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## 1 Introduction

- 1.1 This briefing is intended to provide an update on current developments on the Tram Project.

## 2 Grant Award Letter

- 2.1 A positive meeting was held between CEC (Finance, City Development & Legal) and Transport Scotland's (TS) John Ramsay and legal representative Teddy Davidson of Dundas and Wilson (D&W) on 27<sup>th</sup> November around agreement of several outstanding queries on the Grant Award Letter and associated schedules.
- 2.2 Agreement was reached over the funding split percentage between TS and CEC as 91.7% and 8.3% respectively with all paragraphs in the draft with this reference amended.
- 2.3 CEC are to email John Ramsay with request for extension to the drop dead date of 31 March 2011 (para 3.1 of schedule). This request will be for extension to 31 March 2013 to accommodate any project costs that will still have to be settled such as land compensation payments. John Ramsay was receptive to this and legal representatives will look at a form of wording.
- 2.4 Para 4.2.2 detailing Period end dates and Application dates will be updated to Financial Year 2008/09 for the final Grant Award Letter.
- 2.5 Para 4.4 of the draft sets out payment terms and timescales for payment by TS. CEC raised a query on whether interest could be charged to TS in the event of late payment. TS stated that the likelihood of late payment would be extremely low and there will be absolutely no intention of this happening. TS legal reps will amend this paragraph to provide comment on interest.
- 2.6 Para 12.1.1 & 12.1.2 gives guidance in communication protocol. This involves CEC/tie/TEL giving Scottish Ministers 5 business days of all major announcements regarding the project and 48 hours notice of minor announcements and that CEC/tie/TEL do not communicate with the media without prior approval of Scottish Ministers. This was seen as unworkable from CEC/tie/TEL's perspective and it was agreed CEC should get back to TS with wording on a comms proposal to ensure Scottish Ministers and TS get "no surprises".
- 2.7 Possible leasing of trams has always been seen as a way to free up funding for the project. Para 18.1 & 18.3 of the schedule has implications for this possibility. CEC have to supply TS a letter detailing our intentions/possible leasing options for the future.
- 2.8 Para 20.1 of the schedule seems to prevent CEC from seeking any other Public Sector Contribution without having to pay back TS the

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matching amount. TS agreed this would not make sense should CEC wish to explore further funding options should they become available for Phase 1b or any shortfall in CEC's £45m contribution.

- 2.9 Additional cosmetic changes will also be made to the Grant Award on minor issues.
- 2.10 As a result the outstanding issue to be settled with CEC/TS is flexibility of funding arrangements to allow for slippage or acceleration of expenditure. Should interest be incurred due to reasons of annuality constraints of the TS budget, that interest costs can be accrued against the overall costs of the project.

### **3 Potential Additional Project Costs**

The following issues may have an impact on the content of the report to Council on 20<sup>th</sup> December.

- 3.1 The Council report of 25<sup>th</sup> October 2007 gave a forecast outturn for Phase 1a of £498m.
- 3.2 It is currently unclear to CEC as to the scope of the works, the timescale of the project, and the allowance for incomplete detailed design and implication for gaining approved designs (technical and prior approvals). All the above can have potential impacts of time and costs and under this form of contract potential major cost implications because of delay and disruption to the position at financial close.
- 3.3 This form of contract was adopted "fixed price" on the basis of complete approved designs however as this is not where we are this current position requires to be reflected in the QRA and contingency allowance.
- 3.4 The underlying concern is that while it may be achievable to reach a financial close of £498m, this will result in a major challenge in managing this during the contract. It has been confirmed by tie that the extension of time from the current target would have a significant impact on overhead costs on this form of contract.
- 3.5 There is also a physical limit to accelerating the works because of the constraints of maintaining traffic movement in the city centre, hence lost time to extension of time may not be compressed.
- 3.6 Value Engineering savings of £10m have not yet been achieved meaning the £222m figure for Infracore has not yet been achieved.
- 3.7 Additional Project Management costs within tie of £1.5m.
- 3.8 Additional CEC costs resulting from the project for Financial Year 2008/2009 of £650k.

