

Nick Smith

NS 1.1

**From:** Nick Smith  
**Sent:** 01 June 2010 15:06  
**To:** Dave Anderson; Donald McGougan; Marshall Poulton  
**Subject:** RJ meeting

Here is a quick summary of our discussions with Richard this afternoon:

- Richard has received a copy of the full 35 page Project Notice 90.1.2 letter from the lawyers. He does not propose to circulate this to CEC at present. I agreed that we were happy to wait until the outcome of Carlisle as we would not serve it until then.
- Richard confirmed that the 90.1.2 letter would definitely not be sent until after 16 June which is the next meeting between Messrs Mackay, Wakeford and Darcy.
- tie are confident in their case re 90.1.2, but are of the view that serving the notice is potentially a commercial point of no return.
- Richard confirmed that positive is too strong a word to describe recent progress. Finely balanced, robust and constructive are better. Richard thinks it's 50:50 at present.
- BB appear not to be engaged fully and are conditioning tie to receive bad news re costs. tie will not receive cost details until 1 July.
- TS have some concerns with the latest update report. They appear to want to distance themselves from decisions and query whether tie have indeed regularly briefed them. Richard thinks this is nonsense.
- Richard has very strong views on the CEC report and its potential to damage things commercially. Marshall and I advised him of the reasons for this. He understands CEC officers responsibilities but wanted to highlight the issue.
- An interim decision on Mudfa Rev 8 is due today. First question to be answered is whether it is a valid legal claim.
- Richard would like guidance re a go/no go re works in the North of the city - eg Baltic St, Lindsay Road etc.

Hopefully I haven't missed anything but Marshall will no doubt fill any gaps.

Kind regards

Nick

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(t) [REDACTED]

*Please note that I am not in the office on a Monday*

Nick Smith

NS 1.2a

**From:** Fitchie, Andrew <Andrew.Fitchie@dlapiper.com>  
**Sent:** 15 June 2010 19:16  
**To:** Richard Jeffrey; david\_mackay [REDACTED]; Nick Smith  
**Cc:** Anthony Rush; Graeme Bissett  
**Subject:** Council report  
**Attachments:** Scan001.PDF

Legally privileged and FOISA Exempt

**URGENT**

Richard  
Nick

I have reviewed the CEC draft report of which Richard gave me a hard copy yesterday. I spoke to Nick on confidentiality and media point this morning. Since I last saw and comment on this matters have changed to the point where termination is a real possibility.

My observations - based on the very critical stage of the Project and the contract administration - are:

1. **There are repeated references to obtaining legal advice and Counsel's opinion.** Even covered by explicit reference (see my revisions) to the fact that this advice is subject to legal professional privilege, I remain very concerned that mischief is made by BSC in attempting get this advice. Whether they succeed or not is not the point. Applications to get it can tie up resource at a critical point for tie. It should not be overlooked that justifying non-disclosure to the Information Commissioner inspite of public mention of the existence of the advice is not the same has waiver of legal privilege which can occur by error or by too wide a distribution which dilutes the privileged entirely.

Please consider seriously if it is necessary to include these references in the Report and what they actually add.

2. The report contains the views of others (eg Carlisle team). I am asked about defamation and confidentiality. On the latter, I am satisfied that there is no breach of the contractual duty tie owes. On the former the test for defence against allegations of defamatory comment are:

**truth and factual accuracy**  
**public interest**  
**absence of defamatory intent**

In my view, CEC needs to satisfies itself that it is not unreasonably or slavishly reliant upon the opinion of others in adopting and making statements about BSC behaviour so that CEC is content that it holds an informed and dispassionate view based on an analysis and reasonable interpretation of the facts.

We have advised extensively on the subject of defamation - so that I would repeat all of that advice here and am happy to discuss further if required.

kind regards  
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**Andrew S. Fitchie**  
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NS 1.26

CEC paper with Tony's comments.



Item no  
Report no

DLA PIPER  
COMMENTS  
15.06.10

## Edinburgh Tram Project – Update Report DRAFT

The City of Edinburgh Council

24 June 2010

### 1 Purpose of report

- 1.1 The purpose of this report is to update the Council on the progress of the Edinburgh Tram Project and related issues including: current contractual difficulties with the Contractor, the Bilfinger Siemens CAF Consortium ("BSC") (in particular regarding agreed scope and progress of the civil engineering and infrastructure installation works); the approach adopted by tie Limited ("tie") to achieving acceptable resolution of the matters in dispute; budget, scope and programme implications; the Council's funding strategy (including contingency planning); communications with stakeholders and a summary of the current position on utilities diversion works completed on-street.
- 1.2 The project governance arrangements have facilitated communication between tie and Council officers on key aspects of the project. Specifically, the Operating Agreement that is in place between the Council and Transport Edinburgh Limited (TEL) requires that the Council must be made aware when there is a reasonable expectation that the approved price, programme or scope of the project may change and this requirement is being fulfilled in terms of this report. TEL is not, however, seeking any additional budget for the project at this time.
- 1.3 In view of the importance of the project to the city and the ongoing difficulties being experienced, it is considered extremely important to place as much information in the public domain as commercial considerations and confidentiality undertakings allow.

### 2 Summary

- 2.1 A report was provided to the Council meeting of 20 August 2009 which resulted, *inter-alia*, in Council endorsement of the contractual processes on which tie had embarked to provide greater cost and programme certainty in the project. In the intervening period, tie has increasingly had to enforce contractual rights in its engagement with the BSC Consortium to attempt to expedite progress on the tram infrastructure installation works and to compel action to resolve dispute.
- 2.2 Although well behind the rate required by the contractual programme, there has been some degree of construction progress on the off-street sections of the

works, particularly to the West of Murrayfield Stadium and at the tram depot at Gogar. The utility diversions (carried out under separate contract) are also now substantially complete, creating much-improved utility asset quality along some of the city's main thoroughfares as an adjunct to the unobstructed areas for tram installation. Substantial additional utilities work beyond that originally planned has had to be executed which has affected site access for BSC. The construction of the tram vehicles by CAF has proceeded to programme and the first vehicle has arrived on schedule in the city following successful testing at the Siemens facility in Germany.

2.3 There continue to be a number of serious contractual difficulties with BSC relating to design issues (including delay in design completion); impact of delay caused in part by utilities work and associated extension of time claims; and failure to progress by BSC despite client instruction. This report provides a comprehensive update on each of these issues and their respective implications. It may be worth referring specifically to the lack of DAS's and the fact that they haven't delivered a design for on-street trackworks which could be seen to permit operation of the ETN

2.4 The application by tie of the formal Dispute Resolution Procedure ("DRP") within the terms of the contractual agreement with the Consortium ("the Agreement") has achieved resolution on some of the issues subjected to the process. However, the targeted improvement in infrastructure installation performance by BSC has not materialised. Many of the adjudications relate to issues in isolation of the whole picture - we do get some useful feedback.

2.5 Following Council endorsement at the end of 2009 and in the absence of acceptable construction progress, tie set out a number of areas where it was necessary to adopt a more contractually-led approach with BSC in order to protect stakeholders' interests. These included continued application of DRP, audit verification on a number of areas relating to BSC management of the contract and, for the purposes of dispute resolution and in preparation for litigation, (a) detailed legal investigation of the matters under dispute; and (b) Senior Counsel's opinion on the critical areas. A review of strategic delivery options for taking the project forward was performed, including assessment of the option of terminating the Agreement.

2.6 The detailed legal advice received has reinforced tie's interpretation of the contractual position on the main matters under dispute. And applying the contract terms as an entire contract. Although there has been no breakthrough which has restored momentum to the project, negotiations continue with the benefit of the breadth of detailed commercial and legal support, including Senior Counsel's opinion, available to tie.

2.7 This report provides an update on the project budget, scope and the programme implications of developments since the last report to Council. It is now clear that the full Phase 1a tram system cannot be delivered within the available funding envelope of £545m and the overall outcome remains uncertain for so long as the intractable behaviour of BSC persists. tie now has recently received advice based on resequenced programming logic that a properly performing contractor could still have the trams open for revenue service by the end of 2012 (albeit maybe a truncated ETN). However, while

INSERT:

All of this advice is subject to legal privilege and is not for disclosure.

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BSC remains in dispute with tie and construction progress is unsatisfactory, it is not possible to offer any certainty on the cost or programme outcomes.

- 2.8 In the period since the 20 August 2009 update report, Council officers have been analysing contingency funding options in the event that the estimated capital cost of the project does exceed the available funding of £545m. This work has identified options for consideration and this report provides detail on these options. The report also examines the Council's funding strategy and current budget commitment of £45m.
- 2.9 As a prudent contingency, tie has assessed the option to deliver Phase 1a of the tram project on an incremental basis. Details of this assessment are included in the main body of this report.
- 2.10 Since August 2009 there has been regular communication with key stakeholders, in particular to ensure that Transport Scotland has been kept up to date with the issues relating to the project. A series of meetings has taken place with Transport Scotland explaining the areas of dispute, negotiations with BSC and the potential budget and programme implications.
- 2.11 In summary, the current position remains highly unsatisfactory despite extensive and constructive attempts by tie to achieve reliable execution by BSC of its obligations in the Agreement. It is to be hoped that an acceptable outcome can be achieved and current negotiations are examining options which could provide such an outcome. However, in the event that this cannot be achieved, tie is taking the steps necessary to prepare for termination of the Agreement.

### **3 Main report**

#### **Underlying Case for Trams**

- 3.1 The Final Business Case for Phase 1a of the Edinburgh Tram Network was approved in December 2008. The validity of the Business Plan approved at that time remains intact. Since 2008, when construction of tram infrastructure commenced in Edinburgh, a number of other cities in the UK have continued their commitment to tram networks. Manchester Metrolink is currently planning several extensions over a prolonged period of time, while Nottingham Express Transit has two further lines planned. The initial success of the Dublin Luas tram scheme, upon operation in 2004, led to a commitment to seven future lines or extensions over a ten year period in the Irish government's 2005 Transport 21 plan. The evidence from all of the UK networks and also from Dublin is that trams are well-liked by the travelling public, enjoy excellent patronage and enhance the image of the cities in which they operate.
- 3.2 The first tram vehicle has now arrived in the city and is on public display at the tram stop on Princes Street. During the first month on exhibit there were in excess of 30,000 visitors. Feedback so far has been largely positive with 91% of visitors surveyed stating that they were impressed or very impressed by the vehicle.

#### **Current Contractual Difficulties**

3.3 Against that backdrop, the ongoing difficulties experienced with BSC are particularly disappointing. ~~Delete and insert The ongoing difficulties with BSC reflect an obstinate attitude by them rather than the partnership ethic envisaged by the Contract which framed tie's early approach to how the Contract was administered~~ The Agreement to construct the tram infrastructure and deliver the tram vehicles was signed in May 2008 after an 18 month procurement process. The essence of the Agreement was that it provided a lump sum, fixed price for agreed delivery specification and programme, with appropriate mechanisms to attribute the financial impact of any subsequent changes, all as set out in the Agreement. However, a number of problems have arisen in the application of the Agreement terms.

