

From Colin Mackenzie, Principal Solicitor

MEMORANDUM

To Duncan Fraser, City Development
Rebecca Andrew, Finance

Our Ref
Your Ref

Date 6 September 2007

Tie Operating Agreement
CONFIDENTIAL

At the Council meeting on 23 August the Council was instructed to enter into a new operating agreement with tie in relation to the trams project. To that end I should be grateful for instructions from City Development and Finance as to what terms and conditions they would wish the agreement to contain.

In particular, I would highlight the following issues for your further consideration/guidance:

- The simplest format for this arrangement will be a relatively short “legal boilerplate” agreement, supplemented by a very comprehensive schedule. The agreement itself will set out the main terms and conditions, with tie being engaged to provide specified “Services” to the Council. These “Services” will need to be specified in the Schedule in the form of requirements and expected service levels. To this end, City Development and Finance will be required to formulate and finalise such a schedule. In practice, this will require the departments to establish what work needs to be done to introduce the tram system and ensure that all that is required/expected is reflected in the schedule to ensure tie are contractually bound to complete these actions to the Council’s satisfaction.
- Is the agreement simply to look forward, or is it also to deal retrospectively with tie’s actions to date? The agreement could be signed in 2007, but bind the parties with effect from 2003 or before. It is unlikely that tie will be willing to sign up to an agreement which they would breach simply by signing it and, in practical terms, tie will not agree to a retrospective agreement unless it is 100% certain that it has complied with the terms to date. Consideration will therefore have to be given to whether a retrospective application is in fact practical in the circumstances. However, if there is no such retrospective application, you may need to consider what protection the Council has if tie’s actions to date have in fact not been sufficient for the Council’s purposes.
- It is entirely appropriate that some form of formal agreement be put in place to regulate the relationship between tie and the Council. However, it should be appreciated that tie is a wholly-owned and wholly-funded subsidiary company of the Council. Therefore, it is unlikely that the Council would ever choose to sue tie. If this is the case, what sanctions will there be should tie breach the agreement or fail to deliver? Without any “teeth”, such an agreement will be largely redundant in real terms. Is it anticipated that there will be any penalty for tie’s non-performance, and if so, what is this penalty to be? The only

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situation which I presently anticipate would encourage the Council to sue tie in terms of this agreement would be where the Council is able to claim on tie's indemnity insurance cover. Please advise what the level of cover is and that it covers the work undertaken by tie. However, this would clearly have reputational consequences for the Council (ie the perception that the Council is suing itself over a project which it instructed and ostensibly controlled). To give an example, if tie somehow put the Council into breach of the terms of the funding agreement with the Scottish Government, the Scottish Government may demand repayment of a substantial part of the tram funding. In such circumstances, the Council could find itself having to repay sums it doesn't have, whilst only having a partially completed tram system in place. It may then be seeking to rely on an agreement with a subsidiary company which will likely only allow for a small cost recovery in terms of insurance (as it is likely to be capped). This is likely to lead to accusations of mismanagement by the Council which is clearly not an ideal scenario.

- The role of tie to date is not clear cut. It could be argued that tie is acting on the Council's behalf as its agent. However, this raises the question of why the procurement exercise has been carried out in tie's name as contracting party as opposed to in the Council's name. What is the true nature of tie's role?
- Finally, there is the question of who will negotiate this agreement on tie's behalf. If DLA are, as I presently understand, going to be acting for both the Council and tie, is it appropriate that DLA review this contract and, if so, on whose behalf will they do so?

In conclusion, whilst some form of agreement with tie is undoubtedly desirable to more clearly define the respective roles and responsibilities of the parties, the Council should be aware that such an agreement will in no way ameliorate the overall risks to Council of the project.

Against this background, I should be grateful for your views on how best to protect the Council's interests and also for details of any specific terms you would envisage being in the main body of the agreement. In the meantime, I would recommend that both City Development and Finance commence a review of the terms and structure of the project (with specific reference to tie's future role) in order to formulate the specification of services which will require to be appended to the agreement to be drawn up by Legal Services.

Regards,

For Council Solicitor

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