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### **4 Quantified Risk Allowance (QRA)**

- 4.1 The current risk allowance stands at £49m. This figure drops to £34m following financial close due to a number of risks being closed out at that point. This reduction is subject to a number of caveats, not least a 100% fixed price contract being in place at contract close. CEC have not seen the re-run QRA to demonstrate the reasons for the figure decreasing and the risks excluded. This information has been requested from tie as clearly there must have been some changes due to commercial reasons on the £498m and the risk allowance through negotiations with Bilfinger Berger Siemens (BBS).

### **5 First Scotrail (FS)**

- 5.1 One of the 3<sup>rd</sup> party issues not been previously addressed is the Depot and Station change procedure with FS given the lease they have with Network Rail (NR) at Haymarket Station.
- 5.2 The access to land and the potential for NR to stop tram operations during construction and post construction are critical. Clearly restriction to the any part of the works during construction would adversely impact on the works. Also this section is the one section to potentially open first, hence any delay would have an adverse impact on CEC expectations for delivery
- 5.3 FS have 45 days to respond to a request for a depot/station change. NR are not willing to approach FS without finalised drawings and full details to allow FS to take a decision. Without FS consent, there is a concern that CEC/tie will not be able to give BBS access to the land.
- 5.4 Ideally the 45 day period would expire well before the 28 January signing date. If there is a real concern at that point (eg an ORR referral) then at least the Council will not be formally contractually bound to BBS. Whilst the issue may turn out to be easy to solve, it is nevertheless a risk to the project. To resolve this issue, tie and SDS need to provide the relevant documentation to NR to allow FS to start the 45 day period asap and in any event no later than say 12 December.
- 5.5 Although the QRA covers a number of NR issues there is no specific allocation for this. tie to set up meetings with NR and FS to progress Depot and Station Change procedures – before 5/11/07 if possible.

### **6 Utilities**

- 6.1 Scottish Power and Telewest agreements despite being urgent five months ago, have still to be signed. This issue could disrupt MUDFA and Infracore.
- 6.2 There have been problems with Utilities adhering to the MUDFA programme and misadvising of where utility pipes/cables are active.

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- 6.3 The MUDFA works programme has a direct impact on Infraco's ability to start works on street. The MUDFA works have been delayed by design drawing delays. Infraco works are also delayed by the time scale of availability of structures especially at Carrick Knowe and Lindsay Road.

### **7 Consents/Prior Approvals/Incomplete Design**

- 7.1 BBS are presently unhappy with accepting the novation of the SDS contract as effectively SDS are not bound to process the designs within specific timescales, whereas BBS are timebound in terms of project delivery.
- 7.2 They will carry the financial risk of delay if SDS fail to deliver approved drawings on time. They have therefore asked tie whether there are any approvals which the Council would be willing to take back the risk on.
- 7.3 The Council has always sought tie to procure a fixed price contract. Inevitably, the absolute fixing of the price by BBS would require finalised approved drawings. For whatever reason, tie and SDS have failed to obtain approvals for the drawings to date.
- 7.4 Accordingly, the present price must be based on unapproved drawings. If the Council accepts the risk re the approvals rather than BBS this will likely lead to (i) inappropriate pressure being put onto planning colleagues to approve drawings simply to stop an delay and added expense to the project; and (ii) the Council being left to foot the bill for any consequent delays.
- 7.5 Should the Council not accept these risks and BBS continue to be unhappy there may be potential they could walk away from the contract.
- 7.6 One option, should BBS remain concerned, would be to ask them to increase their costs by adding a "risk premium". Whilst making the project delivery perhaps more expensive, it would at least assure the members that the risk has been passed to BBS as originally intended. This is a sensitive commercial issue and is constrained in terms of CEC's ability to be explicit with members as this information could fetter final negotiations. It seems reasonable to have some contingency for the Tram sub-board to approved additional expenditure up to some limit.
- 7.7 A design risk that the project has taken back is in relation to wall fixings.
- 7.8 Wall fixings will be required along certain parts of the route to support the overhead power cables. Should there be a dispute on the location of these fixings and a court could rule that they must be moved which

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would be an additional cost to the project during the construction phase.

