

**The Edinburgh Tram Inquiry**  
**Witness Statement of Kenneth Hogg**

Statement taken by Farrukh Iqbal on 5 and 6 July 2016 in the presence of Jennifer Jack, Solicitor, Harper Macleod.

My full name is Kenneth James Hogg. I am 48 years old. My date of birth is [REDACTED]. My contact details are known to the Inquiry.

My current occupation is as the Scottish Government Director for Local Government and Communities as a senior civil servant. I had two periods of involvement with the Tram Project. The first period was as Head of Transport Division 3 within the then Scottish Executive, between approximately October 2004 and October 2005. That Division had responsibility for the Scottish Executive's engagement with the Edinburgh Tram Project. My second period of involvement subsequently was a non-executive director of TIE (TIE) and later TEL (TEL). I was appointed as a non-executive director in September 2006 for a period of three years with the possibility of renewal. My appointment was renewed and extended in October 2009 and I resigned from that role in May 2011.

Statement:

**Part 1**

**Introduction**

1. My professional background began when I first joined the Scottish Office of the UK Government in 1990. I have over 25 years' experience in Government. My experience includes working with public transport projects, including the procurement of rail services and rail infrastructure projects, and I have

previous experience of corporate governance. I have an understanding of the public sector and the public policy context within which the Tram Project was being developed, and I am a chartered director.

2. My first involvement in the Trams Project was when I was head of Transport Division 3 within the then Scottish Executive. My second period of involvement in the project was when I was one of four non-executive directors of TIE. I undertook that role in a personal capacity, I was not representing the Scottish Executive. I applied for the role of non-executive director through open competition. It was advertised in the newspapers and I was appointed by the City of Edinburgh Council ("CEC"). My employer, the Scottish Executive, was aware that I was applying for the role and I had their permission to apply for it. I did not accept the £12,000 a year financial remuneration that went with the non-executive directorship because of my employment in the public sector.
3. I was chair of the TIE board's and TEL board's Audit Committee during this period. I chaired 16 meetings of the Audit Committee over that period of 52 months, between my appointment in September 2006 and my resignation in May 2011. The first meeting of the TIE Audit Committee I chaired was on 26 February 2007 and the last was on 18 November 2009. In line with wider corporate governance changes, discussed later in this statement, the core functions of the TIE Audit Committee were transferred to the TEL Audit Committee around that time, and I became Chair of the TEL Audit Committee. The first TEL Audit Committee which I chaired was held on 5 May 2010 and the last was held of 16 March 2011.
4. If I begin with my role as head of Transport Division 3 between approximately October 2004 and October 2005. This was one of six divisions which were then part of the Transport Group in the Scottish Executive, which were responsible for developing and delivering policy in relation to all transport matters. My role was as head of the Division which had responsibility for, amongst other things, rail matters.

5. In my second role, I was appointed in September 2006 as a non-executive director of TIE, the TIE board comprised the chair, the four non-executive directors, four councillors, the chief executive of TIE and other senior council officials. The role of the board was to provide strategic direction and control of the company in line with its purposes set out by its owner, CEC. The job description for the non-executive director role said that the successful candidate would be expected to lead and direct the company at a strategic level. The role was essentially to provide corporate governance in line with the duties of directors, as set out in the Companies Acts. As a board member, I played a part in the corporate governance of the company and in setting the direction of the company through the formulation of strategy. The executive management team were responsible for the operational running and management of the business. As a non-executive director, I had no executive role. In other words, I had no delegated executive responsibilities, but I was expected to bring a wider perspective and experience to the board, including in relation to the duty to bring independent judgement to bear on issues of strategy, performance and resources.
  
6. Finally, the role of the TIE Board's Audit Committee was to evaluate risk management and internal control; to maintain oversight over external and internal audit functions; to review the accounts and financial statements, including any accounting issues which might affect financial reporting.

## **Governance**

7. I will outline the roles and responsibilities of TIE, TEL, Tram Project Board ("the TPB"), CEC and Transport Scotland ("TS"), how they worked together and their position in the governance structure hierarchy. TIE, when it was established, was responsible for the design, procurement and delivery of a suite of transport projects. Latterly its scope was reduced to the Tram Project alone. TEL was a company set up to oversee the integration of the Edinburgh tram and bus network, and TEL subsequently became the owner of TIE. The TPB monitored the execution of the tram project and was a sub-committee of TEL. CEC owned the companies involved: TIE, TEL and Lothian Buses.

Memorandums of understanding and operating agreements between CEC and those companies set out the terms of operation for the companies. TS was the major funder of the Edinburgh Tram Project. It committed £500 million to the project.

8. The governance arrangements changed over the course of the Tram Project. In December 2009, they were streamlined when the ownership of TIE was transferred to TEL. TIE remained responsible for all day-to-day management, control and execution of the Tram Project. TEL had responsibility for strategic decisions. The roles and responsibilities of TEL were set out in a new operating agreement signed by CEC and TEL. There was a separate memorandum of understanding between CEC and TIE, which was updated. Those documents clarified that TEL was now in charge, except in matters reserved to CEC; CEC would be informed of and have the final say on cost increases of more than £1 million, any delay of more than three months, any change to service design or service pattern in the Final Business Case. The TPB was established as a formal committee of the TEL board, with delegated responsibilities, and the TEL board membership was also revised at that point.
9. In my view the relevant bodies were able to exercise effective governance and control. The arrangements were complex but also necessary to reflect the circumstances at that time. For example, at the point at which I joined the board of TIE as a non-executive director, TIE was managing a suite of infrastructure projects and the Tram Project was not even necessarily the largest of those projects. In financial costs, that would have been the Edinburgh Airport Rail Link. The arrangements also reflected the fact that it was necessary to facilitate the involvement of different parties, including councillors. Councillors attended all TIE and TEL board meetings.
10. It is important to note the range of projects that TIE had been asked to take forward at various points in time. I have already mentioned the Edinburgh Airport Rail Link. TIE was also responsible for developing Fastlink, which was a guided busway; and for developing and delivering the Ingliston Park and Ride facility. It had a role in overseeing and supporting the delivery of the

Stirling-Alloa-Kincardine railway. It had what it called its portfolio projects, where it had lesser advisory roles on projects involving the Forth Estuary Transport Authority, the Cross Forth Ferry project and a waste management project.

11. I am asked if I was concerned about the governance arrangements. At the point at which the arrangements were streamlined, I agreed that that was a helpful thing to do. It was made possible in part because at that point TIE's involvement with the wider range of projects had diminished and there was more of a single focus on the Edinburgh Tram Project. Therefore, it made sense that the streamlining which took place at the end of 2009/beginning of 2010 was a sensible improvement to the corporate governance arrangements. I thought that the roles and responsibilities of each of the bodies involved in the delivery and governance of the project were sufficiently clear. I did not feel that I was unable to carry out my duties as a non-executive director or that the TIE board as a whole was unable to exercise direction and control over the company. I did not feel this adversely affected the independence, objectivity and effectiveness of the governance arrangements, by leading to a merging or overlap of the roles of the different bodies,
  
12. I am asked if I felt that cross-membership adversely affected the independence, objectivity and effectiveness of the governance arrangements. I did not feel that that was the case. In my view, the cross-membership of a few individuals who were on a few of these boards was a beneficial thing to ensure that the Tram Project was being taken forward in a way that was fully informed by wider relevant factors and that enabled a single integrated transport system for Edinburgh to be delivered. For example, it was very important that Lothian Buses were involved with the process of the Tram Project development, given that the intention was to deliver a single integrated system for Edinburgh. The cross-membership of people involved in Lothian Buses and, for example, the TIE board, helped enable that. The Chief Executive of Lothian Buses attended TIE board meetings and there was cross-membership between TEL and TIE. The governance structures allowed board members of the different organisations to exercise effective control over

the project. TEL was ultimately responsible for the Tram Project through its ownership of TIE and within the conditions set for it by CEC.

13. Several years previously, in my role as Head of Transport Division 3 within the Scottish Executive, in a memo dated 18 August 2005, I wrote to the Minister of Transport to seek the Minister's agreement to release money to conclude development of the Outline Business Case (document reference **TRS00001917**). Annex A to the memo includes a summary of the procurement strategy set out in the interim outline business case. On page 4, under the heading, "*Outstanding issues*" I state that "*There is general agreement across all stakeholders and financial advisors that TIE's proposed procurement strategy will require increased attention to governance issues.*" My recollection is that the statement refers to the fact that the procurement strategy being proposed and undertaken by TIE was to separate the procurement of different elements of the contract and to use a phased construction process. That is why governance issues would have required increased attention, compared to a process which had carried out all the works under a single governance structure. In doing so, TIE had taken into account lessons learned from other light rail projects. The Audit Scotland 2011 report on the Tram Project refers to TIE having taken lessons from other light rail projects and refers to TIE learning lessons from the National Audit Office's conclusion that in five out of seven light rail projects in England which had been examined; the design, build, maintain and operate form of contract could result in higher construction costs. Consortia might not be best placed to bear all the revenue risks of running a light rail system and the contract structure gave contractors the scope to play to their strengths, therefore reducing risk. The procurement strategy required increased attention essentially because of the separation of the procurement of different elements of the project into discrete contracts that necessarily required increased governance attention. I do not know whether the governance issues were resolved because I left that role in October 2005 and then had no involvement with the Tram Project for a further year before I was appointed as a non-executive director in September 2006. To some extent, the appointment of four new non-executive directors, including myself, might have been a response to those issues. I am not in a

position to say what else happened between those two dates. In that memo, I go on to say that the Executive is tackling risks such as costs increases "Through discussion and consideration of tighter project governance, including the potential for the Executive to maintain a more direct influence on TIE rather than indirect influence through CEC". I do not recall in detail what "tighter project governance" meant at that stage and how it was to be implemented. I do recall that the Scottish Executive was attending TIE board meetings regularly during 2005 during which period I had the responsibility for implementing tighter project governance. For example, on 25 October 2004, I attended the TIE board meeting along with John Ewing. On 22 November 2004, I attended the TIE board meeting. On 20 December 2004, John Ewing attended the TIE board meeting. On 25 January 2005, I attended the TIE board meeting. On 28 February 2005, Damian Sharp attended the TIE board meeting. On 21 March 2005, Damian Sharp attended the TIE board meeting. I do not have records for the next few months, but I do have one indicating that I attended the TIE board meeting on 22 August 2005. I do not recall what the potential options were that the Executive was considering to maintain a more direct influence over TIE. I cannot comment further because I left that role in October 2005 and I had no further involvement in the Edinburgh Tram Project from within the Scottish Executive or Scottish Government.

14. In an email from Willie Gallagher to me, dated 15 December 2007, about the draft operating agreement between CEC and TIE (document reference **CEC01509153**), Willie Gallagher says that "*We have resolved the governance conflicts which would have put TIE in a bad place*". I do not know what was in Willie Gallagher's mind. My own concerns were set out in my email of 16 December 2007, sent at 18.47, (document reference **CEC01509164**). Specifically, I was concerned that the early draft of the operating agreement did not provide for CEC's Trams Monitoring Officer (TMO) to be a member of the TPB. I felt it was essential that the TMO was a member of the TPB in order to avoid setting up parallel governance structures. I was also concerned that the draft seemed to propose that CEC not only approve the remuneration policy for TIE staff but also decide on its application, in other words, taking

decisions about individuals. That seemed to me to cut across the responsibility of the TIE Remuneration Committee.

15. A draft paper was circulated for discussion on 25 November 2008 entitled "*Governance performance and restructuring options*" (document reference **CEC01162045**). It discusses some of the weaknesses of the governance structure. It says there is "*one company too many*" and that TEL was created in 2004 to bring in Lothian Buses at a time when relationships were poor. The paper proposes to create a single legal entity which would clarify and streamline responsibilities. This would be done by having TIE take on the responsibilities of TEL. Given the changing project responsibilities of TIE which I mentioned earlier I agreed that there was scope for streamlining the roles and responsibilities of TIE and TEL. I agreed that TIE was being seen as being accountable for the Tram Project, but that that accountability was not optimally aligned with its actual responsibilities. I agreed that there was overlap between discussion at the TIE board and the TPB and that unnecessary duplication could be removed. These proposals were put forward in due course. The ownership of TIE was transferred to TEL. There was a need for reform in late 2008 because of the complexity of the Tram Project and the slow mobilisation of the infrastructure contractor.
  
16. Deloitte undertook a review of the governance arrangements within TIE and published its report in March 2009, (document references **CEC00111616** and **CEC00111617**). Amongst other findings it reported that the governance structure gave rise to "potential ambiguity" as to where decisions were made and ratified. It recommended a merging of TIE and TEL's functions. The draft review was discussed by the Audit Committee, which I chaired at its meeting on 22 January 2009. In its consideration of the draft internal audit report undertaken by Deloitte, the Audit Committee agreed with the draft report's conclusions. In that report, which was titled, "*Review of governance*" and its reference number was 2008-01 (document reference **CEC00111617**), the report said "*The governance arrangements which were developed as part of the business case for the Edinburgh Tram Project appeared to have been operating effectively. No control weaknesses were noted in relation to the*



*current governance structure. However, there are opportunities to improve the current arrangements as the project moves from the construction phase through to commissioning and operation over the next couple of years.*" The report goes on to say *"The creation of a single legal entity owned by CEC, encapsulating TIE, TEL and Lothian Buses, would help streamline governance arrangements."* Those views, which were put forward by Deloitte, our internal auditors, were views which I and the rest of the Audit Committee agreed with. The governance arrangements were streamlined in line with these findings later that year including with the transfer of ownership of TIE from CEC to TEL, and the re-establishment of the TPB as a sub committee of the TEL board. Two legal entities remained with the continued existence of the two companies, and the objectives around streamlining and reducing potential for ambiguity were achieved by the transfer of ownership.

17. David Mackay was chair of TEL and had been appointed at that stage as the interim chair of TIE. He was subsequently confirmed later as the chair of TIE. That would be an example of the cross-membership I referred to earlier, which in my view was a helpful development. My recollection is that at that meeting the chair of TIE, David Mackay, was able to inform the Audit Committee, and indeed the TIE board, that discussions with CEC were already underway to address this issue. In other words, Deloitte was commenting on an issue which was already understood and was a matter of active discussion between CEC and the chair of TIE and perhaps others.
18. The minutes of the TIE board meeting on 26 August 2009, (document reference **CEC00736751**), record that *"GB updated the board on the outstanding matters to be resolved in regard to governance, noting that the legal drafting is currently under review by CEC legal services. An urgent conclusion to matters is being pursued"*. I have checked my papers for that board meeting and the presentations given at that board meeting and I can find no further reference which would relate to that comment. I could speculate that the phrase *"legal drafting"* refers to the drafting of a revised operating agreement or memorandum of understanding, but that is my speculation at this point. I do not recall what I knew at the time.

19. In an email discussion from September 2009 (document reference **TIE00033729**), involving myself, in which Graeme Bissett recommends winding down the TIE board, transferring much of its functions to the TEL board, but keeping the slimmed-down TIE board desirable for contractual and tax purposes. My views were set out in my email to Graeme Bissett dated 30 September 2009, (document reference **TIE00033729**). Essentially, I agreed with the course of action being recommended for the reasons that I cited in that email. The governance arrangements were subsequently streamlined, as recommended, and were approved by CEC on 17 December 2009.
  
20. The minutes of the TIE board meeting on 16 December 2009 (document reference **CEC00531325**) report that this might be the last formal TIE board meeting and would be replaced by the new TEL board. The TIE board did meet subsequently on at least two occasions that I can identify from my records. It met on 30 June 2010 to approve the accounts for TIE and to approve the appointment of external auditors. It met on 9 February 2011 to agree the appointment of Vic Emery to the TIE board. These were necessary meetings of the TIE board to comply with corporate governance best practice and procedures. They were not meetings of the TIE board which discussed the substantive tram issues. So technically, the board met at least twice more, but it only met for those corporate governance purposes. I sat on the TEL board from that point. All the four non-executive directors of TIE were appointed as non-executive directors of TEL. This was something which had been recommended by CEC and to which they had given their approval.
  
21. A letter dated 9 February 2010 from Deloitte to Stewart McGarrity acknowledged the changes to the corporate structure relating to TEL, TIE and CEC (document reference **CEC00111629**). The ownership of TIE was transferred to TEL. TIE had previously been owned directly by CEC. Both companies remained in existence, but one now owned the other. Their roles and responsibilities were now set out in a new operating agreement, signed by CEC and TEL. A separate memorandum of understanding was updated between CEC and TIE. These clarified that TEL was now in charge overall, except in matters reserved to CEC. I referred to these matters earlier,

essentially the reserved matters were cost increases of more than £1 million; any delay of more than three months and; any change to the design or service pattern in the Final Business Case. The TPB was now established as a formal committee of the TEL board with delegated responsibilities.

22. The TEL board membership was revised and these appointments are set out in the Audit Scotland 2011 report on page 32, document reference **(ADS00046)**. The TEL board membership was revised to include six councillors, not four, which had been the case previously with TIE. It included the Finance Director and the Director of City Development of CEC. It included the Managing Director of Lothian Buses. It included the bus/tram integration Director and it included the Chief Executive of TIE, who also became the Chief Executive of TEL.
  
23. I believe the last meeting of the TIE board under the previous corporate governance arrangements was on 16 December 2009, after which point it ceased to meet regularly, apart from the occasions which I referred to earlier such as 30 June 2010 and 9 February 2011. The TIE board's main corporate governance functions were now transferred to the TEL board, and the TEL board met approximately monthly from that point onwards. The TPB became a formal sub-committee of the TEL board. This move clarified the relationship between the TPB and the TEL board.
  
24. The minutes of the TEL board meeting 10 February 2010 (document reference **CEC00475301**) quotes "*The TIE governance powers were now transferred to TEL and the TEL board will retain control over major changes in scope. TEL board will give the TPB delegated authority up to £545 million.*" These minutes also set down the matters that must be reported to CEC. From what was reported to the board, the transfer of power did take place. The roles of TIE and TEL now were in line with my previous explanation, at paragraphs 23 and 24. The TEL report identified the matters that must be reported to CEC, and CEC councillors and senior officials were also present at every meeting of the TEL board. Certainly senior CEC officials were present at every meeting of the TPB in addition to formal reports. So CEC was

not relying on regular reporting to know what was going on. CEC were present at every meeting of the TPB.

## TIE

25. I have some understanding of the reasons for TIE's creation from my involvement with the Tram Project in the Scottish Executive and in previous Scottish Executive roles before I took on my responsibility for our engagement with the Tram Project. My understanding is that the key issue was a lack of existing in-house experience and expertise within CEC to manage a public transport project of this size and complexity, and indeed to manage a portfolio of public transport projects which far exceeded the scope of the Tram Project alone. The largest rail infrastructure project which CEC had managed previously, at least in recent years, was the construction of the Edinburgh Park rail station which opened in December 2003. That cost approximately £3 million to build. I believe the CEC had less than ten staff working on that project. The Edinburgh Tram Project and the wider portfolio of projects, including the Edinburgh Airport rail link, were many times bigger and much more complex than public transport infrastructure projects that CEC, or indeed any other individual Scottish local authority, had responsibility for previously. Additional expertise and capacity was therefore required. My understanding is that the decision to create an arm's length body and specifically a private company limited by shares, as opposed to simply increasing the size of the council itself, was informed by first of all the perceived advantages of having a bespoke specialist organisation, focussed on managing a portfolio of public transport projects of which trams was one, and secondly, the flexibilities which that option brought in being able to offer market competitive terms and conditions of employment which a local authority would not have been able to offer.
26. The role, remit, duties and responsibilities of TIE were set out throughout this process in TIE's memorandum and articles of association. The first was "*To promote, support and/or effect the development, procurement and implementation of projects defined or referred to in an integrated transport*

*strategy, as determined and varied from time to time by CEC and to do all such other things as are incidental or conducive to the attainment of those objects."* The important point is that throughout this process, what TIE and what TEL could and could not do was not an arbitrary matter. Their roles and responsibilities were set out clearly in their articles of association and memoranda – which were determined by the company's owner, CEC.

27. In regards to powers formally delegated to TIE, by whom and when, I will comment here specifically about the Edinburgh Tram Project. I am conscious that TIE had responsibility for several other transport projects. This was set out initially in CEC/TIE written operating agreement. For example *"TIE hereby agree to provide the services to the council throughout the duration of this agreement in order to assist in, carry out, promote, manage and administer the project."* Later, these powers were set out in an updated memorandum of understanding between CEC, TIE and TEL. Again, that is where the formal delegation of powers was set out. TIE did the various things required to deliver what was asked of it, for example, by the letting and managing of multiple contracts to create the Edinburgh tram scheme. TIE was the contracting party.
28. Initially TIE formally reported to CEC. Latterly, TIE was owned by TEL. It is important to be careful with the terminology here. The staff who were working on the Edinburgh Tram Project - which would vary over time up to about 100 members of staff - were employed by the company called TIE. So in one sense *"TIE"* means all the staff who were working on the project. That is a separate thing from there being two companies. There was TEL and TIE. So at the point at which TIE became owned by TEL, the non-executive directors of TIE also took up non-executive directorships of TEL. Therefore, the staff were being questioned by the TEL board, which included the non-executive directors and the councillors and the council staff, for example. So staff who were employed by TIE were in a sense reporting to the board of TEL, which in turn submitted regular reports to CEC who owned TEL. In addition, the council were part of the TEL board.

29. With regard to the formal and day-to-day relationship between TIE and TEL, each company had a distinct purpose which changed over time. The day-to-day engagement is really a matter for the operational management of the companies. It was not the case that there was contact between TIE and TEL at the level of non-executive directors, not least because in some cases they were the same people, latterly. Likewise, between TIE and the TPB, the TPB was not a company board and that is an important distinction. It was a sub-committee, latterly, of TEL and so the engagement between the non-executive directors on TIE and the TPB took place at meetings. One of the changes that took place was that in order to avoid having the same conversation twice, the TIE directors would attend or were invited to attend some meetings of the TPB and therefore were able to engage in those meetings with members of the TPB. My recollection is that at the point at which I joined TIE as a non-executive director, the meetings that I attended were TIE board meetings. There was a point during 2007 when it was agreed that it made sense to hold the TIE board meetings on the same morning as the TPB meetings and for TIE board members to be able to be present in the Trams Project Board meetings in order to avoid having the same discussion twice. For example, if they were talking about a particular technical matter, perhaps to do with utilities diversions or with the contract, the conversation would be had with all the relevant people in the room just once. That change took place during 2007, I believe, in addition to the company ownership structure which I mentioned earlier - and that happened later - whereby TIE became owned by TEL.
30. At particular points in time, there were certainly occasions when TIE employees were under a lot of stress because of the nature of the dispute that arose. Like other Directors I was concerned for their welfare, but I did not have concerns about TIE itself. My views reflected those in the 2007 Audit Scotland report about the Tram Project, which commented on the satisfactory nature of the arrangements being in place at that point. In general I did not have concerns. There was one specific matter which refers to the performance of a company advising TIE, I will come on to that later. I did and do have concerns about what may or may not have happened in relation to

that advice. That was not a TIE member of staff, nor is it a concern relating to the company itself. TIE seemed to me to have been a sensible thing to create in order to carry out the functions which were being asked of it. The fact that it subsequently changed its relationship with TEL again was a sensible move in line with the circumstances at that time, specifically the fact that many of the other projects which TIE had been asked to deliver were either completed, like Fastlink, or were not being progressed, like the Edinburgh Airport rail link.

31. I was appointed non-executive director of TIE in September 2006 at the same time as three other non-executive directors, all of whom were recruited under the same open recruitment process and appointed by CEC. I undertook that role in a personal capacity with the knowledge and agreement of the Scottish Executive, who was my employer, but specifically not as a representative of the Scottish Executive. Indeed, I had no further conversations about the Edinburgh Tram Project with colleagues inside the Scottish Executive or with TS, its transport agency, from the point at which I was appointed as a non-executive director of TIE. I joined TIE as a non-executive director of my own choosing.
32. During the periods in which I served as a non-executive director of TIE and of TEL I remained a civil servant in the Scottish Executive and Scottish Government in a number of roles, none of which had any connection with the Edinburgh Tram Project. Initially I was head of public health and substance misuse between October 2005 and April 2008. I was head of health delivery between April 2008 and April 2009. I was the director with responsibility for co-ordinating the pandemic flu response between April 2009 and October 2009. I was the director for safer communities between October 2009 and December 2012. I had no relationship with TS while I was a non-executive director and did not report to TS about the tram project.
33. I am asked about the extent of my qualifications, skills and experience that made me suitable for a role as a non-executive director on the TIE board. That was really a judgement for CEC who appointed me to the role to make. Some of the things I offered were four years of experience as head of Scottish

Executive divisions with responsibility for policy on public transport, primarily in relation to railways. That included the commercial procurement of the ScotRail franchise and it included engaging with infrastructure project development and funding. I also brought wider government experience gained since 1990, including of public finance and project financing and project management.

34. I sat on the TIE board from 25 October 2004 to 22 August 2005 as a representative of the Scottish Executive. During that period representation by the Scottish Executive at TIE board meetings varied between three individuals, one of whom reported to me and one of whom I reported to. The reason for my beginning to sit on the TIE board from October 2004 is that responsibility for the Scottish Executive's engagement with the Tram Project transferred from another division to mine at that time. So my existing role was expanded with the inclusion of responsibility for our engagement with the Edinburgh Tram Project. At that point, TS was not yet in existence. This was the period during which TS was being established, and indeed, one of my functions was to help establish, at least in respect of railways related functions, the new organisation that was TS. From the point at which TS did exist, they then took on the responsibility on behalf of the Scottish Executive for engaging with the Edinburgh Tram Project. During the year in which I had some involvement with the Tram Project in my Scottish Executive capacity, my impression was that the TIE board meetings did fulfil their purpose. During that year from 2004/2005 and in my subsequent role with the TIE board as a non-executive director, I would say that the TIE board meetings were professionally run and there was a good quality of discussion. I do not recall having concerns about the information that was being provided to the TIE board in the period 2004/2005. I did have a concern about one specific matter relating to legal advice during my subsequent period on the TIE board which I referred to earlier and which I set out in more detail at paragraph 44 on page 71 below.
35. In my email dated 28 September 2007, (document reference **CEC01667446**), which was a response to a Tram Project governance paper, (document



reference **CEC01667392**), I stated that the TIE board should be primarily concerned with ensuring the successful delivery of the Tram Project. I wanted to see a clearer articulation of the TIE board's role in governance. I felt at the time that the language of the drafting I was looking at in the Tram Project governance paper did not fully reflect the importance of delivering the Tram Project on time and within budget as opposed to commenting on wider concepts of effective corporate governance. Ensuring effective delivery was something that I felt should be more prominent in the language used in this document. I do not know what action was taken in response to my concerns.