Agree

3.4 Certain design-related matters have been disputed as to their inclusion or otherwise in the contracted scope of work and therefore their inclusion or otherwise in the contractual price. tie has accepted that certain matters would require to be treated as legitimate additions to that price and has concluded agreement on some £18m of extra payments for changes such as soft ground treatment; additional demolition works; utilities diversions undertaken by BSC; and the draw down of provisional sums or revised specifications to address Council or third party requirements. There remains disagreement with BSC on other matters and the DRP process in the Agreement is being deployed to enable issues in dispute to be resolved either through negotiation or by the decision of the adjudicator. The application of this formal process does not prejudice either party's right subsequently to take an issue to court; however, both parties must first exhaust the process set out in the Agreement.

appear not to be

Comment [MSOffice1]: Update to confirm

Contractually required design assurance statements

3.4.4 ~~It is significant that Infracore are not holding the designer SDS to account for substantial and unprecedented delays. This gives rise to what may be an accurate conclusion that Infracore are themselves responsible for those delays. In many cases the delay in delivering DAS's for integrated design appear to be rooted in integration problems within Infracore and in some cases (eg: the trackwork) integrating German design standards into UK requirements~~

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3.54.1 Fifteen matters have been processed through DRP. Overall, the application of DRP to disputed matters has reduced BSC's claims for additional payment by circa £11m. This includes the sum of nearly £4m saved through application of the DRP on two claims resolved near the end of May 2010. The majority of the claims submitted have been prepared by Bilfinger Berger. tie is satisfied that the overall balance of adjudication outcomes has more than justified its interrogation of the initial claims made by Bilfinger Berger. tie's firm legal advice (prepared in contemplation of litigation) including advice from Senior Counsel, is that tie's general argument on many of these matters is to be preferred to BSCs.

all

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SEE EARLIER POINT

3.54.2 tie accepts that construction works have been impacted by a delay to the completion of some utility works and has already offered (as part of addressing impact of other client changes and compensation events) a reasonable extension of time and associated costs to BSC. The link between utility delays and other causes of delay in the construction works is complicated, though capable of resolution with the involvement of qualified parties engaged by tie.

3-74.3 However, the issue which is having the biggest impact on progress and the programme budget is the adoption by BSC of an approach of not progressing works where there is a change, or an alleged change, to the contracted scope of works until the financial entitlements from change are definitively resolved. This is not consistent with the ~~conventional~~ terms of the Agreement which requires progress to be made on such matters while work is undertaken to assess the impact (if any) on programme and costs. Such mechanisms are normal in construction contracts to avoid delay to progress, ~~where a contractor adopts the approach adopted by BSC. BSC offer the excuse that their efforts are hampered by delays by third parties giving approval to design. Such delays are a compensation event unless caused by themselves. BSC.~~

*continue to issue*

3-84.4 tie has ~~issued~~ ~~are issuing~~ a series of formal instructions to proceed with works within the terms of the Agreement, but BSC has not complied with these, asserting that the instructions are not valid. In anticipation and for the purposes of legal proceedings, tie has taken Senior Counsel's opinion on this matter which has confirmed tie's interpretation. It is also noteworthy that many of the specific claims BSC assert require a competent estimate of the financial, programme and performance effects of the matter to be prepared by BSC, which in many cases has not been provided or has been delayed by very long periods, in some cases many months.

SAME POINT AS ABOVE

3-94.5 The disputes surrounding design-related changes, causes of programme delay and BSC's unwillingness to act on formal instructions from its client are the core reasons for lack of progress and increasing cost. tie and the Council have a duty to secure best value for public money and it would be entirely inappropriate for tie to accept unsupported or inaccurate claims for additional money made by BSC. BSC refuse in some cases to comply with instructions which do not place the in breach of Contract Terms or prejudice their position - such obstinacy is contrary to the underlying agreement to work in a cooperative manner.

3-404.6 Whilst there have been disputes on design-related matters, as summarised above, it is ~~normal~~ not unusual in any large public works construction project for the scope of the project to change in marginal ways for a variety of technical and commercial reasons.

3-444.7 To ensure there is a robust validation of such changes, a formal change management process is set out within the Agreement. The justification for the formal treatment of such changes under the terms of the Agreement is carefully evaluated to ensure that public funds are protected and to enable examination of any options which would mitigate their cost implications. A large percentage of the changes proposed by BSC remain unresolved, mainly due to a lack of timeous, evidence-based technical justification. Should refer to best value - whole life cost being a passed on duty

3-424.8 To date there have been fifteen issues launched into DRP, eleven by tie and four by BSC. Once an issue is in the DRP process the argument put forward by BSC in 3.7 above is definitely removed.

repeats 4-1

3-434.9 Of the fifteen DRP issues, three were resolved by negotiation, three were resolved through external mediation, seven have been referred for



external adjudication of which six have been concluded and two matters are at an early stage of the process. The sum saved by tie through application of the DRP process to date represents cXX% of the final sum agreed as payable to BSC. ~~Taking into account matters which have been resolved under the DRP process and also changes put forward by BSC which were concluded outwith the DRP process, the sum saved by tie's negotiation of the claims submitted represents over XX% of the sum finally agreed.~~ It should be noted that the DRP outcomes in terms of legal principles is finely balanced and still subject to debate between the parties.

3-144 10 tie has been successful in achieving part of its objective it aimed to achieve by setting DRP processes in motion: getting work started at some locations and significantly driving down the final value of claims submitted by BSC. This has generally been a success. However, the DRP process has not yet achieved the momentum that the project needs to ensure its completion within an acceptable extended programme.

#### Approach adopted by tie to achieve resolution

3-154 11 The development of the dispute with BSC has been regularly reported to the Council, including reports prepared for the April, August and December 2009 Council meetings. ~~(REFER TO PREVIOUS REPORTS RELEVANT TO THE DISPUTE).~~ In brief, following BSC's refusal to fulfil their contractual obligations in relation to works on Princes Street in early 2009, an alternative approach was agreed recognising the critical nature of the specific city centre work to the well-being of retailers and the travelling public. However, the period since early 2009 has been characterised by continued intransigence by BSC over performance of their contractual obligations. As a result, in the Summer of 2009, tie began to apply the DRP process with the results described above.

Comment [MSOffice2]: ACNS to provide

3-164 12 Towards the end of 2009, it became clear to tie and Council Officers that little real progress was being achieved in persuading BSC to progress the civil engineering and infrastructure installation works (for which Bilfinger Berger were responsible as BSC consortium member) according to the contractual programme. tie has therefore had to adopt a considerably more robust approach to enforcing its contractual rights.

3-174 13 To supplement tie's project team and principal advisers, tie has deployed additional expert resource in the areas of contract and dispute management, technical, commercial, forensic planning/delay analysis and litigation expertise. This has been done to enable a robust commercial approach to be taken with BSC and one which also sets the foundation, in due course, for a more formal entitlements enforcement process to be pursued through the courts, should that prove necessary. The cost of this additional resource has been covered many times over by the savings achieved through negotiation and the DRP.

3-184 14 The approach taken has included audits of BSC's performance in key areas such as design management and integration, programme management (including compliance with duty to mitigate delays) and sub-contractor arrangements. The evidence gathered from these audits has reinforced tie's

concerns about the reasons for the commercial dispute with BSC and poses serious questions about BSC's proper discharge of its obligations.

Comment (NS3): DLAP to confirm ok and not defamatory

### Options Review

- | 3-194.15 In December 2009, the Tram Project Board (TPB) concurred with tie's proposal that, in view of the lack of progress, a fundamental review should be conducted of the contractual position with BSC and that, if required, formal legal processes should be started to bring the major issues to a head and to enable the project to progress.
- | 3-204.16 The analysis gathered from this work has enabled tie to evaluate a number of strategic options. A variety of options and sub-options has been examined and the preferred strategy was reported to the TPB on 10 March 2010.
- | 3-244.17 Before setting out the approach approved, it is instructive to record a number of matters which are relevant to the actions now underway. Throughout the period of the dispute, progress on construction has been severely hampered by BSC's refusal to execute the works according to their contractual responsibilities, in an apparent attempt to coerce tie into agreeing to change the form of contract to a 'cost plus' arrangement. This has most recently been demonstrated by joint work to examine how to remove dispute over on street works, culminating in BSC's proposal to fundamentally alter the balance of risk in the Agreement by seeking 'cost-plus' arrangements for the balance of the 'on-street' works across the city. Such an approach would not achieve best value and would also potentially put tie in breach of EU procurement law if applied across the whole scope of the works. Accordingly this proposal has been rejected.
- | 3-224.18 Over the last year, tie has tried a number of approaches to overcome the difficulties in the relationship with BSC. These have included making a specific change in relation to the work on Princes Street (due to the importance of the thoroughfare to the commercial interests of Edinburgh's city centre retail businesses and the city's tourism economy and Festivals); attempting to resolve impasses through external mediation; meetings with different levels of senior management within BSC; and offering an extension of time for completion of the works programme despite the absence of a properly justified submission from BSC. Unfortunately, BSC remains wedded to the concept that tie must agree to the value of all changes before the relevant work begins, thereby all but paralysing the sequential works programme.
- | 3-234.19 Against the backdrop of lack of progress and unwillingness on the part of BSC to adhere to its contractual responsibilities, tie has had to invest considerable time and public money to instruct external legal advice as well as commercial advice from independent experts. This advice has confirmed the validity of tie's contractual interpretation on a number of key issues. The advice reinforces tie's position, acknowledging that there will always be an inherent level of risk in seeking a determination through the courts. The process ~~we~~ have embarked on is helping to define how BSC's delinquency may amount to a material and repudiatory breach of contract. Being obstinate in itself may

Tie  
7  
RECOMMEND  
THAT THIS  
TAKEN OUT IT  
REVEALS Tie's  
HAND.

cumulative

not be enough for tie to rely on – but not producing a design for trackwork which would permit the ETN to operate would be.

3-244.20 The assessment of options by the TPB concluded that it was untenable to continue to seek a change in BSC's behaviour through informal commercial negotiation and that the investment of time and money in the reinforcement of tie's contractual position was a necessary next step.

3-254.21 Current dialogue with BSC is focussed on revision to the programme, the sequencing of work and the parties' responsibilities in a manner which will mitigate the range of disputed matters while maintaining a best value outcome. Although some degree of momentum has been achieved in recent weeks, the outcome remains very uncertain. This approach is currently believed to represent the first of two possible outcomes. An approach which doesn't de facto wipe the slate clean for Infraco without a price being paid.

3-264.22 The second possible outcome is termination of the BSC Agreement. The options review addressed how the Agreement might be terminated and the consequences of such a termination. There is a contractually defined process in place to do this. BSC's failure to adhere to its contractual obligations, notably its direct failure to respond to instructions, supports the grounds for termination, should tie and the Council conclude that such an approach would be the best means of protecting public money. It is hoped that this outcome can be avoided but the grounds for such an approach have been extensively examined by tie and its advisors and preparatory work for litigation, should that prove to be necessary, is underway.

