PRIVATE AND CONFIDENTIAL

Edinburgh Tram Project

City of Edinburgh Council Funding Commitments

June 2010

Introduction

This document sets out the current position with regard the City of Edinburgh Council's funding position for the Edinburgh Tram Project. This document focuses on both the current commitment of £45m but also the Council's contingency planning options currently under consideration.

Transport Scotland and the City of Edinburgh Council have now been informed that it is highly likely that the full scope of Phase 1a cannot be delivered within the budget of £545.

Against this backdrop, and the current contractual difficulties that have contributed to this scenario, tie Ltd (tie) and the Council have undertaken planning for contingency measures to address potential funding issues. This approach looks at both additional funding and the possibility of incremental delivery.

Original Council Commitment

The Council's original commitment of £45m was made up from the following sources;

CEC Contribution Breakdown	Planned Contribution	Current Position v Plan
Council Cash	£2.5m	£2.5m
Council Land	£6.2m	£6.2m
Developer Contributions – Cash	£25.4m	£4.9m
Developer Contributions – Land	£1.2m	£1.2m
Capital Receipts (Development Gains)	£2.8m	£0.0m
Capital Receipts	£6.9m	£2.0m
Prudential Borrowing (in advance of developers contributions)		
Total	£45.0m	£16.8m

The Council's actual contribution to the project to date is £34m. £25m of this has been borrowed under the Prudential Framework in advance of receipt of Developers contributions and Capital Receipts.

Developers Contributions and Further Development

The Council's planning analysis shows that there is further development in the future that would enable CEC to realise the required contributions for the tram project.

These future developments are for the first and second phases of the Leith Docks development, Princes Street development and also the West Edinburgh Planning Framework. The full potential total contribution from these developments could be upwards of £26m. Currently there are £16m of contributions in the planning cycle. However, we have heavily discounted the total values from these developments, taking a pessimistic view on the pace and size of these potential developments to take account of the effect of the credit crunch. Based on these assumptions and the potential uplift in Capital Receipts, the Council could still achieve the required developers contributions in the 20 year time frame even if the scope of the project was reduced in the short term.

Capital Receipts

No receipts were received during the last financial year, and the forecast timescale for disposals is that nothing is expected before 2013, based on the current tram programme. It is likely that the level of developer interest in the residual sites will increase when confidence on the completion of the Tram Scheme is assured, as works are completed and test running commences.

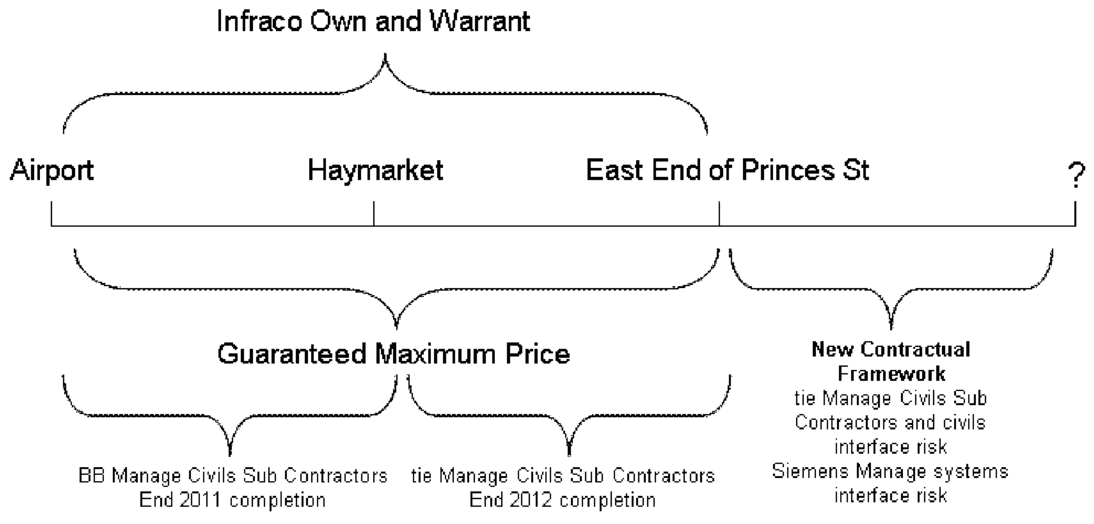
The best value for most of the sites is based on residential value. ESPC reported in April 2010 that house prices in Edinburgh are rising at 11.6% pa, with a 37% increase in transaction volume. This is, however, still below pre-credit-crunch levels.