36. In an email dated 1 October 2007, Graeme Bissett responded to my comments, (document reference **CEC01682986**). Mr Bissett forwarded that email to Colin McLauchlan and Steven Bell saying *"Predictably, [the non-executive directors] are seeking to understand what exactly is the role of the TIE board."* This comment refers to the proposed governance changes. I understood the role of the TIE board at that time to be to execute its responsibilities in line with its memorandum and articles of association and the tram's operating agreement. It was fundamentally a corporate governance role. I believed that the TIE board was effective in its role and provided effective oversight of TIE until the first few months of 2011 – a matter which I have commented on separately in this statement.
37. I am aware that the minutes of the TIE board meeting on 22 August 2005, (document reference **TRS00008535**), record at section 11 *"It is proposed that since the TPB... will assume much of what the TIE board has been addressing, the TIE board meetings be held bi-monthly."* A change in the frequency of TIE Board meetings is not the same thing as a change in remit of the TIE Board. I do not know whether or not the remit changed and I do not know whether the TIE Board moved to bi-monthly meetings. I left my role as Head of Transport Division 3 two months after this document, at which point I ceased my involvement with the project from within the Scottish Executive. So I am really not able to comment beyond October 2005. Certainly, at the point at which I joined the TIE Board subsequently meetings were not bi-monthly and the Board met monthly, and in the later stages meetings were

held back to back with the TEL board. I cannot comment on what happened between October 2005 and the autumn of 2006. From the start of 2007, meetings were held monthly, not bi-monthly. From my records, I believe that I attended 45 TIE Board meetings during my time on the Board and was absent on 8 occasions. So there were at least 53 TIE Board meetings over an approximately four and a half year period, which leads me to believe that the Board did meet on the whole monthly, not bi-monthly.

38. There is an email from Willie Gallagher to TIE board members dated 8 January 2008, (document reference **CEC01514658**), saying it makes sense to merge the TPB and the TIE board for the purpose of reporting on the Tram Project. The remainder of the TIE board would follow after the TPB. I can confirm that the TIE board and the TPB continued to be distinct entities. They were not merged into the same entity. I believe that this reference relates to holding the two meetings on the same day, and indeed back to back, and inviting the TIE board members to attend the TPB so that they had the most up-to-date information and to avoid duplicating discussions. That is quite different from suggesting that the two entities were merged. They were not merged. It is an important point to me because I was a non-executive director of the company called TIE and then TEL. I was not a non-executive director of the TPB because that was not a company.
  
39. I am aware that the minutes of the TIE board meeting on 12 March 2008, (document reference **CEC01271457**), record that "*As there is now a joint TPB and TIE board preceding the main TIE board, the main focus of the TIE board will be health and safety.*" I do not believe that the remit of the TIE board was changed. The reference to the joint TPB and TIE Board meeting was to show how discussion was directed on various matters in each of the meetings. In addition, the TIE board on 12 March, and indeed subsequently, discussed a far wider range of matters than just health and safety. For example, on that 12 March date, at the TIE board there was a very full discussion about finalisation of the Infraco contract.

40. I note that the minutes of the TIE board meeting on 23 September 2009, (document reference **CEC00707843**), record that "*The TPB will be the main focus for discussion with the TIE board meeting on a lesser frequency.*" I do not believe it is the case that the TIE board met on a lesser frequency. For example, the TIE board met one month later in October and again in November and December. So I do not think it is true that the TIE board met on any lesser frequency. It is true that the TPB focused in more detail on operational matters and about progress on construction. The point of this change was to avoid duplicating that operational management discussion at both a TPB and again at a TIE board meeting, both for efficiency reasons and to make sure that there was clarity about what was being said and what was being agreed. Matters which still required to be taken at the TIE board were taken at the TIE board. In addition, even at this point TIE continued to have some engagement with other projects beyond the Tram Project. I listed some of those projects in paragraph 10 above. I do not have to hand information about the dates on which TIE's formal engagement ended with each of them, however for example the papers for the 16 December 2009 TIE Board meeting include a paper on TIE's Portfolio Projects, and that includes reference to TIE's continuing role as Authorised Undertaker in relation to the Edinburgh Airport Rail Link ("EARL"), which brought with it ongoing duties in respect of land and planning matters even after the suspension of the EARL project. So there were other reasons for the continuation of the TIE board.
41. The minutes of the TIE board meeting on 26 March 2007 record that "*The board asked for clarification on the composition and competency of the sub-committees for Infraco and Tramco.*" These are included in the papers for the April meeting (document reference **CEC01579851**). I believe this was directors carrying out their function in satisfying themselves that appropriate quality assurance and scrutiny was in place and that is recorded in the minutes. The purpose of these sub-committees was to carry out detailed scrutiny and to challenge the information presented when required and they fulfilled that purpose.

## Tram Project Board

42. In general, the Tram Project Board (TPB) was the place where detailed decisions were discussed and taken about a wide range of operational management issues to do with the Trams Project and the contracts. It was not, however, the TPB's responsibility to set the overall strategy for the Trams Project. That remained with the TIE board and then the TEL board. Powers were formally delegated to the TPB by TEL. I am not able to provide the dates. I believe the individual who was most involved within TIE in matters of corporate governance was Graeme Bissett, who had significant previous experience in this area. He would have the detailed knowledge of this and other governance arrangements. However, CEC was also heavily involved and was ultimately in charge of the corporate governance arrangements for managing the Tram Project, including the appointment of myself and the other non-executive directors.
43. The TPB fulfilled its duties and responsibilities by meeting very regularly and discussing in an organised way the range of issues that needed to be dealt with. The TPB formally reported to TEL. The relationship where the TPB reported to TEL was sharpened at the point at which TEL took on ownership of TIE. In either December 2009 or in early 2010, the TPB was formally constituted as a sub-committee of TEL. It was not a main board of a company. I do not recall any votes being taken at the TPB. It was attended by TIE employees, by CEC officials, by TEL staff, by councillors and at times by the non-executive directors of TIE. I did not have any concerns at any time in relation to the TPB or in relation to individual members of the TPB. In my experience, the TPB meetings were professionally run and managed and they fulfilled their purpose. I had no concerns about the information that was being provided to the TPB, and felt that information was always fully and accurately reported. In my impression, the TPB was well-functioning and did fulfil its purpose.

## TEL

44. TEL's creation predates my involvement as a non-executive director and my involvement via my roles in the Scottish Executive. TEL was created to ensure the integration of bus, tram and potentially other public transport schemes in Edinburgh to provide a single integrated public transport system. TEL was not to my knowledge created to address any concerns by Lothian Buses in relation to the Trams Project, although Lothian Buses were an important piece of the jigsaw. My direct involvement with TEL only began in 2010, when TEL took on the ownership of TIE. I had not been a non-executive director of TEL before that point. From that point, the role, remit, duties and responsibilities of TEL were set out in the Memorandum of Understanding agreed in late 2009, (document reference **CEC00690440**), between CEC, TIE and TEL. Powers formally delegated to TEL were set out in that memorandum of understanding. This Memorandum of Understanding was put to CEC policy and strategy committee on 29 September 2009 as a draft memorandum of understanding between CEC, TIE and TEL. In particular, section 2 sets out TEL's obligations under this new arrangement. Paragraphs 2.1 through 3.10.
45. It was important for the directors of TIE and TEL to be clear what their roles and remit was, and as I said before, these were not arbitrary things. They were set down very clearly throughout the process in the various operating agreements between CEC and the companies and in the Memorandum of Understanding, (document reference **CEC00690440**). The roles and remit that were set down explained the limits of the powers that the companies had, for example, in committing expenditure. Matters such as committing expenditure in excess of a given threshold would be referred to the CEC to make final decisions on.
46. TEL was owned by CEC and reported to CEC regularly. CEC was represented on the board of TEL, and TEL reported to CEC within the formal reporting arrangements that took place during TEL board meetings. I stated previously how these matters changed over time, whereby TEL took over ownership of TIE. That was the main change. I was a Director of TEL between

18 December 2009, (document reference **CEC00645841**) and 12 May 2011. I had no concerns at any time in relation to TEL as an organisation or in relation to individual members of the Board or in relation to individual employees. My impression of the TEL Board meetings was that they were conducted professionally and they fulfilled their purpose. I had no concerns about the information that was being provided to the TEL Board and whether information was always fully and accurately reported.

### **TIE Board Audit Committee**

47. I became the Chair of the TIE Board Audit Committee in early 2007. There had been an Audit Committee before that point and I am not able to comment on the Committee before the point of my involvement. My understanding of why it existed at the point at which I became the Chair was to be entirely in line with the principles of good corporate governance. The core roles of Audit Committees include being the guardians of the integrity of a company's financial statements. The Audit Committee had to approve financial statements for publication. Other core roles included checking the company's internal financial controls and ensuring that necessary risk management systems are in place, including the tasking and monitoring of internal audit functions. The Audit Committee had specific duties in respect of external audit, for example, recommending to the TIE board the appointment of the external auditors and approving their fees. In relation to fraud prevention, for example, the Audit Committee had to ensure that there were opportunities for employees of TIE to act as whistle-blowers.
48. I can confirm that the TIE Board Audit Committee's remit is stated in (document reference **CEC00300925**) dated January 2009. Whereas the remit stated that the Audit Committee should meet at least twice a year, in practice it met more often. On average it met around four times per year and specifically between January 2007 and May 2011, during that 52-month period, it met 16 times. I chaired all of those meetings and to my recollection I never missed a meeting of the Audit Committee. The duties and responsibilities of the Audit Committee related to all of TIE's expenditure,

including sums spent by TIE on the various Tram Project contracts. So, for example, it included both the expenditure on procuring the trams and expenditure on staff costs, wages and overheads.

49. I do not know when the Audit Committee was first created as this preceded my involvement. However, during my tenure as Chair of the Audit Committee the remit was available at every meeting and I reported back to the full TIE board after the Audit Committee meetings. The remit was agreed by the TIE Board.
50. The Audit Committee performed its duties and responsibilities through holding regular meetings, by commissioning and overseeing the internal and external audit processes, by monitoring and approving the financial statements for TIE, and as I mentioned before, I would usually update the full TIE board after each Audit Committee meeting. The Chair of the TIE Board, the Chief Executive of the company, the Financial Director and a number of other directors attended Audit Committee meetings. So amongst those key individuals there was good visibility of what the Audit Committee was discussing.
51. Initially the Audit Committee formally reported to the TIE Board and then subsequently, after the governance changes, the TEL Board. I set out the relevant dates of these corporate governance changes in paragraph 3 above, and I comment on why they took place on several occasions in this statement including in Part 1 at paragraphs 16, 19 and 54. It subsequently became the TEL Audit Committee. It undertook a significant programme of internal audit. It oversaw the re-procurement of internal audit services to TIE, resulting in that role transferring from Scott-Moncrieff to Deloitte. Deloitte started in the role in November 2008. To give some examples of the sort of work the TIE Audit Committee undertook, in 2007 we commissioned internal audit reviews on internal financial controls, corporate governance, procurement and tendering procedures, contract monitoring and management, health and safety, project management arrangements, ICT infrastructure, EARL project suspension, security arrangements and MUDFA. In 2008/09 there were internal audit

reviews on corporate governance, stakeholder management, Infracore and MUDFA, financial control, project and programme reporting and following up on previous reviews.

52. The Audit Committee would recommend the approval of financial statements to the full TIE board and the financial statements would be published. In the case of internal audit, where internal audit recommendations were made, the executive team in TIE were asked to respond to those recommendations and to follow up on them. One of the functions that I oversaw on the Audit Committee was to ensure the action and completion of recommendations by the executive team within TIE in response to internal audit recommendations. I considered that the Audit Committee did fulfil its purpose. I did not have concerns in relation to the Audit Committee or in relation to individual members of the Audit Committee. I am not aware of any concerns having been raised about the Audit Committee.
53. The remit of the Audit Committee is set out on page 11 in TIE's business plan, financial year 2008/09, dated 15 January 2008 (document reference **CEC01221938**). In reference to my previous statement, the Audit Committee met on average four times a year. My recollection is that it met on 26 February 2007, 10 July 2007, 11 December 2007, 12 March 2008, 3 July 2008, 9 October 2008, 22 January 2009, 11 March 2009, 6 May 2009, 3 June 2009, 8 July 2009, 18 November 2009, 5 May 2010, 30 June 2010, 15 December 2010 and 16 March 2011. Those were the dates within my tenure as Chair of the Audit Committee.
54. A letter dated 9 February 2010 from Deloitte to Stewart McGarrity acknowledges the disbandment of the TIE Audit Committee and the creation of a TEL Audit Committee (document reference **CEC00111629**). With regard to the length of time the Audit Committee operated, I refer to my previous statement. The functions of the old TIE Board Audit Committee transferred to the TEL Board Audit Committee. I can confirm this change, and the change was in line with the wider changes to corporate governance arrangements agreed by CEC.



55. I am aware of a PowerPoint presentation dated 9 October 2008 (document reference **CEC00111612**), about Deloitte's proposed three-year strategic internal plan 2008/09 to 2010/11. It states that "*Six internal audits will be carried out in 2008/09. These audits will cover a number of areas such as governance, Infraco, financial control etc.*" This was normal and expected good practice for any company. Internal audit is an essential and a core part of good corporate governance and the appropriate committee to oversee that process is the Audit Committee. Deloitte undertook a wide range of internal audit reviews for TIE over the period that I have mentioned. I have given some examples of that in my previous example. The purpose of Deloitte's work was to carry out the internal audit reviews commissioned by the Audit Committee on behalf of the board. Deloitte carried out its work by undertaking reviews of varying lengths. Some of the reviews could take up to 30 days of people's time, while others were less resource-intensive than that. Deloitte would produce reports which the Audit Committee would consider. I am not aware of the internal audit work undertaken by Deloitte having been used externally by TIE, as part of a justification or explanation given to an external organisation. This was about internal assurance for the company.
56. Deloitte produced numerous internal reviews, all of which were reported to the Audit Committee. The Committee decided on what action to take in relation to the reviews. To my knowledge, all recommendations produced by the Audit Committee by Deloitte were acted upon, and indeed there was a process to ensure follow-up of internal audit recommendations. Deloitte were the internal auditors from November 2008, before that date the internal auditors were Scott-Moncrieff and they conducted a similar function on behalf of the Audit Committee and for the company. The reviews carried out by Deloitte informed decisions taken by the TIE and TEL Boards. The reviews were available to CEC through its representation on the Audit Committee by a Councillor, in line with the fact that 4 councillors were members of the TIE Board, and the reviews may well have been shared by TIE executive staff with CEC officials – that would have been entirely appropriate. So I expect that the reviews also informed wider CEC decisions as well.

## **Withdrawal of TS from Governance Arrangements**

57. I recall that after the Scottish Parliament voted in favour of the Trams Project in June 2007, it was decided that TS should withdraw its participation in the governance of the project. Until that point TS was represented at TIE board meetings by a senior official and also received regular written and oral updates from TIE officials. My recollection is that there was frequent contact until this point between TIE and TS staff. I was not involved in the communication between TIE and TS, other than through my participation in Board meetings at which TS were represented. Much of that communication happened at executive level. I was not involved in the decision of TS to withdraw from participation in the TIE board from June 2007. In my capacity as a TIE director, before the 2007 elections, I do not know what TS's intended involvement was to be in future project governance, that was a matter for TS. TS received regular updates from TIE, both formal written updates and oral discussions with executive staff, including a four-weekly regular review of the Trams Project.
58. The reasons for TS withdrawing from governance were a matter for TS and are for TS to explain. The TIE board's opinion of TS's withdrawal was not a matter which the board discussed or took a view on. It was a matter of fact that TS had taken this position. I do not recall the board ever forming an opinion on it. I do not know the TPB's opinion of TS's withdrawal, although the same facts remain, that this was a decision taken by TS. I don't think it was a matter which was opined on by the TPB.
59. I have been asked what were the reasons for TS withdrawing from tram governance arrangements. I do not think it is fully accurate to say that TS withdrew from the tram project governance arrangements. They retained a number of significant governance positions, for example, to ensure that the level of expenditure which had been committed to the project was not breached and they continued to have regular discussions and updates from TIE. In my opinion TS remained involved with the governance of the tram project. My view on TS's discontinued representation on the TIE board was

that this was a significant event and that it remained important, nevertheless, that TIE had strong and regular communication with TS, given their role as majority funders of the project. At that point they had committed £500 million.

## **Business Case**

60. The TIE board did not produce the business cases. Those were produced by the executive teams in both TIE and CEC. I do not know what the involvement was of the TPB in the production of the business cases. The business cases were largely written before my appointment as a non-executive director of TIE. The Final Business Case was approved by CEC in December 2007. The TIE Board endorsed the Final Business Case v1, dated 3 October 2007, at its meeting on 15 October 2007 but final approval was a matter for CEC. The Final Business Case v1 was formally submitted to CEC on 18 October and that version was endorsed by the full Council on 25 October 2007. The Final Business Case v2 included updated information from the appointment of preferred bidders and other on-going matters and at that point the intention was to enable financial close in January 2008. I do not know who was involved in producing the business cases specifically beyond officials from TIE, CEC and Lothian Buses and potentially others such as consultants. The estimates for the project were calculated by the executive teams in both TIE and CEC in line with the TS Appraisal Guidance (STAG) methodology. STAG was at that time, and I believe remains still, the standard guidance which is required to be used in appraising all Scottish Executive funded transport projects. It is written by TS, and ensures that best practice is followed in, for example, appraising the costs, benefits and risks of projects.
61. The scope of the project that was delivered changed from that envisaged in the Final Business Case, so it is impossible to make direct comparisons about performance against plan. However, my understanding from media reports since my involvement as a non-executive director ended is that the expectations around trams' patronage have been exceeded relative to the revised scope of the project. But one cannot make a direct comparison between the patronage of the delivered Tram Project and the patronage

envisaged in the Final Business Case, because that Final Business Case envisaged the trams running from the airport all the way to Newhaven.

### Optimism Bias

62. I am aware that in the Communications Progress Reports submitted to the TIE board on the 24 October 2005 (document reference **TRS00008535**) it is noted that there had been coverage of the impact of inflation and optimism bias on the base cost of trams. I was familiar with the concept of optimism bias at that time. Optimism bias has a precise meaning and at the time it was defined in the Scottish Public Finance Manual, which in turn referred to the HM Treasury Green Book. It is a term for financial sums that should be built into the estimated costs of projects, relative to their stage of development and decreasing over time, in recognition of the fact that risks can materialise which end up costing projects more. I had gained experience of examining business cases for other public transport projects, which included optimism bias as part of their cost estimates, from my previous role as the head of a Transport Division in the Scottish Executive. The need to include an allowance for optimism bias increased the capital cost estimate of the Trams Project. Optimism bias was included throughout the cost estimates process for the tram project. I was not aware of pressure to reduce optimism bias so as to reduce the cost of the tram project.
63. I am aware that the December 2006 Draft Final Business Case (document reference **CEC01821403**) at page 137 noted that "*TIE... has determined in consultation with Transport Scotland that no allowances for optimism bias are required in addition to the 12 per cent risk allowance.*" The same statement appeared in the December 2007 Final Business Case (document reference **CEC01395434**) at paragraph 10.14. My understanding of the matter was that optimism bias relates to the same thing as is referred to here as risk allowance. Optimism bias is a concept which relates to experience of risks materialising. The way in which that concept is then operationalised is by inserting a risk allowance into budget estimates. My understanding of that statement is that the 12 per cent risk allowance referred to was in recognition

December 2006  
should be  
November 2006

of the need to have optimism bias built into the estimates. They are essentially one and the same thing. I am not aware of who in TS agreed that no additional allowance should be made for optimism bias. But I do not agree with the premise of the statement put to me that the two things are different; in my view if a risk allowance or contingency was being provided for, my understanding is that it is the same thing as providing for optimism bias.

64. My view in late 2007, early 2008, on the adequacy of the risk allowance and whether the decision not to make any allowance for optimism bias should be revisited, in particular given the problems and delay at that time in relation to design, statutory approvals and consents and total diversion works, was that I had no reason to query the existing levels of risk allowance or optimism bias. The level of optimism bias that should be applied to public transport projects is not arbitrary. Guidance on the levels of optimism bias to be applied to projects as they move beyond initial ideas through the business case process, through procurement and then to delivery, is set out in the Scottish Public Finance Manual and the HM Treasury Green Book. So over time the amount of recommended optimism bias to be applied to project cost estimates should decrease as the scope for risks to crystallise lessens.
65. I am aware that the Scottish Executive said it would commit up to £375 million to the Trams Project at quite an early stage in the life of the Tram Project, before the Draft Final Business Case and Final Business Case were submitted. I am referred to a memo dated 20 December 2006 (document reference **TRS00003385**) from Malcolm Reed to the Minister of Transport, which states that the sum was indexed according to the standard TS indexation model. This memo post-dates my time working in the Scottish Executive Transport Division and pre-dates my membership of the TIE Board so I cannot comment on that issue. During the period when I was working in the Scottish Executive on transport matters, I did not have concerns in relation to the Scottish Executive commitment of up to £375 million being indexed. My understanding and my experience is that each major infrastructure project needs to be considered in relation to its own particular set of circumstances and this includes the tram project.

66. I cannot speak on behalf of the whole TIE board or all of TIE, but my observation is that the early commitment of money from the Scottish Executive did not put any inappropriate pressure on TIE to ensure the project always remained within budget. However, it is important to say that the specific budget envelope that was agreed for the project did put pressure on TIE to ensure the project remained within budget and that was something which was formally addressed in the operating agreement and in the memorandum of understanding between TIE, TEL and CEC. That is an important fact, bearing in mind the project breached the previous budget envelope in the later stages of the tram project. During my period of involvement with TIE and TEL it was never within their gift to commit or spend money for which it did not have approval from CEC.

#### **Design – ‘SDS’ Contract**

67. I did not have any involvement in the procurement of the SDS contract. That predated my time as a non-executive director of TIE. I had some concerns about the SDS contract, in the sense that the TIE board during my period received reports with concerns about the quality of work done under that contract and about the time that it took to do it. I am aware that problems with the SDS contract were reported to the TIE board. I am referring to the following examples: the Executive Chairman's Report for TIE board meeting on 30 October 2006 (document reference **CEC01579849**); the Executive Chairman's Report for the TIE board meeting on 11 December 2006 (document reference **CEC01579852**); the minutes of the TIE board meeting on 26 February 2007 (document reference **USB00000028**); and TIE board meeting on 24 September 2007 (document reference **TIE00147433**). Progress with design matters and SDS, as with all other major elements of the project, was discussed and reported at every TIE Board and Trams Project Board meeting I attended. At each stage, next steps and actions were agreed. For example, on 10 July 2007 and 27 August 2007, the TIE board discussed SDS performance and handling of the financial claims that SDS were making. Ultimately, responsibility for the SDS contract was novated to

the infrastructure company in order that risks arising from SDS could be better managed.

68. I am referred to one of the papers for the TIE board meeting on 13 April 2007 (document reference **CEC01579851**), which is a Tram Project Update of April 2007. Paragraph 1.1.1 states "*That preliminary design has now been accepted in detail and is approximately 50 per cent complete on average.*" The minutes of the TIE board meeting on 24 September 2007 (document reference **TIE00147433**) at section 6, Tram Project, state that "*The detailed design work is now circa 58 per cent complete*". I do not recall the details of this, but I do recall the key issue being reported to the TIE Board at that time was the under-performance of the contractor, particularly in terms of quality of work done, which required the same work to be done more than once. My recollection is that the original intention was that the detailed design be largely complete by contract close, if not fully complete.
69. My understanding of the risks that arose if design was not complete, and all approvals and consents were not obtained, before Infraco contract close, to the extent that those risks remained, was that it was important that the risks be managed by those best-placed to do so, and that was by concluding the infrastructure contract. It was negotiated that the infrastructure company would take on responsibility for normal design development because they would be closer to the actual design work and therefore better placed to manage design risk, than if TIE retained the risk with them. Examples of the risks that could arise was that slower than planned production of design drawings would require the infrastructure contractor to price in risk commensurate with corresponding uncertainty about what structures should be built, and that poor quality design work would have to be re-done and therefore introduce delays in agreeing final designs. It therefore made sense that the infrastructure contractor should manage that design contract directly, and this was agreed by the parties and reflected in the final contract signed.
70. Novation of that contract into the Infraco contract was not the only response that TIE took to SDS quality problems and delays. The TIE board were told

that there were multiple and frequent discussions every week between TIE staff and SDS staff about quality and delay issues, but those were discussions with which I was not personally involved. Discussions with SDS were led by TIE's executive team and so I cannot give a detailed account of what was discussed. A key individual involved in discussions with SDS would be Steven Bell, whose job title changed over the course of the project, but he could have been Tram Project Director at that point. My memory is that he had a senior role in dealing with the SDS discussions and performance issues, as he had for other aspects like utilities diversions and the infrastructure contract delivery.

71. The impact that delayed and incomplete design, approvals and consents had on utilities and infrastructure contracts and works was that it introduced some delays and risks into the utilities diversions and infrastructure contracts works, examples of which I mentioned in paragraph 69 above. However, it is not my understanding that this was the key issue which led to problems particularly with infrastructure contracts subsequently. In other words, design delays do not really explain what happened with the infrastructure contract.

#### **Utilities Diversion Works – 'MUDFA' Contract**

72. I did not have any involvement in the procurement of the MUDFA contract; it predated my involvement as a non-executive director. I had no concerns about the procurement of MUDFA. I did have concerns about the execution and delivery of the MUDFA contract. The extent of work that would have to be done under the MUDFA contract, and the additional cost and delays that came with that, were a matter of very great importance to the TIE board throughout this process, until the MUDFA works were completed. The length of meterage of utilities to be diverted ended up being twice as much as had been originally forecast. So that matter was of great concern to the TIE board. MUDFA was discussed at every TIE board meeting and the board sought information about the actions being taken in response and sought to satisfy itself as to whether those actions were sufficient.



