

Bilfinger Berger Siemens CAF Consortium  
9 Lochside Avenue  
Edinburgh  
EH12 9DJ

Our Ref: INF CORR 5859

Date: 24<sup>th</sup> August 2010

**DELIVERED BY HAND TO MR KITZMAN**

**STRICTLY CONFIDENTIAL – LEGALLY PRIVILEGED AND FOISA EXEMPT**

Dear Sirs,

**Project Carlisle – Proposal for discussion and finalisation**

We confirm that your letter dated 29 June 2010 (reference 25.1.201/RJW/6133) does not form a basis on which the process we jointly refer to as Project Carlisle can be concluded. After preliminary discussions held in May of this year we set out an outline of the scope and terms that would enable us to jointly implement the best options referred to by Mr. Kenneth Reid in his letter to our Chairman on 5 March 2010.

Despite the disappointment of receiving your letter in late June, we have been encouraged by the involvement of Mr. Ed Kitzman in agreeing and contributing to the content of our letter dated 22 June 2010 (reference INF. CORR. 5410) and his being actively and constructively involved in the work we have pressed forward with since receiving your letter. We are pleased to note that when he met Mr. Anthony Rush and Mr. James Molyneux on 17 August he was broadly in agreement with the outline explanation given to him which described the scope and reasoning of what we set out below and the programme for bringing this matter to a conclusion.

We have on a number of occasions expressed our appreciation of Mr. Kitzman – we would add that he has also given our stakeholders confidence that the Infraco Consortium can deliver an Edinburgh Tram Network whilst maintaining the integrity of the Infraco Contract.

Our proposal, referred to as **The Guaranteed Maximum Price tie Change ("GMP")**, is explained by this letter and the draft documents attached hereto. They are without prejudice to our rights under the Infraco Contract and in Law and the proposal cannot be founded upon by the Infraco Parties or any other parties in any proceedings, or be construed to be an offer (either in part or in whole) capable of acceptance without our expressed agreement in writing. Any agreement which arises from this letter will be subject to a Deed of Variation approved by a Minute of the Limited's Board. Moreover, our proposal cannot be construed as implying the Limited's admission of any liability to the Infraco Parties or the Limited's waiver of any rights or claims against the Infraco Parties.

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## Governance and Guiding Principles

Acknowledging that after 28 months there have been circumstances which were excluded from the Contract Price - arising from Specified Exclusions, Provisional Sums, Pricing Assumptions and the requirements of third parties and **tie** - the objective of Project Carlisle is to put the parties into the position in which they would have been at May 2008, had such changes been known at the time. In doing so we are *inter alia* governed by the Ethical Standards in Public Life etc. (Scotland) Act 2000 - Model Code of Conduct and EU Procurement Law. What we agree with the Infraco has to be in the public interest. Moreover, it has to protect the integrity of the Infraco Contract arrived at after an advertised competition. Moreover, as far as we can, we have satisfied ourselves that had the original tender been based on what we propose it would not have altered the outcome of the pre-qualification and tender processes.

You will be well aware that from the outset there were expectations by some that the Infraco Contract gave certainty of out-turn cost. Whether such expectations were realistic or not is not material to us here other than to emphasise that after 28 months it is wholly reasonable to expect, and indeed require, the Infraco to agree to giving **tie** (and thereby the Public) price certainty. Consequently our proposal extinguishes the Infraco's ability to claim for additional payments arising pursuant to Schedule Part 4 of the Infraco Contract. Moreover, with the exception of certain enabling works to the Edinburgh Gateway Project (formerly known as Gogar Interchange), **tie**'s ability to vary the scope of the Infraco Works will be limited to it being necessary for the satisfactory and contractually compliant completion of the Infraco Works.

## Arriving at a revised Contract Price

Factually, the Infraco has not substantiated sufficient of its purported claims for additional payment under the Infraco Contract for such substantiation to be used as a basis for coming to a revised Contract Price. We have therefore, in addition to attempting to put the Parties back to where they would have been in May 2008, broadly adopted the following principles:

1. Hadley & Baxendale - payments which may fairly and reasonably be considered as either arising naturally in the normal course of things, or may reasonably have been contemplated by both Parties when they entered into the Infraco Contract.
2. Without admitting that **tie** is in default, referring to the principles articulated under Clauses 88.8.1 to 88.8.4 of the Infraco Contract when determining fair value.

