

## PROOF CORRECTIONS TO MALCOLM REED'S WITNESS STATEMENT

Page 1 line 1, **Christopher** inserted between **Malcolm** and **Reed**

Para 24 (page 10) 4<sup>th</sup> line from end – add **d** to scrutinise [**scrutinised**]

Para 69 (page 31) 11<sup>th</sup> line from end, delete full stop after **had{.}**

Para 110 (page 50) 7<sup>th</sup> and 15<sup>th</sup> lines, replace **Programmes** with **Investment**

Para 123 (page 56) 14<sup>th</sup> line from bottom of page. **8** should be **18** [cf para 125]

Para 123 (page 57) 4<sup>th</sup> line from top, delete **this**

Para 125 (page 58) 2<sup>nd</sup> line from end, delete **with**

Para 127 (page 60) 2<sup>nd</sup> line down, delete 1<sup>st</sup> **that** [to read **documents I have seen that TIE....**]

Para 131 (page 61) 5<sup>th</sup> line from end, delete **and**

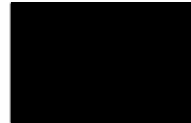
Para 133 (page 63) 2<sup>nd</sup> line from top, delete comma after **Stewart{,}**

Para 141 (page 66) 10<sup>th</sup> line down, replace **dispersed** with **disbursed**

Para 153 (page 72) 6<sup>th</sup> line from end, insert **to** after **relating**

Para 164 (page 76) 4<sup>th</sup> line, delete **a** after **however**,

Para 166 (page 77) last line, replace **achieved** with **implemented**





**The Edinburgh Tram Inquiry**  
**Witness Statement of Malcolm Reed**

My full name is Malcolm Christopher Reed. I am aged 72 as at the date of this statement. My contact details are known to the Inquiry.

I was the Chief Executive of Transport Scotland from August 2005 until my retirement in February 2009.

Statement:

**General**

1. I was appointed as Chief Executive designate of Transport Scotland (TS) with effect from 8 August 2005. At that time my primary responsibility was to establish this new organisation, which became operational as an executive agency of the Scottish Government on 1 January 2006. However, to accommodate the transfer of some powers from the Strategic Railway Authority to the Scottish Executive, in November 2005 I was asked by John Ewing, the Head of the Scottish Executive's Transport Group, to take on line management responsibility for the Group's rail division before TS formally went "live". From late November 2005 I was therefore exercising oversight of the Scottish Government's rail functions on behalf of John Ewing before these and the other transferring functions became part of the new TS organisation at the start of 2006.
2. I retired from the Civil Service on 17 February 2009. My time at TS overlapped with that of my successor, David Middleton, for about a week. From the date that he took up his post I ceased to be the accountable officer.

3. While I was Chief Executive of TS, my role was to deliver those transport responsibilities which had been assigned to TS by the Scottish Ministers. These included managing a substantial project portfolio of about £2,000 million in value. Bill Reeve reported directly to me, as did Damian Sharp when this was appropriate because of the nature of his responsibilities. In organisational terms, my responsibility for the tram project was exercised through Bill Reeve. Ministerial designations changed in 2007, but initially the Minister to whom I was primarily accountable was Tavish Scott MSP, the Transport Minister at that time. After the 2007 elections my accountability was to John Swinney MSP, the Cabinet Secretary for Finance and Sustainable Growth, and to Stewart Stevenson MSP, who was his junior as Minister for Transport, Infrastructure and Climate Change.
4. The appendices of two Audit Scotland reports contain a comprehensive list of the major projects that TS were funding around the same time as the Edinburgh tram project. The first of these Audit Scotland reports was issued in 2006 and entitled *Scottish Executive: an overview of the performance of transport in Scotland*, (**ADS00078**). The second report was published in June 2008 under the title *Review of Major Capital Projects in Scotland* (**CEC01318113**). Funding responsibility for all the active transport projects listed in those reports transferred to TS on 1 January 2006.
5. Besides the Edinburgh tram project, the initial estimate for which was shown in the Audit Scotland 2006 report (**ADS00078**) as £473 million, TS had responsibility on behalf of the Scottish Ministers for: the Borders Railway project, the initial estimate for which was £130 million; the Edinburgh Airport Rail Link (EARL), estimated cost £497 million; the Glasgow Airport Rail Link (GARL), estimated cost £160 million; the Edinburgh to Bathgate Railway, estimated at £341 million; and the Stirling, Alloa and Kincardine Railway project (SAK), estimated at £37 million. Waverley Station upgrade phase 1 was also being funded at a cost of £150 million. In the trunk roads portfolio, TS was responsible for: the M74 completion at an estimated cost of £150 million; the Aberdeen Western Peripheral Road at an estimated cost of £120 million; the A8 Baillieston to Newhouse upgrade at an estimated cost of £105

million; the New Kincardine Bridge at an estimated cost of £71 million; the A80 phases 1 to 3 at an estimated cost of £120 million; and the A68 Dalkeith Bypass at an estimated cost of £30 million - £40 million. There were also two projects in development relating to improvements of the M8.

6. All of these projects had been initiated before TS was established, and the nature of the role that TS inherited varied between different projects. Two of the roads projects, the M74 completion and the Aberdeen Western Peripheral Route, were joint projects with the respective local authorities. In those cases there was a steering group comprising local authority and TS representatives. The other trunk road projects were entirely TS projects, and their procurement and delivery was managed in-house within TS's corporate governance processes.
7. Trunk roads were a long-standing Scottish Office/Scottish Government function, and TS staff were directly and heavily involved in trunk road project development and management. In the case of the major rail projects, without exception the promoter and statutory undertaker was an outside body, not the Scottish Executive. The City of Edinburgh Council (CEC) was the promoter of the Edinburgh tram project; Clackmannanshire Council was the promoter of the SAK scheme; and the Scottish Borders Council was similarly the promoter of the Borders Railway project. The Waverley Station phase 1 project was well under way when TS was established, and was being taken forward by Network Rail. However, because the Waverley Station upgrade was a Scottish Executive grant-funded project, TS was represented on the steering group for the project. Ownership and delivery of the Waverley Station project nevertheless rested with Network Rail, and similarly Network Rail took on responsibility for the Airdrie/Bathgate Rail link.
8. In summary, TS inherited a portfolio of ongoing projects in 2006. Their oversight and management processes had already been established and were generally tailored to their specific characteristics, particularly where the public transport projects were concerned. For each of the latter it was the promoter, not TS, which held the authority to deliver the project as the

statutory undertaker, despite the Scottish Ministers' large financial stake in these projects. There was no standard governance template, but the arrangements for taking a project forward tended to reflect its nature and origins.

9. So far as the Edinburgh Tram Scheme was concerned, TS's role changed in 2007 from that of a project partner into simply that of a funder. The two airport rail links, EARL and GARL, did not go ahead, so the issue of TS's role in their delivery arrangements did not materialise. At its outset the tram project was similar to other joint projects. However, the outcome of decisions by the Scottish Ministers and the Scottish Parliament in 2007 was that there was a change in responsibilities for the tram project and the nature of its governance, reflecting an explicit risk transfer from the Scottish Government to CEC. Those arrangements differentiated the tram project from the rest of the portfolio after the summer of 2007, and while I was Chief Executive there was no other project where TS's role was only that of "banker".
10. In most cases TS participated directly in the management arrangements for externally-promoted projects that it was funding or part-funding on behalf of the Scottish Ministers. Whether it was as part of a steering group or a board, TS would usually be represented on that group or board. The one exception was the SAK project, where TS was not initially represented in its management arrangements. But whatever the mechanism adopted, we maintained oversight of all the transport projects where the Scottish Government was exposed to financial risk. TS did this in most cases through formalised reporting mechanisms, but we also made use of our own access to projects to supplement the reports we received from the project owners.
11. The Audit Scotland reports that I have cited defined any project costing over £5 million as a major project, so in that definition the Edinburgh tram project was a major project for TS. It was not, however, the most important project for TS. All were significant, but their importance and profile varied from time to time depending on their stage of development and the demands of each project. For example, when Transport Scotland was established there was no

expectation that a second Forth road crossing at Queensferry would be built. However, because of the emergence of problems with the existing Forth Road Bridge, a replacement Forth crossing went from nowhere to being top of our priority list in a matter of months. The development of the replacement Forth crossing overlapped with the delivery of the Edinburgh tram project.