73. In terms of the procurement strategy, the original intention was that the utility diversion works would be completed before the infrastructure works commenced. The risk that arose if the utility diversion works were not complete before the infrastructure works commenced would depend on the nature and location of those outstanding utility diversion works. So, for example, utility diversion works were predominantly, if not wholly, in the on-street sections of the Tram Project, in other words, where utilities ran directly underneath the tracks that the trams would run on. However, there was not the same extent of utility diversions required in the off-street sections of the infrastructure and track. Therefore, incomplete utility diversions on the on-street sections would not necessarily prevent the infrastructure contractor undertaking the work on the off-street sections.
74. In order to address these risks the handling of the MUDFA contract and performance under the MUDFA contract was discussed at every TIE Board meeting. The TIE Board sought to satisfy itself that the actions being proposed by the executive team were the right actions to take in order to get the problems resolved as quickly as possible. Some of the problems that arose with the MUDFA contract were not simply a matter of contractor performance but were the result of the state and complexity of the utilities that were discovered under the roads, which were not as had been predicted by the existing maps and plans at that time. I recall human remains being found in one site which required special measures to be taken. So the complexity of the works turned out to be in excess of what everybody had anticipated, even allowing for contingencies, and even having maps which showed the location and nature of the existing utilities.
75. Incomplete utility diversion works had some effect on the infrastructure works but not as much as was sometimes stated. On 7 May 2008, at the point of Infracore contract close, the TPB papers noted that a total of 77 per cent of the planned diversions had been achieved. By 26 August 2009, 96.6 per cent of the MUDFA works had been completed. The scope of the MUDFA works was revised between those two dates, so those two figures, 77 per cent and 96.6 per cent, are not directly comparable. Nevertheless, a significant proportion of

the MUDFA works were completed, both at contract signature and then again over the first years of the contract, and therefore the state of completion of MUDFA works was not actually a good reason as to why the infrastructure contractor could not begin works on sections of the tram project.

### **Infrastructure Contract – ‘Infraco’**

76. My involvement in the procurement of the Infraco contract was from the appointment of preferred bidder onwards until my resignation on 12 May 2011. The TIE board had previously overseen the letting of the Infraco contract and the earlier stages of the procurement process. At the time I had no concerns about the Infraco contract or the procurement of Infraco. I was pleased to see a phased approach being taken to the procurement of different elements of the Tram Project, which learned from the experience of other UK light rail projects which had not sought to separate out the contracts. This, as I mentioned earlier, was something commented on by Audit Scotland in their 2007 report on the Tram Project (document reference **ADS00047**).
77. I understand the term ‘fixed-price contract’ to mean a contract which delivers what has been specified within a fixed financial price, unless the specification of the contract changes. When I and others asked about the nature of the Infraco contract at the TIE board, it was described as being a 95 per cent fixed-price contract. There were other contractual options that could have been taken, for example, a cost-plus contract model, whereby you essentially pay as you go. However, a largely fixed-price contract was thought to be preferable because resources available for the Tram Project were fixed and it was important that the Tram Project procured would be affordable and in line with the public resources available to pay for it. Other risks were also included in that fixed-price contract which I mentioned before, for example, the future design development. At the time of the Infraco contract close, in response to questions from me and other board members, and indeed reflected in the paperwork provided, the Infraco contract was described as being a 95 per cent fixed-price contract.

78. The papers presented to the 12 March 2008 TPB meeting (document reference **CEC01362332**), noted that *"95 per cent of the combined Infraco/Tramco price is firm - the remainder being provisional sums which have been reviewed by TIE and BBS for adequacy. Risk allowance of £33.4 million is 10.8 per cent of £308.7 million base costs to go beyond financial close."* The minutes of that meeting record that Stewart McGarrity *"... pointed out that increases in Infraco contract price of circa £10 million meant that the baseline project estimate rises to £508 million from £498 million."* The minutes also record *"WG [Willie Gallagher] explained that in particular to buy out the risk of SDS non-performance was considered good value for money. He also confirmed that the current price reflected the programme and scope for construction that BBS could deliver."*
79. 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.
80. I recall that on the 9 April 2008 at the TPB and TEL board meetings, the Executive Summary paper (document reference **CEC00114831**), notes that sufficient progress was made to issue the notification to award on 19 March 2008. In the papers for that meeting there is a report from DLA, the legal advisors. The report says *"At the council's request DLA have reported their advice on the legal acceptability of the Infraco contract suite separately to the council. The report contains a detailed risk matrix which demonstrates where residual risk falls between the public and private sectors. This risk analysis has been matched with the risk contingency calculations embedded in the final project budget to ensure that we have full alignment of risk and costs."*

81. The Close Report, version 9, dated 9 April 2008 (document reference **CEC01486902**) at paragraph 8.2 states, "*Price certainty achieved*". It goes on to say "*The Infraco price of £234 million comprises: £228.3 million of firm costs; less £13.7 million of value engineering initiatives taken into the price with the agreement of BBS, but with qualifications attached; plus £19.4 million of items which remain provisional at financial close. Crucially the price includes for normal design development, meaning the evolution of design to construction stage and excluding changes of design, principal shape, form and outline specification, as per the employer's requirements.*" The report at that meeting on the Infraco contract suite says "*Price. A contract price has been agreed. A substantial proportion 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 as such provisional sums are included. The agreement contains a relatively conventional contractual change mechanism in relation to the management and evaluation of the variations.*"
82. It goes on to talk about the principle of novation; "*The novation of SDS, provider to Infraco, involves Infraco taking responsibility for managing SDS to produce the remaining design and approvals for the Edinburgh tram network. The principle of novation was to ensure that the integration of design and construction is the responsibility of BBS and gives BBS recourse to the same contractual remedies against SDS as TIE would have had in that situation, including particularly the ability to claim against SDS in relation to defective design carried out by SDS.*"
83. On 7 May 2008 at the TPB meeting, the PowerPoint slides (document reference **CEC01282186**), where BB refers to Bilfinger Berger, and S refers to Siemens, say "*Full set of legal documentation sent to BBS on 22 April 2008 as agreed. Meeting with BB&S on 24 April 2008 (senior representatives) confirmed all commercial matters concluded. Legal diligence proceeds. WG receives call from BB (Walker) on 30 April 2008 am requesting £12 million price increase. Emergency TPB held same day to discuss. Meeting of senior principals held 5 May 2008 being driven by BBS. S claimed to have sought to influence but no sign of impact. BB support for the price increase is sketchy,*

*confused and wholly unconvincing. All signs are that it is last minute, unprofessional brinkmanship. BB claimed their costs are £17 million wrong, have reworded internally to arrive at £12 million."* The slide goes on to say *"BBS response disjointed and confused, coupled with further evidence of horse-trading; injected new demand for sequential design process, rejected long ago. Ultimatum sent close of play 6 May 2008. Response received this morning, requesting pricing adjustment of £9 million and alignment of design process."* Options are set out in the slides for that meeting, including an option of not proceeding to award the contract to that contractor in the light of this behaviour and previous incidents. The slides note the potential for delays of 3, 6 or 12 months under the options set out. The recommendation on balance is to continue to award the contract to that provider.

84. The phrases "*fixed price*" and "*firm price*" were used in meetings prior to the 7 May 2008 meeting. For example, at the TIE board meeting on 23 January 2008, the Executive Summary paper refers to "*The discussion with BBS resulted in the signing of the 'Agreement for contract price for phase 1(a) on 21 December, essentially fixing the Infraco contract price based on a number of conditions.'*"
85. Between then and the actual contract close in May 2008 yet further risk was transferred contractually from the public sector to the private sector contractor, specifically around normal design development. The key point I am making is that not only was this described as being a 95 per cent fixed-price contract, but in the weeks leading up to contract signature yet further risk was transferred across in return for an increased payment being made. It is an important point because of the issue around price certainty and of what transpired around about the awarding of that contract, particularly the infrastructure contract, where the eventual cost of the infrastructure works under the contract increased.
86. With regards to disputes with the Bilfinger Siemens Consortium that affected the Infraco contract after it had been signed and what involvement the TIE board had, in terms of the actual conversations with the Bilfinger Siemens

Consortium, neither I nor, to my knowledge, the other non-executive directors were involved directly at any of these meetings. The chair of TIE was, and I believe that the senior executives were directly involved. The involvement of the TIE board and involvement of the non-executive directors was in discussing the response to what was occurring and in setting the strategy for delivering the trams under the contract. The TIE board was told about the disputes with Infraco, and these disputes comprised the bulk of TIE board discussions from the month of contract signature until the remainder of my involvement with the process.

87. Audit Scotland's 2011 report (document reference **ADS00046**), correctly refers to a major dispute arising in February 2009. However, that was not the first dispute that arose. In fact, it was clear as early as the 3 July 2008 meeting that mobilisation by Bilfinger Berger and Siemens consortium had not begun as planned from the very start of the contract. The contract was signed in May 2008. The TIE board met a little over one month later. At that meeting, on 3 July, the TIE board minutes (document reference **CEC01282131**) note "*It was noted that Infraco mobilisation is still too slow with delays on the package contractors. A meeting will be arranged with Infraco next week to address this issue*".
88. Again on 13 August 2008 (document reference **CEC01150362**), the TIE board papers referred to Infraco delays and, "*Infraco mobilisation impacting programme*" became the top-ranked risk to the whole Trams Project, noted in the slides. It remained as the top-ranked risk from then on, for the remainder of the project. In the papers for 11 September 2008 meeting, the Tram Project Report, Executive Summary for Period 05 2008/09 (document reference **CEC01164912**), states: "*The slow mobilisation of Infraco is continuing to impact planned progress*". Again, the top risk in the risk register is, "*Infraco mobilisation impacting programme*". The 19 November 2008 papers for the joint TPB and TIE meeting (document reference **CEC01053731**) say "*The project continues to experience problems with slow mobilisation and, in particular, appointment of direct BSC resource and the final appointment of the main package contractors*".

89. By January 2009 the planned total of Infraco works that should have been completed was 25.7 per cent of the total amount of works, but the actual progress was 1 per cent, noted in the Progress Report for period 19 (document reference **CEC00988026**). Six months later, on 26 July 2009, even although 96.6 per cent of the MUDFA works were complete; the actual cumulative Infraco progress against plan was 6.3 per cent, as opposed to a planned cumulative total of 57.7 per cent. In other words, disputes arose from the very start of the contract because the consortium did not mobilise from day one to undertake the works to which they had committed in the contract.

period 19 should  
be period 10

90. On 11 February 2009, Andrew Fitchie of DLA Piper spoke to the TIE board. I made some manuscript notes of what he said when he spoke which I have provided to the inquiry (document reference **WED00000138**). In his remarks he highlighted three key themes. The first of the three was, "*Contractor behaviour since 14 May of contract signature*". On that point Mr Fitchie said there "*is a pattern of behaviour from contractor intended to block progress.*" My notes indicate he went on to say that BSC demonstrated no ability to produce estimates and update the master programme. The minutes of that meeting on 11 February 2009 (document reference **CEC00438304**) say "*The TIE board was updated on the issues arising from our meeting with senior representative of Infraco. The board expressed its extreme concern over the performance of the consortium and delivery against the contract, noting that the current behaviour of Infraco and the number of breaches of contract continue to frustrate TIE's ability to manage the contract and to act responsibly as client.*" The reason that I raise this is because one could gain the impression, from the Audit Scotland report at least, that it was some ten months until the first dispute arose with Bilfinger Berger in particular, and that was simply not the case. What was reported to the TIE board was that from the very first month after contract signature mobilisation by Bilfinger Berger did not happen on anything like the scale that it had contracted to do.

91. In response to any argument that somehow the nature of the contract prevented the contractor from starting work, I note the fact that the contractor had spent seven months as the preferred bidder, negotiating and agreeing

every word of the contract that they signed, including amending the contract with TIE's agreement, and undertaking due diligence. So my impression was that the contractor intimately knew the contract and what they were agreeing to. I do not believe that if even some of the contract provisions which were subsequently the subject of the dispute resolution process had been different this would have significantly affected progress on the project. Because the lack of mobilisation by Bilfinger Berger – the infrastructure contractor - occurred immediately after contract signature, before there had been any time at all for these provisions to be tested in practice.

92. This is a key point in the story of this project. There was nothing actually preventing the Infraco contractor from mobilising on time, particularly in areas where the utilities diversion works were not an issue, because there were sections of this project that were not dependent on utilities diversion works being undertaken. And certainly nothing in the contract that they had just signed. I also note that the performance of other contractors who were part of the same consortium was much better. For example, the performance of the trams manufacturer was strong, and I don't believe that problems arose with the third party in the consortium, Siemens, on anything like the scale they arose with Bilfinger Berger.
93. A key issue that the board was facing was around the underlying motivation of the Infraco contractor. The information that I was receiving was that the underlying motivational issue for the Infraco contractor was primarily financial. In particular, over the course of 2008, it became apparent from comments made to TIE executive staff, and subsequently reported to the non-executives, that the Infraco contractor wanted and were asking for additional payments significantly in excess of what they had contracted for. Sums of between £50 million and £100 million were mentioned at this point. That led to a discussion, for example, on 19 November 2008 at the joint TIE Board and TPB meeting where the minutes (document reference **CEC00988024**), record me as saying *"KH added that TIE must have a strategic response to small issues that will be incremental in their effect. He stressed that, as the scheme is being constructed with public money, TIE must receive £1 of value for every £1*



*spent. Although it may be acceptable in private companies, under public finance rules TIE cannot pay to 'grease the wheels'. He added that there cannot be any doubt in the contractor's mind on the scope of the project's ability to pay."* By using the phrase 'grease the wheels' I meant by paying extra money to BSC. In retrospect, there were signs of this motivation and this behaviour manifesting itself before contract signature. I referred previously to the discussion held on 7 May 2008 and to the reports of the behaviour of the preferred bidder at that stage, in the days leading up to contract signature and even before then, asking for 11<sup>th</sup> hour increases in funding, essentially because BSC were saying they had got their sums wrong.

94. The dispute resolution procedure (the "DRP") was something separate. What I have been referring to are disputes that arose before the DRP was started. This is an important distinction. At times in the discussion about this project the word "*dispute*" is used loosely. The point I am making is that disputes arose from day one of contract signature, in fact, even before day one, because of the behaviour of the contractor, primarily around not beginning work, not mobilising, not starting work on site. The TIE board took a decision to refer matters to the contractual dispute resolution procedure. The TIE board was updated about the outcome of every DRP proceeding, and more than that, the TIE board were sighted on which issues were being put into the DRP process in the first place. In summary, the TIE board were very disappointed with the performance of the Infracore contractor, and in particular its failure to mobilise from day one after contract signature. I shared those views.
95. It was during 2010 that the TIE Board first became aware that the scope of phase 1A of the project was unlikely to be delivered on time and within the given £545 million budget. When that happened, the chair of TIE, David Mackay, wrote to CEC on 8 June 2010 (document reference **CEC00223543**) saying "*This letter is to formally advise you that the TEL board now consider that it is reasonably expected that the full scope of line 1A cannot be delivered within a budget of £545 million and by October 2012.*"

96. In broad terms, I think one of the key questions for the Inquiry is what the TIE board did about the disputes with Infraco. A key role for the TIE board was to agree a strategy in line with its responsibilities as a company board. In response to the disputes with Infraco, over time the TIE board agreed and endorsed two different approaches intended to incentivise the contractor to begin the work and to get the project back on track in terms of delivering the specification on time and on budget. The first strategic approach in response to the disputes was a partnership approach intended to build trust, relationships, and confidence between the Infraco contractor and the project. In summary, that approach involved TIE going the extra mile to reach a supplemental agreement, in addition to the main contract, to get the Princes Street works done. Those works commenced in March 2009. The slides for the 15 April 2009 joint TIE and TPB board meeting (document reference **CEC00971385**) note that "*Work has commenced on Princes Street under a supplemental agreement which provides an equitable and constructive way forward to facilitate the consortium working flexibly in encountering impediments or obstructions, and is consistent with the obligations under the Infraco contract.*"
97. In other words, the initial approach that TIE took to respond to disputes was to seek to accommodate the concerns being raised by the contractor, and to strengthen that relationship to the extent of agreeing a supplement agreement in respect of the Princes Street works, in a way which it was hoped would reassure them about some of the risks as they perceived them about the project. A second example of this approach would be in the establishment of a project management panel, again discussed on 15 April 2009 "*As the forum for more constructive engagement between TIE and BSC*", which is the key element of the commercial strategy. It continues "*Workstreams approach: first and foremost, work constructively with BSC.*"
98. It was only after at least 18 months of continuing with the strategy of seeking to build a partnership, seeking to build trust and good faith between the contractor and the project, that the TIE board agreed that a different approach was required. That second approach was to robustly enforce the contract,

which the contractor had knowingly entered into, having been preferred bidder for seven months and therefore having become familiar with the contract terms before contract signature. It was under that more robust approach that, for example, the use of the dispute resolution procedure was increased and indeed other options were also explored including those within what was called Project Pitchfork which I refer to in Part 2, at paragraphs 129 and 130 below.

99. I make this point because some of the media reporting about the project problems was that they stemmed from the relationship between TIE and the company and the Infraco contractor, and because TIE had been too robust in enforcing the contract. The approach of more robustly enforcing contractual compliance was only tried after at least 18 months of a different approach, intended to build confidence and trust and work in partnership with the contractor and to give the contractor every opportunity of mobilising and getting the works back on track in line with the contract. Therefore in my view the root cause of the problems was not the nature of the relationship between the parties. I had no concerns about the quality or accuracy of the information about the disputes that was being provided to the TIE board. A key issue for the Inquiry to focus on would be the motivation and the behaviour of the Infraco contractor.
100. I am aware that the minutes of the TIE board on 11 February 2009, (document reference **CEC00438304**), record that "*The Board expressed its extreme concern over the performance of the consortium and delivery against the contract, noting that the current behaviour of Infraco and the number of breaches of contract continue to frustrate TIE's ability to manage the contract and to act responsibly as a client.*" These comments are in relation to the Princes Street dispute. My recollection is that about one week before works were due to commence on Princes Street early in 2009, the Infraco contractor indicated that it was not content to start, and indeed I believe it made a financial claim at that point. This matter was discussed fully at the TIE board. The TIE board's approval was sought and given before entering into the Princes Street Supplementary Agreement.

101. My views generally at this stage in the project were that the right thing to do was to seek to build confidence in the project on the part of the Infraco contractor. If entering into a supplementary agreement was an effective way to do that, then that was the right approach, on the condition that we understood the risks, both financial and otherwise, in doing so.
102. The minutes of 17 December 2008 joint TIE and TPB meeting (document reference **CEC01053908**) record me as saying "*KH noted that he was pleased at the solution arrived at for the closure of Princes Street*", this is in respect of the initial dispute, "*He asked for an explanation on the process taken to reach this outcome and what had changed since the last board meeting*". The minutes of that meeting go on to record the following "*Both KH and PS [PS refers to Peter Strachan, who is another non-executive director] questioned whether costs associated with the current Princes Street strategy would be covered within the £512 million budget and risk allowance. SB, SMG and DJM all agreed that the additional cost of the measures (having one lane available for a period of time, additional TM, contingency enabling works and breakdown vehicle) as well as the diversions at the Mound not being complete were an extra cost as BSC had priced them having full access to Princes Street and the additional contingency had not specifically been allowed for in the budget or risk allowance.*" Later "*Following KH's concerns, discussion then centred on the reputational impact on TIE and the Tram Project if a sub-optimal option were chosen and whether TIE was obliged to do the work.*" It continues "*DJM noted that TS were aware of the proposed option and the discussion continues.*"
103. In other words, both I and the other non-executive directors were keen to establish the implications of entering into the supplemental agreement. But overall, we were content that it was the right thing to do because over the last ten months, frankly, nothing else had worked to induce the Infraco provider to start work on the project. At that meeting on 11 February 2009, this issue was being discussed long before the final agreement was reached. At that time, although the planned cumulative total of Infraco works that should have happened by then were 30.5 per cent, in practice only 1.5 per cent of actual

works cumulatively had been delivered. In other words, some nine or ten months after contract signature, only 1.5 per cent of the works had been completed rather than almost one-third of the total works. That was very much the context within which the board was considering reaching a supplementary agreement, bearing in mind our overall strategy of looking to work in partnership with BSC to build confidence and trust and relationships. As I previously stated, subsequently the TIE board reached a view that that approach was not working and we took a different view. That sets the context for those decisions at that time. The TIE board were clear that this was a one-off agreement that did not set a precedent for other works, over which the main contract still remained relevant. This was a specific agreement in relation only to Princes Street.

104. It is not the case that works should have started on Princes Street first of all in the project. There was a whole programme of works that should have started in June 2008. The fact that they had not started is a matter for Bilfinger Berger to explain. The reason why Princes Street was dealt with at this point was because that was when the Princes Street works were scheduled to begin. TIE and CEC were very keen that, given the sensitivity of disruptions to Princes Street in a central location in the city, and given its World Heritage status, implications for the retail sector, and given its proximity to major events such as the Edinburgh Festival taking place in Edinburgh, that they be handled as sensitively as possible. That is why Princes Street was being given particular attention. Also given its iconic status as part of the trams route, it was hoped that if this agreement could be delivered successfully, the contractor would then have had gained positive hands-on experience of actually delivering the contract in a substantial way that would give it the confidence to complete the rest of the works under the main contract.
105. I recall that the TIE board members were told of the on-going dispute with BSC in relation to on-street works in August 2009 (document reference **CEC00788086**). My response is the document (**CEC00825101**). TIE board's role as I have stated previously was to agree the strategic approach for the company to take in securing delivery of the contract, which changed over

time. The various disputes were reported at every TIE board meeting, both disputes that were referred on to the formal dispute resolution procedure and also other disputes which were not, for example, the primary dispute around the failure to mobilise and generally to execute the Infraco contract works.

106. I am referred to the minutes of the Audit Committee meeting on 18 November 2009 (document reference **CEC00348932**) which record Deloitte's report that the main issues arose around the open for revenue date and the anticipated final costs. Both of these items were affected by the programme disagreements and disputes. As demonstrated in Deloitte's internal audit review of financial control dated June 2010 (document reference **CEC00111661**) the Audit Committee were aware of the uncertain Anticipated Final Cost (AFC) and the uncertainty produced by changes in TIE's approach to issuing change orders. The Audit Committee first became aware that the project would not be delivered on time or on budget at the same time as the full TIE board became aware, which was in mid-2010.
107. Throughout the process, the Audit Committee had engaged with the main risks around delivery of the project and indeed very often those main risks were discussed at the full TIE board rather than in the Audit Committee, given their importance. In addition, as I mentioned earlier, the Audit Committee commissioned a range of internal audit work throughout the life of the project. For example, at the Audit Committee meeting of 18 November 2009, it considered an internal audit of project and programme reporting/Infraco, document reference (**CEC00111623**). That internal audit report outlines the underlying cause of the poor relations between TIE and BSC.
108. The Audit Committee commissioned further internal audit reports that were pertinent to the disputes and the problems, for example, report 2010-05, document reference (**CEC00380705**), on commercial strategy. That was considered at the 30 June 2010 Audit Committee. The overall conclusion of that report is that *"From the discussions undertaken as part of this work, under review of the documents provided by management, it appears that TIE has*

*adopted a robust decision-making process since the nature of the disagreements with BSC became clearer following contract signature."*

109. Throughout this process the Audit Committee commissioned repeated reviews on internal financial control in line with good corporate governance. The report taken at that meeting on 30 June 2010, document reference **(CEC00183022)**, reported "*Adequate assurance continues. The corporate financial control environment is robust and commercial procedures surrounding the Tram Project operate effectively.*" In other words the Audit Committee was repeatedly taking steps to seek independent assurance and independent challenge of our internal processes and strategy through its use of the internal audit facility.

### **Bonus Scheme**

110. I am aware of a report to CEC on 26 June 2003 (document reference **CEC02083550**) which noted when considering TIE's draft business plan that a performance-related bonus scheme had been introduced for TIE staff. According to the minutes of the Audit Committee meeting on 11 December 2007 (document reference **(CEC01467526)**) it was agreed that the appropriate committee to oversee the bonus payments was the Remuneration Committee. I can confirm this was the case. The Audit Committee was not responsible for overseeing employee remuneration and bonuses at TIE. The decision for a bonus scheme to be introduced for TIE staff predated my appointment as a non-executive director and I was not involved in that decision.
111. I do not know if the bonus scheme applied only to TIE employees or if it also included individuals seconded to TIE from other organisations and individuals and organisations engaged by TIE as consultants. I believe it may have applied to at least one seconded individual, Andrew Fitchie, but I do not know for sure. I was not involved in the operation of the bonus scheme and do not know how it operated.

112. Oversight and control was exercised over the TIE bonus scheme through the Remuneration Committee of the TIE board. I was not a member of the Remuneration Committee. However, I did attend some of those meetings at the invitation of the chair of the Remuneration Committee, Brian Cox. For example, I attended a meeting on 21 October 2010 and I also have some papers from meetings on 10 July 2007 (document reference **WED00000140**). I have a copy of an agenda of 24 September 2007 and for 16 March 2011, but I cannot recall if I attended those meetings. Based on the papers I have from those meetings that I did attend, the June 2010 Remuneration Committee paper (document reference **CEC00396659**), explains that in September 2009 the Remuneration Committee approved two bonus schemes for TIE: one bonus scheme based purely on project completion; and a separate scheme that had both an annual and a project completion element. My recollection is that the Remuneration Committee approved the bonus scheme policy, which was then applied by the Executive Chair and then later by the Chief Executive up to their level of seniority. For the Executive Chair or Chief Executive, the application of the policy was applied by the Remuneration Committee. I can recall one discussion about the level of bonus award for the Executive Chair of TIE, Willie Gallagher, during which the Remuneration Committee took the view that, in spite of efforts to succeed and in spite of factors beyond his control, the Executive Chair should be awarded only partial bonus for the year concerned.
113. I recall an email from Willie Gallagher to myself dated 16 December 2007 (document reference **CEC01509164**), in the context of a discussion on the draft operating agreement between TIE and CEC, in which Willie Gallagher indicated that he was unhappy about having to inform the Tram Monitoring Officer and therefore CEC about TIE's remuneration policy. In a further email on 17 December 2007 (document reference **CEC01514119**) I discuss proposed CEC involvement in TIE's remuneration arrangement. In summary, the proposals seemed to me to undermine part of the reason for having a company in the first place, with the flexibilities that that brought in respect of remuneration. In relation to the second document referred to, my view at the time was that the implication in the document was that CEC would decide on



the application of the remuneration policy to individual cases, and yet in my view CEC was too far removed to be able to make that judgement in a fully informed way. I do not know if CEC was aware of the sums paid in bonuses to TIE staff each year, including the sums paid to individual members of staff.

114. My views on the TIE bonus scheme at the time were that the existence of a bonus scheme was part of the expected and usual arrangements for this employment sector, and that it was relevant to TIE's ability to recruit staff who were of high quality, but also unlikely to want to work for a local authority under standard local authority terms and conditions. I had no concerns in relation to the existence of a bonus scheme, including whether it could give rise to a conflict of interest on the part of TIE staff.

115. I am referred to emails from December 2008 (document reference **TIE00167241**) discussing Willie Gallagher's departure and bonus. I cannot remember the details. My recollection is that the non-executive directors had been told that Willie Gallagher was leaving TIE. Legal advice had been taken on what the financial implications of that were contractually. From the emails, the position that I was taking was that the outcome should be to stick to whatever had been agreed to in relation to salary payable under these conditions and only to enter into more discretionary or negotiated territory if that was absolutely necessary. I was also clear that accessing potential future project completion bonus should play no part in the settlement, since we had not completed the project.

