

Edinburgh Tram Project – Update Report

The City of Edinburgh Council

24 June 2010

1 Purpose of report

1.1 The purpose of this report is to update the Council on the progress of the Edinburgh Tram Project and related issues including:

- the current contractual difficulties with the Contractor, the Bilfinger Siemens CAF Consortium (“BSC”) (in particular regarding agreed scope and progress of the civil engineering and infrastructure installation works);
- the approach adopted by **tie Limited (“tie”)** to achieve acceptable resolution of the matters in dispute;
- budget, scope and programme implications;
- the Council’s funding strategy (including contingency planning);
- communications with stakeholders; and,
- a summary of the status of on-street utilities diversion works.

1.2 The governance arrangements for the tram project ensure that regular communications between **tie**, Council officers, Transport Scotland and Scottish Ministers on the progress of the project take place. The Operating Agreement in place between the Council and Transport Edinburgh Limited (TEL) requires that the Council must be made aware when there is a reasonable expectation that the approved price, programme or scope of the project may change. TEL has now advised the Council’s Tram Monitoring Officer that this point has been reached. However, at this point in time TEL is not seeking additional funding.

1.3 In view of the importance of the project to the city and the ongoing difficulties being experienced with the contractor, it is considered extremely important to place as much information in the public domain as commercial and contractual considerations allow.

2 Summary

2.1 A report was provided to the Council meeting of 20 August 2009 which resulted, *inter-alia*, in endorsement by the Council of the contractual processes on which **tie** had embarked with a view to achieving greater cost and programme certainty for the project. In the intervening period, **tie** increasingly has had to enforce contractual rights in its engagement with the BSC to attempt

to expedite progress on the tram infrastructure installation works and to compel action to resolve the dispute.

- 2.2 The contractual programme remains well behind the required schedule. However, there has been some degree of progress in the construction of the off-street sections of the works, particularly to the West of Murrayfield Stadium and at the Gogar tram depot. The utility diversions (carried out under separate contract) are now substantially complete, creating much-improved utility asset quality along the tram route in some of the city's main thoroughfares. Substantial utilities work beyond the original programme scope has had to be carried out and this has, in some instances, affected site access for BSC. The construction of the tram vehicles in Spain by CAF has proceeded to programme and the first vehicle arrived in the city following successful equipment trials at the Siemens test track facility in Germany.
- 2.3 However, there continue to be serious contractual difficulties with BSC. The main areas of dispute relate to design issues (including delays in design completion); the impact of delays caused mainly by utilities work and associated extension of time claims; and apparent failures to achieve progress on the works. This report provides a comprehensive update on each of these issues and their respective implications.
- 2.4 The application by **tie** of the formal Dispute Resolution Procedure ("DRP") within the terms of the contractual agreement with BSC ("the Agreement") has achieved resolution of a number of issues subjected to the process and reduced by almost 60% the amounts initially claimed by the contractor, saving circa £11m to date. However, the improvement sought in infrastructure installation productivity by BSC has not materialised.
- 2.5 Following endorsement by the Council at the end of 2009 in the absence of acceptable progress on infrastructure construction, **tie** embarked upon a more formal, contractually-led approach to its relationship with BSC in order to protect stakeholders' interests. This has involved the continued application of Dispute Resolution procedures, audit based verification of aspects of BSC's contract management and, in preparation for potential litigation, (a) detailed legal investigation of the matters under dispute; and (b) Senior Counsel's opinion on critical issues. A formal review of alternative delivery options for the project was also undertaken, including the option of terminating the Agreement.
- 2.6 Although the formal adjudications under the DRP have produced mixed results, the advice received has reinforced **tie's** interpretation of the contractual position on the key matters under dispute and has also saved circa £11m from the initial claims submitted by BSC. There has been no real breakthrough despite several months of negotiations to restore real momentum to the project. Negotiations to secure a satisfactory way forward are continuing with the benefit of significant and detailed commercial and legal support.
- 2.7 This report provides an update on the project budget, scope and developments since the last report to Council and explains the implications for the programme. It now appears that the full Phase 1a tram system cannot be delivered within the available funding envelope of £545m and the overall outcome will remain uncertain for so long as the dispute persists. Despite the

current difficulties **tie** has recently received credible external advice that a properly performing contractor should be able to have the trams open for revenue service by the end of 2012. However, while BSC remains in dispute with **tie** and progress on infrastructure construction remains unsatisfactory, it is not possible to offer certainty on the cost or programme outcomes.

