

From: John Nicholls
Transport Scotland
13 September 2017

Cabinet Secretary for Finance and the Constitution
Minister for Transport and the Islands

FERGUSON MARINE ENGINEERING LIMITED CMAL AND MEDIATION

Purpose

1. To provide Ministers with background briefing in advance of Mr Yousof's proposed meeting with the Chair and Chief Executive of Caledonian Maritime Assets Ltd (CMAL). The meeting has been called to discuss CMAL's concerns regarding the proposed mediation process between CMAL and Ferguson Marine Engineering Ltd (FMEL) as a means of resolving the on-going contractual dispute between CMAL and FMEL.

Priority

2. Urgent – an early meeting with CMAL will enable Ministers to get a better understanding of their position and may help to forestall further representations from CBC/FMEL.

Background

3. Ministers will be familiar with the on-going financial challenges facing FMEL and the recent package of measures put together by the Scottish Government to offer continued financial support to FMEL in the form of a commercial loan. Ministers will also be aware that the only significant orders on FMEL's books are for the construction of two large ferries for CMAL for subsequent deployment on the Clyde and Hebrides ferry services network. FMEL has on-going contract variation claims against CMAL in relation to these orders totalling some £17.5m. CMAL disputes these claims.

4. As part of the financial support offer from the Scottish Government to FMEL, it was made clear to Jim McColl that the package of measures was conditional on three points, one of which was a "*commitment to a mediation process in relation to the CMAL contracts in line with the relevant provision set out in the contracts*". In preparation of the written offer to Mr McColl, Transport Scotland officials spoke to senior representatives of CMAL to ensure that they were content with that approach. It was confirmed in discussions that "mediation" is one of the permitted contract dispute resolution mechanisms available in the contract between FMEL and CMAL. While CMAL made it clear that the "mediation" mechanism wasn't their preferred route, they indicated they were content for the Scottish Government to write to Mr McColl in these terms.

5. In response, FMEL subsequently wrote to CMAL on 31 August indicating their request to CMAL to enter into a mediation process. To date, CMAL have not yet replied to that letter, at our request, pending the resolution of matters discussed in the remainder of the submission.

6. Since the loan agreement was put in place between SG and FMEL, the CMAL chair, Erik Ostergaard has indicated that they are not content to go down the mediation route, preferring one of the other two dispute resolution mechanisms in the contract, namely;

- Expert Determination, or
- Commercial Court of the Court of Session in Edinburgh.

Both of the above mechanisms are binding on the participants. In terms of timescale, expert determination should be available within 5-6 weeks, whereas court proceedings would take much longer.

7. CMAL's views in recommending either of the other two alternative mechanisms are,

- the mediation process is non-binding, whereas both other routes are binding.
- the perceived weaknesses, in CMAL's view, of the FMEL case and CMAL's fundamental disagreement of the validity of FMEL's variation to contract claims mean that any "mediation" process is unlikely to reach a mutually satisfactory resolution.
- following on from that, in CMAL's view, a process of mediation would be a significant distraction and ineffective use of FMEL's, and CMAL's resources, and likely cause damage to the fragile relationship that currently exists between FMEL and CMAL.

8. [Redacted]

9. Transport Scotland officials have discussed this with the CMAL Chair and CEO to emphasise the likelihood of a negative reaction from FMEL and CBC, and the low risks involved in the non-binding mediation process. The CMAL Chair remains adamant that he will not support a move to mediation. Liz Ditchburn will be speaking to the CMAL Chair tomorrow (Thursday 14 September) and will update Ministers as necessary following that call.

Way Forward

10. The proposed meeting between Mr Yousaf and Erik Ostergaard, Chair of CMAL and Kevin Hobbs, Chief Executive of CMAL, provides the opportunity for Ministers to hear CMAL's views first hand, and, if appropriate, re-emphasise the need for CMAL to

engage in the mediation process with FMEL. It is clearly important for all parties involved to honour the commitments in correspondence between the Scottish Government and FMEL. Clearly all of this is tied to ensuring the continued viability of FMEL as a way of protecting jobs and the local economy in Port Glasgow and to ensure delivery of these two new vessels for deployment on the Clyde and Hebrides ferry network.

11. From a Scottish Government / Transport Scotland perspective, it is difficult to see what CMAL have to lose from entering into a mediation process with FMEL. Given the process is non-binding, neither CMAL nor FMEL will be bound by the outcome. It is understood that some of CMAL's frustrations relate to concerns that the mediation process will be influenced by Mr McColl making parallel representations to Scottish Ministers with the aim of forcing CMAL to agree to contract variation claims that, in CMAL's view, are not substantiated and would represent an unjustified use of public money. The view of Scottish Government and Transport Scotland is that should the proposed mediation process between FMEL and CMAL not yield a successful outcome, then that process would still have some merit, notably,

- keeping all sides talking
- it is Scottish Government policy for disputes to go through a process before going to arbitration or court
- if it ended up in court then the courts would expect those in dispute to have previously sought to reach agreement in some other way
- mediation is an opportunity to draw out the other sides arguments that can be useful in any subsequent court case.

12. It is hoped that discussions between Scottish Ministers and the CMAL representatives will be sufficient to allow CMAL to subsequently indicate to FMEL their willingness to enter into a mediation process. [Redacted]

Meeting with Mr Yousaf

13. Mr YOUSAF's office is in the process of agreeing a date for the meeting with CMAL, and our advice is that this should happen sooner rather than later. CMAL will be represented by their Chair, Erik Ostergaard and Chief Executive, Kevin Hobbs. Supporting officials will be DG Economy Director Liz Ditchburn, Roy Brannen, Chief Executive of Transport Scotland and John Nicholls, Director of Aviation, Maritime, Freight and Canals in Transport Scotland

John Nicholls

Transport Scotland

Ext [Redacted]

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Copies to:

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