

Risk to INFRACO Contract Award

INFRACO works are expected to commence in September 2008. Positive engagement between EAL and BBS is ongoing and as a result, risk to award of INFRACO Contract is considered low.

Network Rail (NR) agreements – general

The suite of NR agreements comprises the following :

- Asset Protection Agreement
- Station & Depot Change (NR with the Train Operating Companies)
- Framework Agreement
- Lease and Servitude Agreements
- Neighbour Agreement
- Bridge Agreement and Lease
- Lift & Shift Agreement
- Immunisation

5.10 Network Rail Asset Protection Agreement *

Purpose of the Agreement

The APA is an agreement between NR and CEC which governs design/construction activities as well as access to Network Rail land. The APA is designed to ensure that the heavy rail network can operate in tandem with the construction and commissioning of the ETN.

Current Status of Agreement

The APA has been signed.

Risk to INFRACO Contract Award

This allows INFRACO to undertake works on NR land and there is consequently no material risk.

Additional comment provided by DLA

The Asset Protection Agreement with NR has been concluded. This has been an arduous process, however the outcome is a document which achieves significant commercial improvements for tie/CEC on what was originally offered by Network Rail. The arrangement is nevertheless heavily tilted in Network Rail's favour, as is inevitable given the starting point of the biased regulatory template agreements. The main improvements secured have been:

- *Significant widening of the circumstances in which tie can recover money from Network Rail;*
- *Reasonableness in Network Rail actions and ability to refer to the Infraco ETN Suite form of Dispute Resolution Procedure;*
- *Dilution of indemnities given by tie to Network Rail to a mutually acceptable level.*

The unreasonable position taken by Network Rail regarding the indemnities contained in the Protection Provisions Agreements (entered into to remove Network Rail's objection to the tram scheme) delayed closure for a considerable time. This has now been resolved to restrict the scope and duration of this indemnity, particularly during construction.

5.11 Network Rail Depot Change *

Purpose of Document

This is a regulated process between Network Rail and First ScotRail, the operator of the Haymarket Light Maintenance Depot. Depot change is the process which defines the revised lease arrangements which will be required as a result of the tram construction and operation. This procedure also defines the methodology of undertaking works in the vicinity of the Haymarket Depot and sets out the interface requirements of the Depot Manager. A key requirement of FSR is that only one contractor (at a single work site) will be permitted to conduct works within the depot area at any given time. BBS, NR and First ScotRail are working together to ensure that this requirement can be met.

Current Status of Document

The formal submission of the Depot Change (by NR) to FSR was completed on 11/01/08. The regulated process allows for a maximum review period of 45 calendar days for comments to be submitted. FRS notified NR on 04/03/08 of their acceptance of the Depot Change proposal. The confirmed Depot Change Proposal was sent to the ORR for ratification on 07/04/08.

Risk to INFRACO Contract Award

INFRACO works at Haymarket Depot are scheduled for commencement after completion of the NR Pollution Prevention Works Contract (PPLMD). tie, BBS and NR are currently working to integrate the two programmes in order to minimise the risk of delay to INFRACO. At present, NR expect the PPMLD works to be completed at the end of September 2008, with INFRACO works scheduled to commence on the Roseburn Street Viaduct in January 2009.

The Risk to award of INFRACO Contract is therefore considered low.

5.12 Network Rail Station Change *

Purpose of Document

This is a regulated process between Network Rail and First ScotRail as the operator of Haymarket Station. The Station Change procedure also requires the consent of the other Train Operating Companies (TOC's) using the station and these are; Arriva Cross Country, Virgin, Trans Pennine Express, National Express East Coast and EWC.

The station change concerns the permanent loss of 49 parking spaces at Haymarket Station Car Park and the temporary closure of the car park as a result of the construction of the Haymarket Viaduct and Tram Stop, as well as the relocation of taxis currently operating from the forecourt of station.

Current Status of Document

NR formally submitted the Station Change proposal to FSR on 16/01/08, which triggers the start of the 45 calendar day consultation process which ended on 01/03/08. FRS notified NR on 04/03/08 of their acceptance of the Station Change proposal. The confirmed Station Change Proposal was sent to the ORR for ratification on 07/04/08.

Risk to INFRACO Contract Award

As the Station Change proposal has been accepted by FSR and the other train operating companies who use Haymarket Station, the Risk to award of INFRACO Contract is considered minimal.

5.13 Car Park Compensation Agreements

Purpose of Document

The loss of income generating car park spaces at Haymarket Station is a compensation matter for both NR and FSR. Under Station Change, FRS receives a standard indemnity from Network Rail to cover losses, so the commercial arrangements can be negotiated separately and do not form part of the Station Change approval process.

Current Status of Document

FSR have confirmed that the compensation formulae adopted for the Platform Zero settlement will be used as a basis for this negotiation, reflecting the duration of the FSR franchise. An estimate of the likely compensation to NR has been prepared with input from the District Valuer. The Valuer's internal calculations on this basis indicate that the final compensation settlement is likely to be within the current budget allowance.

Risk to INFRACO Contract Award

The compensation settlement to both NR and FSR are commercial arrangements which have a budget allocation within the FBC and are not part of the Station Change approval process. There is therefore minimal risk to the award of the INFRACO contract.

5.14 Network Rail Framework Agreement *

Purpose of Agreement

This is an overarching document beneath which reside a suite of construction, property and operations related agreements.

Current Status of Agreement

The Framework agreement has been approved by Network Rail management and legal advisors and we are awaiting formal signature by NR London.

Risk to INFRACO Contract Award

The agreement is not construction related and therefore represents minimal risk to award of the INFRACO contract.

5.15 Network Rail Lease Agreements & Servitudes

Purpose of Document

Two leases are proposed, the first; with NR as landlord is a 175 year lease to allow operation of the ETN on NR owned land. The second lease is with CEC as landlord and allows NR to use the relocated car park at Haymarket Depot. The servitude agreements for Balgreen Road and Haymarket Station allow NR rights of access to the railway and NR owned infrastructure over CEC owned land.

Current Status of the Agreements

The documents are in agreed and final form. The tram lease does not become active until after construction and commissioning have been completed, and is suspensive on the execution of an Operating Agreement with Network Rail.

Risk to INFRACO Contract Award

These documents are not construction related, so the Risk to award of INFRACO Contract is insignificant.

5.16 Forth Ports Agreement

Purpose of Agreement

The original "Minute of Agreement" between CEC and Forth Ports was signed in February 2006 and sets out a range of requirements for the SDS design in key areas of Forth Ports land. A variation of the Minute of Agreement was documented in Heads of Terms in November 2007. The variation related to changes requested by FP to the design which will be funded by Forth Ports.

Current Status of Agreements

Forth Ports have stated that they have a concern about the composition of the baseline design in one specific area (Lindsay Road junction) against which future changes will be measured and funded by FP. Resolution of this matter will now delay signing the agreement with FP and depends on the final agreed scope of junction works at Ocean Drive West and the extent of funding from Forth Ports to support their aspirations.

The transfer of land from Forth Ports to CEC will be part of the FP contribution to the project, and this is part of the existing Section 75 agreement.

Risk to INFRACO Contract Award

This agreement should not impede signing of the Infraco contract. Although tie believes there is an important principle at stake which FP have sought to revise inappropriately, there is common ground on the design aspiration and the solution will emerge from the joint assessment of design options. The matter is assessed in risk terms at Section 8.5 below.

5.17 Stanley Casinos Agreement

The Stanley Casinos side agreement is also design dependant and is in agreed form and takes cognisance of the revised junction and access proposals at the Constitution Street/Ocean Drive junction. The agreement will also include provision for remodelling the Casino car Park. There is no risk to award of the INFRACO Contract.

5.18 Other Site Specific Code of Construction Plans

Purpose of Documents

As part of the suite of side agreements drawn down into Schedule 14 of the INFRACO Contract, there is a requirement in several agreements for the contractor to develop a local construction plan or CoCP as part of the notification/consultation process in advance of the works commencement. The relevant agreements are:

- USS
- Safeway/Morrisons
- Murrayfield Indoor Sports Club
- ADM Milling
- Ocean Terminal
- Royal Yacht Britannia
- Baird Drive Residents (Community Liaison Group undertaking)

Current Status of Documents

tie and BBS have prepared a suite of drafts setting out the construction related requirements of the relevant side agreements.

It is notable that the construction requirements laid down in these side agreements generally relate to those aspects of site working such as confirmation of programme, maintenance of access during the works, pedestrian management, dealing with dust/noise, site cleanliness, reinstatement of property etc, that one would normally expect a competent contractor to be cognisant of.

Risk to INFRACO Contract Award

All relevant 3rd Party agreements are detailed within the INFRACO contract in Schedule 14. The requirements on Infraco are entirely in line with normal construction practice and the risk to CEC for award of the INFRACO contract is considered low.

5.19 Licence – The Gyle

Purpose of Document

The licence will allow the INFRACO contractor to undertake the works within Gyle owned land prior to permanent acquisition. In agreeing to undertake this work under licence, CEC will be able to meet the terms of the existing side agreement whereby permanent land take is to be minimised. At this stage in the design process, SDS cannot define with certainty the extent of the operational land. The proposal made to The Gyle is therefore to defer permanent acquisition until this certainty is available.

The acquisition of the 'as built' operational land will eliminate the risk of not meeting the obligations of the side agreement. The existing side agreement already makes provision for a licence to undertake works.

Current Status of Agreement

The Gyle have accepted the proposal to construct the works under licence. The licence is now signed.

Risk to INFRACO Contract Award

INFRACO works are expected to commence in the vicinity of The Gyle from June 2008. There is no risk to the award of the INFRACO contract.

5.20 Licence – West Craigs

Purpose of Document

The licence will allow the INFRACO contractor to undertake the works within West Craigs owned land prior to permanent acquisition. In agreeing to undertake this work under licence, CEC will be able to meet the terms of the existing side agreement whereby permanent land take is to be minimised. At this stage in the design process, SDS cannot define with certainty the extent of the operational land. The proposal made to West Craigs is therefore to defer permanent acquisition until this certainty is available.

The acquisition of the 'as built' operational land will eliminate the risk of not meeting the obligations of the side agreement. The existing side agreement already makes provision for a licence to undertake works.

Current Status of Agreement

The license is now signed.

Risk to INFRACO Contract Award

INFRACO works are expected to commence on the proposed licence site from January 2009. There is no risk to award of the INFRACO contract.

5.21 Network Rail – Neighbour Agreement

Purpose of Agreement

This agreement sets out the benefited and burdened property between CEC and Network Rail land. This agreement ensures that access to the railway network across tram land is maintained at specified points, and defines the various structures supporting the adjacent heavy rail property.

Current Status of the Agreement

The neighbour agreement is in agreed and final form and does not get signed per se, but rather the agreed burdened property plans are registered with The Keeper (Registers of Scotland). This will happen when the framework agreement is returned

Risk to INFRACO Contract Award

The Neighbour Agreement is a non-construction related document, and for this reason, it offers insignificant risk to CEC for award of the INFRACO Contract.

5.22 Network Rail – Operating Agreement

Purpose of Agreement

The purpose of the operating agreement is to set out operational interface arrangements and procedures for running tram passenger services adjacent to the railway line. This agreement will be an evolving document which will be updated periodically during the lifetime of the project.

Current Status of Agreement

A draft is current under review by tie and TEL. The intention is to develop this document into draft agreement form during the first quarter of 2008, and complete the agreement prior to commencement of passenger services.

Risk to INFRACO Contract Award

The Operating Agreement is a non-construction related document and the risk to award of INFRACO Contract is considered low.

5.23 Network Rail – Bridge Agreement & Bridge Lease

Purpose of Agreement

The purpose of the Bridge Agreement and Bridge Lease is to allow operation of the ETN and set ongoing maintenance and operational responsibilities for the Carrick Knowe and Edinburgh Park Station Bridges, as these structures interface directly with the heavy rail network. The APA governs the construction of these bridges.

Current Status of Agreement

The framework agreement sets out that NR and CEC will work together, both acting reasonably, to develop a post construction Bridge Agreement. CEC will not be exposed to future network enhancement costs in relation to bridges.

Risk to INFRACO Contract Award

The Bridge Agreement is a non-construction related document, and for this reason, it offers insignificant risk to CEC for award of the INFRACO Contract.

5.24 Telewest utility agreement

Purpose of Agreement

The purpose of the Agreement is to set out how the diversion of utilities owned by Telewest are to be managed during the MUDFA works.

Current Status of Agreement

The contract has now been signed.

Risk to INFRACO Contract Award

This is a MUDFA related agreement, and as a result it offers insignificant risk to CEC for award of the INFRACO Contract.

5.25 Scottish Power utility agreement

Purpose of Agreement

The purpose of the Agreement is to set out how the diversion of utilities owned by Scottish Power are to be managed during the MUDFA works.

Current Status of Agreement

The agreement is in agreed and final form, and the return of the signed, engrossed agreement is awaited from Scottish Power.

Risk to INFRACO Contract Award

This is a MUDFA related agreement, and as a result it offers insignificant risk to CEC for award of the INFRACO Contract.

5.26 DPOFA 2007 Revision

A negotiation was concluded with Transdev to amend the DPOFA signed in 2004. The process is now complete and the principal agreed changes relate to :

- Improved performance bond underpinning both mobilisation and operating obligations
- Alignment with Infraco contract where previous drafting was based on anticipated Infraco terms
- Scope revised to reflect the Phase 1a / 1b configuration from the originally anticipated Lines 1 and 2
- Revisals to KPI performance regime based on up to date commercial view.
- Replacement of original tram revenue incentive mechanism with a reduced cost recharge, reflecting a fully integrated bus and tram system
- Alignment of insurance arrangements under OCIP
- Obtained tram cost synergy savings with introduction of TEL being responsible for transport integration

5.27 Mobilisation agreements (Infraco and Tramco)

The pre-close mobilization agreements with Infraco and Tramco are designed to enable works necessary to maintain programme. The agreements are The Advance Works and Mobilisation Contract ("AWM") and Tram Advance Works Contract ("TAW").

The core of the AWM is that Infraco will perform a schedule of works with payment determined by "Agreed Element Estimates" agreed by the parties in respect of each element of work.

The AWM does not overlap with the Infraco Contract because, when the Infraco Contract is entered into, the AWM automatically terminates. The Infraco Contract therefore deals with payment and other terms relating to advance works underway at that time. The TAW works similarly, in that it ends automatically when the Tram Supply Agreement is entered into.

(6) Land acquisition arrangements

Purpose of process

The process of assembling land required for the construction and operation of the Edinburgh Tram Network has been managed using a combination of Compulsory Purchase (using the General Vesting Declaration Procedure), and entering into long term lease arrangements with Network Rail and Edinburgh Airport Limited.

