CONFIDENTIAL NOTE –
WHERE DOES THE CEC £45m COME FROM?

Rebecca,

Re your earlier email – I am very happy someone is thinking about this. I've included for easy reference:

- Annex 1 - An extract from the paper tie prepared for discussion between CEC and SE back in July 05 (you got it I think) which describes how an amount of £45m might be delivered.

- Annex 2 - An extract from the paper on Tram funding and phasing which went to full Council on 26 Jan 06.

The 26 January 06 Council paper had a table in it outlining the sources of the £45m as follows. This was prepared by CEC Transport but as I was in correspondence with them while it was being prepared I can comment on the sources as follows:

Council cash contribution	£2.5m	Note 1
Council land contribution (at out-turn prices)	£6.5m	Note 2
Imminent S75 planning agreements	£7.9m	Note 2
Anticipated development gains on Council sites	£5.0m	Note 3
Current S75 planning agreements	£3.2m	Note 4
Anticipated future S75 planning agreements	£7.9m	Note 4
Anticipated Capital Receipts from Council Sites	£13.0m	Note 5
Total Council contribution	£45.0m	

Notes

1. We've already had £1m of this in 0506 (I presume this will still be dealt with by deduction from the Jan 06 claim to SE as you previously stated). I noted that the 26 Jan paper said the other £1.5m would not be available till 0708 at the earliest? Did you have input to that decision?

2. These are the value in aggregate of land required to build the Tram on and which is either already held by CEC or which will be contributed to CEC under S.75 agreements eg with Forth Ports. This is therefore not a cash injection and will effectively be treated as injected into the project at the point Infraco is licensed by CEC to start building on the land. We may have a head-scratching issue to deal with here and that is whether the value of these land holdings is already fixed for funding purposes or if it is subject to revaluation at the point of contribution to the project. What happens to the £45m if the value of this land turns out to be less than was forecast? To be discussed. Would need revisiting to assess the impact on the land contribution of not building the Granton leg – maybe £2m less – again how does that effect the £45m contribution?

3. This was the income stream anticipated in the IOBC (and previous OBC iterations) as being delivered via a JV between tie and EDI into which CEC would contribute a number of development sites adjacent to the Tram which could be developed by the JV for profits. The latest **tie** work to put a value on the profits from those sites is summarised at Annex 3. The proposed tie/EDI JV appears to have stalled more than a year ago. We should be revisiting whether this is still the desired way to extract value from these sites and if so get on with it after Royal Assent. Profit unlikely in any case to be crystallised until after commencement of Tram operations.

4. These are the anticipated future income streams from the Non-Statutory Developers Contributions policy i.e. the formula based contributions from developers. The £3.2m is what is already agreed with developers in respect of planning permissions granted.

The £7.9m was an extrapolation of what the policy might deliver in the period up to commencement of Tram operations. You will recall from the IOBC that tie conservatively estimated this policy should deliver around £1m per annum over the life of the Tram project. Receipts from developments by Forth Ports in particular could bring about significant levels of contribution. The timing of all of it is however very uncertain. I have heard an idea that CEC might be able to negotiate a lump sum contribution from Forth Ports in lieu of the application of the policy. Is that such a ridiculous idea? Would need revisiting to assess the impact on projected contributions of not building the Granton leg.

5. This was the balancing figure to make up the £45m. CEC Transport identified at least 2 sites which might make a significant contribution to this sum if sold for residential development – one being part of the site of what would have been the Line 1 depot and the other being the site of the Tram depot many years ago on the east side of Leith Walk. My own expectancy was that CEC Transport reckoned they could deliver this amount by land sales in the next 2-4 years but I could be completely mistaken here and you should discuss it with them.

What all this boils down to is that there is an uncertainty about the timing of a large part of the receipts which are anticipated to provide the £45m contribution. However we heard KPMG say that SE are pretty clear that they will want certainty about when and how the CEC contribution will go into the project. The obvious answer is some kind of borrowing mechanism as per your email and there would be an interest cost associated with that. In a collaborative world you might get support from SE to service that borrowing in the event that the receipts above did not materialise as expected – thus reducing the financial risk CEC might be taking on.

Hope this is a step forward for you and all of the above might be part of our discussion at Keith's office on Thursday.

Stewart

Annex 1 - Extract from a paper tie prepared and submitted for discussion to CEC Transport and SE back in July 2005 and which is where the figure of £45m originated from:

CEC contribution to capital costs of phase 1

The IOBC concluded that CEC does not have the financial capacity to contribute to Phase 1 capital costs beyond the level of risk-sharing described above. For the purposes of promoting a discussion the following analysis assumes that the SE will index the grant in return for a substantive, indexed contribution from CEC. The possible sources of contribution by CEC are:

- Cash contributions to development

The Council have committed £1m to the next phase of development and implementation funding, focussed on the period to Spring 2006 when the OBC will be produced. Financial close is scheduled for mid-2007 and the level of the implementation expenditure is expected to continue at the current level. Early construction works, primarily utility diversions, will commence in 2006 following Royal Assent, would be in addition. The Council are prepared to commit to a further £1.0m in financial year 2006-7 and £0.5m in 2007-8 to sustain their commitment to sharing the cost of the development and implementation process. Allowing for indexation, these sums will amount to a total contribution prior to financial close of **£2.6m**. This replaces funding by the Executive from the grant.

- S75 agreements and reasonably certain development contributions

tie's capital cost estimates include the costs of acquiring land which we have a reasonable expectancy will be contributed to the project under S75 agreements. The indexed amounts are:

Line 1	CEC owned - £1.8m Waterfront Edinburgh - £0.5m Forth Ports - £7.8m Total Line 1 - **£10.1m**
Line 2	CEC owned - £4.7m Edinburgh Park - £1.6m Total Line 2 - **£6.3m**

These contributions are not in cash but rather are items which have been negotiated or offered by the Council and largely represent capital expenditure which will not be incurred. Most of the land has intrinsic value and would potentially be realised in another form by the Council if it were not to be contributed to the tram project. Allowing for the Executive's own land contribution identified above, the total available from S75 agreement plus secured developers' contributions before financial close (from sites to be jointly developed with EDI and other sites) can reasonably be expected to be **£20m** in inflated terms by financial close.

- Future CEC cash flows from the Trams

The March IOBC identified the possibility of CEC borrowing against its forecast future cash inflows from the Tram network. The borrowings reflected in the financial model showed CEC utilising its entire forecast future income streams to borrow c£60m to contribute to the capital costs of network of lines 1 and 2 less the Newbridge extension. At the time CEC concluded that it did not have the capacity to take on the risks associated with such loans, primarily due to the uncertainties regarding the forecast farebox revenues, and indeed consolidated revenues of TEL, which would be the primary source of funds to repay such borrowings.

CEC have revisited this area and are willing to discuss an approach to contribution in anticipation of future receipts which represents a manageable level of risk to the Council. The components would include:

- CEC provide a contribution to the capital costs of phase 1 totalling **£15m**, measured in 2003 money, in line with the basis of the capital cost estimates and the SE grant**.** Assuming indexation, which in this case allows for above inflation growth in underlying property assets which may be used to part-repay the loan, this would arrive at c**£22m**. This contribution could be structured as borrowings against CEC's Capital Receipts Programme to be repaid out of proceeds from property or land sales over a 3-5 year period. Alternatively all or part of the amount might be lent to CEC by SE on favourable terms and with flexible repayment terms such that, in the initial years of Tram operation, the risk of not generating enough surplus in any given year to service the borrowings would be the mitigated. A variation to be investigated and which is potentially attractive would be for the Council, through TEL or Lothian Buses, to lease the tram vehicles within a tax group which ensures capital allowances can be used effectively.

There are a number of combinations or variants to this approach which may be adopted and which would be subject to further analysis. The contribution to capital costs by CEC would amount to **£45m** (including indexation).

Annex 2 - Extract from report to the Council on funding and phasing of 26 Jan 06 (NB – Not prepared by tie)

Proposed Council Funding Contribution

3.16 In response to the Scottish Executive's position, the Council, as Promoter, would also make a contribution towards the capital cost of its tram project, to be structured in a manner which minimises financial risk. The Council has already committed £1m for the current financial year as a contribution towards development and implementation and could allocate a further £1.5m but not earlier than financial year 2008-09.

3.17 The Council must, however, balance its desire to support the project with its fiduciary responsibility and limited resources. The Council's contribution would, therefore, comprise only such amounts as could reasonably be expected to be funded from future tram related development income and receipts, rather than from general funds or from Council Tax. The anticipated sources of such receipts include:

a land contributions by the Council;
b anticipated development gains accruing to the Council on Council owned sites;
c Section 75 planning agreements already negotiated and anticipated future agreements;
d third party developments around the tram routes; and
e anticipated capital receipts from tram related Council owned sites.