12. If a project was a mainstream trunk roads project which TS was taking forward directly, then it would have been entirely a TS project. In that scenario TS or its predecessor would have specified the requirement, ensured that the proposal was the right solution to the particular issue it was intended to address, including a full financial appraisal, developed the design to tender stage, and carried out all of the procurement.
13. Most of the public transport projects that TS inherited had gone through a prior screening within the Scottish Executive, which involved testing the value for money of the project and whether it was deliverable. Apart from the Waverley station upgrade, all the major rail projects inherited by TS required parliamentary approval to authorise acquisition of the necessary land and the construction of the scheme, and this subjected them to detailed scrutiny and appraisal. As a project moved from the preliminary stages into the parliamentary process and then, if approved, into the delivery phase, the scale and nature of its funding and process requirements changed. Scottish Government funding for such schemes at all stages was generally provided through a grant mechanism, but the responsibility for scheme delivery, including procurement, remained with the promoter of the project, and TS's role was usually that of monitoring rather than leading delivery.
14. The fundamental rule of the grant aid process is that the Scottish Ministers have to be satisfied that money is being properly spent. Funding for projects was released against agreed deliverables during each project's progress. Ministers would never provide open-ended funding for a project. TS's responsibility was to ensure on their behalf that what was being charged for was being delivered.

15. Public transport projects differed from each other according to the nature of their promotion, procurement, and the regulatory regimes within which they operated. TS would therefore adopt different approaches to them. For example, Network Rail was subject to the scrutiny of an independent statutory regulator, and this extended to the company's performance in delivering new projects. TS therefore did not get involved in the detailed monitoring of Network Rail's delivery of the Airdrie-Bathgate scheme, despite its scale, because the Office of Rail Regulation was carrying out that task as part of its statutory duties, on which it reported to the Scottish Ministers.

## **The Parliamentary Process**

16. I am aware that Parliamentary Bills for lines 1 and 2 were submitted to the Scottish Parliament in early 2004. I am aware that in March 2006 the Edinburgh Tram (Line One) Act 2006 and the Edinburgh Tram (Line Two) Act 2006 were passed. I have been shown emails dated 27 and 28 November 2003 from Graeme Bissett (**TIE00058492**), which related to the preparation of documents in advance of presenting the Bills to Parliament. I note that attached to those emails was a document entitled 'Background Paper for Meeting with the Scottish Executive' dated 26 November 2003 (**TIE00058493**). That paper discussed funding requirements relating to Lines 1 and 2. I have also been referred to an email Ian Kendall sent to Damian Sharp on 23 September 2005 (**TRS00001961**), forwarding legal advice received by TIE from Senior Counsel and Dundas & Wilson, and attached note of advice (**TRS00001962**). The note discussed a funding gap. I have also been shown a report prepared by the CEC signed on 2 December 2004 and dated 9 December 2004 (**CEC00455293**), which sought approval for lodging the Edinburgh Tram (Line Three) Bill in the Scottish Parliament.
17. TS had not been established when these matters relating to the Bills, the funding for lines 1 and 2, and approval for line 3 were under discussion. Anything prior to 1 January 2006 would be a matter for the then Head of the



Transport Group within the Scottish Executive. I am therefore unable to comment on these issues from direct knowledge.

18. I have been referred to an email chain dated 18 October 2007, including the first email in the chain sent by Rebecca Andrew, the Acting Principal Finance Manager for CEC (**CEC01541278**). At paragraph 6 of her email, she noted TS's view that the grant paid for the cost of the parliamentary process of £17 million was included in the total Scottish Government grant contribution to the tram project of £500 million. I have also been referred to an email chain dated 1 November 2007, including the first email in the chain from Rebecca Andrew (**CEC01497231**). In that email, she discussed the costs of the Parliamentary process. I have also been shown an email dated 23 October 2007 from Willie Gallagher to the Transport Minister Stewart Stevenson MSP (**CEC01506875**), which noted that the costs of the parliamentary process were not included in the Final Business Case in 2007. I cannot comment on the detail of these costs. However, I have been referred to Audit Scotland's Report dated June 2007 (**CEC00785541**). On page 13 of that report at paragraph 48, it records the Auditor General for Scotland's view that parliamentary process costs were not counted against the project's overall anticipated final cost. All these parliamentary costs were committed before TS was in existence, and most of the money would have been disbursed by the Transport Group of the Scottish Executive. I am therefore not in a position to confirm from direct knowledge that this £17 million was not included in the anticipated overall scheme costs, but I must assume that the Auditor General had sound reasons for reaching that view. The bulk of those costs would have been incurred whether or not the Bills succeeded in obtaining parliamentary approval. That was a risk that the Scottish Executive had evidently decided to underwrite.
19. In the email I have already been referred to from Willie Gallagher to Stewart Stevenson MSP (**CEC01506875**), Mr Gallagher wrote: *"The costs for the project start from the moment that parliamentary approval has been granted...."* I am not aware whether the costs of the tram project as stated in the Final Business Case in 2007 included any of the costs incurred on the tram project prior to parliamentary approval in 2006. I am unaware of the

composition of the costs that were incurred before parliamentary approval, but the nature of the parliamentary process is such that an adequate level of design would have had to be undertaken both to define the physical scope of the scheme and to inform the required estimates of cost. I am not aware of the extent to which there was separate accounting for non-Bill activity before the Bills were passed. These are all matters of which I have no direct knowledge and upon which I am unable to comment further.

## **Phasing of Construction Works**

20. I have been shown a report prepared by CEC signed by Andrew Holmes on 19 January 2006 and dated 26 January 2006 (**CEC02083547**). In that report, recommendations were made for funding and phasing the tram network. I am not aware when the view was first reached that there was insufficient funding to build both Lines 1 and 2 and that it would be necessary to build these lines in phases. That issue arose before TS was established. The project that TS took forward was to build line 1a, with line 1b as an option if and when additional funding became available. With regard to the recommendation that a first phase be built from the Airport to Leith Waterfront and the benefits of this as compared with other options, these issues go back to the origins of the project and what were considered to be the priorities at that time. I was not involved in that decision-making and I cannot therefore comment on what factors informed that decision.
21. The reservations that TS had about the cost estimation process and affordability of the tram project were expressed in the advice that went to Ministers (**TRS00003413**). TS was aware of issues, but, as in any developing project, estimates would be refined as the scheme progressed. At the beginning cost estimates were at an outline level sufficient to satisfy parliamentary requirements and it was only as more detailed design was undertaken that a firmer understanding about costs would emerge.

## Budget and Cost Estimates

22. I am aware that the Scottish Executive committed £375 million to the tram project. I have been shown a Scottish Executive document entitled *Building Better Transport* dated March 2003 (**CEC02083844**), where the budget is noted at page 3 in the Ministerial Foreword. Appendix 1 (**ADS00078**, page 46) of the 2006 Audit Scotland document rehearses the Labour/Liberal Democrat partnership agreement that was reached to set up the coalition in that year. One of the commitments within that partnership agreement was to invest in a tram network in Edinburgh. That was a political agreement reached between the two governing political parties in 2003 and I am assuming that whatever information was available to officials at that time informed the political decision to commit £375 million to the tram project. But as I have already explained, these events precede the establishment of TS and my own involvement. I am not in a position to comment further.
23. I have been shown a CEC report signed by Donald McGougan and Andrew Holmes on 17 December 2007 and dated 20 December 2007 (**CEC02083448**). The purpose of that report was to recommend approval of the Final Business Case version 2 prepared by TIE. As noted at paragraph 8.2 of the report, the final cost estimate reported in the Final Business Case version 2 in December 2007 was £498 million. Cost estimation was an iterative process. That figure of £498 million was consistent with previous figures after allowing for indexation, which was an important element in this. Estimates had started from a 2003 price base, but had to look forward to an anticipated completion date which at that stage was 2011. When the CEC report was issued in December 2007 the project had changed, and the Scottish Ministers were not at risk beyond the commitment of up to £500 million at outturn prices. CEC and TIE were involved in the production of the final cost estimate of £498 million, and I have no knowledge of who within those organisations was responsible for them. TS did not produce cost estimates for schemes promoted by other organisations. At various stages TS took a view of the sensitivities of those estimates but ultimately it was the

responsibility of the promoter – in this case CEC – to satisfy itself of the accuracy of the estimates.

