

EDINBURGH TRAM PROJECT.

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Report to Stewart McGarrity tie SRO.
Copies: Steven Bell, David Mackay Marshall Poulton.

Submitted By: members of peer review Team
Date: 19th March 2009

SUBJECT: TIE Change Order No 21 "Provision of contingency bus lane to Princes Street (For 2 week Period)" and associated Dispute Resolution Procedure ("DRP") referrals.

INTRODUCTION

Members of the Peer review team have been asked to provide tie with an independent review of the issues surrounding Change Order 21 and its referral to DRP.

The terms of reference for the work are attached as Appendix 1.

We met tie representatives in Edinburgh on 5th March to obtain background information in addition to receiving documentation sent by tie on 26th February which contained the two DRP position papers and background correspondence preceding them. Our objective is to provide, in this short report, some views on the likelihood of these referrals succeeding at adjudication, including our view on how an adjudicator may view the documentation and matters that are likely to be raised by an experienced contractor if it chooses to defend them.

We have seen comments from tie in response to a number of the points made here. We believe it is essential that we keep our respective responsibilities separate and we have incorporated tie's comments where there are factual changes to our draft. By doing this we can meet our terms of reference and produce a document that can assist tie in deciding how to take matters forward.

BACKGROUND

From the papers we have seen, we recognise that there has been growing dissatisfaction and frustration within tie over the performance of the Bilfinger Siemens Caf consortium ("BSC"). The frustration relates to inadequate progress against the original programme, failure to provide timely estimates for changes, the excessive prices originally estimated compared with those finally determined and a general failure to adopt the "partnering" approach that secured partner status compounded by what tie perceives as re-opening commercial issues that had been closed, notably on changes relating to design and programme. At this stage, tie views Bilfinger as the principal "blocker" to meeting the original expectations that were enshrined in the Infraco contract. tie perceives that this behaviour must be seen in context of a number of negotiations since the original tender which increased the contract price. In mid February it appears that BSC said to tie that there was a 16 month delay to the project (unmitigated) and that all costs since FC to resolve it and other changes would be to tie's account and would be in the range £50-80m. tie's evidence for this is in the contemporaneous notes of meetings taken by its staff. There is no written evidence of the "claim" by BSC although the numbers and delay are referenced in correspondence between David Mackay and Bilfinger's Dr. Keysberg.

tie considered its options taking advice from DLA Piper and concluded that in consequence of BSC's failure to engage meaningfully in discussions over a broad range of commercial disagreements over a period of time, as evidenced by BSC taking an increasingly entrenched position, establishing some principles over pricing and adherence to the contract through DRP would both move things forward in terms of resolving differences of interpretation and demonstrate commercial resolve.

On the 12th of January 2009, tie issued a Notice of Change indicating it wished to implement a Change to provide, for a two week period, a bus lane on Princes Street to allow contingency for traffic management alongside the substantive works in Princes Street that had been programmed to start in January and were then expected to start on 21st February. [BSC had previously been advised of this requirement in December 2008 prior to the formal notice of change requesting an estimate] Change Order No. 21 was issued on the 13th of February and had previously been priced by BSC in a way that tie considered at variance with the contract Schedule Part 4. tie returned it duly amended and attempted unsuccessfully to agree this with BSC. On 19th February, tie issued an instruction, in accordance with Clauses 80.13 and 80.15, to implement the change described in Change Order 21 in Princes Street and also gave notice that the unagreed Estimate was being referred to DRP.

There were two referrals to DRP. The first related to the issues concerning the pricing of the Estimate for Change Order No. 21 where BSC had applied Preliminaries to the change which were not in accordance with schedule 4.

The second related to the refusal by BSC evidenced by their statement that they were not contractually obliged to work on Princes Street to follow tie's instruction in accordance with Clause 80.15.. This refusal had arisen suddenly as a consequence of a request by tie for confirmation of these works starting (on 21st February as previously advised to tie) by tie's Chairman when the wider issues were being discussed.

We attach our sequence of events gleaned from the documents by way of reference as Appendix 2. We have not spoken to BSC and have only seen the notes of the first DRP meeting held on 20th February Bell/Brady and the outline position paper produced by BSC in response to tie's position papers.

CONSIDERATION OF THE DRP POSITION PAPERS.

We need to set out some principles that we have taken into account in giving our views on these matters.

