further authorisation from the Council (or the Tram Sub-committee, as appropriate) with regard to (i) further costs increases in excess of £10m; (ii) any further delays of over three months; (iii) settlement of claims in excess of £500,000; or (iv) any substantial change to the design, scope or services pattern set out in the FBC.

3.8 On the 20 December 2007 Council delegated authority to the Council Solicitor to conclude and execute the Guarantee on behalf of the Council for the benefit of BBS.

Quantified Risk Allowance (QRA)

3.9 The QRA has reduced from £49m at FBC to £32m. The material change in the QRA relates to procurement risks for Tramco and Infraco closed out at the signing of the contracts offset by allowance to provide for risks and uncertainties to be managed by **tie Ltd** during construction.

3.10 A number of the adjustments to risk allocation are positive, reflected in the reduced QRA. As a result of the overlapping period of design and construction a new risk area has emerged which has been the subject of extensive and difficult negotiation. **tie Ltd** advise that the outcome is the best deal that is currently available to themselves and the Council. Both **tie Ltd** and the Council have worked and will continue to work diligently to examine and reduce this risk in practical terms.

3.11 A written statement from **tie Ltd** has been provided stating that they are satisfied that £32m is an adequate level of risk allowance.

4 Financial Implications

4.1 Following closure of procurement risks the baseline cost of the project has increased from to £449m to £476m with the QRA reducing from £49m to £32m resulting in the final price of the project increasing from £498m to £508m. The estimate remains well within the agreed funding envelope of £545m.

5 Conclusions

5.1 It is proposed that the Tramco and Infraco contracts should be awarded to CAF and BBS respectively, securing the best deal possible for the Council and Transport Scotland. The awarding of these two contracts will represent a significant milestone in the implementation of the Tram project. A significant level of risk has been assumed by the private sector considerably reducing the Council's exposure to future uncertainty. Communications about the commitment to these important contracts will be co-ordinated with **tie Ltd** and Transport Scotland.

6 Recommendations

6.1 It is recommended that the Council:

- note the imminent award of the two contracts with a final price for the Edinburgh Tram Network of £508m which is within the funding envelope of £545m;

- refresh the delegated powers already given, to authorise me to instruct **tie Ltd** to enter the contracts with Infraco bidder and Tramco bidder, in light of recent changes noted in this report;

- note that the FBCv2 which was approved by Council on 20 December 2007 is modified to reflect the above position;

- note the **tie Ltd** and TEL operating agreements have been amended to reflect the fully up to date position; and

- note that the Guarantee to be executed on behalf of the Council for the benefit of BBS will be provided at financial close.

Tom Aitchison
Chief Executive

Appendices	None
Contact/tel	Andy Conway Alan Coyle [redacted]
Wards affected	All
Background Papers	Draft **tie Ltd** operating agreement Draft TEL operating agreement Council Guarantee

REPORT ON INFRACO CONTRACT SUITE

Content of this section

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

Process of drafting, negotiation, review and quality control

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

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

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

This report is not a substitute for reading the Contract itself. It is focussed on those provisions in which CEC has expressed particular interest and has directed tie should be included in the report. It should be understood that the ETN Contract Suite has undergone a lengthy and difficult negotiation and close out phase.BBS has on a number of occasions moved from a previous firm position and this has required detailed re-examination and recasting of contractual provisions in order to reinstate acceptability.

General description of scope, parties and contract structure

Subsequent to the position described in this paper being reached, a further round of negotiations instigated by Bilfinger Berger took place. The detail behind the final position reached has been documented separately for CEC in the parallel paper entitled "Close Considerations and event history".

The Infraco contract suite comprises the following principal contracts :

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

Overview of Infraco contract terms

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

Authority to Transact

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

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

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

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

Conditions Precedent

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

Warranties

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

Duty of Care and General Obligations

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

Indemnity Provisions

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

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

The Infraco is wholly responsible to tie for any actions or omissions of its employees, agents, advisers and sub-contractors. Deleted: ¶ ¶

Principal Exclusions are the following:

- any act or omission of tie or CEC is the cause of such death, injury or damage to property;

- proportion of loss caused by tie/CEC;

- indirect losses of tie/CEC by reason of Infraco breach or negligence, but certain indirect losses claimed by a third party are carved out of this prohibition. Infraco would therefore be liable to indemnify tie/CEC against a claim for lost revenue asserted by a business for physical damage caused by Infraco's breach, but not for economic loss, unless flowing from physical damage or otherwise insured.

- Insurance deductibles and excesses where the claim has been caused by CEC/tie's contributory fault or because tie has altered OCIP to accept a higher level of excess or deductible.

- any liability incurred by Infraco to a third party where Infraco is performing its obligations in accordance with the Agreement (i.e. claims in nuisance).

ETN Assets

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

Price

A contract price has been agreed. The detailed contract price and pricing schedules for carrying out the Infraco Works is contained in Schedules to the Infraco Contract. A substantial portion of the Contract Price is agreed on a lump sum fixed price basis. There are certain work elements that cannot be definitively concluded in price and therefore Provisional Sums are included. A number of core pricing and programming assumptions have been agreed as the basis for the Contract Price. If these do not hold, Infraco is entitled to a price and programme variation known as "Notified Departure".

Programme

The Agreement provides that Infraco shall progress the Infraco Works to achieve timeous delivery and completion of the Infraco Works (or parts thereof) and in their obligations under the Agreement, all in accordance with an agreed Programme which is bound into the Schedules. This Programme is the product of tie, Infraco and SDS Provider negotiations and is cardinal to the control of Infraco and SDS Provider's performance and their potential entitlements to relief or additional payment. Following contract signature, it is expected that BBS will seek a Notified Departure on Programme due to SDS delay in design production. However, both BBS and SDS have a contractual obligation to mitigate. The exposure has been assessed in detail by tie and confirmed as acceptably within the risk contingency.

Milestones and Payment schedule

The construction sequence is broken down into construction milestones and critical milestones and Procedures have been agreed for the monitoring of progress toward each milestone based upon milestone schedules. Interim payments will be made to Infraco 4-weekly subject to and in accordance with the completion of stated Milestones. The Agreement obliges Infraco to complete the Infraco Work in sections and failure to complete sections by the sectional completion date will result in Infraco becoming liable to pay liquidated and ascertained damages to tie at amounts stated in the Agreement. If Infraco are delayed by reason of certain prescribed contractual events they may be able to apply for an Extension of Time and/or claim costs.

Novations

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

Network Rail Interface

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

Operator Interface

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

Safety

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

Site Access

tie warrants to the Infraco that access to all necessary land can be provided and has committed to an Access Permit Procedure to enable Infraco to enter and remain upon the permanent land for the term of the Agreement and exclusive licence to enter and remain upon designated working areas (the public road) during Infraco Works and shall provide Infraco with all necessary land consents. Works on permanent land or temporary sites by Infraco are subject to compliance with the requirements of third parties and in particular the constraints on site occupation and working practices imposed by EAL at Edinburgh Airport and also NR APA constraints.

Infraco Maintenance

Infraco shall comply with the requirements of the Code of Construction Practice and Code of Maintenance Practice with regard to the maintenance of occupied and adjacent properties, bus stops, bus services and closure of roads. The Infraco is obliged to undertake maintenance of the ETN from the time when any section is completed and afterwards under the full Maintenance Services regime once Service Commencement occurs. The Maintenance Services regime is for ten years post Service Commencement, with a unilateral option for tie to extend for 5 years, subject to any required changes. tie may terminate the Infraco Contract on 6 months' notice at any time after 3 years of ETN operation. Compensation is payable as if such termination had occurred for tie Default.

Contract changes

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

Phase 1b and Network Expansions

Infraco acknowledges that tie may, subject to notice instruct the Phase 1b works to be carried out provided that the election is made no later than 6th July 2009. The Agreement contains a mechanism for estimating the cost of Phase 1b as a tie Change under which Infraco would carry out Phase 1b works if so instructed. Network Expansion (i.e. a spur, interconnect or modification) would fall to be dealt with as a tie Change under the Change mechanism.

Termination

If tie defaults (on payment exceeding £250,000 overdue for more than 30 days or becomes insolvent) Infraco may serve a termination notice in accordance with the Agreement. The Agreement sets out the treatment of such termination. If Infraco defaults in certain prescribed matters, tie may, after giving required notice, terminate the Agreement. The Agreement again sets out the rules relating to such proposed termination as to final account, compensation (if any) and tie's entitlements to compensation under these provisions. The compensation entitlements are sole remedies.

Dispute Resolution

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

Disputes are to be dealt with through a rapid escalation process to Chief Executive level or equivalent in order to achieve amicable resolution of any unsolved dispute within 15 days. If no settlement is possible, the Chief Executives may elect mediation, adjudication, or court proceedings as the resolution process. The Dispute Resolution Procedure mechanic allows for joinder of related disputes (i.e. Key sub-contractors, SDS Provider and certain third parties such as NR and EAL) at the instigation of either party. The provisions are exempt from the application of mandatory adjudication time limits (under the Housing Grants Construction Regeneration Act 1996) by virtue of the Tram Acts.

SDS Novation Agreement and design delivery and approval process

Principles of Novation

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

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

SDS Provider Novation outcome

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

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

There is an SDS Provider parent company guarantee and there is a £500,000 bond which is callable by tie if SDS Provider fails to novate. Post novation tie will hold an SDS Collateral Warranty and a Collateral Warranty from Halcrow, SDS's sub-consultant.

Design expectations of the Infraco

Deleted: ¶

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

The construction programme included in the final 'Infraco' proposal has been updated to match up with version 26 of the SDS design programme (dated 4 February 2008). The Novation Agreement is based on version 30 of the SDS design programme and the differences between these programmes has been documented and will form the basis of the expected Notified Departure referred to in the programme section above and which has been risk-assessed.

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

Managing Approvals Risk

The risk of securing approvals has been shared between SDS and tie Ltd. SDS takes the risk of achieving delivery of batches for approval on the agreed date to the agreed quality. That risk is capped at £1,000,000 pounds liquidated damages at approximately £10,000 per package. Provided the application for approval is made on time and the quality of application is in line with agreed expectations then tie ltd takes the risk that the Council does not process the application within the 8 week period included in the programme. SDS is also incentivised by a bonus pot of £1,000,000 pounds with approximately £10,000 attaching to each deliverable package. The bonus is lost if the programme date is missed for any reason other than tie Change.

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

Design Guidance

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

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

Confirmation of BBS acceptance of modelling

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

Employer's Requirements

The Infraco Proposals and the Employer's Requirements

No comprehensive legal review has been instructed by tie in relation to the Infraco Proposals, on the basis that these are technical responses to the outline Employer's Requirements issued initially by tie in October 2006 at ITN stage and then progressively until selection of preferred bidder in October 2007.

Since DLAP's initial exercise there have been several further iterations of the Employer's Requirements which have been controlled by tie's technical team but no further legal review. Consequently, DLAP cannot give legal assurance regarding the current content of the Employer's Requirements and their consistency with the Infraco core terms and conditions. BBS' position as of 4 March 2008 was that they could not sign the Infraco Contract without a thorough review of the Employer's Requirements by their legal team. tie has instructed SDS to carry out an exercise to bring the Employer's Requirements and the Infraco Proposals into alignment so that SDS Provider are able to confirm that their design will be in compliance the Employer's Requirements. This may result in further changes to the Employer's Requirements and/or the Infraco Proposals and/or the SDS design.

The risk created by discrepancies between the version of the Employer's Requirements eventually settled on and the Infraco core terms and conditions lies in the Infraco attempting to exploit ambiguity to engineer the need for tie Change or Relief when none is in fact justified. tie project management will need to be vigilant in identifying and closing off such opportunities, using the mitigating contract provisions which impose duties on Infraco to respect ambiguities and discrepancies and permits tie Representative to interpret provisions to avoid these difficulties.

Advance purchase materials

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

Infraco Payment mechanism

<u>Construction</u>

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

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

- Save in respect of agreed advance payments, Infraco will not be paid in advance of its own outgoing cash flows through its own supply chain

- The individual milestones are defined such that the process of determining whether or not they have been achieved will be subject to the minimum of uncertainty or dispute

- The certification of a milestone will require evidence that all required relevant consents and approvals have been delivered in respect of the related works

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

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

Commissioning and Maintenance

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

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

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

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

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

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

Infraco performance security arrangements

Bonds during construction period

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

The Performance Bond is in the amount of approximately £23m throughout the construction period reducing to £11.5m when a certificate of Revenue Service Commitment is issued and further reducing to £9.2m when a certificate of Network Certificate relating to the achievement of performance criteria is issued. The issue of the aforementioned certificates is subject to a rigorous testing regime as defined in the Employers Requirements, including evidence that all relevant consents and approvals have been delivered, and provides both security for tie/CEC and incentive to Infraco to perform.
The Retention Bond is in the amount of £2m initially, adjusting to the following amounts at sectional completions:

- £4m section A – The depot
- £6m section B – Depot to the Airport
- £8m section C – The rest of Phase 1a
- £10m section D – Driver training and commissioning
- £6m at issue of Network Certificate (pertaining to reliability as defined in the Employers Requirements)

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

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

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

Parent Company Guarantees (PCGs)

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

The PCGs respect the joint and several liability provisions in the Infraco contract; each claim by tie under the PCG's must be served on each of the parent companies in the proportion of their share of the Infraco consortium but in the event of either parent company failing to honour payment of such a claim, the other parent company is liable up to the limit of overall liability specified in the Infraco contract (20% of the Infraco contract price but subject to graduated step down over 10 years).

The PCGs provide that in the event of a change in control or ownership of the subsidiary companies which are entering into the Infraco contract, the PCG's remain in force until a replacement PCG has been provided on terms which are acceptable to tie. PCGs cover liability for latent defects, patent defects, pre existing obligations and third party claims arising from latent defects (up to £9,000,000). Liability for maintenance related activity is capped at £3.5 million pounds.

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

Brief Overview of Tramco contract terms

Authority to Transact

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

Joint and Several Liability

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

Conditions Precedent

As for Infraco Contract.

Indemnities

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

Warranties

The Three principal Warranties relate to:

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

Consents

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

Termination

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

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

System Integration

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

Operator Interface

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

Contract changes

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

Quality Assurance

Tramco shall at all times utilise a Project Quality Assurance Programme compliant to standards. A tram manufacturing and delivery programme is agreed and regular monitoring of progress will take place.

There is provision is the Agreement for tie to be involved in inspecting the trams at various stages of the manufacturing process. Tramco shall deliver the trams to the designated point of delivery at the depot and delivery tests shall be conducted. Tramco, tie and the operator shall agree a training programme and the detailed implementation.

Transfer of Title

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

2.11 Tramco payment mechanism

Supply agreement

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

- Initial mobilisation and establishment of supply chain
- Delivery of tram vehicles
- Attainment of performance and reliability standards as specified

2.12 Tramco performance security arrangements

Bonds during supply period

Tramco will provide a Reliability bond in the defined amount of 5% of the Tramco price such bond to be provided on or before the due date of delivery of the first Tram vehicle. An advance payment bond in the full amount of the initial milestones of £11m under the supply contract is being provided direct to tie by an A rated surety on the date of contract signature. This security will remain in place until the reliability bond as above is provided.

Deleted: A further advance payment bond is to be provided to tie.