Current Status of Agreement

By financial close, the position in regard to Land available to INFRACO is as follows:

Nature Of Land	Land Area (sqm)	Available to INFRACO	Land Take Achieved	Target Date	No Plots
Pre GVD	498	Yes	0.1%	Nov-05	3
GVD 1&2	177467	Yes	21.0%	Feb-07	43
GVD 3	167854	Yes	19.9%	Jul-07	22
GVD4	43323	Yes	5.1%	Sep-07	19
GVD5	2381	Yes	0.3%	Dec-07	5
GVD6	83588	Yes	9.9%	Dec-07	17
Licences	24885	Yes	2.9%	Jan-08	14
BAA Licence	18388	Yes	2.2%	Nov-07	17
NR APA	42480	Yes	5.0%	Feb-08	37
Forth Ports (S75)	80293	Yes	9.5%	Mar-08	51
Adopted Roads	202521	Yes	24.0%	Achieved	78
	843679		100.0%	Total	306

Of the total land required, 85.5 % is under the control of CEC through ownership or license, a further 9.5% is committed under Forth Ports existing S75 agreement with the balance of 5% subject to the Network Rail APA agreement which has now been signed.

(7) Governance & corporate arrangements

7.1 Governance & delegations

The Governance model deployed to oversee and control the project has evolved as the project itself has moved through different stages of development. Appendix 2 is a detailed paper which was approved by the Boards on 23rd January 2008 and which has been updated to reflect the final position as at Financial Close. The paper sets out :

- 1) the proposed governance model for the construction period ; and
- 2) the proposed levels of delegated authority

The paper is an update of previous submissions to the Boards and differs only in two material respects – the inclusion of specific levels of delegated authority and alignment with the terms of the tie and TEL Operating Agreements (see below). Neither of these factors should cause concern : the levels of delegated authority are in line with those previously deployed by the TPB and the terms of the operating agreements have been subject to significant scrutiny by senior people over recent months.

7.2 Operating agreements

These agreements are now in final agreed form.

tie

The tie agreement was previously reviewed by the tie Board in December 2007 and the changes since then are in line with the request made by the tie Board. The tie agreement supercedes the existing agreement on matters relating to the tram project and sets out tie and the Council's mutual responsibilities for delivering the tram project.

TEL

The TEL agreement reflects TEL's role but the detailed wording is consistent with the tie agreement. The TEL agreement sets out the specific authority delegated to it by the Council with acknowledgement that TEL will sub-delegate its authority to the TPB.

These internal agreements have been settled, where possible, taking account of DLA Piper's advice to tie and CEC in relation to (i) their acceptability as evidence of agency authority to transact and (ii) their potential adverse impact on the project's strategy towards competition law.

7.3 Taxation

Advice has been taken from PwC on two principle areas :

- 1) The tax effect of the Infraco contract suite structure ; and
- 2) The VAT status of the grant funding

The main objective in tax planning has been to ensure that the arrangements were VAT neutral such that there would be no irrecoverable input VAT and that no unforeseen output VAT would require to be accounted for. We have a formal report from PwC addressed to tie, CEC and TEL confirming this. We have also engaged with HMRC and have a clearance letter from them confirming that the objective is achieved. The contract structure has also been assessed by PwC to ensure that it will be possible in due course to establish a cost base in TEL by either selling or leasing system assets owned by CEC which will create corporation tax shelter in TEL. This could prove very valuable over the operating period of the integrated system.

(8) Risk assessment of in-process and provisional arrangements

This section contributed by Stewart McGarrity, who reviewed those areas of the documents which are provisional in nature and the documents which will be in draft form at Close.

THE MATERIAL IN THIS SECTION IS COMMERCIALY CONFIDENTIAL AND FOISA EXEMPT.

8.1 Overview

tie's approach to identifying and managing risks was fully explained in the Final Business Case. This section reviews the current status of the risks relating to the Infraco and Tramco contracts which have been identified as wholly or partly retained by the public sector beyond Financial Close which are:

- The process for granting of approvals and consents;
- The process for granting of permanent TRO's
- The interface with the implementation of utility diversion works
- Delays to design approvals for reasons outside the control of the Infraco
- Stakeholder instructed design changes

Specific areas covered are:

- Price certainty achieved through the Infraco and Tramco contracts with a view on items included in the contract price which will remain provisional at Financial Close
- Specific exclusions from the Infraco contract price
- Responsibility for consents and approvals

And as an area of particular concern to stakeholders:

- The risks associated with significant 3rd Party Agreements not concluded in full at Financial Close.

8.2 Price certainty achieved

The Tramco price agreed at £55m is a fixed sum in pounds sterling for the supply of trams. The overall capital costs estimate for Tramco also includes fixed sums totalling £3.0m for mobilisation costs associated with the maintenance contract and items of equipment for the depot which will be paid prior to the commencement of operations.

The Infraco price of £234.0mm comprises

- £228.3m of firm costs
- less £13.7m of Value Engineering initiatives taken into the price with the agreement of BBS but with qualifications attached
- plus £19.4m of items which remain provisional at Financial Close.

A thorough risk appraisal has been carried out on the deliverability of the Value Engineering initiatives with reference to the qualifications which attach to them. As a result a prudent allowance of £4m has been made against the possibility that for certain items these qualifications will not be removed (of which £2m has been included in the base cost estimate for Infraco and £2m has been included in the overall risk Allowance for the project).

Provisional items comprise a defined list of 22 items each with a clear process for and programme for resolution. The estimate for each item has been reviewed by tie's technical consultants and by BBS and the risk of understatement is considered to be low. The most significant items are a £6.3m allowance for civil works, including utilities, at Picardy Place as the design for the approved layout is not yet complete. (the cost of the actual tramway, tram stop and associated works at Picardy Place are included in the firm element of the price) ; £3.1m in respect of works which may be carried out on behalf of 3rd parties (eg Forth Ports) and which are recoverable from those third parties and a £5.0m allowance for Urban Traffic Control works (traffic lights) associated with the implementation of the project.

The overall capital cost estimate for Infraco includes a further £5.0m, comprising £2.6m for maintenance mobilisation (as for Tramco), and £1m for major spare parts based upon a schedule of prices provided by Infraco and a £1.0m provision for known design changes at the Airport tram stop yet to be included in the Infraco price and £1.4m for other items for which the status or procurement method are yet to be finalised.

8.3 Infraco price basis and exclusions

The Infraco price is based upon the Employers Requirements which have been in turn subject to thorough quality assurance and the significant areas where post contract alignment of the SDS design will be required. Crucially the price includes for normal design development (through to the completion of the consents and approvals process – see below) meaning the evolution of design to construction stage and excluding changes if design principle shape form and outline specification as per the Employers Requirements. The responsibility for consents and approvals is further considered below.

Significant exclusions from the Infraco price are items not included in the Employers Requirements in respect of (responsibility for securing incremental sources of funding in brackets):

- Additional works at Picardy Place, London Road and York place (CEC)
- Additional works at Bernard Street (CEC)
- Full footway reconstruction in Leith Walk (CEC)
- Additional works in St Andrew Square outwith the tram alignment (CEC)
- Changes within the Forth Ports area (Forth Ports)
- Any other scope required by third parties not already included in the Employers Requirements by virtue of a commitment in an existing agreement

8.4 Responsibility for consents and approvals

As previously tie/CEC will retain the risk associated with the process of obtaining TROs and TTROs (some for TTROs post-Service Commencement which are Infraco's responsibility). Full provision has been made in the Risk Allowance for the possible costs associated with a legal challenge to the TRO process which it is not anticipated will include a formal public hearing.

As fully detailed in Appendix 1, for all other required consents and approvals (either design or construction related) the principles which apply are:

1. Infraco (including SDS) will bear any costs and programme consequences associated with design quality and constructability for all consented and/or approved design.
2. in respect of consents and approvals outstanding at Financial Close, tie/CEC will bear any incremental construction programme cost consequences of SDS failure to deliver design outputs in a timely and sufficient manner to the consenting or approving

authority insofar as the cost is not recoverable by Infraco from SDS under a capped liquidated damages provision or can otherwise be mitigated by the Infraco.

3. tie/CEC will bear the incremental cost and programme consequences associated with a delay in granting consents or approval having received the required information in a timely and sufficient manner and/or the cost and programme consequences of changes to design principle shape form and outline specification (as per the Employers Requirements) required to obtain the consent or approval.

Taking due cognisance of all mitigations described in Appendix 1, the Risk Allowance (see 8.6 below) includes provisions totalling £3.3m for delays associated with outstanding design work at Financial Close in addition to a £6.7m provision for general programme delay.

To clearly delineate responsibility and therefore risk allocation the Infraco contract and associated schedules, including the SDS Novation Agreement, clearly defines in detail and in a manner agreed by Infraco, SDS and tie/CEC:

- The necessary consents and approvals already obtained at Financial Close
- The remaining consents and approvals and whether the information to obtain such rests with Infraco or SDS
- The expectations with regard to quality of information including compliance with relevant law and regulation
- The programmed dates for delivering information and obtaining the necessary consents and approvals consistent with achieving the overall programme for the project

The role of tie in this complex process is to carefully manage the programme of delivery and take mitigating action as necessary to avoid any cost or programme implications from slippage on individual items. tie also retains responsibility for obtaining specific items including obtaining NR possessions which align with the construction programme agreed with Infraco.

The Risk Allowance does not provide for the cost or programme consequences associated with a wholesale failure of this process – see QRA alignment & Risk Allowance below.

8.5 3rd Party Agreements

There are three groups of residual third party related risks :

- EAL – there is a legal matter to resolve around a future redevelopment of the Airport terminus area. This issue and some contract alignment issues are described in the DLA Report and are not anticipated to create any material risk. .
- NR – a number of mostly programme related risks arising from the NR agreements which are in the normal course of business for doing business with NR. The QRA covers for these in the general delay provision
- Forth Ports - risk that the contribution to extra construction costs of their revised design requirements as capped in their agreement proves to be insufficient to cover the costs. This matter remains under negotiation and the cap should accommodate all reasonable requirements. In the final analysis, resort can be had to imposition of the original design to force an acceptable result however a compromise design is expected to be agreed.

8.6 QRA and Risk Allowance

tie's risk identification and management procedures as detailed in the FBC describe a process whereby risks associated with the project which have not been transferred to the private sector are logged in the project Risk Register. Where possible the cost of these risks is quantified by a QRA in terms of a range of possible outcomes, probability of occurrence and thereby the Risk Allowance which is included in the capital cost estimate for the project.

The project Risk Register also details the "treatment plans" being followed to mitigate individual risks and thereby avoid all or part of the cost allowance.

As the Infraco and Tramco procurements have progressed tie has maintained and reviewed contractual Risk Allocation Matrices, which reflect the risks retained by the public sector arising from the contracts, and has exercised prudence in ensuring the Risk Register, QRA and therefore Risk allowance provide adequately for risks retained for the public sector including the major areas or risk assessed above.

The only material change in the Risk Allocation Matrices between Preferred Bidder stage and the position at Financial Close is in respect of the construction programme costs associated with any delay by SDS in delivery of remaining design submissions into the consents and approvals process beyond Financial Close.

The Project Control Budget at Financial Close totals £508m (Final Business Case £498m) including a risk allowance of £32m (Final Business Case £49m). This change primarily reflects the closure of procurement stage risks on Infraco and Tramco including all the risks associated with achieving price certainty and risk transfer to the private sector as has been effectively achieved in the Infraco contract as summarised above.

The risk allowance of £32m includes the following provisions for residual risks retained by the public sector during the construction phase of Infraco and Tramco.

- £8.8m in respect of specifically identified risks held by and to be managed by tie during the construction phase including adverse ground conditions, unidentified utilities and the interface with non-tram works and post close alignment of the Infraco proposals with the SDS design.
- £2m in respect of the risk that conditions attaching to the VE items taken into the Infraco price may not be removed
- £3.3m in respect of post Financial Close consents and approvals risks which provides for the cost or programme consequences of imperfections which may arise in elements of the consents and approval risk transfer as described above.
- £6.6m to provide for the cost of minor Infraco / Tramco programme slippage of up to 3 months (other than as a result of delays to MUDFA which is provided for elsewhere in the risk allowance).

tie has assessed these amounts as providing adequately for the residual risk retained by the public sector arising from the Infraco and Tramco works and the post Financial Close consents and approvals process. However the Risk Allowance does not provide for the costs of:

- Significant changes in scope from that defined in the Employers Requirements – whether such changes were to emerge from the consents and approvals process or otherwise
- Significant delays to the programme as a result of the consenting or approving authorities failing to adhere to the agreed programme (Infraco/SDS having met their own

obligations) or any other tie/CEC initiated amendment to the construction programme which forms part of the Infraco contract.

All other things being equal any such changes falling into these categories would give rise to an increase in the cost estimate for Phase 1a of the project above of £508m.

8.7 Value Engineering Opportunities

As explained at 10.2 above, the Infraco price is stated after deducting VE opportunities with an aggregate value of £13.8m subject to satisfying certain conditions including the approvability certain items through the consents and approvals proves. A total of £4m have been provided against the possibility that such conditions will not be satisfied.

Value Engineering is a continuing process during construction and tie continue to seek to present value for money opportunities to save on construction and project management costs.

8.8 Alignment of QRA and Risk Allowance to DLA Letter and Risk Matrices

tie has considered the DLA Report and appended risk allocation matrices and considers that the Risk Allowance of £32m contained in the projected Control Budget at Financial Close and associated QRA adequately reflects the risks identified and the change in such risks retained by the public sector since approval of the FBC in December 2007.

The following references are to specific paragraphs/sections in the DLA letter:

5.1 Employers Requirements (ERs) – Alignment issues

There is a well understood and limited level of uncertainty with regard to the alignment of the ERs, the SDS design and the Infraco proposals (on which their price is based). The alignment work described at Section 2.3 above resulted in limited amendment to cost and risk contingencies.

5.2 Project Master Programme

The Project Master Programme which forms part of the Infraco contract is now agreed in all material respects.

The QRA provides an amount of £6.6m (equivalent to 2-3 months complete delay in the programme) for general delay risk which has been assessed by tie management as adequate for the management of the programme but will not provide for any significant stakeholder initiated change beyond the point of Financial Close.

6.4 EAL – Option to shift tramway post 1/1/13

The capital cost of any shift in the Tramway at the airport beyond 1/1/13 would be at the expense of BAA and is not therefore a risk which should be provided for in the Phase 1a budget.

7.1 Consents – Delay on post-close consents

This is the one significant change in the risk profile retained by the public sector since December 2007. The exact nature of tie/CEC's continuing risks have been well rehearsed and are detailed in Appendix 1 as are the mitigating actions and processes tie has in place to manage these risks. A risk assessment in relation to the QRA is provided at section 8.4 above.