24. Up until the summer of 2007, when the status of the project changed, TS would have scrutinised the estimates and commented as appropriate. That was because the Scottish Government potentially had a financial exposure to any cost overruns. When the status of the project changed, CEC continued to be asked, as a condition of grant, to produce a Final Business Case and also to carry out a Gateway Review. That was in order to provide assurance to the Scottish Ministers that the scheme was in good shape before further funds were released for the main construction phase. At that point TS would not have double-checked CEC's calculations, whereas previously TS would have scrutinised the estimates, and any issues of concern would have been noted and discussed with TIE. However, whether before or after the change in the status of the project, responsibility for the production and accuracy of the estimates lay, as I have already stated, with CEC and TIE rather than TS.
25. Prices generally change over a project's lifetime from inception through construction to completion. The usual practice in civil engineering contracts is to apply an index of construction costs, which is not the same as the retail price index or the consumer price index. Examples such as Baxter's index are specifically tailored to reflect movements of items such as materials and labour costs within the construction sector. I note from **(TRS00002378)** that the Minister of Transport had secured Cabinet agreement to indexation of the Scottish Executive's £375 million contribution to the tram project in line with increases in general construction costs since 2003 (page 1, paragraph 5, 4<sup>th</sup> indent). A subsequent paper **(TRS0003840)** dates that Cabinet decision to December 2005 (page 1, paragraph 1), shortly before TS was formally established. I do not recall that this Cabinet decision was specifically discussed with me, and it appears from a CEC report signed on 19 January 2006 **(CEC02083547)** (page 9, indent (v)) that previous agreement in principle to indexation on this basis had been reached between CEC and the Scottish Executive.

TRS0003840  
should be  
TRS00003840

26. While the available funding envelope would obviously set the parameters of overall scheme costs, it would not of itself affect the basis upon which individual cost components were estimated. As was the case with the tram project, the scope of the scheme would be adjusted if required to keep it within the available funds. When taking a project forward it has to be kept in mind that the benefit to cost ratio depends on the project costs. If these are underestimated, the project may not deliver the expected return. The middle years of the last decade can be characterised as a very overheated period in the construction sector. There was heavy demand for construction work in Britain at the time, arising from schemes such as Heathrow Terminal 5 and the preparations for the Olympics. All the major construction firms in Britain were very busy and could effectively select what work they wanted to do at the prices they put in, and at TS we were concerned at times whether we would be able to attract bidders for some projects. At the height of the construction industry boom in 2005-2007 the market was essentially a sellers', rather than a buyers', market. That must be borne in mind when looking at outturn prices for any project that was being tendered during that period.
27. It has been put to me that after the commitment of £375 million was made for the tram project in March 2003, which was subsequently indexed to £500 million, the cost estimate never changed substantially despite the production and refinement of further Business Cases. As I have already explained, I am not aware of the basis of the original £375 million estimate, but clearly it is not unknown for project costs to increase beyond inflation. The Auditor General's 2006 report (**ADS00078**) gave examples of projects where the initial estimates and subsequent projects costs varied significantly and it identified reasons for these increases, such as increases in scope and under-estimation of land costs. But while the Audit Scotland report identified several examples of contemporary projects where there was a cost increase beyond anticipated levels, its findings were that in most cases the increase in project costs over the lifetime of a project could be attributed largely to inflation and not to anything fundamentally wrong with the initial estimates (**ADS000078**, appendix 3).

**ADS000078  
should be  
ADS00078**



28. TS could only operate within approved budgets and we could not fund a project, whether directly or by way of grant, unless we had budgetary cover, which depended on Ministerial and ultimately parliamentary approval. The projects which TS inherited had gone through appraisal processes which led to their being approved. Once a project was approved and budget cover obtained, then funding authorisation would be available. However, TS did not announce funding for projects: such announcements were made by Ministers and then incorporated into TS's budgets as part of the annual financial cycle. As noted, the Edinburgh tram project was included in the Labour and Liberal Democrat parties' 2003 partnership agreement commitments when the scheme was at a very early stage. There is an inescapable risk in announcing a funding commitment before there is a final business case and tenders have been accepted. Once funding is announced for a project you must assume that the costs will be contained within the budget, but that does not always happen. However, programme management is a dynamic process, and within a large project portfolio such as that operated by TS one can expect some offsetting effects between different projects
29. I have been asked whether the announcement of a budget would entice bidders to lower their prices artificially in order to come in under the set budget and therefore implicitly assist the scheme to proceed. That is perhaps a theoretical possibility. However at that particular time TS, and I suspect other commissioning organisations such as the Highways Agency in England and Network Rail, were having difficulty in getting sufficient bidders for projects because of the market conditions that I have already described. I am not persuaded that, in the then-prevailing circumstances of strong demand in the construction market, tenderers would have underbid to get the Edinburgh tram project through.
30. It seems reasonable to assume that before the parliamentary vote in 2007 it was expected that TS and CEC would share the burden of any cost overruns on the tram project, but I have previously explained that I am not aware of the background to any arrangements that were made before I was in post. It was

a jointly-funded project and, had things not changed in 2007, I assume that any cost overruns would have been considered and managed jointly.

31. I have been shown a handwritten note about costs by John Ramsay, TS, sent to Julian Ware, KPMG, and dated 10 November 2006 (**KPM00000020**). The note records at page 2 that TS required a more detailed breakdown of the separate tram Line 1a and 1b elements, including risk. I do not know if TS or KPMG received that breakdown. The note is dated during the period leading up to the papers which were considered formally by TS in December 2006. I assume, but cannot confirm, that this note was part of the working preparation for those papers.
32. I note that the final page of the document states that the capital cost estimate was obtained from an independent report by CS (which must be Cyril Sweett), other tram schemes (Liverpool and Dublin), and from indicative costs supplied throughout the procurement process. I have no reason to doubt that Cyril Sweett would have done a thorough job. The reference to other tram schemes indicates that information had been obtained from other cities with existing or proposed tram projects.
33. I have been shown a letter from Tom Aitchison to me dated 23 November 2006 (**TRS00003119**). The letter seeks an increase in funding. I have also been shown an email chain dated 23 and 24 November 2006 to which I was party (**TRS00003127**). In his email of 24 November, which was included in that chain, Damian Sharp responded to me and Bill Reeve expressing concern at what he considered to be an attempt to bounce TS and the Scottish Ministers into increasing funding for the tram project. There is an important passage in Tom Aitchison's letter on page 2, second paragraph: *"There is little doubt that the introduction of the Granton tram line would accelerate development and indeed we see the regeneration work and the enhancement of transport links as integrated processes. Equally we recognise that financial prudence must be applied to the decisions needed for the line to proceed. The addition of this line takes the total estimated capital cost to £592m."* I draw attention to this reference to financial prudence. The letter

goes on to state that, if there was agreement to increase total project funding to £595m, CEC would increase its share of the uplift beyond the agreed ratio applying to the underlying project - an offer which Mr Aitchison described as significantly more onerous for CEC. Towards the end of the letter (on page 4) the qualification implied in the reference to financial prudence was made more explicit: *"A total package of £595m would support a conditional commitment to the full Airport - Leith - Granton network and allow a modest sum for the preliminary work needed to refresh the work in support of a further extension to the South East of the City. It will reinforce confidence in the project as a whole, but will not commit either the Council or Transport Scotland to the full network"*. So while the earlier section of the letter appeared to be basing the proposition for additional funding on the objective of including Line 1b to serve Granton, by the end of his letter Mr Aitchison was actually stating that there would be no firm commitment to its inclusion. The CEC proposal was therefore effectively to increase the entire funding envelope without any bankable commitment to an additional deliverable. Damien's email of 24 November 2006 (**TRS00003127**) set out cogent reasons why the proposal should not be supported by TS. His concerns about estimates related to the combined total of £592 million for Lines 1a and 1b, and to the best of my recollection I believe related to the fact that the 1b estimate was less developed and the assumption that the Infracore contractor would price the additional work at marginal cost. His concern about reducing the pressure on developers stemmed from the objective of securing significant private sector contributions towards the eventual construction of Line 1b, to capture some of the development gain that the line would make possible. If additional public sector funding was seen as already committed that would create the impression among developers that Line 1b would go ahead regardless of any contributions that they might choose make.

