

OUR REF C2174.55/DJA
YOUR REF
1 November 2010

Nicholas Dennys Esq
Atkin Chambers
1 Atkin Building
Gray's Inn
London
WC1R 5AT

Dear Mr Dennys

**City of Edinburgh Council ("CEC")
Edinburgh Tram Project**

We have recently been instructed on behalf of the City of Edinburgh Council in relation to the Edinburgh Tram Project.

We set out the background and the specific questions upon which we would wish your Opinion in the sections below. In summary, CEC anticipate being asked to consent to the termination of the consortium of companies undertaking the Tram Project. In order to assist their analysis in relation to that decision, they wish to obtain independent legal advice in relation to (i) whether termination can properly be undertaken in terms of the Contract; and (ii) the reasonableness of the decision being taken.

At the outset we would highlight that the Contract is governed by Scots law and we appreciate that you are not qualified within this jurisdiction. CEC intend to address this by seeking a supporting Opinion from Senior Counsel in Scotland, James Wolffe QC, who will be asked to identify whether there are any pertinent points of Scots law which arise from your analysis. Therefore, for the purposes of your Opinion please proceed upon the assumption that the law in Scotland is identical to the law of England in relation to the points raised by us for your Opinion.

In terms of timescales, the matter of termination is likely to be dealt with at a full meeting of the Council on 16 December 2010. Therefore, CEC would wish to have your Opinion in final form by no later than 2 December 2010 to allow this to form part of the briefing pack being issued to Councillors in advance of the full meeting of the Council. It is anticipated that we will seek to arrange a conference with you towards the middle of November to address any queries that you might have once you have had the opportunity of considering the papers.

1. The Contract

- 1.1 The Edinburgh Tram Project is being undertaken by a consortium of companies, namely (i) Bilfinger Berger Civil UK Limited ("BBC UK"); (ii) Siemens plc ("Siemens"); and (iii) Construcciones y Auxiliar de Ferrocarrillessa ("CAF"). The Contract was executed by BBC UK and Siemens on 14 May 2008. The employer under the Contract is TIE Limited ("tie"). tie is a wholly owned subsidiary of CEC.

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1 EXCHANGE CRESCENT
CONFERENCE SQUARE
EDINBURGH EH3 8UL
DX 551970 EDINBURGH 53
T: +44 (0)131 [REDACTED]
F: +44 (0)131 228 1222
www.shepwedd.co.uk

155 ST. VINCENT STREET
GLASGOW
G2 5NR
DX GW409 GLASGOW
T: +44 (0)141 [REDACTED]
F: +44 (0)141 565 1222

CONDOR HOUSE
10 ST. PAUL'S CHURCHYARD
LONDON EC4M 8AL
DX 98945 CHEAPSIDE 2
T: +44 (0)20 [REDACTED]
F: +44 (0)20 7329 5939

