

Bill Reeve
 Transport Scotland
 8th Floor
 Buchanan House
 58 Port Dundas Road
 Glasgow
 G4 0HF

Received/Issued		01/08/06	
Document No:		002652	
Signature:		[Redacted]	
For Information	DI	AI	
For Action			
File location:		40.03.04.11	

Our Ref: 40.03.04.11

26th July 2006

Dear Bill,

Re: Edinburgh Tram Project Bidders' Costs

As you are aware, the process to pre-qualify candidates for the Infraco contract has been launched and is close to reaching a conclusion. Having originally received responses from a number of organisations who would not have been able to undertake the whole Infraco contract and following a dialogue with these organisations, we have now received a consolidated response from the market. The three candidates who have provided complete pre-qualification submissions are the following:

- * Amec Spie Rail Systems Limited
- * Bilfinger Berger – Siemens – Morgan Est (BBSME)
- * Tramlines (Bombardier Transportation – Laing O'Rourke – Grant Rail)

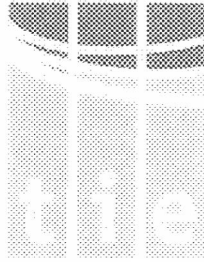
The second and third candidates are each constituted as two party consortium, between the electro-mechanical partner (Siemens or Bombardier) and a joint venture of the two other companies. This configuration is relatively common in the rail sector internationally.

The evaluation of the candidates' submissions is currently being finalised. The submission provided by BBSME has been qualified on the following points which are outside tie's ability to address:

- * Confirmation of adequate funding availability
- * Reimbursement of bidding costs in the event that the project is cancelled or delayed for more than 18 months for whatever reason

The other points raised are within tie's gift to address.

These qualifications prevent us from concluding the prequalification of BBSME, who otherwise, along with the other two candidates have submitted a competent and acceptable prequalification submission.



The other candidates have made no mention of these issues, however as you are aware, the UK light rail market has recently experienced a number of high profile project cancellations. The market is understandably nervous about British light rail projects, which is one of the reasons why BBSME have raised these points. They have also cited examples of other Scottish transportation projects, where bidders' costs have been reimbursed, in particular the Kinkardine Bridge and the A92 between Dundee and Arbroath.

We have estimated that bidders' costs for the initial bidding phase will be of the order of £500k, which is substantially lower than for PFI style procurements which have been the UK norm for the last decade. Another difference with previous procurements is that the bidders' cost profile is expected to be significantly based on internal labour, with a much lower reliance on external advisors.

On the basis that we have three bidders, tie's envisaged procurement strategy will be to reduce this number to two, following initial assessments of bids and interviews. The two remaining candidates will be taken through a CARP and BAFO process, during which we estimate that each bidder would typically expend a further £500k.

Finally, there will be work required to support the finalisation of the contract. This is envisaged as being a relatively rapid process, but inevitably will require significant legal input.

Precedents for re-imburement of bidders' costs have been set in the UK light rail market on the following projects: Manchester Phase 3, South Hampshire, Leeds & Merseytram. On these projects, reimbursement was limited to external costs and was capped.

In order to address BBSME's concerns, the following cost re-imburement mechanism could be considered:

Candidates' external costs will be reimbursed in the event that the Edinburgh tram project is cancelled or delayed for more than 18 months relative to the timetable set out in the Invitation to Negotiate documents. Cost reimbursement will be allowable only in the event that the candidate submits a complete proposal and would only apply to the following categories of expenditure:

- * External legal costs
- * Bid production costs

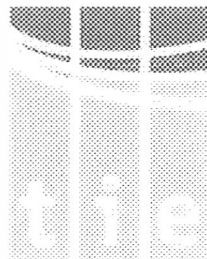
During the initial bidding period, such costs will be reimbursable up to a limit of £200k. During the CARP/BAFO process, a further £200k of external legal costs will be eligible for re-imburement. Thereafter, once the preferred candidate has been identified, a final tranche of £100k of external legal costs, incurred in the final negotiation of the contract documents will be eligible for re-imburement. All costs claimed will need to be fully auditable. Once the Infracore contract has been let, no claim for cost re-imburement will be allowed from any candidate.

tie limited

Verity House 19 Haymarket Yards Edinburgh EH12 5BH
Tel: +44(0)131 222 8300 Fax: +44(0)131 222 8301 www.tie.co.uk
Registered in Scotland No. 230140 at City Chambers, High Street, Edinburgh EH1 1YJ

Project (Ref): 001 (001) [REDACTED]
Contract (Ref): 001 (001) [REDACTED]
Web: www.tie.co.uk

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We may also adopt a process whereby the preferred candidate is identified following the initial bids, which would reduce the amounts payable to the unsuccessful candidates.

In our opinion, the most likely point at which the Infracore procurement process could be cancelled would be following receipt of the initial proposals, in the event that the project becomes unaffordable. In this circumstance, cost reimbursement for the initial tendering period would be payable to each contractor.

The maximum payable under this mechanism is as follows:

1. Initial bidding:	3 x £200k	£600k
2. CARP/BAFO:	2 x £200k	£400k
3. Final negotiations:		£100k
Total		£1,100k

We seek your approval to proceed on the basis set out above.

Yours sincerely,

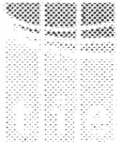


Andie Harper
Project Director - Trams

Tie Limited

Verity House, 19 Haymarket Yards, Edinburgh EH12 5BH
 tel: +44(0)131 528 8700 fax: +44(0)131 522 8700 www.tie.co.uk
 Registered in Scotland No. 210943 at City Chambers, High Street, Edinburgh EH1 1YS

Direct dial: +44(0)131 [Redacted]
 Email: andie.harper@tie.co.uk
www.tie.co.uk



Record of Document Review

Document originator

Ensure that this record of review sheet is applied to any document requiring signed evidence of review / agreement pre issue.

Document type: Letter Report Minutes of Meeting Drawing Other (details) _____

Document Number: 40.03.04.11

Document title: Edinburgh Tram Project Bidders Costs

Revision: 1

Originator: DP/AH

Issue status: Draft Issue for comment Formal issue

Name	Organisation	Comments	Resubmit	Issue	Signature
AH	TIC				[Redacted]
DP	TIC				

Administrator

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