Firstly, it will be important that the DRP process relating to Change Order No. 21 has complied with the provisions of the contract agreement otherwise there will be a real possibility that one party will seek a declaration to set it aside as it is invalid. (*"Process matters"*)

Secondly, that adjudicators will be keen to determine the matter in front of them and will be reluctant to make a decision of far reaching consequence (in the opinion of one of the parties) without ample evidence that it is proper for them to do so based on the facts and the case before them. In our experience they will apply a materiality test to the matters and be influenced by the extent that the parties have tried to avoid the dispute that is being presented, unless it is being presented jointly as a "failure to agree", which requires being determined. (*"Determination Matters"*)

Our views on this second aspect are re-inforced by reference to an article that appeared in the magazine of the Chartered Institute of Purchasing and Supply (CIPS) on 5th March [Supply Management 5th March 2009 p36-37] where the 4 main methods of Dispute Resolution are considered.

In considering adjudication, the author draws attention to its speediness, confidentiality, timeliness and cheapness as advantages of the approach. More relevant to the matter at hand he lists the disadvantages relative to enforceability, the absence of case law and most importantly for tie the following which are quoted in their entirety

"It is prone to ambush; a party could spend months preparing their claim and due to short timescales the defendant may struggle to respond in time." We think this point is relevant given the

lack of comment from BSC on matters to date. We do think that tie should resist taking confidence from a position that “they haven’t raised it so far”

“An adjudicator can only preside over the matter before him. There is no opportunity to counter claim on a different issue-in that instance a separate action would be raised”. We make that point so tie can consider its strategy in this dispute and whether the strategy of developing a wider argument about non compliance with the contract as set out in DLA Piper’s views will be accepted. We make no further comment on this point as we are only making initial observations based on the papers we have seen.

Our preliminary views on these are set out below.

Process matters.

We think that the following matters will need consideration if tie wishes to take DRP to the next stage. Tie has subsequently commented on these points and is confident they can be addressed.

In relation to the points 1 to 6 below, please see DLA Piper's Note of 16th March. **The DLA Piper note is and remains legally privileged advice provided to tie in relation to contentious proceedings and has been made available to the PRG in order for them to discharge their mandate and for no other purpose.**

1. Notification of the DRP. We think this was done by letter from the tie Chairman on February 19th. Is it clear that he is able to give such notification?
2. Can there be obfuscation by BSC of the role of the Project Director as Project Director and tie’s representative in terms of giving instructions?
3. Did the signatory of Change Order No. 21 have tie Representative’s delegated authority and is it documented?
4. Did tie issue the instruction to carry out the works on Princes Street before electing to refer the matter to DRP whereas Clause 80.15 requires it to happen afterwards?
5. Did tie issue a second change order to instruct the works as required by our interpretation of Clause 80.15?
6. Why did the Change Order not give any dates on it?

Determination matters.

Providing that the generic “Process matters” can be dealt with then we have considered the two DRPs separately as “Estimates” DRP Referral 1 and “proceeding with Change Order 21” DRP Referral 2.

Estimates.

In our experience tie should be successful in its claim assuming it can demonstrate how the methodology of pricing preliminaries has changed since January 2009 as stated to us. tie has made it clear to BSC that BSC has the opportunity to identify specific activities that it has been required to undertake for Change 21 and has failed to do so in its pricing. It will be for tie to demonstrate the opportunities that were available to BSC to adjust pricing away from the formulae set out in Schedule 4 and how it has agreed to such variations in the past.

An issue for the adjudicator, who will be very familiar with such issues, is why such a small value matter was not sorted out between the respective Quantity Surveyors. It will be for tie to explain why such a change is being presented for determination as an issue of principle. There seems to us to be no reason why tie should not achieve this.

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Proceeding with Change Order 21.

Based on the papers we have seen so far, we think tie will find it more difficult to convince the adjudicator of the merits of its case on “proceeding with Change Order 21 “

- a) There is no evidence of efforts to resolve the dispute before DRP. If tie is to succeed in persuading the adjudicator that it had no option but to go to DRP then it will need to set out its grounds.

- b) The involvement of the two organisations’ principals so early in the dispute as evidenced by tie’s Chairman issuing the DRP and BSC’s response will be seen as a message that the two sides have little interest in using the range of DRP options.

- c) Faced with a “materiality” defence it will be for tie to be absolutely persuasive that it can instruct the works in Princes Street consequent to the Change Order. We have found the reasoning difficult to follow and would suggest that so will an adjudicator. The fact that the right for tie to insist on BSC to continue working is buried away in Schedule 9 and talks about undisputed obligations when Tie is seeking to make BSC work on while the dispute(pricing) is resolved does not seem helpful to us. We also think the absence of reference to this obligation in the DRP is an unfortunate omission.