The improvement in house selling prices will cascade into increased development value, and a positive differential between land value increase and borrowing rate interest. The prudent advice remains to consider the sale of these development sites when the unit value increases. This is expected as both the general housing market improves, and the tram works near completion.

The achievement of increased value remains less risky than the alternative of marketing now and seeking a share of value increases through an agreement – commonly known as gold clauses – which are difficult to enforce with reluctant partners.

Incremental Delivery

One of the contingency plans to ensure the affordability of Phase 1a is to construct the route on a phased basis. This strategy would also fit with tie's current negotiations to cease the Bilfinger Berger role as the civils partner in the consortium. A broad outline of the potential contractual arrangements under project Carlisle is demonstrated below;



From the financial analysis that has been undertaken it is forecast that incremental delivery option to St Andrew's Square/York Place could be delivered for the current committed funding of £545m.

The total amount of developers contributions in the Planning System total £16m. Should the tram be constructed in an incremental delivery fashion, from west to east, there may be implications for the receipt of developer contributions from developments towards the east. However, under the terms of the Tram Developer Contribution Guideline, the Council has until 2020 to utilise contributions received to date, meaning that as long as the full scope of the scheme from the Airport to Newhaven is constructed by 2020, the Council will not be required to repay contributions to developers at the eastern end of the route.
Of the £16m currently in the planning system, £4m relates to developments in the Leith area, although it should be noted that the development guideline means that if the development is within 750 metres of the tram line a contribution is triggered.

CEC Financial Contingency Planning
As reported to Full Council on the 24th June 2010, the Council have undertaken contingency planning up to 10% above the funding currently approved. It is currently considered that beyond this level of contingency the tram would become unaffordable for the Council. It is not beyond the realms of possibility that a tramway to the Foot of Leith Walk or even Ocean Terminal could be delivered for £600m.

The Council's contingency funding come primarily from two areas.
The Council has made an allowance of £2m per annum within its Long-Term Financial Plan (LTFP) to cover additional infrastructure development costs. The LTPF has been updated to reflect the Coalition Governments recent budget announcements. 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, but this will form party of the Council's budget considerations.

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.

The table below is an extract of the TEL Business Plan approved at Council meeting in August 2009.

Tram in service	**Pre-tram**		**Post Tram - Phase 1a**			
Tram service pattern	**n/a**	**n/a**	**6/12**	**8/16**	**8/16**	**8/16**
Year	**2006**	**2010**	**2012**	**2016**	**2021**	**2031**
Patronage (million)						
Bus	108.0	107.0	98.7	109.4	121.6	133.4
Tram	-	-	11.9	17.8	20.2	25.5
Total TEL Patronage	**108.0**	**107.0**	**110.6**	**127.3**	**141.8**	**158.9**
Bus Revenues (£million)						
Farebox	82.0	107.6	106.5	140.9	195.1	332.2
Other	6.0	6.9	7.3	8.4	9.7	12.9
Total Bus Revenues (a)	**88.0**	**114.5**	**113.8**	**149.3**	**204.8**	**345.1**
Tram Revenues (£million)						
Farebox	-	-	12.5	22.3	31.5	61.7
Other	-	-	0.7	0.9	1.1	1.4
Total Tram Revenues (b)	-	-	13.2	23.2	32.6	63.1
Total TEL Revenues (a + b)	**88.0**	**114.5**	**127.0**	**172.5**	**237.4**	**408.2**
Operating Costs (£million)						
Bus			107.3	133.7	186.0	339.3
Tram			17.3	22.1	32.0	52.4
TEL head office			2.0	1.7	2.1	2.9
Total TEL operating costs (c)			**126.6**	**157.5**	**220.1**	**394.6**
Pre-tax operating profit/loss (a + b) - c			**0.4**	**15.0**	**17.3**	**13.6**
Notional taxation			0.1	4.2	4.8	3.8
Dividend payment			-	2.6	3.0	4.1
Net TEL cash surplus/deficit			**0.3**	**8.2**	**9.5**	**5.7**

This table shows a level of profits by 2016 of £8.2 per annum with dividend payable to shareholders.

There is work underway at present to revise the business planning assumptions for TEL. This will include an update to the economic assumptions underpinning development in Edinburgh and the knock on effect to tram revenues. In addition the impact of incremental delivery on tram revenues is also under assessment. The initial work has indicated that a tram to York Place can make a small profit without subsidy from the wider TEL business. This work will continue at pace over the coming weeks and will be presented to Transport Scotland at the earliest opportunity to aid the decision making process for project Carlisle.

Taking all over the above information into account, the Council would consider funding up to 10% above the current approved funding level achievable.