- 2.8 In the period since the Council report of 20 August 2009, Council officers have reviewed contingency funding options in the event that the estimated capital costs of the project were to exceed the available funding of £545m. This report provides details of the key options and examines the Council's funding strategy and the status of its commitment of £45m towards the costs of the project.
- 2.9 As a contingency measure, **tie** has also assessed the option to deliver Phase 1a of the tram project in a series of incremental stages. Details of this assessment are included in the main body of this report.
- 2.10 Regular communication has continued throughout the past year with key stakeholders, in particular to ensure that Transport Scotland has been kept informed about all relevant issues. A series of meetings has taken place with Transport Scotland to explain the issues in dispute, to report back on negotiations with BSC and review the related budget and programme implications.
- 2.11 In summary, the status of the project remains highly unsatisfactory despite extensive and constructive attempts by **tie** to achieve reliable execution by BSC of its obligations in the Agreement. The current negotiations are focusing on options which could realise an acceptable outcome for all parties. However, in the event that this cannot be achieved, **tie** has looked at the potential for terminating the Agreement in an appropriate manner.

3 Main report

Underlying Case for Trams

- 3.1 The Final Business Case for Phase 1a of the Edinburgh Tram Network was approved in December 2008. The validity of the Business Plan approved at that time remains intact. Since 2008, when construction of tram infrastructure commenced in Edinburgh, a number of other cities in the UK have continued to develop their tram networks. Manchester Metrolink is currently planning several extensions over a period of time, while Nottingham Express Transit has two further lines planned. The initial success of the Dublin Luas tram scheme, upon operation in 2004, led to a commitment to seven future lines or extensions over a ten year period in the Irish government's 2005 Transport 21 plan. The evidence from other UK tram networks and also from Dublin is that trams are well-liked by the travelling public, enjoy excellent patronage and enhance the image of the cities in which they operate.
- 3.2 The first tram vehicle has now arrived in the city and is on public display at the tram stop on Princes Street. During the first month on exhibit there were over 30,000 visitors. Feedback so far has been largely positive with 91% of visitors surveyed stating that they were either 'impressed' or 'very impressed' with the vehicle.

Current Contractual Difficulties

- 3.3 In contrast with the excellent progress on vehicle construction, the difficulties experienced with BSC on infrastructure construction are extremely disappointing. The Agreement to construct the tram infrastructure and deliver the tram vehicles was signed in May 2008 following an 18 month procurement process. The essence of the Agreement was that it provided a lump sum, fixed price for an agreed delivery specification and programme, with appropriate mechanisms to attribute the financial and time impact of any subsequent changes, all as set out in the Agreement. However, a number of problems have arisen in the application of the Agreement terms.
- 3.4 Some design-related matters have been disputed concerning their inclusion or otherwise in the contracted scope of work and consequentially their inclusion or otherwise in the contracted price. **tie** has accepted that certain matters do require to be treated as legitimate additions to that price and agreement has been reached on some £18.2m of additional payments for changes such as soft ground treatment; additional demolition works; utilities diversions undertaken by BSC; and the draw down of provisional sums or revised specifications to address Council or third party requirements. The initial claim from BSC for these items totalled £32m. However, there remains disagreement with BSC on other matters and the DRP process in the Agreement is being deployed to enable the issues in dispute to be resolved either through negotiation or by the decision of the adjudicator. The application of this formal process does not prejudice either party's right subsequently to take an issue to court; however, both parties are required first to exhaust the process as set out in the Agreement.
- 3.5 Fifteen matters have now been processed through DRP. Overall, the application of DRP to disputed matters has reduced BSC's claims for additional payment from £18.2m to £7.6m (a saving of £10.6m to the public purse) in relation to those DRPs which have actually reached financial settlement (9 of the 15 DRPs). This includes the sum of nearly £4m saved through application of the DRP on two claims resolved towards the end of May 2010. **tie** is satisfied that the overall balance of adjudication outcomes has more than justified its interrogation of the initial claims made by BSC.
- 3.6 **tie** has accepted that some construction works have been impacted by delays to the completion of utility works. As a result **tie** has offered (as part of addressing impact of other client changes and compensation events) a reasonable extension of time to BSC to take account of such delays. The link between utility delays and other causes of delay in the construction works is complicated, though capable of resolution with the involvement of suitably qualified parties.
- 3.7 However, we are advised by **tie** that the issue which is having the biggest impact on the progress of the project and the programme budget is the apparent adoption by BSC of an approach of not progressing works where there is a change, or an alleged change, to the contracted scope of works until the financial entitlements from change are definitively resolved. This approach appears inconsistent with the terms of the Agreement which require that progress should continue on the project while work is undertaken in parallel to

