Trams for Edinburgh
...connecting our Capital

Edinburgh Tram Network

Phase 1 a

Evaluation of Strategic Options

Summary

The purpose of this report is to update Council senior management on the strategic options put forward by tie and commenting on additional considerations the Council may face in light of the recent developments in the DRP. The options put forward by tie as well as some other issues are given consideration below.

Strategic Commercial Options Considered

Five commercial options had been presented to the Tram Project Board by tie. Three of these options have now been considered as sub optimal.

- **Option A Termination of the Infraco contract** – even if tie were confident on valid grounds to terminate, it would mean losing the whole contract presently in place, including the Siemens and CAF capability, tie are broadly satisfied with and the supply chain Bilfinger have now assembled. This option also presents very significant uncertainties with regard to an acceptable re-procurement timescale and pricing as well as the greatest risk of loss of stakeholder support for the project. In all likelihood re-procurement would mean cancellation due to lack of affordability. There must also be concern as to whether this option, with a delayed funding profile, would fit in with the Scottish Government's (Transport Scotland) financial programme.

- **Option C tie step into the civils role** – discounted due to the additional risks and interfaces tie would need to manage. In addition, this conflicts with what was set out in the Business Case.

- **Option D Negotiate a settlement of contractual disputes and programme** – in essence this is what Bilfinger want and is likely to be a very (likely prohibitively) expensive option indeed. Under the current Bilfinger stance this would involve working on a 'cost plus' basis out with the contract to be able to make acceptable progress with construction. Due to the quantum of BB's suggested demands this option could also have procurement law implications making it unworkable in any event.

A further two options remain from tie's original proposal. It should be stressed that the cost estimates featured are in their infancy; further detailed analysis of the numbers is required.

Option B Facilitate the removal of BB and replacement with new civils partner (Estimated Cost range from £573m to £593m) - In the event tie are unable to reach an acceptable commercial outcome with BB and/or are unable to satisfy stakeholders that BB are willing and able to deliver the project in accordance with the contract then this is an attractive option. There is still a conviction that Siemens and CAF are the right partners to deliver the technically specialist areas of the project.

However, the dispute is with the consortium as a whole and any decision to remove BB would have to be made by the other consortium partners, not by tie. This presents the challenge of exploring the position and objectives of Siemens within the consortium.

A core part of tie's tactics to deliver Option B would be to:

- Emphasise the delayed start to e.g. Princes St, the attendant risk to reputation and demonstrate resolve and thereby bring about greater influence by Siemens in both the management of the project on the ground and in senior level engagement.
- Keep Siemens well briefed on the nature and extent of the principal contractual disputes faced and the detailed analysis of the issues and BB's delivery shortcomings whilst progressing a targeted DRP campaign. (It should be considered whether tie/CEC can legitimately brief against one consortium partner to another?)

tie believe that Siemens material prices largely hold firm but that programme delay and disruption is a serious concern to them.

It seems likely that should the replacement of the civils partner ultimately become desirable and necessary, the best result in terms of minimising time and cost impacts would be for Siemens themselves or the civils arm of their track work subcontractor BAM to undertake the role. Intuitively this would minimise the time to reassemble the complete consortium and it may be the case that the premium Siemens would try to negotiate to take on the civils work to be lower than that required by a new civils partner.

If BB were to be replaced, the best outcome would be a preservation of the assembled BB supply chain as much as practicable and a continuation with programme critical activities whilst the new arrangements were being negotiated and put in effect.

Further Option B Considerations

- Time delay associated with management of civils work. If a new civils partner was brought in as part of the consortium, it is possible that there would be "material change" and procurement rule implications as well as costs analysis required to demonstrate best value. This may not allow option B to be viable at all. DLA should perhaps be asked to comment on this ASAP.
- The Council/tie would have to perform due diligence on the new consortium formation.
- Time delay to movement on programme due to Siemens and CAF weighing up their options regarding a new civils partner or management there of.
- Threat to programme and cost resulting from BB action on remaining consortium members in the event they were ejected.

Option E Pursue the settlement of all significant contractual disputes through the DRP under the contract (Estimated Cost £571m) - In the analysis of all options above it seems clear that if there is to be no significant u-turn by the BSC consortium on the significant contractual points in dispute then the best outcome in any case will be served by a prompt and uncompromising progression of the disputed matters through the DRP process.

The time imperative is critical – the DRP process is governed by strict timetables and whilst tie cannot in any way compromise upon the quality of submission made in each case it will require the indulgence of stakeholders with regard to continuing uncertainty and continued expenditure on the project whilst we go through DRP until resolution is reached on all significant matters.

