

Legally privileged and prepared in anticipation of litigation

Legal Strategy – Trams

1. Purpose

- 1.1 The purpose of this note is to set out in very clear, brief terms:
 - 1.1.1 the present approach being pursued by tie;
 - 1.1.2 the view expressed by CEC's independent QC, Nicholas Denny (the "QC") on that approach; and
 - 1.1.3 the QC's view on the preferred approach as to the way forward.

2. Background

- 2.1 tie have been considering various options:
 - 2.1.1 status quo;
 - 2.1.2 mature divorce;
 - 2.1.3 termination;
 - 2.1.4 enforcing performance of the contract;
 - 2.1.5 meeting with Infraco; and
 - 2.1.6 mediation.
- 2.2 Most recently tie have been exploring:
 - 2.2.1 termination following service of various remediable termination notices ("RTNs"); and
 - 2.2.2 mediation following an emergency motion passed by CEC on 16 November 2010.
- 2.3 In order to avoid the unquantifiable risks arising from wrongful termination of the contract, tie's latest legal advice is to test the validity of the RTNs served to date by means of the dispute resolution procedure in the Infraco contract.
- 2.4 tie have been taking advice initially from DLA and more recently from McGrigors and Richard Keen QC. That advice has helped inform their strategy.
- 2.5 To date CEC has been content to allow tie to investigate the factual position and take the lead on strategy. Under the operating agreement tie/TBL

requires the approval of CEC for certain material actions, including termination of the Infraco contract. We were previously led by tie to expect that TEL/tie would come forward to the December Council meeting with a request for consent to terminate.

3 **Strategy – the QC’s view on tie’s present approach**

3.1 **Credibility Issues**

There is a real concern as to the lack of credibility in the eyes of the Infraco (and indeed of stakeholders) due to:

- 3.1.1 the continual shift in direction and apparent lack of a coherent strategy for the way forward with the project;
- 3.1.2 vague/badly formulated RTNs which have been met with apparent derision by the consortium; and
- 3.1.3 the new and precipitate attempt to move to a further means of dispute resolution by way of mediation.

3.2 **Termination**

Whilst the possibility that tie does have grounds for termination cannot be ruled out at this stage and whilst that needs to be investigated further by McGrigors, there are significant concerns that:

- 3.2.1 the Princes Street RTN is back in tie’s court and has not been responded to;
- 3.2.2 the remaining RTNs are too vague and unspecific to enable termination (even if supported by the facts);
- 3.2.3 at present, CEC does not have the full factual picture; and
- 3.2.4 the manner of prosecuting any alleged Infraco default has been ineffectual.

To put this more clearly, termination on the basis of the present RTNs is not advisable. However on any view, given progress to date by the consortium on the delivery of the works, it would appear probable that if properly investigated and formulated, valid grounds of breach could be articulated effectively in due course.

3.3 **Mediation**

- 3.3.1 If properly run, mediation should be fully prepared for on the basis of full factual information and with a known strategy, once CEC/tie is on a substantially surer footing.
- 3.3.2 That process will take months and whilst there is a political imperative it should be slowed down to enable a clearer, more incisive strategy to be put into effect.
- 3.3.3 Mediation at this stage is legally premature and may lead parties to a further entrenched position.

3.4 **Meeting with Infraco**

Whilst this was chosen to neutralise possible judicial review in relation to termination, it makes sense for the CEC meeting to proceed in order to elicit further information and to ascertain what Bilfinger Berger (Germany) in particular would like to discuss.

3.5 **Factual position at time of contract entry**

There should be a full investigation into the communications between the parties leading up to the contract being entered into, in order to ascertain the full factual matrix and assess whether there are any other matters that may assist in relation to the present contractual difficulties.

3.6 **Infraco position**

- 3.6.1 It is likely that Bilfinger Berger do not fear termination as presently proposed by tie and, indeed, CEC/tie could well be playing into their hands by terminating the contract.
- 3.6.2 Siemens are likely to take a shorter term view, wanting a return on their investment.
- 3.6.3 CAF are likely (notwithstanding joint and several liability) simply to be thinking of supplying the tram vehicles.

4. **CEC's proposed strategy – the way forward**

- 4.1 Given the number of competing variables it helps to analyse what it is that CEC would like to achieve.
- 4.2 That is something that the Tram IPG needs to agree.
- 4.3 The working assumption is that CEC would like an operational tram from Edinburgh Airport to at least St Andrew Square for the best price possible and as soon as possible.

- 4.4 There are only two ways in which that can be achieved:
- (a) reduce the scope, rebase the contract and keep the existing contractor ("Option 1"); and
 - (b) terminate the contract and reprocure with a new contractor ("Option 2").
- 4.5 In any event, the immediate strategy should be to force the contractor to perform the contract and incur expense. If that does not yield a result by unlocking the present contractual deadlock and providing us with a stronger position from which to negotiate a rebasing of the existing contract (Option 1) the contract would need to be terminated (Option 2). It is hoped that pursuit of the strategy of enforced performance should assist in that event, by providing fresh and more compelling grounds for termination linked to the Infraco's failure to progress the works.
- 4.6 The contractor at present is not taking tie's termination arguments seriously and tie do not appear to be exerting sufficient or credible pressure on the consortium to hold them to the contract.
- 4.7 From the QC's review of the documents it is fair to say that the project management provided by tie to date has not been conducive to the most orderly completion of the project and a more sceptical approach towards tie is needed than has been shown to date. Serious consideration should be given as to tie's ongoing involvement in the project.
- 4.8 The proposed approach is that:
- 4.8.1 tie ask the consortium for an update immediately on:
 - (a) the state of the design; and
 - (b) the current programme ie. when they will complete the works and other contract deliverables.
 - 4.8.2 tie then require the consortium to continue with the works (and, in particular the Princes Street works). It goes without saying that contract changes proposed by tie should be kept to a minimum.
 - 4.8.3 in parallel, McGrigors should be required to continue with the existing investigation into the factual matrix but on the assumption that the existing RTNs served to date are too unspecific to provide an effective ground for termination; and
 - 4.8.4 if a decision is subsequently taken to terminate the contract this must be on the basis of firstly, a proper evaluation of the factual

position and secondly, fresh RTNs - most likely linked to a failure to carry out the works referred to at (b) above.

5 Conclusion

5.1 In summary:

- 5.1.1 the existing strategy has been both inconsistent and ineffectively formulated and executed to date;
- 5.1.2 the mediation in the immediate term is premature and inadvisable;
- 5.1.3 the meeting with Infracore should proceed;
- 5.1.4 termination should not proceed on the basis of the existing RTNs (and it follows that tie's proposed strategy of testing the RTNs through the dispute resolution procedure in the contract should not be pursued);
- 5.1.5 performance of the contract by Infracore should be enforced as set out above;
- 5.1.6 the investigation into the factual position should be urgently finalised; and
- 5.1.7 tie's ongoing position as project manager should be seriously reconsidered.

- 5.2 The legal strategy above clearly needs to be considered in the light of all other relevant considerations such as financial, PR and political.

Head of Legal and Administrative Services
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