The total risk allowance provided in the QRA in respect of continuing Consents and Approvals Risk is £3.3m. This equates to the cost of some 3 months of BBS standing time and is considered adequate by tie management in the context of the number and criticality of consents still to be delivered, the liquidated damages available to BBS from SDS in the event the delay is caused by SDS, the responsibility of BBS to mitigate the costs of any delay and the close management of the process beyond Financial Close by tie.

The risks summarised in the DLA Report are therefore accommodated in the risk and contingency allowance to an acceptable degree.

(9) Update on critical workstreams and readiness for construction

9.1 Design due diligence

The process and procedures laid out in the design management plan and design assurance process formal design reviews have been undertaken every week since September 2007 to inform and finalise the detailed design submissions. These submissions are then consolidated to form the necessary technical and prior approval packages for CEC to discharge their statutory obligations.

In parallel with the process since August 2007, BBS have had access to the detailed design submission across the range of asset for the Edinburgh Tram Network to enable Infraco's design due diligence to be undertaken. Appendix 1 sets out the status of the design process as at Financial close.

9.2 Run-time due diligence

The Infraco contractor has undertaken modelling based on the updated data provided by SDS and CAF to accept the "laws of physics" runtime as part of the finalised Employer's Requirements.

9.3 TTRO / TRO process

The process for gaining the TRO's for the project is documented in the TRO strategy produced in 2007. A major risk in this respect was removed when the Scottish Government amended the TRO Regulations to remove the need for a mandatory hearing for Tram TRO's. CEC can still elect to hold a hearing if they consider the level of objection to any particular TRO merits such action.

Completion of the TRO's is now driven entirely by design and modelling works being undertaken by SDS and JRC and managed closely by tie. The programme identifies the Orders being made in August 2009 which is in line with the overall construction programme.

9.4 MUDFA including interface with INFRACO programme

The Multi Utilities Diversion Framework Agreement [MUDFA] is currently being progressed to Programme Revision 06 as agreed in November 2007.

This programme has been utilised to integrate with the INFRACO programme and is identified as a constraint in a number of construction items. This has been reflected in the INFRACO Construction Programme with the agreement of BBS and other principal stakeholders as part of the sign up to overall construction methodology. Specific elements of diversions have been transferred to INFRACO where it is required by construction sequencing for the final utilities works.

It is expected that, despite detailed subdivision of works to facilitate BT cabling and commissioning, there will remain some overlapping of work sections as INFRACO commences. It is likely to be restricted to section 1C and 1B and can be managed with INFRACO, BT, AMIS and tie.

Overall progress on the utilities works has been good in terms of adherence to budget (with no contingency drawdown to date) and to programme. In addition, the public communications process has worked well although it is fully acknowledged that there is a long way to go.

9.5 Management team and Handover

The Tram Project Team to manage the construction phase of the project has now been designed and is substantially populated. Interim arrangements are in place for all key posts where a permanent appointment is awaited. Handover arrangements and detailed documentation of the final contract terms are underway and key procurement phase staff are contracted to remain until this handover is successfully completed.

The Infraco Director and team have commenced detailed works from February 2008 and are already managing and monitoring the Mobilisation Agreements with BBS and CAF. In addition, 3rd party facilitation arrangements have been commissioned to accelerate the forming of effective working relationships between BBS and tie.

9.6 Safety

Safety management systems are in place. The governance paper at Appendix 3 sets out the overall approach being taken by tie in collaboration with the contractors and stakeholders. Safety management will be under the specific oversight of a tie Board committee chaired by one of the tie non-executive directors who is an experienced industry professional.

9.7 Commercial Management

tie have appointed their post-contract award Commercial Director, who commenced work on 7 January 2008. He is currently progressing the remaining recruitment to ensure a competent, fully populated commercial team is in place to manage the INFRACO contract (including novated contracts for SDS & TRAMCO) immediately on Financial Close. Updated commercial processes and procedures have also been established.

9.8 Insurance

The project insurance arrangements have been in place for some time under the Owner Controlled Insurance Programme (OCIP) implemented with advice and direction from Heath Lambert. The programme has also been subject to evaluation by the Infraco consortium.

9.9 Risk Management

tie's risk identification and management procedures as detailed in the FBC describe a process whereby risks associated with the project which have not been transferred to the private sector are logged in the project Risk Register. Where possible the cost of these risks is quantified by a QRA in terms of a range of possible outcomes, probability of occurrence and thereby the Risk Allowance which is included in the capital cost estimate for the project.

The project Risk Register also details the "treatment plans" being followed to mitigate individual risks and thereby avoid all or part of the cost allowance. There is an agreed risk management procedure currently in operation to manage and treat risks which is owned by tie's risk manager and subject to detailed scrutiny each period with the individual project managers at the period Project Director's Review.

tie and CEC have also agreed an interface to the project where a filter and review is applied to any risks raised by CEC which may be considered relevant as a project risk and requiring a necessary treatment plan.

tie are focused on managing the delivery risks and associated treatment and mitigation plans to avoid or minimise any cost, quality or programme implications.

(10) Specific confirmations

On the basis of the content of this report, the DLA Report and supporting documentation, it is considered that :

- The Infraco Contract Suite is in terms acceptable for commitment ; and in particular
 - The Tramco Novation Agreement is in terms acceptable for commitment
 - The SDS Novation Agreement is in terms acceptable for commitment
- The CEC Financial Guarantee is in terms acceptable for commitment and is aligned in all material respects with the Infraco Contract Suite
- The tie Operating Agreement is in terms acceptable for commitment
- The TEL Operating Agreement is in terms acceptable for commitment

APPENDIX 1

EDINBURGH TRAM PROJECT SDS – DELIVERY AND CONSENT RISK MANAGEMENT

This paper is in draft form as at 12th March 2008 and will be updated for any necessary changes up to Financial Close. This will apply to facts and judgements. The content of this draft is our current best estimate of how the final position will crystallise.

Background

Negotiations have taken place over a lengthy period of time with the objective of defining a process and set of contractual terms which will enable tie and CEC to manage the risks arising from the overlapping design and construction periods. This problem was not anticipated when the SDS contract was concluded in 2005. The recent discussions have taken place under the umbrella of the SDS Novation Agreement, but it is important to distinguish two groups of issues :

Cost certainty : The primary objective of the novation approach was to ensure that design work could commence long before commitment to the construction contract suite generating maximum construction price certainty and transferring design risk to the construction partner.

Outstanding design risk : SDS have resisted accepting liability to BBS for the timeliness of submission and approval of design packages after Financial Close. Their concern is that the risk is different from (and incremental to) the underlying risk arising from the quality of their work. A delay, they argue, could result in hefty exposure because of the linkage to construction programme delay. SDS did not anticipate this risk when committing to their contract - the expectation was that the majority of design scope and certainly all approvals would be complete prior to Financial Close.

The packages which have been delivered to BBS, with the requisite approvals, by Financial Close (“Approved Packages”) are subject to the Novation terms, which inter alia result in BBS accepting the design quality risk, with resort to SDS in the event of failure under the terms of the existing SDS agreement. The exposure to SDS could be potentially onerous, but was accepted when they entered into the existing contract and is not currently contentious.

This means that the primary objective above of cost certainty and risk transfer has been achieved relative to Approved Packages.

The problem relates to design packages which as at Financial Close are either :

- Submitted for Prior / Technical Approval but not yet approved (“Submitted Packages”) ; or
- Work in progress and not yet submitted (“Outstanding Packages”).

The rest of this paper provides an analysis of the residual risk to tie / CEC arising from these two groups of design packages. The paper does not address so-called “tie Consents” – TROs, TTROs and consents relating to statutory authority to implement the scheme - which have been accepted as out with the responsibility of SDS and BBS, except that BBS (and through them SDS) have an agreed contractual responsibility to assist in the process.

Risk overview

The risks which arise from the overlap of design and construction periods are summarised below :

- A. The Submitted packages are not of requisite standard, preventing CEC from providing consent timeously and creating delay to the construction programme.**
- B. The Submitted packages are of requisite standard, but CEC fail to provide consent timeously, creating delay to the construction programme.**

- C. SDS fail to provide the Outstanding packages on a timely basis relative to the agreed programme, preventing CEC from providing consent timeously and creating delay to the construction programme.**
- D. SDS fail to provide the Outstanding packages to the requisite standard, requiring rework and delay, preventing CEC from providing consent timeously and creating delay to the construction programme.**
- E. CEC provide consents and approvals timeously, but SDS then fails to provide IFC (“Issued For Construction”) drawings to BBS timeously creating delay to the construction programme.**
- F. SDS provide the Outstanding packages on time and to the requisite standard, but CEC fail to provide consent timeously, creating delay to the construction programme.**

It is not anticipated that the final Outstanding Packages will be delivered until Autumn 2008. The option of delaying Financial Close to eliminate the risk is therefore unattractive.

SDS has resisted accepting any liability in the event of any of these scenarios. Since the point of investing in a procurement of a design appointment in Autumn 2005 was to secure a completed approvals process with an advanced network design development, there was no allowance for the implications of a coincident design and construction process in the existing SDS agreement. Accordingly, tie / CEC’s leverage over SDS on the issue is limited.

BBS have similarly resisted accepting any liability for the consequences of delay arising from the Submitted or Outstanding packages. Their position was reserved (as was Tramlines’ position) at preferred bidder, pending due diligence on SDS, as they were aware of the issue at the Preferred Bidder stage, but again we have only limited sanction over them.

There has been no sustained attempt by BBS to sidestep the transfer of design quality risk once the Submitted and Outstanding packages are eventually signed over to them with consent. In fact they have now explicitly accepted the design quality risk as part of the Agreement made on Friday 7 March for Contract Price adjustment. Accordingly, the remaining risk is focussed on construction programme delay as a result of late delivery of design and hence IFC drawings impacting construction.

Resolving this issue has been made more difficult because of concern built up over a long period about the quality and timeliness of SDS’s work on the part of tie, CEC and BBS.

There is also a concern that performance against the agreed submission programme could be obfuscated with the intent (or at least result) that design packages fall out with BBS / SDS responsibility because of claimed failure by CEC. This could happen in four ways:

1. Confusion about submission date if a package is returned by CEC for quality improvement
2. Swamping CEC with a high volume of design packages which cannot be processed within the 8-week period
3. BBS and SDS by some means acting in concert to subvert the process
4. Lack of clarity about the quality of submissions

In summary therefore, tie / CEC are exposed to risks relating to timeliness of submission and / or quality. The risk could be heightened by deliberate or inadvertent actions by BBS / SDS. The next section describes the primary means by which these risks can be contained, through an effective management process controlled by tie / CEC.

Development of the design submission and approval management process

Recent process improvements

The process of managing SDS has not been smooth. The performance of SDS has been consistently disappointing on a number of levels and it is fair to say that weaknesses have also existed in execution by tie and CEC.

More recently, building on the existing Tram and Roads Design Working Groups, a number of important initiatives have been implemented to improve all-round performance. These have together improved both the rate of design production and the quality of those designs.

(1) Co-location of staff

The co-location of tie, CEC and SDS staff in Citypoint shortened lines of communication and promoted a healthy working relationship that has led to quicker resolution of issues.

(2) Improved contract management arrangements

tie has increased the number and calibre of resource devoted to managing the design contract, strengthening both its capability to deal with engineering issues and to manage the overall relationship including commercial management and issues resolution.

(3) Focus on resolution of outstanding design issues

By instituting the weekly critical issues meeting with attendance from tie, CEC and SDS aimed at clearing critical issues so that they did not hold up design production, tie brought together the relevant individuals, assigned clear responsibility for securing resolution and monitored progress. In recent weeks that has resolved almost all issues that are holding up SDS design and allowed a number of designs that were almost complete to take the critical final step to full completion and submission for approval.

(4) Closing out third party agreements

Many of the outstanding design issues involved reaching final agreement with third parties. Although steady progress had been made with many third parties a small number of third party negotiations were not moving to a satisfactory conclusion. tie devoted additional resources to closing out these issues and worked closely with CEC and SDS to ensure final agreements were reached.

Documentation of process and execution

The management process is captured in the Design Management Plan (“DMP”) This, along with the review procedure forms Schedule 14 of the Infraco Contract. In recent months, SDS has had much greater clarity over the reasonable expectations of the approvals bodies. All of SDS’s design packages are clearly defined. A programme has been agreed for the submission of each and the quality of information to be provided with the submissions has been defined. In this context, “quality” relates to an objective assessment of the fitness for purpose of the package, not a subjective assessment of the aesthetic character of the content. A well-defined process of informal consultation prior to submission with relevant CEC people is in effective operation. Once submitted, CEC have an agreed period of 8 weeks to deliver Prior and / or Technical Approval as necessary (“consent”) for each package.

Following novation of SDS to Infraco at Financial Close, tie will continue to use the DMP, working with CEC and InfraCo, to manage the design and consent process and maintain the improved performance in design production and approval. The DMP has been updated to incorporate the role of Infraco in managing SDS following novation but the key principles and initiatives remain in place. This process will be applied to complete the consent process for Submitted and Outstanding Packages as defined above.

tie is holding daily meetings with SDS and CEC to maintain the focus on delivery of individual Outstanding Packages and identify any problems early enough for them to be resolved with minimum impact on the programme. This will continue (also involving InfraCo) once the contract has been awarded.

CEC’s involvement in the daily meeting ensures that there is timely and effective feedback from the approval body of progress with Submitted Packages. It also allows CEC to raise any issues that need to be resolved before a submission can be made.

Whilst some of the Outstanding Packages lie on the critical path for construction, many do not. This means that there is still some flexibility in the agreed approvals programme. Management of that flexibility lies with tie and CEC and BBS/SDS can only take advantage of the flexibility with tie’s consent.

There will be some changes to the design that SDS submits/has already submitted. Mainly these are necessary refinement of the detail of items where the detailed design will be completed by BBS and these have been allowed for within the programme. Where BBS is proposing an alternative design to that already submitted by SDS, BBS will be responsible for securing approval of that alternative design. In these cases BBS will draw on the experience of SDS to manage that consultation and approval programme.

Contractual underpinning

The contractual terms which capture these arrangements reflect:

- The contractual responsibility for managing SDS design and development work supporting Submitted and Outstanding Packages sits with BBS;
- BBS are contractually obliged to follow the regime under the Review Process and Design Management Plan, as are SDS;
- SDS agree to liquidated damages to be applied by Infracore regarding late or deficient submissions to CEC;
- Contractual clarity as to primary responsibility for categories of Consents
- Excusable delay in failure to obtain CEC Consent entails evidence of full compliance by SDS/BBS with agreed regime: timing, sequence, quality, notification;
- The absolute nature of SDS contractual responsibility to obtain all Consents has been adjusted to reduce tension surrounding interface with CEC;
- The risk of prolongation cost as a result of SDS failings in terms of causing delay (through not obtaining Consent) is to be taken by tie.
- the risk to programme (and generally) of SDS consented design containing a quality deficiency is ultimately taken by SDS and, in the first instance, by BBS. BBS have now explicitly accepted this as part of the Contract Price. tie will hold a collateral warranty from SDS.