3-27.

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3-284.23 Amid the difficulties on the principal civil engineering works being carried out under management of Bilfinger Berger, it is important to recognise that the work carried out under the contract by the other Consortium partners, Siemens and CAF, has generally been conducted in a robust but constructive manner. The most tangible evidence of this is the recent successful testing on Siemens' facility in Germany of the first tram vehicle manufactured by CAF and the appearance of the tram vehicle in Princes Street. All 27 trams ordered have now been completed or are in the process of being constructed. While the Agreement rests between tie and BSC, not the individual members of the Consortium, it is unfortunate that Bilfinger Berger have not adopted the approach adopted by their Consortium partners. We may just reflect on what role Siemens may have played or not have played – the Consortium are working very much at arm's length with each other – it is evident that the Infrac Representative is employed by BB first and foremost and it could be said doesn't fulfil the role envisaged by Clause 26.4.2

3-284.24 Throughout the period of the dispute, the governance model established for the project has been operated rigorously. The levels of authority delegated to the parties with responsibilities for governance is fully documented and has been adhered to; the Tram Project Board, a formal committee of the TEL Board, has also met regularly to receive reports on progress and on the matters in dispute and their impact on the project. Despite many matters being

Summary:  
The Consortium has never been a properly conjunct contracting partner for tie. Leading to numerous difficulties in administering the contract & not establishing true responsibilities.

commercially sensitive, there has been regular reporting from tie through the governance structure to Council officers and regular reports to Group Leaders.

**3.304.25** In addition to communications between tie and Council officers through the project governance structure, other key stakeholders have been kept fully informed. There has been regular dialogue between tie, Council officers and senior representatives of Transport Scotland. Inquiries about the project from members of the public, MSPs, the media and other interested parties have been responded to as fully as possible, always subject to the need for confidentiality in order to protect public funds and to respect the terms of the Agreement.

**3.314.26** In summary, the current position remains highly unsatisfactory despite extensive and constructive attempts by tie to achieve reliable execution of the obligations in the Agreement. tie has been required to adopt increasingly forceful tactics in relation to its rights and obligations under the Agreement and in the face of BSC's unwillingness to adhere to its obligations. Negotiations on the key matters continue and it is to be hoped that an acceptable outcome can be achieved. In the event that this cannot be achieved, tie is taking the steps necessary to prepare for termination of the Agreement.

#### Utilities

**3.324.27** One of the most visible aspects of the project and one which has had most impact on Edinburgh's travelling public has been the diversion of extensive utility works along the route. The multi-utility framework strategy was a unique and innovative approach to the challenge of costly and disruptive diversion work and this diversion work is now substantially complete with only minor cabling works and commissioning of new assets currently being finished in the city centre.

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**3.334.28** As reported to the Tram Sub-Committee on 22 March 2010 the majority of the utilities diversion work was originally undertaken by Alfred McAlpine Infrastructure Services (AMIS) under the Multi-Utilities Diversion Framework Agreement (MUDFA). Work commenced under this contract in July 2007.

**3.344.29** Subsequently AMIS was subject to takeover by Carillion plc who progressed the MUDFA until the end of November 2009.

**3.354.30** The remaining utilities works are being undertaken by two separate contractors, Clancy Docwra and Farrans.

**3.364.31** The works undertaken represent significant betterment to the infrastructure in Edinburgh as many of the cables and pipes were in need of replacement which would have resulted in ongoing disruption to the city traffic over a number of years. This investment will be of long term benefit to the city and there will be a reduced requirement for maintenance and replacement of this infrastructure in the future.

**3.374.32** The original scope of works covered 27,000m of cabling, this had to be significantly expanded once physical conditions underground became clear. The complexity of utilities along the tram route, congestion of pipes and cables in key locations and unforeseen obstructions has proven to be much more

problematic than originally anticipated. In addition the records held by Scottish Utilities Companies and the Council were not comprehensive. The final scope of diverted utilities is estimated at c50,000m. Currently 48,000m of the expected volume has been completed.

3.384.33 The estimated cost for this part of the project has increased by approximately 25% to take account of the additional project scope and time. Of this increase 15% was anticipated and provided for in the original risk allowance. The net costs of utilities have been calculated after deducting a substantial credit from the Statutory Utilities Companies for betterment of their assets.

3.394.34 In summary, the MUDFA utilities works have required a net 10% increase in budget which is considered reasonable given the significant increase in volume of works encountered and the benefit of the enduring enhancement to the city's utility infrastructure along key traffic corridors.

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3.404.35 The agreement of the final account with Carillion is subject to determination of additional amounts relating to claims by the contractor for alleged delay and disruption to the works they carried out. These claims will be subject to discussion with the Tram Monitoring Officer, in accordance with the Operating Agreement, before any settlement is made.

#### Budget, Scope and Programme

3.414.36 The original project budget at contract award was £512m for the full scope of Phase 1a (plus an additional £3.2m should Phase 1b not be progressed) with an Open for Revenue Service (OFRS) date of July 2011.

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3.424.37 The report to Council on 20 August 2009 highlighted that delivery of Phase 1a within the funding envelope of £545m would be very difficult to achieve and that the Council would undertake contingency planning in the event that the estimated capital cost of the project exceeded the available funding envelope.

3.434.38 It is now anticipated the full scope of Phase 1a cannot be delivered for the approved funding of £545m. It is thought that, given the problems with BSC it is prudent to plan for a contingency of 10% above the approved funding of £545m due to lack of clarity on programme and cost. However, TEL is not seeking approval for an increased budget at this time.

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3.444.39 Spend to date on the project, to the end of Financial Year 2009/10, is £347.8m. It should be noted that a construction project of this nature requires a significant amount of upfront costs, including land acquisition, design, procurement and legal costs. The contract with BSC accounts for £240m of the original budget of £512m and of this amount £135m relates to the civil engineering costs (substantially contracted to Bilfinger Berger) of the project. The table below shows each individual element of spend to date.

	Financial Close Budget	Current Spend £m

	£m	
Infrastructure	250.5	117.1
Vehicles	58.2	42.2
Utilities	48.4	62.4
Design	26.9	31.2
Resources	68.3	63.4
Other (Including Land Acquisition Costs)	32.6	31.5
Risk + Phase 1b postponement and design costs (included in Current Spend in right hand column)	30.3	
	<b>515.2</b>	<b>347.8</b>

3.454.40 The original risk allowance within the budget of £515.2m has now been allocated to the individual budget headings.

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3.464.41 Of the expenditure to date, it should be noted that the components relating to Design and Utilities are almost complete. Therefore, exposure to additional costs in these areas is not significant.

3.474.42 The final anticipated cost related to Vehicles is £58m. With the exception of minor internal design changes related expenditure, this area of the project is on budget and ahead of schedule.

3.484.43 Other costs primarily relate to land acquisition costs. These costs were accrued earlier in the project and therefore the remaining cost exposure in this area is minimal although there are some residual risks related to future claims.

3.494.44 Resource costs for the project are currently running higher than previously envisaged. The primary driver for the additional cost is the commercial and legal resource that has been required due to the ongoing disputes with BSC and a prospectively longer construction programme. There has also been an increase in costs related to Traffic Management arrangements and embargoes.

3.504.45 Therefore, the remaining uncertainty primarily surrounds the infrastructure costs and the current dispute with BSC.

4.46 One of the reasons for the increase in infrastructure costs has been the cost incurred for the Princes Street works on Princes Street which have now been substantially completed. Given the unique nature of Princes Street and the commercial impact on key city stakeholders, a customised approach to the completion of construction activity on Princes Street was required. An arrangement was reached whereby additional work, including the costs of programme acceleration, would be reimbursed on the basis of demonstrable costs by BSC.

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4.47 The final account for this section has now been substantially completed and shows a significant increase compared to the original sum of circa £2m included within the Infraco contract. Negotiations continue with BSC over a potential £11m of costs, but tie have already certified £8m of these. It should be noted that certain of these costs would have been additional to the original contract in any event (eg improvements to the track base, full-depth road reconstruction, use of setts on Princes Street and utility conflicts).

4.48 Some of these potential additional costs can be justified given the unique nature of Princes Street and the achievement of a tight programme schedule in a critical area in the city. Nevertheless, it is clear that the experience with this arrangement to date demonstrates that this approach cannot be extended to all on-street works.

~~3.51~~

~~3.52 In February 2000, BSC refused to commence the construction works as planned on Princes Street, despite the access and extensive traffic diversions arranged by tie and the Council.~~

~~3.53 Completion of the key works along Princes Street was especially critical. The Council and tie were very sensitive to both the unique nature of Princes Street and the needs of key stakeholders and commercial interests in the city centre. In addition it was vital that the 2000 Edinburgh Festival and the vitally important pre-Christmas and New Year shopping period could proceed with minimum disruption.~~

~~3.54 Accordingly, the potential for commercial harm to the city of major disruption during these periods required a customised approach to the completion of construction activity on Princes Street.~~

~~3.55 tie, therefore, agreed an arrangement whereby additional work, including the costs of programme acceleration, would be reimbursed on the basis of demonstrable costs by BSC.~~

~~3.56 The final account for this section has now been substantially completed and shows a significant increase compared to the original sum of circa £2m included within the Infraco contract. Negotiations with BSC continue to conclude the final account, although tie have now certified £8m of costs relating to Princes Street. However it should be noted significant commercial matters require to be resolved with BSC.~~

~~3.57 It should be noted that there are a number of elements within these costs which would have been incurred over and above the original contractually agreed price in any event. These items include improvements to the track base, full-depth road reconstruction (which was not included in the original contract price), the use of setts in response to Princes Street's status as part of a world heritage site and additional work associated with utility conflicts.~~

~~3.58 These items total £3m and it should further be noted that there will be a substantial increase in the value of the Council's road asset due to full depth reconstruction which should reduce the need for further carriageway works on Princes Street in the future years.~~

~~3.59 In addition, costs of £2m were incurred relating to delay, disruption and subsequent acceleration to achieve the end of November 2009 embargo timescale.~~

~~3.60 The remaining premium cost of potentially £6m remains the subject of discussion with BSC. Some of these additional costs can be justified given the unique nature of Princes Street and the achievement of a tight programme schedule in a critical area in the city.~~

~~3.61 Nevertheless, it is clear that the experience with this arrangement to date demonstrates that this approach cannot be extended to all on-street works.~~

### Council Funding Strategy, Contingency Planning and Incremental Delivery

3.624.49 The Council's funding strategy for its commitment of £45m was derived from a variety of sources, including capital receipts of land assets along the route of the tram line, developers' contributions and contributions from the Council's Capital Investment Programme. The original breakdown of the Council's funding and the contributions made to date is shown in the table below.