Parent Company Guarantee (PCG)

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

Maintenance agreement

The Infraco is responsible for providing tram maintenance through Tramco performing the tram maintenance agreement. This is a relatively standard agreement, developed from UK sector models.

Performance securities under maintenance agreement

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

CEC Financial Guarantee

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

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

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

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

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

tie Limited
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REPORT ON INFRACO CONTRACT SUITE

Content of this section

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

Process of drafting, negotiation, review and quality control

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

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

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

This report is not a substitute for reading the Contract itself. It is focussed on those provisions in which CEC has expressed particular interest and has directed tie should be included in the report. It should be understood that the ETN Contract Suite has undergone a lengthy and difficult negotiation and close out phase.BBS has on a number of occasions moved from a previous firm position and this has required detailed re-examination and recasting of contractual provisions in order to reinstate acceptability.

General description of scope, parties and contract structure

<u>Subsequent to the position described in this paper being reached, a further round of negotiations instigated by Bilfinger Berger took place. The detail behind the final position reached has been documented separately for CEC in the parallel paper entitled "Close Considerations and event history".</u>

The Infraco contract suite comprises the following principal contracts :

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

Overview of Infraco contract terms

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

<u>Authority to Transact</u>

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

- each party will produce certified board minutes or other legally competent evidence of the corporate decision to enter into the ETN Contract Suite;

- all signatories will demonstrate legally effective power of attorney from their respective organisations; and

- in relation to foreign companies, an external counsel's opinion covering the legally binding nature of the corporate acts (re Contract execution) carried out in accordance with corporate governance, the signatories' delegated authority and the enforceability of the Contracts against the parties through the courts in their respective home jurisdictions.

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

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

Conditions Precedent

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

Warranties

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

Duty of Care and General Obligations

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

Indemnity Provisions

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

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

The Infraco is wholly responsible to tie for any actions or omissions of its employees, agents, advisers and sub-contractors.

Principal Exclusions are the following:

- any act or omission of tie or CEC is the cause of such death, injury or damage to property;

- proportion of loss caused by tie/CEC;

- indirect losses of tie/CEC by reason of Infraco breach or negligence, but certain indirect losses claimed by a third party are carved out of this prohibition. Infraco would therefore be liable to indemnify tie/CEC against a claim for lost revenue asserted by a business for physical damage caused by Infraco's breach, but not for economic loss, unless flowing from physical damage or otherwise insured.

- Insurance deductibles and excesses where the claim has been caused by CEC/tie's contributory fault or because tie has altered OCIP to accept a higher level of excess or deductible.

- any liability incurred by Infraco to a third party where Infraco is performing its obligations in accordance with the Agreement (i.e. claims in nuisance).

ETN Assets

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

Price

A contract price has been agreed. The detailed contract price and pricing schedules for carrying out the Infraco Works is contained in Schedules to the Infraco Contract. A substantial portion of the Contract Price is agreed on a lump sum fixed price basis. There are certain work elements that cannot be definitively concluded in price and therefore Provisional Sums are included. A number of core pricing and programming assumptions have been agreed as the basis for the Contract Price. If these do not hold, Infraco is entitled to a price and programme variation known as "Notified Departure".

Programme

The Agreement provides that Infraco shall progress the Infraco Works to achieve timeous delivery and completion of the Infraco Works (or parts thereof) and in their obligations under the Agreement, all in accordance with an agreed Programme which is bound into the Schedules. This Programme is the product of tie, Infraco and SDS Provider negotiations and is cardinal to the control of Infraco and SDS Provider's performance and their potential entitlements to relief or additional payment. Following contract signature, it is expected that BBS will seek a Notified Departure on Programme due to SDS delay in design production. However, both BBS and SDS have a contractual obligation to mitigate. The exposure has been assessed in detail by tie and confirmed as acceptably within the risk contingency.

Milestones and Payment schedule

The construction sequence is broken down into construction milestones and critical milestones and Procedures have been agreed for the monitoring of progress toward each milestone based upon milestone schedules. Interim payments will be made to Infraco 4-weekly subject to and in accordance with the completion of stated Milestones. The Agreement obliges Infraco to complete the Infraco Work in sections and failure to complete sections by the sectional completion date will result in Infraco becoming liable to pay liquidated and ascertained damages to tie at amounts stated in the Agreement. If Infraco are delayed by reason of certain prescribed contractual events they may be able to apply for an Extension of Time and/or claim costs.

Novations

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

Network Rail Interface

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

Operator Interface

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

Safety

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

Site Access

tie warrants to the Infraco that access to all necessary land can be provided and has committed to an Access Permit Procedure to enable Infraco to enter and remain upon the permanent land for the term of the Agreement and exclusive licence to enter and remain upon designated working areas (the public road) during Infraco Works and shall provide Infraco with all necessary land consents. Works on permanent land or temporary sites by Infraco are subject to compliance with the requirements of third parties and in particular the constraints on site occupation and working practices imposed by EAL at Edinburgh Airport and also NR APA constraints.

Infraco Maintenance

Infraco shall comply with the requirements of the Code of Construction Practice and Code of Maintenance Practice with regard to the maintenance of occupied and adjacent properties, bus stops, bus services and closure of roads. The Infraco is obliged to undertake maintenance of the ETN from the time when any section is completed and afterwards under the full Maintenance Services regime once Service Commencement occurs. The Maintenance Services regime is for ten years post Service Commencement, with a unilateral option for tie to extend for 5 years, subject to any required changes. tie may terminate the Infraco Contract on 6 months' notice at any time after 3 years of ETN operation. Compensation is payable as if such termination had occurred for tie Default.

Contract changes

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

Phase 1b and Network Expansions

Infraco acknowledges that tie may, subject to notice instruct the Phase 1b works to be carried out provided that the election is made no later than 6th July 2009. The Agreement contains a mechanism for estimating the cost of Phase 1b as a tie Change under which Infraco would carry out Phase 1b works if so instructed. Network Expansion (i.e. a spur, interconnect or modification) would fall to be dealt with as a tie Change under the Change mechanism.

Termination

If tie defaults (on payment exceeding £250,000 overdue for more than 30 days or becomes insolvent) Infraco may serve a termination notice in accordance with the Agreement. The Agreement sets out the treatment of such termination. If Infraco defaults in certain prescribed matters, tie may, after giving required notice, terminate the Agreement. The Agreement again sets out the rules relating to such proposed termination as to final account, compensation (if any) and tie's entitlements to compensation under these provisions. The compensation entitlements are sole remedies.

Dispute Resolution

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

Disputes are to be dealt with through a rapid escalation process to Chief Executive level or equivalent in order to achieve amicable resolution of any unsolved dispute within 15 days. If no settlement is possible, the Chief Executives may elect mediation, adjudication, or court proceedings as the resolution process. The Dispute Resolution Procedure mechanic allows for joinder of related disputes (i.e. Key sub-contractors, SDS Provider and certain third parties such as NR and EAL) at the instigation of either party. The provisions are exempt from the application of mandatory adjudication time limits (under the Housing Grants Construction Regeneration Act 1996) by virtue of the Tram Acts.

SDS Novation Agreement and design delivery and approval process

Principles of Novation

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

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

SDS Provider Novation outcome

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

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

There is an SDS Provider parent company guarantee and there is a £500,000 bond which is callable by tie if SDS Provider fails to novate. Post novation tie will hold an SDS Collateral Warranty and a Collateral Warranty from Halcrow, SDS's sub-consultant.

Design expectations of the Infraco

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

The construction programme included in the final 'Infraco' proposal has been updated to match up with version 26 of the SDS design programme (dated 4 February 2008). The Novation Agreement is based on version 30 of the SDS design programme and the differences between these programmes has been documented and will form the basis of the expected Notified Departure referred to in the programme section above and which has been risk-assessed.

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

Managing Approvals Risk

The risk of securing approvals has been shared between SDS and tie Ltd. SDS takes the risk of achieving delivery of batches for approval on the agreed date to the agreed quality. That risk is capped at £1,000,000 pounds liquidated damages at approximately £10,000 per package. Provided the application for approval is made on time and the quality of application is in line with agreed expectations then tie ltd takes the risk that the Council does not process the application within the 8 week period included in the programme. SDS is also incentivised by a bonus pot of £1,000,000 pounds with approximately £10,000 attaching to each deliverable package. The bonus is lost if the programme date is missed for any reason other than tie Change.

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

Design Guidance

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

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

Confirmation of BBS acceptance of modelling

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

Employer's Requirements

The Infraco Proposals and the Employer's Requirements

No comprehensive legal review has been instructed by tie in relation to the Infraco Proposals, on the basis that these are technical responses to the outline Employer's Requirements issued initially by tie in October 2006 at ITN stage and then progressively until selection of preferred bidder in October 2007.

Since DLAP's initial exercise there have been several further iterations of the Employer's Requirements which have been controlled by tie's technical team but no further legal review. Consequently, DLAP cannot give legal assurance regarding the current content of the Employer's Requirements and their consistency with the Infraco core terms and conditions. BBS' position as of 4 March 2008 was that they could not sign the Infraco Contract without a thorough review of the Employer's Requirements by their legal team. tie has instructed SDS to carry out an exercise to bring the Employer's Requirements and the Infraco Proposals into alignment so that SDS Provider are able to confirm that their design will be in compliance the Employer's Requirements. This may result in further changes to the Employer's Requirements and/or the Infraco Proposals and/or the SDS design.

The risk created by discrepancies between the version of the Employer's Requirements eventually settled on and the Infraco core terms and conditions lies in the Infraco attempting to exploit ambiguity to engineer the need for tie Change or Relief when none is in fact justified. tie project management will need to be vigilant in identifying and closing off such opportunities, using the mitigating contract provisions which impose duties on Infraco to respect ambiguities and discrepancies and permits tie Representative to interpret provisions to avoid these difficulties.

Advance purchase materials

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

Infraco Payment mechanism

Construction

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

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

- Save in respect of agreed advance payments, Infraco will not be paid in advance of its own outgoing cash flows through its own supply chain

- The individual milestones are defined such that the process of determining whether or not they have been achieved will be subject to the minimum of uncertainty or dispute

- The certification of a milestone will require evidence that all required relevant consents and approvals have been delivered in respect of the related works

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

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

Commissioning and Maintenance

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

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

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

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

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

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

Infraco performance security arrangements

Bonds during construction period

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

The Performance Bond is in the amount of approximately £23m throughout the construction period reducing to £11.5m when a certificate of Revenue Service Commitment is issued and further reducing to £9.2m when a certificate of Network Certificate relating to the achievement of performance criteria is issued. The issue of the aforementioned certificates is subject to a rigorous testing regime as defined in the Employers Requirements, including evidence that all relevant consents and approvals have been delivered, and provides both security for tie/CEC and incentive to Infraco to perform.
The Retention Bond is in the amount of £2m initially, adjusting to the following amounts at sectional completions:

- £4m section A – The depot
- £6m section B – Depot to the Airport
- £8m section C – The rest of Phase 1a
- £10m section D – Driver training and commissioning
- £6m at issue of Network Certificate (pertaining to reliability as defined in the Employers Requirements)

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

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

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

Parent Company Guarantees (PCGs)

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

The PCGs respect the joint and several liability provisions in the Infraco contract; each claim by tie under the PCG's must be served on each of the parent companies in the proportion of their share of the Infraco consortium but in the event of either parent company failing to honour payment of such a claim, the other parent company is liable up to the limit of overall liability specified in the Infraco contract (20% of the Infraco contract price but subject to graduated step down over 10 years).

The PCGs provide that in the event of a change in control or ownership of the subsidiary companies which are entering into the Infraco contract, the PCG's remain in force until a replacement PCG has been provided on terms which are acceptable to tie. PCGs cover liability for latent defects, patent defects, pre existing obligations and third party claims arising from latent defects (up to £9,000,000). Liability for maintenance related activity is capped at £3.5 million pounds.

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

Brief Overview of Tramco contract terms

Authority to Transact

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

Joint and Several Liability

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

Conditions Precedent

As for Infraco Contract.

Indemnities

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

Warranties

The Three principal Warranties relate to:

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

Consents

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

Termination

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

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

System Integration

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

Operator Interface

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

Contract changes

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

Quality Assurance

Tramco shall at all times utilise a Project Quality Assurance Programme compliant to standards. A tram manufacturing and delivery programme is agreed and regular monitoring of progress will take place.

There is provision is the Agreement for tie to be involved in inspecting the trams at various stages of the manufacturing process. Tramco shall deliver the trams to the designated point of delivery at the depot and delivery tests shall be conducted. Tramco, tie and the operator shall agree a training programme and the detailed implementation.

Transfer of Title

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

2.11 Tramco payment mechanism

Supply agreement

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

- Initial mobilisation and establishment of supply chain
- Delivery of tram vehicles
- Attainment of performance and reliability standards as specified

2.12 Tramco performance security arrangements

Bonds during supply period

Tramco will provide a Reliability bond in the defined amount of 5% of the Tramco price such bond to be provided on or before the due date of delivery of the first Tram vehicle. An advance payment bond in the full amount of the initial milestones of £11m under the supply contract is being provided direct to tie by an A rated surety on the date of contract signature. This security will remain in place until the reliability bond as above is provided.

Parent Company Guarantee (PCG)

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

Maintenance agreement

The Infraco is responsible for providing tram maintenance through Tramco performing the tram maintenance agreement. This is a relatively standard agreement, developed from UK sector models.

Performance securities under maintenance agreement

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

CEC Financial Guarantee

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

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

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

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

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

tie Limited
12.05.08

EDINBURGH TRAM PROJECT
ASSESSMENT OF RISK OF SUCCESSFUL PROCUREMENT CHALLENGE

Background

The Intention to Award notices were issued on 18th March and contract completion is imminent. The purpose of this paper is to summarise tie's assessment of the risk of a successful challenge under procurement regulations. Technically, a challenge could emerge from many quarters, but the most likely source in any procurement is from unsuccessful bidders, especially those who reached a late stage in the process. It is this threat which is addressed in this paper.

It must be borne in mind that the source and basis for a challenge cannot be predicted with certainty. This paper is not a substitute for the documentation that may be required to defend tie's actions in the event of a challenge.

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A review of the procurement process was performed by Jim McEwan which covered the period from selection of the preferred bidders in October 2007 through to the end of January 2008. This was independent of those who had been involved in the procurement process and concluded that the processes and documentation were in order. This review is included in the Close Report which supports the decision-making on Financial Close. Because the Close Report is potentially a public document, the more commercially confidential information contained in this paper will not be reflected in the Close Report.

Overall outcome

The current position was summarised for the Tram Project Board on 12th March 2008, which concluded that the outcome of the contractual negotiations was in line in all material respects with the Business Case which supported the selection of the Preferred Bidders in October 2007.

There have been further amendments to the contractual terms since that date but tie does not believe these would be contentious in the view of a bidder. In addition, a challenger would have difficulty establishing prejudice because these amendments are the outcome of the process transparently declared in the ITN as part of post preferred bidder sessions. This does not of itself support a conclusion that principal Infraco / Tramco terms are materially unchanged. However, these contracts represent the core of the project and the majority of the funding. Compliance of the final position with the business case is therefore valid and influential background.

