
- 18.11 The previous problems with the delays in SDS issuing drawings and the concerns over who would be responsible to pay them for redesigns persisted in 2009.

Progress of Infraco works (including reasons for difficulties)

- 18.12 On 9/10 February 2009 Infraco and TIE met to discuss the issues between them. By then there had been approximately 250 change notices intimated. Infraco said that it estimated that costs would end up being approximately £50-80m more than in the contract on the basis of estimated increase of £20m of direct costs of notified departures, £20m

⁹¹⁶ CEC01182823

for and extension of time to the programme and £10m for delay and disruption. Steven Bell strongly refuted any suggestion by Richard Walker that representatives of TIE had known about that sort of level of increase before the contract was signed⁹¹⁷. The meeting did not resolve the problems⁹¹⁸. Subsequently the dispute in relation to Princes Street was dealt with separately leading to the PSSA referred to above.

18.13 An informal mediation took place between 29 June 2009 and 3 July 2009. The issues parties considered included Value Engineering; the potential for further On Street Supplemental Agreements; Off Street Issues: including, Gogarburn bridge, Carrick Knowe Bridge and Depot; Misalignments between Infracore Proposals and SDS Design, Hilton Hotel car park; Evaluation of Change, Evaluation of Extensions of Time and Agreement on BDDI Drawings. No agreement was reached.

18.14 Discussions continued in the second half of 2009, in particular in relation to the on-street works. Parties met on 6 October 2009, and thereafter, to explore the possibility of using the PSSA as a template for a wider on-street supplemental agreement. Richard Walker thought it was rejected by TIE because it said it would be contrary to EU procurement rules. He could not understand why the proposal was any different from the PSSA in that regard.

Options considered and Strategy by TIE

⁹¹⁷ Witness statement of Steven Bell TRI00000109 page 105

⁹¹⁸ Witness statement of Richard Walker TRI00000072 pages 55-56

18.15 A joint meeting of the Tram Project Board and the TIE Board on 8 July 2009 considered the options with the preferred option being to adopt a formal contractual approach⁹¹⁹. This led to TIE issuing hundreds of letters to Infraco and insisting on audits being carried out. Richard Walker said TIE was “*auditing us to death*”⁹²⁰. It also led to the decision to enter into the formal DRP process. TIE took legal advice from DLA and Richard Keen QC in relation to the potential DRPs. It also appointed McGrigors LLP in preparation for the DRPs and in late 2009 Tony Rush was appointed as a consultant because of his extensive experience in relation to construction contract disputes.

DRP processes

18.16 As noted above an informal mediation took place between TIE and Infraco between 29 June and 3 July 2009 but was unsuccessful.

18.17 On 29 August 2009 the TPB discussed the matters that had been chosen to propose for formal DRP. These had been chosen as they were high value and high risk delay items and their resolution should give clarity on the points of principle in dispute between the parties which could be used over the other areas of disagreement⁹²¹. The items were:

18.17.1 Tranche 1: Extension of Time 1 and Hilton Hotel car park

18.17.2 Tranche 2: BDDI Gogarburn Bridge and BDDI Carrick Knowe Bridge

⁹¹⁹ CEC00783725

⁹²⁰ Witness statement of Richard Walker TRI00000072 page 66

⁹²¹ Witness statement of Susan Clark TRI00000112 page 52

18.17.3 Tranche 3: BDDI Russell Road Bridge, BDDI Earthworks in Section 7/Gogar to the Airport and Value Engineering

18.17.4 Tranche 4: to be notified, but encompassed Extension of Time 2 and SDS

18.17.5 Tranche 5: Edinburgh Park valuation, had been agreed at £50k without the need for DRP, against a claim of £450k

18.18 At page 105 of the SETE written submissions, it is asserted that *"nobody pointed out to TIE at that time [the second half of 2009] that PA1 was fundamentally flawed or that the concept of normal design development was redundant on a literal reading"*. Shortly after they had been first instructed, McGrigors LLP produced 2 papers in August 2009 in relation to the challenge sessions for Gogarburn Bridge (24 August 2009)⁹²² and Carrick Knowe Bridge (26 August 2009)⁹²³. The words at the end of Clause 3.4. of Schedule part 4 are quoted, and the paper in relation to Gogarburn states at paragraph 6:

"...tie's position is that the drawings do not go beyond normal design development and in particular there are no changes of design principle, shape and form and outline specification".

18.19 At paragraph 8 of the paper, it is stated:

"Whether a Notified Departure has occurred is a question of fact and specifically engineering judgement as to whether the IFC drawings represent normal design development and in particular do not reveal

⁹²² CEC00805685

⁹²³ CEC00805783 and CEC00805739

changes of design principle, shape and form and outline specification. In the context of adjudication or litigation proceedings expert engineering evidence would properly fall to be adduced and would be highly influential".

18.20 The paper in relation to Carrick Knowe stated "*The comments in respect of 5a [Gogarburn] are entirely applicable and are not narrated again*".

18.21 The same comments are referred to in the paper on Russell Road Retaining Wall dated 4 September 2009⁹²⁴. _

18.22 The foregoing comments highlighted in clear terms that the question of whether design development from BDDI to IFC constituted a Notified Departure depended on there being no changes of design principle, shape and form and outline specification.

18.23 The footnote to the quote from McGrigors' paper dated 16 October 2009⁹²⁵ referred to at page 105 of the SETE submissions states "*See McGrigors' comment papers on DRP cases 5A,5B and 5C*". Paragraphs 30 and 31 of the paper make it clear that a Notified Departure is triggered where the facts and circumstances differ from the Base Case Assumptions.

18.24 Shortly thereafter, and as referred to in the witness statement of Brandon Nolan⁹²⁶ the Hunter decisions on Gogarburn and Carrick Knowe "*...held that the development of the design from BDDI to IFC*

⁹²⁴ CEC00805917

⁹²⁵ CEC00797337

⁹²⁶ Answer 19 on page 10 of the witness statement of Brandon Nolan TRI00000114

came within the ambit of the final sentence of Pricing Assumption 1 as a matter of fact".

18.25 In this context, and contrary to what is asserted on behalf of SETE⁹²⁷, TIE did not instruct McGrigors "*to effectively audit the evolution of Schedule 4*". In the report of 23 March 2010⁹²⁸, McGrigors referred to a factual investigation within the context of establishing whether something could be said to have "gone wrong" with the wording of Pricing Assumption No. 1⁹²⁹.

18.26 The DRP processes are discussed in more detail at section 19 of these submissions.

⁹²⁷ Final bullet point on page 70 of the written submissions of SETE dated 27 April 2018

⁹²⁸ CEC00591754 – Report on Certain Contractual Issues concerning Edinburgh Tram Project

⁹²⁹ See for example paragraph 8.3 of the report of 23 March 2010

19. **DRP events**

Summary

19.1 This is a chronological account of the DRP processes (principally adjudications) which dovetails with the summary contained in chapter 1. The background events have been set out by the ETI in the Statement of Main Documents and Events, the most relevant parts of which are summarised.

19.2 Two key points are identified:

- (a) Lack of clarity about what the purpose was of referring disputes to adjudication and then, when results began to emerge, not properly addressing consequences.
- (b) TIE did not give a full and accurate picture to the Council about the outcome of the adjudications. The matters were being reported over-optimistically and Council officers were seeing only one side.

Dispute Resolution Procedure

19.3 The part played by the Dispute Resolution Procedure (“DRP”) in the outcome of the Project relates to a significant extent to the various adjudications which took place between 2009 and 2011. The most relevant of these and the decisions reached have already been addressed and summarised in chapter 1 at section 2. As has already been said, these decisions may have confirmed the deficiencies in

Schedule part 4 and clause 80 which led to the increases in cost and the delays to the Project but the adjudication decisions did not cause those consequences because they were the result of the particular contractual provisions entered into by TIE in the Infraco contract. The issues raised in this part of the submissions for the Council are thus part of the scope for lessons to be learned rather than related to the principal cause of the consequences referred to in the first point in the terms of reference of the Inquiry. Reference is made in this respect to chapter 4 at section 24 of these submissions.

19.4 The background events as set out in the Statement of Main Documents and Events and the most relevant for present purposes may be summarised as follows.

19.5 At the point of agreeing to enter into the Infraco and other contracts, TIE and Council officers received a set of internal approval documents which included a Report on Infraco Contract Suite⁹³⁰. The Report included reference to the DRP procedure and described a process of "*rapid escalation*" through Chief Executive level to mediation, adjudication, or court proceedings.

19.6 A dispute arose in relation to track laying works on Princes Street due to commence in February 2009. By e-mail dated 18 February 2009, Infraco advised that it did not consider itself contractually obliged to start work in Princes Street⁹³¹. TIE formally activated the DRP but this dispute was resolved by agreement and the Princes Street

⁹³⁰ CEC01338851 and CEC01338852

⁹³¹ CEC00867153

Supplemental Agreement (“PSSA”) is dealt with elsewhere in these submissions. A Project Management Panel was set up following the resolution of this dispute although it was recognised that some issues would still require to be dealt with by DRP.

19.7 Between 29 June and 3 July 2009, an informal mediation was held between TIE and Infraco which examined, among other things, the principles of the evaluation of change, the precedence of Schedule part 4, extensions of time and other issues arising between the parties. The taking place of that mediation is consistent with the recognition by the parties at that stage of the potential significance for the future of Schedule part 4.

19.8 On 20 August 2009, the Council received a report which stated that in the absence of agreement between TIE and Infraco, TIE had received the approval of the Tram Project Board to take a more formal contractual approach to resolve the outstanding issues⁹³². The report confirmed that TIE had taken extensive supportive legal and technical advice although it was unreasonable to expect that all adjudication outcomes would be awarded in favour of TIE.

19.9 On 13 October 2009, an adjudication decision was issued by Robert Howie QC in the dispute arising under the Infraco contract in relation to the Hilton Hotel car park⁹³³. On 16 November 2009, John Hunter issued his two adjudication decisions in the disputes arising under the Infraco contract in relation to Gogarburn Bridge and Carrick Knowe Bridge and

⁹³² CEC00738172

⁹³³ WED00000026

which are “the first Hunter Decisions” referred to in chapter 1 above⁹³⁴. On 4 January 2010, Alan Wilson issued his adjudication decision in the dispute arising under the Infraco contract in relation to the Russell Road Retaining Wall Two and which is “the Wilson Decision” discussed above⁹³⁵.

19.10 By letter dated 8 March 2010, Infraco wrote to the Council expressing their concerns about TIE and the lack of meaningful progress to resolving the outstanding disputes, including the fundamental dispute concerning the correct interpretation of the contract⁹³⁶.

19.11 On 18 May 2010, Alan Hunter issued his adjudication decision in the dispute in relation to the Tower Place Bridge which is the Second Hunter Decision discussed above⁹³⁷. On 25 May 2010, T Gordon Coutts QC issued his adjudication decision in the dispute in relation to section 7A - Track Drainage and which is “the Coutts Decision”⁹³⁸. On or about 4 June 2010, Robert Howie QC issued his reasons for a decision, which had been intimated to parties on 1 June 2010, in relation to two preliminary issues in an adjudication concerning Incomplete MUDFA Works⁹³⁹. On 16 July 2010 he intimated his final decision to the parties⁹⁴⁰, and issued his reasons for that decision on 26 July 2010⁹⁴¹ which reasons are mentioned briefly in chapter 1.

⁹³⁴ CEC00479432 and CEC00479431

⁹³⁵ CEC00034842

⁹³⁶ CEC00548728

⁹³⁷ CEC00373726 and CEC00325885

⁹³⁸ TIE00231893

⁹³⁹ BFB00053359

⁹⁴⁰ CEC00310163

⁹⁴¹ CEC00407650

19.12 On 24 June 2010, the Council was provided with an update and a report was provided by the Director of City Development and the Director of Finance⁹⁴². This indicated that the contractual programme remained well behind schedule and that there continued to be serious contractual difficulties with Infraco. In relation to the DRP, the report noted:

*"Although the formal adjudications under the 'Dispute Resolution Procedure' have produced mixed results, the advice received has reinforced tie's interpretation of the contractual position on the key matters under dispute and has also saved circa £11m from the initial claims submitted by BSC... Taking into account matters which have been resolved under the DRP process and changes put forward by BSC concluded outside the DRP process, the sum saved by tie's negotiation of the submitted claims represents over 77% of the sum finally agreed. The outcome of the DRPs, in terms of legal principles, remains finely balanced and subject to debate between the parties".*⁹⁴³

19.13 At this stage, Infraco sent their first "Project Carlisle" proposal to TIE⁹⁴⁴ which proposed to complete the line from the Airport to the east end of Princes Street for a Guaranteed Maximum Price of approximately £433 million and other elements including a shortened list of Pricing Assumptions. The proposal was rejected by TIE who provided a counter-proposal⁹⁴⁵.

⁹⁴² CEC02083184

⁹⁴³ CEC02083184, pages 2 to 5

⁹⁴⁴ CEC00183919

⁹⁴⁵ CEC00221164

- 19.14 On 7 August 2010, Lord Dervaird issued his adjudication decision in the dispute arising under the Infraco contract in relation to the Murrayfield Underpass which is referred to above as "the Dervaird Decision"⁹⁴⁶.
- 19.15 Between 9 August and 12 October 2010, TIE served on Infraco ten Remediable Termination Notices (RTNs) and three Underperformance Warning Notices (UWNs). In response, Infraco denied that the RTNs constituted valid notices and, in some cases, produced Rectification Plans.
- 19.16 By letter dated 11 September 2010, Infraco submitted its second "Project Carlisle" proposal to TIE, in which Infraco offered to complete the line from the Airport to Haymarket for a Guaranteed Maximum Price of approximately £403 million subject to the previously suggested shortened list of Pricing Assumptions⁹⁴⁷. TIE rejected the proposal and responded with a further counter-proposal⁹⁴⁸.
- 19.17 On 22 September 2010, Brian Porter issued his adjudication decision in the dispute arising under the Infraco contract in relation to the Depot Access Bridge S32⁹⁴⁹.
- 19.18 By letter dated 29 September 2010, Infraco advised TIE that it was no longer prepared to carry out "goodwill" works being the works which were the subject of 94 outstanding INTCs. Infraco considered that it

⁹⁴⁶ BFB00053462

⁹⁴⁷ TIE00667410

⁹⁴⁸ CEC00129943

⁹⁴⁹ BFB00053391

was not required to carry out such works under the Infraco contract in advance of receipt of a TIE Change Order or an agreed Estimate⁹⁵⁰.

19.19 On 26 November 2010, Lord Dervaird issued his adjudication decision in the dispute arising under the Infraco contract in relation to Landfill Tax⁹⁵¹. By letter dated 13 December 2010, Robert Howie QC issued his adjudication decision dated 15 December 2010 in a dispute arising under the Infraco contract in relation to the approval of subcontract terms⁹⁵².

19.20 On 2 March 2011, Lord Dervaird issued his adjudication decision in the dispute arising under the Infraco contract in relation to the Payment of Preliminaries⁹⁵³.

19.21 It is not necessary to consider the details of the most relevant of the adjudication decisions which were given in the period in question and the conclusions which may be drawn in relation to the Pricing Assumptions in Schedule part 4, in particular Pricing Assumption No. 1, and the effects of clause 80.13. These have already been addressed at paragraph 2.54 above, which states that "*The significance of these adjudication decisions is that they confirm what ought to have been apparent in respect of Pricing Assumption No. 1 and its relationship with the change mechanism at the time that the Infraco Contract was entered into. Not only did these give rise to potential dispute on every occasion that an IFC design was issued leading to a claim by Infraco it*

⁹⁵⁰ TIE00409574

⁹⁵¹ BFB00053475

⁹⁵² BFB00053482

⁹⁵³ BFB00053489

departed too far from the BDDI design, but it also gave rise to disruption and delay in a situation where an Estimate had neither been provided nor agreed. In a situation where a Notified Departure had occurred, the Dervaird Decision determined that TIE could not issue an instruction requiring the work to be recommenced in terms of clause 80.13 and that is what gave Infraco the ultimate ability to cease to carry out works pending the determination of outstanding disputes."

19.22 There are two aspects of the approach of TIE to the DRP about which the Council would wish to comment. First, it may be said that there was insufficient clarity about what was the purpose of referring disputes to adjudication and then, when results began to emerge, not properly addressing the consequences. It appears that TIE wished adjudication decisions in order to clarify their position under Schedule part 4, and then under clause 80, and the first of these matters was clarified, at least at the adjudication level, in the first Hunter decisions and the Wilson Decision. The latest of these decisions was issued on 4 January 2010. At that stage, TIE might either have acted on that outcome and brought it fully to the attention of the Council for a strategic decision or possibly sought final clarification in the courts. But the officers of TIE did neither and they continued to pursue adjudications. In fairness they did so with the benefit of legal advice.

19.23 The second aspect is that the evidence has demonstrated that officers of TIE did not give a full and accurate picture to the Council about the outcome of the adjudications. There has been substantial evidence about this, and counsel for the selected TIE employees has repeatedly

attempted to draw attention to evidence which might suggest that those in the Council were or ought to have been aware of the true situation regarding DRP. In the light of all of the evidence, it is submitted that these attempts have not been successful.

19.24 The evidence concerning the circumstances in which decisions were taken to initiate and pursue DRP by way of adjudications is extensive. The Council refers to all of that evidence but for the purpose of the submissions on this aspect, reference is made to the following particular passages.

19.25 Richard Jeffrey gave evidence of the circumstances in which the decision was made to adopt DRP and the subsequent legal advice and instructions to counsel.⁹⁵⁴ Steven Bell gave evidence about the events from late 2008 onwards.⁹⁵⁵ He recalled that Andrew Fitchie had suggested that TIE should use the Dispute Resolution Procedure at some point in 2008 but that was not done initially.⁹⁵⁶ David Mackay described the decisions made and said that, in connection with a possible “Plan B”, TIE was relying on advice. He also said that they wanted to roll out as many adjudications as possible to put pressure on Infracore⁹⁵⁷.

19.26 With reference to the adjudication decisions received between late 2009 and early 2011, Steven Bell explained that these had been examined

⁹⁵⁴ Transcript of oral evidence of Richard Jeffrey 8 November 2017, in particular at pages 77:2 to 79:8.

⁹⁵⁵ Transcript of oral evidence of Steven Bell 25 October 2017, page 43:1 onwards

⁹⁵⁶ Transcript of oral evidence of Steven Bell 25 October 2017, page 42:8-25

⁹⁵⁷ Transcript of oral evidence of David Mackay 21 November 2017, pages 110:12 to 118:21, in particular page 117:5-7

with the benefit of legal advice and that there were areas in which TIE still wanted clarification. Although he did not accept the characterisation of winning and losing, he did say that “*there was certainly a number of adjudications where the adjudicator found for the argument of principle with the Infraco*”. He was then asked by Inquiry counsel whether it might be suggested that overall TIE “*tended to lose on liability but have some success on the quantum*” to which he replied that “*That probably is a little bit of over-simplification but there are certain elements of truth in [Inquiry counsel’s] statement*”.⁹⁵⁸ Richard Jeffrey did not get involved in the instructions to counsel concerning the adjudication decisions, it was Stuart Bell and DLA. He said that a strong part of the advice was that the Infraco interpretation could not be correct.⁹⁵⁹ David Mackay said that it was the Dervaird Decision relating to Murrayfield which put doubt in TIE’s interpretation of clause 80.13 (and clause 34.1) and which brought about the decision to cease DRPs.⁹⁶⁰ Richard Jeffery did not accept that the outcome of the adjudications had put TIE in a weaker position but rather had failed to put them in a stronger position.⁹⁶¹ Stewart McGarrity accepted that it was in general true that the adjudication decisions had not gone in TIE’s favour.⁹⁶²

19.27 Of the councillors who had been directors of TIE, Gordon Mackenzie described the approach of TIE officers to initiating DRP. The TIE officers were “*quite bullish*” about TIE’s prospects in initiating the DRP

⁹⁵⁸ Transcript of oral evidence of Steven Bell 25 October 2017, pages 45 to 48, in particular page 46:24 to page 47:18

⁹⁵⁹ Transcript of oral evidence of Richard Jeffrey 8 November 2017, pages 79:1 to 80:17

⁹⁶⁰ Transcript of oral evidence of David Mackay 21 November 2017, page 136:13- 19

⁹⁶¹ Transcript of oral evidence of Richard Jeffrey 9 November 2017, page 64:6- 16

⁹⁶² Transcript of oral evidence of Stewart McGarrity 12 December 2017, page 190:20- 22

and there was no discussion about a Plan B. Having sought what were the first Hunter Decisions, TIE carried on despite those decisions being unfavourable.⁹⁶³ Phil Wheeler likewise did not recall any discussion about what would happen if TIE was to be unsuccessful in DRP. He agreed that there was to be a review of the first Hunter Decisions but could not recall being given the result of that review. The outcome of the DRPs had been described as “*finely balanced*”⁹⁶⁴.