assess the potential impact on programme and costs. Such mechanisms are normal in construction contracts to avoid delay to progress.

- 3.8 **tie** has issued a series of formal instructions to BSC to proceed with works within the terms of the Agreement. However, **tie** has informed the Council that BSC has not complied with these. It is noteworthy that many of the specific claims asserted by BSC require a competent estimate of the financial, programme and performance effects of the matter to be prepared by BSC; in many cases estimates have either not been provided or have been delayed by long periods, in some cases many months.
- 3.9 The disputes surrounding design-related changes, causes of programme delay and the apparent unwillingness of BSC to act upon formal instructions from its client are the primary reasons for the lack of progress on tram infrastructure and increasing costs. **tie** and the Council have a duty to secure best value for public money and it would be entirely inappropriate for **tie** to accept unsupported or inaccurate claims for additional money without interrogating the validity of such matters.
- 3.10 Whilst there have been disputes on design-related matters, as summarised above, it is normal in any large construction project for the scope of the project to change in marginal ways, for a variety of technical and commercial reasons.
- 3.11 To ensure a robust validation of such changes, a formal change management process is set out in the Agreement. The justification for the formal treatment of such changes is, under the terms of the Agreement, carefully evaluated to ensure that public funds are protected and to enable examination of any options which would mitigate their cost implications. A large percentage of the changes proposed by BSC remain unresolved, mainly due to a lack of timely, evidence-based technical justification.
- 3.12 Of the fifteen DRP issues to date, three have been resolved by negotiation, three were resolved through external mediation, seven have been referred for external adjudication (of which six have been concluded) and two matters remain at an early stage of the process. Taking into account matters which have been resolved under the DRP process and changes put forward by BSC concluded outside the DRP process, the sum saved by **tie's** negotiation of the submitted claims represents over 77% of the sum finally agreed. The outcome of the DRPs, in terms of legal principles, remains finely balanced and subject to debate between the parties.
- 3.13 **tie** has been successful, in part, in realising the objectives it set out to achieve by setting DRP processes in motion: getting work started at some locations and significantly driving down the final value of claims submitted by BSC. However, the DRP process has not yet achieved the momentum that the project needs to ensure its completion within an acceptable, extended programme.

Approach adopted by tie to achieve resolution

- 3.14 The development of the dispute with BSC has been reported regularly to the Council, with reports prepared for the April and August 2009 Council meetings. In brief, following BSC's refusal to fulfil their contractual obligations in relation to

works on Princes Street in early 2009, an alternative approach to work on Princes Street was agreed taking into account the critical nature of city centre tram work to the well-being of retailers, the travelling public and visitors to the city. In the summer of 2009, **tie** began to apply the DRP process with the results described above.

- 3.15 Towards the end of 2009, that Council was advised by **tie** that little real progress was being achieved in persuading BSC to progress the civil engineering and infrastructure installation works (for which Bilfinger Berger were responsible as BSC consortium member) according to the contractual programme. **tie** has therefore since late 2009 adopted a considerably more robust approach to enforcing its contractual rights.
- 3.16 To supplement **tie's** project team and principal advisers, **tie** has deployed additional expert resource in the areas of contract and dispute management, technical, commercial, forensic planning/delay analysis and litigation expertise. This has been done to enable a robust commercial approach to be taken with BSC and one which also sets the foundation, in due course, for a more formal entitlements enforcement process to be pursued through the courts, should that prove necessary. The cost of this additional resource has been covered many times over by the savings achieved through negotiation and the DRP.
- 3.17 The approach taken by **tie** has included audits of BSC's performance in key areas such as design management and integration, programme management (including compliance with duty to mitigate delays) and sub-contractor arrangements.