Elapse of time

The considerable elapse of time since selection is an unhelpful factor as it is prima facie indicative of a lengthy period of post-selection negotiation. The reality has been that the delay and most of the effort since October 2007 has been caused by the difficulty of aligning the SDS provider with its novation responsibilities under their contract, coupled with the volume of work involved in the alignment of the SDS design with critical interface documents including the Employer's Requirements and the BBS Proposal. It is considered unlikely that selection of a different bidder would have reduced the time required to reach today's position. All bidders were on notice that SDS Novation was a prerequisite to completion. A draft Novation agreement was incorporated in the tender documents. Both bidders had quite significant commercial and contractual qualifications on their offers.

Price

In the period post the selection of preferred Infraco bidder, there has, as normal and expected, been movement in the commercial pricing of the contract based on a number of key drivers:

- Both parties in the preferred bidder review had lodged substantial and material qualifications to their bids and it was a key requirement in the ensuing months and prior to contract close that these were understood and resolved/removed, leading inevitably to change in contract terms.

- The substantial revision of the Employer's requirements, which are now at version 4.0 (Version 2.4 at conclusion of preferred bidder selection). These changes in requirements have been crystallised as both parties went through a process of harmonising and clarifying the requisite specifications. Included amongst these were the CEC's requirement for tapered poles in the heritage areas.

- Completion of further elements of the overall design which were not available at the time of the preferred bidder selection.

- Following the recognised changes to Employer Requirements and the completion and refinement of further aspects of the overall design, a review of the programme timescale has seen the programme move from delivery at the end of March 2011 to 16th July 2011 with concomitant effect on price.

- Review of the Depot equipment base with the TRAMCO preferred bidder has seen a number of changes to said base to assure compliance.

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Whilst the BBS price has been increased, in a directly comparative situation, the BBS relative competitive position remains the same as at preferred position. This is because the primary reasons for the price shift are not bidder specific. The detailed analysis is shown in the Appendix. Clearly, all of the price adjustments negotiated by BBS are under very different circumstances to those prior to preferred bidder as BBS's negotiating position strengthens.

Programme

The programme to project completion has moved out by c3 months from the basis on which selection was made. The primary reason for this is the same as that described under elapse of time above, which affects the anticipated commencement of construction. The construction programme itself has not materially extended. It is considered that the delayed commencement and completion dates would have similarly arisen with alternative bidders.

Risk profile

It would be normal to expect that the risk profile will change as contracts are concluded, but only to a marginal degree. This is the case for the Infraco / Tramco contracts and risk profile. One specific area requires more detailed assessment – the risks arising from the overlap of design and construction.

This was anticipated at the time of bidder selection, but the detailed mechanics of dealing with the issue have been developed since selection. The issue of overlap would almost certainly have arisen in the same form with any bidder and it is believed that the solution would have been similarly concluded. This covers both the legal process and protections and the management processes.

Contract security terms

These terms could be relevant if any changes implied that the perceived risk were materially different from the basis of selection.

In substance the only material change in security terms between Preferred Bidder stage and the final negotiated deal is that the previous 30% liability cap during the construction phase (with no performance bond) on Infraco is now a 20% liability cap plus two separate on-demand bonds of a further c25% which is over and above the liability cap – therefore amounting to the same cover. There have been alterations to the duration and function of the liability cap post-construction, but within acceptable bounds. All security terms have been negotiated and have emerged broadly within the range of expected market terms. The bonding support is on balance more advantageous to tie / CEC than might have been anticipated. The PCG arrangements are stated in acceptable terms but are complex and it is recognised that any material claim on these instruments will not be a straight-forward process.

Intimations

We have had no indications from any party that they are considering a challenge. Reaction to selection was normal although it should be noted that the losing bidder in Infraco has formally requested a de-brief and will take a close interest in the final terms of award, particularly final price, given the investment made in the bid process.

It is also worth noting that there may be a legal defect in the unsuccessful bidder's tender which would offer defensive material if a challenge is made although this has been explained by the bidder as a reaction to the PB deal they were asked to sign being incomplete. The issue is that tie does not have a valid Tramlines' committed commercial proposal on the same comparative basis as Tramlines because Tramlines refused to sign the draft deal document at the point of selection of preferred bidder.

DLA Letter

An accompanying letter from DLA provides their view of the content of this paper.

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tie considers that the conduct of the procurement process and the management of contract completion since selection of preferred bidders have been in line with procurement regulation. Should a challenge be made, tie would be in a strong position to resist successfully. Accordingly, there should be no concern about contract award.

tie Limited
12.05.08

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DETAILED ANALYSIS OF THE PROCUREMENT PROCESS APPENDIX 1

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This appendix sets out important detailed information on the background, processes and movements since the preferred bidder award. It is intended to provide the basis to refute any challenge, though focussed on the possibility of a challenge by the losing Infraco bidder Tramlines.

1. Preferred Bidder Decision Basis

Preferred bidder appointment was made in October 2007.

The decision to select BBS over Tramlines was based on the agreed award criteria. In summary:

- Price: On a fully normalised CAPEX comparison, BBS were £7.6m (4%) lower than Tramlines. This delta increased to £10m (5%) on a PV comparison.

- Programme and Project Execution: Both bids were similarly matched and acceptable to tie. In respect of programme, Tramlines were penalised for the degree of overlap with the MUDFA programme. Efforts to close this gap were unsuccessful.

- Legal and Commercial: BBS proposal contained fewer mark ups and was generally in a more more favourable position in respect of financial liability caps and latent defect periods. BBS showed a greater degree of flexibility and tractability compared to Tramlines.

- Technical: Both bidders were closely matched and were acceptable to tie. In view of its widespread application in Europe, BBS 'Sedra' trackform was generally preferred to Tramlines. BBS adopted a more competitive position in respect of NR immunisation which meant lower levels of residual risk for tie and a price reduction.

- Maintenance: Both proposals were similarly matched, but BBS was more competitive by some 16%. It was considered that BBS' overall approach arguably provided greater delivery certainty over Tramlines.

Both bidders negotiated a Draft Deal which consolidated their respective commercial and contractual positions and set out the basis for any future adjustments. Whilst BBS signed their agreement, Tramlines declined to sign. Importantly, this means that tie doesn't currently have a valid and confirmed Tramlines proposal against which we can compare.

2. Fixing the Price

Both bidders' civils' prices were based on the Preliminary Design prevailing at the time of the latter stages of the negotiated process. They were qualified accordingly with firm and provisional sums. The procurement strategy was based on re-measuring these price elements during the preferred bidder stage as designs were completed and prices adjusted at the declared rates from the Draft Deal.

After selection of BBS and the commencement of due diligence, a number of circumstances made it more difficult for BBS to firm up the provisional elements of their bid (structures, roads, pavings and drainage). These were:

- The SDS design was taking longer to be completed, and also being finished in a piecemeal fashion making it difficult to price.

- The design that was emerging contained a greater number of differences than anticipated at preliminary design stage (the BaFO datum) . For example structures and tram stops.

- BBS were not sufficiently resourced to quickly turn the emerging designs into quantities and prices. Other activities on the programme such as VE and due diligence distracted the team from the core pricing requirements.

The net affect of this was to frustrate tie's attempt to gain a greater 'fix' on the price and hence the budget in order to progress the FBC v2 approval with the Council and Transport Scotland. In response to this dilemma tie requested that BBS consider fixing their price.

Wiesbaden

Following protracted negotiations covering a range of contractual, technical and importantly commercial issues, BBS finally agreed to fix their price albeit with qualifications. This culminated in senior level negotiations in Wiesbaden and tie/BBS signing an agreement the following week (20 December 2007). In addition to fixing their price the deal also committed BBS to accepting a number of VE initiatives, again subject to a number of qualifications.

3. Closing negotiations and adjustments

Following the FBC approval milestone in December, both parties have since worked strenuously to close out all remaining aspects of the contract suite. The work has been extensive and required good faith negotiations to:

1. Finalise the remaining Contract terms
2. Deal with the CAF novation alignment issues
3. Deal with the SDS novation alignment issues
4. Finalise the Employers Requirements
5. Consolidate the BBS proposal
6. Ensure alignment with the SDS design

BBS have increasingly hardened their negotiation game as tie have approached specific procurement milestone dates. This is not untypical for contractors in this phase as their bargaining power increases considerably. In each case tie have pushed back and been prepared to move a milestone in order to get a better deal for tie/CEC.

During this period BBS have continued to reappraise their commercial position as more and more knowledge becomes available. They have now completed their due diligence on all aspects of the project. This has included ascertaining the quality of SDS outputs and gaps, the reliability of the design programme and a review of the design work and resources going forward. This due diligence has informed their negotiating stance in all regards and has remained at the top of their 'deal breaker' list.

In summary, areas where BBS have needed to move their commercial position are:

- Systems resources: BBS (Siemens) have re-evaluated the level of resources they would need to fill any gaps within the scope to ensure successful completion. Prior to preferred bidder tie encouraged both BBS and Tramlines to reduce their engineering resources on the grounds that SDS were carrying out these activities.

- SDS civils design quality: This is seen as a significant risk to BBS which in their view, could cause delay costs whilst designs are reworked.

- CAF alignment: in contract negotiations both CAF and BBS expressed concern that commercial alignment between the two contracts placed them both at risk. To the extent possible, these misalignments were remedied in each contract. However, some unforeseen alignment risks remained. BBS insisted on pricing the typical time impact of such risks as well covering with contingency sums which was negotiated done.

- Programme: This has moved 3 months, largely reflecting a longer than forecast close programme (+2 months) and the need to have complete acceptance by BBS, CAF, SDS and CEC of the design construction master programme.

- ER changes. Reasons include assumed VE changes that are now unacceptable, the Council's preference on equipment specifications (e.g. tapered poles) and the need for pricing of previously excluded items (e.g. Scottish Power breakers). In virtually every case Tramlines would have needed to revise their price in the same way that BBS have done.

4. Comparison between Preferred Bidder and Close position

Table 1 provides a summary comparison of BBS competitive position at time of preferred bidder with their position at today. It also indicates a hypothetical position from Tramlines based on the discussion above.

5. Conclusions from the detailed analysis in this Appendix

The evaluation decision at preferred bidder remains robust. Tramlines have few grounds for challenging the decision and the current financial close outcome. If they chose to do so, the arguments and adjudication would be complex, lengthy and in some cases subjective.

Whilst the BBS price has been increased, in a directly comparative situation, the BBS relative competitive position remains the same as at preferred position. This is because the primary reasons for the price shift are not bidder specific: the SDS design emerging with a higher specification and cost than at preliminary design (the BaFo price datum); the SDS due diligence findings including design quality, systems resources, gaps etc; contractual alignment issues with CAF; the time taken to close out the complex contract and novation process; and the many ER/ VE related changes. In virtually every case, Tramlines would have needed to increase their price on broadly the same basis as BBS.

In respect of the technical changes, the preferred bidder situation remains materially unaltered.

Contractually, there have been small movements which have may have arguably bought BBS and Tramlines closer together, but overall, the comparative situation remains similar. The principal contract changes in BBS position, relate to consents and approvals where tie/CEC are now accepting more risk. Here tie is confident Tramlines would have adopted a similar negotiating stance because they were similarly qualified at the time of preferred bidder.

Clearly, all of the recent price adjustments by BBS are under very different circumstances to those prior to preferred bidder. The closer tie get to financial close, the more difficult and costly it becomes for tie to revert to Tramlines. BBS are using this vast reduction in competitive pressure to their commercial advantage. Would Tramlines have been less aggressive, or priced changes more economically? The procurement team strongly believe that they would not. Indeed BBS' 'new entrant' position in the market suggests that relative to Tramlines they would be tactically more cautious, since a high profile failure at this stage would create large repercussions in the market. This would damage future prospects for BBS' target order book.

Today, tie does not have a valid Tramlines' committed commercial proposal on the same comparative basis as Tramlines. If they were today asked to sign the draft deal, there is no reason to suggest that the terms or price wouldn't increase reflecting the change in commercial circumstances.

Table 1 Summary comparison of BBS competitive position at time of preferred bidder with their position at today

Key BBS Differentiator	BBS Summary Shifts to Close	£M	Hypothetical Tramlines Position	Challenge risk?
PRICE Price was 4-10% lower	Wiesbaden Fixed Price including: Earthworks, Landscaping, Traffic Signals, Noise and Vibration, Tramstops, Balgreen Road Bridge. Subject to conditions.	+8	Increase relates to design completion risk and would have also been priced by Tramlines. The amount would have been based on negotiation tactics and judgement.	Unlikely
	VE acceptance (with conditions)	- (13.8)	It is uncertain that whether Tramlines have been as bullish in accepting this level of reductions.	No!
	Rutland Square CAF alignment risks	+0.5	Tramlines position on acceptance of CAF novation was the same at preferred bidder.	No
	SDS systems resources	+2.5	Tramlines were also pressurised by tie to remove systems resources. It is probable that Tramlines would do likewise.	No
	BBS resources to manage CAF	+0.8	It is unclear if Tramlines would have responded in this way.	Possible
	Brunel Price changes			
	ER's compliance	1.4	Mostly tie changes which were unagreed at preferred bidder.	No
	SDS civil's quality	2.8	Tramlines would have discovered similar issues (e.g earth works etc) which would have made them reluctant to accept novation related risks with price adjustment.	Unlikely
	Programme shift + 3 months	3.5	Mostly results from delays in closing. Unlikely that Tramlines would have closed more quickly. Tramlines may be probably more cautious.	No
	Tapered poles	0.9	Tramlines (likewise did not) propose these.	No

Key BBS Differentiator	BBS Summary Shifts to Close	Impact	Hypothetical Tramlines Position	Challenge risk?
Programme and Project Execution BBS Programme worked with few MUDFA clashes	Programme shift + 3 months	+ 3 months	Position could worsen because their proposal was poorer to start with. See comments above too.	No
Maintenance Price was ~16% lower	Price	Nil	No shift	No
Technical				
Trackform preferred	Rheda City now proposed (c.f Sedra)	Nil	No price impact. Tie still regard this as a more reliable Trackform than Tramlines proposal	No
NR Immunisation risks	Some attempt to shift position from that at PB	3m	Tramlines were considerably less competitive and would have been unlikely to have moved to the BBS position without greater competitive pressure.	Possible
Legal & Commercial	Attitude – has hardened as procurement milestones are approached.	Nil	Tramlines would have no doubt played a harder game as these same deadlines approach.	No
	Defect liability periods now reduced from 20 years.	12yrs	Tramlines offered a qualified 15 years considerably less competitive at the time and would have been unlikely to have moved to the BBS position without greater competitive pressure.	Possible
	Consents changes/ relations (partial risk shift to tie)		Consent was also qualified by Tramlines. Unlikely tie would end up in a better position with Tramlines.	No

EDINBURGH TRAM PROJECT
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Following the FBC approval milestone in December, both parties have since worked strenuously to close out all remaining aspects of the contract suite. The work has been extensive and required good faith negotiations to:

1. Finalise the remaining Contract terms
2. Deal with the CAF novation alignment issues
3. Deal with the SDS novation alignment issues
4. Finalise the Employers Requirements
5. Consolidate the BBS proposal
6. Ensure alignment with the SDS design

BBS have increasingly hardened their negotiation game as tie have approached specific procurement milestone dates. This is not untypical for contractors in this phase as their bargaining power increases considerably. In each case tie have pushed back and been prepared to move a milestone in order to get a better deal for tie/CEC.

During this period BBS have continued to reappraise their commercial position as more and more knowledge becomes available. They have now completed their due diligence on all aspects of the project. This has included ascertaining the quality of SDS outputs and gaps, the reliability of the design programme and a review of the design work and resources going forward. This due diligence has informed their negotiating stance in all regards and has remained at the top of their 'deal breaker' list.