19.28 From the point of view of senior Council officers, Donald McGougan said that it became clear by 2010 that things were not improving with respect to the adjudication decisions.⁹⁶⁵ David Anderson said that he had had implicit trust in Richard Jeffrey’s judgment but that the description of “*finely balanced*” came to be not appropriate although he accepted that it had been his phrase in the first place. The matters were being reported over-optimistically and Council officers were seeing only one side. After the first Hunter Decisions and the Wilson Decision, there had been a round of party briefings and this was the first time that it was evident that things were going seriously awry⁹⁶⁶. Alastair Maclean had received a more positive view of the outcomes of the adjudications until he read them and this evidence was given in the overall context of the poor relationship between officers of TIE and the Council⁹⁶⁷.

⁹⁶³ Transcript of oral evidence of Gordon Mackenzie 1 November 2017, pages 62:16 to 81:16

⁹⁶⁴ Transcript of oral evidence of Phil Wheeler 2 November 2017, pages 82:11 to 87:8

⁹⁶⁵ Transcript of oral evidence of Donald McGougan 30 November 2017, pages 77:8- 21

⁹⁶⁶ Transcript of oral evidence of David Anderson 30 November 2017, pages 171:17 to 178:5

⁹⁶⁷ Transcript of oral evidence of Alastair Maclean 20 September 2017, pages 44:16 to 49:2

- 19.29 It was only at the stage of the first Hunter Decisions that in a discussion of TIE directors “*Questions were beginning to arise at this point about the contract*”⁹⁶⁸.
- 19.30 Richard Jeffrey described the situation following the Coutts Decision in May 2010 as being that TIE was “*losing confidence in our ability to achieve the outcomes we required or desired using the existing contract.*” It confirmed that TIE needed to be looking for alternatives.⁹⁶⁹ He referred to the decision to issue termination notices. He did approve them but did not agree that at that stage TIE was “*hurtling*” towards termination⁹⁷⁰. Richard Walker of BB got the impression that TIE was talking about termination anyway⁹⁷¹.
- 19.31 Overall, the impression of Sue Bruce, who was a person entering the course of events, was that by the time of the moves towards mediation the contractors had won the adjudications and TIE was on the back foot⁹⁷².
- 19.32 These are just a number of particular aspects of the overall evidence but in the submission of the Council it is possible to draw the conclusion that in initiating the DRP mechanism on the Infraco contract, and by proceeding to adjudications, TIE did not have a proper strategy to deal with the outcomes. There was no Plan B in general terms and the officers of TIE did not properly decide on what should be done as

⁹⁶⁸ Transcript of oral evidence of Kenneth Hogg 13 December 2017, page 122:10 onwards in particular page 124:9 to page 125:1

⁹⁶⁹ Transcript of oral evidence of Richard Jeffrey 9 November 2017, page 29:6-12

⁹⁷⁰ Transcript of oral evidence of Richard Jeffrey 9 November 2017, page 48:10- 17

⁹⁷¹ Transcript of oral evidence of Richard Walker 15 November 2017, pages 150:25 to 151:9

⁹⁷² Transcript of oral evidence of Sue Bruce 15 March 2018, page 21:19-25

adverse decisions emerged. Whilst it is accepted that they took account of legal advice which is referred to in the evidence, it is submitted that that did not absolve them from identifying a strategy of what to do if TIE's view of Schedule part 4 in particular continued to be the subject of adverse decisions. This is confirmed by the fact that it apparently only started looking for alternatives after the Coutts Decision.

19.33 At pages 101 to 103 of their submissions, SETE have responded to the suggestion that TIE did not give proper consideration to a "Plan B". SETE have suggested that TIE did have a number of alternative possibilities under the heading of Project Pitchfork. These included truncation of the route, the possible ejection of Bilfinger and termination of the Infraco Contract. The Council submits that these were not examples of a Plan B but rather the possible alternative consequences of the strategy already being pursued by TIE. What was needed was a strategy which planned for what to do if the views of TIE on the meaning and effect of Schedule part 4 and clause 80 turned out not to be supported by adjudicators (as was the case). The supposed elements of the Plan B for TIE just summarised all depended upon TIE having established some form of contractual entitlement against Infraco in general, and Bilfinger in particular, so as to justify a substantial alteration to, or the ending of, the Infraco Contract or Bilfinger's participation in it. But in a situation where TIE did not turn out to be successful in establishing such contractual entitlements, then what was needed, and was needed in advance, was an alternative strategy to

deal with a position for TIE which had not provided any right or lever to renegotiate or end the Infraco Contract.

19.34 The evidence has also demonstrated that the senior officers of the Council, as well as the TIE directors who were members of the Council, were not getting a full picture of the way that the adjudication decisions were going at least until the latter stages. The officers of TIE should not have allowed this to happen and it is a symptom of the way in which those in TIE tended to keep the Council out of its decision-making.

19.35 The impression created by this evidence is consistent with the evidence of those in the Council that TIE did not provide proper information about the results of the adjudications. This was the subject of the evidence of a number of witnesses but the following may be noted. There was evidence from several sources that TIE would lose the legal argument but a lower amount than the claim would be awarded and TIE would then claim this as a win whereas it was Infraco which had won the more important legal argument⁹⁷³.

19.36 The evidence of those who were involved at the time supports the conclusion that officers of TIE were not being fully open about the outcome of adjudications. The following evidence is consistent with that. Phil Wheeler said that the advice that he was getting on the strength of the DRP arguments was still that they were robust and no one had said otherwise.⁹⁷⁴ Steve Cardownie said that members of the Council had been told that TIE was winning the disputes with Infraco whereas that

⁹⁷³ For example, transcript of oral evidence of Nick Smith 14 September 2017, page 47:3-10

⁹⁷⁴ Transcript of oral evidence of Phil Wheeler 2 November 2017, page 81:21 to 82:6

was not the case.⁹⁷⁵ Lesley Hinds said when describing claims of confidentiality that it was frustrating in the context of the dispute resolution process when councillors were being told that the process was going in favour of TIE and TIE was winning and Infracore losing.⁹⁷⁶ It was Alastair Maclean's position that by late 2010, he considered that councillors had not been properly advised in the past.⁹⁷⁷ David Anderson said that TIE was not transparent from February 2009 because it was wary about commercially sensitive information leaking into the public domain. It was only in June 2010 that members were given any information about Schedule part 4 and its significance⁹⁷⁸.

19.37 That is consistent with the evidence of what was believed elsewhere. Donald Anderson, a former councillor who was advising BB and Siemens by the time of the adjudication decisions, said that it was clear from the information which they were receiving that the decisions were being presented to the Council as if TIE had won them which was an inaccurate assessment⁹⁷⁹. From the perspective of Transport Scotland, John Ramsay considered that Transport Scotland was in the same position as the Council in that TIE was not "*giving the actuality that tie knew they had in front of them*" and unless the Council made a specific demand⁹⁸⁰. That the reporting of the DRP procedures "*did not allow Transport Scotland to assess the impact of the outcomes of dispute*

⁹⁷⁵ Transcript of oral evidence of Steve Cardownie 26 September 2017, page 79:17-19

⁹⁷⁶ Transcript of oral evidence of Lesley Hinds 6 September 2017, page 62:12-21

⁹⁷⁷ Transcript of oral evidence of Alastair Maclean 20 September 2017, page 77:12 to 78:15

⁹⁷⁸ Transcript of oral evidence of David Anderson 30 November 2017, page 166:13 to 169:23

⁹⁷⁹ Transcript of oral evidence of Donald Anderson 6 September 2017, pages 219:6 to 220:22

⁹⁸⁰ Transcript of oral evidence of John Ramsay 28 September 2017, page 54:7-18

resolution procedures" is the position of the Scottish Ministers in their submissions at Chapter 4, paragraph 10.

- 19.38 Regarding the decision to withhold adjudication decisions from councillors, it was the evidence of David Mackay that these were not provided to councillors or the TPB because of concerns about leaks⁹⁸¹. Richard Jeffrey said that the adjudication decisions were not provided to the members of the TPB because it could not be certain that they would not leak and because they needed a degree of interpretation. He did not recall whether they were provided to councillors but said that a decision not to disclose to councillors would have been "a wise move" so as to avoid leaks and prevent matters coming to the attention of the press.⁹⁸² Donald McGougan thought that overall the Council was fair and reasonable in reporting matters to members, including in relation to DRP, and he supported the decision not to put figures into the public domain.⁹⁸³ From the perspective of a member of the Council at the time, Ian Perry accepted that the adjudications could be confidential because they were about money but that after adjudication decisions were released, they should not have remained confidential.⁹⁸⁴
- 19.39 It may be accepted that there was an issue at the time about whether members of the Council could be allowed to see the adjudication decisions which had been issued. That is essentially a separate and subsidiary issue to what was the undoubted obligation upon TIE

⁹⁸¹ Transcript of oral evidence of David Mackay 21 November 2017, page 117:13-24

⁹⁸² Transcript of oral evidence of Richard Jeffrey 8 November 2017, pages 139:9 to 142:8

⁹⁸³ Transcript of oral evidence of Donald McGougan 30 November 2017, pages 77:22 to 82:7

⁹⁸⁴ Transcript of oral evidence of Ian Perry 1 November 2017, pages 154:25 to 156:24

properly to report matters to the Council, its officers and members, which has already been referred to in this section of the submissions. The two issues may have been seen to be linked in the way that the evidence was presented by officers of TIE in particular but that should not be allowed to obscure the primary obligation which was that TIE should properly and fully report matters to the Council as it became apparent as a result of adjudication decisions that the way in which TIE had sought to rely upon the Infraco contract, and Schedule part 4 and clause 80 in particular, was not being sustained.

19.40 It is impossible to know what might have happened if this obligation had been fulfilled by TIE and whether, because of the earlier and greater involvement of the Council, the overall disputes might have been resolved sooner. For the purposes of identifying the causes of the increase in costs, delay and reduction of route of the Project, however, that is not critical. This is because, as already said, these consequences were caused by the form of the Infraco contract including Schedule part 4 and clause 80 and these consequences became inevitable once the Infraco contract was entered into. Whatever might be said about the outcomes of the DRP, and the ways in which the adjudication decisions were inadequately addressed and reported upon by TIE, these outcomes were the result of the Infraco contract and not anything which came about later.

19.41 This means, in the submission of the Council, that although the evidence on the DRP and the reporting of its outcomes to the Council may be a matter upon which lessons can be learned, this is not an

aspect which had any bearing upon the principal purpose of the Inquiry which is to identify the reasons for the increase in costs, the delays and the reduction of route of the Project.

19.42 Before leaving the topic of the DRP and the shortcomings in the reporting of the outcome of adjudications by officers of TIE, it is interesting to note that in the SETE submissions, they continue to maintain that the outcomes of adjudications were a success for TIE. At page 110 of the SETE submissions, it is submitted that "*The savings through the DRP process were significant...*" This continues to misrepresent the true outcomes because it was not a "*saving*" where Infraco was successful in establishing an entitlement under Schedule part 4 but was awarded by an adjudicator less than the amount claimed. That is not a saving but a loss to the overall budget of the Project in a situation where there would have been no additional sum awarded if the Pricing Assumptions mechanism had not permitted Infraco to make and establish a valid claim in the first place. There can be no doubt about this and it is also stated to be the position in the Bilfinger submissions at paragraph 281 in connection with the Russell Road adjudication (the Wilson Decision).

19.43 This contention which is made now by SETE is all the more remarkable because at page 92 of the SETE submissions it is submitted that in producing estimates, Infraco demonstrated a "*practice of habitually over-billing*". If it was the case that TIE, and the individuals in SETE, believed at the time and now that Infraco was over-billing as a matter of practice, then it can hardly be described as an achievement when an

adjudicator recognised that and awarded a lesser sum when allowing a claim.

19.44 One conclusion which can be drawn from what TIE employees did at the time, and what SETE appear to continue to believe now, is that they did not report the outcomes of the adjudications accurately to the Council because they did not actually understand the true consequences of the DRP adjudications in which TIE was engaged. The alternative is that they did and do understand the outcomes of the DRP adjudications but did not report that accurately and fully at the time, and they continue to maintain the position that these outcomes were successes because otherwise their failings at the time would be obvious. Either way the employees of TIE, including those in SETE, were responsible for failing properly to report the outcomes of the adjudications and the Council refers to all of the submissions already advanced in this section.

20. **Mediation**

Summary

- 20.1 By late 2010 all parties were agreed that the Project was stalled and were considering all options including termination of the Infraco contract. Following both parties meeting separately with John Swinney they agreed to enter into a formal mediation process.
- 20.2 The Council and TIE prepared together for the mediation using TIE's figures and outside advisers, although the Council and external advisers later came to regard TIE's estimates as being too low. Shortly before the mediation the Council's view of the "trigger point" for considering termination increased by £150m to £740m.
- 20.3 The Council's preference was to continue with a reduced line option with Infraco, in order to end up with a useable asset. Disruption and damage to the reputation of the city were considerations for the Council as well as price. However the Council was not prepared to proceed with Infraco "at any cost". Infraco also viewed it as an important part of the process to re-establish trust and co-operation not merely to agree a revised price.
- 20.4 At Mar Hall, following initial opening statements, negotiations were carried out between the "principals". For the Council/TIE this was Sue Bruce, Vic Emery and Ainslie McLaughlin of Transport Scotland.
- 20.5 It was implicit that following the mediation the Council would take over as the main client and TIE would be side-lined. At the mediation TIE's

representatives other than Vic Emery were in the background providing details to allow consideration of the figures proposed.

20.6 Non-binding heads of terms were agreed with a fixed price of £362.5m for off-street works and a target price of £39m for on-street. The commencement of “Priority Works” and the transfer of Siemens materials and design for rest of route were also agreed. All witnesses agreed this was a commercial settlement of all issues including outstanding claims and could be regarded as a “horse-trade”. No-one thought it was a “good deal” but all agreed that it was the best that could be agreed, and the alternative was separation. TIE (Richard Jeffrey and Steven Bell) thought that the Council was paying too much.

20.7 The Council's initial decision was to authorise construction only to Haymarket. Scottish Government intimated that if the line did not extend to at least St Andrews Square it would not release the remaining grant funding. 2 weeks later the Council revised its decision and authorised construction to York Place.

Decision to seek mediation

- 20.8 As referred to above, by late 2010 the Project was stalled and the parties were involved in various DRPs. RTNs had been served by TIE and revisions to the scope and price of the Project, such as the first and second “Project Carlisle”, had been proposed and rejected. It was apparent to everyone that the Project was not progressing satisfactorily and something required to be done.
- 20.9 In passing, it is noted that in the Siemens submissions at paragraphs 214 to 241, Siemens submits that allegations that Siemens had under-priced their work are unjustified. Detailed costings are presented, to some extent demonstrated by documents not previously before the Inquiry, in order to support this submission. The Council is content to leave that matter to the Inquiry for determination but for present purposes it is submitted that it is not material to the Council’s position. The issues which are material are the conduct and outcome of the mediation process and the financial and practical consequences of that, and these are discussed in this part of the submissions for the Council. It is that ultimate outcome which is material and whether a party who was involved in the mediation process had previously under- (or over-) priced its work does not matter other than as a potential criticism of the conduct of the particular party more generally.
- 20.10 By letter dated 29 September 2010, Infraco advised TIE that Infraco was no longer prepared to carry out “*goodwill*” works (i.e. works which were the subject of 94 outstanding INTCs which Infraco considered it

was not required to carry out under the contract in advance of receipt of a TIE Change Order or an agreed Estimate)⁹⁸⁵.

20.11 Two weeks later on 13 October 2010 Infraco wrote to the Council setting out their perspective on the situation and advising that they were willing to discuss matters directly with the Council⁹⁸⁶.

20.12 On 14 October 2010 the Council was provided with a refreshed Business Case for the Project and a report by the Director of City Development and the Director of Finance⁹⁸⁷. It reported that the main focus for incremental delivery would be from the Airport to St Andrew Square as the first phase. It indicated that termination of the Infraco contract was also being considered.

20.13 Following Dave Mackay's resignation from TIE Richard Walker wrote a further letter to councillors on 5 November 2010⁹⁸⁸.

20.14 On 8 November 2010 Richard Walker and Dr Keysberg met with John Swinney, Cabinet Secretary for Finance and Sustainable Growth, and Ainslie McLaughlin of Transport Scotland. Dr Keysberg and Richard Walker's evidence was that Infraco had been considering all options including the possibility that the Infraco contract would be terminated by TIE (or Infraco) and were keen to contact the Council and Scottish Government to try to find another party to talk to because the handling of the project by TIE had become more and more desperate. BB had another project in Scotland (on the M80) where they had worked with

⁹⁸⁵ TIE00409574

⁹⁸⁶ CEC00012755

⁹⁸⁷ CEC02083124

⁹⁸⁸ CEC00013012

Transport Scotland whom Dr Keysberg regarded as an extremely knowledgeable and experienced construction authority to whom they could explain the situation⁹⁸⁹. Dr Keysberg attributed his meeting with John Swinney as having led to his later meeting with Jennifer Dawe and Sue Bruce at which it was confirmed that the parties were willing to mediate⁹⁹⁰. After that Richard Walker had a meeting with Alastair Maclean and Donald McGougan of the Council and after that an agreement was reached to mediate⁹⁹¹.

20.15 On 15 November 2010 Tom Aitchison, the Council's Chief Executive, wrote to BB⁹⁹². On 16 November he and Jenny Dawe, Council Leader, met with Mr Swinney to discuss the possibility of going to mediation. Jenny Dawe's evidence was that the idea of mediation had been in her mind for quite some time and various third parties, including the German Consul General, had been offering to try to bring the parties together⁹⁹³. She had previously taken the advice of TIE that it would not be helpful for the relationship between TIE and Infracore if councillors or Council officials met with Infracore directly, but Council officers' and her view changed at this time and it appeared to be the appropriate thing to do.

20.16 On 18 November 2010 the Council approved an emergency motion proposed by the Leader of the Council, Jenny Dawe, to instruct the

⁹⁸⁹ Transcript of oral evidence of Jochen Keysberg 16 November 2017, pages 59:9 to 61:5 and witness statement of Jochen Keysberg TRI00000050, page 28

⁹⁹⁰ Transcript of oral evidence of Jochen Keysberg 16 November 2017 page 61:8 - 18 and witness statement of Jochen Keysberg TRI00000050, page 28

⁹⁹¹ Transcript of oral evidence of Richard Walker TRI00000072 15 November 2017 pages 152:12 to 154:3 and witness statement of Richard Walker TRI00000072, pages 79 to 80

⁹⁹² CEC00054284

⁹⁹³ Witness statement of Jennifer Dawe TRI00000019, pages 183 to 185

Chief Executive of the Council to continue to make preparations with TIE and Infraco for mediation or other dispute resolution processes⁹⁹⁴.

The motion noted that:

20.16.1 *"the Chief Executive wrote to the Managing Director of Billfinger Berger Civil UK Limited on 16 November to offer a meeting with Council officers;*

20.16.2 *the Council Leader and Chief Executive later that day met the Cabinet Secretary for Finance and Sustainable Growth at which they discussed the possibility of mediation as a means of progressing the tram project;*

20.16.3 *the Council Leader will take all appropriate steps to facilitate mediation and asked the Chief Executive to take forward a mediation proposal;*

20.16.4 *the Chief Executive subsequently discussed with the Chief Executive of tie the potential for using mediation or any other form of dispute resolution; and*

20.16.5 *the Tram Project Board on 17 November agreed to support an independent mediation process."*

The Council instructed the Chief Executive to continue to make preparations with TIE and Infraco for mediation or other dispute resolution processes and requested that the Chief Executive report back on progress in these matters.

⁹⁹⁴ CEC00054300

20.17 On 3 December 2010 a meeting took place between the Council officers and representatives of BB and CAF⁹⁹⁵. On 13 December, Jenny Dawe, Donald McGougan and Tom Aitchison met representatives of Infraco and she was reassured that they were serious about resolving matters at mediation⁹⁹⁶.