34. I have been shown emails sent by Graeme Bissett dated 30 November 2006 (**CEC01820789**). I was one of the recipients of the second email in that chain. Referenced in that email were (i) a draft letter from David MacKay and Willie Gallagher to me and Tom Aitchison dated 30 November 2006 (**CEC01820790**), (ii) a draft reply which it was proposed would come from me



to Tom Aitchison (**CEC01820791**), and (iii) a draft reply which was drafted to come from Tom Aitchison to David MacKay (**CEC01820792**). It has been put to me that, despite the concerns expressed by Damian Sharp in (**TRS00003127**), the proposed draft letters seem to suggest that TS would commit further money for the full Phase 1 network. That is not apparent to me from these documents. By that stage internal discussion was already taking place within TS about the Draft Final Business Case (DFBC). The position that we reached in December 2006 represented TS's considered view that only Line 1a could be supported at that stage. This was clearly stated and explained in the advice we provided to Ministers (**TRS00003413\_0003** paragraph 15 and **TRS00003840\_0006** paragraphs 26-7).

35. I have been shown a letter sent by Tom Aitchison to David Mackay at TEL on 13 December 2006 (**TRS00003220**). That letter was copied to myself, and is stamped as received in TS on 18 December 2006. The letter is evidently based on the draft circulated previously (**CEC01820792**). Although it was put to me by the Inquiry that (**TRS00003220**) let TEL know that "TS might up their funding", detailed reading of the content shows this not to have been the case. The letter was very carefully drafted, and the only reference to increased TS funding, on page 1, is couched in highly conditional terms and makes no suggestion that TS would be likely to recommend that course of action. I have also been shown a paper dated 20 December 2006 which was prepared in my name and sent to the Scottish Ministers (**TRS00003413**). That paper recommended that the Scottish Ministers should not take any decision to support Phase 1b at that time (paragraph 15 on page 3). There was no inconsistency in TS's position: the CEC documents discussed above simply demonstrate that discussions were going on between CEC, TIE and TEL as part of the preparation for CEC's consideration of the project's DFBC, and that aspirations still appear to have existed among those parties to extend the scope of the project. It seems from the papers that I have been shown that Bill Reeve was sighted on those discussions; however, I was not aware of this at the time. Damian Sharp's email dated 24 November 2006 considered earlier (**TRS00003127**) represented and continued to represent the underlying

position of TS, which was unequivocally confirmed in the advice that was sent to Ministers (**TRS00003413**; **TRS00003840**).

36. The papers to which I have just referred stated the position that funding was only agreed for phase 1a and that the addition of phase 1b, although potentially increasing the BCR of the project, was not affordable within available funding. There may have been a wish on the part of TIE and CEC to keep the option of phase 1b open, but any future agreement would have been conditional upon external funding coming forward or upon significant savings in project costs. The recommendation was therefore to approve the DFBC for Line 1a, subject to confirmation of affordability when bids had been received, but that no decision to support Line 1b should be taken at that time. This recommendation explicitly reflected the advisability of not reducing the pressure on developers to contribute additional funding for that phase, to which I have already referred.
37. I have been shown an email chain which includes an email from Damian Sharp to Lorna Davies at TS dated 30 January 2007 (**TRS00003584**). That email records the reasons why TS did not send the draft letter to CEC that I have already mentioned and which was circulated by Graeme Bissett on 30 November 2006 (**CEC01820791**). The corporate position within TS as to the funding commitment remained entirely consistent, and there was no difference of opinion: all that was being debated in (**TRS00003584**) was whether the estimated contribution at outturn should be expressed as a range or at the potential upper bound. It is not the case that the Scottish Ministers made a new decision in or by January 2007 to cap their funding for the tram project at £375 million indexed to £450-£500 million. They were simply adhering to the existing position, which was the commitment that had been made in 2003. I believe from context, but cannot confirm, that the problem with the calculation of inflation that I have been referred to was simply uncertainty at that point whether TIE had used the same basis when calculating inflation on project costs and on the Scottish Ministers' financial contribution. Damian Sharp's email indicated the intention to resolve this when the scheme estimate was reviewed after the receipt of Infraco bids.

38. I have been shown an email that Damian Sharp sent to me dated 28 February 2007 (TRS00003935). Attached was a draft letter prepared for me to send to Tom Aitchison at CEC (TRS00003937). The draft concerned phase 1a of the project. In March 2007, when Scottish Ministers approved the allocation of £60 million for MUDFA and for tender evaluation, they made it clear that the BCR would have to be reassessed when the Final Business Case was submitted. The reason for this goes back to concerns that were flagged up in the document which contained advice to the Transport Minister, Tavish Scott MSP, dated 20 December 2006 (TRS00003413). We made a number of recommendations in that document about conditions which were proposed in order to achieve greater certainty in the cost estimates and the robustness of the BCR. It can be seen from paragraph 14 on page 3 that our advice was very direct, stating: *"note that the Business Case is marginal"*. TS did not suggest that the project was more beneficial than it was, and Damian was articulating conditions in the draft letter he sent to me in February 2007 that were designed to ensure that, by the time final bids were received, TS would be in a position to reach a recommendation about commitment to the full construction of the project that was based upon fuller evidence. At that point we could not anticipate that the status of the project would change profoundly later in the year. TS was at this stage asking for conditions to be met which would have been appropriate if Scottish Ministers had continued to have a potential financial exposure beyond their initial commitment. That of course ceased to be the case, and the immediate purpose of some of those conditions was overtaken by events following the Scottish parliamentary election and the change in Government. They nevertheless continued to have relevance for CEC in its ongoing management of the project.
39. I am asked why the BCR had to be re-assessed. That was because the project's procurement and delivery programme was phased, and the advance works were a stage in that programme. Full evidence on the likely costs of delivery would only become available when bidders' final submissions had been received and assessed. TS did not provide money on its own responsibility for the tram project: any release of further funding required Ministerial agreement. By early in 2007 TS had satisfied itself that the BCR

remained positive, and that was the basis on which we advised Scottish Ministers to approve the allocation of further funding for the next phase of the programme, to cover advance works and appraisal of final bids. No money was released before that point was reached and the final advice had been sent to Scottish Ministers and received their approval. It is also important to emphasise that TS was not recommending the release of £60 million as a lump sum. The recommendation was for the allocation of funds to be spent when required for tender evaluation and against the contract which had already been entered into by TIE for the MUDFA works. As I recall, MUDFA was a framework contract which provided rates for labour and materials. The MUDFA contract did not commit to a specific quantum of work. It was effectively a drawdown contract which TIE managed and, if TS had required to stop the project at any point during 2007, it is unlikely that all of that provision would have been spent. The funding was allocated against future approved expenditure as it was incurred, and during the period in the summer of 2007, when the future of the project was under further discussion, the MUDFA works were put on hold.