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CEC Contribution Breakdown	Planned Contribution	Achieved Contribution
Council Cash	£2.5m	£2.5m
Council Land	£6.2m	£6.2m
Developer Contributions – Cash	£25.4m	£4.5m
Developer Contributions – Land	£1.2m	£1.2m
Capital Receipts (Development Gains)	£2.8m	£0.0m
Capital Receipts	£6.9m	£2.0m
<b>Total</b>	<b>£45.0m</b>	<b>£16.4m</b>

3.634.50 When this strategy was originally devised, it was assumed that capital receipts and developers' contributions would be accrued over a time horizon of twenty years; therefore it was never assumed these funds would be in place during the construction phase of the tram project.

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3.644.51 There is no doubt that the rate of funding from developer led sources has been affected by the economic downturn. However, evidence in recent months indicates that would suggest that the rate of contributions are still being generated has increased. £1m of the total developers contributions achieved of £4.5m, has been received since November 2009.

3.654.52 However, there remains a risk that the full level of contributions may not be achieved. The Council will continue to monitor the levels and progress of



the developers' contributions and assess these within the wider contingency planning being carried out on the project.

- | ~~3.664.53~~ As detailed earlier in the report, it is now envisaged the full scope of Phase 1a cannot be delivered within the approved funding envelope and within the originally envisaged timescales.
- | ~~3.674.54~~ Whilst TEL is not seeking approval for an increased budget or formal change to the baseline programme date at this point in time, in terms of the Operating Agreements it is appropriate that Council is made aware of the current position. Any changes to cost, programme or scope which emerge from future negotiations with BSC will be formalised as a request for approval from the Council prior to any commitment.
- | ~~3.684.55~~ In terms of balancing demands, the factors of scope, project cost and date of delivery need to be considered together. This work is ongoing as the Tram Project Board considers how best to balance the varying demands of the programme.
- | ~~3.694.56~~ It should be noted that whilst there remains significant commercial uncertainty, it is not possible to provide a robust estimate for the full cost of phase 1a. However, based on the strategic options work which the has undertaken and as a result of all the other factors included in this report, it is now considered prudent for the Council to plan for a further 10% over the available funding of £545m, on the understanding that further potential risks have been identified beyond this level.
- | ~~3.704.57~~ Contingency plans up to a funding level of 10% above the approved project funding have therefore been examined. The contingency planning undertaken has primarily identified two potential sources of funding to allow the Council to borrow under the Prudential Framework.
- | ~~3.714.58~~ The Council has made allowance within the Council's Long Term Financial Plan of £2m per annum to cover infrastructure development costs. This provision would allow the Council to borrow £24m under the Prudential Framework; this would represent an opportunity cost for the Council but would have no impact on specific projects already in the capital programme. Headroom within the existing budget for loan charges may also allow future investment in infrastructure beyond this sum.
- | ~~3.724.59~~ Further borrowing, should it be necessary, can be financed from the future profits of Transport Edinburgh Limited (TEL). Based on the full scope of Phase 1a TEL's forecast cumulative net profit from 2013 – 2031 would allow the Council to prudently borrow additional funding up to the level of circa £600m.
- | ~~3.734.60~~ The Council's contingency planning is dependant on its ability to use the prudential borrowing framework. However, a risk has emerged recently around potential restrictions on the use of the prudential framework given the current economic difficulties at UK level. If this risk crystallised the Council would have to investigate alternative funding arrangements. Further contingency planning will be undertaken in this regard.

3.744.61 Following recent meetings of the Tram Project Board, tie has been instructed to review the options for incremental delivery for Phase 1a as a further contingency plan. This review requires the input of colleagues at Lothian Buses to ensure the extent of Tram services delivered at any point in time can be integrated with appropriately adjusted bus services. This review will be undertaken as the outcome of current negotiations with BSC becomes clearer.

3.754.62 The incremental delivery options review will address the imperative to manage the affordability risks of the project (in the context of the current commercial disputes with BSC) by means of flexible incremental delivery of the on street sections over a longer period of time and in a way which provides the Council greater control over the precise timing of the remaining on-street works. The approach will ensure the investment already made in the in the project is realised by the delivery of a viable tram service, integrated with bus services, whilst preserving for delivery the entirety of the scope of Phase 1a as detailed in the Final Business Case. The stages of Phase 1a service delivery under examination are;

- Airport – Haymarket (core off-street street works under construction)
- Airport - York Place (connects the Airport to the City Centre)
- Airport - Foot of the Walk (achieves integration with bus services on Leith Walk and interchange at FOW)
- Airport – Ocean Terminal (serves the core of the Leith Docks development)
- Airport – Newhaven (Full Scope of Phase 1a)

3.764.63 The capital costs of each of the options will allow future decisions to be taken within the overall context of the affordability of funding. The full assessment of these options and the overall funding strategy can only meaningfully be performed once there is clarity on the dispute with BSC.

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#### 45 Financial Implications

4.45.1 It is now considered that the full scope of Phase 1a cannot be delivered within the approved funding envelope of £545m.

4.25.2 The contingency planning work that ~~has been~~ is being undertaken has ~~identified~~ to identify funding options which could facilitate project costs up to £600m.

4.35.3 There are further risks that could impact on the costs of the project. As part of the work tie have undertaken on strategic options, potential incremental delivery of construction, based on affordability assessments may need to be considered in the future.

#### 56 Environmental Impact

5.45.1 The Edinburgh Tram Project will make a positive contribution towards the vehicular emissions and air quality in the city centre and the transport corridor

to the west of the city and the airport. This will have a positive impact on current pollution levels and provide a quieter mode of public transport.

**67** Conclusions

~~6-17.1~~

**78** Recommendations

~~7-18.1~~

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Director's Name  
Director of (Dept title but not using "Department")

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Appendices        1

Contact/tel/Email

Wards affected

Single Outcome  
Agreement

Background  
Papers

Nick Smith

NS1.3

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**From:** Dave Anderson  
**Sent:** 15 June 2010 16:36  
**To:** Nick Smith; Alan Coyle; Donald McGougan; Gordon Mackenzie; Jenny Dawe; Alastair Maclean; Richard Jeffrey; David Mackay  
**Subject:** Tram report  
**Attachments:** Council Report 24 June 2010 v1.20.doc

Colleagues I have given the report a pretty thorough editing, in advance of Thursday's Council report deadline. If there are any further comments I would be grateful to receive these by close of business tomorrow. ( Password edinburgh.) Best regards. Dave

Dave Anderson | Director of City Development | The City of Edinburgh Council | G1 Waverley Court | 4 East Market Street | Edinburgh EH8 8BG | [REDACTED] | [dave.anderson@edinburgh.gov.uk](mailto:dave.anderson@edinburgh.gov.uk)

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**From:** Nick Smith  
**Sent:** 27 August 2010 17:02  
**To:** 'Richard Jeffrey'  
**Cc:** Alastair Maclean; Marshall Poulton; Dave Anderson; Donald McGougan; Alan Coyle; Ailie Wilson; Andy Conway; Carol Campbell  
**Subject:** Meeting followup  
**Attachments:** Tram Matrix v1 270810.doc

Richard

Further to the meeting yesterday I thought I would set out my views on what CEC currently requires to inform the on-going decision making process. Please note that it is sent subject to Dave and Donald's comments as neither have had a chance to review these points as yet. However, some of the requests are simply a reiteration of Donald's email to you on 18 August .

1. A legal view on the use of 80.20. I understand that tie is of the view that this has been looked at before and it is a no-go option. If this is the case then it appears from a practical perspective Infraco can hold tie to ransom as effectively there is no way to get them to progress works unless (i) an estimate is agreed (80.13); or (ii) the matter is in DRP (80.15). We would still like to see the analysis of the effect of 80.20 to finally close it out as an option. The issue of the effectiveness of clauses 34.1/34.3 also needs to be bottomed out. I appreciate that the TPB's view is that "as is" is not an option, but I think we still need to explore this avenue to inform the other options and perhaps even weaken Infraco's negotiating position.
2. My current thinking is that there are broadly four outcomes (i) continue with the existing contract; (ii) terminate and win ; (iii) terminate and lose; and (iv) Carlisle. A decision as to what to do after termination (ie continue, postpone or cancel) will require to be taken at the appropriate stage but we will know which is the viable option here before a final view is taken on termination.
3. Can tie please provide estimates of (i) the worst case cost scenario for terminate and lose under the Infraco contract assuming tie *lost* all the DRP/disputed issues (eg BDDI); (ii) the worst case cost scenario for terminate and lose under the Infraco contract assuming tie *won* all the DRP/disputed issues (eg BDDI); (iii) separately, a total of all other non-Infraco contract costs (so that when added to (i) or (ii) it would give a total cost estimate for termination); (iv) the estimated cost of a re-procure for the remaining works from Airport to St Andrew Square and separately from St Andrew Square to Newhaven; (v) the estimated total cost of termination for Infraco default with Infraco paying for the differential in completion costs (interestingly this would presumably include Airport to Newhaven for the final settled cost of the current contract rather than just to St Andrew Sq); and (vi) the proposed cost of Carlisle.
4. I appreciate (v) is very difficult as it depends on the total cost (which we don't know yet) and on whether you assume tie win or lose the contract interpretation questions - ie if tie lose the arguments re BDDI etc then tie is due to pay more and consequently the difference between the cost of Infraco doing the work and a third party doing the work is less.
5. A legal view is required on whether termination notices should be served piecemeal or all at once (the difference here being timescale for termination). I suspect this may be more of a tactical issue than a legal one but we should get a view so a decision can be taken.
6. Richard Keen's view on the case for Infraco default based on the evidence tie has amassed when set against the contract terms. ie what does he think are the chances of success? Fully appreciate this is reliant upon receipt of info from Infraco in response to the notices.

Stewart has previously provided figures for some variation of 3(iii) above. The latest was on 10 June at £415m, but this was for a termination and cancellation and also included a lot of cost which would not be required under a re-procure and continue option and also factored in £40m for litigation risk. I'm also not sure whether this included the sums paid to Infraco or whether this would reduce further due to actual value of work

done. However, on a quick analysis, at a rough base figure of £350m, could we not simply add the estimated cost of a re-procure (for either part or whole route) and arrive at a total estimated project cost? From memory the whole infraco part of the contract was £243m so adding those together would give you £593 for the whole scope. A re-procure would hopefully cost less in this market. This would also be a worst case scenario as our position would always be that Infracore are in default. I am probably massively oversimplifying here.

Identifying the worst case scenarios cost wise will allow us to eliminate the litigation risk issue as it can only ever then be an upside for the project costs. The difficulty of course comes when weighing up both cost and other influencing factors such as PR, political view, funding options and risk profile generally, but in my view the above information would at least allow us to narrow the options.

I am currently working on some form of matrix setting out the estimated costs and headline issues so that we can hopefully give tie an early steer to tie as to which options are still in the running and thereby allow tie to focus its resource most effectively as requested. I'll send this over once it is more developed. However, skeleton attached for info.