In considering all of the issues, we have decided that the following items are to be excluded and should be subject to separate investigation and negotiation:

- All works executed under or in connection with the Princes Street Supplemental Agreement.
- Any payment to the SDS Provider and/or liability of the SDS Provider.

## Proposed revised Scope

The Infraco Works are to be separated into two parts:

- Part A**      Airport to Waverley Bridge
- Part B**      Waverley Bridge to Newhaven

### Part A – Airport to Waverley Bridge.

With the exception of those works detailed in Appendix B, completion of the Infraco Works in Part A is to be executed by the Infraco in accordance with the revised Sectional Completion Dates explained below.

For Part A, the Infraco will be required to deliver no more than 20 Trams

### Part B – Waverley Bridge to Newhaven

At its absolute discretion **tie** may instruct the Infraco to carry out the Infraco Works (excepting those omitted Civil Engineering Works) between Systems Points and to deliver the remaining 7 Trams.

Our proposal is based on the premise that the Infraco will not be required to carry out any further Civil Engineering work east of Haymarket, other than completing the Enabling Works in Section 1A and correcting defects between Lothian Road and Waverley Bridge. Our reasoning includes:

- The Infraco Members have expressed a strong desire not to carry out any Civil Engineering works east of Haymarket.
- At the present time, subject to programming for traffic management and embargo restrictions, the Infraco could be carrying out work to all but approximately 1 kilometre of On-street trackwork.
- To date the Infraco Parties have failed to issue an assured integrated design for the track and track foundation which has been approved by the Roads Authority and competent to achieve no objection from the Independent Competent Person.
- We have no confidence that the Infraco Parties, including SDS, have sufficient experience to produce such a design which represents best value, taking account of whole life costs.
- The work carried out in Princes Street is defective. The defects suggest that the Infraco Parties do not have adequate knowledge of the DMRB and local materials. The Infraco has failed to produce a remediation plan and **tie** has had to consequently issue a Remediable Termination Notice pursuant to Clause 90.1.2.
- Moreover, the defects suggest that the Infraco Parties do not possess the skilled resources and supervision required to satisfactorily complete 7.5 km of On-street work to sensitive city streets.
- The Infraco's behaviour when coming across adverse conditions is contrary to the spirit of co-operation and expediency required for such work.

### **Revised dates for completion, liquidated damages, programme etc.**

The Infraco has made no properly detailed submissions for extension of time other than in respect of Rev 1 and MUDFA Rev 8. The former has been granted and Robert Howie QC has determined by adjudication the Infraco's entitlement in respect of the latter. We also note that **tie** offered a global nine months' extension of time on 13 November 2009.

We have decided therefore that it would be fair and reasonable, taking account of the circumstances explained below, to set new Sectional Completion Dates where Robert Howie has determined them (albeit not finally binding on the Parties) with the exception of where he has decided that the Infraco has no further entitlement. For those sections we set them in accordance with **tie's** letter of 13 November 2009.

The revised Completion Dates for Part A become:

Section A	Set by Robert Howie QC	2 November 2010
Section B	Set by <b>tie</b> letter dated 13 November 2009	1 April 2011
Section C	Set by <b>tie</b> letter dated 13 November 2009	1 December 2011
Section D	Set by <b>tie</b> letter dated 13 November 2009	6 June 2012

### Programming

In relation to the revised Infraco Works from the Airport to Waverley Bridge, other than requiring you to meet the above dates we see no reason why at this late stage we should not revise the requirements of Clause 60 in relation to Schedule Part 2 (Employer's Requirements) and we have put forward suitable changes to these provisions in the attached draft **tie** Change Order.

To assist you in meeting the revised Completion Date for Section D we are prepared to discuss with you measures which will allow us to reduce the period between the completion of Section C and Section D. Such measures may require giving us partial access to Section B works; storing and reducing the number of trams delivered as part of Part A Scope.