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- d) So far we cannot find a linkage between the obligation to do the works in Change Order 21 and the conformance with the wider programme other than references to other contractual provisions described to us by DLA. We understand that the works in Princes Street were programmed to start in January and had not and infer that the February 21st start date also relates to tie’s stakeholder issues. So far there have been no references to other contractual failings in the DRP so the issues will be limited to Change Order21 unless tie chooses to widen the matter.

- e) We are concerned that tie considers its position in respect of the desire to instruct this change as an issue of principle or just for Princes Street. We think tie should think very carefully that it is not running the risk of importing the programme risk by setting this precedent, as an experienced contractor might use a generic ruling in tie's favour by always asking "what do you want us to do" whenever there is a problem citing tie's willingness to instruct in Princes Street as precedent.

tie



CONCLUSION

We have not taken any legal advice on the contractual matters herein and there are a number of inter-related issues. Our views are therefore based on our experience of such disputes.

We think it is critical to get over as many of the process hurdles as possible. To the extent that some of these cannot be overcome then we think an adjudicator might still be persuaded to determine the estimates issue as that is evidential and limited in scope.

We are less convinced of the merits of the programme issue beyond determining commencing the works relating to Change Order 21 and any implications thereof especially if the process matter relating to Clause 80.15 and the Change Order details are not fixed. This coupled with the materiality defence and an adjudicator's natural caution over jurisdiction might well limit any determination to the circumstances surrounding Change order 21.



We understand that Tie is involved in discussions with BSC about a way forward on contract management issues generally and if these DRPs have brought the parties to engage more meaningfully than they have recently, then tie will have achieved the commercial objectives it put to us.



RECOMMENDATION

Given the dynamic nature of the relationship between tie and BSC we are not well placed to advise tie what to do next but have given our independent opinion of the prospects for the two DRPs.

We would recommend that the next Peer Review session planned for late April is entirely focused on all aspects of Contract Management seeing how things have developed between now and then and looks at Dispute Avoidance as well as Dispute Resolution. Dispute Avoidance requires someone independent to talk to BSC and set out its position, without the discussion becoming a negotiation, in accordance with current best practice. Malcolm will be able to speak on the subject in the light of his involvement in developing such arrangements for the 2012 Olympic Contracts.

Willie Gillan, Mike Heath, Malcolm Hutchinson.

Appendix 1 Terms of reference

Edinburgh Tram - tie Peer Review

Terms of Reference for Review beginning on 5th March 2009

Mike Heath, Willie Gillan and Malcolm Hutchinson (plus Marshall Poulton as observer)

Background

During the period since early December 2008, **tie** has found itself in an escalating and increasingly entrenched series of disagreements with the BSC consortium on a range of contractual issues. This has arisen in parallel with a very late mobilisation and start on construction by BSC and has lately manifested in an impasse such that BSC (led by Bilfinger Berger) have clearly stated they will not work on sections of the project until **tie** accept their overarching contractual conditions and thereby allow them to recover very substantial additional direct costs, prolongation and delay and disruption they have forecast they will incur to complete the project. During the week ending 20th February this uncooperative stance expanded into a refusal by BSC to start permanent works on Princes Street until matters BSC stated were not instructed in respect of Princes Street in particular, including the valuation of all changes, had been resolved.

After taking very robust legal advice and with clear and unambiguous support from the **tie** Board, the Tram Project Board and City of Edinburgh Council, **tie** has now commenced proceedings under the contractual Dispute Resolution Procedure with a view to, inter-alia, getting the permanent infrastructure works on Princes Street started as soon as possible.

The **tie** Chairman has asked the **tie** Peer Review team to provide an independent view on the circumstances leading to the referral of the two current disputes and to test the decision to invoke the DRP procedure.