Two broad but possibly challenging priorities are faced in the conduct of the DRP process in that tie want to refer issues in a way which will best facilitate the progression of the most urgent works to mitigate further delay to the programme and therefore delay related costs, but at the same time tie want to establish the position on the broader points of dispute as quickly as possible to provide stakeholder comfort on costs and programme.

It should be noted that taking the costs quoted by tie under the two options above, we are now into the territory of potentially de-scoping the project to maintain affordability in the event that no other marginal cost savings can be made. It is imperative that a thorough evaluation of project costs is undertaken.

The options outlined by tie generally pre-suppose successful conclusion of the DRP, any decisions on options before conclusion of DRP would be risky.

Further Option E Considerations

- tie have acknowledged that the very future of the project may rest on the ability of tie to be successful on all major points of contractual principle in dispute. It is therefore imperative that CEC is certain that tie's defences and arguments are absolutely robust prior to a relationship-threatening legal battle.
- The life of the project cannot be managed in this manner. Contingency planning for other options would have to be made in the event that DRP was enacted on many issues. This would prove costly and time consuming. DRP can only be a short term solution to problems in the hope that commercial settlement in tie's favour brings about a change in attitude of BB.
- Even if tie are successful with their arguments, there is the significant possibility that BB will still not engage fully and will seek to claw back any and all costs throughout the remainder of the project. I.e. it will cause commercial animosity and point-scoring which is not conducive to a good relationship and consequential cost balancing.
- It is not clear to CEC what rights exist under the contract. If for example, tie are 100% successful in their arguments, does this entitle tie to compensation from BSC to the full extent of the delay and associated cost overruns. This requires clarification as the risk/reward matrix may shift if it does not.

Strategic Scope Options

In light of the recent commercial dispute it is prudent to evaluate any options relating to scope principally to examine what can be delivered within the funding constraints.

- **Curtailment from Edinburgh Airport –** Services to Edinburgh Airport fulfils the Scottish Governments objective of a fixed transport link to the Airport following the termination of EARL. This would be highly unacceptable to stakeholders.
- **Curtailment from Newhaven –** This represents minimal impact on the business case and may drive out savings of up to £15m, this saving is likely to be less due to requirement to re-design and implement the turn around points. The impact on the Councils S75 contribution would be £43k.
- **Curtailment from Foot of the Walk** – This has major implications for the Councils S75 agreement with Forth Ports. Even should the extension to Ocean Terminal form a future piece of construction, the Council needs the Forth Ports contribution to

fund current borrowing. This option would also increase bus service costs and is likely to be unacceptable to the Scottish Government as it does not service Victoria Quay. The impact on the Councils S75 contribution would be in the region of £30m based on the Forth Ports agreement and S75 land at Western Harbour.

Any of the above scenarios may require, if Transport Scotland insists, a refresh of the STAG and a recalculation of the BCR which could take several months. If these options were to be considered, early commencement of this work would be advisable.

Further considerations of any change in scope would be;

- Business Case impact and loss of patronage.
- Impact on Transport Scotland funding, would they be willing to provide funding of £500m for less infrastructure.
- Could BSC claim loss of profits for de-scoping, this would have to be set off against any savings.

Project Cancellation – While clearly the nuclear scenario, consideration would have to be given to the following factors should there be no other option especially with the project becoming increasingly unaffordable to the Council.

- It has to be borne in mind that tie's latest cost analysis figures are likely to be conservative and are being predicted at a time when the project is still a long way from completion. There is clearly scope for further increases as the project evolves. This could have serious consequences for the Council's funding requirements.
- Payback of Transport Scotland funding, resources required for cost recovery through Bonds and PCG's and the risk of BSC legal fight.
- Transport Scotland could insist on project cancellation due to escalating costs. In this event insistence on payback of grant would be unlikely although commitment would be needed from TS that costs of project cancellation would be funded. This would be a better scenario for the Council than the Council cancelling the project.
- If the Council cancels the project could BSC fight the Council for breach of contract and loss of profits? The mechanism here would be that the Council instructs **tie** to terminate the contract. Such a course of action is then likely to produce a claim against **tie** and the Council. The case against the Council would proceed on the basis that it had encouraged tie to breach the contract.
- There may still be room for a divergence of views between the Council and tie about cancellation or continuation of the contract. In the event of a disagreement, the Council's view would have to prevail given that it has funding obligations and liabilities,

whereas although **tie** is the contracting party it is also just an agent of the Council

- tie wind up costs – legally unlikely that the Council would be on the hook however morally there could be an obligation on the Council for redundancy costs etc.

This report is submitted without the benefit of the responses to a series of legal questions submitted to DLA on 5 March 2009.