40. I am also asked whether the reassessment of the BCR would have provided a realistic check point bearing in mind the sums that would already have been spent on the project. I have already explained that that the tram project was being taken forward on a phased basis, and various hurdles were involved in that process, the first of which had been the necessity to obtain parliamentary approval. I cannot recall any instance where a project had proceeded to a late stage and the BCR had been found to be too low. If the BCR of the tram scheme had been found to be too low when the FBC was resubmitted, then any irretrievable expenditure that had already been incurred would have been at risk if no other options (such as re-scoping) were available. But this was a risk that the tram scheme shared with any other phased project. I am asked if TS advanced money to other projects in such circumstances. The precise meaning of that question is unclear to me, but I have to repeat that TS did not itself advance money to projects. All project funding was approved by Ministers from budgets that were agreed by the Scottish Parliament, and money was disbursed in accordance with the requirements of the Scottish

Public Finance Manual. If the question is instead whether funding was ever provided to projects that were subsequently cancelled, then the EARL scheme is an example of such a case.

41. I have been shown an email chain which included at the top my email to John Ewing dated 21 February 2007 (**TRS00003868**). This email was my response to his concerns, expressed in his email of 16 February 2007, that TS had not recalculated the BCR. I have also been shown an email chain which includes emails between Andy Park and Damian Sharp on 19 February 2007 (**TRS00003795**). My email on 21 February was written after that exchange of emails, and was informed by it. My email and the emails between Damian Sharp and Andy Park indicate the point we had reached in the assessment of the DFBC. Damian Sharp was the project's Senior Responsible Officer (SRO) and Andy Park was one of TS's economic analysts. Andy Park had expressed doubts about the valuation of the BCR in some earlier email exchanges but in the final analysis he calculated a BCR of 1.07 (the final email in his exchange with Damian Sharp), which was slightly higher than Damian Sharp's assessment of 1.04 (Damian Sharp's last email to Andy Park). Andy Park was well equipped professionally to review such calculations, and at the end of a thorough process of clarification and reappraisal he had concluded that the BCR was well above unity. Their emails illustrate the working through of our internal processes of consultation, scrutiny and challenge, which enabled me to feel comfortable in giving Scottish Ministers advice that, on the available evidence, the project had satisfied the BCR test. As I have already explained, the BCR was the responsibility of the project promoter, CEC. TS did not recalculate the BCR from scratch. Instead, the sensitivities underlying TIE's calculation on behalf of CEC were identified and discussed in detail between the SRO for the project, Damian Sharp, and the professional adviser on the economic side, Andy Park. They satisfied themselves that the BCR exceeded 1, and that was duly accepted through our management processes as the collective view in TS before being relayed to Scottish Ministers. If at any point Andy Park had felt that he was not happy with the outcome, or if his Director, Frances Duffy, had considered that his advice was not being followed, that

would have been brought to my attention. My email of 21 February 2007 to John Ewing embodied the outcome of two or three months of intensive work.

42. I am referred again to the Audit Scotland Report that I have already mentioned dated June 2007 (**CEC00785541**). I note that page 13 carries the headline that £79 million was spent on the tram project up to the end of May 2007, and that paragraph 48 attributes this expenditure to TIE. The same report records that TIE spent £17 million in taking the two tram Bills through Parliament, and that £60 million in funding from TS was provided for in the 2007/08 financial year. I have been referred to an email from Andrew Cooper to Ainslie McLaughlin dated 15 June 2012 (**TRS00026729**). Attached to that email is a document which includes, at pages 40 - 46, minutes of a meeting on 2 August 2007 between TS and TIE (**TRS00026730**). The funding allocation was discussed at that meeting. The £79 million allocation was used to support TIE in developing the project, and part of the money would have been spent on TIE's own costs in progressing the scheme and some of it on design and other external advice. It was not an open-ended grant: all costs incurred had to be accounted for and TIE would have been required to produce evidence of how they had spent all the money included in the total funding commitment.
43. The £79 million spent was part of the Scottish Ministers' total funding commitment, some of which had been disbursed before TS was established. Since most of the parliamentary costs were incurred before I was in post I am, as already explained, not in a position to confirm from direct knowledge on the statement in paragraph 48 of the Audit Scotland report (**CEC00785541**) that the £17 million spent on these parliamentary costs did not count against the project's anticipated final cost. I have been shown a TS Board paper dated April 2006 (**TRS00002378**). At page 3 of that paper, there is a breakdown of £32 million being the costs anticipated for April - December 2006. This illustrates the type of detail that TS was provided with when considering grant funding for the tram project.



44. I would accept that there was a danger that the provision of such sums before submission of the DFBC and FBC built momentum to go ahead with the tram project regardless of what further Business Cases might say. We clearly recognised this risk in paragraph 10 of the advice to Scottish Ministers already referred to (**TRS00003413\_002**). It made it less easy to stop the project, but not impossible. Any phased project could be stopped at any stage but some expenditure would inevitably be written off. Not all the money spent would be wasted, however - for example the investment in improving the utility services in Edinburgh had a longer-term value, and land acquired for the project could have been resold. However, the risk of momentum was one that we did not hide from Ministers. It was a risk that the tram project shared with any phased project.
45. All sums provided for the tram project as described in the Audit Scotland report of June 2007 (**CEC00785541**) would have been allocated against approved expenditure. I no longer have access to the relevant detail, and I have explained that some of the £79 million was spent before I was in post. However, as I have already described, the TS paper dated April 2006 (**TSR00002378**) gives at page 3 a breakdown of expenditure proposed from April to December 2006. The further £60 million allocated to the tram project in March 2007 formed part of the Scottish Ministers' total committed funding for the project, and was provided solely to ensure that the project stayed on programme. If MUDFA had not proceeded the whole programme for the tram project would have slipped and that in turn would have impacted on the assumptions underlying the Business Case. Such a delay might also have undermined the confidence of tenderers for the main contracts that the project would proceed, risking their withdrawal. TS certainly did not recommend its release to help ensure that the project would survive the election of a new administration. The tram project was an existing commitment by Scottish Ministers, and the £60 million provision was simply to allow the project to maintain the programme that had been the basis for the original approval.

## Interim Outline Business Case (IOBC) and Outline Business Case (OBC)

46. I am aware that several versions of the Business Case were produced in the run-up to financial close in May 2008. I do not recollect whether I saw the original versions of these business cases. Those that were considered when I was in post in TS would have been reported to me as part of our normal processes. I would certainly have been made aware of the findings of these business cases and any issues that they generated, but at this distance in time I cannot recall specific details.
47. When TS received the various iterations of the Business Case, the responsibility for receiving and checking them would lie with the part of TS which was managing the rail projects. As I have explained, Bill Reeve was the Director of Rail Delivery and Damian Sharp the Head of Rail Projects. They would draw as necessary on internal advice from other parts of TS, including advice from the economic analysts. On occasion, because of resource and time pressures, external advisers such as KMPG were used to provide additional input to the consideration of business cases. If there was an issue with a business case then TS would go back to CEC and TIE in the first instance to seek clarification and where necessary their re-examination of particular aspects.
48. I have been shown a letter sent by John Ramsay dated 22 April 2005 to Stewart McGarrity, which included a refined list of TS comments on the Interim Outline Business Case of 31 March 2005 (**TRS00008519**). I was not briefed on and did not see the IOBC, as that was before I was in post. I cannot therefore comment on the specific issues raised at that point. I have already explained that all the major public transport projects that formed part of TS's initial portfolio were inherited from the Scottish Executive's Transport Group, and had been approved by the Scottish Ministers before I was appointed. I cannot say whether Optimism Bias (OB) was applied, how, and at what level.