Finally and critically, the overall programme for consents is not only embedded in the SDS Novation agreement to which SDS and BBS are parties, but the programme has been interfaced in detail with the construction programme.

In summary, there is confidence among the tie and CEC managers involved that the management process can be executed rigorously after Financial Close.

Focussed risk analysis

In addition to executing effective management control across all design packages, it is useful to identify those packages which carry the greatest risk. This facilitates prioritisation and mitigation action and also creates a clearer view of the residual risk arising from the overlapping design consent and construction programmes.

On 15th February 2008, CEC and tie jointly reviewed the status and risk profile of every Submitted and Outstanding Package relating to Phase 1a, allowing for anticipated progress to Financial Close. The review will be updated through the period to Financial Close, allowing a fresh assessment of risk at both point of Notification of Award and at Financial Close.

The best estimate of progress by mid-April will be that 10 Prior Approvals and 7 Technical approvals will have been achieved, making a total of 17 Approved Packages.

The review of the Submitted and Outstanding Packages assessed for each design package seeking Prior and / or Technical Approval :

1. The risk arising from the criticality of the package relative to the construction programme ; and
2. The risk arising from the quality and complexity of the package, which could affect timely consent

A graduated risk measurement was applied to each package for each of the two risk criteria : those packages which were required for the earliest stages of the construction programme having a higher risk rating than those required for later stages ; and more complex or sensitive packages or those with known quality issues were given a higher risk rating than those of a simpler character. The two risk ratings were multiplied together to give a risk rating tabulation across the whole population of Submitted and Outstanding Packages. The tabulation was then stratified into Critical, High, Medium and Low categories based on the risk ratings.

The people who contributed to this process and who have confirmed they are comfortable that the results are properly presented were Susan Clark (tie Programme Director), Andy Conway (CEC Tram Coordinator), Damian Sharp (tie Design Project Manager i/c of the SDS design and approval process), Tom Hickman (tie Programme Manager) and Mark Hamill (tie Risk Manager).

81 individual packages were reviewed, of which 75 were assessed as medium or low risk. The remaining 6 packages in each category were :

<u>Submitted Packages</u>	<u>Critical</u>	<u>High</u>
Prior Approval	0	1
Technical Approval	0	2
<u>Outstanding Packages</u>	<u>Critical</u>	<u>High</u>
Prior Approval	0	1
Technical Approval	1	1

Appendix 1 lists these Critical and High risk packages with a brief summary of their risk profile and the mitigating factors which can be deployed to manage the risk

A report is available which provides a detailed breakdown of the entire population of 81 packages.

For each package, the issue is well understood and mitigation plans have been identified to ensure that the risk is being managed on an ongoing basis. Appendix 1 contains full details of these.

In overall terms, the limited number of Critical / High risk packages is no surprise given the short anticipated time to finalise the consent process relative to the overall construction programme and the extent of work done to date to meet the needs of the approval authority.

Third party approval risk

In addition to approvals by CEC a number of the Submitted and Outstanding Packages also require approval by third parties. The most frequent and significant third party approval body is Network Rail. There has been substantial informal consultation with Network Rail throughout the development of the design and Network Rail has expressed satisfaction with many of the designs in principle. Network Rail has agreed to review Submitted Packages for technical approval in parallel with the CEC consideration of those packages. This means that Network Rail will be in a position to confirm approval very soon after CEC approval is granted. This is a significant concession by Network Rail and reflects their confidence in the design following the consultation to date.

The other significant third party in this context is BAA. Within the EAL Licence, Schedule 3 allows EAL to review tram works data – primarily design & construction related method statements. There is a 30 day review period, and EAL could object to this data, but only on the basis of adverse impact on airport operations or safety. There is also a DRP set out in the licence if an agreed position on design change (both acting reasonably) cannot be resolved.

We are taking EAL through the design and the MUDFA works in a scheduled process of meetings (held 4 weekly, but also in the case of MUDFA, more regularly), there is nothing to suggest that the risk of designs not being accepted is low.

Forth Ports is another player, but the agreement scheduled to be signed with them, and the generally constructive working relationship on these issues, creates a good level of comfort.

No serious issues are anticipated with the other third parties, with whom the approval process is fairly commonplace. Overall, it is considered that the third party arrangements create no material risk to the construction programme.

Higher-level mitigations

In addition to the mitigation arising from control of the well-defined management and approval process and the limited number of Critical / High risk locations, there are a number of higher-level mitigations which are relevant to the overall evaluation.

SDS Liability

In relation to the Submitted and Approved Packages, one contractual feature of importance in assessing the overall risk is the reward / penalty mechanisms to be applied to keep the design process on track after Financial Close. These mechanisms relate to what can reasonably be defined as SDS's performance. SDS will however accept no liability arising from CEC delay (risks B and F above). The effect of these arrangements has been incorporated into the assessment of risk contingency described below.

A general legal protection exists whereby SDS is exposed to claims from BBS following novation for "culpable failure" which could supersede the cap.

Funding support

Any uncapped exposure will carry no financial protection to tie / CEC. However, should this result in increased project cost, assuming legitimately incurred, the terms of the grant funding from Transport Scotland mean that the cost will be substantially covered by grant, to the extent that there remains headroom beneath the aggregate funding of £545m. It must be borne in mind that this factor cushions risk to tie / CEC but not to the project as a whole.

Existing risk contingency

The project cost contains risk contingency amounting to £3.3m linked to the consent risks described in this paper.

Conclusion

The overlap of continuing design and approval processes with the construction programme has created a risk. Experience in the early years of managing the design and approval process was not happy, but recent initiatives have successfully developed a well-defined and effective management process, led and directed by tie / CEC. This management process will continue following Financial Close with minimum risk of interference.

A thorough risk-focussed review of the consents has been performed by competent people from tie and CEC. This has concluded that the residual risk is contained in a small number of design packages. These have been the subject of prioritisation to mitigate their risk profile.

The combination of controlling the management process and focus on the key elements of the residual risk, constitute an effective risk mitigation framework. There are other higher-level mitigations which provide further help, notably the funding arrangements and the existence of a risk contingency in the project budget.

It is the view of the tie and CEC project team that these factors can be relied upon to manage the exposure successfully.

Prior & Technical Approvals

APPENDIX 1

Critical Risks >21	Description	Risk	Issue	Mitigations
Technical Outstanding	A8 underpass	25	Underpass – sewer conflict	Technical solution now agreed and requires sewer to be diverted
High Risks 11 - 20		Risk	Issue	Mitigations
Technical Outstanding	Roseburn St Viaduct	20	VE solution changes design	Feasibility study complete – awaiting approval from NR. Options reviewed by CEC structures 10/3/8 and all options acceptable
Technical Submitted	Building Regulations approval	15	At 4 locations full planning approval is required	SDS to submit drawings for planning approval
Technical Outstanding	Depot earthworks	15	Requirement for earthworks to be approved separately	SDS to split batch into “for excavation” and “embankments”. CEC are considering need to prior approval for these slope as they are natural slopes. If prior approval is not required this will be removed as a risk
Prior Outstanding	Accommodation works – Murrayfield Murrayfield stadium retaining wall Roseburn St Bridge Murrayfield turnstiles	15	VE solution changes design	Feasibility study ongoing and due and we await final approval from NR
Prior Outstanding	Tram Stop Haymarket Haymarket Viaduct Substation Haymarket Relocation of war Memorial Line of route	15	Road Safety audit thrown up issues requiring rework	The issues are understood and rework is ongoing to allow resubmission.

Paper to : tie Board, Tram Project Board, TEL Board, CEC
 Subject : Project Governance after Financial Close
 Date : UPDATED 7th April 2008

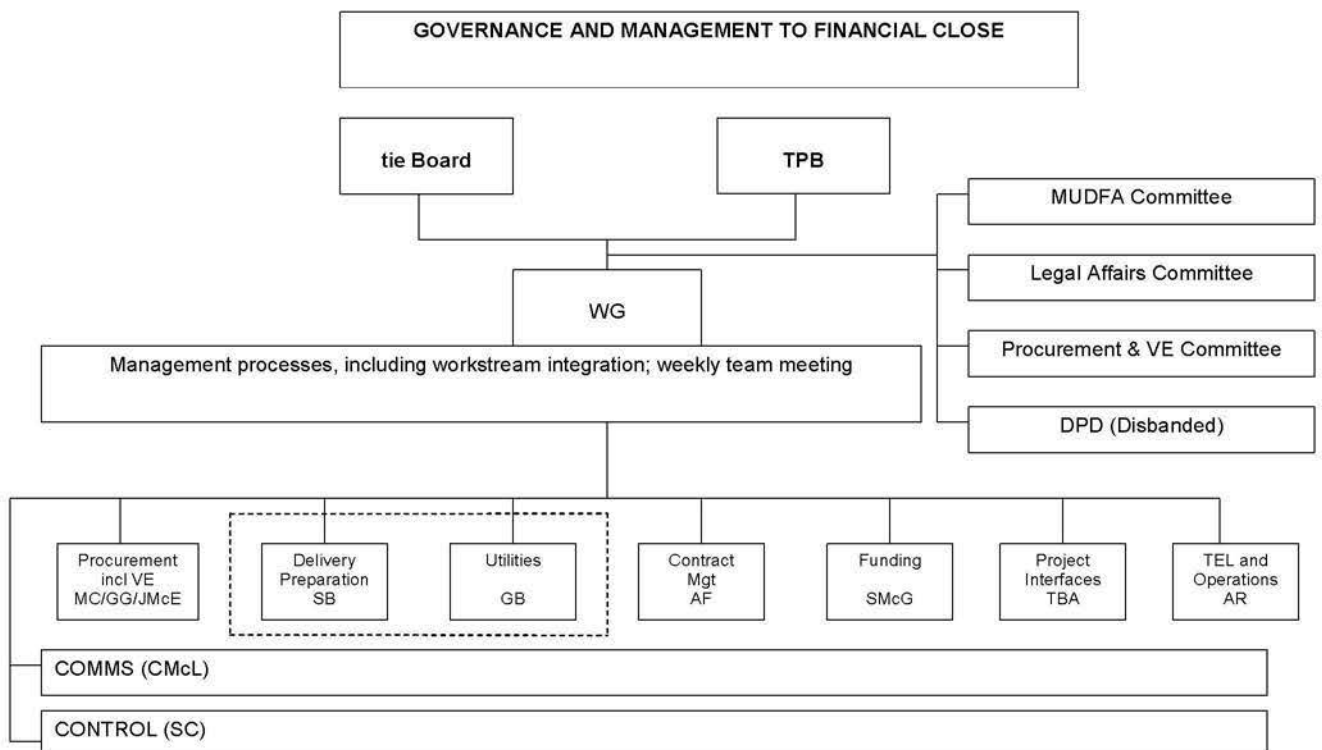
THIS PAPER SUMMARISES THE PROPOSED GOVERNANCE AND MANAGEMENT MODEL AS IT STANDS AT 7th APRIL 2008. THE AREAS WHICH HAVE NOW BEEN UPDATED INCLUDE FINALISATION OF OPERATING AGREEMENTS AND THE DELEGATED AUTHORITY WHICH FLOWS FROM THOSE AGREEMENTS. THIS PAPER IS THE FINAL FORM SUPPORTING FINANCIAL CLOSE

**Edinburgh’s integrated transport system
 Project governance for the construction period**

(1) Governance and management model in period to financial close

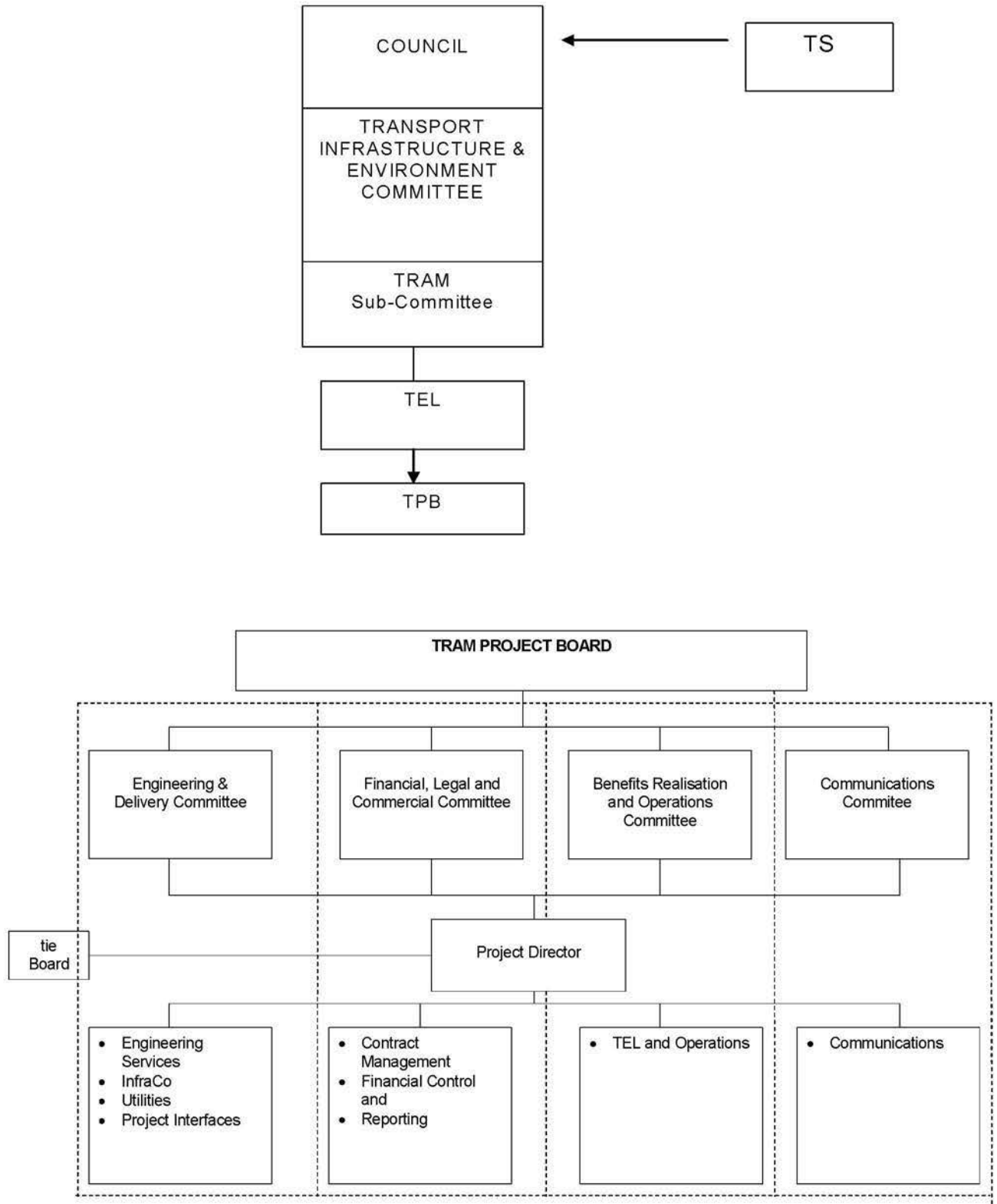
The recipients of this paper approved a governance and project management model for the period to Financial Close prior to the Council’s meeting on 25 October 2007. The purpose of this paper is to present the proposed model for the period from Financial Close to operational commencement, planned for Q2 2011. The proposed model is very similar to the outline presented in October but this paper is drafted to be independent of previous submissions.