Access for the Infraco to carry out the Infraco Works from Waverley Bridge to Newhaven will be at the absolute discretion of **tie** and subject to individual programmes between "Systems Points" which are consistent with systems control, power supply, tramstops and parking for "dead" trams. It is our intention to establish a temporary System Point at St Andrews Square.

### Liquidated Damages

As the calculation of losses reflected in Liquidated Damages will not be less for a truncated project, Liquidated Damages for Sectional Completion of Part A remain as stipulated by Clause 62 of the Infraco Contract. We will set Liquidated Damages for Part B at the anticipated cost of maintaining traffic management and direct supervision for the individual programmes of works to be carried out between Systems Points.

### **Excluded Items**

#### Works executed to Princes Street (Lothian Road to Waverley Bridge)

Final agreement of the costs claimed by the Infraco arising from the Princes Street Supplemental Agreement will in any event not be possible until the Infraco and **tie** have agreed a Remediation Plan which is approved by the Roads Authority. In the meantime, **tie** will continue to pay, on-account, the amount currently certified as an interim payment, under reservation of being able to reduce such payment on a final conclusion as to liability.

## SDS Provider

We are puzzled by your inclusion of the SDS Provider's claim for a payment of £16.275 million. It leads us to conclude that it deserves further investigation. We intend therefore to carry out a detailed investigation and audit of how the SDS Provider has performed and how the Infraco has managed them. Part of that investigation will take account of the agreement you admit has been entered into between Bilfinger Berger (and possibly others) with Parsons Brinkerhoff (and possibly others).

Until such time as we are able to come to a conclusive decision on the liabilities owed by us, or owed to us, we intend to agree to no further payment for the SDS Provider. Moreover, we reserve our rights to pursue any of the Infraco Parties (either individually or jointly) for recovery (under the Infraco Contract or in delict) of any losses and damages suffered by **tie** and arising from breach of contract, negligence, misrepresentation or any other wrongful act on the part of the SDS Provider or any other Infraco Party in relation to the services provided by the SDS Provider.

The SDS Provider and the Infraco are required to fulfil their obligations to deliver the design services relating to Phase 1b. In the event that they fail to do so, **tie** will recover the amounts previously paid to the SDS Provider for these services from payments due to the Infraco.

For the purposes of the GMP, Clause 61.8 will be deleted.

## **Conditions**

Any Agreement arising from this proposal will *inter alia* be subject to the following conditions:

- The Infraco shall procure such design assurance as is necessary for the Independent Competent Person to admit a design for the On-Street trackwork which is approved by and meets the requirements of the Roads Authority and of **tie** acting with absolute discretion.
- The completed, approved, assured, integrated and compliant Design for the Edinburgh Tram Network Phases 1a and 1b, will include certification thereof by each Infraco Member, the SDS Provider and any Infraco Party or SDS Provider Party involved in the production or development of Design or the Infraco's Design.
- The Infraco shall be responsible for all additional costs which may arise from any development or revision to the design of the Infraco Works other than as required by a **tie** Change.
- The Infraco shall be entitled to the benefits of any value engineering savings achieved from the date of the Agreement.
- The Infraco shall not be entitled to extension of time to the revised Sectional Completion Dates for Sections C and D unless:
  - a **tie** procures and completes the Civil Engineering Work from Haymarket to Lothian Road in such time as would prevent the Infraco, working reasonably in Designated Working Areas, from achieving those revised Sectional Completion Dates; and
  - b **tie** issues a Change Order pursuant to revised Clause 80.

