CEC Tram Funding

Contingency Measures

16th June 2009

Introduction

This report seeks to evaluate funding measures the Council may require to find in the event that either the tram project exceeds the funding envelope of £545m or the Council is unsuccessful in securing the required contributions from developers under Section 75 agreements or from capital receipts due to falling land values. The detail of the Council's contribution secured to date excluding prudential borrowing to date is highlighted in the table below. There is a substantial degree of risk now relating to the planned contributions from developers and from capital receipts due to the economic downturn. These funding streams are currently being evaluated by DTZ with a view to reporting by the end of June on their findings, the result of which will help inform the extent of risk the Council face on the original assumptions. In the event that the Council cannot achieve the planned contribution in these areas we will have to find alternative funding sources to fund our £45m contribution.

CEC Contribution Breakdown	Planned Contribution	Achieved Contribution
Council Cash	£2.5m	£2.5m
Council Land	£6.2m	£4.3m
Developer Contributions – Cash*	£25.4m	£3.2m
Developer Contributions – Land	£1.2m	£1.2m
Capital Receipts (Development Gains)	£2.8m	£0.0m
Capital Receipts	£6.9m	£2.0m
Total	**£45.0m**	**£13.2m**

Current Risks to Funding

Currently there are risks to the Council's funding position related to both any potential cost overrun of Phase 1a and funding gaps related to the Council's current funding of the £45m.

The current position assumes funding of £45m from developers contributions and a further £9.7m in capital receipts. To date the Council have secured

£3.2m of developers contributions, agreement with Forth Ports on their level of contribution for the Leith Docks development would significantly de-risk the Council's current funding requirement. In assessing the affordability of Phase 1a of the tram, which may lead to suggestions of curtailment of the line before Newhaven, the impact on developers contributions as a result of this action will have to be considered. Curtailment at Ocean Terminal produces no great loss in contributions. Should curtailment at the foot of the Leith walk, or any point before be considered, the impact on contributions would be very significant with lost contributions of £30m if Phase 1a doesn't run to Ocean Terminal.

Capital receipts contribute £9.7m to the £45m. The original estimate of the site's in relation to tram was in the region of £13m. A reassessment of these values has subsequently been undertaken which show that these sites are now worth £7.4m although any upturn in the market would obviously have a positive effect.

Strategic Options

Following the delay on commencement of Princes Street infrastructure works in February 2009 tie produced a range of options on the commercial position with Infraco. These options range from replacing Infraco to continuing all matters through the Dispute Resolution Process and highlighting the monetary impact of these options. Following engagement with Council officers these options were expanded to look at scope truncation and cancellation costs. tie have been refining the strategic options work streams as more information becomes available on programme and costs issues arising from the Project Management Panel and the DRP process. Regular updates have been given to the Tram Project Board on the outputs of this work with the preferred option being continuation with BSC while working through the commercial issues in PMP and DRP.

tie have committed to providing a commercially agreed programme and re-calibrated budget with BSC in time for a report going to the Council meeting of 20th August 2009. tie have also been asked to provide a range of confidence levels and residual risks on the project being delivered within the £545m budget. It is imperative that Council officers have full visibility and understanding of the assumptions that back up the numbers. tie have also been asked to provide the most up to date view at various time intervals as to the cost of project cancellation and scope truncation. Once this information is available it will provide some indication as to any further funding requirement in tandem with the expected revised agreed programme.

DTZ Evaluation

As previously mentioned, DTZ are currently working with Council officers from City Development and Finance on the robustness of the Councils funding strategy for tram in light of the current economic crisis. The main areas under evaluation are;

- Funding assumptions relating to Developer's contributions
- Funding assumptions relating to Capital Receipts
- Financial Modelling assumptions

It is expected that DTZ will report back to Council officers by the end of June, though it is envisaged that this exercise be reviewed on a six monthly basis given the uncertainty in the economy.

A further update will be produced once the report from DTZ is available and the financial impact has been assessed.

Potential Funding Options

In light of the risks highlighted above it is prudent that the Council look at contingency planning should we require further funding sources. Some initial options are explored below.

1. **Prudential Borrowing secured against future TEL revenues.**

   The TEL Business Plan assumes a level of profits from which could support interests costs of £2m per annum from 2016. This translates to £25m worth of borrowing. Lothian Buses have historically paid the Council an annual dividend of £2m.

   The risks related to this option would be that the operating profits of TEL are adversely affected by external factors that cannot support the level of borrowing the Council has made.

2. **Prudential Borrowing with costs of borrowing paid by CEC revenue budgets.**

   The Council could borrow £25m that would have a revenue impact of £2m per annum. This option would create further pressure on the Council's revenue budget and would have to be taken into account when the Council sets its budget.

3. **Substitute against spending on other CEC Capital projects**

   The Council set its capital programme in February 2009 that highlighted £67m for 2011/12 £64m for 2012/13. Should the Council take the decision to re-direct funding from other projects this would have a serious impact on important priorities such as Asset Maintenance, Schools and Flood Prevention.

4. **Prudential Borrowing funded by future lease payments**

   Once tram is operation, current tax planning assumptions are that the Council, who will own the assets from the project, will lease the assets to TEL. This will allow TEL to reduce their CT exposure and will allow the

Council to benefit from an additional revenue stream. By structuring the lease agreement to dovetail with the expected ramp up in TEL's operating profits would mean that the Council could borrow on future income streams while making the leasing arrangements affordable to TEL.

5. Further Scottish Government Funding

Given the current pressures on the public purse and competing priorities it is unlikely that this option could provide any additional funding. This is not to say that should the need arise that the option should not be explored.

6. Tax Incremental Financing (TIF)

TIF had previously been explored as a funding stream for Phase 1b. This proposal works through ring-fencing the uplift in business rates for new businesses in a particular area to fund investment. It is unlikely that this proposal would provide any other funding.

7. Sale of Assets to Private Sector

The Council could choose to sell tram assets to a private sector partner to free up capital. The Council would then lease the assets back at an annual charge. This option would be impacted on by the terms of the funding agreement with Transport Scotland whereby sale out with the Council group would result in the Council having to payback 91.7% of the funded assets.

A Coyle
01/06/2015