The current model is set out in the following diagram, including the project workstream structure under the TPD.



(2) Governance and management model in construction period

The diagram below sets out the proposed governance model for the construction period .



The roles & responsibilities of the entities within the new governance and management model are summarised below.

Transport Scotland (TS)

TS exercise their oversight of the project through 4-weekly reporting in prescribed format and a 4-weekly meeting with the City of Edinburgh Council (CEC).

The principal contractual relationship between TS and CEC is the Grant Award Letter which sets out the terms on which TS will provide the balance of the £500m grant. This contains detailed reporting and certification requirements appropriate to the conduct and scale of the project..

CEC

CEC have established a "Tram sub-Committee" of the existing Transport, Infrastructure and Environment Committee. The sub-Committee is chaired by the Executive Member for Transport with a 6-8 weekly meeting cycle. The purpose of the sub-Committee is to review and oversee decisions with respect to the project. This will include addressing matters directly affecting the Council and providing assurance that matters which cross Council departmental boundaries are managed cohesively (for example, responsibilities for roads & traffic management and budgets).

CEC have prepared Operating Agreements between the Council and respectively tie Limited and Transport Edinburgh Limited (TEL) to codify the arrangements between the entities and the responsibilities of the two subsidiaries. The signing of the Operating Agreements creates the authority for tie and TEL to execute their responsibilities.

The Council Report approved on 20 December 2007 indicated that some issues will require to be referred to Council including the approval of the annual business plans for tie and TEL respectively and significant changes to Council obligations including material changes to scope and cost within the Tram Project, will also be reserved to Council. Full Council will also require to ratify settlement of any claims greater than £500k or £1million in a 12 month period. The precise definition of the delegated interface between the full Council and its committees is a matter for the Council.

The Operating Agreements also specify certain matters which require the approval of a Council Monitoring Officer. The Monitoring Officer will be the same individual with respect to both tie and TEL and will also be a member of the TPB, in order to ensure that the governance structure is clear and singular.

TEL

The TEL Board is focussed on its overall responsibility to deliver an integrated tram and bus network for Edinburgh, on behalf of CEC. The Board is responsible for compliance with its Operating Agreement and it will also address any matters outwith the direct arena of Integrated Bus and Tram systems and any statutory TEL considerations.

The TEL Board comprises an independent non-executive Chairman, independent non-executive directors, Elected Members and Executive management. There is appropriate common membership across the TEL, tie and LB Boards to ensure consistency of approach.

The following matters will be a matter for the TEL Board to determine :

All matters affecting the programme, cost and scope of the Project except the following which are matters reserved to the Council:

- (A) (i) any actual or reasonably expected delay to the Project programme of greater than 3 months; or (ii) any increased cost of over £10m; relative respectively to the programme leading to commencement of revenue service by 31 July 2011 and capital cost of £508m (Phase 1Aa) or £87m (Phase 1Bb) as set out in the Final Business Case or as subsequently approved by the Council prior to commitment by tie to the Infraco Contract ; or (iii) notwithstanding the terms of (i) and (ii) above, any projected or actual overspend of the available funding budget (being £545 million) at any time (whether on an annual or overall basis); or (iv) any substantial change to the design, scope or service pattern set out in the Final Business Case; and
- (B) the settlement of any single claim in excess of £500,000, or series of claims in any 12 month period which would exceed in aggregate £1,000,000;

TEL may delegate responsibility for all matters other than those specified at A and B above to the TPB and the TPB may in turn delegate responsibility for all other matters to tie, but only to the extent that such delegation is already within the remit of tie in the context of the tie Operating Agreement. TEL agrees that it shall retain ultimate responsibility for all matters it so delegates.

The Council's majority shareholding in Lothian Buses (LB) will be transferred to TEL and parallel changes to the composition of the Lothian Buses Board will be effected in due course.

Tram Project Board (TPB) and its sub-Committees

The TPB maintains its role as the pivotal oversight body in the governance structure. The TPB is established as a formal sub-Committee of the TEL Board with full delegated authority to execute the project in line with the proposed remit set out in Appendix 1. In summary, the TPB has full delegated authority to take the actions needed to deliver the project to the agreed standards of cost, programme and quality within the authority delegated to the TEL Board.

The suggested membership of the TPB is 7 people (Office of Government Commerce constituency definitions "highlighted"):

- Chair (David Mackay)
- Senior CEC Representatives - "Senior User Representatives" (Donald McGougan and Andrew Holmes)
- TEL CEO and Project "Senior Responsible Owner" (Neil Renilson)
- "Senior Supplier" representatives (tie Executive Chairman and TEL Operations Director) (Willie Gallagher and Bill Campbell)
- Executive Member for Transport (Phil Wheeler)

The Chair will continue to be the TEL Non-executive Chairman, rather than the Project SRO. Other parties, principally senior project management and advisers, will be called to attend as required, though it is anticipated that a common group of senior project directors will attend

The remit and delegated authority given by TEL to the TPB, and by the TPB to the SRO and Tram Project Director (TPD) are set out in Appendix 1. The TPD will formalise delegated authority downwards to senior members of the delivery team.

tie Limited

tie's role is to deliver the tram network fit for operational purpose, on time and budget. For the foreseeable future, tie will have only one major project, the tram. It will maintain roles with certain smaller projects and will require to comply with normal statutory responsibilities as a limited company, including formal compliance with its Operating Agreement.

The tie Board presently comprises a group of independent non-executive directors and Elected Members under the Executive Chairman. The Elected Members will be the same on each of the TEL and tie Boards to ensure consistency of view across delivery of the system and operations. The independent non-executive members will also provide experienced participation in the TPB's sub-committee deliberations, as explained below.

In overall terms, the composition of the tie Board will be maintained in its present form. The Board will maintain its Audit and Remuneration committees, membership of which are restricted to the NXDs. In addition, a new tie Board sub-Committee will be established to address Health & Safety, chaired by an experienced NXD.

In its role on the tram project, tie provides services to the TPB. The tie Operating Agreement provides tie with the legal authority to enter into all competent contracts to deliver the tram system. The tie Board will delegate authority to its Executive Chairman to execute its contractual responsibilities for the tram project. The Tram Project Director (a tie employee) is given delegated authority by the tie Executive Chairman to manage and deliver the project. The authority given to the TPD in his role as a tie employee is synchronised with the authority delegated to him by the TPB. This ensures that the TPD leads the project delivery under delegated authority from his employer (tie) and from the project client (TEL through the TPB) which is consistently defined.

Further changes to the composition of the TEL, tie and LB Boards will be effected as is deemed necessary over the period ahead. In particular, in the event that tie assumes responsibility for additional major projects in the future, the Board composition may need to be addressed. All such changes will require the formal approval of the Council.

In summary, the roles of the parties are :

CEC

- To be responsible for the creation of a financially viable integrated bus and tram system in line with the approved Business Case ;
- Compliance with the terms of the Grant Award Letter

TEL

- Under authority delegated by its parent CEC, to prepare for the operation of the integrated tram and bus network, including oversight of the delivery of the tram infrastructure executed through its sub-Committee, the TPB ;
- Compliance with the CEC / TEL Operating Agreement ;
- Statutory responsibilities including Board membership, statutory reporting, maintenance of books of account and statutory records ;
- Matters relating to TEL employees including Health & Safety

TPB

- Prepare for the operation of the integrated tram and bus network, including oversight of the delivery of the tram infrastructure, conducted directly or through scrutiny by sub-committees of the TPB of specific activities within the project

tie

- Management of the delivery of the tram infrastructure including management of the contracts written with third parties to achieve delivery of the tram network fit for operational purpose, on time and budget
- Compliance with the CEC / tie Operating Agreement ;
- Statutory responsibilities including Board membership, statutory reporting, maintenance of books of account and statutory records ;
- Matters relating to tie employees including Health & Safety

TS

- To provide grant funding in line with the terms of the Grant Award Letter

(3) Practical operation of the governance model

It is recognised that there is inevitable duplication between the scrutiny by the tie Board of its Executive activities and the oversight role performed by TEL and the TPB. However, this situation is normal, if tie's role of providing a service to its client, in this case TEL, is borne in mind.

It is suggested that the tie and TEL Boards will meet every second period on a period-about basis. The frequency of TEL Board meetings is expected to increase as operational commencement approaches. The TPB and its sub-committees will operate on a 4-weekly cycle, linked to the 4-weekly report to TS. The means by which the Project Director arranges day to day management of the project is not reflected in this paper but will also follow the 4-weekly cycle and will respond to the reporting requirements of the tie and TEL Boards.

The outstanding matters required to finalise the calendar following Financial Close are :

- Dates for proposed CEC Tram sub-committee meeting
- Dates for 4-weekly TS / CEC meetings

The current TPB sub-Committee structure will be dissolved and the new sub-Committee structure will comprise :

Engineering & Delivery Committee (E&D)

- Delivery under contracts - Infracore, Tramco, Utilities / MUDFA, design,
- Health & Safety, Quality & Environment
- Improvement initiatives – VE, Innovation, ICT
- Project interfaces & approvals – Land & Property, Traffic, third parties

Financial, Commercial & Legal Committee (FCL)

- Financial management – reporting, control, audit, risk management, insurance
- Contract management – reporting, compliance, interface with delivery, claims & variations

Benefits Realisation & Operations Committee (BRO)

- Operational & integration planning
- O&M contract planning
- Transdev
- Marketing

Communications Committee

- Comms management – utilities / MUDFA, Construction, Media, stakeholders

It is anticipated that the BRO and Communications committees will not meet for the early period of construction in the absence of any material issues arising which require separate scrutiny. The TPB will deal directly with any relevant matters under these headings for the foreseeable future.

In order to create close cohesiveness between the TPB / sub-Committee governance model and the project management structure, the sub-Committees will be directly interfaced with the Project workstreams and the individual directors responsible. Appendix 2 sets out the interfaces which effectively constitute the remits for these committees.

To further reinforce cohesion, the tie Executive Chairman will Chair each of the sub-Committees. The attendance of senior project and client officers, and the clear responsibilities allocated to individual Project Directors, will ensure that appropriate independence and challenge is achieved. As currently, the sub-Committees will have clear remits and will focus on detailed interrogation of key issues, leading to recommendations to the TPB which retains decision-making authority over all key areas.

(4) Health & Safety

A detailed analysis of the means by which H&S responsibilities are discharged is set out in Appendix 2. In summary, H&S is clearly of paramount importance both currently and in the construction phase of the Project. CDM 2007 will be a key focus and will be given appropriate prioritisation by all parties at all levels. The application of legal H&S responsibilities in the context of the governance and management of a large, complex project requires very careful analysis.

The detailed definition, allocation and communication of responsibilities will be executed as part of the readiness process in advance of construction commencement.

(5) Approvals requested from recipients of this document – tie Board, TPB, TEL Board and CEC in appropriate sessions

The following approvals have been completed :

1. Approval of the proposed governance model for the period from financial close to operational commencement.
2. Approval of the tie and TEL Operating Agreements and all related delegated authorities
3. Confirmation of the proposed members and participants in the governance bodies
4. Confirmation of the proposed meeting cycle
5. Approval of the proposed H&S regime.

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Appendix 1 - Tram Project Board ("TPB") Remit

TPB has delegated responsibility for the delivery of an integrated Edinburgh Tram and Bus Network on behalf of TEL and CEC, in particular :

1. To oversee the execution of all matters relevant to the delivery of an integrated Edinburgh Tram and Bus Network, with the following delegations :
 - a. Changes above the following thresholds
 - i. Delays to key milestones of > 1 month
 - ii. Increases in capital cost of > £1m
 - iii. Adversely affects annual operational surplus by >£100k
 - iv. is (or is likely to) materially affect economic viability, measured by BCR impact of > 0.1
 - b. Changes to project design which significantly and adversely affect prospective service quality, physical presentation or have material impact on other aspects of activity in the city
 - c. Delegate authority for execution of changes to TEL CEO (the Project SRO) with a cumulative impact as follows:
 - i. Delays to key milestones of up to 1 month
 - ii. Increases in capital cost of up to £1m
 - iii. Adversely affects annual operational surplus by <£100k pa
 - iv. is (or is likely to) materially affect economic viability, measured by BCR impact of <0.1

[Note: these are cumulative impacts since the last position approved by the TPB.]

The TEL CEO will delegate similar authority to the Tram Project Director.

These levels of authority apply to all matters affecting the programme, cost and scope of the Project except the following which are matters reserved to the Council:

- (A) (i) any actual or reasonably expected delay to the Project programme of greater than 3 months; or (ii) any increased cost of over £10m; relative respectively to the programme leading to commencement of revenue service by 31 July 2011 and capital cost of £508m (Phase 1Aa) or £87m (Phase 1Bb) as set out in the Final Business Case or as subsequently approved by the Council prior to commitment by tie to the Infraco contract ; or (iii) notwithstanding the terms of (i) and (ii) above, any projected or actual overspend of the available funding budget (being £545 million) at any time (whether on an annual or overall basis); or (iv) any substantial change to the design, scope or service pattern set out in the Final Business Case; and
- (B) the settlement of any single claim in excess of £500,000, or series of claims in any 12 month period which would exceed in aggregate £1,000,000;

All matters which fall to the determination of the TPB will be reported to the TEL Board on a comprehensive and timely basis.

Matters which do not fall within the TPB and TEL Board's delegated authority levels described above will require determination by the Tram Sub-Committee of the Council.

2. To appoint the Senior Responsible Owner (SRO) and Tram Project Director (TPD) for the project and to receive reports from the SRO and TPD on project progress
3. To receive reports from sub-committees established to oversee specific areas, as approved by the TPB

4. To ensure project workstreams are executed according to robust programmes under the leadership of Project Director.
5. To approve the submission of funding requests and to recommend approval of funding terms to the TEL Board. TPB will also confirm to CEC compliance with all relevant aspects of the grant award letter.
6. To ensure proper reporting through the TPB Chairman to the TEL Board and to CEC (as appropriate) of decisions made.