116. I do not know why Willie Gallagher left TIE. I do not know if Willie Gallagher received a bonus when he left TIE and what his remuneration package was when he left.

## Mar Hall Mediation

117. I am aware that in March 2011, the parties involved in the tram project met at the Mar Hall hotel outside Glasgow to mediate a settlement to the on-going disputes. I was not, and to my knowledge, the other non-executive directors were not, involved in the mediation. My understanding is that Vic Emery, who was the then Chair of TEL and TIE, and the Chief Executive of TIE and TEL, Richard Jeffrey, attended Mar Hall. In the period before the mediation, during mediation and immediately afterwards, I did not feel that the TIE board was being marginalised. The mediation had been planned for some months, with the knowledge of the TIE Board, at least since late 2010.
118. My understanding of what happened at Mar Hall is based on an oral report by the Chair, Vic Emery, to the non-executive directors on the completion of the mediation process. The oral report took place on 15 March 2011. We were told that the mediation had resulted in a non-binding agreement between the parties about a proposal which would see the Trams Project completed to a certain stage of the tramline under the current consortium, but that a formal contract variation which would give effect to that agreement would be put to the board subsequently for approval. We were told that the fuller contract variation was now being worked up and the content of that was subject to confidentiality constraints agreed as part of the mediation process.
119. With regards to the outcome of the Mar Hall mediation and the settlement eventually reached, I was never privy to the full terms of the mediated agreement and settlement. Subsequently, I understood from papers in the public domain put to CEC that an additional £231 million, in addition to the previously committed £545 million, was agreed and paid to the contractor. Presumably, the majority of that money went to Bilfinger Berger, given that the trams had been largely built, bought and paid for by that point. My view on those sums at that time was simply to note that the payment of additional monies beyond the £545 million budget was never an option open to TIE or TEL during my time as a non-executive director, under the financial constraints set by CEC at that time.

120. I resigned from the TIE and TEL boards in May 2011 because the extant corporate governance arrangements were being bypassed, in my view, on a critical issue, namely contract variation, and because I was put in a position whereby I was unable to exercise my duties as a non-executive director. I wrote to the chief executive of CEC on 12 May 2011 (document reference **TIE00617811**). I stated in that letter the reasons for my resignation.
121. On Monday 9 May 2011, in a conference call which began at 6.30 am, between Vic Emery, the Chair, Richard Jeffrey, the Chief Executive, and the four non-executive directors, I was told about a Minute of Variation 4, which included a £27 million payment which had already been made to the contractor on 3 and 4 May as part of a total additional £70 million to be paid to the contractor under the terms of this contractual variation. I was told that this Minute of Variation 4 was to be followed by a Minute of Variation 5 later in the summer, under which the remainder of the works would be carried out.
122. I was told the Minute of Variation 4 had been negotiated directly between CEC and the contractors and the sums of money to be paid were determined by CEC on the advice of Colin Smith, an independent quantity surveyor appointed by CEC, rather than taking the advice on costs presented by TIE staff. I had had no knowledge of these developments, including Minute of Variation 4 and Minute of Variation 5, until this telephone call, even though the payment which had already been made without the non-executive directors' knowledge clearly breached the terms of the existing operating agreement between TIE and CEC. I had been sent an email on 5 May from Richard Jeffrey, (document reference **WED00000139**), alluding to these variations to the contract but without the full background. The telephone call was the first opportunity I had to discuss it and to hear about the full background. That email from Richard Jeffrey made clear that the sum to be paid to the contractor under Minute of Variation 4 "*is not supported by our analysis*". For example, on one element of the agreement, the TIE staff valuation was that £19 million was due to be paid, whereas in fact £49 million was paid on that element. This was one of a number of concerns that were listed.

123. Following the phone conversation on Monday 9 May, and following further email correspondence with non-executive directors, I emailed those non-executive directors on 11 May 2009 and I emailed Vic Emery copying to the other non-executive directors, setting out my concerns.
124. At the meeting of the TPB on 11 May 2011, I made clear my views on the unacceptability of what had happened in respect of the payment which had already been made without the knowledge of the non-executive directors of the company and in respect of the further committed payments to be made under Minutes of Variation 4 and 5. I asked that my concerns be minuted. Those concerns were minuted and are set out in the minutes of that meeting (document reference **TIE00896987**). I then wrote a resignation letter to Sue Bruce, the Chief Executive of CEC, on 12 May resigning (document reference **TIE00617811**). I received an acknowledgement of receipt of my letter from her assistant but received no other response.
125. With regards to the settlement eventually reached at the Mar Hall mediation, I never saw the full detail of what had been agreed and therefore was then and am now unable to reach a view on how good or bad an outcome that was. I note that the 25 August 2011 paper put to a meeting of the full council sought CEC's agreement to give effect to the contractual variation which followed the Mar Hall mediated agreement, (document reference **TRS00011725**). CEC indicated that this outcome would cost an additional £231 million on top of the already agreed £545 million contract. I noted how the additional £231 million sum compared to the £545 million that had already been agreed to under the original contract for Infraco, which I had been involved with.
126. My recollection is that the original Infraco contract provided for approximately £240 million to be paid to Bilfinger Berger and Siemens. So the payment of an additional £231 million would approximately double the income being paid to the infrastructure contractor, even though some of the major works had already been completed. For example, the depot was largely finished, some of the major structures were finished, such as the airport bridge and the Gogar flyover, plus some off and on-street track work had been laid. And this sum

was being paid despite the fact that the route had then been considerably shortened to go from the airport to York Place, as opposed to Newhaven.

127. At the point that I resigned from TIE, TIE had paid out about £400 million of the £545 million budget. At that point, a further £15 million was owed to CAF, the tram manufacturer, for works carried out. So approximately £415 million had been paid or was about to be paid shortly. Those payments had funded the delivery of approximately 75 per cent of the project being completed. All the trams had been built. All the utilities diversions had been done. The Bill had been taken through Parliament. The preparatory work had been done on the business case. The Audit Scotland Interim Report dated February 2011 (document reference **ADS00046**) noted that at that point approximately 28 per cent of the infrastructure works had been done. Given all of that, the remaining works to be done to finish the project had been significantly de-risked, as all the other elements were in place. So if those sums are correct, then £415 million would have been paid with approximately 75 per cent of the works completed for the full scope of the project as originally specified in the contract. The amount of £776 million was almost twice the £415 million already paid, with approximately 25 per cent of the works remaining to be carried out and indeed a reduced specification to be delivered with a shorter track length only as far as York Place rather than Newhaven. I am asked for my views on the settlement eventually reached with the contractor following the mediation process. Having not been privy to what was agreed through that process beyond what I have referred to above and information in the public domain I am not in a position to form a fully informed view of that settlement. However if the figures I have just quoted are correct then I believe it would be fair to say that that the contractor did considerably better financially out of the mediated settlement compared to the terms of the original contract they signed considering the limited and reduced amount of work they agreed to do in return for an almost doubling of their overall payment.

128. My final recollection of that period is that during those last few days the non-executive directors did ask the Chief Executive whether there were other

options available, accepting that those were not the agreed outcomes from mediation, and it was confirmed that the other option available would have been to re-procure the remaining works to be carried out, accepting that that might lead to additional delay but perhaps significantly less cost.

129. To reflect back on what the board of TIE were being told about the contractor's position back in 2008 and 2009 and 2010, whereby the repeated message from them was that they required more money over and above what they had agreed to in the Infraco contract, in order for them to be prepared to undertake the works they had agreed to do under the contract. I simply note that at the end of the day the contractors were indeed paid a significantly increased sum of money.

### **Audit Scotland**

130. I am aware of an email dated 8 June 2007, (document reference **CEC01677282**) from Graeme Bissett to myself and others discussing the upcoming Audit Scotland review. Audit Scotland undertook reviews of the Tram Project in June 2007 and February 2011 (**CEC01607203** and **ADS00046**). I had no involvement with the Audit Scotland reviews. I do not know how Audit Scotland undertook the reviews. I had no visibility of the actual work undertaken by Audit Scotland. I only saw the final reports and I thought that their findings were a fair representation of the Tram Project as I had experienced it.
131. I largely agreed with the findings of the two reports, June 2007 and May 2011. I say largely rather than completely agree because I have mentioned earlier that, for example, in the 2011 report Audit Scotland cites the Princes Street dispute in early 2009 as being the first major dispute, when in fact my experience was that disputes and problems and difficulties arose as early as June and July 2008 and continued continuously throughout the life of the project. But the report was largely accurate and I agree with it.

## Part 2 – TPB Meetings

### General

132. TPB meetings were scheduled in advance. Discussion was structured around an agenda. There were some standing items, for example to discuss progress over the previous period and key issues for the forthcoming period, cost and implications for budget, programme, risk, and approvals or decisions required. The detailed agenda varied according to the issues to be discussed at that time. The meetings were chaired meetings. The agenda was worked through and actions were minuted. There was a lot of discussion on the issues that were put to the TPB. The executive members were questioned on the matters arising and they were able to provide answers. I was a non-executive director of the TIE board and Chair of the Audit Committee and attended TIE and Audit Committee board meetings. I was not a member of the TPB, although I did subsequently attend some of those meetings. I began to formally attend TPB meetings from 12 March 2008.
133. Information was provided to each of the TPB meetings by papers that were circulated in advance of the meetings. I was happy with the quality and volume of the information made available. There were some exceptional occasions when I asked for additional information but I have not kept a record. I cannot recall what this related to or from whom I requested it. The area in which I tended to request additional information related to my work as Chair of the Audit Committee in which, for example, I would meet individually with the Finance Director, Stewart McGarrity, regularly to discuss the financial position of the company, and at which I would seek further information about issues. I considered that the Project Director's Reports and the TS reports gave an accurate and complete picture of the project as it progressed.
134. There is repetition in format from one month to the next in the Project Director's Report and the reports to TS. I believe that content is repeated where the content is still relevant. That repetition was not improper or

unhelpful, and in my view the information provided in these reports was helpful. I do not feel that this made it difficult to determine precisely what is happening at any time. For the most part, I found the material provided to me could readily be understood. At times, I asked for further clarification around technical detail, for example, around engineering matters.

135. The failure of SDS to produce designs on time is a matter mentioned in almost all of the TPB reports. In my view the Board were being regularly briefed about the delays and problems with SDS. As far as I was aware, everything that could have been done by the TPB to resolve matters was being done, and to my knowledge at no point was an option to resolve the problems suggested which the TPB wished to take forward but felt it was prevented from doing so. The lead TIE executive team members reported on the discussions that they were having regularly with SDS to improve the situation, and set out remedial plans repeatedly throughout this period. I cannot recall the specifics of the action taken, but along with utilities diversions, the design production was discussed at every board meeting, and in depth, and I know that the papers for the TPB provide updates on the specific actions taken.
136. Overall, the performance of the contractor under SDS was poor, and my recollection is that the TPB were disappointed with that performance. Executives were having regular meetings with the SDS contractor, TPB and TIE Board were being regularly briefed about SDS delays. I am not aware of anything else that could have been done. Certainly, this was the subject of constant attention and effort, and the TPB and everybody else in TIE was fully aware of the importance of this element and its interaction with the other elements of the project, such as construction. One action that was taken, which I have mentioned previously, was to novate the contract to the Infracore company in order to better align risk with the people best placed to handle that risk, by agreement with BBS and as part of the overall contractual settlement in May 2008.
137. In my view, it was appropriate to continue with the procurement and then the construction programmes as the design was partially available. In particular I



believe it was appropriate to award the Infraco contract despite the absence of completed detailed design and in the knowledge that late design was causing delays to MUDFA. I base that view partly on the fact that the Infraco contractors were fully aware of the position about design, and indeed were specifically involved in negotiating the novation of that contract to Infraco in return for increased funding. Infraco accepted design risk in return for the higher sum agreed at May 2008 compared to the lower sum that was on the table earlier that year. The Infraco contractor would have priced in the design risk that it was taking on, having conducted its own due diligence on this matter. There was no question of the infrastructure contractor being forced to take on responsibility that it was not prepared to take on. These issues were discussed at the TPB, although I did not attend every meeting of the TPB. I attended meetings when the TIE or TEL boards were run consecutively with the TPB, so I cannot speak comprehensively on behalf of every TPB meeting.

138. Almost all the reports to TS noted reasons for design slippage and were being reviewed and recorded each week (see for example page 27 of **CEC00983221**). The point in stating this every time was to factually report the situation. I do not know what was done with the information, I understand that this was sent as a report to TS. I do not recall the detailed discussions at the TPB of these reviews, but I do recall that design slippage was regularly and fully discussed. Just to reiterate, my position on this project was that of a non-executive director and my role there was to provide strategic direction and control, not to either manage the works - that is the role of the executive team - or to manage the operational detail. I believe that I can add more value to the Inquiry in talking about the overall approach taken, the overall strategy taken, to managing the tram project than I can in commenting on some of the more detailed operational matters. Also it is the case that clearly I was not a full-time member of staff on the Tram Project. The non-executive directors might spend perhaps two days per month on this, so again my memory of some of the detailed technical discussions is not as clear as my memory and, indeed, my notes and records are, of the wider strategic issues.

139. I am not in a position to give a view on whether or not any action to tackle design slippage made any difference and I am not in a position to know whether or not anything else was tried beyond what was reported to the TIE Board. What I can add is that the non-executive directors on the board of TIE, and subsequently of TEL, were very aware of the risks to the whole project that rested with design slippage, and indeed these were recorded in the various risk registers for the project. This was an issue to which we returned repeatedly over the course of the project, along with utilities diversions at least for the first couple of years, and certainly the Infracore issues that I have mentioned earlier. But I am not in a position to recall the detailed initiatives and meetings held in respect of resolving the design issues. As time went on and the design became more complete, design issues had less effect on the progress of works throughout the project. However, my recollection is that design issues also were one of those issues referred to the dispute resolution process. If I am correct in that recollection, it would be fair to say that design still had issues, certainly during 2009 if not in 2010.
140. I note that an anticipated final cost is included in the Project Director's Reports and the reports of TS. This would have been expected as part of such a report, bearing in mind the fixed nature of the funding available for this project.
141. Risk was managed at the TPB by discussion structured around both the risk report, which itemised and quantified risks, and also separately in relation to specific items for discussion. It would be fair to say that the majority of the discussions at the TPB, and indeed at the TIE board and the TEL board, were one way or another about risk management.
142. There was an allowance for risk on the project and drawdowns were made against it month by month. Papers were presented for approval of these drawdowns. These papers were discussed at the TPB meetings. There was an option to not approve the drawdowns. Had approval not been given then the related actions would not have progressed. I am not certain what QRA stands for; it might stand for a quantified risk allocation.

143. Itemised and quantified risks on the project were considered fully at the various TPB meetings. Extracts from risk registers were often produced. These were discussed, although in addition often the risk issues were the main topic of discussion anyway. The TIE and TEL boards also discussed risk extensively. The risk treatments were evaluated to assess whether it was likely that they would be able to mitigate risk or whether they were, in fact, doing so. In other words, if they were prospective risk treatments, then the former would apply. If it was discussion of this treatment already underway, then the latter would apply. I was satisfied that the risk treatments were an appropriate means of addressing the various risks. Much of the discussion around this at the TIE and TEL boards was around managing strategic risk, given our focus on putting in place a strategy which would ensure that the contract was delivered.
144. I note that the reports in the TPB papers routinely note that risks have been reviewed. I do not know in detail what the review entailed as these would be reviews carried out by executive staff, not non-executives. Discussion always focused around mitigation in addition to being mindful of the financial implications. I do not have any recollection and I am not really in a position to comment on this level of detail regarding whether allowance was made for the Base Date Design Information, BDDI.
145. I am referred to the PD Reports in the June 2009 papers, which states that the QRA output was as accurate as reasonably possible (document reference **CEC01021587**, page 17). I do not recall this report and cannot comment.
146. I note that the PD report for September 2009 (document reference **CEC00848256**, page 19) states that TIE will continue to report on the risk allocation at financial close until a new budget with an updated QRA is approved. I believe this statement relates to the reality at that moment in time. It would be impossible to accurately forecast an outturn figure for the project with the various risks quantified at that time, given the degree of uncertainty around the project, such as issues which were in dispute and being taken forward as part of the DRP process.

147. I recall that during the project there were significant disputes in relation to changes in drawings, sometimes referred to as the BDDI-IFC issue, and BSC's refusal to start work. The financial risk assessment and allowance of this was carried out by the executive staff within TIE and so I cannot comment upon the detail of this.
148. At page 32 of the papers of the meeting in late July 2009 it is proposed that the Financial, Commercial and Legal Sub-Committee (the "FCL") should oversee resolution of disputed areas (document reference **CEC00843272**). Based on what the paper referred to states, rather than my recollection, I believe the FCL was set up because of the extent of the issues in dispute at that time. This committee had not existed previously. Again from what the papers themselves say as opposed to my recollection, the disputes were delegated to it because of the extent of the workload and that this needed specific resource allocated to it. I did not attend the meeting in late July 2009.
149. I note that the paper mentioned above says that a document entitled "*Resolution Strategy*" will be presented for TPB approval on 29 July 2009 (document reference **CEC00750538**). From a reading of the papers as opposed to my recollection, I believe this document is the resolution strategy that went to the TPB and that informed discussion. The resolution strategy was the analysis of which issues to progress from pages 9 and 10. This was a process for making balanced and informed judgements about which specific issues to take into the disputes resolution process. This includes the desirability of reaching clarity about key issues blocking progress, rather than just indiscriminately submitting all disputed issues into the DRP. From the papers of the meeting in late July 2009, the role of the Challenge team is referred to on page 11, to make and test the assessments. I do not know how it functioned as I was not there.

**TPB papers for 31 October 2007 (CEC01357124)**

150. I am referred to item 3.20 in the late September 2007 minutes, document reference (**CEC01357124**), which notes that 58 to 60 per cent of detailed

design was completed. I do not recall the details of this, but under-performance of the design contract had been reported regularly. It was certainly an issue that was discussed in regards to the effect that this might have on the tendering exercise for Infracore.

151. I note that at page 8 there is concern expressed that the estimated capital cost included VE savings. VE stands for value engineering. Value engineering was a process by which through discussion with the bidder in this case, or subsequently with the contractor, different, more efficient, better value ways are identified of achieving the same or better outcomes. I do not know what levers were available to the project to ensure any changes in value engineering could be absorbed in the estimate.
152. The papers include minutes of the meeting on 15 October 2007. I queried how much of the price was based on SDS design at item 3.3. I understand by the answer noted from Geoff Gilbert that 30 per cent of bidders' costs were based on preliminary designs, mainly structures and highways. I understand that these were the key price sensitive items and that bidders could price other items without having detailed designs. With regards as to why other structures and highways could be priced without detailed design, this is really a technical operational matter which would require a professionally qualified response. My understanding from a non-executive perspective is that the costs on other items would not vary so much depending on the specific designs. For example, the cost of track, assuming it is all of a standard quality and construction, would simply vary according to the length of track, rather than being so sensitive to design matters. By contrast, the cost of a bridge could vary enormously depending on the design of that bridge. This is really a level of question which would be better answered by one of the engineering staff.
153. Item 4.1 notes the TPB endorsed the recommendations and conclusions from FBC v1. The FBC v1 made available to us information such as capital cost, programme risks and affordability. The basis of my endorsement, I cannot speak on behalf of others, was by applying my judgement based on

information made available to me, both in writing and discussion, and bearing in mind that by then we had received bids for the work. Item 8.1 notes that TPB decision to endorse the recommendation of the preferred bidder was endorsed. The decision to endorse the recommendation of the preferred bidder was based on the information presented to the TPB, including in the slides presented to that meeting, which compared the relative merits of the bids received. In this minute, it notes that the issue of governance was postponed, but in the progress report in the same set of papers it notes that a revised version of the governance structure was approved on 26 September 2007, page 13. I cannot explain this. These design risks were not assessed as green, page 31. I would have wished it was otherwise, that the risks were such that they could have been assessed as green, but the way they were presented as being not green accurately reflected the status at that time.

#### **PowerPoint Presentation for TPB on 15 October 2007 (CEC01358513)**

154. I was not present at the TPB meeting on 15 October 2007. OGC stands for the Office of Government Commerce. It is part of the UK Government. It has designed a process that is applicable across the civil service and the wider public sector called Gateway Reviews. A Gateway Review had been carried out on the Edinburgh Trams Project, which concluded on 3 October 2007, as explained in the slides. Gateway Reviews take place at different stages of a project's life. They always contained recommendations to increase the chances of successful delivery of that project. They usually give an indication of timescale for that recommendation being put into effect. The recommendation mentioned here is recommendation number 1 listed on slide 6. It says, "*Recommendation that the preferred bidder is appointed as soon as possible*" and the status was cited as, "*As soon as possible*". I do not recall whether or not that recommendation was discussed in detail, but certainly the slides generally were the subject of significant discussion at that board meeting. My recollection is that there was agreement that a balanced approach was required: on the one hand the importance of keeping the competition for the contract alive for as long as was necessary to reach a stage where a preferred bidder could be appointed with confidence, and on

the other hand the need to not unfairly require bidders to continue with the process and incur cost without there being a reasonable opportunity for them to win the contract. It was consistent with the recommendation that the TIE team should consider how the desired levels of certainty should be achieved, but the fact is that the OGC recommendation in itself was not binding here. It was a matter for the contracting authority, TIE, to decide when was the right moment to appoint a preferred bidder, not that of the OGC. The OGC findings are advisory, they are not binding.

155. It is apparent from slide 26 that both bids were too high. I do not recall the TPB reaction to this. My experience is that in processes like this, one would expect to see a refinement of bids in the process leading up to the submission of best and final offers. Slide 59 refers to firm prices and rates. I understood that to mean firm and final prices received from bidders, and firm in the sense of fixed. To a significant extent, the terms of the bid were settled at this stage, but as it turned out there was further change in the bid of the preferred bidder. The 12 March 2008 board meeting records this point whereby the sum of money to be paid overall rose to £508 million from £498 million, in part to buy out the risk of SDS non-performance. I do not have the full breakdown to hand of how the figure of £498 million was made up. Part of that figure refers to the bid from the contractor, codenamed Wallace, and that is set out in slide 37. The other elements would have included the utilities diversions work, the design work, the cost of the trams procurement and other elements, including project management. I do not have papers to hand which would provide that breakdown, however that breakdown is available, and I am sure the Inquiry will have that in other papers.
156. I note that slide 51 states that 15 per cent was allowed for risk and contingency. I do not know if this had been discussed at the TPB. With reference to my comments earlier about optimism bias and contingency where, in line with best practice, it makes sense to build into project estimates sums to cope with risks crystallising which end up costing you more money, and that is what this referred to. I do not have direct comparison details to other projects or to guidance to hand, but in general at this stage in the

procurement process a 15 per cent contingency allowance would be, in my experience, in line with normal practice.

157. My understanding is that slide 52 shows different ways of expressing the proportion of the budget which is being allocated to accommodate risk and contingency. Two of those scenarios are actual scenarios and two of those scenarios are projected scenarios. In other words, it expresses £49 million as a proportion of varying sums of money depending on how you count it and what materialises. In considering how the risk allowance relates to the headroom referred to in slide 53, I believe it is the same figure, accepting that was a £2 million difference. I cannot explain that from the papers I have at this time.

**TPB papers for 7 December 2007 (CEC01023764)**

158. There was a TIE board meeting on 12 November 2007, I was not present at it but I have been provided by the Inquiry with a copy of a presentation that was given at it (document reference **CEC01427080**). The non-executives had not yet become members of the TPB, therefore I did not attend the TPB meeting on 7 December 2007 and I did not receive the papers for this meeting (document reference **CEC01023764**). I am aware that a decision had been taken to migrate TIE Board members to the TPB but I do not recall why they were still not involved by this stage. I am referred to documents for TPB meetings held on October 2007 (document reference **CEC01023764**) and 7 December 2007 (document reference **CEC01023764**). I did not attend these meetings so I cannot comment on these documents. I did attend a TIE board meeting on 11 December 2007, document reference (**CEC01048838**), at which, amongst other things, I gave a verbal update from the TIE Audit Committee meeting held earlier in the day.

CEC01023764  
should be  
CEC01357124

**TPB papers for 19 December 2007 (CEC01526422)**

159. I am referred to the minutes for the early December TPB meeting (document reference **CEC01526422**). I did not attend this TPB meeting on 19 December



2007, neither did the other non-executive directors of TIE, so I am not able to comment on that meeting.

160. I am referred to the papers for the early December TPB meeting (document reference **CEC01526422**). I did not attend this TPB meeting on 19 December 2007, neither did the other non-executive directors of TIE, so I am not able to comment on that meeting. The only thing I can comment on after the event is to interpret tables on pages 10 and 11, as this does not depend on me being in the meeting. The tables on pages 10 and 11 seem to be explaining the differences between the proposals put forward by the preferred bidder before, and then after, what became known as the Wiesbaden deal which took place on the 13 December 2007. Looking now at the table on page 10, one of the salient points was that whereas before that date firm elements of the bid had comprised approximately 77 per cent of the bid at preferred bidder stage, the effect of the Wiesbaden deal, according to the table, was to increase that proportion to 96.5 per cent and to be in the category of firm prices. A second salient fact would be the increase in price to the public sector of agreeing the bid. The table on page 10 refers to a £10.37 million increase in the cost of the bid and the table on page 11 sets out in more detail the implications of that, and the other movements and the other elements of the Tram Project, and the implications of that in turn for the remaining risk allowance, which decreased from a total of £49 million, as set out in the Final Business Case, to £38.9 million.

**PowerPoint Presentation for TPB Meeting on 19 December 2007  
(CEC01483731)**

161. I am referred to the PowerPoint for the TPB meeting on 19 December 2007, (document reference **CEC01483731**). I did not attend this TPB meeting and therefore I cannot comment. I am referring to page 5 and page 8, where Stewart McGarrity reported that BBS were to take the detailed design development risk; these issues were discussed at the TIE board subsequently in January, which I did attend.

**TPB papers for 9 January 2008 (CEC01363703)**

162. I am referring to the minutes for the TPB meeting on 19 December 2007 (document reference **CEC01363703**). I was not at this meeting and neither were the non-executive directors, therefore I cannot comment. Previously the non-executive directors had not been invited to attend meetings of the TPB. Subsequently the decision was made to change this and I was present at the TPB meeting on the 23 January 2008.

