

Paper to: TPB **Date:** 14 August 2007
Subject: SDS Commercial Issues Resolution – Update on way forward
Agenda item:
Preparer: Geoff Gilbert

1.0 Introduction

- 1.1 The Board paper dated 9 August 2007 seeking authority to negotiate a settlement with SDS was not approved at the last Tram Project Board. The main reasons were:
- The contract was awarded to SDS based on a proffered capability that they had the ‘toolkit’ (experience, processes, strength and depth of management and design personnel) to deliver the scheme. This has not been evident in their delivery of the design services.
 - Will the approach to settlement take sufficient cognisance of **tie**’s potential counterclaim against SDS
 - A lack of confidence in SDS’s capability to consistently deliver to any agreed programme.
 - Lack of clarity on what **tie** will or can do to manage and mitigate the design delivery risk between now and the point at which novation occurs (Financial Close). This includes opportunities for de-scoping SDS works.
- 1.2 These issues were discussed at the **tie** Exec Meeting on 14 August 2007 and a proposed way forward developed.

2.0 Proposed way forward

- 2.1 The **tie** Exec concluded that:
- If possible, a commercial settlement should be negotiated by the end of August and that this should take due account of **tie**’s potential counterclaim. This recognises that SDS have a valid entitlement on two counts:
 1. Delays to the approval of Preliminary Design and
 2. The failure to resolve the critical issues in a timely manner.
 - An initial formal response to their claim should be made to SDS, to protect **tie**’s longer term position if a commercial settlement does not produce an acceptable result.
 - There is major risk to programme and budget if the commercial situation results in adjudication and legal proceedings.
 - Termination of SDS and subsequent replacement of SDS could potentially add up 12 months in view of the tender, mobilisation, learning, ramp up and dealing with interfaces and partially completed design packages. This would apply irrespective of whether it was a **tie** or Infracore appointment.
 - A high level summary of the grounds for a potential counterclaim has been generated, but the production of the evidence to support this has not. This would take many weeks of effort and distract commercial staff from other critical activities. This would risk other procurement programme objectives. (A decision was taken in May to make the preparation of a detailed counter claim a lower priority).

- Opportunities for reducing SDS's scope is to be explored - see statement.
- Potential for Infraco bidders taking on certain aspects of the design is also to be considered.
- A persistent breach notice needs to be issued to SDS to protect **tie**'s future contractual position in the event that an improvement in design delivery is not realised.

2.2 The position in respect of **tie**'s counterclaim was summarised at the meeting as follows:

- The heads of a counterclaim are:
 - Delay in signing the SDS contract
 - Delay in completing Requirement Definition Phase
 - Preliminary Design Performance
 - Utilities Design Performance
 - Failure to provide adequate standard of management that is reasonably expected of an organisation of PB's stature to deliver the services procured under the SDS contract.
- The potential value of the counterclaim is over £15m consisting of the cost of **tie** Project overhead and the theoretical impact on Infraco and Tramco contract costs of delays to the design programme (i.e. the additional inflation costs)
- The risks in successfully pursuing a counterclaim formally are:
 - Whilst the delays to the design process 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.
 - That, given the magnitude of the claim, SDS 'walk away' from the Project and leave the designs incomplete or that their performance drops further.
 - 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.

3.0 Actions

3.1 To implement the above the following actions are proposed:

1. Negotiations to agree a figure in principle are progressed. The potential **tie** counterclaim heads and values will be deployed to minimise the settlement figure. Incentivisation mechanisms to be negotiated into the settlement as outlined in the Tram Project Board Paper. Settlement proposals are to be presented to the Tram Project Board Procurement Sub Committee before formalisation. This is to be progressed with a view to concluding by the end of August. Action – Geoff Gilbert
2. Formal contractual communication to SDS in respect of:
 - A. **tie** counterclaim,
 - B. Response to SDS claim and
 - C. Persistent breach notice.

The persistent breach notice is to be based on failure by SDS to provide adequate standard of management that is reasonably expected of an organisation of PB's stature to deliver the services procured under the SDS

contract. A and B to be drafted by DLA and issued next week, dependent on the outcome of the negotiation discussions to be held this week. C to be issued next week regardless of the outcome of the discussions. Action – Geoff Gilbert supported by Andrew Fitchie.

3. Opportunities (and costs and risks) to reduce SDS design scope to be identified in respect of:
- o Structures that will be subject to change under VE
 - o Remaining utilities designs
 - o Other elements that bidders will do themselves in any event e.g. OLE, power, comms and system integration.

Report to be prepared in respect of the above which sets out the viable de-scoping, taking account of bidders differing positions on design, potential additional cost and potential impact on programme. To be prepared for the next Tram Project Board. Action – Steven Bell.

4.0 Recommendation

- 4.1 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

Date: 14 August 2007

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