- 7.9 Should residents wish to do external works to their property which would require movement of fixings a temporary fixing would have made anchored to concrete blocks on the footway which will be an operating cost to the project.
- 7.10 The fact that the design is incomplete will increase the risk of variation orders, delay to MUDFA and subsequent delay to Infracore and have a knock on effect to the TRO process.

### **8 Third Party Agreements**

- 8.1 The Council need to be absolutely certain that tie have disclosed all relevant third party agreements to BBS and that BBS accept the terms of them.

### **9 Governance**

- 9.1 There still appears to be missing parts of the delegated authority chain giving Tram Project Board (TPB) its mandate from CEC. Unless documentation can be located which shows TPB have the relevant powers from CEC, TPB may not presently have valid decision making powers. Duncan Fraser is to respond on this issue.

### **10 PI Cover/Guarantee**

- 10.1 It appears that no PI cover is available to tie to allow CEC to be indemnified. In short, this means that CEC will effectively have no recourse to tie, even if there is an operating agreement in place.
- 10.2 Indeed, CEC will have no recourse even if tie are entirely negligent. This causes concern if for example tie were to negligently put the Council in breach of the Funding Agreement, TS pull the funding, but CEC has given a payment guarantee to BBS with no funds to cover the fees due. It may be an unlikely scenario, but the December report should reflect this risk.
- 10.3 This is linked to the guarantee issue. DLA originally provided sample guarantee letters by some months ago. They contained wording that the guarantee was subject to TS funding being provided. The proposed new guarantee does not have this caveat. From a commercial perspective this is understandable (ie BBS should not have to rely on TS's actions when they have done their job correctly), but it leaves the Council at further risk.

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## 11 Operating Agreements

- 11.1 Whilst the tie operating agreement is certainly useful as a guide to what tie should be delivering, given they have no assets or PI cover, there is little protection being provided in practice. This should be highlighted to members as previous reports have noted that the operating agreement would provide solutions to some issues.

## 12 Further Issues

- 12.1 Carillion were about to take over Alfred McAlpine – could this impact in MUDFA.
- 12.2 There has been reported allegations of corruption against Siemens in the US and subsequent investigation, is this a point which tie should satisfy the Council on.
- 12.3 The scandal at the firm concerns allegations that senior managers ran a slush fund of up to 420m euros (\$572m; £286m) to help win overseas contracts.

## 13 Contract Risk

- 13.1 Following the OGC risk report they highlighted potential weaknesses in the contract document. These concerns were raised at LAC on 22/10/07 by the Council Solicitor following information provided by CEC finance.
- 13.2 Andrew Fitchie was to take these items up with the members of the OGC team, there has been no information feedback.
- 13.3 The items in question were:
- It places obligations on **tie** to manage the Infraco – if **tie** fails to do this, they could be open to legitimate claims from Infraco. The paragraph they pointed us to concerned the requirement to tie to give permission for the covering up of works (but there are likely to be others).
  - The contract is a fairly standard contract, with all the detailed specification being in the Employers Requirements. The team have experience of judges making rulings based on what is said in a main contract, ignoring accompanying schedules. One of the panel quoted losing £40m in a similar situation.

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13.4 There is also the issue that Council official's do not understand the contract nor have had any independent review of the contract document.

13.5 Additionally there has been no sign off by Council of Employers Requirement.

### **14 tie**

14.1 Several difficult issues were raised at Legal Affairs Committee on the 26<sup>th</sup> November regarding issues on consent and contract negotiations with BBS and it was clear tie project managers are worried by the lack of progress on key aspects of the contract, which suggests the Council should be also.

14.2 The Council members are committing to the biggest project it has ever undertaken and as Council officers we must ensure we are presenting them with enough information to allow them to make a competent decision.

### **15 Conclusion**

15.1 Guidance is being sought from Council Officers from the Director's of Finance and City Development on how the issues detailed above should be reported in the Council report of 20<sup>th</sup> December 2007.

15.2 Guidance is being sought from Council Officers providing input to the Council report on 20<sup>th</sup> December 2007 on the issues detailed above whether the Council is well informed enough at this stage in proceedings whether a report on the 20<sup>th</sup> December 2007 is appropriate given the outstanding issues.