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**Edinburgh TRAM Project**  
**(Commercial In Confidence)**

**tie Limited**

**Paper to** : **Tram Project Board**

**Subject** : **SDS Commercial Settlement On Claim and Historical Changes**

**Date** : **5 September 2007**

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**1.0 Introduction**

- 1.1 The Board paper dated 15 August 2007 seeking authority to negotiate a draft settlement with SDS was approved.
- 1.2 Subsequently negotiations were concluded on a without prejudice basis resulting in a draft settlement proposal being put to SDS. In summary the resultant settlement of £2.5m in respect of:-
- Their claim claim,
  - certain historical unresolved changes and
  - unbudgeted changes required to out of value engineering
- represents a saving of £650,000 on the budget. In addition payment of £2m of the claim is deferred until delivery of the final items for each of the three critical design workstages – MUDFA designs, Design Completion Notifications and Design Assurance package. The first payment of £0.5m is not due until October, by which time any further issues with performance will have come to light.

**2.0 Background**

- 2.1 SDS submitted a claim totalling £2.8m, in addition there remained £1.1m of historical changes which remained unresolved, a total of £3.9m.
- 2.2 The Project's view in respect of the claim and changes is:-
- Claim £1.2m to £1.8m for a 3 month delay due failures to deal with Preliminary Design expeditiously and in respect of Critical Issues resolution delays.
  - Changes - £0.5m to £0.97m
- A total of £1.7m to £2.77m.
- 2.2 tie have identified a potential counterclaim in respect of the impact of delays by SDS prior to the commencement of Detailed Design. As noted in previous papers the value of this is up to £15m. However, to date only an outline claim has been developed for the purposes of reducing the value of their claim and expectations in respect of disputed historical changes.
- 2.3 The options for resolving the claim and counter claim are:-
- Follow the stepped contract dispute resolution process of resolution between principals, adjudication and finally if unresolved by the former, litigation.
  - A negotiated settlement

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- 2.4 The reasons for pursuing a negotiated settlement rather than pursuing the strict contractual approach are:-
- To minimise the risks to the Infraco procurement. Novation of SDS to Infraco is a key element of the procurement strategy. Whilst SDS must, under their contract, accept novation Infraco is able to reject or qualify novation. Ongoing or escalating dispute with SDS is likely to provide Infraco with a reason for heavily qualifying the novation. The likely qualification would at best be that the unresolved dispute remains with tie to settle or dispute. Whilst we are seeking to finalise a deal with Infraco such a situation would not help maintain the Infraco risk transfer objectives.
  - To avoid the cost and distraction to the Project at this critical time in the programme.
  - To recognise and settle quickly around the valid elements of the SDS claim whilst using the levers of a counterclaim to reduce the settlement figure.
  - Whilst the delays to the design process on which the counterclaim is based can be evidenced as fact the causes of the delays are largely based on anecdotal evidence and interpolation from events at the time. This is particularly the case for the events pre August 2006. The contracts do not appear to have been managed effectively by either party prior to this date. A significant proportion of the additional cost, circa £10m, relates to additional Infraco and Tramco inflation costs due to delay. This is a future potential loss not an accrued loss at this point in time. Demonstrating this could prove difficult, particularly in the light of market price changes. In addition the contract terms arguably time out any counterclaim, given the length of time that has elapsed since these events arose.

### 3.0 Negotiations

- 3.1 Negotiations were undertaken in on SDS's figure of £3.9m. Both parties were not able to agree an acceptable figure based on the scope of the negotiations outlined above. In order to find a basis for an acceptable compromise three further items were introduced into the negotiations:-
- The redesign of the Depot to take account of VE opportunities (£SDS value £380k)
  - Redesign of the alignment to take account of the omission of the EARL bridge at Ingliston (SDS value £125k)
  - Provision of full technical support for MUDFA (SDS value estimated at £100k)
  - The Projects view of the price for these items is £480k (best case)
- 3.2 Taking these items into account the Parties view of the positions is:-
- SDS - £5.1m
  - Tie – 2.2m, best case and £3.5m worst case.
- Details of the parties positions is shown in Appendix A.
- 3.3 A draft settlement was agreed taking account of these additional items at £2.5m.