Appendix 2

Interface between new governance bodies and project management structure in the construction period – people identified are included for discussion only at this stage

TPB Governance body	Chair	Management responsibility	Director
Engineering & Delivery Committee	Gallagher	Engineering & Delivery - Infracore Tramco Utilities / MUDFA Engineering design Health & Safety planning & management	Bell
		Improvement - VE Quality & Environment ICT Innovation	McEwan
		Project Interfaces & Approvals - Land & Property Traffic management / regulatory Other CEC, third party	Sim
Financial, Commercial & Legal Committee	Gallagher	Financial management - Financial reporting Financial control, internal audit Risk management Insurance	McGarrity/ Thorne
		Contract management - Contractual reporting & compliance Claims & Variations management	Fitchie
Benefits Realisation & Operations Committee	Gallagher	Operational Planning - Integration & service planning O & M planning Transdev Commissioning Marketing	Richards
Communications Committee	Gallagher	Communications management - Utilities / MUDFA Construction Media Stakeholder	McLauchlan

Appendix 3

Health & Safety background and proposed operational structure

General

H&S obligations are well-understood and entrenched in the project governance and management structure. The increased level of physical activity which may give rise to H&S risks once construction commences reinforces the need to ensure H&S responsibilities are clear and that the highest standards of H&S management are applied. These considerations must be addressed on a daily basis in all actions and at all levels by parties involved in Project.

In overall terms, the key H&S considerations for CEC, TEL, the TPB and tie are:

- the health & safety of their people - the corporate H&S Management Systems address this responsibility
- ensuring that CEC, TEL, the TPB and tie deliver against clearly stated H&S responsibilities in the framework of the project including working alongside third party H&S management systems
- monitoring and reporting regularly that these responsibilities are being properly discharged
- ensuring that all persons employed by CEC, TEL and tie are competent
- ensuring that contracts entered into address H&S issues adequately
- ensuring that H&S ramifications are considered when key investments and business decisions are made

These H&S considerations apply currently, throughout the period to Financial Close and throughout the period of construction and into operation of the tram system. The H&S responsibilities are currently defined clearly to meet the demands of the current project activity including the utility works now underway. These responsibilities will require to be revised to integrate with the revised governance structure described in this paper and to enable effective management of the full-scale construction activity which will follow Financial close. The narrative below provides a description of the responsibilities of the bodies involved in the project and has been drafted with the full involvement of DLA. A precise and legally supported H&S regime will be put forward for approval and then implemented in advance of financial close.

Relationship of revised governance model to H&S responsibilities

The TPB creates an "inclusive" decision making process which is important for the effective operation of the project. The TPB will be a formal sub-Committee of the TEL Board so that members of the TEL Board on the sub-Committee retain the formal responsibility for decisions taken at the TPB, with all other parties to TPB deliberations being participants or observers only. The TPB itself is not a shelter from health and safety liabilities or a clearing house for liabilities. Legally CEC, TEL and tie cannot delegate H&S responsibility to the TPB in the governance structure and thereby declare that they have discharged their health and safety liabilities and have no further duty regarding input into or consideration of health and safety issues.

The ultimate responsibilities for the TPB decisions flow up to the TEL Board and CEC, subject to the intended election under the Construction Design and Management Regulations 2007 ("CDM 2007") of tie as "Client" under those regulations. A Procurator Fiscal may consider that all parties (CEC, TEL and tie), together constitute the entity for the discharge of H&S obligations. As a result H&S implications must be considered by all these parties when making significant decisions affecting design and implementation through the construction phase of the Project. The HSC guidance *Director's Responsibilities for Health & Safety* must be followed by CEC, TEL, the TPB and tie. Appropriate leadership should be demonstrated in this area by the boards and senior management.

Where changes are submitted for TPB approval, or are requested by the TPB, tie/TEL/CEC (and the appointed CDM 2007 parties) will be legally responsible for identifying and managing any impact that these changes will have on safety. The TPB will be responsible for ensuring that they understand and have responsibility for any decisions made in this respect. It is intended that tie will be mainly responsible for implementing the decisions made throughout the construction period.

It is considered that TEL/CEC would remain the "client" in terms" of CDM 2007 as the TPB is not a separate legal entity although it will make decisions on behalf of TEL/CEC. tie is responsible as the elected second client under CDM 2007 and the client/employer (for general health & safety regulations) for the overall project safety management for the development and implementation of the Project. Such an election is, however, not a full delegation of all rights and responsibilities. tie and the TPB must ensure that its activities or its stakeholders or advisors do not undertake actions that encroach upon the role of the designer under CDM 2007, because this would mean that they would require to demonstrate competency in this role and fulfil added responsibilities.

The revised project governance structure described in this paper will distance Transport Scotland from the H&S responsibilities as their responsibilities are related to those of the principal funder of the project, in the absence of any material involvement in design or construction matters.

Health & Safety, Quality & Environment will form an element of one of the new TPB governance sub-Committees. H&S matters within tie will be the responsibility of the Engineering and Delivery Director. In addition to the E&D Director's leadership on this issue, a senior NXD will be the nominated chair of the H&SQE sub-committee of the tie Board to add a further H&S check in the operation of tie and the TPB.

A regular safety report is produced and presented to the tie Board and to the TPB each month. The TPB will ensure that safety is a core agenda item for each meeting and will ensure that the safety report tabled at each meeting is actioned where appropriate. Copies of these reports, or summary documents as appropriate, will be disseminated to TEL and CEC. This will ensure that H&S issues are considered at senior level on a regular and disciplined basis.

Legal backdrop

There may be occasions where a decision which is made by the TPB under its delegated authority from TEL is driven by one of the stakeholder directors to the exclusion of the other members of the board. In the event of an incident, this may result in the contractual relationships or duties between the stakeholders being considered. Notwithstanding that financial indemnities could be put in place to cover losses suffered, if a particular party declares that it will be held accountable for a decision impacting safety, it is important to highlight that it is not possible to ensure that fines imposed as a result of prosecution can be the subject of an enforceable indemnity. It is not possible to contract out of criminal liability nor is it possible to insure against a fine. Although it may be competent to include a clause in a contract, it is possible that such a clause would be construed by the courts as unenforceable and contrary to public policy. In this context, the representative of each stakeholder would need to look to their employer, with regard to personal accountability.

The creation of appropriate safety responsibility structures, safety management systems and culture will form a key defence to any prosecution assuming all procedures have been followed. Clearly there could also be a number of other parties involved in a safety incident, for example contractors, sub-contractors, agency staff, designers, CDM-Coordination and third parties.

The Corporate Manslaughter and Corporate Homicide Act 2007 came into force on 6 April 2008. Corporate homicide will be committed where a death is caused by an unlawful or grossly negligent act of the senior management of an organisation. The management and organisation of activities by senior management must constitute a "substantial element" of the breach, in other words, partial delegation of the duty will not prevent liability attaching to senior management. Breach is punishable by a fine. Although directors do not face personal liability under the Act, the offence will make directors more vulnerable to disciplinary action and further crystallise their accountability for health and safety compliance to their stakeholders. It remains possible for directors and senior management to face personal liability if there is sufficient evidence to bring a prosecution under the existing common law or under the Health & Safety at Work etc Act 1974.

REPORT BY TIE LIMITED ON INFRACO CONTRACT SUITE AND COUNCIL GUARANTEE

SECTION TO BE UPDATED FOR FINAL AMENDMENTS

Content of this section

- Process of drafting, negotiation, review and quality control
- General description of scope, parties and contract structure
- Overview of Infraco contract terms
- SDS Novation Agreement and design delivery and approval process
- Confirmation of BBS acceptance of modelling
- Employer's Requirements and Infraco & Tramco Proposals
- Advance purchase materials
- Infraco payment mechanism
- Infraco performance security arrangements
- Overview of Tramco contract terms
- Tramco payment mechanism
- Tramco performance security arrangements
- Council financial guarantee

Process of drafting, negotiation, review and quality control

The structure, membership and competence of the tie / TEL commercial and technical negotiating team have been assessed by tie and have remained largely consistent since the bid evaluation process commenced. Council officers have operated in an integrated manner with the main negotiating team, which has also had extensive support from our external legal advisors (in DLA Piper's case from late September 2007 onwards, following instruction to disengage from the process in May 2007), Transdev and other advisors. DLAP's engagement on the development of the Tramco Contracts has been more limited following tie's in house legal team taking over this part of the procurement from May 2007 onwards.

Appropriate quality control procedures have been applied to finalisation of the Infraco contract suite. In a number of critical areas, senior tie and TEL people have performed a review of terms independent of the main negotiating team, the important elements of which are set out in this report. The TPB, TEL and tie Boards have been regularly kept abreast of progress in all important areas and have confirmed or redirected effort as appropriate. Communications on these key matters with senior Council officers has been conducted both through the TPB and its sub-committees and also through frequent informal contact. Finally, the OGC Gateway 3 Review Team examined key areas of the contract suite before approval in advance of the October 2007 Council meeting.

In broad terms, the principal pillars of the ETN contract suite in terms of scope and risk transfer have not changed materially since the approval of the Final Business Case in October 2007. It is felt that the process of negotiation and quality control has operated effectively to ensure the final contract terms are robust and that where risk allocation has altered this has been adequately reflected in suitable commercial compromises.

This report is not a substitute for reading the Contract itself. It summarises those provisions in which CEC has expressed particular interest. It should be understood that the ETN Contract Suite has undergone a lengthy and difficult negotiation and close out phase.

General description of scope, parties and contract structure

The Infraco contract suite comprises the following principal contracts :

- Infraco system design, construction and maintenance contract between tie and BBS;
- Employer's Requirements and Infraco Proposals;
- Tramco vehicle supply and maintenance contracts between tie and CAF;
- Tramco Novation Agreement establishing Infraco – Tramco arrangements;
- SDS Novation Agreement establishing Infraco – SDS Provider arrangements;
- Security documentation; and
- Ancillary agreements and Collateral Warranties

Overview of Infraco contract terms

The Infraco Works are to be carried out pursuant to an Infraco Contract between tie Ltd and Bilfinger Berger (UK) Limited and Siemens plc. Bilfinger Berger (UK) Limited and Siemens plc have formed an unincorporated consortium to carry out the Infraco Works and are together called the 'Infraco', each company separately being an Infraco Member. Bilfinger Berger (UK) Limited and Siemens plc have joint and several liability for the performance and discharge of all obligations under the Infraco Contract and the three novated agreements that will be housed within it.

Authority to Transact

The legal authority of the various counterparties to tie and to CEC (under its Guarantee) will be confirmed in the conventional manner:

- each party will produce certified board minutes or other legally competent evidence of the corporate decision to enter into the ETN Contract Suite;
- all signatories will demonstrate legally effective power of attorney from their respective organisations; and
- in relation to foreign companies, an external counsel's opinion covering the legally binding nature of the corporate acts (re Contract execution) carried out in accordance with the Board resolutions, the signatories' delegated authority and the enforceability of the Contracts against the parties through the courts in their respective home jurisdictions.

CEC and tie will be required to produce their own legal authority to transact as has been explained and agreed previously with CEC Legal.

The Infraco Contract executed by tie Limited, Bilfinger Berger (UK) Limited and Siemens plc comprises the Core Terms and Conditions and a series of detailed Schedules which contain the price for and the scope of the Infraco Works and amplify the responsibilities and commitments accepted by the Infraco.

Conditions Precedent

At present, the draft Infraco Contract provides that the delivery of various ancillary agreements (notably the novations and the performance security package) are conditions precedent to Contract effectiveness. Since the intention is for all documentation to be closed, provided and executed simultaneously, this technical provision may be removed prior to contract award date.

Warranties

The Infraco members provide key individual warranties regarding the Infraco Proposals meeting the Employer's Requirements and regarding their capacity to enter into the Infraco Agreement.

Duty of Care and General Obligations

Under the Infraco Contract, the Infraco has a duty of care and general obligation to carry out and complete the Infraco Works fully in accordance with the Agreement. Infraco is further obligated to procure that the Infraco Parties (the Infraco members and their agents, advisors, consultants and sub contractors) carry out the Infraco Works in accordance with, inter alia, the Contract, the general Law and stipulated tie and CEC policies to enable the Edinburgh Tram Network to be designed, constructed, installed, integrated, tested, commissioned and thereafter maintained. The scope for which the Infraco has contracted is contained in the Employer's Requirements and the Infraco Proposals.

Indemnity Provisions

Generally, the Infraco must indemnify tie and CEC from all losses incurred as a result of a breach of the Infraco Contract by the Infraco or negligent or wilful acts of the Infraco. This includes where the breach or negligence causes:

- death or injury;
- damage to property or to the Infraco Works;
- infringement of third party IPR;
- causing tie or CEC to breach any law, consents, third party agreements or undertakings entered into prior to the date of the Infraco Contract;
- causing tie or CEC to breach the Network Rail Asset Protection Agreement, the DPOFA or the Tram Inspector Agreement.

The Infraco also has a specific obligation to indemnify tie in respect of any losses suffered resulting from the adverse impact of the Infraco Works in respect of the property interests, liabilities or statutory obligations of Forth Ports and Stakis. The Infraco is wholly responsible to tie for any actions or omissions of its employees, agents, advisers and sub-contractors.

Principal Exclusions are the following:

- any act or omission of tie or CEC is the cause of such death, injury or damage to property;
- proportion of loss caused by tie/CEC;
- indirect losses of tie/CEC by reason of Infraco breach or negligence, but indirect losses claimed by a third party are carved out of this prohibition. Infraco would therefore be liable to indemnify tie/CEC against a claim for lost revenue asserted by a business adversely affected by Infraco's breach.

ETN Assets

The Agreement provides for the direct transfer of title to CEC in all materials, goods, and equipment which are intended to be part of the completed Edinburgh Tram Network. Infraco shall procure that all ETN assets are supplied free from security interests and that any goods or materials stored off site are identified as belonging to CEC, wherever practicable.

Price

A contract price has been agreed. The contract price and pricing schedules for carrying out the Infraco Works is contained in Schedules to the Infraco Contract. A substantial portion of the Contract Price is agreed on a lump sum fixed price basis. There are certain work elements that cannot be definitively concluded in price and as such Provisional Sums are included.

Programme

The Agreement provides that Infraco shall progress the Infraco Works to achieve timeous delivery and completion of the Infraco Works (or parts thereof) and in their obligations under the Agreement, all in accordance with an agreed Programme which is bound into the Schedules. This Programme is the product of tie, Infraco and SDS Provider negotiations and is cardinal to the control of Infraco and SDS Provider's performance and their potential entitlements to relief or additional cost.

Novations

The Agreement provides that, as a condition precedent, Infraco shall enter into and execute Novation Agreements to incorporate and bind previous agreements between tie and the design provider (SDS), the Tram supplier (Tramco) and the Tram Maintenance provider (Tramco), into the Infraco Contract. These agreements therefore become the full responsibility of Infraco as an essential component of the carrying out of the Infraco

Works. In addition to the Novation Agreements, assignable collateral warranties are to be provided to tie by the design provider (SDS), the Tram supplier (Tramco) and the Tram Maintenance provider.