I also appreciate that the result of the strength of the legal position may not be known by October Council as we may not have the responses to the breach notices. However, a view on the estimates/issues for Carlisle versus a best and worst case for termination would at least inform the current thinking.

In addition, I appreciate that for certain of the estimates CEC will necessarily have to trust tie's judgement on the issues - eg tie will have to take a view on how best to re-procure and that methodology will likely affect the cost estimate. So long as we understand the working assumptions we can discuss them at that point.

Hopefully the above is clear but please let me know if not. Happy to discuss.

Kind regards

Nick

Nick Smith  
Principal Solicitor  
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City of Edinburgh Council  
Level 3, Waverley Court  
East Market Street  
Edinburgh EH8 8BG

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*Please note that I am not in the office on a Monday*

**Nick Smith**

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**From:** Nick Smith  
**Sent:** 06 October 2010 14:43  
**To:** Alan Coyle  
**Cc:** Alastair Maclean; Carol Campbell  
**Subject:** Tram report  
**Attachments:** Tram Update Report 14 October v1 6.doc

Alan

Further draft attached after Alastair's review. It's saved as 1.6 in the drive. He is rightly concerned that disclosing certain of the info could potentially breach the wide confidentiality provisions under the contract. Donald was ok with this approach.

Donald has asked that a further draft not be circulated until further comments have been incorporated. There is a meeting of bosses tomorrow at 11.30 to discuss.

Kind regards

Nick

Nick Smith  
Principal Solicitor - Commercial, Procurement & Finance  
Legal Services Division  
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Level 3, Waverley Court  
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*Please note that I am not in the office on a Monday*

## Edinburgh Tram Update Report (Draft v1.65)

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City of Edinburgh Council

14th October 2010

### 1 Purpose of report

- 1.1 The purpose of this report is to update the Council on the recent contractual negotiations on the Edinburgh Tram Project.
- 1.2 The report also addresses the motion from 24<sup>th</sup> June 2010 Council which requested a separate report outlining a refreshed Business Case detailing the capital and revenue implications of all the options currently being investigated by tie and taking into account assumptions contained within the original plan (eg anticipated development) that either no longer apply or where the timescales were now substantially changed.

### 2 Summary

- 2.1 In the period since the last report to Full Council on the 24<sup>th</sup> June, tie have continued to seek a resolution to the contractual dispute with the Bilfinger, Siemens, CAF consortium (BSC), including examination of incremental delivery options for the construction of the project. This report provides an update on these negotiations.
- 2.2 In addition to the work to resolve the contractual dispute, a significant amount of work has been undertaken to refresh the Business Case. This refresh includes the impact of incremental delivery, an update on the economic case for tram and deals with funding and affordability issues.

### 3 Main report

#### Tram Business Case Refresh

- 3.1 The refresh of the Business Case was requested by motion of Full Council on 24<sup>th</sup> June 2010. Its purpose is to refresh the assumptions made in the Final Business Case (FBC) for Phase 1a of the Edinburgh Tram Project, as approved by the Council in October 2007.
- 3.2 The Council's request is set against a backdrop of commercial disputes with the infrastructure contractor, which have resulted in significant programme slippage and increasing project costs. In addition, the difficulties with the contractor have come at a time of economic recession.



- 3.3 The outputs of the refresh of the Business Case result from a significant amount of work which has been carried out to reassess the assumptions underlying the FBC put together with the recent commercial experience of Lothian Buses.
- 3.4 The Council's Planning function has had input to the development assumptions that underpin the economic case for tram. Furthermore, the Council's Finance function has had visibility of, and input to, a number of the key work streams.
- 3.5 In addition to the key input of the, Lothian Buses have been closely involved in the input and assumptions made to the refresh of the TEL Business Plan. There has also been considerable work on the refresh from Steer Davies Gleeve and Colin Buchanans, providing independent key consultancy input to model the revised patronage assumptions.
- 3.6 The refresh of the Business Case has primarily focused on the consideration and assessment of incremental delivery; updating the economic case for Phase 1a; updating of the TEL Business Plan (taking into account the revenue impacts of incremental delivery); investment to date; and funding and affordability.

#### **Consideration and Assessment of Incremental Delivery**

- 3.7 Due to the cost and programme difficulties experienced on Phase 1a there has been a requirement to consider completion of Phase 1a in incremental stages. The main focus of incremental delivery has been on delivering Airport to St Andrew Square as the first phase.
- 3.8 Delivery of the project on a phased basis addresses the imperative to manage the affordability risks of the project by examining flexible incremental delivery of the on-street sections. This approach aims to ensure the investment in the project is realised by the delivery of a viable tram service integrated with bus services whilst preserving the entire scope of Phase 1a, as detailed in the FBC.
- 3.9 Incremental delivery allows the whole of Phase 1a to be delivered in stages and over a flexible timescale under the Council's control. The Council can then ensure that the infrastructure being delivered at any point in time is matched with available funding.
- 3.10 A first incremental opening of tram services from Airport to St Andrew Square yields near-term benefits and provides a fixed transport link between the city and Airport. It also provides a rail link to other areas of Scotland as a result of the interface with the Edinburgh Gateway Project. A tram operating from the Airport to St Andrew Square also secures a high proportion of the economic benefits anticipated in the FBC and is capable of being integrated with Lothian Buses successfully.
- 3.11 One of the key considerations under the incremental delivery option is to evaluate whether the potential first phase of construction to St Andrew Square is capable of delivering a positive contribution to the TEL business.
- 3.12 The evaluation of incremental delivery has shown that the TEL business as a whole is stronger in the medium to long term with tram added to the existing

bus business even if the tram is only operated between the Airport and St. Andrew Square. The key outputs from the TEL Business Plan are highlighted later in this report.

#### **Updating the Economic Case for Phase 1a**

- 3.13 An update of the economic case for tram has addressed both the full scope of Phase 1a and incremental delivery.
- 3.14 The economic case for tram refreshes the patronage sources and growth drivers in the city, taking into account a review of development profiles for Leith, the City Centre and West Edinburgh and assesses the impact of the development of the Airport and the broader regional drivers such as the Edinburgh Gateway project and the Edinburgh-Glasgow Improvement Plan. The update also looks at the longer term context of the Council's Transport 2030 vision and modal shift away from private car that is a key policy driver for the Council and Transport Scotland.
- 3.15 The need for tram has been examined against the wider context of Edinburgh's long term strategic position.
- 3.16 Edinburgh's population is currently expanding by around 1% per annum and is forecast to reach 514,000 by 2020 and 543,000 by 2030. As significant, the volume of commuters coming into the city to work from the surrounding city region and further afield was estimated at 85,000 per day at the 2001 census and is now around 100,000 per day and growing.
- 3.17 The city's growth has led to rapidly increasing demand for road use and increasing demand for public transport. Between 2000 and 2009, Lothian Buses patronage growth has been 18.9% in total, which equates to 2.1% per annum.
- 3.18 Tram is, in itself, considered to be a key stimulant to economic regeneration and new development. The extent of new development forecast is lower than was anticipated when the FBC was prepared in 2007 as a result of the economic downturn. With the key input of Council planning officers, an update of the likely timing of committed new development has been undertaken.
- 3.19 Whilst the actual residential development in the North of the city and in Leith completed at commencement of tram operations is projected to be significantly lower than was originally anticipated, the Council is forecasting a recovery such that by 2012 30% of the original forecast will be completed, 80% of the original forecast will be completed by 2020, and by 2031 the residential development in North Edinburgh will have recovered and the original development forecast will apply. The forecasts broadly anticipate a 4-5 year period of very slow development as a result the economic downturn, following which a return to growth will prevail.
- 3.20 It should be noted that the revised development profile only comprises committed developments or developments that have achieved outline planning consent.

- 3.21 It is clear that whilst the impact of the recession on the pace and size of development in the city has been significant, most notably at the Waterfront, it is important to consider the longer term view. The tram remains an important stimulant to development and regeneration in the West and North of Edinburgh.

#### **The TEL Business Plan**

- 3.22 The update of the TEL Business Plan is the key output that is derived from the updated economic case for tram. The key area under examination is the revised patronage and profitability forecasts for Phase 1a in total and the assessment of the impact of incremental delivery on TEL. In addition to the revised development assumptions, the updated forecasts for TEL are also built on the recent experience of Lothian Buses and further patronage modelling by external consultants, Steer Davis Gleave and Colin Buchannan. These forecasts have been profiled against incremental delivery to St Andrew Square to assess the impact on the TEL business.
- 3.23 As part of the preparation of this refresh, a review of the key assumptions and projections for the TEL Business Plan has been undertaken. This review has confirmed that the outputs from the previous work remain valid for the whole of Phase 1a. It has also confirmed that the operation of incremental delivery of Phase 1a from Airport to St. Andrew Square is sustainable and has a positive impact on the TEL forecasts in the medium to long term.
- 3.24 The approach to integration of the key local public transport modes, bus and tram, sets Edinburgh apart from other UK tram schemes. The integration of high quality bus and tram services will improve the attractiveness of the combined network to something greater than the sum of its constituent parts. The levels of demand projected by the transport modelling, undertaken by Steer Davies Gleave and Colin Buchanan, indicate a significant profit potential for TEL operating with the tram in the medium to long term..
- 3.25 Following a short initial period of tram patronage build up, partial opening of Airport to St. Andrew Square will be profitable and will experience significant growth in profits in the longer term.
- 3.26 In addition, significant work has been undertaken to assess the positive and negative sensitivities in the business plan assumptions in the early years of tram operation. This analysis will allow management action to be taken to ensure the profitability of the tram remains intact. The main sensitivities examined were in relation to patronage, electricity, fuel, labour and yield. It should be noted that another key sensitivity is in relation to the application of the Concessionary Fares Scheme. Discussions with Transport Scotland have indicated that the business planning assumption should continue to be that the Concessionary Scheme should apply to tram.

#### **Investment to Date**

- 3.27 A large infrastructure project such as the Tram Project requires a substantial amount of work to be undertaken in advance of construction works.

- 3.28 The budget for tram infrastructure represents 46% of the overall project budget with the most significant construction elements within this expenditure to date related to Gogar Depot, the structures along the off-street section of the railway corridor and tram works along Princes Street.
- 3.29 Significant progress has been made on the construction of the 27 tram vehicles. This element of the project represents 11% of the original project budget.
- 3.30 The diversion of utilities has resulted in a significant enhancement of the utility assets in the City including faster broadband services and enhanced water supplies.
- 3.31 As previously reported, the scope for the utilities diversions has gone from 27,000 linear metres to around 48,000 linear metres. This represents an increase of some 78%. There has also been an increase in cost relating to this scope increase of around 30%.
- 3.32 A further area of expenditure relates to the costs of the design and purchase of the land that is required for the project. This accounts for 12% of the project budget expenditure to date.
- 3.33 In summary, while there has clearly been significant delay to the infrastructure works, a vast amount of work and investment has gone into the tram project to date.

#### **Funding and Affordability**

- 3.34 Given the increasing project costs, it is critical to assess the current committed funding and affordability constraints of the project.
- 3.35 As set out in the Council report of 24<sup>th</sup> June 2010, contingency planning has been undertaken up to a level of 10% above the current funding and consideration given to incremental delivery options.
- 3.36 The Council has made an allowance of £2m per annum within its long-term Financial Plan to cover additional infrastructure development costs. This provision would allow the Council to borrow £24m under the Prudential Framework. Headroom within the existing budget for loan charges may also allow future investment in infrastructure beyond this sum if required.
- 3.37 Further borrowing, should it be necessary, can potentially be financed from the future profits of Transport Edinburgh Limited (TEL).
- 3.38 Of the current funding, the Council has committed £45m to the project, of which £25m is anticipated from developers' contributions. The slow down in development has impacted on the pace of developers' contributions expected to be received by the Council. However, over the 20 year period set out in the Tram Developers contribution guideline, it remains possible to achieve the £25m total.
- 3.39 The current impact on developers' contributions from incremental delivery is £7m if the route were to be curtailed at St Andrew Square. This means that if

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the full route of Phase 1a is not delivered then the Council would have to fund this additional £7m as part of their £45m commitment.

- 3.40 Whilst commitment remains to deliver the full scope of Phase 1a, affordability remains the primary consideration given the current level of funding and the forthcoming constraints on public sector spending.
- 3.41 The tram project has faced many challenges since the start of construction. This has resulted in increased costs and significant delay. This has required options to be considered for delivering Phase 1a incrementally.
- 3.42 While a tram operating from the Airport to St Andrew Square can deliver significant benefits, and importantly can be profitable, further benefits would accrue from the full scope of Phase 1a. Therefore, an important assessment will be required at the appropriate time to appraise the benefits gained from constructing the full route of Phase 1a versus the capital cost and available funding.

#### Current Position

- 3.43 In the report to Council on 24 June, Council was provided with an updated position on the dispute between tie and the BSC consortium.
- 3.44 Over the intervening months tie have been pursuing a twin track approach to try to break the impasse that exists with BSC.
- 3.45 It is important to acknowledge that there has been progress on-site whilst tie has been pursuing this twin track approach. Work on-site has been progressing in the West of the city, albeit at a slower rate than would be expected. This progress off-street is considerable and includes bridges, viaducts and the well progressed construction of the depot.
- 3.46 There have also been some recent developments in relation to BSC demobilising a certain element of their workforce claiming that they will not continue to work on certain parts of the project.
- 3.47 The twin track approach adopted has been;
- To seek to agree a revised scope, price and programme, with the outcome of a tram operating to at least St Andrew Square, with a very high degree of cost and programme certainty.
  - To continue to administer the project in a robust manner; including compiling evidence of any BSC's breaches of contract by BSC; clarifying contractual principles regarding contractual changes; and bringing the design to completion.
- 3.48 Despite intensive and detailed negotiations having taken place over the last few months, the parties have to date been unable to reach agreement which would achieve a revised scope, price and programme acceptable to both parties. Whilst negotiations have not been formally suspended, an acceptable commercial settlement now unfortunately appears unlikely in the short term.

~~3.49 To date tie has been exercising its various rights and remedies under the contract but, for legal reasons, the detail of that needs to remain confidential at this stage. However, the Council should be aware that all options are being considered.~~

~~3.49 To date 15 matters have been referred to the formal Dispute Resolution Process (DRP) under the contract. 9 of these have been resolved by adjudication (not all 15 as erroneously reported in the press), 4 by mutual agreement and 2 at mediation. Of the 9 decided at adjudication 7 involved financial matters, one was a claim for extension of time and one involved a principle of progressing the works under one specific sub-clause of the contract in particular circumstances.~~

~~3.50 The claim for extension of time was substantially rejected by the adjudicator. On the dispute over the use of the particular sub-clause to instruct progress the adjudicator preferred BSC's interpretation.~~

~~3.51 Of the 7 adjudications which involve issues of value, BSC's claims have been reduced (in aggregate) by approximately £5.2m to less than half of the original claims.~~

~~3.52 Of the 15 disputes (including the 9 adjudications) where issues of value have been involved, BSC claims have been reduced in aggregate by approximately £12.4m, again to less than half the amount originally claimed. Reports in the press that tie has 'lost 13 of the 15 adjudications' need to be viewed in light of the above facts.~~

~~3.53 To date tie has served nine remediable termination notices on the BSC consortium detailing various breaches of contract. Under the contract the Infrago has to respond to these notices within a specified timescale with proposals to remedy the alleged breaches. The consortium have responded to the first of these notices by predictably refuting the allegation of a breach but also providing outline rectification plans on a strictly without prejudice basis. Tie have reviewed and considered the remediation plans and have rejected the remediation plans put forward by the consortium.~~

~~3.543.50 Any decision to terminate the contract would clearly have significant consequences and therefore this option will be considered after taking into account extensive legal advice. These matters are already in hand and the legal issues are being considered, together with the commercial and other consequences. It is vital that proper sufficient time is allowed for due and proper legal process and that the outcome of that process is not pre-judged to protect the interests of tie and the Council.~~

~~3.553.51 In the meantime, tie will continue to enforce the terms of the existing contract.~~

~~3.563.52 Any recommendation from tie to terminate the contract will require to be presented as a formal request for approval from the Council Transport Scotland will also need to be informed of the position.~~

~~3.573.53 In the event approval for the termination of the contract is sought tie will also bring forward options for delivering the project in an alternative manner. It~~

is proposed that the above matters would form part of a further comprehensive report to be brought to the December Council meeting (or an earlier Special Meeting of the Council) outlining the recommended available options. This would consider all implications and proposals for the project going forward.

3.583.54 In the meantime, discussions will continue with the consortium to attempt to reach an agreed solution as outlined above.

#### **Governance of Bus and Tram Integration**

3.593.55 It has long been a policy aim of the City of Edinburgh Council to develop an integrated public transport network delivering high quality bus and tram services in the city. Over the last two years the Chief Executive has submitted a number of reports to Council on the steps necessary to bring this about.

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3.603.56 Work on the final phase of the agreed integration of the, TEL and Lothian Buses has been underway for some time. A number of complex and inter-related actions need to be taken to prepare the way for the revised governance arrangements that the advent of trams will require. As previously reported, a work programme embracing the following key issues is proceeding:

- legal and contractual matters;
- finance (including tax planning);
- employment; and
- communications and reporting.

It is anticipated that these work streams will be completed by the middle of 2011.

3.613.57 To direct and oversee the work programme on bus and tram integration it is essential that senior management arrangements, with clearly specified roles and responsibilities, are in place. Having completed the appropriate HR procedures, based on those used by the Council and involving a "matching process", the Board of TEL has agreed that Richard Jeffrey will take on the role of Chief Executive (Designate) and Ian Craig will take on the role of Chief Operating Officer (Designate). There will be no change meantime to existing remuneration arrangements or any additional contractual liabilities.

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3.623.58 These appointments are an essential foundation for the new arrangements. It gives Richard Jeffrey and Ian Craig the full authority, under the direction of the Boards of TEL and Lothian Buses, to lead the demanding work programme associated with public transport integration over the next nine months and beyond. It will be an early priority for the two senior postholders to establish a shared vision, values and brand for the future; establishing a common IT platform; devise and implement management and organisational structures and recruit/appoint to them; business planning; training and the like.

#### **4 Financial Implications**

- 4.1 As previously reported, the contingency planning work that has been undertaken by the Council and tie has identified funding options which could address project costs of up to £600m. Due to the current uncertainty it is not possible to provide an update at this time on the ultimate capital cost of the project.

#### **5 Environmental Impact**

- 5.1 The Edinburgh Tram Project will make a positive contribution towards the vehicular emissions and air quality in the city centre and the transport corridor to the West of the city and the airport. This will have a positive impact on current pollution levels and provide a quieter mode of public transport.

#### **6 Conclusions**

- 6.1 Following the recent refresh, the Business Case remains positive even with incremental delivery only to St Andrew Square.
- 6.2 Whilst negotiations have not been formally suspended, an acceptable commercial settlement now appears unlikely to be achieved in the short term.
- 6.3 Contract enforcement continues with the due legal process needing to be followed prior to an early report back to Council.

#### **7 Recommendations**

##### **7.1 The Council;**

- a) Note the disappointing lack of progress in relation to the negotiations and progress of physical works.
- b) Note that following the refresh of the Business Case, which included the update of the economic case for tram, the first phase of construction to deliver an operating tram to St Andrew Square delivers a profitable tram following the initial year of patronage build up.
- c) Endorse rigorous application of the contract by tie.
- d) Note that in the absence of robust remediation plans from the consortium and a change of behaviour in relation to progressing the works, serious consideration may need to be given to termination of the contract in the event that Infracore are considered to be in breach of contract. If the contract is terminated, Re-procurement and alternative delivery strategies will also require to be considered and executed.
- e) Note the recent Governance developments and future work streams.
- f) Note that a report will be prepared for the December Council or and earlier Special Meeting if required on the next steps.

Director's Name

9



Director of (Dept title but not using "Department")

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Appendices 1

Contact/te/Email

Wards affected

Single Outcome  
Agreement

Background  
Papers

**Nick Smith**

NS 1.6

**From:** Nick Smith  
**Sent:** 07 October 2010 14:49  
**To:** Steven Bell  
**Subject:** wording

**Importance:** High

Further to the figures reported to the Council in June, to date the application of DRP to disputed matters has reduced BSC's claims for additional payment from £[ ]m to £[ ]m (a saving of £[ ]m). tie remains satisfied that the overall balance of adjudication outcomes has more than justified its interrogation of the initial claims made by BSC.

Kind regards

Nick

Nick Smith  
Principal Solicitor - Commercial, Procurement & Finance  
Legal Services Division  
City of Edinburgh Council  
Level 3, Waverley Court  
East Market Street  
Edinburgh EH8 8BG

(t) [REDACTED]

*Please note that I am not in the office on a Monday*

NS1.7a

**Nick Smith**

---

**From:** Richard Jeffrey <Richard.Jeffrey@tie.ltd.uk>  
**Sent:** 07 October 2010 20:01  
**To:** Alan Coyle; Nick Smith  
**Cc:** Donald McGougan; david\_mackay [REDACTED]  
**Subject:** RE: Report  
**Attachments:** Tram Update Report 14 October v1 8 (RJ Comments).doc

Sorry to keep picking at this, but some minor comments added.

Numbers added by me in paras 2.26 to 2.32 need checking, if you agree inclusion, I will verify.

Well done Alan, great patience on this!

R

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**From:** Alan Coyle [mailto:Alan.Coyle@edinburgh.gov.uk]  
**Sent:** 07 October 2010 17:27  
**To:** Richard Jeffrey  
**Subject:** Report

Richard,

Hopefully this is the final version incorporating all the changes from earlier. Can I draw you to para 2.24 and the rework of the legals.

Regards

Alan Coyle | Financial Services | Corporate Finance Team (Edinburgh Trams) | Level 2/6 Waverley Court | 4 East Market St EH8 8BG  
| [alan.coyle@edinburgh.gov.uk](mailto:alan.coyle@edinburgh.gov.uk) |  
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.....

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## Edinburgh Tram Update Report

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City of Edinburgh Council

14th October 2010

### 1 Purpose of report

- 1.1 The purpose of the report addresses the motion from 24<sup>th</sup> June 2010 Council which requested a separate report outlining a refreshed Business Case detailing the capital and revenue implications of all the options currently being investigated by tie and taking into account assumptions contained within the original plan (eg anticipated development) that either no longer apply or whose timescales were have now substantially changed.
- 1.2 The report also provides updates on the recent contractual negotiations on the Edinburgh Tram Project and an update on the governance arrangements.

### 2 Main report

#### Tram Business Case Refresh

- 2.1 The refresh of the Business Case was instructed by the Council on 24<sup>th</sup> June 2010. Its purpose is to refresh the assumptions made in the Final Business Case (FBC) for Phase 1a of the Edinburgh Tram Project, as approved by the Council in October 2007.
- 2.2 The Council's instruction is set against a backdrop of commercial disputes with the infrastructure contractor, which have resulted in significant programme slippage and increasing project costs. In addition, the difficulties with the contractor have come at a time of economic downturn which has had an impact on the original planning assumptions.
- 2.3 The outputs of the refresh of the Business Case result from a significant amount of work carried out to reassess the assumptions underlying the FBC and are informed by the recent commercial experience of Lothian Buses.
- 2.4 In addition to the contribution of tie, Lothian Buses' management have been fully involved in the refresh of the TEL Business Plan. These inputs contain commercially sensitive information on patronage assumptions for buses as well as trams and consequently the detailed figures must remain commercially confidential. There has also been considerable work done by consultants Steer Davies Gleave and Colin Buchanan, providing independent input to model the revised patronage assumptions.

- 2.5 The refresh of the Business Case has primarily focused on updating the economic case for Phase 1a; incremental delivery; and updating of the TEL Business Plan (taking into account the revenue impacts of incremental delivery; investment to date; and funding and affordability).

### **Consideration and Assessment of Incremental Delivery**

- 2.6 Due to the cost and programme difficulties experienced on Phase 1a there has been a requirement to consider completion of Phase 1a in incremental stages as a contingency measure. The main focus of incremental delivery would be to deliver Airport to St Andrew Square as the first phase.
- 2.7 The phased delivery of the project would provide the opportunity ~~addresses the imperative to~~ manage key affordability risks through ~~by examining the~~ incremental delivery of the on-street sections. This approach would ensure that investment in the project is realised by the delivery of a viable tram service, integrated with bus services, whilst preserving the entire scope of Phase 1a, as detailed in the FBC.
- 2.8 Incremental delivery would allow the whole of Phase 1a to be delivered in stages and over a flexible timescale under the Council's control. The Council could then ensure that the infrastructure being delivered, at any point in time, is matched with available funding.
- 2.9 A first incremental opening of tram services from Airport to St Andrew Square would yield early economic and integration benefits and would provide an enhanced transport link between the city and Airport and would also provide a rail link to other areas of Scotland as a result of the interface with the Edinburgh Gateway Project (Gogar Station). A tram operating from the Airport to St Andrew Square also secures a high proportion of the economic benefits anticipated in the FBC and is capable of being successfully integrated with Lothian Buses' operations.
- 2.10 One of the key considerations under the incremental delivery option is to evaluate whether the potential first phase of construction to St Andrew Square is capable of delivering a positive contribution to the TEL business.
- 2.11 The evaluation of incremental delivery has shown that the TEL business as a whole is stronger in the medium to long term with tram added to the existing bus business even if the tram is only operated between the Airport and St. Andrew Square. The key outputs from the TEL Business Plan are highlighted later in this report.

### **Updating the Economic Case for Phase 1a**

- 2.12 An update of the economic case for tram has addressed both the full scope of Phase 1a and the option of incremental delivery.
- 2.13 The review of the economic case for tram refreshes the patronage sources and growth drivers in the city, taking into account a review of development profiles for Leith, the City Centre and West Edinburgh and assesses the impact of the development of the Airport and the broader regional drivers such as Gogar Station and the Edinburgh-Glasgow Improvement Plan. The update also looks

at the longer term context of the Council's Transport 2030 vision and modal shift away from private car that is a key policy driver for the Council and Transport Scotland.

- 2.14 The need for tram has been examined against the wider context of Edinburgh's short, medium and long term strategic position.
- 2.15 Edinburgh's population is currently expanding by around 1% per annum and is forecast to reach 514,000 by 2020 and 543,000 by 2030. As significant, the volume of commuters coming into the city to work from the surrounding city region and further afield was estimated at 85,000 per day at the 2001 census and is now around 100,000 per day and growing.
- 2.16 The city's growth has led to rapidly increasing demand for road use and increasing demand for public transport. Between 2000 and 2009, Lothian Buses patronage growth has been 18.9% in total, which equates to 2.1% per annum.
- 2.17 Tram is, in itself, considered to be a key stimulant to economic regeneration and new development. The extent of new development forecast is lower than was anticipated when the FBC was prepared in 2007 as a result of the economic downturn. With the key input of Council planning officers, an update of the likely timing of committed new development has been undertaken.
- 2.18 Whilst the residential development in the North of the city and in Leith completed at commencement of tram operations is projected to be more restricted than originally anticipated, the Council is forecasting a recovery such that, by 2012, 30% of the original forecast will be completed, 80% of the original forecast will be completed by 2020, and by 2031 the residential development in North Edinburgh will have recovered and the original development forecast will apply. The forecasts broadly anticipate a 4-5 year period of very slow development as a result the economic downturn, following which a return to growth will prevail.
- 2.19 It should be noted that the revised development profile only comprises committed developments or developments that have achieved outline planning consent. And as such is considered prudent.
- 2.20 It is clear that whilst the impact of the recession on the pace and size of development in the city has been significant, most notably at the Waterfront, it is important to consider the longer term view. The tram remains an important stimulant to development and regeneration in the West and North of Edinburgh.

### **The TEL Business Plan**

- 2.21 The update of the TEL Business Plan is the key output from the updated economic case for tram. The primary area under examination is the revised patronage and profitability forecasts for Phase 1a in total and the assessment of the impact of incremental delivery on TEL. In addition to the revised development assumptions, the updated forecasts for TEL are also built on the recent experience of Lothian Buses and further patronage modelling by external consultants, Steer Davis Gleeve and Colin Buchanan. These forecasts have been profiled against incremental delivery to St Andrew Square

to assess the impact on the TEL business. As mentioned previously, these inputs contain commercially sensitive information on patronage assumptions for buses as well as trams and consequently the detailed figures must remain commercially confidential.

- 2.22 As part of the preparation of this refresh, a review of the key assumptions and projections for the TEL Business Plan has been undertaken. This review has confirmed the validity for the whole of Phase 1a. It has also confirmed that the operation of incremental delivery of Phase 1a from Airport to St. Andrew Square is sustainable and has a positive impact on the TEL forecasts in the medium to long term.
- 2.23 The approach to integration of the key local public transport modes, bus and tram, sets Edinburgh apart from other UK tram schemes. The integration of high quality bus and tram services will improve the attractiveness of the combined network to something greater than the sum of its constituent parts. The levels of demand projected by the transport modelling, undertaken by Steer Davies Gleave and Colin Buchanan, indicate a significant profit potential for TEL operating with the tram in the medium to long term.
- 2.24 The key conclusions relating to the profitability of revenue running from the Airport to St Andrew Square are;
- TEL as a whole will be profitable from year one of operations.
  - Tram will be profitable following an initial three year period of patronage build up.
  - The business will experience significant growth in profits in the longer term.
- 2.25 In addition, significant work has been undertaken to assess positive and negative sensitivities in the business plan assumptions in the early years of tram operation. This analysis will inform management to allow action to be taken to ensure the profitability of TEL ~~the tram~~ remains intact. The sensitivities examined included patronage, electricity, fuel, labour and yield. It should be noted that another key sensitivity is in relation to the application of the Concessionary Fares Scheme. Discussions with Transport Scotland have indicated that the business planning assumption should continue to be that the Concessionary Scheme should continue to apply to buses and incorporate trams.

#### **Investment to Date**

- 2.26 A large infrastructure project such as the Tram Project requires a substantial amount of work to be undertaken in advance of the main construction works.
- 2.27 The budget for tram infrastructure represents 46% of the overall project budget with the most significant construction elements within this expenditure to date relating to Gogar Depot, the structures along the off-street section of the railway corridor and tram works along Princes Street. Currently, progress against the iselement of the prject is assessed as 22% [check]



- 2.28 Significant progress has been made on the construction of the 27 tram vehicles. This element of the project represents 11% of the original project budget. Currently this element of the project is assessed as over 60% complete [check]
- 2.29 The diversion of utilities has also resulted in a significant enhancement of the utility assets in the City including faster broadband services and enhanced water supplies. In the longer term, these investments made will mean that not only is there a uniquely documented record of all the utility pipes and cables positioning, but already there is a dramatic reduction in bursts of old pipes along the route. Although it is recognised that these improvements have caused disruption, it will mean that in the future, access to utility cabling will be predictable, much shorter in duration and less intrusive to the people of Edinburgh. This element of the project is currently assessed as over 95% complete
- 2.30 As previously reported, the scope for the utilities diversions has risen from 27,000 linear metres to around 48,000 linear metres. This represents an increase of some 78%. There has also been a consequential increase in cost relating to this scope increase of around 30%. In total expenditure on utilities is expected to be approximately 10% of the total project cost
- 2.31 A further area of expenditure relates to the costs of the design and purchase of the land that is required for the project. This accounts for 12% of the project budget expenditure to date, and it approximately XX % complete.
- 2.32 In summary, while there has clearly been significant delay to the infrastructure works, a vast amount of work and investment has gone into the tram project to date. Total spend on the project to date is £XXm
- 2.33 As can be seen from this, recent reports of 22% progress for 80% of the funding are both erroneous and misleading.

### **Funding and Affordability**

- 2.34 Given the increasing project costs, it is critical to assess the current committed funding and affordability constraints of the project.
- 2.35 As set out in the Council report of 24<sup>th</sup> June 2010, contingency planning has been undertaken up to a level of 10% above the current funding, allowing for total funding of £600m. Consideration has also been given to incremental delivery options.
- 2.36 The Council has made an allowance of £2m per annum within its long-term Financial Plan to cover additional infrastructure development costs. This provision would allow the Council to borrow £24m under the Prudential Framework. Headroom within the existing budget for loan charges may also allow future investment in infrastructure beyond this sum if required.
- 2.37 Further borrowing, should it be necessary, can potentially be financed from the future profits of TEL.