Options Review

- 3.18 In December 2009, the Tram Project Board (TPB) concurred with **tie's** proposal that, in view of the lack of progress, a fundamental review should be conducted of the contractual position with BSC and that, if required, formal legal processes should be started to bring the major issues to a head to allow the project to progress.
- 3.19 The analysis gathered from this work has enabled **tie** to evaluate specific strategic options. A variety of options and sub-options has been examined and the preferred strategy was reported to the TPB on 10 March 2010.
- 3.20 Over the last year, **tie** has tried a number of approaches to overcome the difficulties in its relationship with BSC. These have included making specific changes in relation to the work on Princes Street (due to the importance of the thoroughfare to Edinburgh's commercial interests tourism economy and Festivals); attempting to resolve impasses through external mediation; meetings with different levels of senior management within BSC; and offering an extension of time for completion of the works programme.
- 3.21 Against the backdrop of lack of progress and an apparent unwillingness on the part of BSC to adhere to its contractual responsibilities, **tie** has had to invest considerable time and public money to instruct external advice from independent experts.

- 3.22 The assessment of options by the TPB concluded that it was untenable to continue to seek a change in BSC's behaviour through informal commercial negotiation and that the investment of time and money to reinforce **tie's** contractual position was a necessary next step.
- 3.23 The current dialogue with BSC is focussed on ensuring a revised programme, with clarity about the sequencing of work and the parties' responsibilities so as to mitigate future disputes and achieve a best value outcome. Although some momentum has been achieved through this recent dialogue the outcome for the programme remains uncertain.
- 3.24 The second option being explored by **tie** is termination of the BSC Agreement. There is a contractually defined process that would enable **tie** to do this. It is hoped that this outcome can be avoided but the grounds for such an approach have been extensively examined by **tie** and its advisors. It is, however, important that any termination is carried out for proper legal and commercial reasons.
- 3.25 Amid the difficulties on the principal civil engineering works, it is important to recognise that the work carried out under the contract by Siemens and CAF has generally been conducted in a robust but constructive manner. The most tangible evidence of this is the recent, successful testing on Siemens' facility in Germany of the first tram vehicle manufactured by CAF, which is now on display in Princes Street. All 27 trams in the Edinburgh fleet have now been completed or are in the process of being constructed.
- 3.26 Throughout the period of the dispute, the governance model established for the project has been operated rigorously. The levels of authority delegated to the parties with responsibilities for governance is fully documented and has been adhered to; the TPB, a formal committee of the TEL Board, has also met regularly to receive reports on progress and on the matters in dispute and their impact on the project. Despite many matters being commercially sensitive, there has been regular reporting from **tie** through the governance structure to Council officers and also regular reports given to political Group Leaders.
- 3.27 In addition to communications between **tie** and Council officers, other key stakeholders have been kept fully informed. There has been regular dialogue between **tie**, Council officers and senior representatives of Transport Scotland. Enquiries about the project from members of the public, MSPs, the media and other interested parties have been responded to as fully as possible, subject to the need for confidentiality in some instances in order to protect public funds and to respect the terms of the Agreement.
- 3.28 The current status of the project remains highly unsatisfactory despite extensive and constructive attempts by **tie** to achieve reliable execution of the obligations in the Agreement. **tie** has been required to adopt increasingly forceful tactics in relation to its rights and obligations under the Agreement. Negotiations on the key matters continue and it is to be hoped that an acceptable outcome can be achieved.

