

Edinburgh Tram – Financial Close and Notification of Contract Award

The City of Edinburgh Council

1 May 2008

1 Purpose of report

- 1.1 To notify the Council of the progress of the two major contracts for the Edinburgh Tram Network (ETN) and to provide an update on financial close and the capital costs.

2 Summary

- 2.1 A report updating the Council on the progress of the contractual negotiations for the ETN was submitted to Council on 20 December 2007. Delegated authority was given to me to allow **tie Ltd** to enter into contracts to deliver the ETN subject to suitable due diligence and providing remaining issues were resolved to my satisfaction.
- 2.2 **tie Ltd** are about to conclude the contractual negotiations and have recommended to me that the contracts for the supply and maintenance of the tram vehicles (Tramco) and for the construction and maintenance of the tram infrastructure (Infraco) be awarded to Construcciones y Auxiliar de Ferrocarriles SA (CAF) and Bilfinger Berger Siemens (BBS) respectively. The contracts include the novation of the CAF and the System Design Services (SDS) contracts to the main Infraco contractor.
- 2.3 Negotiations have taken longer than expected due to the complexity and scale of contractual and related issues arising from the contract suite. There has also been a substantial amount of work undertaken to minimise the Council's exposure to financial risk with significant elements of risk being transferred to the private sector. This has resulted in 95% of the combined Tramco and Infraco costs being fixed with the remainder being provisional sums which **tie Ltd** have confirmed as being adequate. The net result of the negotiations is a final estimate for Phase 1a of the ETN of £508m. This figure secures the best deal possible for the Council and Transport Scotland, and is well within the agreed funding envelope of £545m.
- 2.4 Infrastructure construction work is planned to commence in May 2008 and Phase 1a is programmed to be substantially complete by January 2011. A period of testing, driver training and shadow running (to test the entire system meets the performance requirements) follows on from the Construction phase. Trams will be visible running along the route during this period. Revenue

services are planned to commence in July 2011. The Final Business Case (FBC) highlighted commencement of revenue operations in Quarter 1 of 2011. The changed timescales reflect the positive work undertaken in negotiating major contracts which provide greater price certainty, reduced risk exposure and better overall quality and value for the Council and Transport Scotland.

Main report

Recent Developments

- 3.1 The required notice of intent to award the contracts to CAF (for the Tramco contract) and BBS (for the Infraco contract) was issued on 18 March 2008, following satisfactory close out by **tie Ltd** of the remaining issues required by the Council. Following the mandatory minimum cooling off period, the contracts will be signed once final due diligence on the documentation is completed by **tie Ltd and BBS**.

Financial Close and Capital Cost

- 3.2 The protracted yet progressive nature of the contractual negotiations highlight the work undertaken by **tie Ltd** and written confirmation has been received from **tie Ltd** stating that the contracts represent the best possible value to the Council.
- 3.3 The FBC aggregate estimate for Phase 1a was £498m as reported to Council on 20 December 2007.
- 3.4 Over the period of negotiations with the preferred bidder there have been changes to the overall cost of the project. The make up of the estimated cost of Phase 1a in the FBC was £498m which included base costs of £449m and a Quantified Risk Allowance (QRA) of £49m. The base cost has now increased to £476m with a revised QRA of £32m giving a final estimated cost of £508m. Firm costs represent 95% of this sum, with the remainder being provisional sums which **tie Ltd** have confirmed as being adequate.
- 3.5 The increase in baseline aggregate costs is largely due to the firming up of provisional prices to fixed sums, currency fluctuations and the crystallisation of the risk transfer to the private sector as described in the FBC. Changes in price were expected and were included in the risk provision reported to Council on 20 December 2007 based on the assessment of the bids when the preferred bidders were appointed.
- 3.6 The revised costs are based upon the construction programme as advised by **tie Ltd** with works anticipated to commence in May 2008 and Phase 1a being substantially complete by January 2011. Revenue services are planned to commence in July 2011. **tie Ltd** continues, through its appointed contractor, to execute the work under the contract for utility diversion along the tram route on behalf of the Council and reports that this work, which is part of the authorised works under the statutory authority granted to Council under the Edinburgh Tram Acts, is progressing to programme and budget.
- 3.7 The Council approved on 20 December 2007 the draft **tie Ltd** operating agreement and delegated authority to the Council Solicitor to execute the operating agreements with **tie Ltd** and TEL on behalf of the Council. The draft operating agreements have been amended to reflect the fully up to date position including provision for the Tram Project Board to authorise cost increases of up to £10m and any further delay of up to 3 months.

- 3.8 On the 20 December 2007 Council delegated authority to the Council Solicitor to conclude and execute the Guarantee on behalf of the Council for the benefit of BBS.

Quantified Risk Allowance (QRA)

- 3.9 The QRA has reduced from £49m at FBC to £32m. The material change in the QRA relates to procurement risks for Tramco and Infraco closed out at the signing of the contracts offset by allowance to provide for risks and uncertainties to be managed by **tie Ltd** during construction.
- 3.10 A number of the adjustments to risk allocation are positive, reflected in the reduced QRA. A risk which has been passed on to the Public Sector relates to delay by SDS in gaining approvals. This has been a very difficult point for **tie Ltd** to negotiate and they have provided for the best deal which they advise us is currently available to themselves and the Council. In essence, BBS will accept the design risk for SDS to a high financial ceiling, whereas the Council and **tie Ltd** will remain financially liable for delay by SDS in relation to the provision by them of information for a range of consents and approvals. Both **tie Ltd** and the Council have worked diligently to examine and reduce this risk in practical terms and **tie Ltd** advise that the new risk contingency contains suitable adjustment for this residual risk.
- 3.11 A written statement from **tie Ltd** has been provided stating that they are satisfied that £32m is an adequate level of risk allowance.

4 Financial Implications

- 4.1 The baseline cost of the project has increased from to £449m to £476m with the QRA reducing from £49m to £32m resulting in the final price of the project increasing from £498m to £508m. The estimate remains well within the agreed funding envelope of £545m.

5 Conclusions

- 5.1 It is proposed that the Tramco and Infraco contracts should be awarded to CAF and BBS respectively, securing the best deal possible for the Council and Transport Scotland. The awarding of these two contracts will represent a significant milestone in the implementation of the Tram project. A significant level of risk has been assumed by the private sector considerably reducing the Council's exposure to future uncertainty. Communications about the commitment to these important contracts will be co-ordinated with **tie Ltd** and Transport Scotland.

6 Recommendations

- 6.1 The Council note the imminent award of the two contracts with a final price for the Edinburgh Tram Network of £508m which is within the funding envelope of £545m.
- 6.2 The Council refresh the delegated powers already given, to authorise me to instruct **tie Ltd** to enter the contracts with Infraco bidder and Tramco bidder, in light of recent changes noted in this report.

- 6.3 To note that the FBCv2 which was approved by Council on 20 December 2007 is modified to reflect the above position.
- 6.4 To note the **tie Ltd** and TEL operating agreements have been amended to reflect the fully up to date position.
- 6.5 To note that the Guarantee to be executed on behalf of the Council for the benefit of BBS will be provided at financial close.

**Tom Aitchison
Chief Executive**

Appendices None

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Wards affected All

**Background
Papers** None