49. I have a general understanding of OB. It is a concept that is based in psychology rather than in economics or finance, and stems from the innate tendency on the part of individuals to underestimate risks when assessing an outcome. The introduction of OB was an attempt to counteract this factor when assessing a project by introducing a margin to reflect such optimism. Different rates for OB apply for different projects at different stages – uncertainty is greatest at the outset, but as delivery proceeds the areas and extent of potential risk are reduced. The literature for OB has developed enormously over the last ten years and it is now possible to go online and access spreadsheets which will assist in developing a project-specific allowance for OB. The methodology was not so developed and not so readily available a decade ago, and anyone involved with OB at the earlier stages would still have been feeling their way. I am unable to comment on the actual provision that TIE made for risk or OB because I do not know what TIE's working assumptions were when they made those provisions, whether they were working to a specific percentage, and how they made their assessment of an appropriate level of risk provision for the tram project..
50. I have been referred to a presentation that KPMG gave on the IOBC around July 2005 (**KPM00000053**). I repeat that TS was not in existence at that time and that presentation was before my involvement. I cannot therefore comment from direct knowledge on that presentation, nor on any matters that arose from it.
51. By the time I took on my responsibilities at TS the principle that the tram project was a jointly funded project was already well established. There was always intended to be a CEC contribution. It is public knowledge that CEC had originally proposed a congestion charging scheme as part of its transport strategy for Edinburgh which would have provided CEC with a much more substantial funding stream. I assume that the outcome of the referendum on congestion charging, by removing this potential funding source, influenced the extent of the Scottish Executive funding that was required, but as this was a matter that was resolved before I was in post at TS I have no knowledge of how these joint arrangements were arrived at.

52. I have been shown an email sent to me sent by John Ramsay on 24 April 2006 (**TRS00002376**). Attached was a memo dated 23 April 2006 from Damian Sharp (**TRS00002377**), and a paper on the OBC that Damian Sharp had prepared and to which I have previously referred to in my statement (**TRS00002378**). I note that one of the issues noted at paragraph 2 for discussion was how TS would work with CEC, TIE and TEL. I was not involved in that discussion. Damian Sharp's memo (**TRS00002377**) indicates that Damian was preparing for a further paper to TS's Major Investment Decision Making Board (MIDMB). Damian was simply following good practice by asking for comments on the content of that paper. If I had had any comments I would have discussed the paper with Damian at the time; however, I cannot recall the nature of any conversation that might have taken place.
53. I have been shown a paper about the OBC prepared by John Howison dated 28 April 2006 which was copied to me and others (**TRS00002389**). In the paper he states at paragraph 2 that the procurement strategy hinges around the advance appointment of an operator and that he was not clear about the role of Transdev and TEL. The purpose of that paper was to respond to Damian's request for comments before he finalised his paper. I am confident that Damian would have taken account of John Howison's comments when finalising that paper.

### **Draft Final Business Case (DFBC) – December 2006**

54. The DFBC (**CEC01821403**) was provided to TS in November 2006. I did not see the complete DFBC myself at the time and the extent of my involvement was only in reviewing the papers based on the DFBC that were presented to the MIDMB, and the subsequent advice to Ministers.
55. I have been shown a letter from Damian Sharp to Andy Harper at TIE dated 22 December 2006, which includes the TS minutes of the Panel Review of Major Projects meeting on 24 November 2006 (**CEC01358732**). I did not see

this paper at the time and I was not present at that Panel Review meeting or party to any related discussion. I am not therefore in a position to comment further from direct knowledge.

56. I have been shown a memo on the DFBC by Cyril Sweett dated 27 November 2006 (**TRS00003141**). The memo noted concerns about the lack of information on how TIE reached its cost estimates, the low level of contingency, and lack of Optimism Bias. I did not see this memo at the time; however the comments that were made in it were reflected in the report that came to the MIDMB so I would ultimately have been aware of the substance of the remarks that Cyril Sweett had made.
57. I have been shown an email sent by Andy Park, TS, on 13 November 2006 which was then forwarded to others the next day (**CEC01797363**). Attached to Andy's email was a note that he prepared (**CEC01797364**). In the email and note, he identified what he considered to be a serious error in the Draft Final Business Case. I have been shown two emails in response to Andy Park's email and note. The first was from Stewart McGarrity on 15 November 2006 (**CEC01820077**) and the second from Andie Harper on 17 November 2006 (**TIE00002892**). I have also been referred to Steer Davies Gleave's response dated 14 November 2006, which disputed that there was any error in the BCR (**TIE00737785**). I was aware at a high level as part of the comprehensive report we received about the DFBC that the BCR was an issue. I was not aware of the detail that led to the conclusion that there was a serious error with the BCR and I was not aware of Steer Davies Gleave's comments at the time. I have not been shown any reply to SDG's response of 14 November (**TIE00737785**), nor any other follow-up correspondence, so I am not aware how this particular matter was resolved. It is evident, however, from Andy Park's later comments on the BCR that I have already referred to (**TRS00003795**) that his earlier concerns must have been satisfactorily resolved.
58. What these papers reflect is a process of clarification of the DFBC that was being progressed transparently between the organisations concerned. I have

already explained that this process led to agreement within TS that a BCR higher than 1 had been satisfactorily demonstrated.

59. I have been shown a document entitled 'Edinburgh Trams - Draft Final Business Case - Presentation to Transport Scotland' prepared by KPMG dated 4 December 2006 (**TRS00003162**). This was a presentation, mostly in bullet form, on the Draft Final Business Case. Many of the points that KPMG raised were incorporated into the information that was considered by TS's MIDMB (**TRS00003241**) and subsequently by the Transport Minister, Tavish Scott MSP (**TRS00003413**). They also influenced TS's final comments to CEC on the DFBC (**TRS00004145**).
60. KPMG's presentation included a timeline on page 4, which showed the DFBC's being submitted in December 2006 and approved by the Transport Minister, Tavish Scott MSP, in February 2007. When TS withdrew from actively managing the tram project, it was clear that one of the things that was still expected was a Final Business Case. This remained a condition within the revised grant arrangements. As previously explained, the tram scheme was a developing project and the DFBC was appropriate to the project at that phase of its development. While the FBC was based on fuller information, I wouldn't say that one was more important than the other. Each constituted a point at which the project was reviewed and could be reconsidered if necessary.
61. I am not aware of a final version of the KPMG presentation and I cannot confirm from memory if I have previously seen this presentation or any other version of it. I was certainly aware of the outcome of its consideration as reflected in (**TRS00003413**), to which I have previously referred. I note from the KPMG presentation the project cost estimate was £522 million and KPMG advised that 12% OB uplift was too low and recommended a 20% uplift (page 5). I am unable to say whether OB was being added to a risk provision that TIE had already made in the calculation. If a 20% uplift was applied it would have taken the cost estimate of the project to £557 million. It is suggested to me that it would have been convenient for TIE to reduce OB as much as possible. That might have been a possibility, but I obviously cannot comment

from direct knowledge whether TIE actually did so or not. I note that KPMG stated that the price submitted by bidders before a preferred bidder was selected might not necessarily be accurate, as bidders might tell TIE what they want to hear to remain in the competition (page 12). However, I have already indicated that, given the state of the market at that time, I am not persuaded that bidders would have deliberately under-bid. No evidence has been provided to me that bidders were consciously under-estimating or under-bidding to try and stay in the competition.

62. I note that TIE intended to make most of the payments to Infracore during the construction period, whereas KPMG advised that payment of a significant amount of the contract price would normally be at the end of the construction (page 13). KPMG also advised that if the contractor was paid earlier then it would be prudent to increase the risk contingency (page 13). At that stage TIE was committed beyond the point of recall to the procurement process it had adopted. It had already invited bids, and to have re-opened the basis of the invitation to tender would have invalidated those bids. If TS had asked TIE to change the procurement process at that point then it would have been necessary for the whole process to have been started afresh, putting the entire project programme at risk.
63. TS received the DFBC in November 2006 (**CEC01821403**), and began the process of reviewing it. TIE addressed some of TS's concerns in the form of a revision to the DFBC, before TS produced its final comments on the DFBC on 30 March 2007 (**TRS00004145**). I was not personally involved in the production of TS's comments, but I have already explained that many of the issues included in that response formed part of the content of previous papers. I was aware of the recommendations that Damian Sharp had made to address these issues and I agreed with those recommendations.
64. I have been referred to Section 6 (page 5) of TS's response to the DFBC, which stated that the governance section of the DFBC needed to be strengthened significantly. I cannot confirm at this distance in time whether this referred to improvements in the arrangements for governance itself. It is

equally possible that what was being asked for was that the DFBC should be more explicit about the governance arrangements. Section 10 (pages 7 - 9) noted TS's concerns about how risk management would be taken forward. It stated that 12% risk allowance was optimistic (page 7) and that the P90 figure appeared where a P80 figure was expected (page 8). P90 and P80 figures were the probability of a risk appearing, and the comments seem to suggest that they had been transposed or incorrectly stated. All these concerns would have been addressed in the detailed discussions that Damian Sharp and his colleagues had with TIE before TS produced the final advice to Ministers. The comments noted that the entire detailed design for the project was intended to be completed in October 2007 and questioned whether that was realistic (section 11, page 9). By October 2007 TS was no longer as closely involved in the tram project. However these comments were made early in 2007 and in drawing attention to the fact that the detailed design programme was tight we expected TIE to take account of those comments.

