
From: Stewart McGarrity
Sent: 11 October 2010 16:45
To: Alan Coyle; Gregor Roberts
Cc: Dennis Murray; Richard Jeffrey
Subject: HANDOVER - Edinburgh Trams: Advance payments made to BBS
Attachments: FW: Initial Milestones - Update; Mobilisation Payment; Milestone v Liability Schedule.xls

Sensitivity: Confidential

Follow Up Flag: Follow up
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HANDOVER

Alan/Gregor,

This serves to address John Ramsay's questions below and to download the history behind the mobilisation milestone payments to each of Bilfinger/Siemens/CAF, the accounting treatment and where we stand today in respect of amounts certified versus BSCs entitlement / value of work done.

The mobilisation payments were negotiated as part of the commercial engagement leading up to preferred bidder appointment in Oct 07. My email '*Initial Milestones – Update*' attached has the email exchanges between myself and Guy Houston at TS in February re these amounts. Also attached to that email are the papers provided to Guy in early 2008 (largely the work of Geoff Gilbert with me adding the words on credit risk management) justifying the mobilisation payments as VfM on the basis of the discounts received from the bidding consortium for making these payments.

After final negotiation of the Infraco price in May 2008, the actual mobilisation payments to Infraco were **£45.2m** for BB/S (£22.6m each) and **£11.4m** for CAF, all calculated as 20% of the respective contract sums less undefined provisional sums.

Of these amounts (and with agreement of TS) we treated **£24.2m** (£15.5m for BB/S plus £8.7m for CAF) as prepayments for accounting purposes since these were the estimated proportion of the payments which was in respect of advance procurement of materials / supply chain mobilisation as per the papers provided to Guy Houston in early 2008. This is the prepayment amount referred to Ramsay's email of this morning.

Since contract award the entire CAF prepayment has been reversed and we have reversed £1.1m of the BB/S prepayment meaning we have now reduced our accounting prepayment to **£14.4m**.

The discussion with J Swinney last week centred round the aggregate level of certification to date versus the value of work done by the contractor and entitlement in the event of a termination. The attached email 'Milestone v Liability Schedule.xls' has the estimate of this equation prepared last week by Dennis up to end of Period 6 - with his best estimate of their entitlement to preliminaries he has amounts certified to BB+S at £118.4m versus £86.5m liability for value of work done. NB – our best estimate of entitlement to prelims on this basis would be subject to demonstration in the event of a termination.

To summarise current status in a wee table:

	COWD P6	Certified P6	DM Liability P6
BB & S – Prelims (incl milestone payments £45.2m)	83.0	80.5	41.4
BB & S – Milestones and Change	45.4	37.9	45.2
BB & S - Total	128.4	118.4	86.6
Accounting Prepayment	(14.4)	-	-

CAF	46.0	46.3	46.3
SDS (Post Novation)	7.7	7.7	7.7
	167.7	172.5	140.6

NB

- COWD includes PM estimates of accruals at period end and excludes £3.2m paid in respect of Ph1b
- For CAF it assumes we will get value by taking delivery of the Trams – strictly at present we do not have title to the tram vehicles in Spain

Addressing each of Ramsay's questions:

Is it correct to assume that such advance payment (s) is in addition to the original £24.2m prepayment to CEC?

No it is not correct to assume that (why would someone have come to that conclusion?). The prepayment of £24.2m is the proportion of the aggregate mobilisation payments (estimated advance material purchases element) we agreed with TS to be treated as an accounting prepayment of which we have now reversed £9.8m leaving an accounting prepayment of £14.4m.

If so what is the total of the additional advance payment (s) and what do they cover?

There are no additional advance payments – the £30m referred to is an internal **tie** estimate of the amount BB and S would be entitled to for work done only in the event of termination (including what they have spent on prelims)

In the event of termination, how much is recoverable?

On the face of it the full £30m is recoverable but this is all subject to an actual valuation of the work done and demonstration of their entitlement in respect of prelims.

How will any recovery be achieved? and

Depends on the nature of the termination. If it were amicable there might be sensible commercial settlement. If this were not the case we would secure cash by calling the bonds – we have a performance bond total of £23m plus a £2m retention bond – a total of £25m – plus the value of whatever materials on site came into our hands. If this still left a gap cash wise we'd likely be waiting till any subsequent litigation or other determination of the final account to settle. The bonds are on demand and so long as we go through the correct process with reference to the Cl90.1.2 notices then validity of the calls should not be a problem.

Can you confirm Transport Scotland's understanding that recovery may be via bonds and parent company guarantees, and if so will involve require legal action to secure

See above – we don't need legal action to call the bonds or the PCGs. It's likely a call under the PCGs would be disputed.

Lastly I attach an email from Andrew F called Mobilisation payment wherein he gives comfort that the mobilisation payments were just a part the means of payment in accordance with the milestone schedule and should not be confused with entitlement for work done. There was a suggestion from Walker at one stage that the minute we paid them that money it was theirs to keep.

After you've had a butchers should we discuss to see if there is anything else I can help with in this regard?

Stewart

Stewart McGarrity

Finance Director

Edinburgh Trams

Mobile: [REDACTED]

From: John.Ramsay@transportscotland.gsi.gov.uk [mailto:John.Ramsay@transportscotland.gsi.gov.uk]

Sent: 11 October 2010 11:00

To: Alan Coyle
Cc: Ailie Wilson
Subject: Edinburgh Trams: Advance payments made to BBS:
Importance: High
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Alan

Advance payments made to BBS:

It appears that at last week's update meeting with the Cabinet Secretary, CEC and tie.Ltd, Mr Swinney asked for an explanation concerning the level of advance payments made to BBS by tie under the Infraco contract. I am advised that Richard Jeffrey suggested that some £30m or so has been paid in excess of the value of work delivered and this would have been made in exchange for some discount to the price reflecting factors such as the financing of material purchase.

This raises a number of questions and it would be helpful if you could provide further commentary to this matter and in particular detailed response on the following;

- Is it correct to assume that such advance payment (s) is in addition to the original £24.2m prepayment to CEC?
- If so what is the total of the additional advance payment (s) and what do they cover?
- In the event of termination, how much is recoverable?
- How will any recovery be achieved? and
- Can you confirm Transport Scotland's understanding that recovery may be via bonds and parent company guarantees, and if so will involve require legal action to secure

My apologies for the urgency of this request but David Middleton wishes to provide a response to the Cabinet Secretary on this as soon as possible this week, ideally by COP tomorrow. Happy to discuss

John Ramsay
Project manager - Edinburgh Trams
Rail Directorate
Transport Scotland
Buchanan House
Glasgow G4 0HF

Tel [REDACTED]
mobile [REDACTED]

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