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Our Ref: WG/JPT

3rd July 2007

Dear Malcolm

Edinburgh Tram Project

Following last week's debate in Parliament, we have discussed both within **tie** and with senior colleagues at the Council how best we can proceed on the subject of funding for the project. It is clear from the Minister's decision that the arrangements are now substantially different from those which we previously anticipated. In particular, the Council's responsibility for all additional funding above the Executive's contribution of £500m needs little further elaboration.

You will be aware that there were discussions between your own and Council officials aimed at reaching documented agreement on the funding arrangements. **tie** provided support to that dialogue. We believe we now need to re-activate that dialogue within the new "rules of engagement". **tie** will again be pleased to support the process, not least because the funding arrangements must be agreed and clearly stated in the Final Business Case, which we and our TEL colleagues are responsible for preparing.

I think it will help everyone if we can reach agreement on certain key principles at senior level in our organisations in order to provide leadership to that process. I have set out below a number of points which I would like to discuss and I hope agree with you to provide that guidance.

Funding quantum and drawdown process

Including the most recent funding award letter dated 19th March 2007 for an aggregate sum of £60m, the total funding already awarded by the Executive is £124.8m. This leaves a balance of £375.2m which will require to be regulated as to its drawdown. My suggestion is that we agree two short-term milestones:

delivering transport projects

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1. Preferred bidder recommendation: In September of this year, we anticipate that a formal recommendation will be prepared by tie with respect to the preferred construction bidder, which will incorporate the selection of the vehicle supplier. The recommendation will require to be approved by Council officials and I am anticipating that Transport Scotland will also wish to approve the decision. The recommendation will incorporate a revised view of the capital cost of the project which reflects the preferred bids. Assuming that the recommendation is supported, the funding required following this milestone will be that necessary to see the project through to the next milestone.
2. Final Business Case: This will require to be approved in support of contract completion in January 2008, and will also support the commitment of funding from both Transport Scotland and the Council. At this time we can agree the drawdown milestones for the construction period.

The funding will continue to be awarded by Transport Scotland to the Council, which will in turn pass the funds to tie for settlement of approved expenditure. I believe the controls around this process are working well.

We have an opportunity to review the working arrangements between tie and Transport Scotland. I would propose that the Project Team continue to provide comprehensive 4-weekly reports to Transport Scotland as they have done in the past. We will of course also maintain the tight project governance through the Tram Project Board. We should attempt to minimise further ad-hoc reporting and meetings removing a significant workload burden on both sets of staff.

Contingencies

The revised basis for Scottish Executive funding will remove many of the detailed issues which would have required resolution under the previous proposal. The Council has a clear view of both the Scottish Executive contribution and also of its own responsibilities. However, there are a limited number of circumstances which we might address. These include the possibility that action taken by the Scottish Executive or Ministers leads to a material extension of programme or increase in cost. Another is the possibility that the Ministers determine not to support the project at some stage in the future resulting in termination costs. We and the Council are of course clear that actions taken by us which create material extension of programme or increase in cost will be to the account of the Council.

Another area to address is the possibility of Scottish Executive action which has a material adverse effect on the operational cash flows of the tram. The Council are aware that there is no subsidy anticipated for operations based on present assumptions and would wish to have agreement with the Scottish Executive that a different future scenario will result in a constructive dialogue to resolve the implications.

I would like to discuss how we can allow for these circumstances in a straight-forward manner and without attempting to define a range of hypothetical future scenarios.

Other matters

I would like to get your views on how the Final Business Case should reflect the proposed concessionary fare support arrangements.

I hope this provides a basis for a useful discussion and that we can help our respective organisations proceed effectively on the funding arrangements.

Yours sincerely



Willie Gallagher
Executive Chairman