**Papers for Joint Board Meeting on 23 January 2008 (CEC01015023)**

163. I am referred to the minutes for the TPB meeting on 9 January 2008 (document reference **CEC01015023**). I did not attend the TPB meeting on the 9 January 2008 and neither did I attend the TPB meeting in December 2007 and therefore I cannot comment on the minutes. With regards to page 9 of the PD report, which notes that the governance structures were approved, it is suggested that these changes have been carried out outside of any meeting. I do not have any recollection of being a part of the discussion that said this happened away from a meeting.
164. In January 2008, although I did not attend the TPB meetings, I was present at two other meetings which dealt with some of the same matters from previous meetings such as progress towards securing contract signature. I attended the joint TIE Board and TPB meeting on 23 January 2008 and the Executive Summary paper made available for that meeting (document reference **CEC01015023**) noted the following: *"The negotiations with the preferred bidders for Infraco and Tramco continued. The discussion with BBS resulted in the signing of the agreement for contract price for phase 1A on 21 December, essentially fixing the Infraco contract price, based on a number of conditions. Key points of agreement are: effective transfer of design development risk, excluding scope changes to BBS; construction programme to commence operations in Q1, 2010; and certain exclusions from the fixed price of items outside the scope of the Tram Project, all of which are well-*

*understood and either separately funded or adequately provided for in the overall Tram Project estimate."*

165. In addition, I attended a TIE board meeting on 29 January 2008. The minutes for that meeting (document reference **USB00000293**) note that I attended part of the meeting. The minutes for that meeting note the following: *"Meeting with BBS held mid-January. BBS requested the review and then proposed a revised programme to contract award. There is a four-week delay in terms of the position on the contracts being ready to sign. This should now be finalised to award the contracts for end February."*

**TPB Papers for 13 February 2008 (CEC01246826)**

166. I am referred to minutes for TPB meetings in January 2008 (document reference **CEC01246826**), and to discussions at the TPB meeting in February 2008. I did not attend these meetings and I cannot provide further comment.

**TPB papers for 12 March 2008 (CEC01246825)**

167. The first TPB meeting at which I and the other non-executive directors, and also the elected members from CEC, were invited to attend was the meeting on 12 March 2008. Brian Cox, Neil Scales, Peter Strachan and I were the non-executive directors of TIE. Allan Jackson, Gordon Mackenzie and Phil Wheeler were the councillors. These people were already members of the TIE board and this was the first time that we were invited to attend the TPB. The practice was to separate out items which should be discussed at the TIE board and to hold TIE Board meetings consecutively with the TPB in order not to have duplicate conversations about the same issues in two meetings. It was considered more effective and efficient to have the same discussion once and then separate out those matters which only the TIE board should properly consider, given the different responsibilities.
168. The 12 March 2008 TPB meeting was one of the more significant board meetings, given its proximity to contractual close. There was still no contract

close in March. I understood from the updates provided to the board why that was the case. It was frustrating however that we had not been able to award the contract yet. That was a shared view across the TPB, and indeed the TIE board.

169. I am referred to the minutes for the TPB meeting in February 2008 (document reference **CEC01246825**) in which Donald McGougan is noted as having asked if the design risk could be bought out (page 6) and the response is that neither consortium would accept this. I was not at the February meeting in which this comment is made, but I can say that when the final contract was signed, BSC did take on the risk of future design development as the contract was novated to the Infraco contract. At the point of the February 2008 meeting, or indeed the March 2008 meeting, design risk still lay with TIE as the contracting party through the SDS contract. That was a matter of fact and the risk would remain with TIE until that contractual position changed, which it did do subsequently in May 2008, when that design contract was novated into the Infraco contract.
170. I am referred to the slides presented at the 12 March 2008 meeting which state *"Infraco budget at financial close: £243.8 million, risk allowance £33.4 million. 95 per cent of the combined of the Infraco/Tramco price is firm - the remainder being provisional sums which have been reviewed by TIE and BBS for adequacy. Risk allowance of £33.4 million is 10.8 per cent of £308.7 million base costs to go beyond financial close. Costs to go beyond financial close comprise: £290 million (71 per cent) Infraco, Tramco and other firm contracted costs; £23 million (7 per cent) Infraco provisional sums and sundry works; £31 million (10 per cent) MUDFA and utilities costs with firm rates; £36 million (12 per cent) project management and other costs at mostly known rates."* In addition, from the minutes of the meeting held on 12 March 2008, the following remarks were made by Stewart McGarrity *"Pointed out that the increases of Infraco contract price of circa £10 million meant the baseline project estimate rises to £508 million from £498 million. WG explained that in particular to buy out the risk of SDS non-performance was considered good value for money. He also confirmed that the current price reflected the*

*programme and scope for construction that BBS could deliver. WG provided a summary to the board to approve the project to proceed on the basis of: total project budget at £508 million; programme to commence revenue operations July 2011; that the SDS novation and Network Rail APA are non-negotiable requirements for proceeding. GL [Gill Lindsey] confirmed that CEC was fully engaged in the process of notifying the intent to award."* 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.

171. I am referred to item 6.1 of the minutes of the TPB meeting on 13 February 2008 (document reference **CEC01246825**) in which Stewart McGarrity stated that there was a risk allowance of approximately £30 million relating to £90 million of non-firm future costs: I did not attend this meeting and therefore I cannot comment.
172. I am referred to the fact that the MUDFA works were slipping, page 13 (document reference **CEC01246825**). I do not recall the extent to which MUDFA works were discussed at this meeting. MUDFA works were generally discussed at every meeting. However, on this particular occasion, the negotiations leading to the future award of the Infracore contract were the main focus of the discussion.

#### **TPB Papers for 9 April 2008 (CEC00114831)**

173. I am referred to the papers for the TPB meeting in April 2008 (CEC00114831). I am asked whether the extension to the membership of the TPB changed the way it worked. I am not able to compare how the TPB worked before I attended with how it worked once I began attending. Certainly, the non-executive directors and the councillors did ask questions in the TPB once they were attending it. At this time in April 2008 there was still no contract close.

Closing the Infraco contract was the primary matter of discussion at the TPB in March 2008 meeting and everybody was very focused on achieving that. My view was that it was important to agree the very best contract possible which would deliver the tram system which had been procured. Everybody in the TPB was very aware of the delay in conclusion of the contracts compared to target dates. I suspect that there is no mention of that delay in the minutes because it was just so obvious. This was the number one issue at the time. Contract signature had been planned to happen in January 2008. It had been delayed until March 2008, and there were now further delays in concluding the negotiations with the bidders. So I do not think anybody was remotely unaware of the salience of this issue.

174. I note that the minutes for the TPB meeting in March 2008 (document reference **CEC00114831**) record that the position with BBS was settled in terms of price. The first thing to note is that there was movement in price between the March 2008 meeting and final contract signature. In terms of Schedule 4, I do not recall any discussion about Schedule 4 at the March 2008 meeting or, indeed, the April 2008 meeting or the May 2008 meeting. My recollection is that Schedule 4 was a part of the contract which was relevant to how changes would be dealt with under the terms of the contract. In particular, it was relevant to how issues around changes or the incompleteness of design, and changes arising from other sources, would be handled under the contract. I do not recall now whether Schedule 4 was the subject of any of the referrals to the dispute resolution procedure. I suspect it probably was. It did become apparent over time that Schedule 4 was significant in the view of Bilfinger Berger in terms of its obligations to carry out the works specified under the contract.
175. At a TPB meeting on 16 November 2010, I, along with the other non-executive directors, was told that the firm of Anderson Strathern had been commissioned to review the legal advice which TIE had received in the run-up to contract signature back in 2008, and in particular to review the process which had led to the agreement of Schedule 4 amongst other key clauses in the contract. I was told this by the Chief Executive of TIE, Richard Jeffrey, and

I believe that the work was commissioned either by him or by the Chair of TIE. I do not recall who specifically had commissioned the advice. Subsequently, I was given a copy of the advice received from Anderson Strathern in January 2011 (document references [REDACTED] commenting on the process of negotiation that led to contract signature in May 2008. It included the agreement of Schedule 4 and clauses 4.3, 65 and 80, all of which were relevant clauses in respect of how changes would be handled under the contract. [REDACTED]

[REDACTED]  
[REDACTED]  
[REDACTED] I note that the paper to the TPB in April 2008 (document reference **CEC00114831**) said that the agreement contained "a *relatively conventional contractual change mechanism*", which was part of the subsequent dispute about Schedule 4 [REDACTED]

176. Issues arising in relation to SDS novation were discussed at the TPB. For example, there was a report in the papers for the TPB meeting in April 2008 (document reference **CEC00114831**) about the Infraco contract suite which stated "*A contract price has been agreed...A substantial proportion 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 as such provisional sums are included... The agreement contains a relatively conventional contractual change mechanism in relation to the management and evaluation of variations...The novation of SDS provider to Infraco involves Infraco taking responsibility for managing SDS to produce the remaining design and approvals for the Edinburgh tram network. The principle of novation was to ensure that the integration of design and construction is the responsibility of BBS and gives BBS recourse to the same contractual remedies against SDS as TIE would have had in that situation, including critically the ability to claim against SDS in relation to defective design carried out by SDS.*"

177. My recollection is that the delay around design was primarily around the quality of work done by SDS. Design work had to be repeatedly redone because of the poor quality of the work being produced by SDS. This had been an issue for many months previously. There was no new issue, to my recollection, appearing at this point in the process. I do not know what was included in the SDS contract about novation, but the TPB board were being told at this point that that contract could be novated to the Infraco contract and that is what happened. The papers for the April 2008 TPB meeting (document reference **CEC00114831**) also include the following statement *"At the council's request, DLA have reported their advice on the legal acceptability of the Infraco contract suite separately to the council. Their report contains a detailed risk matrix which demonstrates where residual risk falls between the public and private sectors. The risk analysis has been matched with the risk contingency calculations embedded in the final project budget to ensure we have full alignment of risk and costs."* The Close Report, version 9 (document reference **CEC01486902**) was discussed at the TPB meeting on 9 April 2008. Paragraph 8.2 of the Close Report says *"Price certainty achieved"*. Then it goes on to provide a breakdown of the Infraco price of £234 million.
178. In relation to item 10.1 from the papers for the TPB meeting in April 2008 (document reference **CEC00114831**) it states that there was a £10 million increase in the project price and some components are referred to in item 10.3. This is a reference to discussions on 13 March 2008. This was not the first time that the £10 million increase had been raised. I believe this is a reference to remind the TPB members of why the baseline project estimate was at that point at £508 million rather than £498 million. The reasons for that were the changes in the scope of the contract and also the costs of the contract that were agreed back in December 2007 at a meeting held in Wiesbaden, Germany. That had been discussed at previous TPB meetings. Some components referred to in item 10.3 are arising at this time because that is Stuart McGarrity explaining the primary reasons for the increase in price. In other words, Stewart McGarrity was setting out the items of benefit to TIE which the increased price had bought. The result of the Wiesbaden deal was that a significantly greater proportion of the costs became fixed and firm. I



referred to this previously. In summary, at the preferred bidder stage, the proportion of the Infraco bid which comprised what were called firm elements of the bid was 76.93 per cent. The result of the Wiesbaden deal was to increase that to 96.5 per cent, a very significant benefit to the public sector. That is the first item that Stuart McGarrity is referring to in the minutes at item 10.3. He goes on to talk about the deal providing greater quality assurance. He refers to the novation of the SDS contract, which I referred to previously. He refers to provisions that were secure in relation to maintenance of the tram system, improvements in the rate of mobilisation of the contractor to undertake the work and in relation to spare parts. I do not recall what those three items were in detail. He referred to the fact that under this particular version of the proposed deal, the construction programme would conclude in July 2011. Although they were arising at this time, they were not arising for the first time. These elements had been referred to repeatedly in previous discussions and the minutes and board papers available for those board meetings set those out. For example, they were referred to at the TIE board meeting on 23 January 2008.

179. I note that in item 10.4 of the March 2008 TPB minutes, included in the papers for the TPB meeting in April 2008 (document reference **CEC00114831**), Willie Gallagher referred to the buyout of the risk of SDS non-performance. I believe this is a reference to the issue I have mentioned repeatedly, which was the novation of the SDS contract to the Infraco contract. The significance of that was that responsibility for managing the performance and bearing the financial consequences of the performance under the SDS contract would, by agreement with BBS, now become the responsibility for BBS. In return for this change in responsibility, BBS would be paid a higher sum of money under the contract. In other words BBS would be paid a proportion of the £10 million increase for the buyout of the risk of SDS non-performance.
180. I am referred to item 10.5 from the March 2008 TPB minutes which states the items that were included in the risk allowance and refers to sums being provided for in relation to risks around programme delays, unforeseen delivery issues, design and consent issues and MUDFA-related issues. I have already

referred earlier to the comments made by Stuart McGarrity in a general way to *"The increases in Infraco contract price of circa £10 million meant that the baseline project estimate rises to £508 million from £498 million."*

181. I refer to the PD Report to the April 2008 TPB meeting (document reference **CEC00114831**). I understood that the position was that *"sufficient progress was made to issue the notification to award on 19 March."* It was clear that MUDFA was slipping, page 13, and that the Infraco contract was about to be awarded. I do not recall the specific discussion about MUDFA at this meeting. However, in general, the interaction between MUDFA and Infraco contracts was discussed regularly at TIE Board and TPB meetings. I would summarise those discussions by saying that TIE accepted that there were some instances where the delays in the MUDFA works, in many cases arising because of the unexpected complexity of the work required, were issues which would legitimately cause delay to Infraco in starting work and that therefore Infraco would be entitled to compensation for some of those. Indeed, over the period of time TIE settled a number of claims with Infraco to do exactly that. However, in many other cases that was not the case. There were many sections of the tram route where MUDFA works were not required or had been completed and were therefore not holding up Infraco starting work on the site. Therefore, there was a sense of frustration that even where that was the case, even where there were no apparent impediments to the Infraco contractor mobilising and starting work, no action was being taken to begin work on the part of Infraco. For example, some months later, at the TPB board meeting on 19 November 2008, by that stage, under the contract the cumulative total of planned Infraco works on the route between the airport and Newhaven for Phase 1a of the project was to be 19.3 per cent of the total works planned. However the work actually completed as a cumulative actual total was only 0.7 per cent of the works planned. It did not seem credible to the TPB board that, given what I have said about MUDFA works not holding up all the work on the entire route, that progress of 0.7 per cent six months after mobilisation as opposed to 19.3 per cent represented in any way acceptable or reasonable progress.

182. I note the new format to the Risk Register at page 27 of the papers to the April 2008 TPB (document reference **CEC00114831**). This format sets out, in a series of columns, the individual risks with an identification number. It sets out the effect if these risks are to materialise. It sets out an estimated probability of their impact. It sets a timeframe during which the risks are expected to be exposed. I do not recall what changes had been made to the draft Close Report.

#### **TPB Papers for 7 May 2008 (CEC00079902)**

183. I am aware that the minutes for the April 2008 TPB meeting (document reference **CEC00079902**) state that 30 per cent of all works were complete. With regards to the rationale for splitting the MUDFA works from the Infraco works, I refer you to the comments I made earlier about the procurement strategy adopted by TIE, which learned from best practice and experience of light rail projects elsewhere in the UK, and from evaluation carried out by the National Audit Office. 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 the enabling works would be completed as far as possible before the actual construction work of the main project commenced. A high percentage of MUDFA remained outstanding at the award of Infraco. Page 12 of the papers for the May 2008 meeting (document reference **CEC00079902**) states that *"A total of 77 per cent of the planned diversions have been achieved to date."* I believe the discrepancy between that figure of 77 per cent and the figure of 30 per cent is attributable to the fact that the scope of MUDFA works increased over time, because the state of utilities discovered when they dug up the roads were worse than what had been expected from plans. The scope of the works was extended and revised, however I am not certain the extent of this and other people involved would be better placed to verify that. However, even with only partial completion of the MUDFA contract at the time of the Infraco contract signature, it remained the

case that a situation had been avoided whereby a single contractor was pricing in all risk for the entire scope of all the tram-related works, in a sense blind and without necessarily having the detailed expertise and experience in those sorts of works. Nobody on the TIE Board was at all satisfied with the speed of undertaking the MUDFA works. There was a lot of frustration around that. However, it was also the case that the reasons for those delays were at least as much to do with the state of the utilities underneath the roads when they were dug up as they were to do with the performance of the contractor, unlike for example with delays with the design contract, where the view was that it was fundamentally the performance of the contractor that was disappointing.

184. I cannot explain the increase of £17.8 million in the base cost for Infraco that Stewart McGarrity referred to in item 4.2 of the April 2008 TPB minutes (document reference **CEC00079902**). The part of the Close Report in question is page 50 of the papers for the April 2008 TPB (document reference **CEC00114831**). However, the papers for the meeting on 7 May 2008, at page 13, say that *"The AFC for Phase 1a of the project remains at £508 million, including a risk allowance of £32.3 million. Funding available remains at £545 million."* I do not recall the detailed discussion about concerns that the programme dates were based on the assumption that there would be recovery in the MUDFA programme, item 4.3 of the April 2008 TPB minutes (document reference **CEC00079902**). I do not recall the detailed discussion about the basis for thinking that there would be such a recovery. My view of the further slippage in the signing of Infraco contract, item 7.2 of the April 2008 TPB minutes was, as I have expressed before, and in common with the rest of the board, a combination of keenness to see progress made balanced with the imperative to sign the best possible contract and one which, as the contracting body, we and CEC were happy with. There was minimal additional cost to TIE in the slippage of the contract signature from April into May 2008, or indeed from earlier that year until May 2008. The additional costs incurred related to the staffing costs and the costs of advisers in engaging with the process of finalising contract signature. However, the delay did not necessarily mean an increase in the cost of the contract and indeed what was being reported to the

TPB board was that as time was going on TIE were being successful in negotiating a contract which lessened the risk, including the financial risk, to the public sector and the public purse. Therefore they were negotiating a contract that represented better value for money. That being the case, it made sense to ensure that a better-value contract was procured rather than one that left the public sector more exposed.

185. PUK stood for Partnerships UK, a UK-wide organisation sponsored by HM Treasury, which had experience and expertise in supporting public bodies to enter into contracts. I do not remember specifically why PUK were to cease attending TPB meetings, item 15.2 of the minutes of the April 2008 TPB meeting (document reference **CEC00079902**). Looking back on it now it would make sense to me that PUK no longer had an active role in respect of the Edinburgh Tram Project if the contract was nearing completion. PUK were not actively involved in negotiating the Infraco contract. Their advice was previously around the overall procurement and commercial strategy for the Tram Project, over a period of several years.
186. In my judgement the PD Report, included in the papers for the May 2008 TPB meeting at page 11 (document reference **CEC00079902**), did not cloud the issue of the transfer of design risk. My understanding of the issue of design risk transfer is that one of the key benefits which had been successfully negotiated as far back as December 2007 with the preferred bidder in the so-called Wiesbaden deal was that design risk should be novated into the Infraco contract, which had benefits for both contracting parties. There was a financial benefit in that it increased the cost which TIE would pay to the contracting party for the Infraco contract, but also a risk benefit to the public sector in reallocating the management of the risk to a party that was better placed and in a better position to manage the risk going forward than TIE would be.
187. The TPB was extremely concerned by the requests from BBS on 30 April 2008 for more money. The slides for the 7 May 2008 joint TIE and TPB meeting (document reference **CEC01282186**) make clear the view of the senior executive team. These are an important set of slides. Those slides say,

for example: *"A full set of legal documentation sent to BBS on 22 April as agreed. Meeting with BB&S on 24 April (senior representatives) confirmed all commercial matters concluded. Legal diligence proceeds. WG receives call from BB (Walker) on 30 April am requesting £12 million price increase. Emergency TPB held same day to discuss. Meeting of senior principals held 5 May being driven by BBS claim to have sought influence but no sign of impact. BB support for the price increase is sketchy, confused, and wholly unconvincing. All signs are that it is last-minute, unprofessional brinkmanship. BB claim their costs are £70 million wrong, have reworked internally to arrive at £12 million... BBS response disjointed and confused, coupled with further evidence of horse trading; injected new demand for sequential design process, rejected long ago. Ultimatum sent close of play 6 May - response received this morning, requesting pricing adjustment of £9 million and alignment of design process."* The response of the board was in line with those sentiments, that despite seven months of discussions and negotiations with the preferred bidder, despite the deal being firmed up in Wiesbaden in December 2007, despite the further negotiations in the discussions that had taken place during January and February and March and all of April 2008, yet again, at the eleventh hour there was an additional demand for increased money and the reasons being given for that by Bilfinger Berger seemed to be that they had got their sums wrong. They were not reasons of substance relating to the nature or scope of the works to be carried out. This did prompt a discussion around the Board table about whether this was a party with whom TIE should contract, given the nature of their behaviour. Indeed, the TPB did discuss what the alternative procurement options were at that point, and if we were to take the view that this behaviour was so concerning as to cast doubt over the suitability of this company to enter into the contract. The slides for that meeting recap that alternative procurement options available would be to reach a position whereby the Infracore consortium would be led by Siemens. Siemens were already a partner with Bilfinger Berger but in this scenario you would have a Siemens-led consortium with the Bilfinger Berger construction capability provided by another party. A second option might be to reintroduce the other bidder, who had not been appointed as the preferred bidder; I understand that this would have been possible and legally compliant

under procurement law. The third option was to undertake full re-procurement of the Infraco contract. These options were weighed up, with the costs and benefits discussed in the meeting, and on balance the Board agreed to proceed with the existing contracting party and to close the contract with the Bilfinger Berger Siemens Infraco partnership as part of the consortium with CAF. The slides for the 7 May 2008 meeting set out some more of the reasons and the discussion around that issue.

188. I was aware that MUDFA works were slipping further, page 12 (document reference **CEC00079902**). The effect of this was considered by the TPB. I do not recall why the Risk Register reverts to an old format, pages 16 and following, and the new format was discontinued. The slides for the joint TIE and TPB meeting (document reference **CEC01282186**) include two slides about MUDFA. The slides outline progress, including slippage, and they refer to a reinstatement initiative for Leith Walk, Constitution Street, and Shandwick Place, being very actively pursued. This was an initiative designed to reinstate back to normal appearance streets which had been dug up under the MUDFA initiative and had not yet been put back together again following the completion of the works. In the four and a half years that I spent as a TIE and TEL non-executive director, several meetings stand out as being critical moments in terms of board meetings in the journey of this project and that 7 May 2008 TPB meeting would be one of those meetings. Other important TIE meetings would include those held on 12 March 2008, 9 April 2008, 17 December 2008, 11 March 2009, 2 and 30 June 2010, and 11 May 2011. The 7 May 2008 meeting was one where, with hindsight, concerning behaviour from the contractor was evident; very concerning behaviour at a level that it is fair to say we had not experienced previously, which then became a pattern in the subsequent months and years. The TPB were facing some very significant issues at that meeting. I would also add that the TIE board meeting on 12 March 2008 was another critical meeting. That was the one where the TIE board were really confirming the extent to which this was a fixed price contract and what the different elements of that were. The TPB met on 7 May 2008, followed by a meeting with the TIE Board. Both boards met on that day and I attended both meetings. The discussion I have just referred to, because it was

about the essential issue of the contract signature, took place in the TPB with the TIE non-executives and council elected members participating in that, in line with arrangements which had been agreed to facilitate this process and avoid having the same discussion twice.

#### **TPB Papers for 4 June 2008 (CEC00080738)**

189. I am referred to the minutes of the May 2008 TPB meeting (document reference **CEC00080738**), which refer to a meeting of the TPB on 30 April 2008, following the BSC demand for more money. I do not know if this was minuted and I do not have a copy of any minutes of that meeting in my records.

#### **TPB Papers for 2 July 2008 (USB00000005)**

190. I did not attend the TPB meeting on 2 July 2008 and therefore cannot comment on the papers (document reference **USB00000005**). I do not recall the underlying reasons why David Mackay reported membership of the TPB was to be reduced in the June 2008 TPB meeting (minuted item 12.1, document reference **USB00000005**). The sentiment that Infracore progress was disappointing once the contract was signed was reported in the minutes of a TIE board meeting on 3 July 2008 (document reference **CEC01282131**), which I had seen. The minutes of that meeting say *"It was noted that Infracore mobilisation rate is still too slow, with delays on the package contractors. A meeting will be arranged with Infracore next week to address this issue."* So, although I was not present at that meeting, it was clear to me from discussions with TIE board members and with TIE employees how disappointing and frustrating it was that, effectively from day one, the contractor had not mobilised to schedule, even though nothing new had happened which could have explained that lack of mobilisation in the interim period. In other words, the contract was signed following seven months of BBS being the preferred bidder and having conducted their own due diligence. Mobilisation was due to begin within a number of days of that contract signature. That did not happen and there was no identifiable reason for the



non-mobilisation. The contract itself was not being cited as a reason not to mobilise. I referred earlier to the concerns that were arising around the TPB about why the contractor was not doing what they had agreed to do under the contract. No new information was coming to light at that point which might have given the contractor good reason to stand still. There was a concern at the TPB about the slippage in design in MUDFA and the effect it might have on Infraco, MUDFA was repeatedly discussed in TPB meetings.

191. I am referred to risk drawdowns, such as that mentioned in the papers for the TPB meeting, page 35 (document reference **USB00000005**). Whilst I was not in attendance at that TPB meeting my recollection is that risk drawdowns were put for agreement to TPB meetings and they were fully discussed. In effect, expenditure was agreed to and risk contingency was reduced in response to crystallising a risk such as slippage in the design in MUDFA.

#### **TPB Papers for 27 August 2008 (CEC01053601)**

192. I did not attend the TPB meeting on 27 August 2008 and therefore cannot comment on the papers (document reference **CEC01053601**). I am referred to the TPB July 2008 minutes (document reference **CEC01053601**), which note that Willie Gallagher recorded his concern on MUDFA progress and Infraco mobilisation and progress at item 2.1. The papers for the TPB meeting on 27 August 2008 show a reduction in the number of members for that meeting and I am sure the minutes could confirm that. My own records indicate that there was a TIE Board meeting on 13 August 2008 and I will recap on some of the key points that struck me from the papers and minutes (document reference **CEC01053601**) for that meeting. Papers for that meeting indicate that in terms of cost *"The AFC for Phase 1a of the project remains unchanged from the last period at £512m, including a revised risk allowance of £28.4m...Funding available remains at £545m."* In relation to Infraco, the papers refer to mobilisation delays. In the slides presented at that meeting, the top ranked risk in the top ten corporate risks is, *"Infraco mobilisation impacting programme"* and as I referred to previously, that remained the top risk throughout the life of the programme. Actions to manage

the risk noted in the slides are *"High level review meeting held with the consortium senior executive. Weekly review on and reporting and progress."* The action owner is noted as being Steven Bell. The minutes of the meeting on 13 August 2008 record the following *"The chairman advised the board that there were issues with Carillion, MUDFA and the Infraco mobilisation that he was concerned with...the chairman updated the board on a meeting he had held with senior directors of Carillion on our concerns over their productivity and performance level...on Infraco, package contractors had not yet been appointed but several companies were working under letters of intent."* The only comment I would add is that one of the trends that became apparent over this time is that not only were Bilfinger Berger employees themselves not visibly fully mobilised on the project but, critically, they were not appointing their subcontractors on a committed basis and instead, as the minutes here record, companies were working under letters of intent rather than fully procured subcontract as planned. This reinforced the concerns of the TIE Board about the emerging pattern of the Bilfinger Berger's behaviour which was being evidenced.

#### **TPB Papers for 24 September 2008 (CEC01053637)**

193. I did not attend this meeting on 24 September 2008 of the TPB and neither did the other non-executive directors, therefore I cannot comment. However, there was a TIE Board on 11 September 2008 which I did attend, and the salient points of that meeting, which I have noted, are that the executive summary paper (document reference **CEC01053601**), provided for that meeting states, *"Overall progress remains behind the master programme...the management of the recovery of design delays migration of any potential utility diversion conflicts...and Infraco slow mobilisation and unlocking of Infraco more effectively is being addressed across the project...the slow mobilisation of Infraco is continuing to impact planned progress."* And again, at that meeting, the top risk noted is, *"Infraco mobilisation impacting programme."*

**CEC01053601  
should be  
CEC01164912**

## TPB Papers for 22 October 2008 (CEC01210242)

194. Again, myself and the other non-executive directors and the elected members of the council, were not at the TPB meeting on 22 October 2008. However, there was a TIE Board meeting on 9 October 2008 which I did attend. The key points which I have noted for my records of that meeting are in the slides (document reference **CEC01115673**), presented to the TIE Board, the comment about Infraco progress is, "*Not enough progress yet but building*". In the papers, (document reference **CEC01207880**), for the TIE board meeting the following statements appear "*Overall progress remains behind the master programme. This is due primarily to design slippages... and slow mobilisation of Infraco.*" It notes that progress on design is "*The percentage of plan for phase 1a - prior approvals 78 per cent; technical approval 89 per cent; IFC 73 per cent.*" The comment I would make is that by 9 October 2008, less than six months after contract signature, although there are significant design delays, we have approvals ranging between 78 per cent and 89 per cent of the entire plan. In other words, the majority of design work was at stages of approval, and yet despite that the progress achieved by Infraco is very slow indeed.
195. My recollection is that one of the concerns that TIE had had about the MUDFA contract was that even though part of the delay was due to the extent of works being unexpectedly greater than had been planned in advance, because of the state of utilities beneath the road surface, the works were not being managed as robustly and energetically as TIE would have wished. In addition, the papers note that in respect of MUDFA progress "*Carillion has appointed a new project director as a result of time management intervention to address Carillion's poor performance.*" This reference to a new project director in Carillion relates to discussions that had been had between TIE management and Carillion to inject more energetic and effective management into the delivery of the MUDFA works. I would also note at this point that I believe that on 18 November 2008 David Mackay, the chairman of TEL, was recommended as the interim chair of TIE, to take over from Willie Gallagher at the end of November 2008.

## TPB Papers for 19 November 2008 (CEC01053731)

196. My records indicate that 19 November 2008 was an occasion when we ran the TPB back to back with the TIE Board and indeed the TEL Board and, therefore, I and the other non-executive directors and council elected members did attend the TPB as well as the TIE Board on that day. I was not present at the meeting of the TPB in October 2008 therefore I cannot comment on the minutes of that meeting.
197. I am referred to item 5.2 of the October 2008 TPB minutes (document reference **CEC01053731**). I did not attend this meeting and therefore cannot comment on why it was necessary to maintain bus access one way along Queen Street during the works; my recollection is that this issue was discussed at the subsequent TIE board meeting also on 19 November 2008. The discussion about the issue was that the initial contract, which had been signed with Bilfinger Berger Siemens provided for complete access to Princes Street by the contractor in order to undertake the works. In other words, there should be no traffic going up and down Princes Street at the same time as they were working on it. Since contract signature, however it had become clear that there was pressure, understandably, from various city centre stakeholders, including from the retail sector, to allow continued access via buses and taxis to Princes Street while the works continued. Therefore the option of continuing to allow single lane access to public transport during the works was discussed in the knowledge that it would be a change to the contract and that it would incur additional cost. Therefore, the debate around the Board table was around the relative costs and benefits of choosing such an option.
198. I am referred to the fact that even at this early stage it is clear that there is a lot of repetition of text from the previous PD Report. I do not recall if this was commented on or raised by the TPB. I have mentioned earlier that it was the case that TPB's papers often helpfully set out works that had been undertaken or analysis and description of progress which referred to a longer period than simply the previous month. So the repetition of text from one month to the

next could be a helpful thing to the board members in understanding the bigger picture and the trends for the works being carried out. I do not believe it is the case that repetition implied a lack of forethought or judgement about what should go into the board papers and certainly there was never an occasion where, in my recollection, board papers repeated previous material without including the current updates.

199. I note that an issue arose with the 28 day difference between programme version 26 and version 31 (pages 10 and 11, document reference **CEC01053731**). I am not in a position to comment on that detailed issue. There are others better placed who might recall this, such as Steven Bell and the senior executive team within TIE, also the other staff involved with both MUDFA and Infraco contracts.
200. As far as I can recall in relation to design there is a statement that good progress was being made (pages 11 and 29, document reference **CEC01053731**). I cannot recall in detail where the design standard was in relation to the programme current at that time. In general by this stage in the process, completion of designs was becoming a less pressing issue than it was earlier in the projects, as most of the design work had now been completed.
- 201.
1. In order to keep the adequacy of the risk allowance under review, risk was discussed at every board meeting (page 12, document reference **CEC01053731**), and that included keeping a close eye on the financial risk allowance at each stage in the process.
202. I am referred to page 154 (document reference **CEC01053731**), where the report states that the risk remains at £28.9 million. The slides presented to the TPB meeting on 19 November 2008 (document reference **CEC01053731**), which include reference to risk allowance state *"Carillion performance greatly improved and commercial agreement close to final resolution provided there is no agreement creep. CAF programme progressing well. Infraco programme and commercial negotiations proving very challenging. Princes Street*

*planning following 1 October setback proving complicated and potentially costly. Infraco progress: underlying concern that DSC have not adopted 'ownership' approach to the project with engagement and attitude to address: programme and problem solving; approach to change; acknowledgement of deficiencies; management of the design groups...Finance: overall costs remain at £512 million including £29 million risk allowance. Funding remains at £545 million. Part of risk allowance will crystallise to settle scope and programme issues with MUDFA but within the amounts provided at financial close.*" Again, Infraco mobilisation impacting programme remains as the top risk on the Risk Register and in the papers for the board meeting the following is cited *"The project continues to experience problems with slow mobilisation and in particular appointment of direct BSC resource and the final appointment of the main package contractors. TIE has agreed with BSC a process to create a recalibrated programme. The papers also note that at this point the cumulative planned total Infraco works under the contracts at this point, which is around seven months after contract signature, should have been 19.3 per cent whereas the cumulative actual total completed was 0.7 per cent."* I referred earlier to this slow rate of progress and I will not repeat that now. At this meeting my recollection is that the subject of the requests for increased funding from Infraco was again discussed. I referred previously to the comments that I made at the joint TIE and TPB board meeting on 19 November 2008, which were recorded at paragraph 3.17 of the minutes of that meeting (document reference **CEC00988024**), in which I made clear that it was important that TIE received £1 of value for every £1 spent and that it would not be acceptable for TIE to simply hand over extra public money in the hope that it will motivate the contractor to get down to work without very good reason.

203. I am referred to risk 1077, page 18 (document reference **CEC01053731**). I cannot explain it beyond what it says. The risk is that there is a lack of visibility of design changes made between November 2007 and May 2008. It states that the tram works price was based on design which may have been altered and it is unclear who authorised the design change. The treatment strategy for that risk is to establish a process which will act as a control mechanism for

design changes. I have no further knowledge beyond what it states on this Risk Register. The TPB did consider the lack of progress in design for MUDFA or Infraco. I have referred to that discussion earlier in respect of Infraco progress being at 0.7 per cent rather than 19.3 per cent, which it should have been under the terms of the contract. In respect of MUDFA, my notes indicate that in terms of the revised scope of MUDFA works for Phase 1a the cumulative total MUDFA works planned by this stage in the programme was 70.1 per cent and the cumulative actual progress delivered was 54 per cent against that revised scope. I do not recall if there was any discussion of what the lack of progress meant for the project.

#### **TPB Papers for 17 December 2008 (CEC00988024)**

204. The issue that arose in relation to the Princes Street blockade, item 3.18 and following (document reference **CEC00988024**) is the one I referred to earlier; discussing the works to be undertaken on Princes Street. The paper headed 'Princes Street Closure - Additional Contingency Measures' prepared by E Scott (document reference **CEC01056094**), was given to the TPB on 22 January 2009. TPB members took a full involvement because of the significance of this issue on a number of fronts; its significance financially, its significance in terms of the relationship with and the performance of the contractor; its significance in terms of the impact on the city; its impact on the retail sector. Therefore, the minutes of the TPB meeting on 17 December 2008 (document reference **CEC00988028**), record a lot of that discussion. For example *"KH asked for an explanation on the process taken to reach this outcome, in other words, the solution arrived at for the closure of Princes Street. Both KH and PS questioned whether a cost associated with the current Princes Street strategy would be covered within the £512 million budget and risk allowance. SB, SMG and DJM all agreed that the additional costs of the measures (having one lane available for a period of time, additional TM, contingency enabling works and breakdown vehicle), as well as the diversions at the moment not being complete, were an extra cost, as BSC had priced on having full access to Princes Street and the additional contingency had not specifically been allowed for in the budget or risk allowance."* In other words,

one consequence of continuing with this proposal was that the £512 million figure was likely to be exceeded and some of the risk allowance that existed between that figure and the £545 million figure would therefore be used up. I believe, for all those reasons, that the TPB members took a full involvement in this issue.

205. I am referred to papers for the TPB meeting on 17 December 2008 (document reference **CEC00988024**), and asked to comment on the absence of an announcement or recognition in the papers of an increase in budget such as was referred to in the previous period. I don't recall discussion of this specific point. The financial implications of the Princes Street issue were however fully discussed at the meeting in December 2008. I am aware that in the reasons for slow progress, availability of design and overrunning of MUDFA are both noted in the December papers. I cannot recall in detail what was done about these risks as they were crystallising. I would have expected the risks associated with the proposed way forward for Princes Street to be discussed at the December TPB meeting, and my recollection is, and my notes indicate, that these risks were discussed. I refer to the table in section 5, page 46, of the papers for the TPB meeting on 17 December 2008, (document reference **CEC00988024**). This table reports activity which has been taken to review individual risks. It also sets out who participated in each review of each risk.

#### **TPB Papers for 22 January 2009 (CEC00988028)**

206. Item 2.3 of the December 2008 TPB minutes (document reference **CEC00988028**) notes that I raised issues in connection with the governance structure. This relates to the question of streamlining the TEL and TIE governance arrangements, which I referred to previously, and which were then subsequently brought into effect. This discussion links to an issue which was dealt with by an internal audit review on Review of Governance Report Number 2008-01 (document reference **CEC01009902**). This was one of the many internal audit reviews commissioned by the Audit Committee, which I chaired. To infer, as the question put to me does, that the TPB could not discharge its functions fully would be an inaccurate reflection of what that



report concluded. For example, the draft Internal Audit Report on the Review of Governance (document reference **CEC01009902**) was discussed at a meeting of the TIE Audit Committee on 22 January 2009, and that report said *"The governance arrangements which were developed as part of the business case for the Edinburgh Tram Project appear to have been operating effectively. No control weaknesses were noted in relation to the current government structure, however there are opportunities [and it follows or rather it continues] to improve the current arrangements as the project moves from the construction phase through to commissioning and operations over the next couple of years."*

207. I am referred to the discussion noted at item 2.12 of the December 2008 minutes (document reference **CEC00988028**). I do not recall this specific discussion. I have commented previously on why the same text might appear each month in reports in relation to the lack of progress in various areas.

**Trams Project Board Papers for 11 February 2009 (CEC00988034)**

208. The February TPB meeting was another occasion, as was the January 2009 meeting, when the TIE Board ran back-to-back with the TPB in line with arrangements I discussed earlier and, therefore, I did attend this meeting. I am aware that in the minutes for the TPB meeting in January 2009, page 6, (document reference **CEC00988034**) there was a note that the party with power to regulate governance was CEC. This was accepted by the TPB. TIE and TEL were both companies wholly owned by CEC and it was a matter for CEC to decide what governance they wanted to have in place over the Trams Project throughout its duration.
209. I note the concern expressed with regards to conflict of interest on page 6 of the papers for the TPB meeting on 11 February 2009 (document reference **CEC00988034**). I am not sure what was done to resolve it, but I believe that this refers to the position which councillors were in, whereby they had to balance the responsibility of keeping the full council updated with progress on the Trams Project with the need to keep some commercially sensitive

information confidential, to which they were privy, in the interests of delivering the Trams Project as efficiently and effectively as possible.

210. I was involved in the internal audit on internal governance, item 2.11, (document reference **CEC00988034**). I was the chair of the TIE Board Audit Committee which had commissioned this review and which discussed the draft review report (document reference **CEC01009902**), earlier that same day, 22 January 2009, at the meeting of the Audit Committee. I updated the TPB on the Audit Committee discussion, as was my normal practice. With regards to findings, recommendations and improvements, I have referred earlier in my statement to the key conclusions of the Internal Audit Review (document reference **CEC01009902**). To expand on that, the review said *"There are opportunities to improve the current arrangements as the project moved from the construction phase through to commissioning the operation over the next couple of years...The creation of a single legal entity owned by CEC (encapsulating TIE, TEL and Lothian Buses) would help streamline governance arrangements."* The assignation of contracts arose in this context. The issue was that the contracts for the Tram Project had all been let by TIE as the contracting party. The question was whether, if governance changes were made under which TIE was no longer the contracting party, that would then require re-assignation of those contracts. The reason why that was a matter of substance rather than just process was that, particularly in the prevailing circumstances in which it was proving very difficult to create conditions in which the contractor would mobilise and progress the work to schedule, whether that could then introduce additional risks into that process. I and others would have been wary of anything which introduced yet a further risk into the process which could negatively impact on the delivery of the Tram Project.
211. At paragraph 2.19 of the papers for the TPB meeting on 11 February 2009, (document reference **CEC00988034**), I refer to a paper entitled 'Governance and Corporate Model Restructuring Options', prepared by Graeme Bissett (document reference **CEC01050506**). It is a paper to the TPB to be discussed

on 22 January 2009. That paper sets out the options examined and describes them as options A, B and C.

212. I was made aware that MUDFA was 65 per cent complete, page 8 of the papers for the TPB meeting on 11 February 2009 (document reference **CEC00988034**). In terms of the original programme, before Infraco contract signature, the intention would have been for all the MUDFA works to have been completed by this point. In terms of the revised programme, the papers for the TPB on 11 February 2009 indicate that the percentage of MUDFA works of the plan completed at that point was 72.2 per cent. The percentage of the total works completed at that point was 66.5 per cent, and the percentage planned to have been completed by this point was 92.1 per cent. I believe that we had the information available that we needed at that time about MUDFA progress. I certainly felt that I could ask for any information that I wanted from the executive team in order to satisfy myself about questions I had about the project.

213. I am referred to the PowerPoint for the TPB meeting, February 2009, when there was a note that stated there was a significant risk of a major dispute, page 40 (document reference **CEC00988036**). I do not have a copy of the PowerPoint slides for that meeting, however, as I mentioned earlier, I took manuscript notes from the meeting which recorded the contribution from Andrew Fitchie of DLA. DLA were the legal advisors to TIE. One of the themes in his report was *"contractual behaviour since 14 May 2008 of contract signature"* where he referred to *"a pattern of behaviour from contractor intended to block progress"*. The Minutes of the TIE board meeting on 19 February 2009 (document reference **CEC00438304**) record that *"The TIE Board was updated on the issues arising from a meeting with senior representatives of Infraco. The board expressed its extreme concern over the performance of the consortium and delivery against the contract, noting that the current behaviour of Infraco and the number of breaches of contract continued to frustrate TIE's ability to manage the contract and to act responsibly as client. The board directed that the principals of the Infraco consortium be requested to attend a meeting with the TIE executive team on*

19 February  
2009 should be  
11 February  
2009

*Tuesday, 17 February to discuss the above concerns, and to be given the opportunity at that meeting to set out a remediation plan for TIE's consideration. The board further directed that a letter from the chair to Dr Keysberg be issued prior to the meeting on 17 February to outline the board's position and TIE's requirements of the remediation plan. The letter to be copied to the principals of Siemens and CAF, stressing that all consortium members were required to attend. The board agreed that it was vital to convey to the consortium that each of the stakeholders was resolved and unanimous in their view of the seriousness of the current position. The board resolved to call an emergency meeting of the TIE Board on Thursday, 19 February at 9.00 am to discuss the outcome of the consortium meeting, the options paper and to decide on the next course of action."* So the major dispute referred to on page 40 was around the performance of the Infraco provider, contractor and including around Princes Street and its behaviour. My recollection is that approximately one week before the agreed revised works on Princes Street were due to begin, Bilfinger Berger announced that they would no longer be prepared to carry out those works, and that was one of the events that led to this discussion.

214. In the minutes of the TIE Board meeting on 19 February 2009 which I have just referred to (document reference **CEC00438555**), record that *"The chair outlined to the board the current position on Infraco. A comprehensive debate took place amongst the board as to the next course of action. The board directed DJM to formalise a confidential formal letter to the Infraco setting out in no uncertain terms the board's position. It was emphasised that the message should endorse the unanimous view of TIE/CEC and the awareness of TS and ministers."* I chaired a meeting of the TIE Audit Committee on 11 March 2009. That was a relatively short meeting where we approved external audit arrangements and updated the internal audit schedule. The main item for discussion at the Audit Committee was the risks around Infraco and, given the seriousness of the situation that had emerged in relation to lack of progress in delivering the contract, I took the view and agreed with the chair of TIE, that that discussion should be had at the main TPB board meeting on 11 March 2009, rather than in the Audit Committee. I wanted to ensure that all

Board members had the opportunity to participate in that discussion, rather than just the subset who were involved in the Audit Committee.

**TPB Papers for 11 March 2009 (CEC00573427)**

215. I understood the position in relation to Princes Street to be the non-delivery of the planned and agreed works by the Infracore contractor. A paper was submitted to the 11 March 2009 TPB meeting, dealing with the Dispute Resolution Procedure (document reference **CEC01001220**). The paper said *"Despite lengthy and intensive efforts to conclude a range of issues with BSC through direct discussions, frequent problem solving sessions, facilitated partnership workshops and several escalation meetings with the most senior UK-based staff from Bilfinger and Siemens, it has proved impossible to progress works in an acceptable manner with BSC over the last three months. In addition, a meeting of principals from TIE, Bilfinger Berger, Germany and Siemens, Germany on 17 February resulted in a highly unsatisfactory reiteration of Bilfinger demands without any substantiation or written justification. Progress on estimates for change and practical delivery of core works has stagnated, culminating in a refusal by BSC to accept that they were contractually obliged to progress the Princes Street Works from 21 February, when the Princes Street closure was instigated. They had offered to commence works at Princes Street but 'at no risk' to themselves. It is considered essential to generate a significant change in behaviour by BSC to enable effective execution of the works. The cost impact of this stagnation is increasing with every day of delay."* The paper continues *"It is intolerable to TIE to accept further refusal by BSC to progress legitimate works. Therefore, further to the Strategic Options paper developed last week, TIE is currently preparing a range of issues for use in a series of 'surgical' applications of the Dispute Resolution Procedure (DRP) (Option B as identified in the paper). This is the formal contract mechanism for the resolution of disputes. This approach allows time to focus on the most important areas which are either of the largest contractual/commercial significance, or have a material delay of programme effect, or both. TIE is preparing a shortlist of particular items with the support of DLA to increase the intensity of issue resolution with BSC."* The

TPB had before it a paper on Infraco Options Analysis (document reference **CEC01050506**). Options set out in that paper included Option A, to terminate BSC and procure a replacement Infraco; Option B, to facilitate the removal of BB and replacement with a new civils partner; Option C, facilitate the removal of BB and management of civil subcontract directly by TIE; Option D, negotiate a major variation to the Infraco contract to settle all outstanding contractual disputes. I had noted that Option D was essentially what Bilfinger Berger had been asking for. They had been tabling a £50 million to £80 million claimed loss that they wanted settled. Finally Option E, which was the recommended option, to pursue the settlement of all significant contractual disputes through the Dispute Resolution Process under the Infraco contract. The paper also set out options to reduce the scope of the project to mitigate the impact of any potential cost overrun, in the context of limited funding available. Slides for the meeting refer to *"negotiating a settlement of termination of BSC, not an attractive option"*. This sets the context for the March Board discussion and, again, the reason why I had asked that the discussion around Infraco risk be had at the full TIE Board, rather than only the Audit Committee. My recollection is that the March meeting agreed to proceed with Option E, which was the recommended option, to pursue the settlement of all significant contractual disputes through the Dispute Resolution Procedure under the contract.

216. The slides and presentation made available to the TPB with the attached papers stimulated our very full discussion of the dispute, and I have referred in my earlier comments to the nature of those discussions. I have referred to the paper on the Dispute Resolution Procedure (document reference **CEC01001220**) in my comments which was submitted to the meeting. At the time my recollection is that I participated fully in the TPB's discussion about the use of the DRP but I cannot recall the detail of that. I was content with the quality of the analysis presented in the paper and with the discussion at the board meeting. Alternatives considered at the March TPB meeting included continuing without the use of the Dispute Resolution Procedure, and I cannot recall whether they were specifically discussed in this meeting. Around this time the use of mediation was also discussed and a mediation was held a few

weeks later, between the end of June 2009 and the end of the first week of July 2009. The desired outcome of the DRP was that clarity would be achieved on the disputes, leading to the programme of works being undertaken by the contractor. In terms of contingency plans, the paper that I referred to on Infracore Options Analysis included a number of other options, which I referred to earlier. The view was that the DRP route was the right route to progress at that time in order to give the current contractor every opportunity to work and to deliver the project. So, although other options were available they were not, at this point, actively being taken forward. The role of the TPB in obtaining the resolution of the Princes Street dispute was to reach an agreement about the best way to amicably resolve the dispute.

217. The issue of whether to offer a supplementary agreement was certainly discussed by the TPB and the TIE Board. I cannot recall whether it was discussed at the March meeting. A supplementary agreement held the potential advantage of being able to reach a new agreement with the contractor about the terms under which it would undertake and complete the works on Princes Street, terms which it was satisfied with in a way which apparently they were not satisfied with the main contract. The potential disadvantages of reaching a supplementary agreement included the possibility that that a supplementary agreement would involve less advantageous terms to TIE and, therefore, the public purse and might include other elements which did not synchronise well with the main contract. There was a discussion of the basis of payment under any such agreement and the effect that it would have on costs, however, I do not recall the extent of that discussion at this meeting. I am aware that there are papers for a TPB meeting on 11 March 2009 and it is apparent from the papers for the April meeting that there was also a TPB on 24 March. I do not know if papers were issued for it.

#### **TPB Papers for 15 April 2009 (CEC00888781)**

218. I am referred to item 1.1 in the minutes of the TPB meeting on 11 March 2009. It is noted that David Mackay was going to meet John Swinney MSP and

Stewart Stevenson MSP on 17 March 2009. David Mackay would be best placed to recall the purpose and outcome of that meeting.

219. I do not recall what use was made of PwC for advice on commercial issues during the DRP. This was something which the Executive Team were involved with and the non-executive directors were not involved directly.
220. I am aware that the TPB agreed to the Princes Street change, which would lead to an increase in project costs, item 10.3 in the minutes of the March TPB meeting (document reference **CEC00888781**). The change is summarised in the slides presented at the joint TPB and TIE meeting in April (document reference **CEC00971385**) which say "*Work has commenced on Princes Street under a supplemental agreement (SA) which provides an equitable and constructive way forward to facilitate the consortium working flexibly but encountering impediments or obstructions and is consistent with obligations under the Infraco contract.*" The TPB then discussed the need for a supplemental agreement and my earlier comments refer to the extent of discussions around how to handle the Princes Street issue. I do not recall how much of the financial information was discussed at this meeting and if the Board was told how much a change would cost. A project management panel was established at this point. This was referred to in the slides for this meeting which say "*Our project management panel (PMP) has been established as the forum for a more constructive engagement between TIE and BSC which is a key element of the commercial strategy.*" The slides continue that the approach is "*First and foremost work constructively with BSC*". The slides note that critical success factors include "*Respected and productive relationships at senior TIE/CEC/BSC level. Knowing when middle ground is best value for money, empowered decision-making by BSC team vital; constructive engagement around the PMP process and its relationship to current and future DRP action.*"
221. I would reiterate a point I made earlier, which is around the overall strategy adopted by TIE and TEL in getting the Tram Project delivered. I had said initially that the approach taken during the first year to eighteen months post



contract signature was to adopt a partnering approach and this development here with the PMP is one example of that. Even at this point in the process, despite the problems that had arisen around Princes Street and the general lack of mobilisation and progress everywhere else on the tram route, the strategy was to seek to build a constructive relationship with the contractor, which would facilitate better and full engagement with the project to deliver it in line with the contract. That strategy did change at the end of 2009, following repeated failure to mobilise and continued obstruction by Bilfinger Berger, but I would just note that even at this point in the process, that was still the preferred approach. It contradicts some of what was said publicly about the Tram Project, which was that there was a lack of willingness to develop constructive relationships between the contracting parties. That absolutely was not the case from TIE's point of view, from the point of contract signature until well into 2009.

222. I am referred to item 1.4 in the TPB minutes for 24 March 2009 (document reference **CEC00888781**) which states Steven Bell stressed that the Supplemental Agreement for Princes Street would not increase liability to TIE, compared to that previously, and that there would be no material difference in the way costs would have been agreed. I am not in a position to say whether that was a correct analysis. My understanding is that the Supplemental Agreement for Princes Street did result, and was always known that it would result, in increased cost of the project over and above the £512 million estimated cost at that time and use up some of the contingency budget.
223. I am referring to item 1.8 in the TPB minutes for 24 March 2009 (document reference **CEC00888781**) where it is noted that the PSSA would allow work to be completed in the first week of November, as originally anticipated. *"However, there would be no guarantee that this will be the case if there is a compensation event (the same basis as the original contract)".* I cannot provide further information about the benefits of the PSSA or whether the TPB understood how the PSSA was to work.

224. I am referred to item 1.11 in the TPB minutes for 24 March 2009 (document reference **CEC00888781**) which states that Stewart McGarrity outlined the available headroom in the funding envelope and to item 1.12 which states that Stewart McGarrity essentially said that this headroom only exists as long as there are no further disruptions or delays. Given what had been happening with the project with the Princes Street dispute and its current situation with extra payments to contractors, the TPB were at this point concerned about the budgetary impact. There was discussion of the financial position not only around the TPB and the TIE Board tables but also bilaterally between TIE and CEC, who were aware of the financial position as it evolved. It was clear that TS's funding was capped at £500 million and therefore any increase in cost beyond the £545 million funding envelope would fall to CEC to fund if other sources of funding were not available such as private sector investment which had been considered previously in relation to Line 1b.

#### **TPB Papers for 6 May 2009 (CEC00633071)**

225. I am referred to papers for the TPB meeting on 6 May 2009. I was not present at this meeting and cannot comment on the matters discussed at that time. The only thing I would add is that the papers for that meeting (document reference **CEC00633071**) which I have read, note the progress on the Princes Street works and they say *"Disappointingly progress has continued to be slow or lacking at other locations where work could be ongoing, including the Carrick Knowe Bridge and the Haymarket Viaduct. BSC have still not entered into formal contracts with any of their subcontractors and this appears to TIE to be one reason for slow progress at a number of locations."* Cumulative total planned progress on the Infraco contract should have been 45.4 per cent at this point, whereas cumulative actual progress was only 3 per cent in total. By contrast in relation to the contract with CAF to build the trams *"Good progress continues to be made with progress of deliverables against schedule. The production line has commenced during quarter 1 2009 with delivery of the first tram still on schedule for April 2010."* It is important to note, certainly in my experience of the project, that the contract with the tram manufacturer, CAF, operated very well, that TIE were happy with the quality of

the work done and with the timescales met for tram delivery. In practice, the high quality of the tram vehicles has been delivered as specified.

#### **TPB Papers for 3 June 2009 (CEC01021587)**

226. I note that in terms of the Infraco contract, where the contractor was of the view that circumstances were such that there was a deemed change to the contract requirements, they were entitled to serve an Infraco Notice of TIE Change (INTC). This might entitle them to additional payment under the contract or additional time in which to complete the works. With regards to the number of INTCs that had been served on TIE by the contractors by the end of June 2009, the only information I have available in respect of this is set out on slide 9 of the slides presented to the 3 June joint TPB and TIE board meeting (document reference **CEC01007729**). That indicates that the position at the end of period 1 was that the number of INTCs received from BSC was 341 and at the end of period 2 was 370. I do not know, in detail, what had given rise to them. From my recollection, the joint TPB and TIE board meeting on 3 June was given a report: *"The project continues to experience problems with slow progress for Infraco and in particular the appointment of direct BSC resource and the final appointment of the main package contractors. All BSC subcontractors continue to operate with limited letters of intent whilst awaiting conclusion of the full subcontracts and whereas cumulative progress planned at this point was 49.2 per cent, cumulative actual progress was 4 per cent."* The TIE Board considered, as it always did, the Risk Register. The Risk Register top risk at that point was on 3 June cited as *"Failure to agree revised programme and budget with BSC leading to contractual dispute unknown or future areas of dispute unknown or future changes."*

#### **TPB Papers for 8 July 2009 (CEC00983221)**

227. I am referring to the minutes for the TPB meeting in June 2009, page 7 (document reference **CEC00983221**). It states that there was discussion at the TPB of strategic options. These are the options which I referred to earlier

in the paper on Governance and corporate model restructuring options, presented to the TPB meeting on 22 January 2009 (document reference **CEC01050506**), whose author was Graeme Bissett.

228. I am aware that on page 19 of the reports to TS in early July 2009 the Time Schedule Report in the 4 week Period Reporting Pack 09/10 indicates that many matters have slipped but that recovery can be achieved (document reference **CEC00838683**). This same table and statement appear in other monthly reports, although the degree of slippage increases. My view at the time was that this represented an accurate statement of facts as they were at the time. Recovery could have been effected if the behaviours of the contractor changed. This was not a case of a contractor being fully mobilised and nevertheless slow progress being achieved. The fundamental reason why progress was slipping under the Infraco contract was because the Infraco contractor had not fully mobilised. The progress that was being delivered was commensurate with the very limited amount of resource being deployed by the contractor. To achieve progression a change of behaviour could have resulted in improved performance and at least some recovery in the programme plan. The general issue of progress of the Infraco contract was discussed at probably every meeting of the TPB that I attended.
229. I recall that there was a TIE Board meeting and TPB meeting on 8 July 2009. The slides for the joint TPB and TIE board meeting (document reference **CEC00783725**) note that a mediation process was held between TIE and the Bilfinger Siemens Consortium. The mediation ran from 30 June 2009 to 6 July 2009. The slides report no progress on key issues. The key issues being a commitment to progress, a price for issues to date, a request for between £80 million and £100 million by Bilfinger Berger as additional payments, and the key issue about certainty about the future. The slides from the 8 July meeting (document reference **CEC00783725**) indicate the next steps with the BSC consortium were, "*Back to broader commercial options examined in March*", which means that the broader commercial options available were to reduce the scope of the BSC works, ending the BSC contract and other options. This TPB and TIE board meeting noted that the MUDFA works at that point were

79 per cent complete and the papers for that meeting notes that *"The project continues to experience problems with slow progress for Infracore works and in particular the appointment of direct BSC resource and the final appointment of the main package contractors. All BSC subcontractors continue to operate with limited letters of intent whilst awaiting conclusion of the full subcontracts. Cumulative progress planned at this point was 52.1 per cent, cumulative actual progress at this point was 5 per cent."* I have referred previously to this issue about not appointing subcontractors fully. It seemed to TIE, and it seemed to the board of TIE, an unusual way for a main contractor to go about delivering a project it was supposed to be committed to over a multi-year period. To not actually appoint its main sub-contractors on a firm committed basis, but instead to have them operating on limited letters of intent, did not seem to be an indication of commitment to delivery of the project.

#### **TPB Papers for 29 July 2009 (CEC00843272)**

230. I was invited to, but did not attend, the TPB meeting on 29 July 2009. There was also a meeting of the TIE Board on 29 July 2009. The TIE Board followed a meeting of the TPB, in line with arrangements that were operating at that time of sometimes doing this. I am aware that in the Minutes of the early July TPB meeting there is a note that Richard Jeffrey outlines options for the consideration of the Board, item 3.6 (document reference **CEC00843272**). I had been briefed in advance on these options at previous meetings which gave me adequate opportunity to consider matters. These options had been considered in a previous form at the March 2009 meeting and were the subject of the paper, which I referred to earlier. Essentially, the decision was taken to use DRP and other contractual mechanisms, as it was to provide every opportunity for the project to be delivered under the current contracts, of which the DRP was an element. The view of the TIE board was that, irrespective of whether DRP decisions went for or against the position that TIE was taking, they would nevertheless help to clarify definitively for all the parties involved the deliverability of the project under the contract. TIE was in receipt of legal advice throughout this process, including deciding which

issues to take into the dispute resolution process. I also believe that TIE consulted Counsel on these matters over the course of 2009 and 2010.

231. I am referred to item 3.2 of the Minutes of the early July TPB meeting (document reference **CEC00843272**) which state that the Farrans contract was for a sum less than budgeted for with Carillion. I do not know if this budget reflected the Carillion price. I do not know if the Farrans contract remained within the tendered price. I am not best placed to answer, but the executive staff who were involved with this would have that information.
232. I note that on 29 July 2009 the design slippage issue was presented as being one of the changes from BDDI to IFC, on page 44 of the TPB meeting papers (document reference **CEC00843272**). I do not recall if this was the only source of change or if there was a requirement to change designs in order to get approval or other reasons.
233. I am referred to the Sensitivity Analysis of ETN Risk QRA, page 78 of the TPB papers for the 29 July 2009 meeting (document reference **CEC00843272**). Generally speaking, a sensitivity analysis like this exposes the extent to which an issue is sensitive to various different factors and that is indeed what this analysis does. The analysis shows, for example, that the issue most sensitive was *'Delay to completion of project'*. The second most sensitive factor was cited as *"Tramway runs through area of previously unidentified contamination/hazardous materials and material required to be removed and replaced (dig and dump)"*. You would need to ask those who conducted that analysis, and that would be the executive staff within TIE rather than the non-executive directors, why the delay to completion accorded a greater weighting than the impact of the BDDI to IFC design changes. I am not in a position to comment further on this graph or why it was repeated.
234. I am aware that, month by month, the slippage on the Infracore works increased. For example in May 2009, the works were 42.4 per cent behind, as in the TPB papers for the 6 May 2009 meeting (document reference **CEC00633071**), and at the start of July 2009 they are 47.1 per cent behind,

page 30 of the TPB papers for the 8 July 2009 meeting (document reference **CEC00983221**), whereas by late July 2009, they are 49.3 per cent behind (document reference **CEC00843272**). I have already cited the rates of progress and slow progress evidenced under the Infraco contract that were reported to the TPB and TIE board. On 8 July 2009 the report to the TPB and TIE Board (document reference **CEC00983221**) said that whereas cumulative progress plan was 52.1 per cent by this date, cumulative actual progress by this date was only 5 per cent. This is one year and two months after contract signature. In my view, at the time and since, and in the view of the TPB, the fundamental underlying reasons for this very slow rate of progress do not relate to any one event or obstruction to this work taking place. So, for example, slower than hoped for utilities diversion works do not provide sufficient reason to explain why only 5 per cent of the Infraco works could have been undertaken 14 months after contract signature, given that some parts of the tram route were not dependent on utility works having been done in the first place, particularly those off-street. Neither does the poor performance of the design contract fully explain, or excuse, the slow rate of progress, given that a substantial proportion of the design was available when it was needed. In addition, the main Infraco contractor was in a position from May 2008 to directly manage that risk, since the design contract had been novated to them for that very purpose with their agreement and in return for additional funding. I believe that the fundamental reasons for this exceedingly slow rate of progress relate to behavioural factors on the part of the contractor which were evidenced throughout this process and beginning before contract signature. As I have indicated earlier, it seemed to me at the time that the common theme arising time after time, including in the days before contract signature and in the period since, was that the infrastructure contractor, in particular Bilfinger Berger, simply wanted significantly more money to be paid to them than the amount which they had agreed to in signing the contract and were prepared to frustrate progress on the project in order to apply pressure on the project funders to increase their payments. These sums of money were tens of millions of pounds in excess of the sum agreed at contract signature and indeed up to £100 million was cited at some point in time. In other words, the contractor would mobilise if only TIE agreed to hand over an additional

£100 million and in that circumstance the implication was that the other problems would be overcome. That position was simply unacceptable to TIE and, as a non-executive director of the company, I fully shared that view. This was public money being spent and public money cannot simply be handed over without it achieving full value. As chair of the Audit Committee I was in a position to seek an independent view of the underlying reasons for the slow rate of progress. I was able to do that through commissioning work from Deloitte, a global consulting firm whom we had procured as our internal auditors. As I referred to earlier, Deloitte undertook a significant internal audit review of project and programme reporting and Infracore as part of its 2008/2009 internal audit programme. The resulting Deloitte report dated September 2009 (document reference **CEC00347250**), was numbered 2008-03/05. The report took a similar view of what was going on to that which I have just outlined. Amongst other things, the report of Deloitte's refers to the fact that *"Despite the best efforts of TIE, it appears that BSC is applying a commercially aggressive stance on this project."* The report makes recommendations about how TIE should respond to that, including the fact that although *"During the early stages of the dispute TIE continued to adopt a partnering ethos in attempts to reach agreement with BSC...It appears that TIE management has responded in an appropriate manner to the dispute when the gravity of the dispute became apparent...If BSC continues to adopt an aggressive commercial stance it will be incumbent on TIE senior management to ensure they have put in place a robust action plan to defend their position."* Indeed that is what happened over the following weeks. As I have mentioned earlier, at a later point I resigned from the TIE board, in May 2011, and was therefore not privy to the arrangements put in place under which the contract was ultimately partially completed. Nevertheless, it does seem to me that, from information in the public domain, at the end of the day Infracore was paid substantially increased funding, almost double the original contracted sum, in the region of £230 million over and above the equivalent sum which they had signed up to undertake the contract for initially in 2008. It was only at that point that they completed work to a certain point in the tram route and, with the benefit of hindsight now, that endorses my view that the underlying issue operating throughout the life of this contractor's engagement



with the contract was a desire simply to frustrate the execution of the contract in order to elicit very significant additional payment. Over a period of many months the senior executive staff in TIE were reporting to the TIE Board on their interactions with senior executives from the contractor. Some of those discussions were in relation to specific issues, for example, the Princes Street dispute which I mentioned earlier. Other discussions were in relation to unblocking progress more generally across the scope of the whole contract. What was reported to the Board consistently was that the contractor fundamentally wanted significantly more money over and above the sums it had committed to under the terms of the contract. That is what led me to reach the view that I have just expressed. As a non-executive director I was not directly involved in those discussions. Neither, to my knowledge, were the other three non-executive directors, nor were the elected members of CEC. I do believe that the chair of TIE was involved in some of those discussions, as was the chief executive and the finance director and the project director, and they would be able to provide more specific detail about what was said. My view is formed on what I was told in the TIE board meetings.

235. I believe that BSC did carry out works to on-street sections. I do not know to what extent those were carried out under the original contract or under terms that were varied, for example, as a result of agreements reached under the dispute resolution procedure. From memory, I believe the Audit Scotland Report from 2011 (document reference **ADS00046**) does refer to a proportion of the on-street and off-street works that had been completed at the point at which Audit Scotland published their report in February 2011. They noted that in total only 28 per cent of the scope of works had been delivered. Out of that 28 per cent, the majority of that was off-street and the minority proportion was on-street.

**TPB Papers for 26 August 2009 (CEC00739552)**

236. I am referred to matters in connection with the TPB meeting on 29 July 2009. I was not present at this meeting and therefore cannot comment on the matters discussed.

237. I note that in the reasons for delay given in the PD Report for the August 2009 TPB meeting, page 13, (document reference **CEC00739552**) there is still reference to BSC failing to submit preparatory paperwork. I cannot recall what the subject of this paperwork was, so am not able to comment upon it. There are others far better placed to comment on that with more detail than I am, such as the TIE executives.
238. I am aware that the figure for completed MUDFA works, on page 14 of the papers for the August 2009 TPB meeting (document reference **CEC00739552**), shows a big jump for the figure given to TS in the previous month. I do not recall why there was an increase or the precise dates of the increase for completed MUDFA works but one of the factors that helped to resolve the MUDFA works quickly was that Farrans were contracted to undertake and complete much of the outstanding MUDFA works. My recollection is that it was reported to the TPB that Farrans mobilised quickly and undertook the works and that might explain the quick progress in completing MUDFA works. For example, my notes from the TIE Board and the TPB papers dated 8 July 2009 (document reference **CEC00983221**), indicate that MUDFA works were 79 per cent complete, whereas only one month later the report to the TPB on 29 August (document reference **CEC00739552**), indicates that MUDFA works were 96.6 per cent complete. Part of the reason for that would be the good performance of the new subcontractor brought into play. There might also be a reporting lag in the previous figures, but I do not know that and again you would be better off asking those who were more closely involved with that, the TIE executives.
239. I am referred to a note in the costs section of the PD Report, papers to the TPB meeting on 26 August 2009 (document reference **CEC00739552**), which states that TIE may not have "*sufficient contractual leverage to instruct commencement*" of works. I do not know what the problem was. I suspect that the comment refers to results emerging from the DRP process but I cannot be certain. My understanding of what emerged from the DRP process overall was that, over the range of issues referred to the dispute, both the TIE view of matters and the contractor's view of matters was upheld at different points in

different adjudications. Neither party's interpretation of the contract was fully endorsed. It became apparent that there was more scope in the main contract for the contractor to take actions which had the result of not getting the works done than TIE would have wished if the contractor was so minded. I do not know what was missing from the contracts, if indeed anything was missing. As I have said earlier, my understanding is that there was nothing in the contract that prevented the contractor from undertaking the works. The issue was whether the contractor wished to undertake the works under the contract and under the terms which they had signed up to, including the financial terms they had signed up to.

240. I am referred to the TS Report for August 2009, page 23, document reference **(CEC00847371)**, where there are references to "*Temporary and permanent works re-design*": I did not have any involvement with this matter and I am not able to give a view on this issue.
241. I do not recall if there was any discussion at the TPB on the issue of "*betterment*" in relation to recovery of the costs of the MUDFA works from statutory utility companies, or what was being done in relation to recovering a proportion of the costs.
242. I am referred to a statement in the minutes for the TPB meeting on 29 July 2009 (document reference **CEC00739552**) that Steven Bell was to prepare a summary statement for the August meeting of the outstanding areas where betterment would arise. I was not present at this meeting and cannot comment on the matters discussed at that time.
243. I note that in the PD Report for the 26 August 2009 TPB meeting (document reference **CEC00739552**) a statement is made in writing that it is unlikely that the project can be completed for £545 million and that it was not possible to predict accurately a revised budget outturn. At the meeting of the TIE Board and TPB on 3 June 2009 the following statement appeared in the presentation slides used (document reference **WED00000141**): "*We continue to report against an as yet unapproved outturn estimate for phase 1a of £527.1 million*

which include the risk allowance of £35.7 million for Infraco and is based upon the re-baselined opening date of February 2012. After allowing for the costs of phase 1b postponement of £6.2 million, there is headroom of £11.7 million against the total approved funding of £545 million." In the papers for the 26 August 2009 TPB meeting (document reference **CEC00739552**), the following statement appears on page 19 *"The table above reflects the base costs and risks aligned to the TIE re-baselined programme (12 February) and realignment of the Infraco milestone schedule. The AFC for phase 1a above includes an unapproved increase of £15.1 million to the project risk allowance. The approved estimate for delivery of phase 1a of the project remains at £512 million. The phasing of the £527.1 million plan remains in line with period 3 and will be updated in period 6 by TIE and following that when there is an updated agreed programme with the Infraco contractor. The latest forecast view includes £3.2 million of costs relating to phase 1b which crystallised as contractually payable to BSC due to the postponement of phase 1b (this will require to be covered by current funding). Coupled with the re-base-lined forecast there is £11.7 million of funding headroom within the £545 million funding total available."* This report quoted does not match a statement in the August 2009 TPB meeting papers (page 13, document reference **CEC00739552**) that *"it is now considered unlikely that the full scope of Phase 1a will be completed within the available funding envelope of £545 m."* The slides presented to the TPB meeting on 26 August 2009 (slide 16, document reference **CEC00753157**) reinforced the view contained in the June papers, specifically the slide under "costs and funding" that says *"Transport Scotland Report continues to report outturn of £527 million for Phase 1a but highlights uncertainties in the same manner as the Council report of 20 August. We continue to report a forecast outturn for the current year as £150.1 million for Phase 1a plus £3.2 million for Phase 1b. Transport Scotland Report highlights a possible underspend of as much as £30 million [I think that means in the current year] based on our best judgement ..."* These slides do not seem to me to indicate that £545 million is unlikely to be sufficient. The statement in the PD Report for the August 2009 TPB meeting (document reference **CEC00739552**) does contradict the other statements I have referred to, including the position outlined in the slides. My recollection is that this was the

first time this had been reported to the TPB, although the potential cost implications of the on-going disputes and what it might take to resolve those disputes had very much been in the minds of the TPB board throughout the entire process. It was not the case that this would be the first time that financial implications of the project were discussed in terms of the £545 million budget envelope. I do not recall specifically what had happened since the previous month to justify the statement being made at this stage, other than the continued failure to see the Infracore contractor mobilise fully to any acceptable level.

244. With regard to the effect of not having an AFC, my recollection is that TIE was taking every opportunity possible to apply financial control to the situation in line with its responsibilities agreed with CEC, and that all the partners were aware of the steps being taken including use of the dispute resolution process. In addition, financial commitments were not being made without budget being available to fund them, and indeed that is endorsed by the fact that two years later, at the point at which I left the TIE board in May 2011, only just over £400 million had been actually spent of the £545 million total budget envelope, and there was clarity about what that expenditure had been incurred for. So not being able to predict with confidence a final cost, because of the on-going dispute, did not represent a lack or diminution of financial control. The estimates of costs which could be provided and the actual costs submitted to TPB and TS each month are two separate categories of cost. It was absolutely essential that the TPB and TS had the best available cost information at every point in the process, including distinguishing between actual and estimated costs. For example, in relation to works already carried out, the reference in the Project Director's report in August 2009 (document reference **CEC00739552**) refers to the commercial uncertainties and the continued delays. These uncertainties and delays had a bearing on the extent to which it was possible to predict with confidence the future costs of the project to see it fully delivered, given that we did not have a process in place which was delivering an acceptable rate of progress with the project. I do not think it is accurate to say that there was no longer any estimate at all of final costs. There was a range of costs, at one end of which were the additional

sums being asked for by the contractor. So the question became, what was the best strategic approach to take in the circumstances, given that there was no certainty, or indeed likelihood at that time, that additional budget beyond the £545 million would be available, and that question was then the matter of significant discussion between all the relevant parties, including CEC, over the following months. Options, such as truncating the route short of Newhaven therefore became options that were looked at, rather than persisting with the original scope of the project which was going to be unaffordable within the available budget. I am not best placed to comment on the effect for the stakeholders and in particular CEC of there being no AFC, except to say that CEC had a very direct financial exposure to this project and they were understandably very keen to quantify the extent of that exposure.

**TPB Papers for 23 September 2009 (CEC00848256)**

245. I recall that in relation to progress, page 6 of the August TPB minutes (document reference **CEC00848256**) record that "*SB reported that progress remains slower than desirable for the Infraco works, largely due to on-going contractual matters* " *SB stands for Steven Bell*. My view of performance at this time was that this was very disappointing and it represented the continuation of the trajectory of Infraco progress since contract signature. Even two months later at the 18 November 2009 meeting, cumulative actual progress on the Infraco contract was reported as 10.8 per cent ,as opposed to the cumulative planned progress at that point of 66.3 per cent.
246. I note that page 6 of the August TPB minutes (document reference **CEC00848256**) records that works on Shandwick Tram-stop have not yet started due to on-going discussions with BSC regarding treatment of on-street sections. I do not recall the specific disputes that were holding up works at Shandwick place at this time. I do not recall whether I knew what the position taken by the contractors in relation to this section of works was.

247. I am referred to matters in connection with the TPB meeting on 23 September 2009. I was not present at this meeting and cannot comment on the matters discussed at that time.

**TPB Papers for 21 October 2009 (CEC00842029)**

248. I am referred to matters in connection with the TPB meeting on 21 October 2009. I was not present at this meeting and cannot comment on the matters discussed at that time.

**TPB Papers for 18 November 2009 (CEC00681328)**

249. I am referred to the minutes for the TPB meeting on 21 October 2009 (document reference **CEC00681328**). I was not present at this meeting and cannot comment on the matters discussed at that time. I was, however, at the meeting on 18 November at which there was both a TIE Board meeting and a TPB.

250. I am referred to the table on page 40 of the progress report in papers for the November TPB meeting (document reference **CEC00681328**) in which it is suggested that all the figures showing the cumulative fall behind schedule (the right-hand column) are inaccurate. The same as for the table in the December report (**CEC00416111**), page 52; the January report (**CEC00473005**), page 53; the February report (**CEC00474418**), page 33, and the March report (**TIE00894384**), page 34. I do not recall whether this was commented upon at the time.

251. The minutes of the TPB meeting on 18 November 2009 (document reference **CEC00416111**) record that Richard Jeffrey provided the Board with a report on the outcome of the decisions from the Carrick Knowe and Gogarburn adjudications. My recollection is that this was an oral report, but I cannot be certain. The Minutes of 18 November 2009 meeting record the following "*KH [myself] asked if TIE's interpretation of the contract has changed through the evolution of this process, and queried whether a review of the strategic*

*direction of the DRP is necessary. The board discussed at length a number of matters including interpretation of the contract both from a legal and technical perspective, as well as the strategic direction of further submissions to the formal process. It was reiterated that it is too early in the process for either party to establish precedence at this stage in the process, and it was agreed that the current strategic direction should continue.*" I do not recall in detail how the outcomes of the adjudications were presented to the TPB by the executive members, but certainly they updated the TPB and TIE boards throughout this period on the outcomes of the DRP adjudications. My understanding of the decisions and the effects that it might have in relationships with BSC in future was that it had a bearing on the respective parties' understanding of the contract. I recall that in these papers for several months afterwards there is a note that the decisions are under review. I do not recall what decisions were under review, who was conducting the review, what considerations were applied and to what extent was the TPB involved in the issue of that review. I cannot provide any further comment. In relation to these disputes, I also do not recall if there was a discussion as to what approach TIE intended to take on the issue of whether certain matters constituted changes under the contract.

252. I am aware that by the time of the November 2009 report to TS, (document reference **CEC00681328**), £11.7 million of funding headroom is available within the £545 million total available, and that the Infracore works are only 10.8 per cent complete. Page 52 of the board papers say that the anticipated final cost is £533 million, which was £12 million less than the budget envelope of £545 million. To repeat a distinction I made earlier, there is a difference between anticipated final costs and money actually spent. In other words, even if the anticipated final cost was to exceed £545 million, it was never the case that anything like that much money was actually spent on the project during my time of involvement with it, and indeed as time went by and more and more of the elements were completed, for example the construction and payment for the trams themselves, then the scope of the remaining works to completion narrowed and the risk narrowed. I am not in a position to comment



on what proportion of the drawdown on the risk allowance was attributable to the BDDI-IFC issue.

253. I recall that there was a TIE Board meeting and a TPB meeting on 16 December 2009. The key points I noted from the slides for that meeting, (document reference **CEC00376427**) were that the Infracore contract at that point was overall 12.5 per cent complete as opposed to the 69.3 per cent that was being planned to be completed at that time; that the MUDFA works were 97 per cent complete. In respect of MUDFA, the Carillion contract had then been closed down and the scope of that contract had transferred to a new firm, Clancy Docwra, who had been engaged to complete the remaining works. There was a validity meeting in April 2010, for which I have no record of attending.

#### **TPB Papers on 14 April 2010 (CEC00420346)**

254. I am referred to matters in connection with the TPB meeting on 14 April 2010. I was not present at this meeting and cannot comment on the matters discussed at that time.

#### **TPB Papers on 5 May 2010 (CEC00245907)**

255. I am referred to the minutes for the TPB meeting on 14 April 2010 (document reference **CEC00245907**). I was not present at this meeting and cannot comment on the matters discussed at that time.

256. I am now aware that page 35 of the May report to TS, (document reference **CEC00245907**), notes that although 82.6 per cent of Infracore works should have been done, only 16.1 per cent had been completed. Despite this on page 51 of the report, against milestones, it still says that recovery is possible. I do not recall why this was said and if there was discussion about it.