65. I have been referred again to the DFBC produced in November 2006 (**CEC01821403**). At paragraph 9.12, page 138, it states that: *"TIE has continued to comply with the HM Treasury recommendations for the estimation of potential Optimism Bias and has determined, in consultation with Transport Scotland, that no allowances for Optimism Bias are required in addition to the 12% risk allowance above."* I have also been referred to the FBC dated 7 December 2007 (**CEC01395434**). At paragraph 10.14 (page 161), it reiterated that TS agreed that there was no need for OB in addition to the 12% risk allowance. I have no knowledge of who within TS specifically agreed to that proposition, and I note from a document that has already been drawn to my attention that the OB allowance was under discussion with the Scottish Executive in 2005, before TS was established (**TRS00008519**). When considering the DFBC TS was aware that part of TIE's case for that lower figure was based on their identification of potential project cost savings which provided an additional risk buffer (**TRS00003840\_0003** paragraph 13). Some TIE documents refer to OB and others to a risk allowance, so there was evident confusion in terminology; however, this was at a relatively early stage in the application of OB and terminology was perhaps not being applied as



precisely as one would now expect. TIE's position was that they had allowed a risk contingency of 12% and the OB guidance was quite explicit that risk could be managed down. It was TIE's responsibility to take a view on the extent to which they judged that they could manage the risk down, and by December 2007 it was for CEC, as the organisation ultimately bearing the financial risk, to satisfy itself with TIE's calculation of the appropriate provision within the FBC. TIE's decision might not be regarded as good practice currently, but at that time, when OB experience was still being developed, I would not say that it was necessarily bad practice.

66. The recommendations made by TS in light of the DFBC were embodied in the conditions of grant which TS recommended to Scottish Ministers in February 2007. TS had a direct means of monitoring adherence to those recommendations up until the change in governance of the tram project in the summer of 2007. Subsequently TS had to rely on the new conditions that had been incorporated into the revised grant offer, which included the requirement for a FBC and a Gateway Review, to ensure that the project remained in good shape going forward. I have been asked if, from the DFBC submitted at the end of 2006 or the FBC at the end of 2007, it had become clear that the project was not viable, what would TS have done, and specifically if it would have withheld funding. That question is hypothetical, and is perhaps expressed in the wrong terms. As I have repeatedly pointed out, the release of funding for the tram project was authorised by Ministers. In any instance of failure to comply with grant conditions, existing authorised funding could be withheld. However, both the DFBC and the FBC were a pre-condition not of current but of future funding tranches, so if either business case had demonstrated a lack of viability I would have advised Ministers of that fact and would have been unable to recommend any further funding release unless the situation was remedied.
67. I have been shown the FBC v2 (**CEC01395434**) which was produced in December 2007. By the time the FBC was produced, the Scottish Government had capped its funding and TS had withdrawn from the

governance structure. I have been shown a background note prepared for First Minister's Questions by John Ramsay on 13 September 2007 (**TRS00004816**). I see that the note states that TS was content to receive a FBC that had been endorsed by CEC. I have also been shown an email chain which includes an email from Lorna Davis, TS, to Andy Park dated 15 October 2007 (**TRS00004991**). In that email, she stated that TS did not need to undertake an in-depth review of the FBC. That is consistent with the nature of the review of the FBC v1 that TS undertook in October 2007 (**TRS00004992**). That paper refers to its status as a "light review" (page 1 paragraph 1), and identified the conditions upon which Ministers required assurance, namely that the project remained affordable; that it continued to demonstrate a BCR greater than 1; and that it required no ongoing subsidy from the Government. The review concluded from the evidence of the FBC that all three conditions had been met. As Ministers' overarching pre-conditions had been met, then in terms of the project governance at that stage that was sufficient for TS if the FBC was otherwise acceptable to CEC (which by that point was carrying the full risk of the tram project).

## **Decision to Proceed**

68. I have been shown an email that Angus Macleod, TS, sent to TS staff dated 12 December 2006 (**TRS00003217**). Attached to that email was the final copy of the tram project paper for the Major Investment Decision Making Board (MIDMB) dated 13 December 2006 (**TRS00003219**). The purpose of the paper was to seek the MIDMB's views on the DFBC, and it was indicated at paragraph 1 that the paper would also form the basis of advice to Scottish Ministers.
69. The MIDMB was a governance process that TS had adopted from the Scottish Executive's Transport Group. As Agency Accountable Officer, I was the Investment Decision Maker (IDM). However, for the purposes of good governance and because there were times when inevitably I could not be present to make those decisions in person, we used the MIDMB process to



provide corporate scrutiny of major projects at key decision points. Our process was deliberately structured so that the advice came not just from the officer who was the project owner or otherwise responsible for the project, but also from other relevant parts of the organisation, including the corporate finance function and the sections within TS that were responsible for evaluation and for policy coordination. In the normal course of events I would seek to attend those meetings, but I did not usually chair them. The designated chair was TS's Director of Strategy and Investment, at the time Frances Duffy. Her directorate had no delivery responsibilities other than for various research projects and for interfacing with the ORR, and Frances had no personal responsibility for major contracts; however what she and her part of the organisation did provide was the analytical, evaluation and policy coordination capabilities. These arrangements provided a means for scrutinising a project systematically and in depth before it reached me for final decision. It meant that when I made a decision on what advice should go to Scottish Ministers about a project or other major investment, I took that decision based on informed corporate advice from within TS. Those who were most directly involved with a project engaged with other senior colleagues within TS to ensure that an objective and informed view was reached when key decisions had to be made about that project.

70. I have been asked why a conditional recommendation was made on the DFBC before full scrutiny of it could be completed, since the DFBC was still being refined when that paper came to the MIDMB. Although TS's final comments on the DFBC were not issued to TIE until March 2007 (**TRS00004145**), internal review had been completed in time to inform the final advice to Ministers of 20 February 2007 (**TRS00003285**). The perceived urgency in late December 2006 arose from TS's understanding at that time that any decision to release further funds for the tram project would require to be made by full Cabinet, making it necessary to fit in with the programme for circulation of Cabinet papers. Consequently TS expected to have to offer a view to the Transport Minister before the end of 2006 in order for it to enter the agenda processes for the next Cabinet meeting. As it transpired, Ministers took the view that the decision should be taken at Cabinet level but not in

TRS00003285  
should be  
TRS00003825

Cabinet itself. Instead the decision was ultimately taken by the First Minister, Jack McConnell PC MSP; the Transport Minister, Tavish Scott MSP; and the Minister for Finance & Public Service Reform, Tom McCabe MSP. Consequently, some of the immediate urgency disappeared from the situation and that allowed subsequent papers to incorporate later information.