20.18 On 16 December 2010 the Council was provided with a further update and a report was provided by the Chief Executive⁹⁹⁷. It noted that mediation talks with Infraco would be taken forward. The Chief Executive's report stated inter alia that:

"3.3 A meeting took place on Friday 3 December 2010 between senior Council officials and representatives of the BSC consortium... At the meeting, BSC confirmed their willingness to explore resolution further with the Council and tie by way of mediation.

3.4 At the time of writing this report arrangements are in hand for the Chief Executive of tie and I to write to the Chairman of the BSC consortium. We will set out our views on a proposed timetable for mediation and suggest a number of options around selecting and agreeing a proposed mediator. We anticipate that the mediation arrangements will be agreed before Christmas and that detailed mediation discussions

⁹⁹⁵ Witness statement of Richard Walker TRI00000072, page 81; see also CEC02084346

⁹⁹⁶ Witness statement of Jenny Dawe TRI00000019, paragraphs 729 to 734

⁹⁹⁷ CEC01891570

involving the Council, tie and the consortium will commence early in the New Year.

3.5 *By their nature, mediation discussions have to be conducted on a confidential basis. It will not be possible to report in detail on the mediation process until it is completed or possible decisions emerge which require consideration by the Council.*

3.6 *While mediation talks are underway tie will continue to administer the contract. Mediation will be approached constructively but at the same time all strategic options will continue to be explored and developed by tie and the Council.*⁹⁹⁸

20.19 As noted above, around the same time, at the end of 2010, further adjudication decisions were issued. On 26 November 2010, Lord Dervaird issued his adjudication decision in the dispute arising under the Infraco contract in relation to landfill tax⁹⁹⁹. By letter dated 13 December 2010 Mr Howie QC issued his adjudication decision in the dispute arising under the Infraco contract in relation to the approval of sub-contract terms¹⁰⁰⁰.

20.20 In January and February 2011 Sue Bruce officially took over as the Council Chief Executive from Tom Aitchison and Vic Emery replaced Dave Mackay at TIE. On 15 February 2011 Dr Keysberg met Sue

⁹⁹⁸ CEC01891570, page 3

⁹⁹⁹ BFB00053475

¹⁰⁰⁰ BFB00053482

Bruce, Jenny Dawe and Vic Emery¹⁰⁰¹ and both sides confirmed their intention to approach the mediation as a genuine attempt to reach a compromise to resolve matters.

Mediation

Preparations including estimates prepared

20.21 Sue Bruce took forward the mediation proposal on the basis of the Council decisions referred to above. The Council and TIE worked together in preparing for the mediation. The preparations included a detailed analysis of costs and issues¹⁰⁰².

20.22 Colin Smith was brought into the project by Sue Bruce to help her¹⁰⁰³. She said that she had worked with him previously and wanted someone independent of the Project whose advice she could trust because she was aware that there were conflicting accounts coming from those who had been previously involved¹⁰⁰⁴. Colin Smith was therefore closely involved in preparations for mediation. Colin Smith and Alan Coyle later prepared a report for the Council entitled "*Review of Progress and Management of the Project January 2011 to June 2012*" (the "Review Report") which recorded the events leading up to and following mediation¹⁰⁰⁵. Alan Coyle was, amongst other things, Principal Finance Manager and Finance Commercial and Legal Manager (Tram). Alan Coyle was seconded to TIE from around November 2010 until the

¹⁰⁰¹ Transcript of oral evidence of Jochen Keysberg 16 November 2017 pages 62:24 to 63:2

¹⁰⁰² Witness statement of Susan Bruce TRI00000084, paragraph 4

¹⁰⁰³ Witness statement of Susan Bruce TRI00000084, paragraph 29

¹⁰⁰⁴ Transcript of oral evidence of Sue Bruce 15 March 2018, page 18:2- 22

¹⁰⁰⁵ WED00000134; TRS00023933 (see also CEC02083824 to CEC02083835, CEC02083973 and BFB00003305)

period of mediation in order “*to get closer to the project finances with a view to providing [Donald McGougan] and CEC with a greater level of transparency and confidence in the numbers...*”¹⁰⁰⁶.

20.23 Although prepared after the event, the Review Report was prepared by individuals personally involved in events before and after mediation, on the basis of documents taken from the project file and it is submitted that it should therefore be given significant weight when considering what happened. Section 7.0 of the Review Report sets out the position in relation to the analysis of costs which formed the background to the position that was achieved at Mar Hall in March 2011. The Council wanted to understand the full financial picture in advance of mediation. Paragraph 7.2 of the Review Report explains the process of the analysis of cost prior to mediation, and the various inputs in relation to that analysis.

20.24 TIE had already had a number of views on the likely commercial/contractual impacts from a number of sources, including legal and quantity surveyors as a result of previous commercial settlements they had attempted with the Infraco consortium as part of the commercial strategy they were following at that time. Prior to mediation, TIE had also employed consultants, Gordon Harris Partnership and Tony Rush and Nigel Robson to advise on and pursue settlement of the commercial issues with Infraco. The Council used this work as the basis for its consideration of issues that would arise at the

¹⁰⁰⁶ Witness statement of Alan Coyle TRI00000028, page 96

mediation. However it was examined in further detail as part of the preparations for mediation.

20.25 The results of the various potential financial outcomes were plotted on a spreadsheet which was given the working title of “Deckchair” Analysis because the various columns were in different colours.

20.26 Paragraphs 7.2 to 7.7 of the Review Report set out the position in relation to costs from the period prior to the mediation, to the end of the mediation itself.

20.27 Paragraph 7.3 of the Review Report summarises TIE's position in relation to its forecast costs of completing the line to Haymarket with Infracore, and completing the line between Haymarket and St Andrew Square with another contractor. TIE's position was a range of figures between £646m and £698m. The basis for these figures is set out in the Deckchair analysis version 1 at Appendix 2. TIE thought that it would be cheaper to terminate the contract and re-procure¹⁰⁰⁷.

20.28 However the Council and its advisers were concerned that the figures supplied by TIE were overly-optimistic. In his statement to the Inquiry¹⁰⁰⁸, Alan Coyle states that "*Tie had ignored a number of costs that would have become apparent in a re-procurement activity.*" His evidence at the oral hearings was to similar effect - that TIE had underestimated the cost of terminating by approximately £150m¹⁰⁰⁹. If that was added to the TIE assessment the cost of terminating and

¹⁰⁰⁷ Transcript of oral evidence of Alan Coyle 22 September 2017 pages 36 to 37 and TIE00355078

¹⁰⁰⁸ Witness statement of Alan Coyle TRI00000028, pages 115 to 116

¹⁰⁰⁹ Transcript of oral evidence of Alan Coyle 22 September 2017, pages 40:8 to 66:21

reprocuring was more expensive than reaching agreement with Infraco. Other witnesses including Tony Rush, Vic Emery, and Colin Smith also thought that the TIE estimates were overly optimistic and omitted key aspects.

20.29 Paragraph 7.4 of the Review Report identifies a number of "*fatal flaws*" in the assumptions that TIE made. For example TIE forecast the cost of settlement with Infraco at £33m, being the balance of entitlement for work done against work certified to date. It did not take into account any contractual entitlement that Infraco had for delay, including MUDFA related delay, or disputed design changes for work that had already been undertaken. TIE's forecast for the costs of a new contractor assumed that a new contractor would be able to take up where Infraco left off without any risk allowance or "*bad project*" premium being allowed for in the new contractor's price. TIE's forecast did not contain any indexation for materials that would be required where the price would have changed by reference to the original contract sum. TIE's forecast price of £19m for the on-street section from Haymarket to St Andrew Square did not allow for any significant risks for the on-street section and it did not allow for any extension to the programme as a result of having to re-procure.

20.30 In addition TIE's position proceeded on the assumption that Infraco would be prepared to agree to their contract being terminated, such that they would walk away from the project having completed the line only to Haymarket. Paragraph 7.6 of the Review Report states that terminating

the Infraco contract and reprocurring another contractor "*went against all the advice that was given by independent advisors at this time*".

20.31 Shortly before the mediation on 24 February 2011 Infraco had provided its "Project Phoenix Proposal" to complete the line from the Airport to Haymarket, and certain other works, for a total price of £449,166,366, subject to a shortened list of Pricing Assumptions¹⁰¹⁰. The total price comprised a payment of £231,837,822 to BB, £136,881,719 to Siemens, £65,306,030 to CAF and £15,140,795 to SDS.

20.32 In an email to Brandon Nolan, dated 27 February 2011¹⁰¹¹ Tony Rush expressed the view that the costs of separation would be substantially more than had been forecast by TIE.

20.33 Paragraph 7.5 of the Review Report states that Infraco's Project Phoenix proposal "*would have resulted in an anticipated final cost of £747m*". The basis of this figure is in Deckchair Analysis version 1 at appendix 2, which shows that the Infraco element of this overall total was £449.9m. However, the Review Report notes at paragraph 7.5 that "*On closer examination of the Infraco Phoenix proposal it became clear that there was c£80m of exclusions in this proposal which may have resulted in a similar addition to the final cost of the project, had CEC signed up to the Phoenix proposal as it was*". Adding £80m to Infraco's Project Phoenix figure results in an anticipated final cost of £827m.

¹⁰¹⁰ BFB00053258

¹⁰¹¹ CEC02084651

20.34 Sue Bruce stated that all of the figures were talked through by the Council, TIE and also Transport Scotland when they joined the client side approach and were “*stress tested*” and kept on the table for consideration. They played into the discussions in the lead up to mediation and were an option although separation was not ultimately recommended as the way forward.

20.35 In his statement to the Inquiry¹⁰¹², Vic Emery stated that the “*Legal advice was that [TIE’s] arguments were weak*”. During his evidence he said that Infraco knew the Council wanted to reach a deal and he did not think that the Council/TIE had any leverage it could use at the mediation. However he did not think that anything more could have been done in preparation to improve the negotiating position at mediation¹⁰¹³. Similarly Sue Bruce accepted in her evidence that the Council was “*on the back foot*” and “*in a difficult position*” prior to the mediation¹⁰¹⁴.

20.36 Sue Bruce and Vic Emery were both aware that TIE had been generally unsuccessful in the various adjudications in relation to its arguments about the proper interpretation of the Infraco contract. In addition the legal advice that had been given by Richard Keen QC in relation to potential termination of the contract was that “*Tie can only be sure of termination of the Infraco Contract if they can prove an Infraco Default which results in a valid notice of termination... a purported termination by tie on grounds which are ultimately not upheld would amount to a*

¹⁰¹² Witness statement of Vic Emery TRI00000035, pages 16 to 17

¹⁰¹³ Transcript of oral evidence of Vic Emery 13 March 2018, pages 42:4 to 45:18

¹⁰¹⁴ Transcript of oral evidence of Sue Bruce 15 March 2018, page 21:24- 25

*repudiatory breach for which Infraco would be entitled to recover damages at common law. There would however be no termination of the Infraco Contract by virtue of such a repudiatory breach, even if Infraco wished to bring about such a result*¹⁰¹⁵. Legal advice had also been given that there would be material risks in relying on the Remediable Termination Notices that had been issued by TIE: the opinion of Richard Keen QC was that "*in the event of tie giving notice of termination of the Agreement in reliance upon the specified [Remediable Termination Notices], there would be a material risk of their acting being found to be a wrongful repudiation of contract*"¹⁰¹⁶. The advice of McGrigors LLP was that it would be unsafe to rely on the Remediable Termination Notices that had been issued by TIE¹⁰¹⁷.

Objectives

- 20.37 It appears that prior to the mediation both sides had contemplated terminating the contract. Some in TIE were in favour of doing so, but those in the Council and Infraco preferred, if possible, to try to reach an agreement that would see a variation to the existing contract in order that the current contractor would be able to construct a reduced tram line and the city would have an asset to show for all the money spent on the Project.
- 20.38 In her witness statement Sue Bruce explained the Council's strategy for mediation "*was to be open-minded and hard-nosed and to seek clarity*

¹⁰¹⁵ TIE00080959, Appendix 1 of the report at paragraphs 10 and 14

¹⁰¹⁶ TIE00080959, Appendix 2 of the report at paragraph 10

¹⁰¹⁷ TIE00080959, paragraph 1.5

over options to take back to Council for their consideration. Above all though, it was not to get a result at any cost.” She also said that “the Scottish Government was supportive of mediation and our approach but had been clear there would be no more money”¹⁰¹⁸. In her evidence she said that when she came in the Council was looking for a way forward although nobody knew what that would be – she was asked to explore the options¹⁰¹⁹. She accepted that the Council’s order of preference was continuing with the contractor to produce a reduced scope for the tram line, followed by terminating the contract and re-procuring a new contract. Carrying on was not an option because the budget would be exceeded and the idea of terminating and having nothing to show for all the money spent would also be unlikely to be acceptable. She (and others including Colin Smith, Alan Coyle and Tony Rush) agreed that more preparation was devoted to the Project Phoenix scenario of carrying on with the contractors to produce a reduced scope but there was a “trigger point” or “line in the sand” at which point it would be worth reviewing the advice to the Council about the relative merit of accepting or terminating the contract. She could not remember the specific figure but agreed it could have been the £740m referred to as having been suggested on the day preceding the mediation in Tony Rush’s notes¹⁰²⁰. Sue Bruce also said that the settlement reached at the mediation was not just about money. Regard was had to the disruption that had been suffered and would continue to be suffered by the city and the adverse

¹⁰¹⁸ Witness statement of Sue Bruce TRI00000084, paragraph 87

¹⁰¹⁹ Transcript of oral evidence of Sue Bruce 15 March 2018, pages 22:11 to 23:13

¹⁰²⁰ Transcript of oral evidence of Sue Bruce 15 March 2018, pages 39:6 to 40:20

effect on its reputation if the project was further delayed or not completed¹⁰²¹.

20.39 Vic Emery's evidence was that the option of "attrition" i.e. carrying on with the present contract was considered by TIE but was not a realistic option. He thought that the overriding desire of the Council was to continue with the Project and that going to a new contractor would have been more expensive and more disruptive to the city. He was aware that terminating the Project and having nothing to show for the millions of pounds spent would be "*unpalatable*" for the Council. He thought Richard Jeffrey would have preferred to terminate the Infraco contract and continue with another contractor but other members of TIE had mixed feelings. Some were emotional and wanted to get out of the contract while others were more sanguine and realised that finding and working with a different contractor might create its own problems and that it would be better to have partial delivery of the tram than to have nothing to show for all the money spent or re-starting with a new contractor¹⁰²².

20.40 The evidence of the councillors and officials was also that they wished to see an agreement reached that would allow for the Project to proceed¹⁰²³.

Events at Mar Hall

¹⁰²¹ Transcript of oral evidence of Sue Bruce 15 March 2018, pages 42:1 to 44:13

¹⁰²² Transcript of oral evidence of Vic Emery 13 March 2018, pages 26:13 to 27:16

¹⁰²³ E.g.: witness statement of Jenny Dawe TRI00000019, paragraphs 711 to 714; transcript of oral evidence of Donald McGougan 30 November 2017, pages 83:5 to 84:17; transcript of oral evidence of David Anderson 30 November 2017, pages 180:20 to 187:1

Options considered and Information available/examined

- 20.41 There was general consensus from the witnesses about how the negotiations progressed at Mar Hall. TIE prepared a mediation statement¹⁰²⁴. Infraco also produced a mediation statement¹⁰²⁵. Sue Bruce, as Chief Executive of the Council, delivered an opening statement on behalf of the Council/TIE¹⁰²⁶ and Richard Walker delivered an opening statement on behalf of Infraco¹⁰²⁷.
- 20.42 After the initial opening statements the main negotiations took place between the “*principals*” on both sides with the remainder of the teams being consulted in separate break-out rooms between negotiation sessions. On the Council/TIE side the three individuals involved in the direct discussions with Infraco were Sue Bruce, Vic Emery and Ainslie McLaughlin. For the consortium the principals were Dr Keysberg (BB), Dr Schnependahl (Siemens) and Antonio Campos (CAF)¹⁰²⁸. It was generally recognised that there was a deliberate intention to keep some other individuals away from the actual negotiations because of their previous disagreements. In particular, after the initial meeting, neither Richard Walker nor Richard Jeffrey took part in the face to face negotiations. Dr Keysberg said that Infraco purposely did not put Richard Walker “*in the front row*” because of previous problems with TIE¹⁰²⁹. Vic Emery and others agree that TIE and some of its personnel might have been regarded by Infraco as “*toxic*” and that would make

¹⁰²⁴ BFB00053300 (with exhibits CEC02084530 to CEC02084561)

¹⁰²⁵ BFB00053260

¹⁰²⁶ CEC02084575

¹⁰²⁷ Transcript of oral evidence of Richard Walker 15 November 2017 page 159:7- 14

¹⁰²⁸ Transcript of oral evidence of Jochen Keysberg 16 November 2017, page 64:12-19

¹⁰²⁹ Transcript of oral evidence of Jochen Keysberg 16 November 2017, pages 65:24 to 66:11

reaching any agreement more difficult. He indicated that there appeared to be an expectation that TIE would not be involved in running the contract after the mediation although that was not written down¹⁰³⁰.

20.43 The Review Report by Colin Smith and Alan Coyle states at paragraph 7.6 that during the initial stages of mediation it soon became clear, through discussion between TIE and the Council "*that tie had not considered a number of cost headings at this time which would have had a significant impact on the final cost. In very broad terms, these items were in the order of £150m for settlement, professional costs, bad project premium risk, systems re-procurement risk and inflation, which would have potentially resulted in a final outturn cost of at least £800m*". In other words, if some of the "*fatal flaws*" in TIE's forecast were costed and added into the potential outturn cost for replacing Infraco with a new contractor, this would result in a forecast of at least £800m to St Andrew Square. This figure is also reflected in the PowerPoint presentation¹⁰³¹ which contains a table headed "*Decision Tree Factors*"; in respect of "*agreed separation*", the range of figures is stated as "*Range from £624.1m - £740m - £800m*"¹⁰³². Similarly in its submissions Siemens is very critical of the accuracy of TIE's estimates of its entitlement under the Infraco contract and depicts it as completely unrealistic¹⁰³³.

Offers/Counter offers

¹⁰³⁰ Transcript of oral evidence of Vic Emery 13 March 2018, page 85:11- 16

¹⁰³¹ CEC01927442

¹⁰³² CEC01927442 and witness statement of Susan Bruce TRI00000084, paragraphs 55 and 56

¹⁰³³ Written submissions of Siemens dated 27 April 2018

20.44 Various witnesses refer to there having been a series of offers and counter offers being made during the course of the mediation, although they had little recollection of the detail of these in terms of figures discussed. Paragraph 7.7 of the Review Report notes that:

"During the course of negotiations over two to three days at mediation, there were a number of offers and counter offers exchanges between the parties.

CEC's first offer to BSC was for £304m for the off-street section. At this point there were still a significant number of exclusions that sat outside the off-street price which were estimated at £80m. This price did not include for the remainder of the on-street works, which were thought to have been in the region of £20m. When the shape of this deal was added to the rest of the project costs, the estimated anticipated final cost was thought to be in the order of £731m.

Infraco did not accept this offer and returned with essentially an updated Phoenix proposal of £404m, which was only for the off street section. When risk, exclusions and the remaining project costs were added to this number the final cost would have been £814m.

CEC then replied with a final offer of £362.5m for the off-street section, with no exclusions and Infraco taking all the risk with the exception of minor utilities. By adding the rest of the project costs, £30m for risk and £22.5m for the on street section (which was an estimated figure and hadn't yet been negotiated) the anticipated final cost was £743.5m. The breakdown of these numbers can be found in Appendix 4 (High Level

Budget Proposal Total Project v1.1)." In the event, the target sum agreed at mediation for the on street works was £39M.

The Deal Done

20.45 Witnesses, including those "*principals*" involved in the direct discussions, Sue Bruce, Vic Emery, Ainslie McLaughlin, and Dr Keysberg stated that the settlement discussions were not just about the price to be paid for the various elements. They included finding a way to settle all outstanding disputes and agree a way forward with improved co-operative relationships and agreed priority works. They were therefore unable to give a detailed breakdown of the figures or refer to any report that justified these particular figures.

20.46 The "*ETN Mediation – Without Prejudice – Mar Hall Agreed Key Points of Principle*" was signed by the parties on 10 March 2011¹⁰³⁴. Dr Keysberg had delayed his departure until then but he flew out afterwards¹⁰³⁵. The principles were later incorporated into a Heads of Terms document¹⁰³⁶. Both documents were non-binding and were subject to contract. They set out various points in particular a proposed fixed price of £362.5 million for the off-street works (i.e. from the Airport to Haymarket, with other enabling works) and a target price of £39 million for the on-street works (i.e. from Haymarket to St Andrew Square).

¹⁰³⁴ CEC02084685

¹⁰³⁵ Transcript of oral evidence of Jochen Keysberg 16 November 2017, page 72:12- 14

¹⁰³⁶ CEC02084685

20.47 In his witness statement, Vic Emery stated that "*Sue Bruce, Ainslie McLaughlin, myself and the TIE/CEC negotiating team and Richard Jeffrey (who was not in the negotiating team) were responsible for the agreement reached*"¹⁰³⁷. In his oral evidence he indicated that the main players on the TIE/the Council side were himself, Sue Bruce, Ainslie McLaughlin, Alastair Maclean and Colin Smith¹⁰³⁸.

20.48 None of those involved were particularly pleased with the price agreed at the mediation but all appeared to agree that it was the best that could be done given the circumstances at the time. All the witnesses agreed that the mediation was a "*commercial agreement*" and to a greater or lesser extent that it could be regarded as something of a "*horse-trade*"¹⁰³⁹.

20.49 Richard Walker said that "*the outcome was a reasonable one and probably the best possible outcome that could be had for both parties. I don't think either party was pleased by the outcome at all. I think they were probably both satisfied with the outcome*"¹⁰⁴⁰.

20.50 Dr Keysberg described it as a "*commercial discussion*" and a compromise figure for which he could not give a breakdown¹⁰⁴¹. He also considered the target price of £39m to be a fair compromise and the outcome of a commercial negotiation with risks remaining on both sides. He also said that the regaining of trust and a different project

¹⁰³⁷ Witness statement of Vic Emery TRI00000035, page 20

¹⁰³⁸ Transcript of oral evidence of Vic Emery 13 March 2018, page 62:8- 10

¹⁰³⁹ Transcript of oral evidence of Alastair Maclean 20 September 2017, pages 114:14 to 115:12, 130; transcript of oral evidence of Vic Emery 13 March 2018, page 63:10- 14; transcript of oral evidence of Sue Bruce 15 March 2018, page 48:1- 5

¹⁰⁴⁰ Transcript of oral evidence of Richard Walker 15 November 2017, page 159:2- 6

¹⁰⁴¹ Transcript of oral evidence of Jochen Keysberg 16 November 2017, pages 69:23 to 71:11

management and governance were also vital elements of the mediation agreement and “*as important as the numbers*”, because the best contract does not protect you if it is not properly managed¹⁰⁴².

20.51 Dr Keysberg refuted the comment in the Faithful-Gould report¹⁰⁴³ that the figures for the on-street works were “*grossly inflated*” and pointed out that the author of that report had perhaps not understood that the method of sub-contracting those works was completely transparent to the Council and they were involved in the tendering process¹⁰⁴⁴.

20.52 In his statement to the Inquiry, Vic Emery stated that the agreement at Mar Hall “*was in two parts because BSC was more confident in their costings for the 'off-street works' than they were for the 'on-street works'. The 'on-street works' were a target sum because BSC still wanted to protect their position with regard to any problems that arose during this section of the work*”. He also stated that “*As I recall, the settlement was an improvement on the Project Phoenix offer*”. And his “*own view was and is that given the overriding desire to continue with the Tram Project, this was the best outcome that could have been achieved*”. “*The deal reached at mediation was the best deal that was achievable given the circumstances at the time. There were many areas where it was a less than satisfactory deal particularly in respect to Siemens costs and the amendments to the contractual terms and*

¹⁰⁴² Transcript of oral evidence of Jochen Keysberg 16 November 2017, pages 71 to 72:4- 11

¹⁰⁴³ CEC02083979

¹⁰⁴⁴ Transcript of oral evidence of Jochen Keysberg 16 November 2017, pages 75:23 to 78:7

conditions but overall it was the best deal we could achieve under the circumstances"¹⁰⁴⁵.

20.53 Mr Emery's evidence was that it was not possible to agree a fixed sum for the on-street works because *"there were still utilities diversions that had not been completed. There were disagreements over the detailed engineering solutions and the 'turnaround' point at St Andrew Square was not yet agreed. In his statement he says that £39m was a figure put forward by BBS*"¹⁰⁴⁶.

20.54 Alan Coyle stated that the separate "target sum" (of £39m) for on street works was accepted because it was acknowledged that ground conditions and utilities still presented a significant risk to the on street section¹⁰⁴⁷. He also explained that it was not possible to agree a fixed sum for those works *"Because of the extent of risk that was becoming apparent in relation to remaining utilities works in the main."* The figure of £39m *"was given as an estimated cost of completion that would be required to be agreed through any forthcoming Agreement"*¹⁰⁴⁸.

20.55 In his evidence at the hearing Mr Emery said that the TIE team did not think that the deal done was good value and you could say that he had to essentially over-rule his own management team, especially Richard Jeffrey who did not think it was a good deal but it was the lowest price that Infracore was prepared to agree to move forward with the works. No-one thought it was a "good deal" but it was the lowest price that Infracore

¹⁰⁴⁵ Witness statement of Vic Emery TRI00000035, pages 12 to 13

¹⁰⁴⁶ Witness statement of Vic Emery TRI00000035, paragraphs 60 to 64

¹⁰⁴⁷ Witness statement of Alan Coyle TRI00000028, page 113

¹⁰⁴⁸ Witness statement of Alan Coyle TRI00000028, pages 125 to 127,

would be willing to offer and TIE/the Council had to accept the deal or walk away¹⁰⁴⁹. He also he thought that Ainslie McLaughlin had to be consulted and they need his agreement to go forward with the figure suggested¹⁰⁵⁰.

20.56 In his statement to the Inquiry, Ainslie McLaughlin stated that:

"The negotiation that took place between the parties during the mediation included a series of offers and counter-offers. One of the issues was that Bilfinger were not prepared to offer a fixed price to go from Haymarket into St Andrew Square because of the amount of uncertainty that still existed with the utilities. That puzzled us to begin with because the view was that the MUDFA contract had cleared all these utilities. We could not see why that would that be an issue until it was explained that the MUDFA contract had been designed on the basis of an outline design which ended up being incompatible with the contractors' design. It had not taken into account things like the foundation bases for the poles that hold the overhead wires up. There were a number of quite significant issues. The contractor said that they had lost a lot of money in the initial phases of the contract when they were ready but the services were not clear. The mediation was about trying to understand some of those risks that the contractor had, and then how you could work round some of their concerns and still get them to commit to building the line into St Andrew Square. Their preference, initially, was to build it to Haymarket and then walk away

¹⁰⁴⁹ Transcript of oral evidence of Vic Emery 13 March 2018, pages 51:15 to 52:6

¹⁰⁵⁰ Transcript of oral evidence of Vic Emery 13 March 2018, page 63:1- 4

and let another contractor build the rest, but that meant that there would be two contractors working at the same time which would have presented other risks... I do not think CEC's position changed over the course of the mediation. They went in with the objective of getting an agreement to build the tram to St Andrew Square, and they got that. They would have had a range of outcomes in terms of how long that would take, and how much it would cost, and some of that would inevitably have to be a compromise on what was negotiated, but their prime objective was achieved.

*BBS's position changed over the course of the mediation in relation to their initial view that they did not want to build the line into St Andrew Square from Haymarket."*¹⁰⁵¹

20.57 Alan Coyle stated that the issue of Pricing Assumptions, in particular in relation to the off street section (for which a figure of £362.5m was agreed), were a subject of contention at the mediation and that "*BSC's position did change, in particular to, in principal, agreement of a lump sum for the off street section, thereby dropping pricing assumptions for this section*"¹⁰⁵². He also described the settlement of £362.5m for the off street works as improving upon the Project Phoenix offer because it "*swept away historic claims, took away exclusions and a high degree of risk for that section and provided a platform to build from*". He also said that "*CEC pushed hard to get agreement on the best deal we thought we could get taking on board the advice of advisors.*" and the

¹⁰⁵¹ Witness statement of Ainslie McLaughlin TRI00000061, paragraphs 100 to 102

¹⁰⁵² Witness statement of Alan Coyle TRI00000028, page 112

agreement reached could be reconciled or compared with previous proposals because it *"was a holistic settlement and didn't include a number of provisional sums/pricing assumptions for example"*¹⁰⁵³.

20.58 It was pointed out to various witnesses during oral evidence that there did not appear to be a document giving a breakdown of the £362.5M sum at the time of the mediation. It is submitted that in the context of a global agreement that included the settling of all outstanding historic claims and potential claims already having arisen under the contract as well as agree a fixed sum for the majority of the works still to be undertaken that is not particularly surprising. However, in his witness statement Alan Coyle refers to an Excel spreadsheet entitled *"Cost Summary for Edinburgh Trams as at 2012/13 Period 6 Ending 15 September 2012"* which contains a number of notes¹⁰⁵⁴ which he confirms in his statement were prepared by him and gives a breakdown of the sums. Note 1 states:

"As members are aware from the confidential appendix to the 25 August 2011 Council report the negotiations with the BBS consortium led to a figure of approximately £360m for (a) off street work; (b) settlement of claims in relation to off street; (c) settlement of claims in relation to on street; and (d) settlement of claims in relation to system wide work

In order to ascertain an allocation of that figure for the purposes of this summary we have calculated that;

¹⁰⁵³ Witness statement of Alan Coyle TRI00000028, pages 113 to 135

¹⁰⁵⁴ BFB00101644 and witness statement of Alan Coyle TRI00000028, pages 123 to 124

(a) £204m relates to off street work;

(b) £25m relates to settlement of claims in relation to off street;

(c) £82m relates to settlement of claims in relation to on street; and

(d) £49m relates to settlement in relation to system wide work."

20.59 Alan Coyle did not disagree that the figure of £362.5m agreed at Mar Hall included a net value for Infraco's claims under the Infraco Contract of £156m¹⁰⁵⁵.

20.60 In her evidence Sue Bruce said the final figures were a result of a collective judgement and that although Tony Rush may have suggested a figure, that would have been based on his experience and he was a hard-nosed and diligent negotiator¹⁰⁵⁶.

Priority Works

20.61 The proposed agreement also included a list of works to be prioritised to get the project going again and to restore confidence and the transfer of all of the Siemens and CAF materials, and the design from York Place to Newhaven. According to amongst others Ainslie McLaughlin agreement of these priorities took up some time at the mediation. The Priority Works were on Princes Street, the A8 underpass and Haymarket Yards and between the tram depot and the airport to allow for storage of the trams and testing to be carried out on the trams before the line was complete. There was also a concern on the part of

¹⁰⁵⁵ Witness statement of Alan Coyle TRI00000028, page 125

¹⁰⁵⁶ Transcript of oral evidence of Sue Bruce 15 March 2018, page 52:11- 15

the Council to try to ensure some works were carried out before the festival in August.

Role of Transport Scotland and Scottish Ministers in discussions

20.62 As referred to above, the Scottish Ministers' involvement was thought by the Infraco witnesses to be instrumental in bringing the parties to mediate in the first place. Vic Emery understood that the Scottish Government, in keeping with the Council, was keen to make progress with the Project with the same contractor rather than stop the Project and find a new contractor or abandon it given the amount of public money that had already been invested in it.

20.63 Sue Bruce said that at the mediation Ainslie McLaughlin's agreement was not absolutely necessary because the Council was aware that they would be responsible for the overspend, but she tried to take everyone along in the decision-making process and he gave his views and she valued his advice and knowledge and support for the process¹⁰⁵⁷.

20.64 Most witnesses stated that at the mediation Ainslie McLaughlin was understood to be there in an observational role. However he was one of the "*principals*" present during the face to face negotiations and was in phone contact with Mr Swinney during the mediation. Mr McLaughlin gave evidence that Mr Swinney "*was naturally interested to know that the mediation was looking like it was going to resolve the contractual issues to the extent that the project could proceed and be completed satisfactorily. He was interested in what the likely figure was going to*

¹⁰⁵⁷ Transcript of oral evidence of Sue Bruce 15 March 2018, pages 13:21 to 14:3

*be, but he wasn't questioning what that figure was... [He was interested in the figure] Because the government was committing 500 million, and he was wanting to make it absolutely clear that anything more than 500 million would be the responsibility of the Council to fund...there was a natural interest in what the final cost of this project was going to be and what the implications of that would be for the Council*¹⁰⁵⁸. Vic Emery indicated that he did not think that the offers that were made on behalf of the Council/TIE would have been made if Mr McLaughlin had not been in agreement with them and Tony Rush thought that Mr McLaughlin had contacted Mr Swinney to seek his approval before the final offer was made to Infraco at the mediation¹⁰⁵⁹.

20.65 As detailed below after the Mar Hall mediation, Scottish Government stated to the Council that it would not provide any further funds if the tram line was not completed to St Andrew Square rather than Haymarket and there was some concern on the part of the Council that Scottish Government would be entitled to reclaim sums already expended if the Project was not completed. This was a matter that the Council required to consider in making its decision to take the line to St Andrew Square.

Council resolutions and the reports/information on which they were based

20.66 On 16 May 2011 the Council was advised of the key outcomes from the mediation process. A report was prepared by the Director of City

¹⁰⁵⁸ Transcript of oral evidence of Ainslie McLaughlin 26 September 2017, page 185:24 to 188:2

¹⁰⁵⁹ Transcript of oral evidence of Anthony Rush 9 November 2017, page 185:11-13

Development, Dave Anderson¹⁰⁶⁰. It was noted that mediation meetings had taken place in March, after which positive dialogue had been maintained between the parties. Good progress had been made in resolving the issues at the heart of the dispute. Short term actions were underway with work recommencing in priority locations along the route, pending the resolution of detailed design and costing work on the first phase of the route, from the Airport to St Andrew Square (with a turn back point in York Place), all in accordance with the agreement reached by the parties during mediation. In addition, Infraco would rectify, at their expense, the surface cracking problems that had arisen on Princes Street.

20.67 A number of short term actions that were identified as being required to restore momentum to the construction of tram infrastructure in priority sections of line 1a and enable the carrying out of work in the priority sections (and which had been resolved through mediation), would be managed through a Minute of Variation. That Minute of Variation would be superseded by a subsequent agreement, reflecting the full terms of any agreement reached between the parties to deal with completion of the revised programme, scope and budget for a line from the Airport to St Andrew Square.

20.68 As a result of the mediation discussions a priority works programme had been agreed and work had recommenced at the following locations in May 2011, namely, the Haymarket Yards, the Tram Depot (including the depot access route and a section of track towards the airport) and

¹⁰⁶⁰ CEC01891505

the A8 underpass. Some auxiliary works would also be carried out to progress detailed site investigations, clearance and demolition at several other locations along the tram route.

20.69 The costs associated with the re-commencement of work, the transfer of materials to Council ownership and related matters had been subject to independent verification by an external Chartered Quantity Surveyor and cleared with Transport Scotland officials. These costs, added to those already incurred, took the cumulative expenditure on the Project up to 6 May 2011 to a total of £440 million. The report stated, *“All of the above have been subject to past dispute and uncertainty and it is clearly now more prudent to complete these works on an agreed basis rather than to suffer further time delays and associated costs”*.

20.70 The Council was thus aware of the proposal to enter into Minute of Variation 4 before it was signed even if there was no formal resolution to authorise its being entered into.

20.71 Minute of Variation 4 was signed on 20 May 2011 and dates in June 2011 although payments in relation to it were made before that. It was primarily entered into to allow for the Priority Works agreed as a result of the mediation to be carried out and to transfer title to the Siemens materials¹⁰⁶¹. Colin Smith agreed that the sum of £49m had been agreed to be paid in 3 instalments following a meeting with BB and Siemens where sums were drawn up on a whiteboard. He had certified £28.2m as payment for the Siemens materials and equipment. He agreed there

¹⁰⁶¹ CEC01731817

was some confusion over the remainder of the payment and Infraco may have regarded it as a mobilisation payment. He was confident that the Council was aware of the payments and they had been discussed at a Tuesday or Thursday morning tram SMT meeting¹⁰⁶². In the second supplementary statement of Axel Eickhorn¹⁰⁶³ and in Siemens' written submissions, Siemens has clarified that in its view the payments were made in respect of sums already outstanding, and to pay for the Siemens' material equipment that had already been purchased for the Project and paid for by Siemens¹⁰⁶⁴. Similarly Bilfinger in its submissions has also stated that the payments were viewed by it as being for sums that were already owing to it rather than a mobilisation payment¹⁰⁶⁵. Vic Emery said he had no concerns about signing MoV4 for TIE. He was confident that he had the authority of the Council to do so and he was unaware of there being any questions raised over that¹⁰⁶⁶. Similarly Sue Bruce could not recall there being any controversy over the signing of the agreement or payments being made under it and strongly refuted any suggestion that the payments might in any way be seen as some sort of "*sham*"¹⁰⁶⁷. She had no recollection of any controversy or why anyone might have thought Alastair Maclean was "*raging*" in relation to any questions raised by TIE over the payment or the possibility that the MoV4 payments meant that TIE had committed

¹⁰⁶² Transcript of oral evidence of Colin Smith 14 March 2018, pages 87 to 100

¹⁰⁶³ TRI00000276

¹⁰⁶⁴ Paragraphs 363-374 on pages 134-139 of written submissions of Siemens dated 27 April 2018

¹⁰⁶⁵ Paragraphs 447-456 of written submissions of Bilfinger dated 27 April 2018

¹⁰⁶⁶ Transcript of oral evidence of Vic Emery 13 March 2018, pages 89:15 to 98:6

¹⁰⁶⁷ Transcript of oral evidence of Sue Bruce 15 March 2018, pages 104:9 to 105:13

to spend more than the total it was authorised to ¹⁰⁶⁸ and Alastair Maclean himself was not asked about the relevant email.

20.72 It is submitted that the signing of MoV4 and the payments made under it did not contribute in any way to the cost overrun or delay in the Project as a whole. The Council was fully aware of the proposal to make the payments and while MoV4 may have affected the timing of payments they did not affect the overall expenditure and ensured that work could be carried out in the meantime rather than being further delayed.

20.73 McGrigors, Solicitors, produced for TIE/the Council a draft "*Report on Certain Issues Concerning Edinburgh Tram Project – Options to York Place*" dated 29 June 2011¹⁰⁶⁹. That report gave a detailed explanation about the options and the potential costs of the alternatives to entering into the Settlement Agreement following Mar Hall. It highlighted a number of potential costs of separation including (a) Infraco's entitlement to payment in respect of work (other than any element of change) which had been carried out up to the date of separation; (b) the value of the many disputed changes to the Infraco Works; (c) the entitlement to Infraco to an extension of time (which it thought Infraco would be successful in securing); (d) extra cost caused by delay; (e) Infraco's entitlement to preliminaries up to 31 March 2011 and preliminaries for the Prioritised Works up to 1 September 2011 in terms of MoV4 (f) Infraco's mobilisation payment of £45.2M at the outset of the contract; (g) the cost of a new contractor to complete the works to

¹⁰⁶⁸ Transcript of oral evidence of Sue Bruce 15 March 2018, page131:9- 17

¹⁰⁶⁹ CEC01942218 - CEC01942225

York Place and (h) other costs including payment to CAF and legal and internal costs in relation to any dispute about the extent of Infraco's entitlement. It also detailed the additional costs for other factors if the Infraco Contract remained in place including (a) Infraco claims in relation to change in future works; (b) the costs of completing the work to York Place and any claims arising from that; and (c) Infraco's potential ability to recover the profit it would have earned in relation to the section of the line to Newhaven that it was no longer going to complete. It also considered the possibility of lengthy and complicated legal proceedings if TIE tried to terminate the Contract.

20.74 On 30 June 2011 the Council was advised of the options for the future of the Project. A report was provided by the Director of City Development¹⁰⁷⁰. It was noted that the strategic rationale and business case for the Project had been subject to further external review and validation. The costs of terminating the project, or continuing under the terms of the existing contract, had also been examined in detail. Neither option was likely to be materially less expensive than completing the first phase of line 1a. Accordingly, it was recommended that the Council should pursue the completion of the first phase of line 1a to St Andrew Square/York Place, subject to identification and confirmation of funding.

20.75 The recommendation in the report was based on the further external review and validation that had been carried out on behalf of the Council after the mediation at Mar Hall. Information in this respect was considered to be confidential and a dataroom set up for councillors to

¹⁰⁷⁰ CEC02044271

visit if they wished to see the details. The dataroom included the confidential appendix to the report with a presentational briefing in the data room with time allocated for them to read the reports that formed the data room and time for questions afterwards¹⁰⁷¹. It included the draft report by McGrigors LLP dated 29 June 2011¹⁰⁷². It also included spreadsheets entitled Edinburgh Tram Budget Settlement Agreement 24-06-11¹⁰⁷³. The spreadsheet at CEC02085605 shows a high (H) and low (L) outturn cost of £772.9m and £725.4m respectively for taking the line to St Andrew Square, the difference being the level of allowance for contingency and specified risk. In each case, the outturn cost includes the lump sum price of £362.5m for off street works. The confidential appendix included a spreadsheet containing a budget appraisal¹⁰⁷⁴. That document contains a summary of the outturn costs of various options as follows (shown here from highest to lowest):

Separate from Infraco and re-procure with another contractor (high)	£1,144.7m
Continue with Infraco to York Place (high)	£1,055.2m
Continue with Infraco to York Place (low)	£941.7m
Unsuccessful termination	£910m+

¹⁰⁷¹ Witness statement of Alan Coyle TRI00000028, page 139

¹⁰⁷² Witness statement of Alan Coyle TRI00000028, page 139; paragraph 3.33 of the report of 30 June 2011; USB00000384, CEC01942217 to CEC01942225

¹⁰⁷³ Witness statement of Alan Coyle TRI00000028, page 140; CEC02085604, CEC02085605

¹⁰⁷⁴ Witness statement of Alan Coyle TRI00000028, page 140; CEC02044271, paragraph 3.42; CEC02085613, CEC02085609, CEC02085610

Settlement agreement (high) £773.4m

Separate from Infraco and mothball/cancel the project £687.1m

(high)

20.76 These figures appeared to show the estimates for separation and re-procurement were £0.5bn more than the original deckchair analysis in the run up to mediation but they were set out in a different way and included significant additional sums for Primary Risk (£106m), bad project risk (£40m), Inflation Risk (£25m) and Specified and Exclusion Risk (£77.5m) as well as £80m for Infraco settlement premium if the contract were terminated. These risk figures were subjective and some witnesses such as Denis Murray thought they might be too high. But he also accepted that because they were speculative and subjective there was no right or wrong answer¹⁰⁷⁵. The total figures were however significantly more than the proposed settlement agreement. In their submissions, SETE have suggested that *"it appears that CEC may have inflated the project costs of termination in order to justify the price paid for settlement at Mar Hall"*¹⁰⁷⁶ and *"the net result of [Colin] Smith's reconciliation of the figures was retrospectively to justify CEC's preference for settlement over termination"*¹⁰⁷⁷. Any inference that the figures were artificially inflated retrospectively to justify the settlement is strongly rejected by the Council. As noted above, the main differences are differences of opinion as to the likely risks and costs of termination that could not be definitively known at the time. TIE had a history of

¹⁰⁷⁵ Additional Questions of Dennis Murray TRI00000249, pages 15 to 18

¹⁰⁷⁶ Page 122 of written submissions of SETE dated 27 April 2018

¹⁰⁷⁷ Page 122 of written submissions of SETE dated 27 April 2018

being over-optimistic in its view of the costs associated with the Project and the likely success in avoiding incurring further costs. The estimates made by Mr Coyle and Mr Smith were more realistic and showed that in a less than best case scenario the likely cost of termination and re-procurement was clearly more than the settlement offered at Mar Hall.

20.77 The confidential appendix also included a report by Atkins (through their subsidiary, Faithful & Gould) entitled "*Independent Review*" and dated 29 June 2011¹⁰⁷⁸ (see below). The figure of £362.5m for off street works "*was settled*" and was therefore not subsequently scrutinised by the Post Settlement Agreement Budget Report produced by Faithful & Gould on 19 August 2011¹⁰⁷⁹.

20.78 The confidential appendix included other information such as a document produced by Colin Smith in relation to the settlement dated 22 June 2011¹⁰⁸⁰; a note on the key terms of revised contract arrangements dated 23 June 2011¹⁰⁸¹ and information in relation to revenue and other financial matters¹⁰⁸².

20.79 The report by the Director of City Development to the Council of 30 June 2011 referred to above included an appraisal of options, based on the workstreams that had been carried out and reflected in the

¹⁰⁷⁸ Witness statement of Alan Coyle TRI00000028, page 140; CEC02044271, paragraph 3.37; CEC02085600

¹⁰⁷⁹ CEC02083979 and witness statement of Alan Coyle TRI00000028, page 157

¹⁰⁸⁰ Witness statement of Alan Coyle TRI00000028, page 140; CEC02085602

¹⁰⁸¹ Witness statement of Alan Coyle TRI00000028, page 140; CEC02044271, paragraph 3.39; CEC02085616

¹⁰⁸² Witness statement of Alan Coyle TRI00000028, page 140; CEC02085588 to CEC02085601, CEC02085603 and CEC02085614

confidential appendix. This appraisal was set out at paragraphs 3.31 to 3.46, with the conclusion at paragraph 3.47 as follows:

"In conclusion, the option to complete the project to St. Andrew Square is believed to yield the best prospect of a return on investment, relative to the original aims of the project. The cost of this option exceeds the available budget. Contingency plans have been drawn up to finance a portion of the necessary funding. Not all of this contingency would be available for the option to Haymarket. However, in both cases the Council will need additional help to bridge the gap, either from the Scottish Government, or from other external sources."

20.80 The options were presented to Council by Dave Anderson, Colin Smith, Alastair Maclean, Alan Coyle and Donald McGougan for their consideration. Standing orders had to be suspended so that officers could speak at Council because it was a huge decision¹⁰⁸³.

20.81 At the Council meeting on 30 June 2011 the Council reached a decision¹⁰⁸⁴ to agree some of the recommendations by the Director of City Development in his report of 30 June 2011 as follows:

"8.1 That the Council:

(a) agrees that of the options available, and subject to funding, Option (iii) (Airport to St Andrew Square/York Place) should be pursued to provide a revenue generating service and realisation of the investment to date...

¹⁰⁸³ Witness statement of Sue Bruce 15 March 2018, paragraphs 90 to 93, 99

¹⁰⁸⁴ CEC02083232

- (c) *authorises tie Ltd to progress on the priority works, in accordance with MoV4, and incur expenditure within the limits of the project budget of £545m, until the end of August 2011...*
- (e) *as shareholder, asks Lothian Buses to assist in preparing for operations, by accepting transfer of ETL (Edinburgh Trams Limited), subject to staff consultation, as soon as possible."*

20.82 It was also decided by the Council on 30 June 2011 that the Director of City Development's recommendations 8.1(b) and (d) should be deleted and replaced with the following:

"8.1(b)(i) Subject to 8.1 (b) (ii) below, to authorise the Chief Executive to enter into the Settlement Agreement (substantially on the terms set out in the Settlement Agreement summary) in respect of option (iii).

8.1(b)(ii) To agree that the Settlement Agreement would not become unconditional until the Council was satisfied that there was sufficient funding available and that the project had been sufficiently derisked.

8.1(b)(iii) To instruct the Chief Executive to bring a report back to the Council (prior to any deadline stated in the Settlement Agreement for satisfaction of the Funding Condition) setting out:

- how that funding was to be provided; and*
- greater detail in relation to:*

- (1) *the risks being incurred particularly in relation to utilities in the Haymarket to St. Andrew Square section;*
 - (2) *the risks surrounding the potential sale or lease of tram vehicles; and*
 - (3) *the extent to which (and how) the Haymarket to St. Andrew Square section had been de-risked,*
- all to enable a fully informed decision to be taken as to the acceptability of that funding..."*

20.83 On 25 August 2011 the Council was advised of progress over the summer and was provided with recommendations on the future funding options and governance arrangements. A report was prepared by the Director of City Development¹⁰⁸⁵. It noted proposed changes to the governance structure. It also noted significant progress had been made on the commercial terms of the Settlement Agreement and good progress had been made towards the completion of agreed priority works at Haymarket Yards, the A8 underpass and the Tram Depot and test track. A detailed review of the key project budget risks had been carried out, validated by Faithful and Gould to ensure that appropriate risk management procedures were in place. The work carried out by Faithful & Gould and referred to in the Review Report and the Report by the Director of City Development for the meeting of the Council on 25 August 2011 referred to Siemens' prices as being "*grossly inflated*". It was now calculated that the overall programme budget should be

¹⁰⁸⁵ TRS00011725

adjusted to £776 million, being comprised of a firmed up base budget of £742 million and a risk allowance of £34 million. The budget represented a figure of £231 million above the currently approved budget of £545 million. It was proposed that the additional £231 million would be funded by prudential borrowing, which would represent an annual revenue cost of £15.3 million over a 30 year period.

20.84 It was suggested that in the event of project cancellation there would be a one year revenue impact of over £180 million. The impact on Council Tax levels to finance this magnitude of revenue would be equivalent to a one year increase of 80%. The Council's current reserves, including earmarked reserves, would not provide the level of revenue required. In his evidence Stuart Fair questioned whether that would in fact have been necessary but it is submitted that that was not itself a determining factor in the Council's decision to continue with Project.

20.85 Before the Council meeting on 25 August 2011 the documents made available to members on a confidential basis included a spreadsheet showing the proposed new budget¹⁰⁸⁶ and a report (prepared by Ashurst Solicitors), "*Key Legal Risks of Revised Contractual Arrangements*"¹⁰⁸⁷.

20.86 At the Council meeting on 25 August 2011, various amendments were proposed before the Council voted in favour of an amendment that the proposal with least risk was to build from the Airport to Haymarket as phase 1 of a longer-term, strategic plan.

¹⁰⁸⁶ CEC02086442

¹⁰⁸⁷ CEC02086443

20.87 By letter dated 30 August 2011 Transport Scotland advised the Chief Executive of the Council that in light of the Council's decision on 25 August to take the tram only to Haymarket, Ministers were now of the view that that represented a fundamental change to the basis on which the Scottish Government originally agreed to contribute up to £500 million¹⁰⁸⁸. The decision to take the tram only to Haymarket would result in the tram requiring a significant ongoing subsidy, which was damaging in public expenditure terms. In these circumstances, Ministers were not prepared to make any further payments to the project and would not extend the existing grant arrangements beyond 31 August 2011. If the Council wished to make further proposals that were consistent with the basis of the original agreement given by Ministers, these would be considered on their merits.

20.88 Primarily in response to the letter from Scottish Government a special meeting of the Council was held on 2 September 2011. A report was provided by the Chief Executive¹⁰⁸⁹. Members were advised that at mediation in March 2011 the parties had agreed that unless terms for settlement of the contractual dispute were agreed by 31 August 2011, and funding confirmed by 5pm on 1 September 2011, the Infraco contract would terminate automatically at that time. The costs of termination would require to be agreed with the Infraco consortium and were likely to be significant. At the time of writing the report the Infraco consortium had agreed a short extension of the deadline to 5pm on 2 September 2011. They were also referred to the letter from Transport

¹⁰⁸⁸ CEC01721794

¹⁰⁸⁹ CEC01891495

Scotland advising that no further payments would be made in light of the Council's decision to take the tram only to Haymarket. It was explained that the balance of the grant from Transport Scotland, amounting to £72 million, would not be available. It was recommended that the Council agree that the option to build from the Airport to St Andrew Square/York Place, as set out in the 30 June 2011 Council report, should be pursued.

20.89 Following a number of votes, the Council agreed on 2 September 2011 to complete the tram line to St Andrew Square, subject to a number of qualifications. Later that day TIE, the Council and Infracore entered into a Second Memorandum of Understanding to extend the timescale for the conclusion of negotiations until 14 September 2011¹⁰⁹⁰. On 14 September 2011 the Cabinet Secretary for Infrastructure and Capital Growth announced that the remaining £72 million of Scottish Government grant would be reinstated to the Project now that the route to St Andrew Square had been similarly reinstated. A team of experienced project managers from Transport Scotland would fill senior roles in the new governance structure to help oversee the final delivery of the project¹⁰⁹¹.

20.90 In his evidence Stuart Fair questioned whether the Council would in fact have had to record the tram expenditure immediately into its revenue budget if it had decided not to continue but it is submitted that that was not itself a determining factor in the Council's decision to continue with

¹⁰⁹⁰ TIE00899947

¹⁰⁹¹ TRS00012212

Project. Mr Fair also suggested that it was very unlikely that the Scottish Government would have actively reclaimed the money it had given by way of grant. He said that would only potentially happen "*if there was a significant divergence of opinion between the Scottish Government and the Council...around the expenditure side...it would be a decision for the Scottish Government...but I think they would have to have due regard to the financial position of the City of Edinburgh as well before trying to recover grant*"¹⁰⁹². Mr Fair accepted that it was part of the conditions attached to the grant funding that the money could be reclaimed if the grant conditions were not complied with¹⁰⁹³. It is submitted that although unlikely, in the scenario where the Project was terminated without the tram being built (which was the major condition on which the grant was made) there was a possibility that the Government might ask for its money back. Even if there was only a small possibility of that happening, it would be a significant risk because the consequences of it happening would have such a severe effect on the Council's finances. Given that the Government was indicating that it would not provide the rest of its committed funding if the line was shorter than St Andrew Square it was a possibility that would not have been prudent to ignore completely.

Settlement Agreement/MoV5

20.91 On 15 September 2011 a Settlement Agreement was entered into between TIE, the Council, BB, Siemens plc and CAF in full and final

¹⁰⁹² Transcript of oral evidence of Stuart Fair 22 March 2018, page 177:7 – 14; pages 178:12 – 179:13

¹⁰⁹³ Transcript of oral evidence of Stuart Fair 22 March 2018, page 176: 4-14

settlement of all past, present or future disputes, claims and entitlements (subject to certain exceptions).¹⁰⁹⁴ The Settlement Agreement was based on the agreement reached at Mar Hall and included:

20.91.1 a lump sum price for the “*off-street*” section between Edinburgh Airport and Haymarket, subject to certain exceptions

20.91.2 a measurement contract basis for the “*on-street*” section, which included the Council carrying certain risks, including those risks associated with utility diversions.

Role of Transport Scotland and Scottish Ministers in project in future

20.92 One of the conditions of the reinstatement of the Scottish Government funding in September 2011 was the involvement of Transport Scotland in the future of the Project.

Conclusions in relation to mediation settlement

20.93 It is submitted that the Council was in a very difficult position by late 2010. The relationship between TIE and Infraco had broken down and the Project was stalled. There was no clear route to get it back on the rails. As Jennifer Dawe said in her witness statement, the Council had given TIE every opportunity to try and resolve their differences with Infraco and it was not working and it became apparent that by the end

¹⁰⁹⁴ CEC02085585. At the same time CEC provided a further Guarantee of TIE's financial obligations under the Infraco contract (BFB00097935).

of 2010 it would be appropriate for the Council to become directly involved in trying to resolve the disputes¹⁰⁹⁵.

20.94 It is submitted that it was a sensible decision to agree to go to mediation and involve new personnel in the negotiations in order to try to re-build trust between the parties. While some witnesses said that more time might have been of benefit before the mediation, it is submitted that in reality TIE/the Council were in a very weak negotiating position and that would not have significantly improved if more time had been taken. There was an imperative to try to get the Project moving and in any event it would have been very difficult to arrive at any significantly more reliable figures. The main differences in estimates between TIE and the Council depended on the views taken of the likely cost of termination and re-procurement. Those could not be accurately predicted. The cost of re-procurement would not just be a matter of money but there would have been very significant further delay caused while the necessary tendering process was undertaken and then a new contract negotiated. It is unlikely that any work would have taken place during that time and the reputational damage to the city and the disruption to its residents would have been significantly greater. If the Project had been abandoned all the money spent would have been wasted.

20.95 It is submitted that there would be no proper basis for concluding that settlement could have been reached with the Infracore consortium at a significantly lower price. While the risks and figures are matters of subjective judgement, it is also submitted that there would not be any

¹⁰⁹⁵ Witness statement of Jenny Dawe TRI00000019, paragraph 707

proper basis to conclude that it would have been possible to terminate the contract and re-procure the construction of the remainder of the tram line by another contractor at lower price. The evidence would not support a conclusion therefore that the increase in cost or delay in the completion of the tram Project was materially contributed to by the actions of the Council at the mediation. It may have been the point at which the true cost of the previous failings was crystallised but the mediation process itself was not a cause of those increases in cost or delay.

20.96 On the contrary the agreement reached at the mediation gave greater certainty to the Project going forward and prevented the very considerable delay that would have ensued if no agreement had been reached and attempts had been made to terminate the contract and re-procure it. It is also extremely likely that a major litigation for breach of contract would have ensued either at the behest of either Infracore or TIE if the cost of termination and outstanding claims could not be amicably agreed - which would appear unlikely given the circumstances at the relevant time. The agreement reached at the mediation gave a much firmer fixed price for the off-street works and settlement of all outstanding disputes, a reduced scope of Pricing Assumptions and changes and a target price with a transparent method for dealing with potential disputes. SETE's characterisation of the settlement as a "*capitulation*"¹⁰⁹⁶ is strongly refuted and shows an on-going failure to appreciate the reality of the situation in which the Council found itself

¹⁰⁹⁶ Page 143 of written submissions of SETE dated 27 April 2018

due to the terms of the Infraco Contract, TIE's failure to manage the Project and a persistent assumption that TIE was correct in its position. As noted above, and as other parties have confirmed in their submissions, the agreement reached was a commercial settlement in which both sides required to compromise. It is simplistic to look only at the price agreed as opposed to the revised terms of the contract and potential costs if agreement had not been agreed and the benefit of having certainty and the ability to move forward without any further delay. While it has been described as a "horse-trade", that is the reality of a commercial settlement.

20.97 It would be inappropriate to compare the price agreed at mediation to the original price in the contract. The circumstances in March 2011 were completely different to the Project starting from a clean slate. There were very significant claims already outstanding due primarily to delays that were likely to be the responsibility of TIE/the Council. The contract that had been entered into contained various clauses that were extremely prejudicial to TIE/the Council and there was no clear right to terminate the contract. If the Council sought to do so it was very likely that there would be a very lengthy and costly litigation for breach of contract.

20.98 The mediation removed the vast majority of those costs and risks. After the mediation and settlement agreement trust was restored and relations between the parties became co-operative. As detailed below after the Settlement Agreement, construction of the reduced scope of the tram line proceeded without significant difficulties and more or less

on budget and on time. It is submitted that the mediation process should be seen as the turning point in the history of the Project that overcame the previous disputes and difficulties and delivered the tram.

21. **Post settlement**

Summary

- 21.1 Following the mediation trust was restored between the parties and a much more collaborative and co-operative approach led to the remainder of the works progressing on schedule and within the revised budget.
- 21.2 Various changes were made to the governance and management of the Project. In particular Turner & Townsend was appointed as project manager and TIE was disbanded. The Council took a much more prominent role in the oversight of the Project with Sue Bruce and Vic Emery holding twice weekly meetings to review progress.
- 21.3 Regular meetings between principals provided a forum to which disputes could be escalated. Colin Smith's appointment as an Independent Certifier helped resolve most potential disputes.
- 21.4 The collaborative approach and joint meetings with utilities companies also resulted in the rapid clearing of outstanding approvals and consents.
- 21.5 Infraco's agreement to share larger work-sites with utilities contractors allowed a "bow-wave" system to be introduced whereby the utilities diversion works were co-ordinated with, and undertaken just in advance of, the construction works which removed the need for the road to be opened up twice.

21.6 The Council submits that after mediation the Project generally progressed smoothly and there was no significant further increase in the cost of the project, nor any significant additional delay. The prime reasons for that was improved oversight and governance by the Council and better working relations between the parties, not because the figures agreed at Mar Hall were overly generous.

Changes in the governance and management of the project

21.7 The need for changes in the governance and management of the Project was recognised before and during the mediation process. As noted in section 20, there appears to have been an implicit agreement at the mediation that in order for the Project to continue it would be better if some individuals were not involved and if the Council took over from TIE on the client side.

21.8 A proposed revised governance structure was set out in appendix 2 to the report to Council on 30 June 2011¹⁰⁹⁷. Under the proposals, a Joint Project Forum would be established, which would bring together the principal representatives of all the key parties involved in the delivery of the project. The Forum was to be chaired by the Council's Chief Executive, Sue Bruce. The Forum would include the key decision makers from the Council, Infraco, Lothian Buses plc, as the proposed end user and operator of the tram, and Transport Scotland, as the main funder on behalf of the Scottish Government.

¹⁰⁹⁷ CEC02044271

21.9 The “principals” Joint Project Forum was set up to provide clear strategic leadership and direction to the project and would be supported operationally by a Joint Project Delivery Group. The Joint Project Delivery Group would manage the operational delivery of the project and report on progress against programme and budget. Major issues requiring consideration at a strategic level would be referred to the Joint Project Forum.

21.10 It was also recognised that it was important to have effective arrangements for political scrutiny of the Project and elected members required to have the opportunity to question arrangements for managing the project and accounting for public funds. An All Party Oversight Group was set up¹⁰⁹⁸.

21.11 A Stakeholder Forum was set up, through which the Council, as Project Sponsor, together with the contractors, could manage key relationships with stakeholders directly impacted by the Project, including organisations such as BAA Edinburgh Airport, Henderson Global Investors (St James Centre), Forth Ports and other groups such as the Edinburgh Business Forum, Essential Edinburgh, the Federation of Small Businesses (Scotland) and the Edinburgh Chamber of Commerce, as well as representatives of local communities in areas impacted by the tram.

21.12 The Council report also recognised that the revised governance arrangements proposed would have implications for the existing

¹⁰⁹⁸ Witness statement of Lesley Hinds TRI00000099, paragraph 658, witness statement of Jennifer Dawe TRI00000019, paragraphs 846 to 848

relationship between the Council, TEL and TIE and as noted below TIE was eventually effectively disbanded.

21.13 On 25 August 2011 the Council was advised of progress over the summer and recommendations on future governance arrangements. A report prepared by the Director of City Development¹⁰⁹⁹ noted that an important question had arisen since mediation as to whether there was, any longer, a legitimate role that could be played by TIE as an arm's length company that could not be met by the Council itself. In order to ensure effective oversight and delivery of the project going forward, the Council was in the process of engaging Turner and Townsend ("T&T") as project managers. T&T had previously been involved in advising on the project and had considerable experience of light rail projects.

21.14 At the beginning of October 2011 T&T was appointed as project and commercial managers for the delivery of the project within an established structure with the Council, as client, and the contractors. Julian Weatherley was the T&T Project Director.

21.15 Following the engagement of T&T as project managers TIE was wound down. On 9 November 2011 a Hive-Up Agreement was entered into whereby the Council acquired certain assets and liabilities of TIE¹¹⁰⁰. On 8 and 12 December 2011 TIE's rights and obligations under the Infracore contract were assigned from TIE to the Council¹¹⁰¹.

¹⁰⁹⁹ TRS00011725

¹¹⁰⁰ CEC01938504

¹¹⁰¹ BFB00005467

- 21.16 In January 2012 Transport Scotland and the Council entered into an agreement to modify the terms and conditions of the grant agreement and to regulate the basis upon which Transport Scotland personnel would collaborate on the project¹¹⁰². Transport Scotland was then represented at all levels in the project management and used its expertise to make useful contributions¹¹⁰³.
- 21.17 To support the new approach, Colin Smith was appointed as Independent Certifier to assist project control and certify the Contractor's interim payment applications. The idea of the role was to provide services in an independent, fair and impartial manner, although the Certifier owed a duty of care to the Council. Alan Coyle was responsible for cost reports which summarised the construction budgets, contract sums and changes.
- 21.18 T&T's post-mediation reports were formal and included detailed period reports on a four weekly basis and progress presentations to the Council executive team, initially on a fortnightly basis between October 2011 to late 2012 and then every four weeks thereafter. T&T produced change control registers, secured sign off to change orders from the Council and provided advice notes where appropriate. Weekly client progress and change control meetings were held by T&T to ensure that the Council had a full understanding of all the key issues and that changes were reviewed and actioned promptly. There was also a

¹¹⁰² TRS00014693

¹¹⁰³ Transcript of oral evidence of Vic Emery 13 March 2018, pages 120:16 to 121:1

commercial control group chaired by Colin Smith, and the four weekly interim valuation payment meetings.

21.19 Colin Smith's role as Independent Certifier role was to: (1) review T&T's cost assessment of changes where there was a difference of opinion with Infraco's assessment, (2) review Infraco's application for payment with T&T's assessment, make a determination and issue valuation certificates to the Council. The Independent Certifier chaired the valuation meetings between T&T and Infraco and facilitated discussions around any issues that arose.

21.20 After the mediation, Sue Bruce held regular twice weekly 8am morning tram update meetings on Tuesdays and Thursdays. It is submitted that the frequency and level of engagement and oversight by the Council's most senior officer was one of the reasons that the Project managed to avoid any major ran difficulties after the mediation agreement. The key project drivers of design, consents, programme, risk, construction and commercial were dealt with at weekly project control meetings. The meetings resolved matters of project management in a tightly managed way. This process was an integral component of the operational project governance arrangements. Where required, any unresolved issues would be referred to the Joint Project Forum for consideration.

21.21 It is submitted that the appointment of the Independent Certifier helped to resolve differences in opinion and avoided formal disputes. There was also a mechanism for any disputes that could not be resolved to be escalated by the Independent Certifier to the Principals. It is submitted

that this process helped to prevent any significant disputes arising or parties adopting entrenched positions that required to be referred to any formal dispute resolution procedures. This was in stark contrast to the situation before mediation.

21.22 Colin Smith became SRO as well as the Independent Certifier. Some witnesses, including Vic Emery, expressed some concern that this created a potential conflict of interest as he was the person who was meant to hold T&T to account but also to adjudicate in any dispute between the project group and the contractor¹¹⁰⁴. It is acknowledged on behalf of the Council that in an ideal world this would not be best practice. However Colin Smith himself thought that no one would have been reluctant to raise an issue with him because he was fulfilling both roles¹¹⁰⁵. The evidence from other witnesses, including Sue Bruce and Dr Keysberg and Martin Foerder, was that both the contractors and the Council were content with Mr Smith fulfilling both roles and in practice it did not lead to any difficulties between the parties or cause any increase in cost or delay to the Project. Indeed Martin Foerder identified it as one of the most beneficial changes post-mediation¹¹⁰⁶.

21.23 Colin Smith acknowledged that he did not always agree with T&T's view on the appropriate level for a payment to be made to the contractor and there were a few bumps in the road before the Project was completed but there were no major disagreements that were not capable of resolution.

¹¹⁰⁴ Transcript of oral evidence of Vic Emery 13 March 2018, pages 111:2 to 114:5

¹¹⁰⁵ Transcript of oral evidence of Colin Smith 14 March 2018, pages 147:9 to 152:13

¹¹⁰⁶ Transcript of oral evidence of Martin Foerder 5 December 2017, pages 166:16 to 168:11

21.24 Sue Bruce accepted that she might have spoken to T&T in December 2011 to ensure that they approached the contract and any disagreements arising from it in the correct manner in order to maintain good relations with the contractor but denied that she would have told them to back off. She re-iterated that while the Council was in favour of working well with the contractor, that was “*not at any cost*”¹¹⁰⁷.

How works were progressed after the settlement agreement (compared with before)

21.25 In relation to future project management and governance arrangements, the report to the Council on 16 May 2011 noted that the mediation process had resulted in a significant change to the joint working relationship between the Council, TIE and the infrastructure contractor, “*reverting more to the project partnering ethos of mutual cooperation*” set out in the main body of the original contract¹¹⁰⁸.

21.26 As a result of the mediation discussions, a priority works programme had been agreed and work had recommenced at the following locations in May 2011, namely, the Haymarket Yards, the Tram Depot (including the depot access route and a section of track towards the airport) and the A8 underpass. Some auxiliary works would also be carried out to progress detailed site investigations, clearance and demolition at several other locations along the tram route.

¹¹⁰⁷ Transcript of oral evidence of Sue Bruce 15 March 2018, pages 152:22 to 158:24

¹¹⁰⁸ CEC01914650 at paragraph 3.17

21.27 Following the mediation talks, major progress was made in clearing the vast majority of design consents for the project. The infrastructure contractor had agreed a self-certification regime that would deliver the completed work to meet the employer's requirements. Post-mediation there was a sharp increase in the number of technical approvals. Martin Foerder of BB said that this was down to the improved collaborative approach between the parties including the sharing of office space and weekly meetings. He strongly disagreed with Damian Sharp's suggestion that the increase in technical approvals showed that the consortium had been deliberately withholding solutions until after the mediation¹¹⁰⁹. Martin Foerder also agreed that the fact that Infracore was dealing directly with the Council rather than TIE, and the fact that they were sharing office space, helped. He also said that issues were resolved quickly. The fact all the partners were working closely together meant that when a problem arose, everyone worked together to identify a solution¹¹¹⁰.

21.28 The report prepared by the Director of City Development for the Council meeting on 25 August 2011¹¹¹¹ noted there had been significant progress on the commercial terms of the Settlement Agreement and good progress had been made towards the completion of agreed priority works at Haymarket Yards, the A8 underpass and the Tram Depot and test track. A detailed review of the key project budget risks

¹¹⁰⁹ Transcript of oral evidence of Martin Foerder 5 December 2017, pages 160:17 to 166:6

¹¹¹⁰ Witness statement of Martin Foerder TRI000000095 page 94

¹¹¹¹ TRS00011725

had been carried out, validated by Faithful and Gould, to ensure that appropriate risk management procedures were in place.

21.29 On 25 October 2012 the Council was provided with an update. A report was provided by the Chief Executive¹¹¹². Since signing the Settlement Agreement significant progress had been made and the project was on target to meet the revised budget and programme. The revised governance and management arrangements for the project were working well. The engagement of T&T had improved the project management arrangements and the involvement of Transport Scotland had proved extremely positive. Key future programme targets included, by the end of November 2012, to have re-positioned and renewed all major utilities. The contractual completion date was July 2014, which would be achieved. Costs remained in line with the revised budget approved by the Council in September 2011, with the cost of work to the end of period 6 for the financial year 2012/13 being £669 million.

21.30 Throughout 2013 it was reported to the Council that the project continued to be completed within the revised programme and budget.

21.31 On 14 November 2013 the Governance, Risk and Best Value Committee of the Council were provided with an update. A report was provided by the Chief Executive¹¹¹³. The project remained on course to be delivered in line within the revised programme and budget. There were no items in dispute in the period covered by the report. The governance arrangements had been revised to provide for the project

¹¹¹² CEC01891499

¹¹¹³ CEC01891500

stage moving from construction to testing and commissioning and to shadow running. While the project control input from the Council remained as before, there was greater involvement from the tram operator, Edinburgh Trams. The governance structure was shown in a diagram contained in appendix 1 of the report. The Senior Responsible Officer continued to report to the Tram Senior Management Team and the Chief Executive of the Council on a twice weekly basis. The weekly Tram Senior Management Team meeting had been reformed to the Tram Transition Board and was augmented by representatives from the Council's tram operations/work permit teams and from the tram operator to achieve the earliest possible revenue service date. The utilities contractor's final account had been agreed and signed "to date".

How works were undertaken in the on-street sections (compared with how the Princes Street works were undertaken)

21.32 At the mediation it was not possible to agree a fixed price for the on-street works because Infraco was not prepared to accept the risk of increased costs due to on-going uncertainties about the utilities diversions and other problems experiences on the route. The parties therefore agreed a target price of £39m for the remaining on-street section. By the time the Settlement Agreement was entered in to in September 2011, it had been clarified that the remaining on-street section would extend to York Place to accommodate a suitable turn-back and the target price had increased.

21.33 One of the main difficulties prior to the mediation had been that the MUDFA works had not been completed before the construction contract was started and even in areas where MUDFA works had taken place there still found to be conflicts with utilities which were discovered when the contractor opened up the ground again. Infraco had previously refused to work in the same area as the utilities contractor and relayed starting in a section until after the utilities works had been completed. Colin Smith is credited with having coined the term “*bow wave*” for a new way of working where by there was co-ordination between the utilities contractor and Infraco such that Infraco would follow closely behind the utilities contractor in the same area and there was no need to open up the ground for a second time¹¹¹⁴. Infraco also agreed to undertake some of the remaining utilities works and sub-contracted the work to McNicholas again this helped the co-operative approach and allowed the bow wave strategy to be deployed.

21.34 In relation to utilities, Colin Smith organised further investigations on key sections of the on-street works between Haymarket and York Place, in particular, to identify conflicts arising as a result of the finalised design, including the locations for overhead line poles. Trial bore holes or slot trenches had been opened up in known utility areas supplemented by radar scanning, which was ongoing, across the entire route covering both the immediate tram movement corridor and the adjacent locations for bases for overhead line equipment poles¹¹¹⁵. These further investigations had identified approximately 550 potential

¹¹¹⁴ Transcript of oral evidence of Colin Smith 14 March 2018, page 138:21 to 146:21

¹¹¹⁵ Transcript of oral evidence of Colin Smith 14 March 2018, page 131:6- 14

utility conflicts, although it was not believed that all of those lay on the critical path. Utility diversions had had a significant effect on the project, both in terms of programme delay and direct costs. Colin Smith confirmed that some of these investigations revealed that some utilities that had already been moved were in conflict with the tram and further work was required at the same location¹¹¹⁶. As part of the new co-operative approach regular meetings with utilities suppliers were undertaken and efforts were made to come to collaborative solutions where multiple utilities companies were involved. This was also aided by a better relationship with those providing the necessary consents and approvals. Initially weekly meetings were held between the various parties from the Council's roads and planning departments and the designers and utilities companies were included in the round table discussions. In addition Stephen Lewcock was appointed as a utilities project manager to aid this process and he played a vital role which it was thought had not been being performed prior to mediation¹¹¹⁷.

21.35 When work re-started Colin Smith was concerned that there was a contractor owned programme of works rather than a joint programme as would usually be the case. There appeared to be a surplus of 22 weeks built into the programme but the potential that if the contractor was delayed because of utilities or other works in an area it could lead to an extension of time. Mr Smith therefore obtained the contractor's agreement to the creation of a 22 week "*time bank*" that could be used to offset any potential extension of time. Against the advice of T&T, the

¹¹¹⁶ Transcript of oral evidence of Colin Smith 14 March 2018, pages 131:19 to 137:10

¹¹¹⁷ Transcript of oral evidence of Colin Smith 14 March 2018, pages 143:15 to 146:21

Council paid Infraco £6.45m in respect of the creation of the time bank. In the end there were no extension of time claims in relation to the completion of the contract works post-settlement¹¹¹⁸. Mr Smith felt this had the dual benefit of avoiding extension of time claims and allowing the tram to become operational and therefore revenue creating earlier.

21.36 It is submitted that it is clear that the improved working relationship between the Council as client and Infraco made a very substantial contribution to the more efficient running of the Project. The evidence taken as a whole clearly showed that Mar Hall was seen by everyone as a turning point. Even Stuart Fair who was still concerned that there would have been more scope to explore the possibility of terminating the contract recognised that after the mediation there was *“an applied focus, a betterment and application, and with a new Chief Executive in post, and driving this with external help in terms of consultancy support, it certainly saved the project”*¹¹¹⁹. Vic Emery and Sue Bruce both put this down to the improved trust and working relationships rather than the increased contract price that the contractor was being paid¹¹²⁰. Dr Keysberg had also identified improved relationship as a major part of the resolution rather than just price¹¹²¹.

21.37 In the end the Project was handed over to the Council very slightly ahead of the revised completion date and trams commenced operation on 31 May 2014.

¹¹¹⁸ Transcript of oral evidence of Colin Smith 14 March 2018, pages 152:15 to 161:23

¹¹¹⁹ Transcript of oral evidence of Stuart Fair 22 March 2018, page 134:16-21

¹¹²⁰ Transcript of oral evidence of Vic Emery 13 March 2018, pages 126:16 to 127:6

¹¹²¹ Transcript of oral evidence of Jochen Keysberg 16 November 2017, page 72:2- 11

22. **Behaviour of Parties and Consequences**

Summary

- 22.1 The Council submits that the poor working relationship between TIE and Infraco contributed to claims under the main (Infraco) contract. The Council recognises that there was fault attributable to the behaviour of both parties. However Infraco exploited the lack of collaborative approach to maximise payment under the contract. Equally TIE was reluctant to consider claims timeously which resulted in the DRP requiring to be utilised.
- 22.2 The working environment of TIE was not healthy. Staff within TIE were stressed and staff turnover was high. The fact that TIE had become solely dependent on the Project as the only project increased these tensions within TIE.
- 22.3 OB was not as fully accounted for as it should have been in the project. However OB was not a significant cause of any delay or expense.

Introduction

- 22.4 The Council submits that the main parties and stakeholders in the Project contributed to the difficulties in terms of delay, and potentially consequent costs, as a result of behaviour, which was unhelpful and in some cases unprofessional. The behaviour affected working relationships. The behaviour, in terms of consequences, was

damaging to the project and thwarted what may have been better outcomes.

- 22.5 The Council submits that the following parties' behaviour requires consideration: (1) the Council; (2) TIE; and (3) Infraco.

City of Edinburgh Council

22.6 Relationship with TIE

- 22.6.1 The Council recognises that the relationships between TIE staff and Council employees were strained at times. Councillor Mackenzie explains in his statement that this was due to the tension between TIE and Council officers. He states that Council officers would comment that their jobs were more wide ranging and difficult but that the pay levels were lower than in TIE¹¹²². This was also highlighted by Andrew Holmes who identified that a number of Council staff left the Council's employment and were employed by TIE "*at considerably elevated salaries compared with what they had been earning before*" which "*caused quite a few tensions*"¹¹²³. Outwith the Council Neil Renilson also confirmed that there was "*bad blood*" between Council and TIE staff due to staff transferred from the Council receiving pay increases and bonuses¹¹²⁴.

- 22.6.2 Whilst the Council recognises there was a need to employ TIE staff on terms competitive with the private sector generally this did not assist the

¹¹²² Witness statement of Gordon Mackenzie TRI00000086, page 21

¹¹²³ Witness statement of Andrew Holmes TRI00000046, page 102

¹¹²⁴ Witness statement of Neil Renilson TRI00000068, page 11

working relationships between TIE and the Council at levels below Senior Officers.

22.6.3 It is suggested by SETE¹¹²⁵ that Council officers withheld information from TIE. This assertion is made solely on the evidence of Gill Lindsay. In this respect Ms Lindsay's views are inconsistent with the evidence of the Chief Executive and Directors having reported to members as discussed above at paragraph 9.30. The Council submits that the evidence of Mr Aitchison (paragraph 9.30.2) and Mr Holmes (9.30.4) should be preferred. Further, and in any event, it is not suggested that any non-disclosure prevented TIE from progressing the project, or led to further costs being incurred.

TIE

22.7 Working Relationships

22.7.1 The Council has identified above the strained relationships between TIE officers and Council officers, and does not repeat those submissions.

22.7.2 More critically, in the context of contributing to the disputes arising under the contract, were the poor working relationships between TIE officers and Infracore, in particular BB officers. As Neil Renilson highlighted, people are of key importance in construction projects and that competent, professional, skilled and motivated staff on both sides can achieve the desired outcome¹¹²⁶. It is submitted that the motivation

¹¹²⁵ Page 16 of the written submissions of SETE dated 27 April 2018

¹¹²⁶ Witness statement of Neil Renilson TRI00000068, page 1

by TIE and Infraco to work in a collaborative manner to achieve the project's objectives was particularly lacking.

22.7.3 The Council relies on the submissions and observations made in section 17 of these submissions in respect of the behaviour of Infraco in the Princes Street Dispute, which would appear to have been engineered to maximise payment under the contract.

22.7.4 The poor working relationship between TIE and Infraco was the subject of evidence from both parties. Richard Jeffrey (formerly of TIE) indicated that Dr Keysberg had stated that the contract enabled Infraco to hold TIE to ransom¹¹²⁷ (a statement Dr Keysberg has since denied making). Councillor Mackenzie formed the view that the contractor was trying to get a better deal than it was entitled to under the Infraco contract¹¹²⁸. Councillor Mackenzie stated that the contractor "*knew that they had us on a hook*" when it came to seeking additional sums. David MacKay states that he "*...found Bilfinger virtually impossible to deal with*"¹¹²⁹.

22.7.5 Infraco does not dispute the poor working relationship between TIE and Infraco. Richard Walker (of BB) described the relationship as "*We had zero respect for each other.*"¹¹³⁰ As an example Mr Walker explained that "*Mr Fitchie could be extremely abusive, and not just to male members of my team.*"¹¹³¹ Mr Walker described the abuse of the

¹¹²⁷ Witness statement of Richard Jeffrey TRI00000097, page 24

¹¹²⁸ Transcript of oral evidence of Gordon Mackenzie 1 November 2017, page 52:8- 12

¹¹²⁹ Witness statement of David Mackay TRI00000113, page 105

¹¹³⁰ Witness statement of Richard Walker TRI00000072, page 60

¹¹³¹ Transcript of oral evidence of Richard Walker 15 November 2017, page 78:15- 16

gagging clause in the context of TIE providing articles for the press and stated that:

*"I have 40 years in this industry and I have never met such a group of disparate, lying, conniving, arrogant individuals in my life. To call themselves public servants is an absolute disgrace"*¹¹³².

The submissions by Bilfinger emphasise that the relationship between TIE and Bilfinger was a "*battle*", in the words of Mr Foerder¹¹³³. The relationship difficulties are also recognised by Siemens who refer to "*...tie's hostility to Infraco...*"¹¹³⁴.

22.7.6 Whilst TIE held the view that Infraco was seeking to make as much money as possible under the contract Infraco was equally suspicious of TIE's behaviour. Mr Walker is of the opinion that:

*"TIE's tactic was to put Infraco under so much pressure and attempt to make us think we were in multiple breaches of contract, that we would give in, abandon our claims for additional time and money in accordance with the Contract and proceed with the works"*¹¹³⁵.

22.7.7 The Council also notes that Infraco made it clear that it would pursue claims through all levels including the Courts¹¹³⁶.

22.7.8 It is submitted that there was a clear difference of opinion between TIE and Infraco and an absence of collaborative working. This is reinforced

¹¹³² Witness statement of Richard Walker TRI00000072, pages 48 to 49

¹¹³³ Paragraph 212 on page 110 of the written submissions of Bilfinger dated 27 April 2018

¹¹³⁴ Paragraph 239 on page 87 of the written submissions of Siemens dated 27 April 2018

¹¹³⁵ Witness statement of Richard Walker TRI00000072, page 110

¹¹³⁶ Witness statement of Joachim Enenkel TRI00000150, page 40

by the inflammatory actions and remarks by both parties, such as Mr Walker offering a fixed price of £1 billion¹¹³⁷ or from TIE's side the threat by DLA of a legal action for defamation¹¹³⁸.

22.7.9 When considering the resolutions achieved at Mar Hall considered in section 20 of these submissions, it is clear that there was scope for a more constructive relationship which may not have resolved the claims but may have resolved disputes, and consequently delay, more quickly thus reducing the cost overrun.

22.8 **Bonuses (in TIE)**

22.8.1 David Mackay's evidence in relation to whether the existence of the bonus structure encouraged those within TIE to get to contract close in 2008 was that "*I have no evidence of that whatsoever...I have no direct evidence of that*"¹¹³⁹.

22.9 **Stability of TIE & Staff Morale**

22.9.1 Councillor Mackenzie highlighted that:

*"The project had a defined life and there was no programme of other projects that TIE would be moving to, so these people were likely going to be start thinking about their next jobs."*¹¹⁴⁰

22.9.2 Irrespective of the limited life of the project Mr Renilson explained that the political uncertainty was such that "*...the fear that the project would*

¹¹³⁷ Witness statement of Richard Walker TRI00000072, page 96

¹¹³⁸ Witness statement of Richard Walker TRI00000072, page 71

¹¹³⁹ Transcript of oral evidence of David Mackay 21 November 2017, page 37:21- 23

¹¹⁴⁰ Witness statement of Gordon Mackenzie TRI00000086, page 93

be cancelled and they would be out of a job...” with variable levels of commitment from staff. This is consistent with the evidence of Matthew Crosse who stated:

“TIE staff were worried about losing their jobs if the tram project was to be scrapped”¹¹⁴¹.

22.9.3 On a related issue the turnover of staff, particularly senior officers, did not create a positive environment. Tony Rush noted that TIE staff were feeling tense particularly when senior managers such as David Mackay and Andrew Fitchie left TIE¹¹⁴². Lesley Hind’s opinion was that that the stability of TIE was affected by management changes. Neil Renilson also identified that the staff turnover was *“particularly high”* and *“the constant changes at senior management level within TIE when I was there had the effect of creating constant instability”¹¹⁴³.*

22.9.4 All these issues led to TIE being a place of work under stress and not achieving what it should have been capable of. The effects may have been lessened if TIE had alternative projects being undertaken alongside the Project.

22.10 Optimism Bias

22.10.1 The Council submits that it may be reasonably concluded that the behaviour of TIE may, to an extent, have been affected by OB. Notwithstanding this view it is submitted that a higher level of OB would

¹¹⁴¹ Witness statement of Matthew Crosse TRI00000031, page 13

¹¹⁴² Witness statement of Tony Rush TRI00000141, page 12

¹¹⁴³ Witness statement of Neil Renilson TRI00000068, page 12

not have avoided or otherwise thwarted the final cost of the project. This is consistent with the opinion of Rebecca Andrew who stated:

“With hindsight the level of risk/optimism bias should undoubtedly been higher. I do not think, however, that a more conservative view of risk produced at the time would have reflected the extent of the project’s eventual cost overrun”¹¹⁴⁴.

22.10.2 The Council submits that in considering OB the question is whether a more conservative OB figure would have brought the project to its knees. The Council is of the view that a more conservative figure for OB would not have caused the project to be terminated at an early stage, and as matters progressed the likelihood of the project being terminated (on grounds of OB) reduced. In forming that view the Council considered a number of witnesses’ evidence.

22.10.3 Those witnesses included Damian Sharp who indicated that the cost benefit analysis was not sufficient to thwart the project despite the true “best case” Benefit Cost Ratio ("BCR") falling below the benchmark 1:1 ratio¹¹⁴⁵. It is noted that Mr McGarrity later suggested that the BCR calculations required alteration to take into account public transport payments which reduced the overall benefits to the trams¹¹⁴⁶.

22.10.4 Alex MacAulay indicated that when OB was first introduced in 2003 it was not clear whether it should be used in addition to a contingency allowance. An allowance for contingency had already been applied.

¹¹⁴⁴ Transcript of oral evidence of Rebecca Andrew 13 September 2017, page 9:4- 8

¹¹⁴⁵ Witness statement of Damien Sharp TRI00000085, page 33

¹¹⁴⁶ Witness statement of Stewart McGarrity TRI00000059, page 30

Accordingly the early application of OB was unclear in terms of what should have been used/applied and what impact it may have had on behaviour and decision making. This is reinforced by the evidence of Mark Hamill who advised that when he joined TIE in May 2007¹¹⁴⁷ OB was not being used¹¹⁴⁸. The Council submits that OB therefore did not have a significant bearing in the early stages and, could be regarded as being paid lip service only.

22.10.5 The Council submits that it is worth considering if the project would have been terminated (beyond 2007) if the OB had been set at a more conservative level at a later stage. In the Council's submission there was evidence which would entitle the Inquiry to conclude that the issue of OB was not presented on a fully informed basis at the later stages which may have influenced continuing with the project. There was the evidence of the "*pockled email*" by Mark Hamill dated 27th May 2008¹¹⁴⁹. SETE's submissions suggest that Mr Hamill sought to "pockle" the figures and avoid scrutiny in order to keep the Council happy and get the project over the line¹¹⁵⁰. In the Council's submission this assertion does not bear any scrutiny as the suggestion is that absent the 'pockled' figures the project would not have proceeded. Further, and in any event, TIE's interest in the project proceeding was critical to the survival of TIE and the positions held by SETE employees such as Mr Hamill. In the SETE submissions it is suggested that the Council was

¹¹⁴⁷ Witness statement of Mark Hamill TRI00000042, page 1

¹¹⁴⁸ Witness statement of Mark Hamill TRI00000042, page 11

¹¹⁴⁹ CEC01288043

¹¹⁵⁰ Page 60 of written submissions of SETE dated 27 April 2018

aware of TIE's adjustment of the risk allowances¹¹⁵¹. This is strongly rejected, and reference is made to paragraph 4.26 of these adjusted submissions in that respect. In the Council's submission, the key point is whether the figures being provided by TIE were genuine and could be relied upon. In this respect the Council was relying upon TIE.

22.10.6 There is also the evidence in Willie Gallagher 's statement that notes:

*"I am asked whether I felt comfortable with the levels of optimism bias and risk built into the cost. In an ideal world we would have had more but we weren't living in an ideal world. The funds were capped."*¹¹⁵²

22.10.7 The Council submits that the true picture of risk and OB may not have been presented at all times. However, on balance, the Council is of the view that OB was not a direct cause of delay or cost overrun. The issue of OB may have influenced behaviour and possibly continuing with the main infrastructure contract but that it was only one of many factors which shaped and guided parties' behaviour.

The Consortium (Infraco)

22.11 Working Relationships

22.11.1 The behaviour of BB is identified above. The Council submits that the behaviour of BB officers and TIE officers equally contributed to disputes which may have been resolved with a more collaborative working style. There can be no doubt that the relationship between TIE and Infraco was an unhappy marriage. The Council anticipates that, to an extent,

¹¹⁵¹ Page 62 of written submissions of SETE dated 27 April 2018

¹¹⁵² Witness statement of William Gallagher TRI00000037, page 74

the issues arose due to the strong personalities involved. Indeed Dr Keysberg specifically appointed Martin Foerder in 2009 as “...*there was already quite a tension between the client organisation and ours...*”¹¹⁵³. In so doing Infraco recognised the difficulties of the working relationship from both sides.

¹¹⁵³ Transcript of oral evidence of Jochen Keysberg 16 November 2017, page 7:11- 12

23. **Other Issues**

Summary

- 23.1 The Council submits that there was a concern within TIE and the Council that the consortium would abandon the contract process before contract completion in May 2008. The Council was aware that issues such as funding and political uncertainty over the future of the project created a risk to bidders. The Council was also mindful that there were only two bidders in respect of the project. This caused the project to be driven forward at a time when a 'contractual pause' may be suggested to have been more appropriate. The pause was not undertaken for fear of the project not re-starting after the pause.
- 23.2 Related to the issue above was 'lock-in' namely whether the Council gave proper consideration to termination. In the Council's submission proper consideration was given to termination and not pursued as the sums expended, and disruption to the City, had to be measured against the value and asset to the project to the City. Nonetheless a pause to the contract and negotiations should have been considered more carefully, but carried a significant and real risk of termination of the project.
- 23.3 The implications for project failure differed for TIE and the Council. For TIE failure would bring an end to the Company and staff employed within TIE. For the Council failure would result in reputational damage.

23.4 The ground conditions were always known to be likely to present challenges in a historic city. However the poor utility records and extent of unknown utilities was not foreseen and caused further delays to the project.

To what extent did fear of Infraco walking away drive TIE/the Council's behaviour?

23.5 The Council recognises that there was an element of the fear of the loss of Infraco which affected the behaviour of the Council and TIE. To an extent this is similar to the issue of pausing or terminating the contract ('lock-in') discussed below. This concern drove the project and TIE forward when other options such as terminating, and more specifically a pause, may have been given further consideration.

23.6 James McEwan describes in his evidence that during March 2008 there were problems trying to align the design with the programme and agree timescales with Infraco. This was at a time when TIE was attempting to enter the contract with Infraco. Mr McEwan explained that the contract negotiation TIE had tried to achieve in the past 18 months was now being attempted to be achieved in as little as two weeks¹¹⁵⁴. As Mr McEwan put it:

¹¹⁵⁴ Transcript of oral evidence of James McEwan 18 October 2017, page 157:20 to 158:3

“...we didn’t have a terrific hand of cards to play in terms of negotiation leverage, with a bidder that had already been signalled as preferred and suchlike. And the contract structure that clearly wasn’t working”¹¹⁵⁵.

23.7 During this time in 2008 (when TIE was trying to finalise matters with BBS) there was the added difficulty that not only were BBS resisting novation but also:

“PB didn’t want to novate. PB didn’t want to be managed by BBS. They had signed up to the TIE contract but didn’t want to novate.”¹¹⁵⁶

23.8 Accordingly two key parties were not keen to enter into the agreement in early 2008. This was just before the economic crisis properly made its mark in the economy and the Council and TIE did not have a huge pool of bidders to consider. As Mr Gallagher highlighted there had only been two responses to the tender. He noted that due to there being a “clear winner” out of the two tenders the Infraco bid had been given preferred status by the procurement subcommittee¹¹⁵⁷. At that stage it would have been too time consuming to deal with two bidders and therefore to an extent the die had been cast. Mr Gallagher highlights that, on reflection, having more than two bidders would have been better¹¹⁵⁸. In those circumstances there would have been less concern or fear of Infraco withdrawing in 2008. Councillor Wheeler states that when BBS sought additional sums in May 2008 consideration was given to bringing back the unsuccessful bidder but that this would “have been

¹¹⁵⁵ Transcript of oral evidence of James McEwan 18 October 2017, page 159:4- 8

¹¹⁵⁶ Witness statement of William Gallagher TRI00000037, page 31

¹¹⁵⁷ Witness statement of William Gallagher TRI00000037, page 72

¹¹⁵⁸ Witness statement of William Gallagher TRI00000037, page 73

likely to cause a 6 month delay” and keeping BBS was the best option for “sustaining the project's momentum”¹¹⁵⁹.

23.9 Furthermore the Council was conscious that the election had already caused MUDFA to be paused whilst a review of the Project was undertaken. The Council and TIE were also aware that BBS was concerned about the project being cancelled, given the position of the SNP, and the removal of Transport Scotland in summer 2007. This made BBS concerned about where the money for their payment would come from¹¹⁶⁰.

23.10 Scott McFadzen highlighted that in October 2006 that BBS:

“...were concerned that we could spend a lot of money bidding for the job and that it might not go ahead because of political and budgetary pressures.”¹¹⁶¹.

23.11 Graeme Bissett also identified that:

“...there wasn't certainty as to the commitment of the funding, particularly the Scottish Executive...”¹¹⁶² and “...it would have been very difficult for tie and the Council to say credibly that this project would happen unless there was clear evidence that the funding would be in place.”¹¹⁶³

¹¹⁵⁹ Witness statement of Philip Wheeler TRI00000092, page 26

¹¹⁶⁰ Witness statement of William Gallagher TRI00000037, page 122

¹¹⁶¹ Witness statement of Scott McFadzen TRI00000058, page 6

¹¹⁶² Transcript of oral evidence of Graeme Bissett 31 October 2017, page 12:10- 12

¹¹⁶³ Transcript of oral evidence of Graeme Bissett 31 October 2017, page 13:3 -6

23.12 Accordingly the Council and TIE were acutely conscious that an anxious and sole preferred bidder created a significant risk of BBS simply abandoning the project. These were real risks as Joachim Enenkel confirmed: *“At times we (Bilfinger Chief Executive Board) considered withdrawing if the project would not get back to an acceptable/manageable risk profile.”*¹¹⁶⁴ This drove the project forward when a pause may have been more appropriate.

Was there an element of project lock-in on the part of TIE and/or the Council? Did the project taken on momentum of its own with no one willing or able to apply brakes?

23.13 Once the procurement strategy discussed in section 8 was determined there was little or no further refinement or alteration of the strategy to meet the changing circumstances. As Trudi Craggs highlighted:

*“no one (August 2006) stopped to consider whether there was a better strategy for the procurement process given the issues with the design. I do not recall taking part in any discussions about it...I do not remember any alternatives being given”*¹¹⁶⁵ and *“no consideration was given to delaying procurement...it seemed to me that the project had to keep programme at all costs”*¹¹⁶⁶.

23.14 Steve Reynolds of Parsons Brinkerhoff was of the opinion that it would be *“sensible”* to delay novation to allow design to be nearer 100%

¹¹⁶⁴ Witness statement of Joachim Enenkel TRI00000150, page 27

¹¹⁶⁵ Witness statement of Trudi Craggs TRI00000029, pages 16 to 17

¹¹⁶⁶ Witness statement of Trudi Craggs TRI00000029, page 17

complete¹¹⁶⁷. However Matthew Crosse recognised that whilst design would have ideally been at a more advanced stage any pausing of the programme was “*not a realistic option*” as “*the deadlines had been made public and stated in the strategic business case*” and that slippage would have cost money¹¹⁶⁸.

23.15 It was not just the views of the public from a PR perspective but also the impact directly on the public as identified by Willie Gallagher:

*“...it was important that, when we told the public we were going to do something we did it. These guys had businesses and lives to lead”*¹¹⁶⁹.

23.16 Richard Walker was also of the view that the tendering process should be “*put on hold for a year to allow the design and MUDFA contracts to be progressed.*”¹¹⁷⁰ Stewart McGarrity highlighted that a pause would cost in excess of £3m per month and, more importantly, that BBS:

*“...may lose those supply chain arrangements and be unable to proceed at all. These were balanced against the risk assessed...with potential overlap with the MUDFA works and the risks associated with outstanding consents and approvals.”*¹¹⁷¹.

23.17 Accordingly, on balance, it is submitted that the risks of a pause were too great as it may have brought the project to a permanent standstill.

¹¹⁶⁷ Transcript of oral evidence of Stephen Reynolds 12 October 2017, page 46:11- 13

¹¹⁶⁸ Witness statement of Matthew Crosse TRI00000031, page 7

¹¹⁶⁹ Witness statement of William Gallagher TRI00000037, page 27

¹¹⁷⁰ Transcript of oral evidence of Richard Walker 15 November 2017, page 18:9- 10

¹¹⁷¹ Witness statement of Stewart McGarrity TRI00000059, page 180

23.18 The Council submits that as the project gathered momentum there was an increasing reluctance within TIE and the Council to seek to slow this. It may be suggested that no consideration was given to abandoning the project however the Council maintains that termination was considered at certain stages of the project. Termination was also being considered by BB's head office¹¹⁷². However termination presented particular perils as noted by Stewart McGarrity in considering the options of termination; replacement of BB and settlement:

*"...there was legal uncertainty as to whether there was sufficient grounds at this time (late 2008) for termination..."*¹¹⁷³

23.19 Prior to May 2008 the Council gave consideration to various options including *"winding up of Tie and bringing the relevant and necessary staff into the employment of the Council."*¹¹⁷⁴

23.20 By the stage of Mar Hall, which is considered in section 20 of these submissions, the Council could have made the decision not to proceed further under the Contract, although by that time a considerable amount of money had been spent¹¹⁷⁵.

23.21 It should be noted that at Mar Hall the money spent (to date) fell below the government contribution. Therefore the consequences for the Council were not financial but were related to the interests of public funding generally.

¹¹⁷² Transcript of oral evidence of Jochen Keysberg 16 November 2017, page 56:12-25

¹¹⁷³ Witness statement of Stewart McGarrity TRI0000059, page 222

¹¹⁷⁴ Transcript of oral evidence of Jim Inch 19 September 2017, page 126:4- 6

¹¹⁷⁵ Transcript of oral evidence of Alastair Maclean 20 September 2017, page 138:21 to 139:9

23.22 As noted by Vic Emery TIE expressed a preference for separation however the Council and Transport Scotland "*were concerned with the legal and political implications of Separation and were therefore keen to pursue mediation to seek resolution*"¹¹⁷⁶.

23.23 In conclusion the Council submits that termination would not only have been a costly option once the SDS and MUDFA works had commenced but would also have resulted in works with no asset to show for that expenditure. It should not be forgotten that the tram is, in terms of its operations, proving to be a commercial success.

What were the implications of project failure for TIE and the Council and for the individuals involved in each organisation?

23.24 Failure of the project had different implications for TIE and the Council respectively.

23.25 For TIE the implications of failure were ultimately not dissimilar from the completion of the project in the context of TIE coming to an end. The Council has already identified that TIE became a one project delivery vehicle. Consequently staff were seeking new positions, and were ultimately made redundant in 2011. Stress and tension was high within TIE as previously discussed. This combined with the stress of the project had the consequence of high staff turnover. Accordingly the stability of the organisation was affected. The stress had taken its toll on staff such as Willie Gallagher whose health suffered as a consequence of his time within TIE. The legacy of the Tram Project on

¹¹⁷⁶ Witness statement of Vic Emery TRI00000035, page 6

the CV's of staff also was noted in evidence. Damian Sharp identified that:

*"...afterwards I could not get another job within transport...and I am certain that was because my previous job had been with the tram project"*¹¹⁷⁷.

23.26 The failure of the Project affected the Council and city adversely. There was real risk of significant damage to the reputation of the Council. The financial consequences of the cost overrun and damage to the local economy/businesses were also significant in scale.

23.27 Donald Anderson noted that:

*"The city's reputation has been severely damaged...and the Council has been clobbered with huge additional costs."*¹¹⁷⁸

23.28 Alan Coyle was of the view that in addition to damage to the reputation of the Council, there had been economic damage suffered by some of Edinburgh's businesses¹¹⁷⁹.

23.29 John Connarty gave detailed evidence of the costs and his statement details that the additional costs were borrowed over a period of 30 years at an annual cost of approximately £13.4m¹¹⁸⁰.

How did the position on the ground affect the Project (including MUDFA)?

¹¹⁷⁷ Witness statement of Damien Sharp TRI00000085, page 160

¹¹⁷⁸ Witness statement of Donald Anderson TRI00000117, page 132

¹¹⁷⁹ Witness statement of Alan Coyle TRI00000028, page 194

¹¹⁸⁰ Witness statement of John Connarty TRI00000153, page 6

23.30 A number of the grounds works were within the world heritage site and all the works were within a historic city. Consequently the existence of archaeology was perhaps unsurprising but the extent of the difficulties was not foreseen. In the Council's submission the scale and complexities of the ground works were principally caused by the difficulties encountered with utility works. It was the works under MUDFA which led to the scale and complexities encountered in (for example) the traffic management.

23.31 One challenging issue was the extent of the works which were unknown. David Crawley notes that: "...190 underground chambers were expected and 295 discovered, and that 27.188 km of pipes were expected and 46.575 km were discovered"¹¹⁸¹.

23.32 Stephen Bell highlighted that the TPB Report of April 2010¹¹⁸² notes that the utilities works cost 170% more than estimated to include unexpected utilities, design, and traffic management¹¹⁸³.

23.33 A further reason for difficulties on the ground was due to both the poor records of utility providers and what was uncovered during excavation. Stephen Bell identified the following difficulties: lack of accurate information from utility providers; congested sites and not having enough room; requiring to incorporate additional services: and extensive traffic management required as a consequence¹¹⁸⁴.

¹¹⁸¹ Witness statement of David Crawley TRI00000030, page 6

¹¹⁸² CEC00245907

¹¹⁸³ Witness statement of Stephen Bell TRI00000109, page 146

¹¹⁸⁴ Witness statement of Stephen Bell TRI00000109, page 14

23.34 The methods of testing for potential utility sites came under scrutiny during evidence and highlighted a number of problems. John Casserly indicated that ground penetrating radar had been used and it is limited in what it can identify¹¹⁸⁵. Mr Casserly gave the example of radar not identifying modern plastic gas pipes¹¹⁸⁶. Radar will show metal pipes but not ones directly below other pipes. Alan Dolan was equally critical of the limitations of radar.

23.35 Scott McFadzen indicated that BBS may have assumed more risk under the contract if an interpretative ground investigation report had been obtained¹¹⁸⁷.

23.36 Mr Casserly indicated trial holes were required¹¹⁸⁸. However it is submitted that it was not practicable to undertake trial holes at every potential site

23.37 Finally it is worth noting that as late as 2011 trial pits were continuing to be undertaken to establish the location of utilities.

23.38 In conclusion the ground conditions were always known to be uncertain. The Council submits that the extent of the problems which emerged was not reasonably foreseeable without extensive trial pits which in themselves would have caused further delay, disruption and additional expense.

¹¹⁸⁵ Transcript of oral evidence of John Casserly 18 October 2017, page 80:11- 15

¹¹⁸⁶ Transcript of oral evidence of John Casserly 18 October 2017, page 80:25

¹¹⁸⁷ Transcript of oral evidence of Scott McFadzen 14 November 2017, page 36:19 to 37:8

¹¹⁸⁸ Transcript of oral evidence of John Casserly 18 October 2017, page 81:12

CHAPTER 4

24. Lessons to be learned

Introduction

- 24.1 The Council has learned lessons from the Project which are summarised in the remainder of this chapter. It wishes to continue to learn from what occurred in the Project, and the recommendations of the Inquiry will inform and help shape its own views as a local authority and corporate body of how major projects can be delivered effectively in future.
- 24.2 The Council has appointed a project team to prepare a full business case in relation to the procurement and construction of the remainder of Phase 1a of the Project to Leith and Newhaven (the “Trams to Newhaven Project”). The business case is scheduled to go before Elected Members for consideration in late 2018. Although the Council wishes to learn lessons from the Inquiry which will be applicable to all major infrastructure projects that it undertakes in the future, the Trams to Newhaven Project and decisions in relation to it brings the need to learn such lessons into sharp and immediate focus.
- 24.3 There were two reviews undertaken in relation to the Project which included a consideration of lessons to be learned¹¹⁸⁹, but these focussed on relatively narrow areas and were therefore not comprehensive. They were also of a high level nature. Some analysis of lessons learned has

¹¹⁸⁹ CEC02084810 and CEC02086414

been carried out in relation to an updated business case in respect of the Trams to Newhaven Project. However, the Council is looking to develop its analysis with the benefit of the evidence before the Inquiry and on the basis of its recommendations.

- 24.4 The Council sets out below certain key lessons it has learned from the Project, grouped for ease of reference into sub-headings. The Council acknowledges that many of the lessons are not standalone and must be viewed holistically to avoid a repeat of past failings.

Project Planning

- 24.5 At an early stage of a project, the initial options appraisal and business case should be subjected to independent legal, financial, commercial and technical audits. This was not done for the development of lines 1 and 2 of the Project¹¹⁹⁰. An independent audit process at this stage should flag any significant areas of risk, allowing problematic elements of the project to be amended before committing further resource or allowing momentum to build in the project.
- 24.6 In relation to the Trams to Newhaven Project a prudent approach has been taken to the analysis underpinning the updated outline business case. The capital cost estimates and the transport forecasting methodology/results for the project were prepared by consultants and then independently audited. The financial model architecture and outputs were also subjected to a high level review.

¹¹⁹⁰ CEC02084810, page 1

24.7 At the preliminary/feasibility stage, there should also be a period of detailed consultation to allow key stakeholders and the public to have their say on the project at its inception CEC02084810, page 2. The Council should carefully consider methods of seeking feedback and how representations will be recorded and acted upon. Notwithstanding the statutory obligations which are now incumbent on the Council in relation to community empowerment, the Council must ensure that consultation exercises are not merely box-ticking exercises. A failure to gain an understanding of stakeholder requirements will likely lead to external frustration and a belief that the project is not being well-managed. It is impossible to manage expectations without first seeking to understand what those expectations are¹¹⁹¹.

24.8 An effective consultation process should minimise objections to a project, but a large scale infrastructure project will inevitably lead to some substantive objections being raised. It is important to deal with objections as early as possible, particularly where this leads to some form of negotiation. In relation to the Project, objections were not dealt with in an organised manner at an early stage, which led to valuable time and resources being used in dealing with them, particularly during the parliamentary hearing stage¹¹⁹².

24.9 The consultation undertaken to date in the Trams to Newhaven Project includes:

¹¹⁹¹ CEC02086414, page 7

¹¹⁹² See CEC02084810, pages 2 and 3

- 24.9.1 Notwithstanding the issues set out above regarding the management of objections, statutory consultation was carried out in relation to the Project, including the section to Newhaven, at inception and preliminary/feasibility stage, as part of the parliamentary process.
- 24.9.2 Regarding the current stage of Trams to Newhaven, a full public consultation is being undertaken on (a) the temporary traffic management proposed during construction of the scheme (b) the tram and streetscape design when the tram is operational and (c) the measures to be included in a support for business scheme. To encourage engagement with the public consultation letters have been sent to residents and businesses along the tram corridor, local advertising has been purchased, public information events have been held along the route along with support for business forums, engagement with organisations representing those with additional needs and attendance at community council meetings. In addition to consultation on the aspects of the project noted above this process has also allowed interested parties to meet the project team and gain information on the terms of the Trams to Newhaven Project.
- 24.9.3 Consultees have been encouraged to respond to the consultation on an online portal. In addition, those attending the public information events have been given the opportunity to comment directly on the plans and further comments and queries made directly at the events gathered and responses given after each event where required.

24.9.4 After the consultation closes the Council will engage with a selection of stakeholders including community councils, community organisations and representatives of local business to co-produce an update of the Council's proposals. After that, the Council will release a summary of the consultation comments along with a note of the responses to those comments and the updated plans for further engagement. Finalised plans will then be put before Transport and Environment Committee and Full Council along with the final business case.

Project Governance

24.10 Good governance is critical and must be clear from the outset of a project.

24.11 Where a project is to be delivered in-house (*i.e.* the Council acting as the contracting party), roles and responsibilities of project working groups, project boards and Council committees must be clearly delineated. Clear lines of communication, audit and approval must be established and put into practice. The Council has developed methods of governing in-house projects, but each project should be viewed on its own merits to ensure that governance arrangements are proportionate and robust.

24.12 A key lesson learned from the Project related to the project governance. Following mediation, revised governance structures were put in place that served the project well through to passenger service. It was recognised by the Trams to Newhaven Project very early on that it was essential to put governance arrangements in place from the outset that

accorded with industry good practice. The key principles underpinning the Trams to Newhaven Project governance structure include:

24.12.1 Strong leadership from councillors and senior Council officers, key stakeholders and the Contractor(s) selected to carry out the works;

24.12.2 Strong political support and regular reporting by officers on risks, issues and costs;

24.12.3 Clearly defined roles and responsibilities within the client organisation with clear reporting lines;

24.12.4 Clear management information used to report through all project levels; and

24.12.5 Professional project management support within the Council.

24.12.6 The above principles have guided the Trams to Newhaven Project governance since 2015 and are reflected in the Project Execution Plan which is updated regularly in accordance with good industry practice.

24.13 Although the Trams to Newhaven Project is not being procured through an arm's length external organisation ("ALEO") it is right that the Council considers how use of an ALEO can be improved in future, given the role of TIE in the Project. If a project is to be delivered by an ALEO, it is crucially important to implement and practise good governance. The inadequate oversight of TIE by the Council and poor lines of communication between the two entities contributed to the problems

encountered by the Project. The Council has established a “Companies Hub” to provide greater oversight and scrutiny of all Council ALEOs¹¹⁹³.

24.14 Guidance on the good governance and operation of ALEOs was published by Audit Scotland in 2011¹¹⁹⁴. In a follow-up inspection report in July 2014¹¹⁹⁵, Audit Scotland stated that the Council had introduced revised arrangements for its ALEOs, which accorded with good practice, albeit that they were still being implemented at the time of the report. The Council continues to work towards establishing and maintaining best practice for all Council ALEOs.

24.15 The Council considers that it remains appropriate to use ALEOs in certain circumstances for major projects. ALEOs can offer reduced costs, streamlined management and flexibility.

24.16 However, the use of ALEOs can lead to increased risk if not managed properly. Given the issues experienced between the Council and TIE on the Project, it is worth noting what arrangements will be put in place to ensure that ALEOs used to deliver Council projects are properly managed:

24.16.1 A decision to use an ALEO to deliver a project must involve an appraisal of the options available and a sound business case, including feasibility and risk assessments.

¹¹⁹³ Council Report 30 June 2016 – item 8.2 "Council Companies" at paragraphs 3.31. to 3.34 published at http://www.edinburgh.gov.uk/meetings/meeting/3978/city_of_edinburgh_council

¹¹⁹⁴ “Arm’s Length External Organisations – Are You Getting It Right?” published June 2011 at http://www.audit-scotland.gov.uk/docs/local/2011/nr_110616_aleos.pdf

¹¹⁹⁵ Reported to the Council’s Governance, Risk and Best Value Committee on 14 August 2014 (Item 7.5) published at http://www.edinburgh.gov.uk/meetings/meeting/3472/governance_risk_and_best_value_committee

24.16.2 The Council must specify the business practices and standards it expects the ALEO to observe from the outset. The ALEO's objectives must align with the Council's project objectives and overall policy objectives. Robust funding and service level agreements must be in place, setting out the relationship between the Council and the ALEO.

24.16.3 The Council must set clear criteria for appointing representatives to the board of the ALEO and their required skills and experience¹¹⁹⁶. Incentive schemes must be appropriate, proportionate and not at risk of potentially driving the wrong behaviours. The Council acknowledges that the incentive scheme in operation at TIE may have been, at times, counter-productive¹¹⁹⁷.

24.16.4 Governance arrangements must be clear and implemented at the outset of a project to ensure that the Council can effectively scrutinise performance and hold the ALEO to account, monitor costs, assess performance and risk and engage service users and citizens. The governance arrangements must set out the roles of boards, committees and the Council in the articles of association and other constitutional documents. All involved in the project must understand their role on the board. Any conflicts of interest must be addressed. Minimum expectations on frequency of board and other committee meetings must be set including quoracy requirements.

¹¹⁹⁶ The Tram Project Director had rail experience but no roads experience, which was an integral part of the project (CEC02086414, page 7)

¹¹⁹⁷ E.g. this may have led to premature Financial Close (CEC02086414, page 7)

24.16.5 The Council must receive good quality monitoring information from the ALEO so that it is aware of its finances, risks and performance. The Council must also have robust information access rights in relation to the contractor, for audit purposes. The Council was not able to access certain contractor information on the Project, particularly in relation to areas of work where the contractor could self-certify.

24.16.6 The Council should regularly consider how well the ALEO is meeting its objectives and if the ALEO is providing value for money. The Council should require full audited accounts and reports from the ALEO to a standard at least that of a medium sized company with no reporting exemptions. Regular reviews must be undertaken to ensure that the ALEO remains the best option for service delivery and swift, decisive action should be taken when problems arise.

24.17 Where a project is significant in scale, professional project management support should be appointed, with experience of large scale projects in the relevant industry. It should be noted that the Trams to Newhaven Project has appointed a consultant team for the project with the relevant industry experience. Strategic advice and project leadership is provided by Anturas Consulting Limited which brings significant experience of light rail project delivery in the UK and Ireland. The Directors of Anturas all took up key roles on the Project following mediation in 2011 and contributed to the successful delivery. Overall project and commercial management is provided by Turner & Townsend which was contracted directly by the Council in 2011 to take over the project from TIE following mediation. A number of the key personnel that helped deliver

the Project have been retained in the current team. Technical advice on the Trams to Newhaven Project is provided by Atkins which is a global multi-disciplinary consultant with extensive experience of delivering complex light rail projects around the world. The technical team advising on the Trams to Newhaven Project have requisite light rail experience.

- 24.18 A lessons learned exercise should be conducted after every project in order to promote continuous improvement in management of Council projects.

Allocation of risk

- 24.19 The transfer of risk to the private sector as envisaged in the Project procurement strategy was not achieved. The Council must learn lessons to ensure that when it sets a risk profile for a project, it is achieved in practice.
- 24.20 In order to achieve the desired risk profile the Council should ensure that sufficient expertise is available either internally or through the use of external advisors to fully understand the risks of the project. The Council should understand the market appetite to risk through market consultation to ensure that risks can be mitigated, where possible in a cost effective manner. All risks should be monitored throughout the project with industry best practice risk analysis utilised throughout the project and steps identified and completed to mitigate those risks which remain with the Council. The impact of Optimism Bias should be fully

understood as part of that strategy and accounted for at the appropriate time.

24.21 The Trams to Newhaven Project has maintained a risk register from the inception of the project which is updated regularly with input from a range of technical, commercial, financial, legal and procurement professionals.

24.22 Once risks have been subject to a detailed impact assessment, Quantitative Risk Assessment (QRA) modelling is used to evaluate the expected impacts of risk in terms of cost (QCRA) and schedule (QSRA), at any given confidence level. For the Trams to Newhaven project the project team has developed an integrated QRA approach to provide a Complete Cost Risk Assessment. This incorporates assessments of the main sources of uncertainty to a project as illustrated below:

24.22.1 Discrete cost risks: events that may occur and have cost impact to the project. This is built from the contents of the regularly maintained risk register;

24.22.2 Estimate uncertainty: assessment on uncertainty within the cost plan;

24.22.3 Cost of schedule delay: outputs of QSRA (inputs are the regularly maintained risk register, assessment of programme uncertainty and project's programme) linked to estimated milestone delay costs;

24.22.4 Unknown unknowns: allowance made for events which are currently unforeseen.

- 24.23 This risk work has been used to develop the risk allowance for the project, as well as the optimism bias used in the economic evaluation. As the project progresses into contract award/project delivery stage QRAs will continue to be used as a management tool on the project and subject to independent audit.
- 24.24 The risk work on the project also informed on the commercial delivery strategy which was developed using a bottom up approach to risk management and apportionment. This work also enabled the project team to instruct external legal advisors responsible for contract drafting to ensure the contract drafting reflects the project risk strategy. Further work is being undertaken of the risk analysis undertaken to date to ensure that it accords with latest industry best practice.
- 24.25 Allocation of risk should be clearly set out in the procurement documentation and reflected in the final contract entered into. Industry standard contracts should be used wherever practicable to provide a degree of comfort that contractual provisions are robust, understood on an industry-wide basis and have been tested. This extends to dispute resolution provisions. Formal market consultation should be undertaken in advance of the procurement process in order to road test the delivery strategy. The Trams to Newhaven Project uses NEC4 standard form contracts throughout.
- 24.26 Although not a feature of the Trams to Newhaven Project, particular care must be exercised when a construction contractor is appointed to work to third party designs. Responsibility for risk must be clearly

delineated and understood, ensuring that there are no obvious lacunas or areas for significant dispute.

24.27 As referred to above, the contract documentation must allow the Council appropriate access to information in order to audit the contractor's progress.

External legal advice

24.28 External legal advice should continue to be sought in relation to major infrastructure projects. The Council's internal legal team is set up to advise the relevant client department on commercial aspects of projects but does not have the specialist expertise or capacity to act as sole legal adviser on a major project. It is also appropriate that the Council should externalise an element of legal risk to the private sector in relation to such projects.

24.29 The Council should be entitled to rely on the expertise of and advice from its external advisers.

24.30 If a project is being delivered through an ALEO, the Council must carefully consider to what extent there is a conflict of interest between the parties and whether this necessitates the appointment of separate legal advisers. In relation to the Project, the interests of the Council and TIE were deemed to be generally aligned. However, the sole focus of TIE on delivering the project and the far wider interests of the Council dictated that this confluence of interest was not as clear-cut as may have been assumed. As above, the objectives of Council ALEOs should

align with the overall goals of the Council. Where there is the potential for conflict, the appointment of separate professional advisers should be considered and the reasons for the decision recorded.

Minimising disruption

24.31 From a practical perspective, lessons have been learned in relation to minimising disruption for the public. The traffic management proposed for the construction phase of the Trams to Newhaven Project allows for large work sites to minimise changes to traffic management and route changes attendant upon that throughout the works. It also provides an element of risk mitigation as the Contractor will be able to work across a larger site, allowing for an element of work flow around unforeseen issues. The Council should also try to complete all road works related to a project at one sitting, to avoid the disruption associated with multiple closures. The Trams to Newhaven Project therefore proposes a "one dig" approach in that road closures will be maintained during utility diversion works and installation of infrastructure.

24.32 Disruption during construction inevitably makes it more difficult for local businesses to sustain trade and lessons from the Project are being taken on board for the Trams to Newhaven Project. Subject to approval of the Trams to Newhaven Project, the Council will be working with local business, business groups, civic organisations and other interested parties to create bespoke and targeted support for business plan for affected areas. This is likely to include (again, subject to political approval):

24.32.1 A financial contribution targeted at small businesses to help maintain business continuity;

24.32.2 A potential reduction in rates to be agreed with the Lothian Valuation Joint Board;

24.32.3 Logistics Centres at key locations to get deliveries in and goods out of local business;

24.32.4 Maintaining permeability for shoppers along Leith Walk by introducing dedicated crossing points at 100-150m centres during the works;

24.32.5 Customer service and wayfinding staff to help people move around the area during construction;

24.32.6 Open for business campaigns;

24.32.7 Events and activities to encourage people into the area; and

24.32.8 Free business improvement workshops for all affected businesses.

Conclusion

24.33 The Council looks forward to receiving the recommendations of the Inquiry so that future delivery of major projects can be aligned with those recommendations. The Trams to Newhaven Project has been developed in line with those lessons learned previously identified by the Council as outlined in this paper. In addition, appropriate audit, challenge and review by independent advisors has been a feature of

the Trams to Newhaven Project and that will continue throughout the project to ensure that industry good practice is maintained throughout.