257. I am referred to pages 18 and 19 of the May PD Report, which states that works cannot be started on-street where sites are available, as BSC have

failed to satisfy their contractual obligations (document reference **CEC00245907**). I do not know which obligations this refers to. I am not able to comment further.

258. I am referred to page 31 of the May report to TS, (document reference **CEC00245907**). I do not know what the problems referred to within this report were. This is a level of detail that I was not familiar with as a non-executive director and others would be better placed to answer who were more closely involved with the operational detail. I have no further knowledge in this area and do not recall if it was discussed at TPB meetings.

#### **TPB Papers for 30 June 2010 (CEC00223543)**

259. At the TPB meeting on 30 June 2010 I updated the board on the minutes following an Audit Committee meeting held earlier that morning. There was not any change in approach either from or to BSC, with the exception of the establishment of the Project Pitchfork work streams at about this time in view of the decisions of the adjudicators in the disputes. Those two work streams both involved discussions with BSC. These were relatively recent developments around this time, but it was in-line with the second broader strategy that I mentioned previously, which was to ensure robust enforcement and delivery of the existing contract. It didn't represent a change in strategic approach.
260. I am aware that on page 7 of the minutes of the meeting on 2 June 2010, (document reference CEC00223543) it notes that an independent expert review of the programme had been conducted and that it had concluded that delivery of Phase 1a could be achievable by December 2012. I do not recall if this report was provided to me and I do not have a copy of that report in the papers I have retained. In respect of the meeting on 2 June, significant new issues were discussed for the first time, at least in my presence at a Board meeting. The Minutes of the 2 June meeting record the following *"RJ updated the board on the current position regarding the options available in dealing with the contractual matters with BSC. Two options are being worked on.*

*BSC are involved in discussions in regard to both approaches and these were discussed in some detail with the board... There are a series of meetings set up with senior BSC representatives during June and the indications are that Siemens and CAF are much more positively engaged in the process than Bilfinger Berger as has been noted by the board over many months... The key points arising from comments raised by the board were: the requirement for certainty on cost and programming going forward; and the absolute necessity to have an agreed way of working in order to complete the scope of works against a backdrop of progress on the ground; general concerns were raised regarding the behaviour of Bilfinger Berger in negotiations on the project to date; it is recognised that all three members of the consortium are jointly and severally liable in regard to the contractual obligations."* The draft copy of slides for the 2 June 2010 meeting (document reference CEC00313733) which were presented, referring to Project Pitchfork, had two work streams. Work stream A is referred to as Project Notice and work stream B is referred to as Project Carlisle "Where BSC complete part of the project and TIE re procure the remainder on an incremental basis." I mention that because these two projects were the beginnings of the work that led ultimately to the events of 2011 and the mediated agreement reached at Mar Hall.

261. At page 6 of the 2 June 2010 (document reference **CEC00223543**) which state that Richard Jeffrey outlines the current position regarding the options available in relation to BSC and that two options were being worked on, which are the two options I have just referred to, Project Notice and Project Carlisle. They are explained more fully in the slide presentations given to the 2 June 2010 TPB meeting, (document reference **CEC00313733**), and the 30 June 2010 TPB meeting (document reference **CEC00422001**). Project Notice concerned the termination of the current contract, whereas Project Carlisle related to a scenario whereby the current consortium completed part of the project and TIE then re-procured the remainder of the project on an incremental basis. These minutes also note on page 8 that a contract was to be awarded for utility works in Baltic Street. I do not recall why new contracts for these works were being awarded at this stage. The papers for the 2 June 2010 TPB meeting include the letter from David Mackay to Marshall Poulton

explaining that the contract could not be completed within the funding envelope of £545 million. Having tried different approaches, under two broad strategies, Project Notice and Project Carlisle, which had not been effective in creating the conditions whereby the contractor carried out the works, tipped the balance of judgement such that it became the right time to send that letter. I do not recall whether Marshall Poulton was specifically involved in the decision taken to instruct the sending of the letter. However, there was continual discussion with CEC officials and elected Council members over the months leading up to this point about the financial position.

262. I am referred to page 24 in the PD Report for TPB meeting on 30 June 2010 (document reference **CEC00223543**) where it notes that there were two independent reports to the effect that recovery of the programme was possible. I do not recall having received those reports and I do not recall what the conclusions of those reports were.
263. I am aware that on page 12 in the PD Report for 30 June 2010 TPB, (document reference **CEC00223543**) it notes a new twin track approach to Infracore. The old approach, in summary, was seeking to enforce the application of the current contract through the use of the dispute resolution procedure to clarify provisions where they were contested between the parties. This new approach crystallised efforts around two work streams in agreement with the current consortium, neither of which were premised on a scenario whereby the original full scope of the main contract works would be carried out. The old approach was stopped at that point because it was not working and nothing that had been tried to enable it to work had been successful. The advantages of the new approach recognised the reality of the cumulative position that we had reached and reduced the scope of works that would be completed under the current contract. The work stream that involved continued delivery by the current consortium for a reduced scope tram route would cost less and also reduce the project delivery risks. The following paragraphs in the report referred to the outcome of the adjudication decisions. I believe they did accurately represent the position and indeed they were also reflected in the Audit Scotland Report published in 2011 (document reference **ADS00046**). I

do not recall discussion about what could be said of these decisions in report to TS or others.

264. I am aware that page 14 of the PD Report for 30 June 2010 TPB (document reference **CEC00223543**) states that Counsellor Gordon Mackenzie had called for the termination of BB's contract. This is the same Gordon Mackenzie who sat on the TPB and I believe he did attend future TPB meetings. I do not recall anything further on the statement.
265. I am aware that on page 26 of the papers for 30 June 2010 TPB (document reference **CEC00223543**) it sets out what the causes are of problems in the Infraco works. It is suggested to me that conflicting causes appear to be put forward, however I am not clear why the causes are thought to be conflicting. I understood the position to be that the project was experiencing the continuation of the contractor not mobilising to deliver the works under the contract. It is not apparent to me why the reasons conflict. There is a statement that says in the document *"Overall the relationship with BSC is suffering in the following key areas; firstly, the refusal of BSC to progress works whilst clause 80 changes are being agreed. Secondly, work unable to start on the street where sites are available and accessible as BSC contractual obligations are not satisfied. Thirdly, resolution of the contractual interpretation on BBDI-IFC (pricing assumption 1, development and completion of design) and, fourthly, refusal by BSC to progress works under TIE instruction in relation to clauses 80/34/22/65."* Those reasons do not seem to me to conflict with each other. What follows beneath that paragraph is a second list which says *"Progression remains behind the master programme primarily due to ..."* Then it lists another nine reasons. The first is a list of reasons why the relationship with BSC is suffering, and the second is a list of reasons why progress remains behind the master programme. Those are two different lists about two different things and I do not understand them to be conflicting. I understood the position to be a continuation of non-delivery of the contract. The information I was provided at this meeting was what was contained in the papers for the board and also in the slides presented to that board meeting.

266. Another significant event that took place at the 30 June 2010 TPB meeting, which is recorded in the Minutes for that meeting, (document reference **CEC00244400**), is that the Board authorised the issue of a remedial termination notice to BSC. The Minutes note that this does not mean cancellation of the project; rather it advises the company of breach of contract. That was a significant point in the process.
267. The Audit Committee also met on 30 June 2010 and considered an internal audit report by Deloitte – Report 2010-05 on Commercial Strategy. This meeting also considered an internal audit report on financial controls. These reports informed my judgement on whether TIE was following the right strategy in light of all the circumstances prevailing at that time.

**TPB Papers for 28 July 2010 (CEC00244400)**

268. The new twin track approach is discussed in a little more detail on page 7, minutes of the 30 June 2010 TPB meeting (document reference **(CEC00244400)**). My recollection is that issuing of the remedial termination notice would not necessarily result in the termination of the contract. Given the advice the TPB was receiving, it was a logical step in the circumstances and it would have been a necessary step in the process, depending on the option finally decided upon. I referred to those two options previously, Project Notice and Project Carlisle. I am not in a position to speculate what would have been done if the contract was terminated at that time. The issue of service of remedial termination notices was discussed significantly at the meeting, and in particular the necessity of providing the contractor with fair notice of TIE's view that the contractor was in breach of contract and of providing an opportunity for the contractor to remedy those breaches. This step would also have been an essential step in the process to have gone through if in due course the contract was terminated. There were two approaches being discussed in parallel. One involved termination of the contract. The other involved completion by the existing consortium of a reduced, truncated scope of works on the tram route. If we are referring to that as the second approach, Project Carlisle, then that was the nature of the discussions. Project Carlisle,

as it is stated in the minutes, was the option whereby the current consortium would complete part of the project and TIE would re-procure the remainder on an incremental basis. I was not involved in those discussions myself and neither, to my knowledge, were the other non-executive directors. I am not able to speculate on what the circumstances would have been at that point if Option A failed to produce a change and the agreement necessary for Option B was not forthcoming. Those were the two options being pursued at that time.

269. Item 2.2. of page 7 of the minutes of the 28 July TPB meeting (document reference **CEC00013703**) notes that advice had been taken on the merits of the Remedial Termination Notice (RTN) approach. This advice was the advice of senior counsel. A paper submitted to the TPB meeting on 28 July (document reference **CEC00244400**) notes *"Consultation with senior QC on 8 July... The conclusion being that there were several areas in which BSC were evidenced to be in breach of the Infraco contract. If BSC did not remediate these breaches according to the contract, TIE have a strong case for issuing remedial termination notices in accordance with the contract which could ultimately lead to termination."* This is also referred to in slides presented at the 28 July 2010 meeting, (document reference **CEC00417585**). It was felt to be important that if the company were in breach of the contract, it was important that they be given opportunity to remediate those breaches. Part of the intention to issue that notice was, therefore, to clarify what the nature of those breaches were and to provide every opportunity for the company to remediate those breaches within a reasonable timescale. In relation to the option B Project Carlisle, I was not involved with negotiations and cannot comment further.
270. The 28 July 2010 TPB minutes note that board members were to be kept informed of each step of progress though the coming week and beyond: I do not recall by what means they were kept informed. I do not have any email correspondence relating to this.

271. I am referred to page 47 of the TS Report for July 2010 (document reference **CEC00244400**), where it states that this appears to be the first time that it is recognised that programme recovery is not possible. I do not recall this and I cannot speculate on this point.
272. I recall that there was a TEL Board meeting and a TPB meeting on 25 August 2010. I would note that the minutes for those meetings (document reference **CEC00013818**) record that *"RJ noted that against the background of work streams A and B, it was unlikely that TIE would launch further matters into DRP at this time"*.

#### **TPB Papers for 22 September 2010 (CEC00013818)**

273. I am aware that on page 7 in the 25 August 2010 minutes (document reference **CEC00013818**), the title of Workstream A is changed from 'Termination' to 'Contract Administration'. I do not know what the significance of this is but I note that the terminology change is not reflected in the slides presented at the same meeting, so perhaps it is of no significance. At Item 2.4 of the minutes and in the SPD Report, page 15, there is a note that no further DRP referrals would be made. This is the issue which I just referred to earlier. I do not recall this in detail, but my recollection is that the use of the DRP had been in line with the previous approach being taken to essentially get the project built under the current contract. We were now into different territory, whereby it was no longer felt by any of the parties that the current contract was going to be the route by which this was going to be resolved. Therefore, it did not seem sensible to continue using a mechanism which was relevant to the previous approach, as opposed to the current approach. It is not my recollection that this was because there was acceptance of the decision in Carrick Knowe and Gogarburn, which had gone against TIE. My recollection is that the decision that no further DRP referrals would be made was a recommendation made by the executive team and endorsed by the TPB.
274. Contractual Strategy is set out in the PD report of the papers for the TPB meeting on 22 September 2010, which is that the first strategic approach to



the project determined by the Board was very much a partnership approach, designed to build trust and confidence in the project on the part of the contractor and to develop the relationship between TIE and the contractor. As I have explained before, after a period of 18 months and more of that approach and it not being successful, TIE adopted the more contractually assertive approach, which was referred to in these two paragraphs. The second of the two paragraphs explains that from period five of the financial year the execution of that contractually assertive approach has included the issuing of several contract notices, including six remedial termination notices and two underperformance warning notices. I note at this point the assessment of overall progress towards completion of the whole project in its entirety was deemed to be at 70 per cent. The detailed breakdown given to the board of that figure was as follows: that the tram vehicles were 59 per cent delivered, utilities were 97 per cent delivered, the infrastructure construction off-street was 35 per cent delivered, including work at the depot and on track, that the Tram Project ancillary works were 80 per cent complete. This is relevant to the statements earlier about the amount of money remaining within the £545 million budget. In other words, taken as a whole, the analysis was suggesting that around 70 per cent of all the works required to create the Tram Project had been delivered at this point in September 2010. My recollection is that was in line with the amount of money spent on the project. At the point at which I left the company, some six months later, about £400 million had been spent with a further £15 million owed of the £545 million total. So it seems to me that broadly speaking the two figures are in sync. There was no suggestion of a lack of financial control within the project and indeed that was repeatedly endorsed by the internal audit reviews of financial control.

#### **TPB Papers for 21 October 2010 (CEC00014055)**

275. I am referred to the PD Report for the TPB meeting on 21 October 2010 (document reference **CEC00014055**), which notes that BB were intending to ramp down their workforce. I am not able to comment on the motivation of Bilfinger Berger. I do not recall what justification BB gave or what the reaction was within TIE to this news. The slides presented at the meeting on 21

October 2010 (document reference **00190765**) do give an indication of Bilfinger Berger's engagement with the on-going discussions about the future of the project. Under Project Carlisle, this was the option in which Bilfinger Berger Siemens would complete part of the project. The slides say "24/09 - TIE final offer sent to BSC; 1/10 BSC implemented action to demobilise subcontractors at a number of sites they claim affected by change; 11/10 - meeting held, heard alternative options for 'mature divorce' proposed by BB and Siemens; 14/10 letter received from BSC - seems to indicate that BSC did not wish to continue negotiations on Carlisle; 19/10 - response sent from TIE asking each Infracore member to clarify its position." The slides presented to the subsequent TPB on 17 November 2010 (document reference **CEC00191912**) indicate that no response was received to that letter from TIE to each Infracore member.

276. I am aware that the TS Report for October (document reference **CEC00014055**) notes on page 32 what has been done by way of referring items to the formal dispute resolution agreement process – in total 11 referred by TIE and 9 by the Infracore contractor. It also notes on page 33 that TIE has continued with the contractually assertive approach to management of the contract. "From Period 7 this has taken the cumulative issue of Contract Notices to: 10 Remedial Termination Notices (RTNs) and 2 Underperformance Warning Notices (UWNs) – a 3<sup>rd</sup> UWN was issued in early Period 8. Rectification plans have been received for 3 RTNs due from 5. All 3 have been rejected by TIE as they do not address the defaults identified with satisfactory proposals." As previously described, after a period of 18 months and more of a partnership approach between TIE and the contractor and it not being successful, TIE adopted the more contractually assertive approach. This was done with a view to giving the contractor fair notice of the company's view that they were in breach of contract, and giving them reasonable opportunity to rectify matters. This was also one in a series of necessary steps to keep the option of termination open, even though in itself it did not automatically mean that would be inevitable. Indeed my impression of the Board's view throughout this process was that if at any point the contractor

had picked up their tools and got on with the job and delivered the project to the contract that they had signed up for, we would have been delighted.

277. My understanding when the October TS Report (document reference **CEC00014055**), refers to a "*financial metric*", page 31, is that when it says "*The total project completion as a financial metric estimated at circa 70 per cent*", it means that the estimated financial value of the works as a proportion of the total which had been completed to date was around 70 per cent.

#### **TPB Papers for 17 November 2010 (CEC00014175)**

278. The practical effect of the resignation of David Mackay on the workings of the TPB was that Brian Cox chaired the meetings of the TPB as the designated senior non-executive director of the company TEL and also of TIE. I do not have a detailed recollection of where the discussions had got to in Project Carlisle. The slides presented to the 17 November 2010 TPB state that in relation to Project Pitchfork, part of which was Project Carlisle, "*Consultations with senior counsel undertaken on 4 November and 15 November with a further series planned.*" At this, as at every other meeting, the non-executive directors were getting direct feedback from TIE officers on their recent discussions with BSC. I do not recall the details of the specific discussion and I have not made any notes of that.

#### **TPB Papers for 15 December 2010 (TIE00896978)**

279. I recall that the November TPB minutes (document reference **TIE00896978**) state the possibility of mediation. I do not know who first suggested the use of mediation at this point. This was not the first time that TIE had used mediation. It had been used previously in the middle of 2009 and had not made significant process. At this point in 2010, my recollection is that the board's openness to entering into another mediation process, despite the failure of the previous one, was part of the board's willingness to exhaust all other options before any possibility of reaching the end of the road and

possible termination of the contract. I do not know what was said by the Scottish Ministers or TS in relation to this.

280. I am referred to page 16 of the papers for the 15 December TPB 2010 meeting (document reference **TIE00896978**) where there is discussion of the outcome of the adjudication on Landfill Tax. I do not recall being provided with copies of the decisions in this and the other adjudications of the detail of this discussion.

**TPB Papers for 12 January 2011 (TIE00897052)**

281. With regards to the 15 December 2010 TPB minutes (document reference **TIE00897052**), mediation was again considered by the TPB and they wanted it progressed as soon as possible. This was the preferred option as I have explained previously. I do not view this approach as being a change of heart in relation to the other remedies that had been pursued since about April 2010. Mediation had been tried before and TIE had always been keen to explore every possible option in order to get the work done under the contract. I have noted from the minutes of the 12 January 2011 TPB meeting (document reference **TIE00897058**) the following statement *"RJ reminded the board of the recommendations from the previous TPB to: commence mediation as soon as possible; scope to cover completion of the route from the airport to St Andrew's Square; to be a fast-track commercial process; performance criteria to be bound into delivery of mediated outcomes; TIE to develop the mediation strategy with CEC legal and finance directors. RJ confirmed that a mediator has been booked and that internal planning sessions have commenced, including detailed input from CEC. The board noted that DA will participate as part of the mediation team as CEC representative. The potential outcomes of the mediation process were discussed at length by the board, and it was agreed that certainty around price and delivery will be key requirements around any mediated settlement, acknowledging that some residual risks and contingency around these are likely to exist. Achieving best value for the public purse is a key consideration*

*throughout this whole process.*" I did not attend the January 2011 meeting of the TPB and therefore I cannot comment about the discussion at that meeting.

**TPB Papers for 9 February 2011 (TIE00897058)**

282. On 3 February 2011, Vic Emery was appointed chair of TIE and TEL, replacing David Mackay and, therefore, he chaired the 3 February 2011 TPB meeting. At that point Vic Emery was also appointed to the board of directors of TIE and TEL.
283. I am aware that on page 23 in the paper on Project Change Control submitted to the February 2011 TPB meeting (document reference **TIE00897058**) there is a reference to a *"write back of budget of £13 million"*. I do not know what the *"write back budget"* was and how it operated. The only point I would like to add in relation to previous meetings was that it was significant in the TPB meeting of 9 February 2011 the slides (document reference **WED00000142**), presented to that meeting provided an update on the dispute resolution process. The slides stated the following *"As at 8/02/11 30 items in DRP - 20 referred by TIE, 10 by BSC. Seven resolved by negotiations and two resolved through mediation. 11 decisions made by adjudication. The value of changes agreed £32.927 million versus the original estimate from BSC of £45.306 million -- 89 per cent reduction."*

**TPB Papers for 13 April 2011 (TIE00897066)**

284. I was not present at the TPB meeting on 13 April 2011 and therefore cannot comment on matters discussed at this meeting. The only thing of note is that in the minute it records that, and this is following the Mar Hall mediation *"It was acknowledged that the mediation is not yet concluded and that those involved in the process are bound by a confidentiality undertaking. As a result, VE [that is Vic Emery] was not able to provide the board with a comprehensive update at this time. He was able to report, however, that a number of works teams are underway to support this process, noting in particular that significant progress has been made on closing out outstanding*

*consents and approvals, and that the decision to co-locate CEC team at Edinburgh Park has been a key factor in this."*

**TPB Minutes for 11 May 2011 (TIE00896987)**

285. The final meeting that I attended of the TPB was on 11 May 2011. My concerns in relation to the mediation agreements which I expressed in the May 2011 TPB meeting are stated on page 3 of the Minutes (document reference **TIE00896987**). Earlier in this statement I set out the concerns I had about the lack of involvement of executive and TEL non-executive directors in approving not only binding variations to the contract, namely Minute of Variation 4 and the Heads of Terms for the Minute of Variation 5, but also the actual payment of monies totalling £27 million which had taken place on 4 and 5 of May 2011, which had happened without our knowledge or consent. I have explained what my concerns were in more detail earlier. These actions were out of line with the existing corporate governance arrangements at that time and also breached the operating agreement between TIE and CEC and with TEL. It was properly a matter for CEC to decide what governance arrangements they wanted to put in place, but new arrangements had not been put in place at that time and therefore the existing arrangements should have been used. I explained this in my letter of resignation to Sue Bruce, the Chief Executive of CEC, on 12 May 2011. Whilst supporting the proposal that revised corporate governance arrangements now be put in place, I was also concerned, and this concern was shared by the other non-executive directors, by any suggestion that we had endorsed or exercised our judgement in relation to the outcomes of the mediation process, which were given effect in Minute of Variation 4 and Minute of Variation 5. We had not been given an opportunity to look at any of that. I was mindful of the fact that I had been sent information indicating that the TIE executives also had concerns about the extent to which the sums of money now being proposed to be paid and sums which had already been paid to the consortium were in fact justified.

## Achieving Objectives

286. I cannot make fully informed judgements on what happened with the Tram Project after I ceased my involvement with the Tram Project.
287. The cost estimates used in the preparation of the business cases were produced by those involved at that time. That work happened largely before my involvement with the Tram Project. The preparation of the Final Business Case happened concurrent with the first year of my appointment as a non-executive director of TIE. The people involved in producing those estimates were TIE employees and CEC employees and also Lothian Buses employees. I do not know who else was involved with that and I have no further information, beyond what is already published in the business cases, and I was not involved in that process directly. The Final Business Case was discussed at the TIE Board and I have referred to that earlier. The first copy of the business case I was given was the Final Business Case, version 1, dated 3 October 2007, which was made available to the TIE Board meeting on 15 October 2007.
288. Optimism Bias was included in the business case in line with the guidance set out in the HM Treasury Green Book and the Scottish Public Finance Manual appropriate to the state application of the project at that stage. I have referred to Optimism Bias and the specific sums earlier.
289. Quantified Risk Assessment refers to the sum included in the overall project cost estimates which was provision made for risks materialising during the course of the project. I am not sure if the QRA has another more technical meaning, and if it does, I do not know what that is and I am not able to comment further on that.
290. I have referred previously to how risk was managed. In summary, risk was considered at every TIE Board and TPB meeting that I attended. It was actively managed between board meetings by the executive staff involved, in line with the risk management processes extant at that time and in line with

the ranked Risk Registers around which the various corporate governance mechanisms structured their discussions. The provision for risk worked by having a sum of money available which could be drawn upon if risks were to materialise. That was its purpose, and the function of the drawdowns against the risk allowance were to approve the allocation of funding against specific items, where risks had indeed materialised. I was not involved directly in making all the decisions whether to approve a drawdown, but my recollection is that a variety of factors were taken into account, including value for money and the reasons why these drawdowns were absolutely necessary to the delivery of the Tram Project.

## **Conclusion**

291. This has been my first interaction with the Inquiry. In terms of future direction of the Inquiry, I believe that the terms of reference are helpful. I believe it is very important that the Inquiry is able to talk with people involved and to distinguish between the different experiences that participants had. For example, I was one of four non-executive directors. It would be important that the Inquiry talks to all four non-executive directors. It would be important that the Inquiry talks to the non-executive chairs of TIE, David Mackay and latterly Vic Emery, and also previously the executive chair of TIE who was Willie Gallagher. It would be important that the Inquiry is able to talk to the senior executives involved in this process, including Richard Jeffrey who was the chief executive who began part way through the process, and also the executive directors, including Stewart McGarrity, who was the finance director for most of this period, as well as Steven Bell who was the main project director and the main engineering director throughout most of this period. I believe that Graeme Bissett would add value to the Inquiry, given his role in the corporate governance arrangements pertaining to TIE and given his wider corporate governance experience. Those people could give further guidance on who else within the executive teams could offer evidence of particular value to the Inquiry.



292. At the end of the day, the fundamental aim of the Inquiry is to establish why the Tram Project incurred delay, cost beyond what was budgeted, and why it delivered less than originally projected. In doing so, I believe it is important to cut through a lot of the complexity around the project to the fundamentals. In giving a statement, I have tried to focus on my understanding of what those fundamentals were and why what happened did happen, and I have done that from the perspective of a non-executive director who was not involved with the project every day, day in and day out, but rather had a role in setting overall strategy, applying independent judgement to the process, bringing challenge and bringing to bear the wider experience which each of us did in that process.
293. Looked at as a whole over my four and a half years' experience as a non-executive director and my previous experience within the Scottish Executive, my reflections are that this was a project with a sound business case, with a positive benefit cost ratio which was procured in line with a strategy that was best practice. It was a project in which problems arose in several of the contracts, but not all of them. In particular, the company building the trams performed very well. The main problems, as I saw them, pertained to the fact that an Infraco contract was signed in May 2008, following a seven month period during which the contractor had been preferred bidder. The companies which comprised the consortium which was appointed as preferred bidder had every opportunity to exercise due diligence over the contract they were about to sign. Bilfinger Berger therefore understood entirely what they were getting into in return for how much money, and understood the contract to which they had had an opportunity to negotiate amendments during the preferred bidder period. And yet having signed the contract Bilfinger Berger then did not mobilise in accordance with the agreed schedule. It was never the case that initial progress was adequate or sufficient and then problems arose later which slowed or halted progress. The contractor did not mobilise on schedule to carry out the works from day one. I have provided information about the single digit percentages of progress that were made over a number of months and years as against planned progress of 50-plus per cent over that same time period. I believe the fundamental question for the Inquiry is why that

happened. Why did that contractor not deliver the contract it had signed up to, or even mobilise on schedule, despite having all the advantages I have just described? I believe the conclusions which the Inquiry reaches will be of benefit to other projects, if they ever find themselves in similar circumstances.

I confirm that the facts to which I attest in this witness statement, consisting of this and the preceding 129 pages are within my direct knowledge and are true. Where they are based on information provided to me by others, I confirm that they are true to the best of my knowledge, information and belief.

Witness signature.....



Date of signing..... 6/2/2017 .....