- 2.38 Of the current funding, the Council has committed £45m to the project, of which £25m is anticipated from developers' contributions. The slow down in development has impacted on the pace of developers' contributions expected to be received by the Council. However, over the 20 year period set out in the Tram Developers contribution guideline, it still remains possible to achieve the £25m total.
- 2.39 The current predicted negative impact on developers' contributions from incremental delivery is £7m if the route were to be curtailed at St Andrew Square. This means that if the full route of Phase 1a is not delivered then the Council would have to fund this additional £7m as part of their £45m commitment.
- 2.40 Whilst the commitment remains to deliver the full scope of Phase 1a, affordability remains the primary consideration given the current level of funding and the likely forthcoming constraints on public sector spending.
- 2.41 The tram project has faced many challenges since the start of construction. This has resulted in increased costs and significant delay. This has required options to be considered for delivering Phase 1a incrementally.
- 2.42 While a tram operating from the Airport to St Andrew Square can deliver significant benefits, and importantly can be profitable, further benefits would accrue from the full scope of Phase 1a. Therefore, an important assessment will be required at the appropriate time to appraise the benefits to be gained from constructing the full route of Phase 1a versus the capital cost and available funding.

### **Current Position**

- 2.43 In the report to Council on 24 June, Council was provided with an updated position on the dispute between tie and the BSC consortium.
- 2.44 Over the intervening months tie have been pursuing a twin track approach to try to break the impasse that exists with BSC.
- 2.45 The twin track approach adopted has been;
- To seek to agree a revised scope, price and programme, with the outcome of a tram operating to at least St Andrew Square, with a very high degree of cost and programme certainty.
  - To continue to administer the project in a robust manner; including compiling evidence of any breaches of contract by BSC; clarifying contractual principles regarding contractual changes; and completing the design.
- 2.46 It is important to acknowledge that there has been progress on-site whilst tie has been pursuing this twin track approach. Work on-site has been progressing in the West of the city, albeit at a slower rate than would be expected. This progress off-street is considerable and includes bridges, viaducts and the well progressed construction of the depot.

- 2.47 There have also, however, been some recent developments in relation to BSC apparently demobilising a certain element of their workforce claiming that they will not continue to work on certain parts of the project claiming that they have not been paid by tie on a goodwill basis. tie are adamant that all payments properly due have been made to the consortium.
- 2.48 Despite intensive and detailed negotiations having taken place over the last few months, tie and the consortium have to date been unable to reach agreement which would achieve a revised scope, price and programme acceptable to both parties. Whilst negotiations have not been suspended, an acceptable commercial settlement now unfortunately appears unlikely in the short term.
- 2.49 tie has been exercising its various rights and remedies under the contract. Further to the figures reported to the Council in June, to date the application of the dispute resolution process to disputed matters has reduced BSC's claims for additional payment from £21.9m to £9.5m (a saving of £12.4m). tie remains satisfied that the overall balance of dispute resolution including adjudication outcomes has more than justified its interrogation of the initial claims made by BSC. Suggestions in the press that BSC have 'won 13 out of 15' adjudications are without any foundation and factually incorrect
- 2.50 Given that acceptable commercial settlement now appears unlikely, all other options for contractual resolution together with alternatives for delivery of the project are being considered by tie. However, for commercial and legal reasons it is important at this point in time that all matters relating to possible contractual resolution remain confidential in order to protect the best interests of both the Council project and the public purse.
- 2.51 One possible option is termination of the current contract where the contractual terms allow this. **Any such decision would clearly have significant consequences and therefore this option will only be considered after taking into account the extensive legal advice which has already been taken, and continues to be taken, in relation to such matters.** As is to be expected, the contract contains defined mechanisms for dealing with alleged breaches and their potential outcomes, and such processes are already being utilised as part of tie's continuous rigorous application of the contractual terms.
- 2.52 In terms of the existing governance arrangements, any recommendation from tie and TEL to terminate the contract will require to be presented as a formal request for approval from the Council. Transport Scotland will also need to be informed of the position.
- 2.53 In the event approval for the termination of the contract is sought, tie will also bring forward options for delivering the project in an alternative manner. It is proposed that the above matters would form part of a further comprehensive report to be brought to the December Council meeting (or if possible an earlier Special Meeting of the Council) outlining the recommended available options. This would consider all implications and proposals for the project going forward.
- 2.54 In the meantime, discussions will continue with the consortium to attempt to reach an agreed solution as outlined above.

## **Governance of Bus and Tram Integration**

- 2.55 It has long been a policy aim of the City of Edinburgh Council to develop an integrated public transport network delivering high quality bus and tram services in the city. Over the last two years the Chief Executive has submitted a number of reports to Council on the steps necessary to bring this about.
- 2.56 Work on the final phase of the agreed integration of ~~tie~~, TEL and Lothian Buses has been underway for some time. A number of complex and inter-related actions need to be taken to prepare the way for the revised governance arrangements that the advent of trams will require. As previously reported, a work programme embracing the following key issues is proceeding:
- legal and contractual matters;
  - finance (including tax planning);
  - employment; and
  - communications and reporting.

It is anticipated that these work streams will be completed by the middle of 2011.

- 2.57 To direct and oversee the work programme on bus and tram integration it is essential that senior management arrangements, with clearly specified roles and responsibilities, are in place. As agreed by Council in December 2009 (and having completed all the appropriate HR procedures, based on those used by the Council and involving a "matching process"), the Board of TEL has agreed that Richard Jeffrey will take on the role of Chief Executive (Designate) and Ian Craig will take on the role of Chief Operating Officer (Designate). There will be no change meantime to existing remuneration arrangements or any additional contractual liabilities.
- 2.58 These appointments are an essential foundation for the new arrangements. It gives Richard Jeffrey and Ian Craig the full authority, under the direction of the Boards of TEL and Lothian Buses, to lead the demanding work programme associated with public transport integration over the next nine months and beyond. It will be an early priority for the two senior postholders to establish a shared vision, values and brand for the future; establish a common IT platform; devise and implement management and organisational structures and

recruit/appoint to them; carry out business planning and drive efficiencies; and carry out training and the like.

### **3 Financial Implications**

- 3.1 As previously reported, the contingency planning work that has been undertaken by the Council and **tie** has identified funding options which could address project costs of up to £600m. Due to the current uncertainty of contractual negotiations, it is not possible to provide an update at this time on the ultimate capital cost of the project.

### **4 Environmental Impact**

- 4.1 The Edinburgh Tram Project will make a positive contribution towards the vehicular emissions and air quality in the city centre and the transport corridor to the West of the city and the airport. This will have a positive impact on current pollution levels and provide a quieter mode of public transport. The tram also provides mitigation against future traffic congestion from population growth and increased commuter demand.

### **5 Conclusions**

- 5.1 Following the recent refresh, the Business Case remains positive, even with incremental delivery only to St Andrew Square.
- 5.2 Whilst negotiations have not been formally suspended, an acceptable commercial settlement now appears unlikely to be achieved in the short term.
- 5.3 Contract enforcement continues with the due legal process needing to be followed prior to a report back to Council.

### **6 Recommendations**

- 6.1 The Council;
- a) Note the position regarding the Business Case and discharge the motion of 24<sup>th</sup> June 2010.
  - b) Note the disappointing lack of progress in relation to the negotiations and progress of physical works.
  - c) Endorse rigorous application of the contract by **tie**.
  - d) Note that in the absence of robust remediation plans from the consortium and a change of behaviour in relation to progressing the works, serious consideration will need to be given to termination of the contract and re-procurement.

- e) Note the recent governance developments and future work streams.
- f) Note that a report will be prepared for the December Council (or possibly an earlier special meeting) on the next steps.

**Dave Anderson**  
Director of City Development

**Donald McGougan**  
Director of Finance

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Appendices          None

Contact/tel/Email    Alan Coyle [REDACTED] alan.coyle@edinburgh.gov.uk  
                             Nick Smith [REDACTED] nick.smith@edinburgh.gov.uk

Wards affected

Single Outcome  
Agreement

Background  
Papers

Nick Smith

NS1.8

**From:** Mandy Haeburn-Little <Mandy.Haeburn-Little@tie.ltd.uk>  
**Sent:** 07 October 2010 10:27  
**To:** Alan Coyle; Richard Jeffrey; Nick Smith; Julie Smith  
**Subject:** Paper - couple of thoughts

I like the paper – very good

We like the DRP info being in – I do want to get this out, it's important to us.

Under 3.28

?" Despite some of the media reporting on this project, the reality is that approximately 70% of the project overall has been delivered against anticipated progress.

Under 3.31 we could say more about the benefits that moving utilities will bring.

? " in the longer term, these investments made will mean that not only is there a uniquely documented record of all the utility cabling positioning, but already there is a dramatic reduction in bursts of old pipes along the route and this alone making a real and practical difference. Although we recognise that these improvements have caused disruption, it will mean that in the future, access to utility cabling will be predictable, much shorter in duration and less intrusive to the people of Edinburgh. "

Under 3.37 we could make reference to the success of the decision on TIF

?" The City continues to review innovative options for borrowing which will benefit the City . This is particularly relevant given the anticipated public sector cuts. , Only this week has announce one of these new options under TIF for the waterfront area."

Richard will bring marked up copy

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**From:** Alan Coyle [mailto:Alan.Coyle@edinburgh.gov.uk]  
**Sent:** 07 October 2010 09:46  
**To:** Mandy Haeburn-Little  
**Subject:**

Mandy,  
As discussed. Password is 14.5  
A

Regards

Alan Coyle | Financial Services | Corporate Finance Team (Edinburgh Trams) | Level 2/6 Waverley Court | 4 East Market St EH8 8BG  
| [alan.coyle@edinburgh.gov.uk](mailto:alan.coyle@edinburgh.gov.uk) |

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Nick Smith

NS 1.9

**From:** Nick Smith  
**Sent:** 05 October 2010 12:23  
**To:** Donald McGougan; Dave Anderson  
**Cc:** Alastair Maclean; Carol Campbell  
**Subject:** Tram - Lawyers

Donald/Dave

After meeting with a couple of firms we think that Shepherd and Wedderburn will be best placed to advise the Council in relation to the possible contract termination or a variation on this theme. Their quote, which is based on some assumptions, is £12,500, which is roughly 50% of the other quote we got. Note that the scope will inevitably expand from this as matters progress and we should probably budget around £20,000 for this work. In addition, we will have Counsel's fees on top.

However, given the importance of the decision, the cost is subordinate to the fact that Shepherds appear to have the knowledge and skill required and will also bringing entirely fresh and un-conflicted views to the table.

I understand this has been discussed with Alastair so I'll go ahead and instruct the lawyers to get them up to speed.

Kind regards

Nick

Nick Smith  
Principal Solicitor - Commercial, Procurement & Finance  
Legal Services Division  
City of Edinburgh Council  
Level 3, Waverley Court  
East Market Street  
Edinburgh EH8 8BG

(t) 

*Please note that I am not in the office on a Monday*