Specific matters to report on

1. The correspondence and emails leading to the above circumstances
2. Decision to commence the DRP process on Princes St in the context of any alternatives course which may be available to **tie**
3. The strength of the case on the matters referred specifically to DRP

Appendix 2 Chronology

DRP Referral 1

The Dispute - Inability to agree correct method of calculating Preliminaries element of Estimate.
Work content agreed

Nov-Dec	Lengthy meetings discussing tie Change No. 21	
12 th Jan	tie Notice of Change issued. (Inf Corr 573)	No Copy
11th Feb	InfraCo response enclosing Estimate (INTC 274)	No Copy
12 th Feb	Letter from tie Chief Executive to Dr. Jochen Keysberg Executive Board Member BB and copied to other members of the consortium raising tie’s serious concerns regarding progress since the project contract was signed. and highlighting (a) Failure by BSC to prepare proper Estimates in relation to variation or Change. (b) Quality of Estimates submitted as being unacceptable (c) Inadequate project progress (d) Lack of compliance with basic contractual obligations	
13 th Feb	tie issues Change Order No.21 Work to be carried out and actual cost contained in Estimate agreed – Preliminaries in dispute.	
18 th Feb	BSC state not obliged to commence work on	No Copy

(14.07)1. Princes Street – lack of exclusive licence to the (e-mail) Designated Working Area and non-agreement of Estimate.

19th Feb tie letter from Chief Executive in response to BSC's

(a.m.) e-mail of 18th directing InfraCo to commence all works in implementation of Change No. 21 without agreement of

Estimate pursuant to Clause 80.15 of the contract. Furthermore, under Clause 80.15 upon reference to DRP tie consider Change urgent and BSC are required to implement Change with immediate effect. Any failure to carry out the works and any failure, refusal or delay to implement change will be a wilful and fundamental breach of contractual obligation.

tie requires a written response by 12.00 noon (19th) that BSC will mobilise on 21st February and that failure to respond positively in the proposed timescale will be seen as evidence of BSC's intention not to commence works in Princes Street on 21st February and will be considered as a further serious breach of contract.

Separately tie give notice under clause 111 and Paragraph 9 of Schedule 9 that they are referring the following two issues to the DRP under Schedule part 9.

- (1) Failure to agree Estimate in relation to the Change No.21
- (2) BSC's assertion in message under reply that they are not contractually obliged to commence works in Princes Street

19th Feb Letter faxed in accordance with Clause 111.1.22 to BSC (p.m.) which requires BCC's representation in tie's office at 10.00a.m. on 20th February for meeting under Para 9 of DRP.

20th Feb DRP meeting held between tie and BSC.

(10.00) Estimate in relation to DRP Referral 1 still not agreed.

Meeting Reference by tie to instruction of the 19th under Clause 80.15 to commence works on Change Order No.21

Both parties agreed to prepare position papers (pursuant to Para 9.2 of Schedule Part 9) for exchange prior to 2nd March (7 business days from notification).

23rd Feb Response from Dr. Keysberg, BB to tie's letters of 12th and 19th February and the meeting of the 17th of February.

BSC not seeking £80m. – Had given a range of £50m.-£80m. and pointing out that a joint exercise by their respective planners had identified a 16 month overrun to completion. BSC are not setting a condition that the above are agreed before commencing work on Princes Street. BSC also referred to the apparent firm belief by tie that the project is fixed price.

BSC's position simply compliance with the Change mechanism set out in the contract and are still of the opinion that there is merit in both parties lawyers meeting to discuss the 3 main unresolved issues, design development, Change mechanism and access.

25th Feb Letter from tie Chief Executive responding to Dr. Keysberg's letter of the 23rd Feb and noting that others at BSC are to respond in detail to the points raised in tie's letters of the 12th and 19th Feb. tie are still concerned with the lack of progress and actions of BSC illustrated by their refusal to answer questions regarding works in Princes Street. tie stated that the forum for dealing with these issues is now the DRP process and confirmed that all performance failures, time and cost inefficiencies are to BSC's account.

DRP Referral 2

The Dispute – The issue of whether BSC is obliged pursuant to BSC Contract and without further instruction, to proceed with carrying out of Works on Princes Street Edinburgh from 21st February 2009 at the latest.

- 12th Feb Letter from tie Chief Executive to Dr. Jochen Keysberg,
Executive Board Member BB and copied to other members of the consortium raising tie's serious concerns regarding progress since the project contract was signed. and highlighting
- (a) Failure by BSC to prepare proper Estimates in relation to variation or Change.
 - (b) Quality of Estimates submitted as being unacceptable
 - (c) Inadequate project progress
 - (d) Lack of compliance with basic contractual obligations
- 17th Feb tie Chief Executive agreed with BSC principals that they would respond by 12 noon on the 18th of February as to whether they would commence works on Princes Street on 21st February.
- 18th Feb Response from BSC stating that they have not had (11.45) enough e-mail time to fully review their position, but will respond by 1p.m.
- 18th Feb tie indicating that this is wholly unsatisfactory and (12.05) requesting a response by return. e-mail
- 18th Feb BSC response stating that in their opinion any material (20.20) changes from e-mail BDDI to IFC, however minor constitute Notified Departure and thus becomes a tie Change leading to additional costs and time. Clause 80 – does not provide for work to be executed unless tie Change has been agreed. BSC is seeking clarification on these issues and the Change mechanism in general.
- BSC still consider there is an issue with access to the works, which has not been fully explored.