71. A recommendation for the release of further funds did not mean that the tram project would continue to go ahead regardless of any new information or changed circumstances. Scottish Ministers always had the option of stopping the tram project and at TS we likewise had the option of advising Scottish Ministers to stop the project. Any decision taken at that time did not preclude a subsequent change of position. If TS had reached a point where we considered that Scottish Ministers were likely to be put at risk beyond the total funding that was allocated to the project, then we would have advised Ministers accordingly. Tender prices, an adverse Business Case, or the emergence of a significant problem during delivery of the project would for example be factors that might have led TS to recommend reconsideration of the future funding of the tram project even after the decision to proceed with utilities diversion had been made.
72. At Annex C, page 13, of the paper for the MIDMB dated 13 December 2006 to which I have already referred (**TRS00003219**), it is stated that TIE had allocated an OB uplift of 12% for tram route 1a and that an OB uplift of 20% was more usual for tram projects. The 20% figure was probably taken from the KPMG presentation on 4 December 2006 (**TRS00003162**) at page 5, to which I have already referred. I have been asked why, when it is stated at Annex C on page 13 that the allocated OB for Phase 1a was £58m on £464m [=£522m], the adjacent box under the heading "Level and Mitigation" states the total cost of the project to be only £500m, i.e. a difference of £22m. At this distance in time I cannot recall what explanatory clarification was given at the meeting. It seems, but I cannot now confirm, that the box specifying the OB figures was populated from the KPMG report, whereas the total of £500m quoted was taken from TIE sources. TIE's practice appears to have been to quote the rounded midpoint of the OB range as a spot value (see

(**TRS00003795\_0002**) dated 19 February 2007 for Damian Sharp's observations to that effect). This seems to be borne out by reference to later documents which continued to attribute an estimate of around £500 million to Line 1a of the tram project (e.g. paragraph 45 on page 12 of the June 2007 Audit Scotland report (**CEC00785541**) and paragraphs 10.9 and 10.36 (pages 161 and 164) of Version 2 of the FBC (**CEC01395434**)). I acknowledge that, in the absence of any accompanying clarification in the document, this difference in the basis of the two boxes is not helpful, but if my assumptions are correct it is a presentational defect rather than "erroneous arithmetic". This difference in how the estimated project cost was expressed does not alter the key message about affordability that appears in the "Level and Mitigation" box, that even with the full 12% OB allowance on the estimated cost [i.e. = £522m] there would still be headroom within a £545 million total funding provision.

73. I am aware that TIE's allocated OB uplift of 12% for Line 1a relied heavily on the success of TIE's risk mitigation strategy. TS's recommended conditions of grant were intended to ensure that TIE's processes and risk mitigation strategy remained effective enough to sustain the level of OB reduction that it proposed. The papers also indicate that TIE ran a Monte Carlo analysis where a large number of scenarios were tested randomly, some of which were at the extremes of probability. Based on this analysis, TIE concluded that there was a greater than 90% chance that the tram project would come within the funding envelope of £545 million. TIE had run a recognised statistical test and the evidence at the time gave a comfortable level of assurance of the expected affordability of the tram project.
74. I have been shown an email from Andy Park to Damian Sharp dated 18 December 2006 (**TRS00003240**). Attached was a marked-up version of the MIDMB report (**TRS00003241**). In his email Andy Park stated that a trawl of the STAG report to include additional benefits had not been entirely positive and he was worried about creating a misleading picture. When TS received a Business Case we would check against standard appraisal techniques to make sure that every potential benefit or disbenefit was included so that we could give the best possible advice to Scottish Ministers. Andy Park was

referring in his email to matters detailed in the marked-up report he attached. One of the intended economic outcomes of the construction of the tram was to increase business activity in the areas affected. Since it was presumed that businesses would enjoy a boost across the local area because of the tram project, more travel would be generated. However, because some of that additional travel would be by car, carbon emissions might go up rather than down because of the tram, an adverse environmental outcome. This was a good example of an unanticipated effect, and Andy Park was being robust in his analysis by identifying that TIE should not attribute additional environmental benefits from the tram project when in fact analysis suggested otherwise. The MIDMB report was also amend to make clear that under different assumptions the initial Value of Time survey outputs would show a reduction in the BCR below 1 for Phase 1a. Papers issued to Ministers after the MIDMB on 13 December took account of further refinement of the issues that were under discussion, and continued to draw attention to remaining risks.

75. My attention has been drawn to page 8 of the advice Damian Sharp gave to the MIDMB (**TRS00003219**), where at paragraph 20 he said that no account was taken by the DFBC of construction impacts. That paragraph was drawing attention to a difference from the methodology used in appraising projects on the regulated Network Rail system, where a financial proxy was available for disruption effects. Damian was advising that in the absence of a financial measure of construction impacts it was important that TIE put in place adequate measures to mitigate such adverse construction impacts.
76. I have been shown an email exchange, of which I was part, dated 22 and 29 December 2006 (**TRS00003412**). In my email of 22 December, I attached a paper with advice on the DFBC (**TRS00003413**) to the Minister for Transport, recommending that Scottish Ministers approve the DFBC dated November 2006 (**CEC01821403**) for Line 1a (paragraph 13), and that no decision should be made to support Line 1b (paragraph 15). I have already referred to this paper in my statement, and to correspondence being generated in draft and final form within TEL, TIE and CEC in late November and earlier in December

2006 about possible increased funding for Line 1 as a whole. This correspondence predated the Ministerial correspondence referred to above, and I refer to Damian Sharp's paper dated 24 November 2006, to which I have previously referred in my statement (**TRS00003127**) as representing TS's underlying position that we should not be bounced into recommending a higher level of commitment. The separate discussions that were taking place between CEC and its delivery organisations, TIE and TEL, related to that Council's own approval processes for the DFBC. TS would not have expected to be kept fully sighted on the nature and basis of those internal discussions between CEC and its subsidiaries.

77. The letter from TS to Tom Aitchison at CEC dated 17 January 2008 and signed by Bill Reeve (**TRS00005069**) to which my attention has been drawn has no relevance to the matters discussed in the immediately preceding paragraph of my statement. It was written in the circumstances of the entirely different arrangements with CEC that applied after the parliamentary election in 2007 and the change in approach towards the tram project that was adopted by the new Scottish Government. While the heading of this letter refers to grant of funding for Line 1, it is completely clear from the body of the letter that Scottish Government funding is being offered, as previously, solely in relation to Line 1a.
78. I have already discussed Optimism Bias, which is intended to counteract the generic risk that people tend to look on the optimistic side and discount risk. Risk allowance related to identified risks to which a specific project may be exposed. It could be as simple as not knowing what ground conditions might be encountered, or recognising the potential impact of a delay that was not within the promoter's control, or providing a margin when anticipating contract prices.
79. Contingency allowance is a related concept but tends to be more immediately relevant to the contractual process. If a contractor submits a bid on a fixed price basis they would be likely to include a percentage figure for contingencies, to provide for any unanticipated risks. A contractor would



include an element for identified risk when pricing a tender, but not every risk can be fully identified or scoped in advance, hence the use of contingency allowances. The construction procurement process has two sides: those seeking tenders for work to be undertaken, and the bidders for that work. Those putting a tender out want to minimise their risk exposure and to have as good a handle as possible on what bidders have offered as an overall price. The bidders want to have a sufficient margin within their overall price to make sure they do not lose money on the project.

80. Referring back to the document TS submitted to the Minister for Transport dated 20 December 2006 (**TRS00003413**), I note that Annex B of the paper set out the key risks facing the tram project. The 'Level & Mitigation' column indicated the level of the risk. This risk was assessed as high for Capex Costs. The mitigation recommend was fuller design work, and a more robust negotiating strategy with Infracore bidders, but it was acknowledged that a weak market was a factor. The paper set out what was being done to address those risks. Beyond that, the conditions of grant which were recommended in this paper (Annex C) included measures for improving the robustness of the project's management by TIE. Approval of the Business Case was being recommended because TS considered that the BCR remained above unity.
81. Annex C of the paper set out the conditions and controls envisaged by TS as necessary to achieve success if Scottish Ministers continued to support the tram project. As I have explained, the status of the tram project changed fundamentally in the summer of 2007. Consequently, conditions that TS had recommended and were appropriate when we envisaged that Scottish Ministers would be at risk on a cost overrun were no longer relevant from a Scottish Government perspective after future cost risk on the tram project had become the responsibility of CEC. