

CALL BETWEEN CABINET SECRETARY FOR FINANCE, ECONOMY AND FAIR WORK AND LUKE VAN BEEK

23 APRIL 2019, 13:15 to 13:45

Participants

- SG: Derek Mackay MSP, Stewart Maxwell, [REDACTED] Richard Rollison and [REDACTED]
- VATIS Limited: Commodore Luke van Beek CBE

Purpose

- An opportunity to hear Commodore van Beek's observations on the dispute between Ferguson Marine (FMEL) and CMAL; to get his impartial advice around potential ways to address the situation; and to consider steps that can be taken now to mitigate matters.
- Luke is the independent operational expert who advises SG in relation to the drawdown of the £30 million SG loan to FMEL.

Luke's observations

- Luke had been engaged by Economic Development Directorate to provide independent assurance in relation to drawdown of funds against SG's £30 million loan to Ferguson Marine. He had visited the yard on a number of occasions since last June, forming the view that Ferguson's is working well day-to-day and is a competent, well-managed shipyard.
- Luke observed that ferries are not essentially difficult to build but the addition of LNG has introduced complexity. However, the yard has experienced problems with the delivery of its contracts for CMAL (two LNG-hybrid ferries) due to a poor contract and a deteriorating relationship with CMAL. Cash flow problems have been an ongoing concern compounded by the delayed schedule.
- Luke has formed the view that the quality of FMEL's work is good although he acknowledges the situation at the earliest stages of the contract may have been different (e.g. the yard's handling of change issues).
- The most pressing issues since last November have been (a) cash flow linked with delayed payment of the SG loan, which has caused significant non-linear slippage in the programme, and (b) the lack of any productive dialogue between the contracting parties.
- Luke acknowledged that the contract dispute has 'two sides' and he felt the yard had not always responded well to design and contract challenges but had worked hard to recover from earlier difficulties.

- Luke has proposed in his written and oral reports to Transport Scotland from last September that a fundamental examination of the contracting relationship between the parties was required. He also recommended a design freeze and open collaborative discussion around the risk register and programme. To his knowledge no such discussions had taken place and the relationship between FMEL and CMAL has become increasingly difficult. Negotiation between the two now appears impossible and this is making any progress on the project extremely difficult.
- In terms of a way forward, Luke's considered view was that a negotiated settlement has the greatest potential of the options under consideration to deliver the two ferries at lowest cost, in the shortest time and with the least impact on the workforce.

Discussion

- Mr Mackay said Ministers are concerned greatly at the prospect of redundancies at the yard and their impact. The Government's strategic priorities have not changed but the lack of progress between the contracting parties and the likelihood of a significant redundancy announcement on Friday 26 April necessitated fresh thinking and the rapid development of a clear plan.
- The Cabinet Secretary sought Luke's view on the basis for a contract negotiation and the limitations of such a course – can the contract terms or value be modified?
- Luke indicated that the priority focus now should be to agree a time and price for the future work as a basis for the yard's continuing work on the contracts. He pointed out that the contract had already been significantly amended (capability and time) and, whichever option is adopted, the contract will require amendment to take account of actual progress. And if, for example, the business entered receivership or was nationalised CMAL would be forced to renegotiate terms to secure completion.
- The introduction of an expert, independent of both FMEL and CMAL, could help with the process of agreeing the time / price of the work to completion of the vessels. For clarity, the independent expert role Luke envisaged was not standard arbitration but something more facilitative.
- Luke had already proposed several actions that could mitigate risk in the ferries programme but he thought there could be more. As an example, he believes plans to commission the LNG system in vessel 801 should be delayed until the shore side fuel bunkering is in place. This action would save time and cost now with little or no operational impact.
- The Cabinet Secretary highlighted the need for strict legal compliance on any options pursued in relation to potential contract amendments and said he was open to considering whether CMAL's client position could be changed as a corporate decision, informed by independent advice.

- The Cabinet Secretary asked Luke if he felt FMEL's claims of unwarranted client interference in the build process were justified; if they rang true to him based on his interaction with the parties and his time spent at the yard. Luke said his experience supported FMEL's position and he believed the client had made many changes to the design and on occasion failed to take decisions promptly. That said, Luke also observed that FMEL had not stood-up to CMAL robustly enough in handling change requests.

- Mr Mackay made it clear that the approach described does not in any way match with the objectives of this project or of Scottish Ministers. Ministers are supportive of the business and the workforce and are concerned at the prospect of any redundancies at the yard.
- Given Luke's comments on the poor state of the relationship between the contracting parties, Richard asked him whether in his view the build contract could be managed by a body other than CMAL and what difference that might make. Luke thought SG should consider taking over the contract (for at least 801) and involve the eventual operator of the vessels (CalMac) in taking decisions on the programme and delivered capability. CMAL had had the option to sit down with FMEL and agree a negotiated settlement but had refused to do so. They appeared resolute in their position that the dispute could only be addressed via the courts.
- If a new time, cost and capability plan for the vessels required some changes (and potential comprises) to the design of the ferries then CalMac, as operator of the vessels, would be well-placed to provide assurance that the vessels remained 'fit for purpose' and to ensure that no operational issues were overlooked.
- The Cabinet Secretary expressed his deep concern for the state of the FMEL-CMAL relationship and the potential consequences of the breakdown. He was aware that FMEL was contemplating large imminent job losses and was conscious of the direct damage that such a step would cause to the CMAL order and wider impacts and cost implications.

Actions

- The Cabinet Secretary felt FMEL would not easily recover from large-scale redundancies and asked officials to:
 - agree the meeting note with Luke van Beek and confirm his statement on CMAL's strategy;
 - prepare urgent advice to the First Minister on options to avoid redundancies at FMEL; and

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