In summary, areas where BBS have needed to move their commercial position are:

- Systems resources: BBS (Siemens) have re-evaluated the level of resources they would need to fill any gaps within the scope to ensure successful completion. Prior to preferred bidder tie encouraged both BBS and Tramlines to reduce their engineering resources on the grounds that SDS were carrying out these activities.

- SDS civils design quality: This is seen as a significant risk to BBS which in their view, could cause delay costs whilst designs are reworked.

- CAF alignment: in contract negotiations both CAF and BBS expressed concern that commercial alignment between the two contracts placed them both at risk. To the extent possible, these misalignments were remedied in each contract. However, some unforeseen alignment risks remained. BBS insisted on pricing the typical time impact of such risks as well covering with contingency sums which was negotiated done.

- Programme: This has moved 3 months, largely reflecting a longer than forecast close programme (+2 months) and the need to have complete acceptance by BBS, CAF, SDS and CEC of the design construction master programme.

- ER changes. Reasons include assumed VE changes that are now unacceptable, the Council's preference on equipment specifications (e.g. tapered poles) and the need for pricing of previously excluded items (e.g. Scottish Power breakers). In virtually every case Tramlines would have needed to revise their price in the same way that BBS have done.

4. Comparison between Preferred Bidder and Close position

Table 1 provides a summary comparison of BBS competitive position at time of preferred bidder with their position at today. It also indicates a hypothetical position from Tramlines based on the discussion above.

5. Conclusions from the detailed analysis in this Appendix

The evaluation decision at preferred bidder remains robust. Tramlines have few grounds for challenging the decision and the current financial close outcome. If they chose to do so, the arguments and adjudication would be complex, lengthy and in some cases subjective.

Whilst the BBS price has been increased, in a directly comparative situation, the BBS relative competitive position remains the same as at preferred position. This is because the primary reasons for the price shift are not bidder specific: the SDS design emerging with a higher specification and cost than at preliminary design (the BaFo price datum); the SDS due diligence findings including design quality, systems resources, gaps etc; contractual alignment issues with CAF; the time taken to close out the complex contract and novation process; and the many ER/ VE related changes. In virtually every case, Tramlines would have needed to increase their price on broadly the same basis as BBS.

In respect of the technical changes, the preferred bidder situation remains materially unaltered.

Contractually, there have been small movements which have may have arguably bought BBS and Tramlines closer together, but overall, the comparative situation remains similar. The principal contract changes in BBS position, relate to consents and approvals where tie/CEC are now accepting more risk. Here tie is confident Tramlines would have adopted a similar negotiating stance because they were similarly qualified at the time of preferred bidder.

Clearly, all of the recent price adjustments by BBS are under very different circumstances to those prior to preferred bidder. The closer tie get to financial close, the more difficult and costly it becomes for tie to revert to Tramlines. BBS are using this vast reduction in competitive pressure to their commercial advantage. Would Tramlines have been less aggressive, or priced changes more economically? The procurement team strongly believe that they would not. Indeed BBS' 'new entrant' position in the market suggests that relative to Tramlines they would be tactically more cautious, since a high profile failure at this stage would create large repercussions in the market. This would damage future prospects for BBS' target order book.

Today, tie does not have a valid Tramlines' committed commercial proposal on the same comparative basis as Tramlines. If they were today asked to sign the draft deal, there is no reason to suggest that the terms or price wouldn't increase reflecting the change in commercial circumstances.

Table 1 Summary comparison of BBS competitive position at time of preferred bidder with their position at today

Key BBS Differentiator	BBS Summary Shifts to Close	£M	Hypothetical Tramlines Position	Challenge risk?
PRICE Price was 4-10% lower	Wiesbaden Fixed Price including: Earthworks, Landscaping, Traffic Signals, Noise and Vibration, Tramstops, Balgreen Road Bridge. Subject to conditions.	+8	Increase relates to design completion risk and would have also been priced by Tramlines. The amount would have been based on negotiation tactics and judgement.	Unlikely
	VE acceptance (with conditions)	-(13.8)	It is uncertain that whether Tramlines have been as bullish in accepting this level of reductions.	No!
	Rutland Square CAF alignment risks	+0.5	Tramlines position on acceptance of CAF novation was the same at preferred bidder.	No
	SDS systems resources	+2.5	Tramlines were also pressurised by tie to remove systems resources. It is probable that Tramlines would do likewise.	No
	BBS resources to manage CAF	+0.8	It is unclear if Tramlines would have responded in this way.	Possible
	Brunel Price changes			
	ER's compliance	1.4	Mostly tie changes which were unagreed at preferred bidder.	No
	SDS civil's quality	2.8	Tramlines would have discovered similar issues (e.g earth works etc) which would have made them reluctant to accept novation related risks with price adjustment.	Unlikely
	Programme shift + 3 months	3.5	Mostly results from delays in closing. Unlikely that Tramlines would have closed more quickly. Tramlines may be probably more cautious.	No
	Tapered poles	0.9	Tramlines (likewise did not) propose these.	No

Key BBS Differentiator	BBS Summary Shifts to Close	Impact	Hypothetical Tramlines Position	Challenge risk?
Programme and Project Execution BBS Programme worked with few MUDFA clashes	Programme shift + 3 months	+ 3 months	Position could worsen because their proposal was poorer to start with. See comments above too.	No
Maintenance Price was ~16% lower	Price	Nil	No shift	No
Technical				
Trackform preferred	Rheda City now proposed (c.f Sedra)	Nil	No price impact. Tie still regard this as a more reliable Trackform than Tramlines proposal	No
NR Immunisation risks	Some attempt to shift position from that at PB	3m	Tramlines were considerably less competitive and would have been unlikely to have moved to the BBS position without greater competitive pressure.	Possible
Legal & Commercial	Attitude – has hardened as procurement milestones are approached.	Nil	Tramlines would have no doubt played a harder game as these same deadlines approach.	No
	Defect liability periods now reduced from 20 years.	12yrs	Tramlines offered a qualified 15 years considerably less competitive at the time and would have been unlikely to have moved to the BBS position without greater competitive pressure.	Possible
	Consents changes/ relations (partial risk shift to tie)		Consent was also qualified by Tramlines. Unlikely tie would end up in a better position with Tramlines.	No

EDINBURGH TRAM PROJECT
FINANCIAL CLOSE PROCESS AND RECORD OF RECENT EVENTS

COMMERCIAL – IN CONFIDENCE
EXEMPT FROM DISCLOSURE UNDER FOISA

Executive Summary

Since selection of the preferred bidders in October 2007, tie Limited has been involved in complex and lengthy negotiations with the bidding consortium to conclude the contractual arrangements for the delivery of the tram system. During this period, the governance machinery has been applied to ensure that the approval requirements of the Council are fulfilled.

Most recently, the Council received a report for its meeting on 1st May 2008 which described the progress made. The final contracts are now concluded and ready for signature. The final terms differ marginally from those anticipated in the recent report of £508.0m, with the capital cost now standing at £512.0m, a sum which remains well within the available funding of £545.0m.

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As was noted in the recent Council Report, underlying costs have been subject to the firming up of provisional prices to fixed sums, currency fluctuations and the crystallisation of the risk transfer to the private sector as described in the project's Final Business Case. The finalisation of the contracts required further amendment for similar reasons and supply chain pressure on the bidding consortium has been accommodated in the marginal increase over the most-recently reported cost estimate. Offsetting the increased cost is a range of negotiated improvements in favour of tie and the Council, in the areas of programme delay mitigation, cost exposure capping and more advantageous contractual positions.

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In addition and as is normal in these circumstances, there is an imperative to bring the contractual matters to an efficient near-term close in order to mitigate against potential cost exposure and programme delay, which could represent a material risk. Tie has recommended that the final terms negotiated represent the best result achievable for the public sector and that the council should authorise tie now to proceed with the contract close.

Tie Limited has maintained a focus on the competitiveness of the developing contract terms to ensure they remain best value and are fully aligned with relevant regulations. They have confirmed to Council officials that the final terms of the contract meet these parameters.

Works on utility diversion works continue on time and to budget. Works in Leith Walk are now coming to a close and earlier than planned completion is anticipated for the works in Shandwick Place. The construction programme for the tram system remains as previously reported with revenue service planned for July 2011.

(1) Background and record of events

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This document is intended to be an objective synopsis of the evolution of the Infraco contract suite negotiations in order to put on record in one place the key events and to support approval of the final negotiated position.

Preferred bidder selection, business case approval and Wiesbaden

BBS were appointed preferred Infraco bidder in October 2007 along with CAF as preferred Tramco bidder. The procurement process and evaluation was conducted under normal rules of public procurement and the appointment decisions were approved within the project governance structure.

In December 2007, the Final Business Case was approved by the Council and appropriate delegated authorities created to execute the project. A series of negotiations culminated in a meeting of senior representatives at Wiesbaden when the contract price was concluded within the business case budget of £498m, supporting revenue service in Spring 2011. This became known as "the Wiesbaden Agreement". The anticipation was that Close would be executed within a few weeks allowing for the Xmas break.

Continuing negotiations, Rutland Square and Award Notification

Negotiations in the period from October to December 2007 were conducted in a constructive if robust manner. However, from January 2008, it became increasingly concerning that the BBS consortium was operating in a manner which militated against an efficient Close. The behaviours included lack of competent senior commercial management involvement, leadership on commercial as well as legal issues by BBS's lawyers, lack of a cohesive approach between the consortium partners and their use of different law firms, consistent re-opening of apparently agreed positions and lack of focus on important matters in favour of volumes of detailed points.

A consistent additional problem was the under-performance and unhelpful approach of PB. This was critical as PB needed to enter into the tri-partite Novation of their design contract. CAF played a more constructive and passive role.

Extended negotiations took place in which the prevailing theme was the attempt by tie to remain close to the draft terms which supported preferred bidder selection in the face of attempts by BBS to improve their position. These negotiations led to a further summit meeting in March 2008, when a further series of lines were drawn. This "Rutland Square Agreement" included different (offsetting) cost and risk transfer terms which drove the overall cost to £508m. The delay in reaching close meant that revenue service could not now commence until July 2011. The negotiations at this stage were substantially driven by Siemens.

Both the Wiesbaden and Rutland Square Agreements were documented and signed by senior representatives of the parties. Tie proceeded to report to the Council that terms were agreed and that Notification of intent to award letters could be sent to the unsuccessful bidders. This was duly approved and the letters were issued on 18th March 2008. De-briefs with Tramlines and Alsthom were held in early April, which were based on the terms agreed at Rutland Square.

Period to Financial Close

Negotiations over detailed documentation continued, although BBS's approach continued to cause concern and delay. On 14th April, senior representatives of BB and S visited tie and marginal residual issues were agreed. The meeting concluded with confirmation that all terms were agreed and the final documents should proceed to final legal quality control and then signing on 2nd May.

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On 30th April 2008, in a telephone call to Willie Gallagher, BB (Richard Walker) requested a last minute and largely unsupported price increase of £12m. This was at the final point before the pre-agreed timing of contract approval for signature. No such request had emerged from Siemens or from CAF or indeed SDS. The anticipation had been that the contracts would be signed on 2nd May and a preparation period of 36 hours was needed.

An emergency meeting of those members of the Tram Project Board who were available plus tie / TEL / CEC representatives was held on 30th April. The options available were discussed and it was concluded that we should deploy tough tactics, but not stonewall the BB request completely as it was felt that the alternatives were likely to be worse notwithstanding the intense frustration at BB's tactics.

Final process

BB senior management visited Edinburgh on 5th May 2008, met by messrs Gallagher, Mackay and Bell. Their support for the price increase was sketchy and confused, focussing around an admitted failure on their part to assess or control their supply chain prices, £ / € movement and a claim for underwriting of central demobilisation cost which they had allocated to their bid for Phase 1B in the light of a more cautious view on the execution of 1B.

All signs pointed to last-minute unprofessional brinkmanship. BB claimed their costs were actually £17m wrong, but that they had reworked internally to arrive at £12m, casting further doubt on their credibility. There were veiled threats that failure to meet the demand now would force BBS to seek every opportunity to create claims during the construction period to achieve their financial target. As a matter of record, tie is comfortable with its contractual position and the experienced people recruited to manage the contract effectively.

The 5th May meeting culminated in a proposal from tie that tie would :

- Absorb £3m of additional cost in return for tangible contractual and risk improvements ;
- Agree to meet BBS allocated demobilisation costs of £3.2m in event that Phase 1B does not proceed

The BBS response on 6th May was disjointed (different responses from different senior people in the BB team). A series of meetings involving messrs Gallagher, Mackay, Bell, Fitchie and Bissett concluded that a formal latter to BBS in the form of an ultimatum was needed to bring matters to a close. In addition to the continuing delay and attendant costs, and the unpalatable alternatives to concluding with BBS, there were concerns that Siemens, CAF and PB may also seek price increases if BB were seen to be making inappropriate progress.

A letter was sent to BBS late on 6th May which reiterated the tie proposal described above. A response was received on 7th May which proposed :

- A payment of £9m to BBS
- Further examination of the contract terms surrounding the design management process, which although unclear pointed to an extended design and consent programme with potentially material adverse consequences for the construction programme.

The letter was silent on tie's contractual requirements.

A combined meeting of the TPB and tie Board was held (as scheduled) in the morning of 7th May. The meeting reviewed the position thoroughly and concluded that the approach which best protected the public sector's position would be to seek a conclusion with BBS within their demand for £12m.

Conclusion to negotiations

Further negotiations were conducted on 7th, 8th and 9th May and an acceptable conclusion reached. The final terms negotiated reflect agreement by tie to increased consideration and contingent cost underwriting in return for early progress to contract signing, improvement in terms and capping of cost exposures.

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The specific terms are as follows :

Financial amendments :

1. Incentivisation bonus – tie will pay a series of incentive bonus payments over the life of the contract on achievement of specified milestones. The aggregate cost will be £4.8m.

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2. Phase 1B cost allocation – tie will underwrite demobilisation costs allocated to Phase 1B in the BBS bid in the event that Phase 1B doesn't proceed. The quantum is £3.2m and this will not be paid if Phase 1B does proceed.

3. Loss reserve – tie has agreed to waive its interest in any residual value from the £3m BBS pot for settling uninsured third party economic and consequential loss claims. This is a theoretical concession of one-third of £3m but has never been accounted for in project cost estimates and is therefore neutral to tie.

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The incentivisation bonus should support programme adherence. In return for the financial amendments, tie has secured a range of improvements to the contract terms and risk profile. The elements of the aggregate risk contingency of £32m which are relevant to the improved position are :

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General programme delay	£6.6m
Delay due to design & consents	£3.3m
Contamination risk	£3.4m
Road reinstatement – direct costs	£2.0m

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1. Immediate contract close on preferred terms - all of tie's preferred positions in the Infraco contract which were under query by BBS and their lawyers would be accepted. As a consequence, the contract execution can proceed forthwith. The documents concluded include the Review and Design Management Plan arrangements which assist management of the design and consents risk and which carries a £3.3m allowance in the QRA. The attempt by BB to revise the design process in a manner which would have created delay was also successfully rebuffed. The early close also stifles extended legal and management costs which are a component of the £6.6m QRA allowance for overall programme delay. The running rate of management and legal costs is £0.8m per month, so a saving of £0.6m would arise over a 3 week period. The risk of any further price increases from the bidder side is also mitigated.