18th Feb
e-mail tie highlighting progress is urgent and needing early (21.36) papers to allow issues to be fully discussed. tie also requesting BSC use all endeavours to bring papers forward at earliest date.

19th Feb tie letter from Chief Executive as per DRP Referral 1. (a.m.)

19th Feb
e-mail BSC response to tie Chief Executive's letter of the 19th (13.39) indicating they will need time to discuss issues raised at a consortium level and will require time to formulate a response.

19th Feb
e-mail tie indicating that as deadlines have passed without any (19.42) written response from BSC regarding mobilisation in Princes Street on 21st Feb they consider this to be further evidence of BSC's intention not to commence work as planned in Princes Street.

19th Feb
e-mail BSC response to tie Chief Executive's letter of 19th Feb (20.25) dealing with only the salient matters BSC are not obliged to accept instructions which they consider not to be in accordance with the Contract, but on a goodwill basis they agree to commence works in Princes Street however BSC's understanding of the Chief Executive's letter of the 19th of February is that these works are to be paid in accordance with Clause 80.15 and Clause 80.16. demonstrable costs as per the agreement reached at the meeting on the evening of the 17th of February. BSC staff is available for a meeting on the 20th February but consider it appropriate for tie and BSC's lawyers to meet in order to try and avoid ongoing disputes throughout the currency of the project.

19th Feb
e-mail tie indicating that BSC are contractually obliged to act (22.15) on instructions and asking BSC to ensure that their Representative attends a meeting at 10.00 a.m. on 20th February.

20th Feb
e-mail BSC repeating that they have difficulty in getting (8.44) consortium responses. They wish to resolve matters quickly but need all components of their 3-tabled issues to be fully dealt with. BSC also requesting that tie refrain from issuing statements on timing since BSC wish to concentrate on augmenting this exercise.

20th Feb tie stating that they do not agree with BSC's assertion (10.00) that they are not contractually obliged to commence works on Princes Street.

Meeting BSC consider they require an instruction to commence works on Princes Street at tie's risk pending finalisation of A-Commercial.

The method of valuing Change work

The Preliminaries which are not agreed.

The process/method of reconciling actual cost with relevant milestones.

B- Technical

OLE bases and associated duct work

Track form

Road reconstruction

Both parties agreed to prepare position papers for exchange prior to the 2nd March.

Both parties also agreed to meet on the afternoon of 20th February to try to progress these disputes in parallel with the formal DRP process

20th Feb e-mail tie reject BSC's offer to start work on Princes Street (10.03) on an extra contractual basis. They request that BSC withdraws its previous statement that tie must accept all risks associated with works on Princes Street.

tie again repeats its previous statement the BSC must meet its contractual obligations and instructs that works on Princes Street be restricted to completion of enabling works, traffic and pedestrian management diversions, provision and maintenance of previously specified fencing and necessary security arrangements.

- 20th Feb e-mail BSC stating they have nothing to add in relation to the (18.52) issues of reimbursement for Changed works and commensurate extensions of time where applicable. BSC have the feeling that tie do not fully understand BSC's position and that the DRPs may have been invoked on the basis of a misunderstanding of the Contract on tie's part. BSC are still seeking an instruction to start work on Princes Street.
- 21st Feb tie restating its position and indicating to BSC that the (13.27) time for legal meetings has passed. tie and BSC have a joint obligation to attempt quickly and in good faith to resolve the current disputes.
- 23rd Feb Response from Dr. Keysberg, BB to tie's letters of 12th and 19th February and the meeting of the 17th of February. BSC not seeking £80m. – had given a range of £50m.-£80m. and pointing out that a joint exercise by their respective planners had identified a 16 month overrun to completion. BSC are not setting a condition that the above are agreed before commencing work on Princes Street. BSC also referred to the apparent firm belief by tie that the project is fixed price. BSC's position simply compliance with the Change mechanism set out in the contract and are still of the opinion that there is merit in both parties lawyers meeting to discuss the 3 main unresolved issues, design development, Change mechanism and access.
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