3.18 The total Council contribution which would be associated with the complete tram network is currently estimated at £45m. To enable the capital funding of the project, it is assumed that the sums shown in Table 2 below would be borrowed, where necessary, against the anticipated receipts. The Council's contribution would not be committed until the completion of a satisfactory final prudent business case.

3.19 This gives a potential capital funding availability of £535m for the first phase of the network.

Table 2 Capital Funding Availability

Indexed Scottish Executive Grant (estimate)	£490m
Council cash contribution	£2.5m
Council land contribution(at out-turn prices)	£6.5m
Anticipated development gains on Council sites	£5.0m
Current S75 planning agreements	£3.2m
Imminent S75 planning agreements	£7.9m
Anticipated future S75 planning agreements	£7.0m
Anticipated Capital Receipts from Council Sites	£13.0m
Total Council contribution	£45m
Total funding available allowing for inflation	**£535m**

Note that current and imminent S75 agreements are reasonably certain sources of funds. Future S75 agreements and anticipated returns from the sale of Council sites are, however, only estimates at this stage.

Annex 3 – Development potential of CEC owned sites

CEC sites approved for 'release' July 2004

Balbirnie Place; (Line 1) this site will not provide any development opportunity, post/pre- tram, owing to steep nature of embankment location and the proximity of other housing and main roads. **Forecast residual land development value – NIL.**

Roseburn Terrace 'Triangle'; (Line 1) this site has limited potential given its shape and elevated location relative to Roseburn Terrace and Roseburn Cliff. Car parking and access are also seen as problematic, given the shape of the site. Wester Coates access, if achieved, would provide better development potential for site. **Forecast residual land development value - £1M - £1.5M.**

Maidencraig/South Groathill; (Line 1) EDI's architects have designed a possible scheme but it would require the tram route to be slightly re-aligned. If not, the strips of land are too narrow to offer any development potential. **Forecast residual land development value - £0.5M.**

South Gyle/Broomhouse; (Line 2) the site description covers the area adjacent to the Broomhouse/Bankhead Drive Roundabout which leads into South Gyle and Edinburgh Park. Seen as a high potential location, a brief outline design has been put forward by the architects which results in a meaningful square footage of residential units and associated car parking. **Forecast residual land development value - £0.75M.**

Additional CEC sites put forward by *tie*/identified by EDI

Telford Drive; (Line 1) this location was put forward by EDI and, again, would require the tram line to be marginally re-aligned, but within deviation limits. Otherwise, the two strips of land offer up little, by way of development potential. **Forecast residual land development value - £0.5M**

Broomhouse Drive; (Line 2) sited opposite Saughton House, the architects have drawn up a sizeable residential design, which maximises the site and yet copes with the close proximity of the ETN corridor. **Forecast residual land development value - £1M.**

Stenhouse Drive; (Line 2) arguably, seen as the most attractive opportunity for residential development, despite the close proximity to Edinburgh/Glasgow rail mainline and guided bus way/tram line. Adjacent to good quality and mature CEC housing, overlooking golf course and beyond to Corstorphine Hill. EDI appear very excited by the potential which this land offers. There may be a question mark over site assembly/ownership as there is a TA/ATC building adjacent to the three parcels of land and which could have a bearing on what could be done on site. **Forecast development value - £1M.**

Carricknowe; (Line 2) this is a very long and narrow strip of land, which boundaries the CEC golf course, the ETN corridor and, beyond, the Edinburgh/Glasgow rail mainline. Access and car parking would be difficult and only prospect might be single aspect housing which would receive an unwelcome response from Head of Planning within CEC. ***tie*** and EDI's view is that this site is not worth pursuing. **Forecast residual land development value - NIL**

West Granton Link; (Line 1) mixed views held on this site which appeared on a ***tie*** review paper, as a site offering development potential. EDI do not hold a formal view but having visited on a couple of occasions, ***tie's*** view would be that the site has already been absorbed into the existing residential/recreational development and should be viewed as a public amenity with little prospect of creating a new residential or commercial development. There is also now a question mark over the beneficial ownership of the site from survey plans provided by Dundas & Wilson. **Forecast residual land development value - NIL**

In summary then, <u>nine</u> sites, of which three offer very little, or no development potential, three which would require a degree of work to become viable or economical to release circa £2.25M

and three which appear, on the face of things, to be relatively straightforward, with a potential value of £2.75M.

Of these nine sites, only four have been approved by the CEC Executive for release and, <u>as a first step, 'access'/permission needs to be obtained for considering and/or advancing the remaining five locations.</u>