2. Elimination of risk of claims arising from works underway - closing out the Mobilisation and Advance Works Contract and waiving any entitlement to claims or relief gives tie a clean financial start to the contract management of the InfraCo contract. This creates an immediate forward-looking focus and the avoidance of difficulties in dealing with immediate claims, spurious or otherwise. Tie has not been notified of any claims to date, but there have been some difficulties in the early works which could have given rise to claims in the hands of a determined contractor. An outline might be in the range of £1.7m. This would be resisted, but the new agreement eliminates the risk.

3. Capping of road reinstatement cost exposure – for reasons that have been well-rehearsed previously, an exposure exists in relation to the roads reinstatement pricing assumption. The QRA allows for £2m above the bid price to cover the exposure. BBS have agreed to cap their claim under this heading at £1.5m resulting in a saving of £0.5m.

4. Capping of roads related prolongation – the consortium will take the risk on prolongation beyond 8 weeks enabling the contingency to be limited to that level and reducing the need for provision by £1.3m. Other improvements affecting contamination and design & consents risk are evaluated at £0.5m.

5. Entry of CAF into Consortium – while welcoming the entry of CAF into the consortium because of improved consortium cohesion, tie had concerns about the potential implications of aspects of the mechanism. BBS have now confirmed they will follow the terms requested by tie, removing excessive negotiation timescales and costs. Specifically, the terms of the BB and Siemens PCGs will be amended to reflect CAF's entry into the consortium, express amendments will be made to the two bonds provided by the BBS sureties and an additional indemnity up to £8m will be provided by BBS covering contingent adverse consequences of CAF joining the consortium (note this indemnity is over and above the full set of existing security arrangements). There is no change to the CEC guarantee in any respect but CEC will be requested confirm no objection to and knowledge of CAF's entry into the consortium in a letter.

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In summary, the late price pressure from Bilfinger Berger arising from their claimed supply chain pressure has been contained at £4.8m with a further agreement that tie will underwrite contingent 1B demobilisation costs of £3.2m if Phase 1B does not proceed with BBS. Some £4.6m of exposures have been removed acknowledging that their evaluation is judgemental. £0.5m is explicitly reflected in the QRA and can be reduced and the balance represents elements of the other provisions noted above. Tie recommends that c one-third of the remaining specific evaluated risk improvement be reflected in the risk contingency, reducing it by a further £1.3m. A range of additional unquantifiable exposures are also eliminated.

Although the funding challenge surrounding Phase 1B remains, there is an intention to pursue this aggressively, sustaining confidence that Phase 1B can be funded and delivered. The balance of evaluated risk improvement amounts to £2.8m which implicitly offsets the risk that the Phase 1B demobilisation payment should become due. It should be borne in mind that Phase 1B design costs of £3m sit outside the Phase 1A budget and other Phase 1B costs may be authorised before it is certain that the phase will proceed. It is therefore logical that the contingent demobilisation costs should be shown separate from the Phase 1A budget for consistency.

Finally, tie recommends that a general risk provision of £1m be included to provide a final level of cushion.

Taking all these matters together, the net result is that tie has negotiated a cash and contingent price amendment in favour of exposure elimination which substantially offsets the majority of the price amendment. tie would recommend that the budget be increased to accommodate the agreed cash amendment of £4.8m ; and that the risk contingency be reduced by a total of £1.8m reflecting a conservative portion of the improved specific risk positions, then augmented by an increased general provision of £1.0m resulting in a net increase to the headline budget of £4.0m. This will result in the overall budget moving from £508m to £512.0m. The underlying base cost is now £480.8m and the risk contingency is £31.2m. Although a case could be made for further reduction in the risk contingency, it would be tie's recommendation that the balance be retained.

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(2) Alternative approaches

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The last minute demand by BBS was the worst form of unprofessional negotiating conduct. However, an evaluation of tie's alternatives concluded that there was no commercial alternative which would better protect the public sector's interests. The evaluation was performed with input from DLA.

A summary of the alternatives is as follows :

A. Siemens to restructure consortium by incorporating a new civils contractor
B. Tramlines re-introduced
C. Full-scale re-procurement
D. Project termination

Tie would have been entitled to terminate the BBS consortium's preferred bidder status because BBS were seeking to materially change the price.

(A) Siemens led consortium

The process would involve :

- Siemens exiting BB from the consortium
- Identification and presentation by Siemens of a new consortium
- Re-qualification by tie of the new consortium
- Re-engagement on the contract suite

The implications included :

- The timescale is likely to be around +3 months if matters progressed reasonably well. Programme will move out by this extent.
- There will be important changes to the current Infraco contract terms to accommodate 1) passage of time (eg programme, design & consents, MUDFA interface) ; 2) requirements of new contractor (unknown).
- No guarantee that the revised consortium would adhere to previous deal and a strong likelihood that both consortium members would seek increments for inflation and other factors
- Probable need to re-assess SDS Novation Agreement (driven by SDS)
- Presumption that CAF will happily go along with this and not seek incremental costs

Although unpalatable, this was the best alternative to completion with BBS and we could reasonably expect both CEC and TS to be supportive given the level of investment already made.

A financial evaluation pointed to cost risk of c£9m but with material risk to the downside.

(B) Reintroduce Tramlines

Tramlines were an entirely credible partner and the preferred bidder decision was close. There were no knock-out defects in the Tramlines bid. However, Tramlines have recently won the Manchester extension work and may not have been willing or able to execute Edinburgh simultaneously.

The process would best involve :

- Tie terminating BBS
- Tie revising the original Tramlines contract to accommodate tie's preferred (and reasonable) position as reflected in the current Infraco contract, but with all undesirable concessions removed
- Agree a one-month "hot review" by Tramlines to confirm all material contract terms or flag variations ; if parties in the same ballpark -
- Finalise all material terms

The implications included :

- The timescale is likely to be around +6 months if matters progressed reasonably well. Programme will move out by this extent.
- There will be important changes to the current Infraco contract terms to accommodate 1) passage of time (eg programme, design & consents, MUDFA interface) ; 2) requirements of Tramlines (unknown)
- Introduction of entire Tramlines Proposal replacing BBS's version and need to align with design and ER's
- Loss of other advantages perceived to be in BBS proposal which supported their selection as preferred bidder.
- No guarantee that Tramlines would adhere to previous deal and a strong likelihood that they will require increments for inflation and other factors ;
- Probable need to re-assess SDS Novation Agreement (driven by SDS)
- Presumption that CAF will happily go along with this and not seek incremental costs

A financial evaluation pointed to cost risk of c£22m but with material risk to the downside.

(C) Full re-procurement

This is the worst-case alternative short of termination. The procurement programme would extend out to around +1 year, adverse programme and cost ramifications are inevitable and it may be difficult to generate sufficient market interest from the limited number of possible players, including those rejected under the current procurement programme. Notwithstanding the extent of public investment already made, it is highly questionable whether the public pound is best protected by embarking on an immediate full-scale re-procurement. CEC and TS's support for this approach is unlikely.

A financial evaluation pointed to cost risk of c£28m but with material risk to the downside.

Recommendation

A range of second order issues was identified, further reinforcing the relative unattractiveness of the alternative options. Over and above all of the analysis, is the loss of revenues from delayed service commencement and the delayed flow of economic benefit.

Against this background, tie's rationale for supporting the final deal is set out below.

- The late price pressure from Bilfinger Berger arising from their claimed supply chain pressure has been contained at £4.8m. Some £4.6m of specific exposures have been removed, of which £1.8m is explicitly reflected in the QRA. The balance relates to general programme risk and other factors reflected in the QRA and which are prudently retained as risk provision. A further £1m has been added as a general risk contingency. A range of additional unquantifiable exposures are also eliminated.

- If Phase 1B proceeds there is no exposure to the £3.2m demobilisation payment; if 1B doesn't proceed the payment will become a real cost, in line with a principle already established. Some Phase 1B sunk costs (management and legal) are absorbed by the Phase 1A budget, but others (design costs of £3m by 31 March 2008 and potentially utilities works) are not incorporated into the capex budget for Phase 1A. The demobilisation costs would be an extension of the latter category. Although the funding challenge surrounding Phase 1B remains, there is an intention to pursue this aggressively, sustaining confidence that Phase 1B can be funded and delivered.

- There is substantial, if unquantifiable, benefit in enabling the contracts to be signed in the near term.

- Alternative options exist but are highly risky in programme and cost terms.

Accordingly, it was tie's recommendation that the deal be concluded with BBS.

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(3) Procurement regulation compliance

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In addition to the commercial and public pound considerations described above, it was necessary to assess whether the conclusion to the negotiations was in compliance with procurement regulation and in particular whether there could be credible grounds for a challenge.

The threat of a challenge arises from under-bidders but also from any interested third party. The latter can never be discounted and the question then becomes whether there are credible grounds for challenge which an investigating body could found on.

In support of the Rutland Square deal which resulted in a revised budget of £508m and the issue of the Notification letters, tie performed a detailed evaluation of the risk of a challenge by the under-bidders. This included the examination of the movement since preferred bidder selection and a shadow comparison of the under-bidder's position. The conclusion was that there was no basis for a credible challenge. This was documented and was the subject of review for legal validity by DLA.

The Notification letter to Tramlines highlighted the following differentials in BBS' favour:

- Capex assessed at 4% lower
- Programme shorter due to MUDFA overlap
- Stronger financial liability caps
- Approach to Network Rail immunisation and lower public sector risk
- Maintenance costs lower by 16%

In addition, although not mentioned in the letter, the assessment highlighted the BBS trackform construction as being materially better. The assessment noted that the fully-normalised capital cost difference at the time of preferred bidder selection was c£8m in favour of BBS. The analysis of changes since selection identified that a small percentage of the differential could be challenged based on the changes.

The final deal is described above. The incentivisation bonus of £4.8m is substantially offset by £4.6m of evaluated risk improvement. Although not all of this is reflected in a reduced final risk contingency, the full quantum is relevant to the assessment of the bid value. The contingent nature of the Phase 1B demobilisation cost makes it difficult to evaluate in this context, but even if full allowance were made for the £3.2m payment, there would remain price headroom in favour of BBS. The other advantages of the BBS bid – programme, liability caps, technical (trackform and approach to NR immunisation), lower maintenance costs - would sustain their preferred position.

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Accordingly, it is not proposed that any further communication be made to the under-bidders.

The entry of CAF into the consortium after the conclusion of matters with BBS was anticipated at the time of the preferred bidder selection and would be as likely to be beneficial to Tramlines as BBS.

In summary, the final negotiated changes imposed by BBS, although unwelcome, do not constitute a credible basis for procurement challenge.

(4) Future relationship with BBS and contract management

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The final matter addressed by tie and discussed at the TPB / tie Boards on 7th May 2008 is the suitability of BBS as a contract partner in view of their behaviour during the negotiations. There are three reasons why this concern should not be a barrier to entering into the contracts :

1. Tie has established a strong commercial team to manage the contract obligations and risks. These experienced operators have had a lengthy period to familiarise themselves with the contract and to anticipate where and how disputes may arise in future.

2. Tie will have the strength of the contract terms as support in future disputes, which will provide a considerably stronger defence against unsupportable positions taken by BBS; in addition, tie is in position to pursue recompense against BBS under the contract, where no such leverage exists pre-Close

3. A considerable degree of uncertainty currently arises from the activities of SDS, which will become much less of a feature after 3-4 months once all design work is complete.

A fourth reason is that BBS is the devil tie knows, there is no guarantee that other contractors would be a more amenable partner.

(5) Conclusion

The process to reach Financial Close has been tortuous and a partnerial approach from BBS has been notable by its absence. However, the final terms are within 2.8% of the business case budget of £498m and 0.8% of the budget most recently notified to the Council.

The programme points to a construction period some 3 months longer than the 39 months envisaged in the business case. The project risk profile remains broadly in balance with the business case and the scope of works is unchanged.

On this basis tie recommends that Close be executed.

tie Limited
12.05.08

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DLA (Andrew Fitchie)¶
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EDINBURGH TRAM PROJECT
FINANCIAL CLOSE PROCESS AND RECORD OF RECENT EVENTS

COMMERCIAL – IN CONFIDENCE
EXEMPT FROM DISCLOSURE UNDER FOISA

Executive Summary

Since selection of the preferred bidders in October 2007, tie Limited has been involved in complex and lengthy negotiations with the bidding consortium to conclude the contractual arrangements for the delivery of the tram system. During this period, the governance machinery has been applied to ensure that the approval requirements of the Council are fulfilled.

Most recently, the Council received a report for its meeting on 1st May 2008 which described the progress made. The final contracts are now concluded and ready for signature. The final terms differ marginally from those anticipated in the recent report of £508.0m, with the capital cost now standing at £512.0m, a sum which remains well within the available funding of £545.0m.

As was noted in the recent Council Report, underlying costs have been subject to the firming up of provisional prices to fixed sums, currency fluctuations and the crystallisation of the risk transfer to the private sector as described in the project's Final Business Case. The finalisation of the contracts required further amendment for similar reasons and supply chain pressure on the bidding consortium has been accommodated in the marginal increase over the most-recently reported cost estimate. Offsetting the increased cost is a range of negotiated improvements in favour of tie and the Council, in the areas of programme delay mitigation, cost exposure capping and more advantageous contractual positions.

In addition and as is normal in these circumstances, there is an imperative to bring the contractual matters to an efficient near-term close in order to mitigate against potential cost exposure and programme delay, which could represent a material risk. Tie has recommended that the final terms negotiated represent the best result achievable for the public sector and that the council should authorise tie now to proceed with the contract close.

Tie Limited has maintained a focus on the competitiveness of the developing contract terms to ensure they remain best value and are fully aligned with relevant regulations. They have confirmed to Council officials that the final terms of the contract meet these parameters.

Works on utility diversion works continue on time and to budget. Works in Leith Walk are now coming to a close and earlier than planned completion is anticipated for the works in Shandwick Place. The construction programme for the tram system remains as previously reported with revenue service planned for July 2011.

(1) Background and record of events

This document is intended to be an objective synopsis of the evolution of the Infraco contract suite negotiations in order to put on record in one place the key events and to support approval of the final negotiated position.

Preferred bidder selection, business case approval and Wiesbaden

BBS were appointed preferred Infraco bidder in October 2007 along with CAF as preferred Tramco bidder. The procurement process and evaluation was conducted under normal rules of public procurement and the appointment decisions were approved within the project governance structure.

In December 2007, the Final Business Case was approved by the Council and appropriate delegated authorities created to execute the project. A series of negotiations culminated in a meeting of senior representatives at Wiesbaden when the contract price was concluded within the business case budget of £498m, supporting revenue service in Spring 2011. This became known as "the Wiesbaden Agreement". The anticipation was that Close would be executed within a few weeks allowing for the Xmas break.

Continuing negotiations, Rutland Square and Award Notification

Negotiations in the period from October to December 2007 were conducted in a constructive if robust manner. However, from January 2008, it became increasingly concerning that the BBS consortium was operating in a manner which militated against an efficient Close. The behaviours included lack of competent senior commercial management involvement, leadership on commercial as well as legal issues by BBS's lawyers, lack of a cohesive approach between the consortium partners and their use of different law firms, consistent re-opening of apparently agreed positions and lack of focus on important matters in favour of volumes of detailed points.

A consistent additional problem was the under-performance and unhelpful approach of PB. This was critical as PB needed to enter into the tri-partite Novation of their design contract. CAF played a more constructive and passive role.

Extended negotiations took place in which the prevailing theme was the attempt by tie to remain close to the draft terms which supported preferred bidder selection in the face of attempts by BBS to improve their position. These negotiations led to a further summit meeting in March 2008, when a further series of lines were drawn. This "Rutland Square Agreement" included different (offsetting) cost and risk transfer terms which drove the overall cost to £508m. The delay in reaching close meant that revenue service could not now commence until July 2011. The negotiations at this stage were substantially driven by Siemens.

Both the Wiesbaden and Rutland Square Agreements were documented and signed by senior representatives of the parties. Tie proceeded to report to the Council that terms were agreed and that Notification of intent to award letters could be sent to the unsuccessful bidders. This was duly approved and the letters were issued on 18th March 2008. De-briefs with Tramlines and Alsthom were held in early April, which were based on the terms agreed at Rutland Square.

Period to Financial Close

Negotiations over detailed documentation continued, although BBS's approach continued to cause concern and delay. On 14th April, senior representatives of BB and S visited tie and marginal residual issues were agreed. The meeting concluded with confirmation that all terms were agreed and the final documents should proceed to final legal quality control and then signing on 2nd May.

On 30th April 2008, in a telephone call to Willie Gallagher, BB (Richard Walker) requested a last minute and largely unsupported price increase of £12m. This was at the final point before the pre-agreed timing of contract approval for signature. No such request had emerged from Siemens or from CAF or indeed SDS. The anticipation had been that the contracts would be signed on 2nd May and a preparation period of 36 hours was needed.

An emergency meeting of those members of the Tram Project Board who were available plus tie / TEL / CEC representatives was held on 30th April. The options available were discussed and it was concluded that we should deploy tough tactics, but not stonewall the BB request completely as it was felt that the alternatives were likely to be worse notwithstanding the intense frustration at BB's tactics.

Final process

BB senior management visited Edinburgh on 5th May 2008, met by messrs Gallagher, Mackay and Bell. Their support for the price increase was sketchy and confused, focussing around an admitted failure on their part to assess or control their supply chain prices, £ / € movement and a claim for underwriting of central demobilisation cost which they had allocated to their bid for Phase 1B in the light of a more cautious view on the execution of 1B.

All signs pointed to last-minute unprofessional brinkmanship. BB claimed their costs were actually £17m wrong, but that they had reworked internally to arrive at £12m, casting further doubt on their credibility. There were veiled threats that failure to meet the demand now would force BBS to seek every opportunity to create claims during the construction period to achieve their financial target. As a matter of record, tie is comfortable with its contractual position and the experienced people recruited to manage the contract effectively.

The 5th May meeting culminated in a proposal from tie that tie would :

- Absorb £3m of additional cost in return for tangible contractual and risk improvements ;
- Agree to meet BBS allocated demobilisation costs of £3.2m in event that Phase 1B does not proceed

The BBS response on 6th May was disjointed (different responses from different senior people in the BB team). A series of meetings involving messrs Gallagher, Mackay, Bell, Fitchie and Bissett concluded that a formal latter to BBS in the form of an ultimatum was needed to bring matters to a close. In addition to the continuing delay and attendant costs, and the unpalatable alternatives to concluding with BBS, there were concerns that Siemens, CAF and PB may also seek price increases if BB were seen to be making inappropriate progress.

A letter was sent to BBS late on 6th May which reiterated the tie proposal described above. A response was received on 7th May which proposed :

- A payment of £9m to BBS
- Further examination of the contract terms surrounding the design management process, which although unclear pointed to an extended design and consent programme with potentially material adverse consequences for the construction programme.

The letter was silent on tie's contractual requirements.

A combined meeting of the TPB and tie Board was held (as scheduled) in the morning of 7th May. The meeting reviewed the position thoroughly and concluded that the approach which best protected the public sector's position would be to seek a conclusion with BBS within their demand for £12m.

Conclusion to negotiations

Further negotiations were conducted on 7th, 8th and 9th May and an acceptable conclusion reached. The final terms negotiated reflect agreement by tie to increased consideration and contingent cost underwriting in return for early progress to contract signing, improvement in terms and capping of cost exposures.

The specific terms are as follows :

Financial amendments :

1. Incentivisation bonus – tie will pay a series of incentive bonus payments over the life of the contract on achievement of specified milestones. The aggregate cost will be £4.8m.

2. Phase 1B cost allocation – tie will underwrite demobilisation costs allocated to Phase 1B in the BBS bid in the event that Phase 1B doesn't proceed. The quantum is £3.2m and this will not be paid if Phase 1B does proceed.

3. Loss reserve – tie has agreed to waive its interest in any residual value from the £3m BBS pot for settling uninsured third party economic and consequential loss claims. This is a theoretical concession of one-third of £3m but has never been accounted for in project cost estimates and is therefore neutral to tie.

The incentivisation bonus should support programme adherence. In return for the financial amendments, tie has secured a range of improvements to the contract terms and risk profile. The elements of the aggregate risk contingency of £32m which are relevant to the improved position are :

General programme delay	£6.6m
Delay due to design & consents	£3.3m
Contamination risk	£3.4m
Road reinstatement – direct costs	£2.0m

1. Immediate contract close on preferred terms - all of tie's preferred positions in the Infraco contract which were under query by BBS and their lawyers would be accepted. As a consequence, the contract execution can proceed forthwith. The documents concluded include the Review and Design Management Plan arrangements which assist management of the design and consents risk and which carries a £3.3m allowance in the QRA. The attempt by BB to revise the design process in a manner which would have created delay was also successfully rebuffed. The early close also stifles extended legal and management costs which are a component of the £6.6m QRA allowance for overall programme delay. The running rate of management and legal costs is £0.8m per month, so a saving of £0.6m would arise over a 3 week period. The risk of any further price increases from the bidder side is also mitigated.

2. Elimination of risk of claims arising from works underway - closing out the Mobilisation and Advance Works Contract and waiving any entitlement to claims or relief gives tie a clean financial start to the contract management of the InfraCo contract. This creates an immediate forward-looking focus and the avoidance of difficulties in dealing with immediate claims, spurious or otherwise. Tie has not been notified of any claims to date, but there have been some difficulties in the early works which could have given rise to claims in the hands of a determined contractor. An outline might be in the range of £1.7m. This would be resisted, but the new agreement eliminates the risk.

3. Capping of road reinstatement cost exposure – for reasons that have been well-rehearsed previously, an exposure exists in relation to the roads reinstatement pricing assumption. The QRA allows for £2m above the bid price to cover the exposure. BBS have agreed to cap their claim under this heading at £1.5m resulting in a saving of £0.5m.

4. Capping of roads related prolongation – the consortium will take the risk on prolongation beyond 8 weeks enabling the contingency to be limited to that level and reducing the need for provision by £1.3m. Other improvements affecting contamination and design & consents risk are evaluated at £0.5m.

5. Entry of CAF into Consortium – while welcoming the entry of CAF into the consortium because of improved consortium cohesion, tie had concerns about the potential implications of aspects of the mechanism. BBS have now confirmed they will follow the terms requested by tie, removing excessive negotiation timescales and costs. Specifically, the terms of the BB and Siemens PCGs will be amended to reflect CAF's entry into the consortium, express amendments will be made to the two bonds provided by the BBS sureties and an additional indemnity up to £8m will be provided by BBS covering contingent adverse consequences of CAF joining the consortium (note this indemnity is over and above the full set of existing security arrangements). There is no change to the CEC guarantee in any respect but CEC will be requested confirm no objection to and knowledge of CAF's entry into the consortium in a letter.

In summary, the late price pressure from Bilfinger Berger arising from their claimed supply chain pressure has been contained at £4.8m with a further agreement that tie will underwrite contingent 1B demobilisation costs of £3.2m if Phase 1B does not proceed with BBS. Some £4.6m of exposures have been removed acknowledging that their evaluation is judgemental. £0.5m is explicitly reflected in the QRA and can be reduced and the balance represents elements of the other provisions noted above. Tie recommends that c one-third of the remaining specific evaluated risk improvement be reflected in the risk contingency, reducing it by a further £1.3m. A range of additional unquantifiable exposures are also eliminated.

Although the funding challenge surrounding Phase 1B remains, there is an intention to pursue this aggressively, sustaining confidence that Phase 1B can be funded and delivered. The balance of evaluated risk improvement amounts to £2.8m which implicitly offsets the risk that the Phase 1B demobilisation payment should become due. It should be borne in mind that Phase 1B design costs of £3m sit outside the Phase 1A budget and other Phase 1B costs may be authorised before it is certain that the phase will proceed. It is therefore logical that the contingent demobilisation costs should be shown separate from the Phase 1A budget for consistency.

Finally, tie recommends that a general risk provision of £1m be included to provide a final level of cushion.

Taking all these matters together, the net result is that tie has negotiated a cash and contingent price amendment in favour of exposure elimination which substantially offsets the majority of the price amendment. tie would recommend that the budget be increased to accommodate the agreed cash amendment of £4.8m ; and that the risk contingency be reduced by a total of £1.8m reflecting a conservative portion of the improved specific risk positions, then augmented by an increased general provision of £1.0m resulting in a net increase to the headline budget of £4.0m. This will result in the overall budget moving from £508m to £512.0m. The underlying base cost is now £480.8m and the risk contingency is £31.2m. Although a case could be made for further reduction in the risk contingency, it would be tie's recommendation that the balance be retained.

(2) Alternative approaches

The last minute demand by BBS was the worst form of unprofessional negotiating conduct. However, an evaluation of tie's alternatives concluded that there was no commercial alternative which would better protect the public sector's interests. The evaluation was performed with input from DLA.

A summary of the alternatives is as follows :

A. Siemens to restructure consortium by incorporating a new civils contractor
B. Tramlines re-introduced
C. Full-scale re-procurement
D. Project termination

Tie would have been entitled to terminate the BBS consortium's preferred bidder status because BBS were seeking to materially change the price.

(A) Siemens led consortium

The process would involve :

- Siemens exiting BB from the consortium
- Identification and presentation by Siemens of a new consortium
- Re-qualification by tie of the new consortium
- Re-engagement on the contract suite

The implications included :

- The timescale is likely to be around +3 months if matters progressed reasonably well. Programme will move out by this extent.
- There will be important changes to the current Infraco contract terms to accommodate 1) passage of time (eg programme, design & consents, MUDFA interface) ; 2) requirements of new contractor (unknown).
- No guarantee that the revised consortium would adhere to previous deal and a strong likelihood that both consortium members would seek increments for inflation and other factors
- Probable need to re-assess SDS Novation Agreement (driven by SDS)
- Presumption that CAF will happily go along with this and not seek incremental costs

Although unpalatable, this was the best alternative to completion with BBS and we could reasonably expect both CEC and TS to be supportive given the level of investment already made.

A financial evaluation pointed to cost risk of c£9m but with material risk to the downside.

(B) Reintroduce Tramlines

Tramlines were an entirely credible partner and the preferred bidder decision was close. There were no knock-out defects in the Tramlines bid. However, Tramlines have recently won the Manchester extension work and may not have been willing or able to execute Edinburgh simultaneously.

The process would best involve :

- Tie terminating BBS
- Tie revising the original Tramlines contract to accommodate tie's preferred (and reasonable) position as reflected in the current Infraco contract, but with all undesirable concessions removed
- Agree a one-month "hot review" by Tramlines to confirm all material contract terms or flag variations ; if parties in the same ballpark -
- Finalise all material terms

The implications included :

- The timescale is likely to be around +6 months if matters progressed reasonably well. Programme will move out by this extent.
- There will be important changes to the current Infraco contract terms to accommodate 1) passage of time (eg programme, design & consents, MUDFA interface) ; 2) requirements of Tramlines (unknown)
- Introduction of entire Tramlines Proposal replacing BBS's version and need to align with design and ER's
- Loss of other advantages perceived to be in BBS proposal which supported their selection as preferred bidder.
- No guarantee that Tramlines would adhere to previous deal and a strong likelihood that they will require increments for inflation and other factors ;
- Probable need to re-assess SDS Novation Agreement (driven by SDS)
- Presumption that CAF will happily go along with this and not seek incremental costs

A financial evaluation pointed to cost risk of c£22m but with material risk to the downside.

(C) Full re-procurement

This is the worst-case alternative short of termination. The procurement programme would extend out to around +1 year, adverse programme and cost ramifications are inevitable and it may be difficult to generate sufficient market interest from the limited number of possible players, including those rejected under the current procurement programme. Notwithstanding the extent of public investment already made, it is highly questionable whether the public pound is best protected by embarking on an immediate full-scale re-procurement. CEC and TS's support for this approach is unlikely.

A financial evaluation pointed to cost risk of c£28m but with material risk to the downside.

Recommendation

A range of second order issues was identified, further reinforcing the relative unattractiveness of the alternative options. Over and above all of the analysis, is the loss of revenues from delayed service commencement and the delayed flow of economic benefit.

Against this background, tie's rationale for supporting the final deal is set out below.

- The late price pressure from Bilfinger Berger arising from their claimed supply chain pressure has been contained at £4.8m. Some £4.6m of specific exposures have been removed, of which £1.8m is explicitly reflected in the QRA. The balance relates to general programme risk and other factors reflected in the QRA and which are prudently retained as risk provision. A further £1m has been added as a general risk contingency. A range of additional unquantifiable exposures are also eliminated.

- If Phase 1B proceeds there is no exposure to the £3.2m demobilisation payment; if 1B doesn't proceed the payment will become a real cost, in line with a principle already established. Some Phase 1B sunk costs (management and legal) are absorbed by the Phase 1A budget, but others (design costs of £3m by 31 March 2008 and potentially utilities works) are not incorporated into the capex budget for Phase 1A. The demobilisation costs would be an extension of the latter category. Although the funding challenge surrounding Phase 1B remains, there is an intention to pursue this aggressively, sustaining confidence that Phase 1B can be funded and delivered.

- There is substantial, if unquantifiable, benefit in enabling the contracts to be signed in the near term.

- Alternative options exist but are highly risky in programme and cost terms.

Accordingly, it was tie's recommendation that the deal be concluded with BBS.

(3) Procurement regulation compliance

In addition to the commercial and public pound considerations described above, it was necessary to assess whether the conclusion to the negotiations was in compliance with procurement regulation and in particular whether there could be credible grounds for a challenge.

The threat of a challenge arises from under-bidders but also from any interested third party. The latter can never be discounted and the question then becomes whether there are credible grounds for challenge which an investigating body could found on.

In support of the Rutland Square deal which resulted in a revised budget of £508m and the issue of the Notification letters, tie performed a detailed evaluation of the risk of a challenge by the under-bidders. This included the examination of the movement since preferred bidder selection and a shadow comparison of the under-bidder's position. The conclusion was that there was no basis for a credible challenge. This was documented and was the subject of review for legal validity by DLA.

The Notification letter to Tramlines highlighted the following differentials in BBS' favour:

- Capex assessed at 4% lower
- Programme shorter due to MUDFA overlap
- Stronger financial liability caps
- Approach to Network Rail immunisation and lower public sector risk
- Maintenance costs lower by 16%

In addition, although not mentioned in the letter, the assessment highlighted the BBS trackform construction as being materially better. The assessment noted that the fully-normalised capital cost difference at the time of preferred bidder selection was c£8m in favour of BBS. The analysis of changes since selection identified that a small percentage of the differential could be challenged based on the changes.