Network Rail Interface

Under the Infraco Contract, Infraco acknowledges that it will require to comply with the Asset Protection Agreement (APA) with Network Rail in relation to the Edinburgh Tram Network. Infraco are to comply with the APA and undertake not to put tie/CEC in breach of the APA. The APA has been stepped down into the Infraco Contract so that the Infraco is fully on notice of those obligations which it will perform on behalf of tie/CEC.

Operator Interface

The Infraco's interface with Transdev is dealt with through Clause 17 of the Agreement. A duty of liaison and cooperation is imposed. Interference with maintenance works by the Operator may entitle an Infraco to claim for a Compensation Event and likewise any adverse affect of unplanned maintenance/defective maintenance would give rise to a right of indemnity for tie against any Transdev claim for relief/cost under the DPOFA. Any change to tram operations which adversely impacts the Infraco maintenance could give rise to a tie Change.

Safety

Infraco is to provide a permanent representation for the Project Safety Committee and shall develop and implement a safety management system and comprehensive plans to address all aspects of safety in working practices during construction, operation and maintenance.

Site Access

tie has granted a non exclusive licence to Infraco to enter and remain upon the permanent land for the term of the contract and exclusive licence to enter and remain upon designated working areas (the public road) during Infraco Works and shall provide Infraco with all necessary land consents.

Works on permanent land or temporary sites by Infraco are subject to compliance with the requirements of third parties.

Infraco Maintenance

Infraco shall comply with the requirements of the Code of Construction Practice and Code of Maintenance Practice with regard to the maintenance of access properties, bus stops, bus services and closure of roads.

The Infraco is obliged to undertake maintenance of the ETN from the time when any section is completed and afterwards under the full Maintenance Services regime once Service Commencement occurs. The Maintenance Services regime is for ten years post Service Commencement, with a unilateral option for tie to extend for five years, subject to any required changes. tie may terminate the Infraco Contract on six months' notice at

any time after three years of ETN operation. Compensation is payable as if such termination had occurred for tie default.

Milestones and Payment schedule

The construction sequence is broken down into construction milestones and critical milestones and Procedures have been agreed for the monitoring of progress toward each milestone based upon milestone schedules. Interim Payments will be made to Infraco monthly subject to and in accordance with the completion of stated Milestones. The Agreement obliges Infraco to complete the Infraco Work in sections and failure to complete sections by the sectional completion date will result in Infraco becoming liable to pay liquidated and ascertained damages to tie at amounts stated in the Agreement. If Infraco are delayed by reason of certain prescribed contractual events they may be able to apply for a Extension of Time and/or claim costs.

Variation

The Agreement contains a relatively conventional contractual change mechanism in relation to the management and evaluation of variations. Variation rules depend upon the type of change instructed whether it is a tie Change, tie Mandatory Change (where an event occurs which needs to be dealt with) or an 'Infraco' Change.

Phase 1b and Network Expansions

Infraco acknowledges that tie may, subject to notice instruct the Phase 1b works to be carried out provided that the election is made no later than 31st March 2009. The Agreement contains specific provisions (Schedule 42) under which Infraco would carry out Phase 1b works if so instructed. Network Expansion (i.e. a spur, interconnect or modification) would fall to be dealt with as a tie Change under the Variation mechanism.

Termination

If tie defaults (on payment above a certain threshold or becomes insolvent) Infraco may serve a termination notice in accordance with the Agreement. The Agreement sets out the treatment of such termination. If Infraco defaults in certain prescribed matters, tie may, after giving required notice, terminate the Agreement. The Agreement again sets out the rules relating to such proposed termination as to final account, compensation (if any) and tie's entitlements to compensation under these provisions, the compensation entitlements are sole remedies.

Dispute Resolution

The Agreement contains provision for the settlement of any disputes under a Dispute Resolution Procedure contained in the Schedules to the Infraco Contract.

Disputes are to be dealt with through a rapid escalation process to Chief Executive level in order to achieve amicable resolution of any unsolved dispute within 15 days. If no settlement is possible, the Chief Executives may elect mediation, adjudication, or court proceedings as the resolution process. The Dispute Resolution Procedure mechanic allows for joinder of related disputes at the instigation of either party. The provisions

are exempt from the application of mandatory adjudication time limits (under the Housing Grants Construction Regeneration Act 1996) by virtue of the Tram Acts.

SDS Novation Agreement and design delivery and approval process

Principles of Novation

The novation of SDS Provider to Infraco involves Infraco taking responsibility for managing SDS to produce the remaining design and approvals for the Edinburgh Tram Network.

The principal of novation was to ensure that the integration of design and construction is the responsibility of BBS and gives BBS recourse to the same contractual remedies against SDS as tie would have had in that situation, including critically the ability to claim against SDS in relation to defective design carried out by SDS.

SDS Provider Novation outcome

The novation of SDS Provider to the Infraco has been the subject of intense negotiation since preferred bidder announcement. tie's ability to close this element of the procurement has been compromised by:

- SDS Provider indifferent performance to design production programme
- BBS increasing visibility of SDS underperformance
- a reluctance by SDS Provider to engage on the terms of the novation
- the evolving status of the Employer's Requirements and the Infraco Proposals
- the negotiating stance of BBS to avoid importing any risk from SDS failure to manage design approval.
- SDS claims relating to earlier periods of design development and previous tie project management's lack of experience in using the SDS Contract to control SDS performance.

There is no SDS Provider performance guarantee. There is a £500,000 bond which is callable if SDS Provider fails to novate.

Design expectations of the Infraco

The Infraco offer is based on design completed to date and a programme for future delivery of design. The offer is also based on those approvals achieved to date and a programme for achieving the remaining prior and technical approvals.

The original 'Infraco' construction programme was based on version 22 of the SDS design programme; the construction programme included in the final 'Infraco' proposal has been updated to match up with version 26 of the SDS design programme (dated 4 February 2008)

The substantial progress with completion of the SDS design has reduced the risk of late production impacting on the construction programme and has given 'Infraco' greater certainty of the construction needed.

Managing Approvals Risk

The risk of securing approvals has been shared between SDS and tie. The 'Infraco' then takes programme and construction risk based on approvals being granted in line with the agreed master programme for the project.

SDS takes a capped risk of achieving delivery of batches for approval on the agreed date to the agreed quality. Provided the application for approval is made on time and the quality of application is in line with agreed expectations then tie takes the risk that the Council does not process the application within the 8 week period included in the programme.

The management of this risk has begun long before the application for approval is made. Designs have been reviewed progressively throughout their development involving the relevant Council officials and representatives of other approval bodies. Before applications are made for prior approval there is an 8-week period of informal consultation on top of the earlier involvement in design development. Addressing the comments received from informal consultation significantly improves the design and the chances of the Council being able to process an application within the 8 week formal period.

Design Guidance

In developing the current design, SDS has been under an obligation to take account of:

- the provisions of the Tram Acts
- the Environmental Statement
- statutory and supplemental planning guidance from the Scottish Government and City of Edinburgh Council
- the Tram Design Manual
- all third party agreements in relation to the project
- UK guidance on the safe design and operation of tram systems

Confirmation of BBS acceptance of modelling

This matter is now enshrined in the Employer's Requirements.

Scope of works and Employer's Requirements

The scope of the project is defined in the Employer's Requirements Schedule to the main Infraco contract and the stated scope has been aligned to the contractor's proposal defining the construction approach and to the scheme design prepared by Parsons Brinckerhoff. This interlocking set of detailed documents combine to form the scope of the project in contractual terms.

The Employers Requirements (ERs) are a comprehensive and detailed set of specifications which set out the project obligations and responsibilities against which the construction consortium (BBS) must comply. It runs to some 650 pages and sits as a schedule within the Infraco contract. The document has evolved as the business case

and design has been developed and reflects the inputs of the key 'user' stakeholders such as the Council, TEL and Transdev.

The document contains sections relating to how the project as a whole is to be delivered (for example project management, testing and commissioning and maintenance) as well the detailed systems and equipment requirements. The document was issued as part of the ITN package. Because it is essentially a procurement specification, wherever possible (and appropriate) tie have avoided being prescriptive and detailed because this would limit the freedom of bidders to propose their own specific, competitive solutions.

Since preferred bidder award, all of the ER terms have been reviewed in a three way technical alignment process:

- BBS proposal → ERs.

To ensure that BBS proposals comply with the ERs. This has involved removing all of the stated non-compliances noted at the preferred bidder stage by either relaxing the ER clause (without affecting the output requirements) or by updating the proposal to make it compliant. Commercial alignment of the ERs and the Infracore proposals has been concluded.

- SDS design → ERs

Because the SDS Design had responded to an up to date though not final draft of the ERs, the final alignment process produced no material mis-alignment issues. The final alignment review identified potential mis-alignment which was documented and assessed for its cost and programme implications and some minor amendments were agreed.

- Proposal → SDS design

To ensure that in areas where the ER terms allow flexibility in approach, it was necessary to ensure that the BBS proposed solution was consistent with the SDS design. A review of the final Proposals against the SDS design was executed and again some minor amendments were agreed. The main issue was the extent of road reinstatement and adequate allowance has been made in the final budget to accommodate this factor.

In addition to these processes the ERs have also been reviewed in varying degrees of detail by three legal teams, DLA, BBS' lawyers and Siemens lawyers (because a far larger part of the ERs relate to Siemens scope). In these cases the ERs were checked for consistency and alignment with the contract suite. All evident ambiguities, duplications and gaps have been dealt with to ensure that as a vital contract document it can be used effectively in the future.

The tie team is confident that the final version of the ERs, the contract version fully meets the requirements of the client, i.e. is consistent with the technical principles of final business case; and is consistent with both the SDS design and BBS proposals.

Advance purchase materials

CEC have required explanation as to what happens if BBS advance purchase to support unapproved design: the risk relating to advance purchase materials is with BBS if material is purchased to support unapproved design or design that has not been consented.

Infraco Payment mechanism

Construction

Payment under the contract is entirely against a 4 weekly application from Infraco in respect of milestones which have previously been certified by tie as having been achieved. The milestone schedule reflects the Infraco price allocated in amounts to series of construction milestones and critical milestones and to the future period in which each milestone is expected to be achieved in accordance with the agreed programme.

The milestone schedule and certification mechanism has been prepared and agreed in accordance with the following key principles:

- Save in respect of agreed advance payments, Infraco will not be paid in advance of its own outgoing cash flows through its own supply chain
- The individual milestones are defined such that the process of determining whether or not they have been achieved will be subject to the minimum of uncertainty or dispute
- The certification of a milestone will require evidence that all required relevant consents and approvals have been delivered in respect of the related works

The contract provides an effective mechanism for the addition and variation to milestones (valuation or date) initiated by either tie or Infraco.

Infraco will submit a detailed claim for payment within 3 business days of the end of each 4 week reporting period in respect of milestones certified as achieved following which tie will have 5 business days to certify the total payment and a further 15 business days to make payment. There are no express retentions of payment, but a retention bond is provided as explained below and tie has a contractual right of set off.

Commissioning and Maintenance

Infraco will commission Phase 1a in 4 key sections, transfer title accordingly and hand over control of each section to the operator and maintainers:

- Section A – The depot, certified after system acceptance test T1 has been passed for that section;
- Section B – Depot to the Airport, certified after system acceptance test T1 has been passed for that section;

- Section C – The rest of Phase 1a, certified after system acceptance test T1 has been passed for that section and system acceptance test T2 has been passed for Phase 1a, and
- Section D – Driver training and commissioning, certified after system performance test T3 has been passed for Phase 1a.

Certification of Section D requires that in addition to passing the system performance demonstration all relevant consents and approvals have been obtained and documentation and initial spares have been delivered.

After the period of trial running without passengers has been completed, passenger service will commence.

During the commissioning period, Infraco will be paid Mobilisation Milestone Payments according to the programme for establishing the maintenance organisation and systems. The Operator, Transdev, will be paid on a 4 week reporting period basis up to a maximum of a capped sum for the commissioning activities as a whole.

After the commencement of passenger operation, the Operator and the Infraco will be paid their respective operating and maintenance fees on a 4 week reporting period basis. The performance of the delivered systems in passenger service will be monitored against two final system acceptance test criteria, Network Performance test T4 and Reliability test T5. After the Reliability Certificate has been issued (Service Commencement + approximately 9 months) then the 4 weekly fees paid will be subject to the performance regime.

Infraco performance security arrangements

Bonds during construction period

Two bonds are being provided by Infraco from Standard & Poors A- rated financial institutions (expected to be ANZ Bank and Deutsche Bank), a Performance Bond and a Retention Bond. Both bonds are in substance 'on-demand', meaning there is no requirement that proof of failure (beyond formal notification) by Infraco must be produced by tie before a claim can be made under the bond.

The Performance Bond is in the amount of £23m throughout the construction period reducing to £11.5m when a certificate of Revenue Service Commitment is issued and further reducing to £9.2m when a certificate of Network Certificate relating to the achievement of performance criteria is issued. The issue of the aforementioned certificates is subject to a rigorous testing regime as defined in the Employers Requirements, including evidence that all relevant consents and approvals have been delivered, and provides both security for tie/CEC and incentive to Infraco to perform.

The Retention Bond is in the amount of £2m initially adjusting to the following amounts at sectional completion:

- £4m section A – The depot
- £6m section B – Depot to the Airport
- £8m section C – The rest of Phase 1a
- £10m section D – Driver training and commissioning

- £6m at issue of Network Certificate (pertaining to reliability as defined in the Employers Requirements)

The Retention Bond is released when a Reliability Certificate is issued.

The Operator provides a Performance Bond in amount of £10,000,000 from a financial institution of good credit. The Bond is 'on-demand', meaning there is no requirement for proof of failure by the Operator to be produced by tie before a claim can be made under the bond.

During the maintenance phase post Service Commencement, Infraco is required to provide a performance security (or submit to a cash deposit/retention regime) at any time that there is determined (by survey) to be remedial work of a value greater than the minimum to reinstate the Edinburgh Tram Network assets to the Handback Condition. The security may be up to £1,000,000.

Parent Company Guarantees (PCGs)

PCGs are provided by the ultimate holding companies of both Infraco consortium members in respect of all performance, financial and other obligations of their subsidiaries which are contracting with tie. The substance of these entities, which are the group holding companies in each case, has been subject to financial verification by tie.

The PCGs respect the joint and several liability provisions in the Infraco contract; each claim by tie under the PCG's must be served on each of the parent companies in the proportion of their share of the Infraco consortium but in the event of either parent company failing to honour payment of such a claim, the other parent company is liable up to the limit of overall liability specified in the Infraco contract (20% of the Infraco contract price but subject to graduated Step down).