Utilities

- 3.29 One of the most visible and disruptive aspects of the project for the travelling public has been the diversion of utility works along the route. The multi-utility framework strategy was a unique and innovative approach to the challenge of costly and disruptive diversion work. The utility diversions are now substantially complete with only minor cabling works and commissioning of new assets currently being finished in the city centre.
- 3.30 As reported to the Tram Sub-Committee on 22 March 2010 the majority of the utilities diversion work was originally undertaken by Alfred McAlpine Infrastructure Services (AMIS) under the Multi-Utilities Diversion Framework Agreement (MUDFA). Work commenced under this contract in July 2007.
- 3.31 Subsequently AMIS was subject to takeover by Carillion plc who managed the MUDFA works until the end of November 2009.
- 3.32 The remaining utilities works are being undertaken by two separate contractors, Clancy Docwra and Farrans.
- 3.33 The works undertaken have produced a major improvement to the city's utilities infrastructure. Many of the cables and pipes were in need of replacement which would have resulted in ongoing disruption to the city traffic over a number of years. This investment will be of long term benefit to the city and there will be a reduced requirement for maintenance and replacement of this infrastructure in the future.
- 3.34 The original scope of utilities works covered 27,000m of pipes and cables. However, this had to be significantly extended once the physical conditions underground became clear. The complexity of utilities along the tram route, congestion of pipes and cables in key locations and unforeseen obstructions has proven to be much more difficult than originally anticipated. In addition the records held by Scottish Utilities Companies and the Council were far from comprehensive. The final extent of diverted utilities is estimated at circa 50,000m. Currently 48,000m of the expected volume has been completed.
- 3.35 The estimated final cost for this part of the project has increased by approximately 25% taking account of the extended project scope and time delays. Of this increase, 15% was anticipated and provided for in the original contingency risk allowance. The net costs of utilities have also been calculated after deducting a substantial credit from the Statutory Utilities Companies for betterment of their assets.
- 3.36 Overall the MUDFA utilities works have required a net 10% increase from the original budget allocation. This is considered reasonable given the significant increase in volume of works encountered and the benefit of the enduring enhancement to the city's utility infrastructure along key traffic corridors.
- 3.37 The agreement of the final account with Carillion will be subject to determination of additional amounts relating to claims by the contractor for alleged delay and disruption to the works they carried out. These claims will be discussed with the Tram Monitoring Officer, in accordance with the Operating Agreement, before any settlement is made.

Budget, Scope and Programme

- 3.38 The original project budget at contract award was £512m for the full scope of Phase 1a with an Open for Revenue Service (OFRS) date of July 2011. An additional amount of £3.2m was due to be paid if Phase 1b was not progressed.
- 3.39 The report to Council on 20 August 2009 highlighted that delivery of Phase 1a within the funding envelope of £545m would be very difficult to achieve and that the Council would undertake contingency planning in the event that the estimated capital cost of the project exceeded the available funding envelope.
- 3.40 It now appears that the full scope of Phase 1a cannot be delivered for the approved funding of £545m. Given the problems with BSC, it is prudent to plan for a contingency of 10% above the approved funding of £545m because of the current lack of clarity on programme and cost. **However, TEL is not seeking approval for an increased budget at this time.**
- 3.41 Spend to date on the project, to the end of Financial Year 2009/10, was £347.8m. However, it should be noted that a construction project of this nature will incur significant front-end costs, including land acquisition, design, procurement and legal costs. The contract with BSC accounts for £240m (less than half) of the original programme budget and only £135m relates to civil engineering costs mainly contracted to Bilfinger Berger. The table below itemises the spend to date.

	Financial Close Budget £m	Current Spend £m
Infrastructure	250.5	117.1
Vehicles	58.2	42.2
Utilities	48.4	62.4
Design	26.9	31.2
Resources	68.3	63.4
Other (Including Land Acquisition Costs)	32.6	31.5
Contingency Risk Reserve + Phase 1b postponement and design costs (included in Current Spend in right hand column)	30.3	
	515.2	347.8

- 3.42 The original risk allowance within the budget of £515.2m has now been allocated to the individual budget headings.
- 3.43 Of the expenditure to date, the components relating to Design and Utilities are now almost complete. Therefore, exposure to additional costs in these areas is not significant.

- 3.44 The final anticipated cost related to Vehicles is £58m. With the exception of expenditure related to minor, internal design changes, this area of the project is on budget and ahead of schedule.
- 3.45 Most of the other costs noted above relate to land acquisition. These were accrued earlier in the project and the remaining cost exposure in this area is minimal, although there are some residual risks related to future claims.
- 3.46 Resource costs for the project are running higher than expected. The primary reason for this is the commercial and legal resource that has been required to deal with the ongoing disputes with BSC and the delayed construction programme. There has also been some increase in costs related to Traffic Management and arrangements to mitigate the impact of the tram during the Festivals.
- 3.47 The remaining uncertainty on the programme and budget primarily surrounds the infrastructure construction costs and the current dispute with BSC.
- 3.48 One of the reasons for the increase in infrastructure costs has been the cost incurred for the Princes Street works. Given the unique nature of Princes Street and the potential impact on city centre businesses a customised approach to construction activity was agreed with BSC whereby additional work, including the costs of programme acceleration, would be reimbursed on the basis of demonstrable costs.
- 3.49 The final account for this section has now been substantially completed and shows a major increase on the original sum of circa £2m included within the Infraco contract. Negotiations continue with BSC over a potential bill of £11m of costs, with **tie** having already certified, on account, £8m of these. Some of the additional costs would, in any event, have been additional to the provisions of the original contract (e.g. necessary improvements to the track base, full-depth road reconstruction along the length of the street, the use of setts and management of utility conflicts).
- 3.50 Some of these potential additional costs can be justified given the unique nature of Princes Street and the need to achieve a tight programme schedule in a critical area in the city to minimise disruption during the Festivals and Christmas shopping period. It should also be noted that the Council has benefited from a significant enhancement to the asset life of the road due to Full Depth road reconstruction. However, the experience of this arrangement demonstrates, clearly, that the approach cannot be extended to the remaining on-street works.