The final deal is described above. The incentivisation bonus of £4.8m is substantially offset by £4.6m of evaluated risk improvement. Although not all of this is reflected in a reduced final risk contingency, the full quantum is relevant to the assessment of the bid value. The contingent nature of the Phase 1B demobilisation cost makes it difficult to evaluate in this context, but even if full allowance were made for the £3.2m payment, there would remain price headroom in favour of BBS. The other advantages of the BBS bid – programme, liability caps, technical (trackform and approach to NR immunisation), lower maintenance costs - would sustain their preferred position.

Accordingly, it is not proposed that any further communication be made to the under-bidders.

The entry of CAF into the consortium after the conclusion of matters with BBS was anticipated at the time of the preferred bidder selection and would be as likely to be beneficial to Tramlines as BBS.

In summary, the final negotiated changes imposed by BBS, although unwelcome, do not constitute a credible basis for procurement challenge.

(4) Future relationship with BBS and contract management

The final matter addressed by tie and discussed at the TPB / tie Boards on 7th May 2008 is the suitability of BBS as a contract partner in view of their behaviour during the negotiations. There are three reasons why this concern should not be a barrier to entering into the contracts :

1. Tie has established a strong commercial team to manage the contract obligations and risks. These experienced operators have had a lengthy period to familiarise themselves with the contract and to anticipate where and how disputes may arise in future.

2. Tie will have the strength of the contract terms as support in future disputes, which will provide a considerably stronger defence against unsupportable positions taken by BBS; in addition, tie is in position to pursue recompense against BBS under the contract, where no such leverage exists pre-Close

3. A considerable degree of uncertainty currently arises from the activities of SDS, which will become much less of a feature after 3-4 months once all design work is complete.

A fourth reason is that BBS is the devil tie knows, there is no guarantee that other contractors would be a more amenable partner.

(5) Conclusion

The process to reach Financial Close has been tortuous and a partnerial approach from BBS has been notable by its absence. However, the final terms are within 2.8% of the business case budget of £498m and 0.8% of the budget most recently notified to the Council.

The programme points to a construction period some 3 months longer than the 39 months envisaged in the business case. The project risk profile remains broadly in balance with the business case and the scope of works is unchanged.

On this basis tie recommends that Close be executed.

tie Limited
12.05.08

EDINBURGH TRAM PROJECT
REPORT ON TERMS OF FINANCIAL CLOSE ("CLOSE REPORT")

FOR THE ATTENTION OF THE TRAM PROJECT BOARD, TEL BOARD AND TIE BOARD

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Purpose of report

The principal contractual commitments to be entered into at Financial Close are :

- Infraco Contract Suite – incorporating Infraco and Tramco construction / supply and maintenance ; Tramco and SDS Novation ; security documentation ; ancillary agreements and schedules including Employer's Requirements. A comprehensive list of the documents to be entered into by tie is included as an Appendix to this report
- Council Financial Guarantee
- Grant Award Letter
- Operating Agreements between the Council and respectively tie and TEL

Various important agreements with third parties have also been completed or are in substantially agreed form.

Two documents have been prepared to provide a comprehensive view of the principal terms of the contracts and related documents which are being committed to at Close. This report from tie provides information across a number of key areas. A parallel report from DLA, with supporting papers from tie, covers the content of the Infraco contract suite including the legal underpinning to the final contract positions, addressing specific CEC concerns. The DLA Report is a separate document in order to protect the confidentiality of the legal advice offered to tie and CEC. Specific issues of interest to CEC are addressed in each document.

A reasonable degree of prior knowledge is assumed. A draft version was reviewed at the meetings of the TPB, tie Board and TEL Board on 23rd January 2008 and the approvals below were granted on that date. The delegated structure has been implemented.

It is understood that the Council will prepare appropriate papers for its own approval purposes, specifically to support the provision of delegated authority to the tie Executive Chairman to execute the contracts. The Council will also require to confirm its approval of the Grant Award Letter and the Financial Guarantee in addition to the contracts which will be entered into by tie.

TPB	approval of terms of Infraco and all related documents including note of main open areas, recommendation to TEL on those terms and on the proposed delegated authority to approve and sign ; approval of governance and delegation paper
TEL	approval of terms of Infraco and all related documents including note of main open areas, recommendation to Council on those terms and the proposed delegated authority to approve and sign ; acknowledgment of terms which will be assigned to TEL in due course ; approval of the TEL Operating Agreement and; approval of governance and delegation paper
Tie	approval of terms of Infraco and all related documents as basis for commitment, including note of main open areas; acknowledgement of the proposed delegated authority to approve and sign ; approval of the tie Operating Agreement ; approval of governance and delegation paper

Report Contents

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Appendices

(1) Introduction

The significant stages in the project to date include :

April 2003	Ministerial approval of initial Business Case and grant award
December 2003	Finalisation of STAG and submission of Bills to Parliament
May 2004	Commencement of early operator involvement with Transdev
October 2005	Commencement of design work under SDS
April / May 2006	Royal Assent to Tram Bills
October 2006	Award of Multi Utility Diversion Framework Agreement to AMIS
April 2007	Commencement of utility diversion work under MUDFA
May / June 2007	Change of government and re-confirmation of project
October 2007	OGC Gateway 3 Review
October 2007	Final Business Case for fully integrated system approved by CEC
December 2007	Resolutions to proceed approved by CEC
December 2007	Mobilisation & advance works contracts awarded to Tramco & Infraco
May 2008	Financial Close – construction and vehicle supply

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Although there have been several key events, the completion of the contract suite which commits delivery of the system is highly significant in terms of the scale of commitment and the definitive nature of the programme to complete the project.

To reach this stage has involved close collaboration over a number of years between tie, TEL and the Council along with principal consulting and contractual partners. Throughout, progress has been monitored by the Project Board and the tie and TEL Boards, with full Council approval at key stages. Until mid-2007, Transport Scotland (and predecessor departments) played an active role in the project, since then a more arms length role has been played but crucially this has supported the commitment to the majority of the funding.

In addition to the routine involvement and monitoring of progress by stakeholders through the governance procedures, the project has been cleared through periodic Gateway Reviews, under the Office of Government Commerce rules and executed by experienced external assessors. A further independent review of the project was performed by Audit Scotland in June 2007, following which the principle of the Scottish Government's grant award was confirmed.

The balance of this report summarises the main features of the project and its supporting documentation as a basis to assess readiness for commitment. More detailed information is available on every aspect on request, subject to commercial confidentiality.

(2) Infraco contract suite

The DLA Report provides extensive commentary on the development and final content of the Infraco Contract Suite.

The narrative below addresses three fundamental areas :

- Price
- Programme
- Scope

A section has also been included to address the interface between the Infraco contract Suite and the agreements with third parties relevant to construction.

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

2.1 Summary Pricing Statement – Infraco and Tramco

The following table summarises the final pricing for Infraco and Tramco in the context of the budget provisions made in the Final Business Case.

Infraco	£m
Negotiated Infraco Price	233.5
Other items / adjustments (see 8.2 below)	5.0
Net other items in Infrastructure budget	5.3
Total budget required for infrastructure	243.8
Increase in Base Cost compared to FBC	*17.8*
Tramco	
Negotiated Tram Supply Price	55.0
Other items (see 8.2 below)	3.0
Total budget required for Tramco	58.0
Increase in Base Cost compared to FBC	*6.6*

The increase in Base Costs for Infraco is a result of a negotiated position on a large number of items including the contractual interfaces between the Infraco, Tramco and SDS contracts and substantially achieving the level of risk transfer to the private sector anticipated by the procurement strategy. It also reflects capital expenditure required on lifecycle related costs including mobilisation of the maintenance teams and acquisition of spare parts.

The increase in Base Costs for Infraco of £17.8m approximates closely to the allowance which was made in the FBC for procurement stage risks i.e. the increase in Base Costs which might have been expected to achieve the level of price certainty and risk transfer which has been achieved.

The increase in Base Costs for Tramco results from lifecycle related costs required and, significantly, a material weakening of Sterling against the Euro in the period between Preferred Bidder appointment and the fixing of the exchange rate in late December following FBC approval.

A simple reconciliation of the total Risk Allowance for the project between FBC and Financial close is:

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	£m
Risk Allowance in FBC	49.0
Risks crystallised in contract costs :	
Infraco	(17.8)
Tramco	(6.6)
Other risk items now in base cost	(2.2)
Increase in Phase 1a risk estimate deemed necessary as a consequence of previous increases and taking cognisance of updated QRA	9.9
Risk Allowance at Financial Close (see 8.6 below)	32.3

Subsequent to the position described in the tables above being reached, a further round of negotiations instigated by Bilfinger Berger took place. The detail behind the final position reached has been documented separately for CEC.

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The total Phase 1a project cost budget is settled at £512m, of which £133m has been incurred by 31st March 2008.

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2.2 Summary of Programme – Infraco and Tramco

The critical milestones are :

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Contract Award	May 2008
Commence on site (demolitions)	May 2008
Commence on Street Works	August 2008
Commence Princes Street Blockade	January 2009
Decision on 1b	By March 2009
Take Delivery of 1st Tram	March 2010
Complete Depot & Test Track	March 2010
TRO made	April 2009
Construction substantially complete	January 2011
Commence Shadow running	April 2011
Edinburgh Tram Line 1a Open for Revenue Service	July 2011
Line 1b Open for Revenue Service (if instructed)	January 2012

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This programme has been developed around key assumptions and constraints such as:

- Operation within Construction Code of Practice working hours
- Compliance with embargoes affecting key city centre and Forth Ports areas
- Design and approvals early start constraints
- MUDFA diversion early start constraints
- Critical BBS skill resource constraints (e.g. track welders / Overhead line staff)

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The most significant of these are outlined below.

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Design and Approvals relationship with INFRACO Construction Programme

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The SDS design and approvals programme (including CEC and other 3rd Party approvals e.g. Network Rail) has been used during the development of, and to agree, the INFRACO Programme.

There are a number of areas where the Design and Approvals Programme is the early start constraint for INFRACO, principal amongst these are:

- Section 1A: Forth Ports area
- Section 2A: Haymarket Viaduct
- Section 5A Structures at Roseburn / Murrayfield
- Section 5B Balgreen Road, Carricknowe Bridge, South Gyle Access Bridge
- Section 5C A8 underpass
- Section 6 Depot
- Section 7A Gogarburn Structures

Sections which link to the critical path within 1 month are:

Section 1A:	Forth Ports area
Sections 1B, 1C, 1D	Track
Section 5A	Structures at Roseburn / Murrayfield
Section 5B	Carricknowe Bridge
Section 5C	A8 underpass
Section 6	Depot

Tie has clear visibility of these critical path linkages and is actively managing their delivery within the management processes described in Appendix 1.

MUDFA relationship with INFRACO Construction Programme

The MUDFA Rev06 programme has been used during the development of and to agree the INFRACO Programme.

There are a number of areas where MUDFA is the early start constraint for Infraco, principal amongst these are:

- Section 6: Depot
- Section 2A: Haymarket Junction
- Section 1C: Princes Street, Picardy Place and St Andrews Square
- Section 1A Ocean Terminal – Newhaven & Ocean Drive at Victoria Bridge

The sections which link to the Construction Critical Path within 1 month are:

Section 6	Depot
Section 2A:	Haymarket Junction
Section 1C:	Princes Street, Picardy Place and St Andrews Square

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The BBS programme is based on V6 of MUDFA. Continual reviews of MUDFA programme have been implemented to avoid conflicts with Infraco undertaken by tie. This evaluation has been consistently evaluated & updated in the QRA

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TRAMCO relationship with INFRACO Programme

The TRAMCO design, manufacture, testing and commissioning programme has been used during the development of the INFRACO programme and has been fully interfaced with the Infraco programme.

Programme version V31 will be contained within the SDS novation agreement. Any variance between V26 and V31 which has an impact on the BBS programme will be dealt with through the contract change process.

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2.3 Scope of works – Employer's Requirements

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

The Employers Requirements (ERs) are a comprehensive set of specifications which set out the project obligations and responsibilities against which the construction consortium (BBS) must comply. It runs to some 650 pages and sits as a schedule within the Infraco contract. The document has evolved as the business case and design has been developed and reflects the inputs of the key 'user' stakeholders such as the Council, TEL and Transdev as well as the requirements of the Tram Design Manual and CEC design guidelines.

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

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

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

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

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

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

DLA have also undertaken a legal review to ensure that within the Infraco Contract there is a contractual mechanism for precedence of T&C's over the ER's in the event of ambiguity and for tie to instruct how any ambiguity or inconsistency is dealt with. tie do not anticipate any significant risks to CEC in this respect.

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

2.4 Interface of Infraco with relevant third party agreements ("3PAs")

During the process of preparing the parliamentary Bills and their passage to Royal Assent, a number of agreements were reached with third parties which affect or could affect tram construction. The objective of these agreements was to mitigate risk that construction could be impeded while accommodating all reasonable requests from the third parties. These arrangements are common in any major project of this type. The commitments entered into were reflected as follows :

- commitments in the Act and related documents (CoCP, Noise & Vibration policy etc)
- 3rd party formal legal agreements
- letters to 3rd parties

Although the legal status is different, it would be tie's objective that the commitments are fulfilled.

There are broadly two groups of agreements – those major agreements where the terms have been stepped down into the Infraco Contract Suite (and which BBS have reviewed) ; and those which are independent of Infraco. The stepped down terms are covered by the full protection against breach implicit in the Infraco contract. The risks from the independent agreements are covered by a general obligation by Infraco not to put tie in breach so long as the terms of the independent 3PAs are reasonable in the context of a normal construction process.

The terms of the agreements and their relationship to the Infraco Contract Suite were the subject of a review by DLA which has been summarised and reported to CEC. Nine Utility Agreements exist but are not stepped down into Infraco and four other agreements (with RBS, FP, SRU & Stanley Casinos) are stepped down into Schedule 13, but not in their final form as these agreements are not yet signed.

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Infraco are likely to undertake some utility diversions where MUDFA are unable to do so. This will be instructed as a tie change. At the same time the nine agreements with utility companies will be varied into Infraco as these are required for the implementation of such works.

The final RBS, Forth Ports, SRU and Stanley Casino agreements will be varied as a tie change once completed. There is low risk in that either budget provision has been made for these items or additional funding is being provided by that 3rd party.

(3) Grant Award Letter

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Transport Scotland will provide up to £500m of the total capital cost and the balance will be provided by CEC, which has initially allocated £45m for this purpose. The source of these funds is a matter for the two funders. The Government grant is documented in an award letter which is specific to the project but follows standard terms for grants under S70 of Transport (Scotland) Act 2001. CEC has identified a range of sources and an independent review confirmed the validity of the assumptions made by the Council.

The programme concentrates on Phase 1a initially and the parties have the opportunity to commit to Phase 1b before 31 March 2009 on pre-agreed terms with BBS. During 2008-9, an assessment will be made of funding availability to support Phase 1b. Government contribution will not exceed £500m under the current arrangements.

Grant will be drawn down pro rata with Council contribution. The amounts of grant available in each financial year will be capped, with the balance of any undrawn grant added to the sum available in 2010-11. There are detailed arrangements for payment approval and audit.