The PCGs provide that in the event of a change in control or ownership of the subsidiary companies which are entering into the Infraco contract, the PCG's remain in force until a replacement PCG has been provided on terms which are acceptable to tie. Securing a stable position on BBS' offer on PCGs has proved very difficult indeed. Currently, the PCGs contain a Step down during the period post Service Commencement in relation to liability for Content defects, patent defects and pre existing obligations. Liability for maintenance related activity is capped at £3.5 million pounds.

All obtainable necessary collateral warranties have been agreed sought and provided for as requirements of Infraco.

Brief Overview of Tramco contract terms

Authority to Transact

This is dealt with in the same manner as under the Infraco Contract.

Joint and Several Liability

This issue is not relevant as CAF is sole Counterparty to both agreements.

Conditions Precedent

As for Infraco Contract.

Indemnities

The indemnity provision is back to back (as required) with the Infraco Contract.

Warranties

The three principal Warranties relate to:

- Tram defects - two years from maintenance commitment
- Paint and finishes - six years from maintenance commitment
- Key Parts - 10 years from maintenance commitment

Consents

The Tramco is required to support the obtaining of relevant operational Consents and permits and is responsible for obtaining Consents relating to the tram vehicles themselves.

Termination

Both Tramco contracts contain conventional and rolling stock market aligned termination provisions for Supplier default, no fault (30 days notice), client default, force majeure and corrupt gifts and fraud. No termination of the Tramco contracts cannot be terminated by Infraco post novation without tie's approval.

Trams will be supplied pursuant to a Tram Supply Agreement between tie Limited and Construcciones y Auxilliar de Ferrocarriles S.A (CAF) "Tramco". Tramco are to carry out the Tram works and design, manufacture, engineer, supply, test, commission deliver and provide 27 trams and if required any additional trams in accordance with the Employer's Requirements, the tram Suppliers Proposal and agreed programme. Tramco shall ensure that all data, component, systems, devices, equipment, software and mechanism incorporated in the trams are fit for purpose and compatible with each other. Tramco shall operate under good industry practice, comply with all applicable laws and consents and ensure that each tram meets the required standards. The parties have agreed to work in mutual cooperation to fulfil the agreed roles and responsibilities to carry out and complete the tram works in accordance with the Agreement. Tramco shall

deliver and finalise the designs, design data and all other deliverables as prescribed in the Employer's Requirements.

System Integration

Tramco shall provide support in respect of the key elements of system integration of the tram works with the Edinburgh Tram Network.

Operator Interface

Tramco acknowledges that the operator shall be responsible for the Operator Maintenance of the Edinburgh Tram Network and that Tramco would at all times liaise with the Operator.

Variation

In Similar fashion to the Infraco Contract the Agreement allows for the introduction of changes either by tie or Tramco always subject to notices and prescribed rules. tie may, subject to notice and terms, order additional trams with related spare parts and special tools.

Quality Assurance

Tramco shall at all times utilise a Project Quality Assurance Programme compliant to standards.

A tram manufacturing and delivery programme is agreed and regular monitoring of progress will take place.

There is provision in the Agreement for tie to be involved in inspecting the trams at various stages of the manufacturing process. Tramco shall deliver the trams to the designated point of delivery at the depot and delivery tests shall be conducted.

Tramco, tie and the operator shall agree a training programme and the detailed implementation.

Transfer of Title

Tramco shall provide Trams free from all security interests title to CEC on delivery or, in certain circumstances, at factory. Ownership earlier than this would expose CEC to not be able to reject a defective tram.

Tramco payment mechanism

Supply agreement

The payment mechanism under the supply contract conforms substantially to that under the Infraco contract as described above with the milestone payments heavily weighted towards:

- Initial mobilisation and establishment of supply chain
- Delivery of tram vehicles

- Attainment of performance and reliability standards as specified

Tramco performance security arrangements

Bonds during supply period

Tramco will provide a Reliability bond in the defined amount of 5% of the Tramco price such bond to be provided on or before the due date of delivery of the first Tram vehicle. A further advance payment bond is under discussion with tie.

Parent Company Guarantee (PCG)

The supply and maintenance contracts with Tramco are with the ultimate holding company so the issue of a PCG does not arise. The liability cap of Tramco under the tram supply agreement is 20% of the Tramco supply price.

Maintenance agreement

The Infraco is responsible for providing tram maintenance through Tramco performing the tram maintenance agreement. This is a relatively standard agreement, developed from UK sector models. Infraco is required to provide a security at any time that there is determined by survey to be remedial work of a value greater than £50,000 to reinstate the Edinburgh Tram Network assets to the Handback Condition. This may either be in the form of a cash deposit or an on-demand Handback Bond covering the full value.

Performance securities under maintenance agreement

Tramco is required to provide a security at any time that there is determined by survey to be remedial work of a value greater than £50,000 required to reinstate the Tram assets to the Handback Condition,. This may either be in the form of a cash deposit or an on-demand Handback Bond covering the full value of the remedial work outstanding. The liability cap of the Tramco under the tram maintenance agreement is 18.5% of the aggregate 30 year Tram maintenance price.

CEC Financial Guarantee

CEC are required to provide a guarantee to the Infraco of the financial obligations (including future variations) of tie under the Infraco contract in recognition of the fact that tie on its own has no capacity to bear any financial commitment insofar as it is not 'back to back' with the funding of the project which is channelled through CEC. In this sense it is materially consistent with the provisions of the PCGs (including periods allowed for payment of amounts due) provided by the Infraco, except that it is a guarantee of financial obligations only and not of performance. The CEC Guarantee will be released upon issue of the ETN Reliability Certificate, that is to say approximately nine to twelve months after Service Commencement. Any pre-existing claims will survive release until settled.

The terms and conditions of the CEC Guarantee and in particular its call mechanics, liability cap and protections are in line with market practice for this type of instrument. It should be noted that the Guarantee may be called upon by the Infraco on multiple occasions if tie is in payment default more than once. The instrument has been drafted, negotiated and settled with direct involvement and support of CEC Legal and Finance.

The guarantee is provided to Infraco meaning either or both of Bilfinger & Berger UK Limited or Siemens PLC or their assignees as permitted and approved under the Infraco contract.

CEC will benefit from the same contractual defences and entitlements to set off as tie and will have no liability greater than tie's. No claim can be made for an amount which is in dispute if tie has been referred the matter under the dispute resolution provisions of the contract.

The practical day to day implication of the Guarantee is that its provisions will not be invoked so long as the process for drawdown of cash from CEC to tie to meet payment obligations as they fall due is uninterrupted. Any dispute under the Guarantee would be subject to court proceedings.

**TIE LIMITED
7 APRIL 2008**

EDINBURGH TRAM PROJECT
FINANCIAL CLOSE PROGRAMME, QC AND APPROVALS PROCESS

(1) Background

This note summarises the process we will follow through to Financial Close and focuses on the quality control actions needed to ensure we have robust final legal documents for which tie and TEL take appropriate collective responsibility.

(2) Overall programme

w/b 24 th March	<ul style="list-style-type: none"> • Completion of the drafting for all critical Infraco Contract Suite issues, schedules and terms • QC programme on all finalised Infraco Schedules, third party agreements
w/b 31 st March	<ul style="list-style-type: none"> • Completion of the drafting for all remaining Infraco Contract Suite issues, schedules and terms • QC programme on all finalised Infraco Schedules, third party agreements • Finalisation of Close Report and DLA Report
w/b 7 th April	<ul style="list-style-type: none"> • QC programme, all remaining areas • Conclusion to Close Report and DLA Report including CEC sign-off • Approvals required from all parties to support Close
Monday 14 th April	<ul style="list-style-type: none"> • All documents ready for signature
Tuesday 15 th April	<ul style="list-style-type: none"> • Financial Close – contract completion

(3) Quality control

Outputs

- Infraco Contract Suite
- Necessary third party agreements
- Close Report + Appendices
- DLA Report + Appendices
- Grant Funding Letter (completed)
- Operating Agreements x2

Processes

- Management of Close process & issue resolution (JM)
- Finalisation of Infraco contract suite (DLA)
- DLA Report + Appendices finalisation (DLA)
- Close Report + Appendices finalisation (GB)
- Approvals process – counter-parties (DLA)
- Approvals process – tie / CEC (GB – see below)

Quality control approach

The objective is to ensure that a knowledgeable tie or TEL person, semi-independent of the front-line negotiating and legal team, reviews the final form of the documents. The review should identify 1) fatal flaws ; 2) potentially important issues needing an internal debate before sign-off ; and 3) obvious errors. This review is not about nuances or minor drafting changes nor is it designed to second-guess negotiated commercial positions unless there is an obvious serious issue.

The attached matrix sets out the detailed responsibilities :

- The responsibility for finalisation of the Infraco Contract Suite is based on the matrix controlled by Geoff Gilbert.
- The Primary Reviewers for each important document must review the document in full and sign-off.
- The scope of work by the Secondary Reviewers should be agreed with the Primary Reviewer and comments finally provided to the Primary Reviewer, who can judge how they should be handled.

Certain of the third party agreements have already been signed. There is no point raising issues on these for amendment, but we should identify any points which may be inconsistent or problematic in some way relative to the final Infraco documents. These reviews are therefore light touch only, but still potentially important.

All matters identified by (or through) the Primary Reviewers should be discussed with Jim McEwan, Steven Bell and Andrew Fitchie before being communicated in any way to the counterparties.

DLA will perform their own legal QC review on the full set of final documents and this will support and complement the review by tie / TEL people.

Susan will manage the Close Programme including the QC work. Each person involved will be expected to sign-off on conclusion of their role in sensible terms, to evidence execution of our QC processes.

(4) Approvals Process

The approvals process should be straight-forward :

Documents required by CEC officials :

- Close Report update
- DLA Report / appendices update
- Letter from WG to CEC Chief Executive recommending completion

The Close Report and DLA Report will be finalised and sent to CEC next week (w/b 31/3) with Q&A and approval by CEC the following week (w/b 7/4).

The letter to Tom will be in similar form to the letter which supported issue of the Notification letters and will be supported by a formal conclusion by the tie / TEL management team.

Once the CEC officials are content, they will no doubt convene with Tom and we should then get the reciprocal letter from Tom to WG approving contract commitment. This letter will be the basis of a meeting of the WG / DM / NR Approvals Committee to finally authorise WG to sign the contracts.

The next TPB is scheduled for Wednesday 9th April and an update on progress will be presented.

There is no further approval required from TS, although courtesy calls on progress and to ensure the money is ready to move would be appropriate.

GB
28th March 2008

FINANCIAL CLOSE - QC PROCESS	Responsibilities :						
	Finalisation (based on Schedule status doc 20.3.08)	Main QC Review	Secondary QC Review(s)				Full DLA QC review
Documents							
Infraco Contract Suite :							
Infraco contract	GG / DLA	SB	DM	JM	SMcG	√	
TSA	AR / DLA	SB	SMcG	DM	BC	√	
TMA	AR / DLA	BC	SMcG			√	
TSA Novation Agreement	AR / DLA	n/a				√	
TMA Novation Agreement	AR / DLA	n/a				√	
CEC guarantee	DLA / CEC	SMcG				√	
SDS Novation Agreement	JM / DLA	SB	DS			√	
<i>Principal schedules (in addition to above) -</i>							
Definitions	GG / DLA	SB	DM	JM	SMcG	AR	√
Employer's Requirements (Sch 2)	MC	SB	JM	DM	GG	AR	√
Pricing (Sch 4)	GG / BD / DM	SMcG	SB				√
Milestone payments (Sch 5)	DM / ES	SMcG					√
Maintenance pricing / payment (Sch 6/7)	AR	BC	SMcG				√
Security package (Sch 9)	DLA	SMcG	GG				√
DRP (Sch 10/11)	DLA	SB	DM				√
Insurances (Sch 12)	DLA	MH	SC				√
TPAs (Sch 14)	DLA	SC	SB	AS			√
Design management (Sch 15)	DS	SB	SC				√
Programme (Sch 16)	TH	SB	SC				√
Tramco spare parts (Sch 26)	AR	BC	SMcG				√
tie obligations (Sch 27)	GG	SB	SC				√
Infraco Proposal (Sch 31)	MC	SB	JM	DM	GG	AR	√
Building Fixing Agreement (Sch 34)	BD	SB	AS				√
Tram Inspector Agreement (Sch 35)	AR	BC					√
Reporting Period end-dates (Sch 36)	BD	SMcG	DM				√
Phase 1B (Sch 38)	GG	SB	DM	SMcG			√
TSA obligations (Sch 40)	AR	BC	SMcG				√
Environmental / H&S KPIs	SB	TC					√
Ground condition information (Sch 42)	SB	GG					√
Utilities information (Sch 43)	SB	GG					√
Close Report :							
Introduction	Complete	SB			CEC		
Infraco Contract Suite	GB	SB			CEC		
Grant award letter	Complete	Complete					
Procurement risk	Complete	SB			CEC		
Third Party Agreements	Complete	GB	DS		CEC		
Land Acquisition Agreements	Complete	GB			CEC		
Governance & corporate matters	Complete	Complete					
Risk assessment - in-process & provisional matters	Complete	SC	MH		CEC		
Readiness for construction	Complete	JM	SC		CEC		
Specific confirmations	Complete	SMcG			CEC		
App 1 - Design management	SC	SB	DS		CEC		
App 2 - Governance & Delegations	Complete	n/a					

FINANCIAL CLOSE - QC PROCESS		Responsibilities :								
		Finalisation (based on Schedule status doc 20.3.08)	Main QC Review	Secondary QC Review(s)					Full DLA QC review	
Documents										
DLA Report										
Letter from DLA	DLA		GB						√	
Infraco summary including Council guarantee	GB		SB	DM					√	
Procurement risk	Complete		SB	MC	JM				√	
Risk matrix	DLA		SMcG	SC					√	
Other key documents :										
Grant funding letter	Complete		n/a							
Operating Agreement - tie / CEC	GB		n/a							
Operating Agreement - TEL / CEC	GB		n/a							
Third Party Agreements :										
BAA license / lease	Complete		SC	DS					√	
Station change	Complete		SC	DS					√	
Depot change	Complete		SC	DS					√	
NR APA	Complete		SC	DS					√	
NR Framework agreement and sub agreements	Complete		SC	DS					√	
Forth Ports	SC		GB	DS					√	
SRU	SC		GB	DS					√	
License - West Craigs	Complete		SC	DS					√	
License - Gyle	Complete		SC	DS					√	
tie and TEL Parties :										
Alastair Richards	AR									
Alasdair Sim	AS									
Bill Campbell	BC									
Bob Dawson	BD									
Dennis Murray	DM									
Damian Sharp	DS									
Eric Smith	ES									
Graeme Bissett	GB									
Geoff Gilbert	GG									
Jim McEwan	JM									
Matthew Crosse	MC									
Mark Hamill	MH									
Steven Bell	SB									
Susan Clark	SC									
Stewart McGarrity	SMcG									
Tom Condie	TC									
Tom Hickman	TH									