9 GOLDEN SQUARE
ABERDEEN
AB10 1RB
DX AB44 ABERDEEN
T: +44 (0) [REDACTED]
F: +44 (0)1224 343 545

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- 1.2 In addition on 14 May 2008 the parties entered into a Minute of Variation with tie and CAF in terms of which CAF became a member of the consortium and was confirmed as a party to the Contract. This Contract is referred to as the "Infraco Contract". The consortium are referred to as "Infraco".
 - 1.3 CEC do not have a direct contractual relationship which tie in terms of the Infraco Contract. However, CEC has issued a guarantee to tie, guaranteeing tie's contractual liabilities. Further, since tie is a wholly owned subsidiary of CEC, tie require CEC's consent to undertake certain actions. One of these actions is the termination of the Infraco Contract.
 - 1.4 The Project has been beset by difficulties all of which have been heavily reported in the local press in Edinburgh and more widely. As a consequence of the many disputes in relation to the Project a plethora of different lawyers have been involved in providing advice. In order to assist in understanding the papers, we would advise that the following parties are represented as follows:
 - 1.4.1 tie – represented by DLA Piper Scotland who have instructed Richard Keen QC (Dean of Faculty in Scotland) to advise on issues relating to termination and Calum MacNeill QC to advise on issues relating to interim payments.
 - 1.4.2 Infraco – represented by Pinsent Masons.
 - 1.5 We are not instructed in relation to these disputes where tie have been taking their own independent legal advice. However, we note from the papers with which we have been provided as at 23 June 2010 there had been 15 separate dispute resolution procedures and a further 50 were anticipated. In terms of the Infraco Contract the works were due to be concluded by 16 July 2011. However, as at July 2010, tie estimated that only approximately 15% of the works have in fact been completed. We have recently been advised that to a large extent tie has demobilised.
 - 1.6 Given the complexity of the Project there are a variety of reasons for the problems which have arisen to date. By way of a high level summary we understand that there are two key issues which have caused the substantive delay. The first relates to the development of the design. In effect the Contract envisaged a design development process which was not completed prior to the Contract being signed. Therefore, there was no clear benchmark by which the design should be assessed for the purposes of identifying whether any change was in fact a variation or simply a development of the existing design for which the Infraco was responsible. There have been a number of adjudications seeking to assess whether a particular design was a tie change or not. Secondly, the amount of work required to divert the services and utilities within Edinburgh were greatly underestimated. This is a risk which rested with tie and substantive delays have been caused as a consequence of this.
 - 1.7 In addition to these two main issues there has been a series of issues relating to the standard to which the design has been undertaken and a specific dispute relating to whether the works on Prince's Street in Edinburgh were defective or not.
 - 1.8 In the course of August 2010 negotiations were ongoing between the parties with a view to trying to achieve a new baseline for the Contract which would allow certain works to be completed on a clear and fixed price basis. It appears to CEC that these negotiations have not been successful and that therefore it will be necessary for tie to consider whether it has grounds for terminating the Contract. tie have been considering the position in this regard and CEC anticipate being presented with a formal request in terms of the Shareholders Agreement to consent to that termination. This is the main purpose for seeking your advice.
- 2. Provisions In Relation To Termination**
- 2.1 The provisions in relation to termination of the Infraco Contract due to an Infraco Default can be found in Clause 90 of the Contract (at page 202). In considering whether there are grounds for default tie

has concentrated upon 3 grounds of Infraco Default, as defined in Schedule Part 1 to the Contract (see page 255/256). These grounds are as follows:

- (a) *"A breach by the Infraco of any of its obligations under this Agreement which materially and adversely affects the carrying out and/or completion of the Infraco Works;...."*
- (g) *the issue of four or more Underperformance Warning Notices in any 12 month period and...*
- (j) *the Infraco has suspended the progress of the Infraco Works without due cause for 15 Business Days after receiving from tie's Representative a written notice to proceed."*

2.2 Clause 90.1.2 provides as follows:

"as stipulated pursuant to Infraco Default (a) (f) (g) (to the extent that the Underperformance Warning Notices have been issued pursuant to Clause 56.7.2) and (j) in Schedule Part 1 occurs tie may give notice in writing to the Infraco specifying the nature of the Infraco Default which has occurred (a "Remediable Termination Notice")."

2.3 Clause 90.2 provides:

"Following services of a remediable Termination Notice by tie in accordance with Clause 90.1.2 the Infraco may submit a comprehensive rectification plan setting out how it intends to remedy the Infraco Default in respect of which the Remediable Termination Notice has been served to tie within 30 Business Days of the date of such Notice (or such longer period as tie may agreed to in its absolute discretion). Tie shall consider such rectification plan and determine, at tie's absolute discretion, within 10 Business Days of receipt whether the rectification plan is acceptable. If tie accepts the rectification plan, the Remediable Termination Notice shall no longer be effective and no further Remediable Termination Notice will be served by tie in respect of the relevant Infraco Default, provided that the Infraco complies in full with the terms of the rectification plan as accepted by tie. Any failure by Infraco to comply with the terms of such rectification plan shall entitle tie to terminate the Agreement on 5 Business Days written notice to the Infraco and there should be no obligation on tie to consider any further rectification plan."

2.4 Clause 56.7 provides:

2.4.1 *"Subject to Clause 56.9, without prejudice to tie's other rights under this Agreement, if*

56.7.1 at any time the Infraco has committed any material breach of its obligations under this Agreement; or

56.7.2 following the issue of the Reliability Certificate, in any Reporting Period where Infraco's performance is below the standard required to achieve the Minimum Performance Payment,

then tie may issue an Underperformance Warning Notice to the Infraco setting out the matter or matters giving rise to such Notice and containing a reminder to the Infraco of the implications of such Notice.