With the contributions agreed, the pro rata drawdown mechanism becomes an accounting process each 4-week period and within tolerances will not create any difficulty. The annual capping does have potential to create difficulty, but it is felt there is sufficient tolerance in the spend plans versus funding availability that this limitation is manageable. The funding position will be actively managed and CEC anticipate receiving recovery from Transport Scotland for any interest cost incurred if borrowing is necessary to meet contractual commitments beyond the funding available from Transport Scotland in a particular period.

The terms of the grant letter are weighted in favour of the awarding body and fall short of the sort of protection which a borrower would seek from a commercial lending bank. This is however normal and the Council are satisfied that the terms of the award offer sufficient protection bearing in mind the relationship between Government and the Council.

The letter was negotiated with TS by tie and Council Finance and Legal officials with comment from DLA. See Section 7 for taxation assessment.

(4) Risk of procurement challenge

This section contributed by Jim McEwan, who performed a review of procurement process integrity independent of the main procurement team.

The legal advice provided to tie and CEC is summarised in the DLA Report and relates to the final negotiated position.

Summary

Over the last 12 months tie has pursued the procurement of both the Infraco contract for the construction and maintenance of the Tram infrastructure in its entirety and the Tramco contract for the supply, delivery and maintenance of the Tram vehicles. The focus of the procurement strategy was to deliver fixed price contracts for each.

The process followed for each contract was consistent with that specified by the EU directive on Public procurement and details of the evaluation methodology employed are outlined below.

The Bilfinger Berger and Siemens (BBS) consortium have been duly awarded preferred bidder status for the Infraco contract.

CAF has been awarded preferred bidder status for the Tramco contracts.

In the event of any challenge to these awards tie is well placed to successfully defend the fairness and integrity of the process undertaken in the selection.

Opportunities have been provided for de-briefing on the procurement to unsuccessful suppliers for both Tramco and Infraco. This was undertaken on 4th April 2008 with one further Tramco debrief to be arranged. No further action is expected from any bidder.

The BBS consortium are in the process of finalising arrangements to include CAF in the consortium. In principle, tie is content that this should happen and indeed the concept was acknowledged at the time of preferred bidder selection, though with CAF Novation being the required approach to support Financial Close. Tie and DLA are monitoring the BBS / CAF arrangements to ensure that no perception of a change in bid terms could be construed.

Infraco

The Evaluation Methodology employed by tie in the Tram Project is detailed in a document dated 8th January 2007 'Evaluation Methodology for submissions in response to the invitation to negotiate issued on 3rd October 2006 for the procurement of the Infraco for Edinburgh Tram Network' .

In the process 6 key areas were identified in the evaluation and a stream leader appointed to each :

Financial
Programme and Project Execution Proposals
Project Team and Resources
Technical and Design proposals
Legal and Commercial
Insurance

Evaluation team members were identified in the methodology together with stream leaders for each of the key areas

Each team was charged to prepare a 'consensus' score matrix on each of the key areas, these have been duly completed and lodged in the central document repository.

Proper probity on the process was maintained with financial information being restricted to only those in the finance stream and to the tie executive team.

Security employed on maintaining confidentiality was consistent with best practice with documentation stored in a locked room and the financial documentation stored in a locked cabinet within the room. (Note: The details of the financial bids were only available to those in the Financial stream, the evaluation of the other streams was therefore carried out without prejudice on costs.)

All meetings with Suppliers were documented and the notes of said proceedings are held in the central repository.

Financial position was reviewed as was the normalisation process which ensures bids are viewed on an equal footing basis

Tramco

The Evaluation Methodology employed by tie in the Tram Project is detailed in a document dated 11th October 2006 and titled Tramco Evaluation Methodology.

The process employed was identical to that employed in the Infraco evaluation as detailed above with 6 streams and the same methods of approach on scoring, confidentiality, probity and security. All required documents have been lodged in the central document repository.

(5) Third Party Agreements

This section contributed by Alasdair Sim, who took the lead role developing the agreements. A second (and consistent) view on risk is provided by Stewart McGarrity in Section 8.

In addition to the principal Infraco Contract Suite, there are a number of agreements which are of varying significance to Financial Close. This section describes the purpose and status of these agreements, together with an assessment of the level of risk to programme / cost arising from the agreements remaining open at the date of Financial Close.

THE AGREEMENTS ASTERISKED ARE REGARDED AS THE MOST IMPORTANT IN RELATION TO REACHING A ROBUST POSITION AS AT FINANCIAL CLOSE.

The agreements addressed in this section are as follows :

5.1 Edinburgh Airport Limited - Licence *
5.2 Edinburgh Airport Limited – Lease *
5.3 Edinburgh Airport Limited – Operating Agreement
5.4 CEC/tie Licence *
5.5 SRU Agreement
5.6 Royal Bank of Scotland Agreement
5.7 Local Code of Construction Practice – Forth Ports *
5.8 Local Code of Construction Practice – New Edinburgh Limited *
5.9 Local Code of Construction Practice – Edinburgh Airport *
5.10 Network Rail Asset Protection Agreement *
5.11 Network Rail Depot Change *
5.12 Network Rail Station Change *
5.13 Car Park Compensation Agreements
5.14 Network Rail Framework Agreement *
5.15 Network Rail Lease & Servitude Agreements
5.16 Forth Ports Agreement
5.17 Stanley Casinos Agreement
5.18 Other Site Specific Code of Construction Plans
5.19 Licence – The Gyle
5.20 Licence – West Craigs
5.21 Network Rail – Neighbour Agreement
5.22 Network Rail – Operating Agreement
5.23 Network Rail – Bridge & Bridge Lease Agreements
5.24 Telewest utility agreement
5.25 Scottish Power utility agreement *
5.26 DPOFA 2007 Revision
5.27 Mobilisation agreements (Infraco and Tramco)

The execution of these agreements has focussed primarily on construction risk. There remains a very low risk that residual agreements will not be agreed prior to operation. tie is creating a plan for completion of these agreements to ensure that they are in place well in advance of operation.

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5.1 Edinburgh Airport Limited - Licence *

Purpose of Agreement
This is a licence agreement between Edinburgh Airport Ltd and City of Edinburgh Council, the purpose of which is to enable/facilitate the construction of the Edinburgh Tram within the boundary of Edinburgh Airport. This agreement covers MUDFA and INFRACO works as well as the construction of the Burnside Road alternative access route, and sets out the working arrangements between EAL, tie/CEC and contractors working on the Edinburgh Tram Network.

Current Status of Agreement
The agreement is signed. This agreement has been drawn down into Schedule 13 of the INFRACO Contract.

5.2 Edinburgh Airport Limited – Lease *

Purpose of Agreement
This is a 175 year lease between Edinburgh Airport Limited and City of Edinburgh Council to facilitate the operation of the Edinburgh Tram Network. This lease follows the terms of the Minute of Agreement signed by the two parties during the Parliamentary process in September 2005.

Current Status of Agreement
This agreement is signed.

5.3 Edinburgh Airport Limited – Operating Agreement

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

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

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

5.4 CEC/tie Licence *

Purpose of Agreement
The purpose of this licence is to pass over responsibility for land acquired for the ETN from CEC to tie. This will enable tie to manage the process of making land available to INFRACO on a programme/needs basis using the agreed Land Access Permit Procedure. CEC will manage the land/asset until the point that INFRACO take occupation of each worksite.

Current Status of Agreement
The agreement is signed.

5.5 SRU Agreement

Purpose of Agreement

This agreement governs design and construction activities in the vicinity of the Murrayfield Stadium. The agreement includes the construction of the Murrayfield Tram Stop, Roseburn Street Viaduct, Murrayfield Stadium Retaining Wall, the Wanderers Clubhouse remodelling, access accommodation works and the relocation of the training pitches. The agreement also sets out the requirement to develop a local construction plan which the INFRACO contractor will be obliged to comply with. This includes arrangements in relation to the temporary occupation of land within the Murrayfield site. The draft SRU agreement has been stepped down into Schedule 13 of the INFRACO Contract.

Current Status of Agreement

The last important outstanding matter related to the S75 agreement. which CEC intend will replace the current Section 50 agreement and it is tie's understanding that this matter is now resolved. All residual minor matters are in process of being finalised and it is not anticipated that there will be difficulty in concluding the agreement..

Risk to INFRACO Contract Award

INFRACO works are expected to commence in the vicinity of Murrayfield in June 2008. Risk to award of INFRACO Contract is considered low.

5.6 Royal Bank of Scotland Agreement

Purpose of Agreement

This agreement builds upon the existing Section 75 Agreement signed in 2002 between RBS and CEC which committed RBS to fund the design, procurement and construction of the Gogarburn Tram Stop. The current proposal is for the INFRACO contractor to undertake the works within RBS land under licence, and sets out the procedure for CEC to later acquire the operational land based on the 'as built' (and at nil cost) using the GVD process. The agreement also covers the desire of RBS to maintain the landscaping between the Gogarburn Tram Stop and the A8 Glasgow Road.

Current Status of Agreement

The agreement is currently in draft format, with finalisation expected on completion of the detail design, as this will allow final costs for the tram stop to be calculated. RBS have provided written confirmation that access to the land will be secured under licence.

Risk to INFRACO Contract Award

INFRACO works are expected to commence in the vicinity of Gogarburn from **mid-2009. Risk to award of INFRACO Contract is considered low.**

5.7 Local Code of Construction Practice – Forth Ports *

Purpose of Document

The existing Minute of Agreement between Forth Ports and CEC requires the development of a Local Code of Construction Plan to govern how the construction works are to be undertaken within the Forth Ports area. This would include method statements, programme details and consultation/notification requirements to be agreed prior to the commencement of construction. The Forth Ports Minute of agreement is included with Schedule 14 of the INFRACO Contract.

Current Status of Document
tie and BBS are currently drafting a local COCP with Forth Ports and have reached agreement with Forth Ports on the general approach to construction in the Leith Docks area. tie meet with the Forth Ports Project Manager on a weekly basis and will continue to evolve the local construction plan as certainty on programme is established.

Risk to INFRACO Contract Award
INFRACO works are expected to commence in the Forth Ports area from November 2008. MUDFA works will recommence in the Leith Docks area following the Easter embargo period from April 2008, and is currently being undertaken on a work by works licence basis, which contains the relevant elements that INFRACO will include within the final Local Code of Construction Practice document.

Forth Ports, tie and BBS have been undertaking preliminary discussions around programme and approach to construction. Forth Ports have expressed a willingness to work with BBS to have the works completed in the Leith Docks area as quickly and seamlessly as possible. As a result, the risk to award of INFRACO Contract is considered low.

5.8 Local Code of Construction Practice – New Edinburgh Limited *

Purpose of Document
The existing Minute of Agreement between New Edinburgh Ltd and CEC requires the development of a Local Code of Construction Plan to govern how the construction works are to be undertaken within Edinburgh Park. This would include method statements, programme details and consultation/notification requirements to be agreed prior to the commencement of construction.

Current Status of Document
tie and BBS are currently drafting a local COCP for Edinburgh Park and have consulted with Edinburgh Park Management Ltd and New Edinburgh Ltd on programme and approach to construction. NEL have confirmed in writing their acceptance of the construction programme.

Risk to INFRACO Contract Award
INFRACO works (track) are expected to commence in Edinburgh Park from June 2008, with construction of the Edinburgh Park Station Bridge commencing in August 2008. NEL have confirmed their acceptance of the programme and as a result, risk to award of INFRACO Contract is considered minimal.

5.9 Local Code of Construction Practice – Edinburgh Airport *

Purpose of Document
The licence between EAL and CEC sets out construction requirements in Schedule Part 5 – Development Rights and Obligations. This agreement has been drawn down into Schedule 14 of the INFRACO Contract.

Current Status of Document
tie and BBS are currently drafting a local COCP based on the obligations set out in Schedule Part 5 of the EAL Licence Agreement. tie meet with the EAL Project Manager on a four weekly basis and are currently working with EAL to ensure that tram construction activities integrate with other works ongoing within the Airport. EAL are content with the approach and tie/BBS will continue to evolve the local construction plan as certainty on programme is established

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

Network Rail (NR) agreements – general

The suite of NR agreements comprises the following :

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

5.10 Network Rail Asset Protection Agreement *

Purpose of the Agreement

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

Current Status of Agreement

The APA has been signed.

Risk to INFRACO Contract Award

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

Additional comment provided by DLA

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

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

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

5.11 Network Rail Depot Change *

Purpose of Document

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

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

Risk to INFRACO Contract Award

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

5.12 Network Rail Station Change *

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

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

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

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

5.13 Car Park Compensation Agreements

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

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

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

5.14 Network Rail Framework Agreement *

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

Current Status of Agreement
The Framework agreement has been approved and signed by Network Rail management and legal advisors and is with CEC for signature.

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

5.15 Network Rail Lease Agreements & Servitudes

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

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

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

5.16 Forth Ports Agreement

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

Current Status of Agreements
The commercial principles are agreed and progress is being made toward concluding the agreement. The transfer of land from Forth Ports to CEC will be part of the FP contribution to the project, and this is part of the existing Section 75 agreement.

Risk to INFRACO Contract Award
This agreement should not impede signing of the Infraco contract.

5.17 Stanley Casinos Agreement

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

5.18 Other Site Specific Code of Construction Plans

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

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

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

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

Risk to INFRACO Contract Award
All relevant 3rd Party agreements are detailed within the INFRACO contract in Schedule 13. The requirements on Infraco are entirely in line with normal construction practice and the risk to CEC for award of the INFRACO contract is considered low.

5.19 Licence – The Gyle

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

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

Current Status of Agreement

The Gyle have accepted the proposal to construct the works under licence. Works to relocate utilities outside the LOD at The Gyle commenced on 21 April 2008, with the main INFRACO works scheduled to commence in August 2008. It has now been agreed that the works will be undertaken under two licences. The first is in agreed & final form and allows for utilities works to take place outside the LOD. A letter from CEC was issued to The Gyle on 21 April 2008, confirming that the utilities licence will be signed by CEC within 3 working days. The second licence will cover the main INFRACO works. There is currently a conflict with the programming of the works on the A8 underpass, elements of which are scheduled to take place over the Christmas Shopping period. INFRACO are obliged under the Gyle Side Agreement to develop a works method statement (to be agreed with The Gyle) which seeks to avoid works causing disruption to businesses in The Gyle during the peak retail periods.

Risk to INFRACO Contract Award

BBS, tie and The Gyle will work to develop an appropriate solution to the current programme issue in advance of commencement of the INFRACO works. Although there is no material risk to the award of the INFRACO contract, the programme revision is being addressed as a priority. tie confirm that there is sufficient risk allowance to accommodate the potential conflict between programme requirements and retail requirements agreed with the Gyle Shopping Centre.

5.20 Licence – West Craigs

Purpose of Document

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

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

Current Status of Agreement

The licence to undertake the works on West Craigs land was incorrectly executed by West Craigs. The engrossed document has been returned unchanged and tie has been informed that it is now signed by West Craigs and is available for CEC signature. Works to relocate the 800mm water main at Gogar Depot will commence on 28 April 2008.

Risk to INFRACO Contract Award

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

5.21 Network Rail – Neighbour Agreement

Purpose of Agreement

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

Current Status of the Agreement

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

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

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5.22 Network Rail – Operating Agreement

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

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

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

5.23 Network Rail – Bridge Agreement & Bridge Lease

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

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

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

5.24 Telewest utility agreement

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

Current Status of Agreement
The contract has now been signed by Telewest and is with CEC for signature.

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