- The On-street Civil Engineering works shall be completed by others under the direct supervision of **tie**. Other than providing design assurances in respect of the design of such works as directed by **tie**, the Infraco shall have no liability for such works. However, the Infraco shall be responsible for integrating the design of the E&M Works with the On-street Civil Engineering works.
- The Infraco shall be responsible for those Trams which have been constructed and commissioned pursuant to the Tram Supply Agreement but which are not required to run on the Edinburgh Tram Network which is constructed under the GMP Scope. The revised Contract Price shall include for any and all storage charges, in Spain or elsewhere, or any other costs and expenses related to the spare Trams which have arisen and may arise as a consequence of delay to the completion of the Infraco Works.
- The Infraco shall deliver to **tie** all information required by the Infraco Contract for all Key Sub-contractors the Infraco intends to employ on the Infraco Contract.
- The Infraco Parties shall disclose all agreements which they have entered into together since 14 May 2008, howsoever arising and which they would have not entered into but for their involvement in the Infraco Contract.
- Pursuant to Clause 26 the Infraco will submit for **tie**'s approval full details of the experience and qualifications of the Infraco Representative and such approval shall be at the absolute discretion of **tie**.
- Only persons nominated as Key Personnel shall have day-to-day responsibility for and be involved in the performance of the Infraco Works.
- The Infraco shall design, carry out and complete enabling works for the Edinburgh Gateway Project at a reasonable price and use reasonable endeavours to complete such works without causing delay to the completion of the revised Infraco Works - Part A.
- The Infraco shall install On-street trackwork to Part A and Part B in accordance with the Infraco Contract and subject to **tie** issuing the Infraco with 14 days' notice to commence work and in accordance with the following provisions:
  1. Providing, taking from store, delivering to site, permanently installing in accordance with the assured integrated design approved pursuant to Clause 19 and by **tie**, in accordance with a reasonable programme agreed by **tie**, track rails and their supports and sleepers on a foundation prepared by others.
  2. The Infraco shall provide and permanently install in accordance with the said design composite packers to the rail flanges prior to handing over the installed track to **tie**.
  3. Other than for its design, the Infraco will bear no responsibility for the foundation to the track, or for any of the omitted civil engineering works subsequent to the installation of the track.
- **tie** shall be entitled to instruct the commencement of all or part of the Part B works at any point up to, but not later than, five years from the date that **tie** issues a Sectional Completion Certificate pursuant to Clause 44.3 of the Infraco Contract for Section D under Part A of the GMP Scope of Works.

- For the purposes of section 2.7.4 of the Employers Requirements, the required maximum journey time for St Andrews Square to the Airport will be 28 minutes, 53 seconds.

### Revised Contract Price

The revised Contract Price, which comprises the total capital expenditure and revenue expenditure payable to the Infraco, including for all entitlements to additional payments (both agreed and not agreed) up to the date of the Deed of Variation, is as follows:

<b>Part A</b>	<b>£</b>
Construction Works Price Part A	216,492,216
SDS Price	To be determined
PSSA Payment	To be determined
Tram Supply Price	45,893,997
Infraco Maintenance Mobilisation	1,633,522
Tram Maintenance Mobilisation	2,275,806
Infraco Spare Parts	1,013,090
<b>Part B</b>	<b>£</b>
<p>Construction Works Price Part B (subject to Prolongation Costs and interim payments for materials as below). The price for each of the following sections shall be subject to separate payment mechanisms for trackworks and other works:</p>	
<p style="padding-left: 40px;">Waverley Bridge to St. Andrew's Square</p>	
<p style="padding-left: 40px;">St. Andrew's Square to York Place</p>	
<p style="padding-left: 40px;">York Place to Foot of the Walk</p>	
<p style="padding-left: 40px;">Foot of the Walk to Ocean Terminal</p>	
<p style="padding-left: 40px;">Ocean Terminal to Newhaven</p>	
Part B Sub-Total	22,595,033
SDS Price	To be determined
Tram Supply Price	9,887,637

Infraco Maintenance Mobilisation	Included in Part A
Tram Maintenance Mobilisation	148,770
Infraco Spare Parts	Included in Part A

Prolongation Costs – Part B only

Reimbursement will be predicated on the assumption that the above rates will be subject to payment from 30 June 2012 for increases in labour and plant costs, calculated annually in line with the CPI published at each 30 June 2013, 2014 etc. (or some such other method to be agreed.)