Council Funding Strategy, Contingency Planning and Incremental Delivery

- 3.51 The Council's funding contribution of £45m was to have come from a variety of sources, including capital receipts from land assets along the route of the tram line, developers' contributions and contributions from the Council's Capital Investment Programme. The original breakdown of the Council's funding and the contributions received to date is shown in the table below.

CEC Contribution Breakdown	Planned Contribution	Achieved Contribution
Council Cash	£2.5m	£2.5m
Council Land	£6.2m	£6.2m
Developer Contributions – Cash	£25.4m	£4.5m
Developer Contributions – Land	£1.2m	£1.2m
Capital Receipts (Development Gains)	£2.8m	£0.0m
Capital Receipts	£6.9m	£2.0m
Total	£45.0m	£16.4m

- 3.52 When this strategy was originally devised, it was assumed that capital receipts and developers' contributions would be accrued over a time horizon of twenty years; it was never assumed these funds would be in place during the construction phase of the tram project.
- 3.53 There is no doubt that the rate of funding from developer led sources has been affected by the economic downturn. However, evidence in recent months indicates that contributions are still being generated.
- 3.54 However, there remains a risk that the full level of contributions may not be achieved. The Council will therefore continue to monitor the levels and progress of the developers' contributions and assess these within the wider contingency planning arrangements being made for the project.
- 3.55 As detailed earlier in the report, it is now envisaged the full scope of Phase 1a cannot be delivered within the approved funding envelope and within the originally envisaged timescales.
- 3.56 Whilst TEL is not presently seeking approval for an increased budget or formal change to the baseline programme date at this point in time, in terms of a provision in its Operating Agreements, it is appropriate that Council is made aware of the current position. Any changes to cost, programme or scope which emerge from future negotiations with BSC will be formalised, as a request for approval from the Council prior to any commitment of new funds.
- 3.57 The factors of project cost and date of delivery need to be considered in the round and are clearly inter-related. Work is ongoing to firm up revised programme estimates as the TPB considers how best to balance the varying demands of the programme.
- 3.58 Whilst there remains significant commercial uncertainty, it is clearly not possible to provide a robust estimate for the full cost of Phase 1a. However, based on the strategic options work which **tie** has undertaken and as a result of all the other factors included in this report, it is now considered prudent for the Council to plan for a further 10% over the currently approved funding of £545m,

on the understanding that further potential risks have been identified beyond this level.