56.8 following the service of an Under Performance Warning Notice in (sic) pursuant to Clause 56.7.2:

56.8.1 the Infraco shall within 10 Business Days of receipt of such Underperformance Warning Notice deliver to tie a plan setting out how the

Infraco propose to remedy the issues which led to the deductions leading to the service of such Underperformance Warning Notice and proposing a suitable timescale to remedy such issues (a "Rectification Plan");

56.8.2 the Parties will use reasonable endeavours to agree the contents of the Rectification Plan within 10 Business Days of receipt by tie; and

56.8.3 if the Parties do not agree the Rectification Plan within 10 Business Days of receipt by tie either Party may refer the matter to the Dispute Resolution Procedure (provided that the Infraco may not refer or cause tie to refer the matter to the Dispute Resolution Procedure vexatiously to delay the agreement of a Rectification Plan)".

- 2.5 In light of the concerns with regard to the performance of Infraco and the likelihood of needing to consider termination, tie sought the Opinion of Richard Keen QC in relation to the termination provisions. This advice was sought over a period of time from June 2009 through to September 2010. Copies of the relevant Letters of Instruction together with the advice which was received can be found at section [insert number] of your papers. In our view the most substantive advice can be found at section [insert number] where the Letters of Instruction and a detailed note of the consultation which took place on 8 July 2010 can be found.
- 2.6 On the basis of Senior Counsel's advice tie has have proceeded to serve a number of Underperformance Warning Notices and Remediable Termination Notices. Copies of the 10 Remediable Termination Notices and the 4 Underperformance Warning Notices can be found in folder [insert reference] of your papers. In addition, responses to the various Notices can also be found within that folder.
- 2.7 We have not been briefed on the detail of the matters which are in dispute because this is a matter for tie to determine whether there are proper grounds for serving the Notices and to assess the probability or otherwise of there being good grounds to terminate. CEC's interest comes from the perspective of seeking to assess whether they should consent to requests from tie (should this be received) to terminate the Infraco Contract. In approaching this exercise CEC has indicated that they are relying upon tie to carry out this assessment and to make a formal recommendation for CEC's approval. However, given that tie is a wholly owned subsidiary of CEC and CEC have granted a guarantee to Infraco it is clearly of practical importance to ensure that any termination is ostensibly valid in terms of the Contract procedures and there is a reasonable basis for asserting that there has been a breach.
- 2.8 Since responsibility for managing the Infraco Contract rests with tie, CEC has not been involved with the detail of the issues raised to date and therefore do not have the detailed knowledge of the breaches upon which tie are seeking to found in looking to terminate the Contract. However, we have asked tie to provide the information which they asset supports their analysis that there has been a breach. This information is set out in folder [insert reference] by reference to each of the Notices upon which tie are founding.
- 2.9 CEC are not, and will not, be in a position to identify and analyse whether the factual circumstances relied upon by tie can be justified in terms of the Notices. Nevertheless, on the basis of the information which has been provided by tie we wish to form a view as to whether it is reasonable for CEC to accept that tie have a basis for serving the Notices, without being able to form a view of the ultimate outcome of any dispute.
3. **Questions for Counsel**
- 3.1 In light of the above, we would be grateful if you could provide your opinion on the following matters:

- 3.1.1 In relation to each of the Underperformance Warning Notices and Remediable Termination Notices served by tie in the period from 9 August 2010 to 12 October 2010, please confirm whether you accept that the grounds relied upon form a proper basis for terminating the Contract or not. If not, please clarify your reasoning in this regard;
- 3.1.2 In light of the information which has been provided by tie to support its assertion that there are factual circumstances which give rise to the grounds for termination, please confirm whether you accept that this evidence with which we have been provided by tie gives a reasonable basis for the ground of default relied upon. In effect, we are undertaking a "desktop review" to establish whether there are proper grounds to terminate, without having the time or resource to identify whether the factual circumstances, on the balance of probabilities, may ultimately be upheld by a court or an adjudicator.
- 3.1.3 Is there anything further which Counsel wishes to add?

We look forward to hearing from you but should you have any queries in the meantime, please do not hesitate to contact David Anderson of this office.

Yours sincerely

David Anderson
For and on behalf of Shepherd and Wedderburn LLP
david.anderson@shepwedd.co.uk
DL: [REDACTED]