Interim payment for materials - Part B only

The Infraco shall be entitled to on-account interim payment for materials (on-site or off-site) provided that:

- i. they are required for the purposes of the revised Infraco Works and have been subject to a binding contract for their purchase prior to the date of any Agreement arising from this proposal;
- ii. (a) the materials have been ordered and delivered prior to the date of any Agreement arising from this proposal, or (b) after the date of any Agreement arising from this proposal they are by written instruction from **tie** ordered and delivered to a location agreed with **tie**;
- iii. they are part of an integrated assured design which has been fully approved under the terms of the Infraco Contract. Such approval will include, but not be limited to, Roads Authority Approval;
- iv. **tie** agrees, acting reasonably, that title is unambiguously and irrevocably jointly in the names of **tie** and the City of Edinburgh Council and their assignees and successors;
- v. where it is necessary to vest the ownership it will be in the name of the City of Edinburgh Council and the materials will be stored separately and identified clearly as being the property of the City of Edinburgh Council;
- vi. the Infraco insures and keeps insured with a reputable insurer all materials against loss, damage (however so arising) and theft;
- vii. the on-account advance payment will not exceed 70% of its certified invoiced cost less a reasonable allowance for shipping and delivering the materials to Site;
- viii. an Infraco Party will provide an On-demand Guarantee or Insurance Bond in favour of **tie** and The City of Edinburgh Council to the full value of the vested materials plus an allowance for their shipping and delivery to site; and
- ix. notwithstanding the Dispute Resolution Procedure, any disputes or differences arising in connection with interim payments for materials will be decided at the absolute discretion of **tie**.



## **Milestone Payments**

Subsequent to agreement of the revised Contract Price, Construction Milestones will have to be agreed from which interim payments may be determined.

The opening values should be calculated:

- Construction - as previously certified less any payment for PSSA and the SDS Provider;
- Preliminaries recalculated as a proportion of Construction Milestone values.

Interim values will be calculated:

- Construction Milestones – as and when completed
- Preliminaries – pro-rata to the difference between the opening value calculated above and the total value of Construction Milestones shown above.
- Any overpayment or underpayment at opening shall be adjusted over a 12 month period at monthly tranches.

## **Bonds & Guarantees etc**

There will be no revision to the Infraco's obligations pursuant to Clauses 74 to 78 inclusive.

## **Maintenance Agreements**

We do not propose amending the terms of the Infraco Contract or Tram Maintenance Agreements other than to reduce the separate payment for each of Part A and Part B on a pro-rata basis to the number of Trams delivered or length of track commissioned.

## **Reaching an Agreement**

Whilst the involvement with Mr. Kitzman will have ironed out many of the points of difference which may otherwise have existed in relation to the revised scope and terms, we recognise that there are still some issues we have not discussed with him. Mr. Kitzman has given us good access to the cost base for future Civil Engineering Works and we have based our pricing proposal on the information given to us. We have also had constructive discussions with him about design and future management of the project which has guided our proposal.

However, you have made it clear to us that Mr. Kitzman is only acting in the capacity of, as you put it, a "point of contact". In our eyes he does not have the authority to reach a final agreement on behalf of all Infraco Parties. Lessons were learned by **tie** and its stakeholders back in May 2008 at the time the Infraco Contract was entered into. Stakeholders in **tie** are clear that there can be no repeat of "last minute" changes in terms and price by the Infraco. It is essential therefore that we work together to the timetable outlined to Mr. Kitzman on 17 August and that the Principals involved are acting as members of and with the full authority of the relevant Parent Company Board responsible for the Infraco Contract.

## Timetable

Activity	By whom	When (2010)
Explain Scope	Joint PC Teams	Done
Finalise and issue Counter Offer	tie PC Team to Infracore PC Team	24 August
Meet and discuss Counter Offer	Joint PC Teams	25 – 28 August
Revise Counter Offer (If required)	Joint PC Teams	29 August
Meet to finalise price and outstanding terms	Principals and advisors	By 3 September
Agree HOTs	Companies and legal advisors	8 September
Finalisation	Companies	15 September

Our proposal builds on Mr. Reid's expression of mutual interest in finding "*if at all possible, a common way forward under the terms of the contract*". Under the explanation we give above of the guiding principles which govern that common way forward, we believe that what we propose achieves Mr. Reid's ambitions and provides for the mandatory and irrevocable requirements which are needed to satisfy our duties as a publicly accountable body.

We look forward to reaching an agreement in the spirit of goodwill and cooperation established by our respective Project Carlisle teams.

Yours faithfully,



Richard Jeffrey  
Chief Executive

For and on behalf of tie Limited