- 3.59 Contingency plans up to a funding level of 10% above the approved project funding have therefore been examined. The contingency planning undertaken has primarily identified two potential sources of funding to allow the Council to borrow under the Prudential Framework.
- 3.60 The Council has made an allowance of £2m per annum within its long-term Financial Plan to cover additional infrastructure development costs. This provision would allow the Council to borrow £24m under the Prudential Framework; this commitment would represent an opportunity cost for the Council but would have no impact on projects already identified in the Council's capital programme. Headroom within the existing budget for loan charges may also allow future investment in infrastructure beyond this sum if required.
- 3.61 Further borrowing, should it be necessary, can be financed from the future profits of Transport Edinburgh Limited (TEL). Based on the full scope of Phase 1a TEL's forecast cumulative net profit from 2013 – 2031 would allow the Council to prudently borrow additional money to fund the balance of costs up to a level of circa £600m.
- 3.62 The Council's contingency planning is dependant on its ability to use the prudential borrowing framework. However, a risk has emerged recently around potential restrictions on the use of the prudential framework given the current economic difficulties at UK level. If this risk were to crystallise the Council would have to investigate alternative funding arrangements. Further contingency planning is being carried out to prepare for such an eventuality.
- 3.63 Following recent meetings of the TPB, **tie** has also been instructed to review options for the incremental delivery of Phase 1a as a further contingency plan. This review requires the input of colleagues at Lothian Buses to ensure the extent of Tram services delivered at any point in time can be integrated with appropriately adjusted bus services. This review will be undertaken as the outcome of current negotiations with BSC becomes clearer.
- 3.64 The review of options for incremental delivery will address the need to manage the project affordability (in the context of the current commercial disputes with BSC) by means of flexible delivery of the on street sections over a longer period of time and in a way which provides the Council greater control over the precise timing of the remaining on-street works. The approach will ensure the investment already made in the in the project is realised through the delivery of a viable tram service, integrated with bus services, whilst preserving for delivery the entirety of the scope of Phase 1a, as detailed in the Final Business Case. The stages of Phase 1a service delivery under examination are;
- Airport – Haymarket (core off-street street works under construction)
 - Airport - York Place (connects the Airport to the City Centre)
 - Airport - Foot of the Walk (achieves integration with bus services on Leith Walk and interchange at FOW)

- Airport – Ocean Terminal (serves the core of the Leith Docks development)
- Airport – Newhaven (Full Scope of Phase 1a)

3.65 The capital costs of each of the options will allow future decisions to be taken within the overall context of affordability. The full assessment of these options and the overall funding strategy can only meaningfully be performed once there is clarity on the outcome of the dispute with BSC.

4 Financial Implications

4.1 It is now considered that the full scope of Phase 1a cannot be delivered within the approved funding envelope of £545m.

4.2 The contingency planning work that has been undertaken by the Council and **tie** has identified funding options which could address project costs of up to £600m.

4.3 There are further risks that could impact on the costs of the project. As part of the work **tie** has undertaken on strategic options, the potential delivery of construction in incremental stages, based on judgments about affordability, may need to be considered in the future.

5 Environmental Impact

5.1 The Edinburgh Tram Project will make a positive contribution towards the vehicular emissions and air quality in the city centre and the transport corridor to the west of the city and the airport. This will have a positive impact on current pollution levels and provide a quieter mode of public transport.

6 Conclusions

6.1 Despite the major increase in pipe and cabling works beyond the original estimates there has been a relatively small corresponding increase in overall utilities costs against budget.

6.2 Despite the parties entering into an alternative arrangement for the delivery of the Princes Street works in good faith, the experience has shown that this would be an inappropriate approach to adopt across the rest of the route.

6.3 Whilst there remains significant commercial uncertainty, it is not possible to provide a robust estimate for the full cost of Phase 1a. However, it now appears that the full scope of Phase 1a of the tram system cannot be delivered within the available funding envelope of £545m.

6.4 Notwithstanding the continuing difficulties, TEL is not seeking any further funding approval at this time. Council officers are however looking at contingency funding options and **tie** are examining the possibility of delivering Phase 1a in incremental sections on a phased basis.

6.5 The current position remains highly unsatisfactory. It is to be hoped that an acceptable outcome can still be achieved through negotiations. However, in

the event that this cannot be achieved, **tie** has indicated that it will need to consider its options further including the possibility of terminating the Agreement in an appropriate manner.

6.6 Any changes to cost, programme or scope which emerge from the negotiations with BSC will be formalised as a request for approval from the Council prior to any commitment.

7 Recommendations

7.1 It is recommended that the Council;

- a) notes the current status of the Project and requests **tie** to continue to seek an acceptable resolution with BSC if at all possible;
- b) notes that whilst no clear estimate of the cost of Phase 1a is available at this time due to uncertainty, Council officers and **tie** are examining all possible options for contingency funding and the possibility of incremental delivery;
- c) notes that, in the event that an acceptable agreement cannot be reached, **tie** has carried out the necessary preparation should termination of the contract be the most appropriate option; and,
- d) notes that any changes to cost, programme or scope which may emerge from the negotiations with BSC will be reported to Council prior to any further funding commitment being made or changes to the project scope or timetable being agreed .


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Appendices None

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Wards affected All

Single Outcome
Agreement

Background
Papers