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**4.0 The Draft Settlement Proposal**

- 4.1 Details of the draft settlement are £2.5m for settlement of SDS's claim and any issues arising from their heads of claim up to 17<sup>th</sup> August 2007, settlement of the historical changes and settlement of the three additional issues introduced.
- 4.2 To incentivise SDS to deliver the key design outputs for Phase 1a payment is staged as follows:-
- £500k on October 07 Valuation.
  - £500K on satisfactory completion of the last utilities design for Phase 1a – estimated...
  - £500k on satisfactory delivery of the last design completion negotiation for Phase 1a – estimated...
  - £100K on satisfactory delivery of the last design assurance package for Phase 1a – estimated June 08

This proposal has been confirmed to SDS but is subject to SDS (PB) Board approval and agreement of the formal settlement. Agreement to be ratified by the TPB in late September.

It should be noted that this draft settlement is specific to the SDS design and the specific charges referred to above.

The settlement does not include:-

- Any settlement of the issues forming **tie's** counterclaim. **tie** can return to this should the need arise in the future.
- Any settlement of **tie's** claims in respect of failures to deliver adequate and timely designs for the MUDFA programme. It is proposed that these are dealt with as part of the SDS final account.
- Any compromise of **tie's** position in respect of any potential future failure to deliver.

**5.0 Benefits of Proposed Settlement**

The benefits of the draft settlement are:

- Avoids, or at least, minimises the opportunity for Infracore to pass SDS performance risk back to **tie**.
- Recognises and recompenses SDS for the valid elements of their claim.
- Settles outstanding historical charges.
- Includes payment in respect of the unbudgeted (but valid charges) in respect of the implementation of the VE changes at the depot and in respect of the EARL bridge (**tie** value of these changes £380K).
- Settlement represents a significant reduction in SDS's expectation and a £0.65m saving against the current budget:-

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	tie settlement (£m)	SDS Expectation (£m)	Difference (£m)
Historical Charges	0.55	1.10	
3 Additional items (VE and MUDFA support)	0.48	0.76	
Claim		2.86	
Totals	2.50	4.26	
Budget	3.15	-	-
Saving on Budget	0.65	-	-

- Provides incentivisation for SDS to deliver to the current programme by deferring payment of substantial sums to the completion of key designs stages. Thus:
  - Incentivise support and alignment with the procurement and construction programme.
  - Keeps open the set-off of settlement sums against any tie claims for any potential future failure in performance.
- Keeps open the option of parrying tie's counterclaim at a future date in the event of failure to perform.
- Avoids disruption and distraction to the project at this critical time.

#### 6.0 Mitigation of future failure by SDS

Whilst SDS's claim that their difficulties in delivering design to programme are now resolved with the resolution of critical issues, there remains the possibility of future failure. Any such significant future failure would result in delay to the procurement programme and subsequent construction programme.

To mitigate against such failure the following are proposed:-

- Intensive monitoring of SDS's delivery programme on a weekly basis to identify any slippages. This provides the earliest opportunity to resolve the issues causing such delay.
- Moratorium on changes to the design along the alignment, unless part of the VE programme.
- No further optioneering of the design along the alignment.
- Put the design of structures that are subject to realisation of VE opportunity on hold, pending development of alternatives with bidders.
- Implementation of the planned due diligence by Infracore to identify and XXXX in the SDS design at an early stage.

#### 7.0 Recommendation

- 7.1 It is recommended that the Board authorises the Project to proceed on the basis outlined above.

Prepared by: Geoff Gilbert, Project Commercial Director

Recommended by: Matthew Crosse, Project Director

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Date: 14 August 2007

Approved ..... Date:- .....  
David Mackay on behalf of the Tram Project Board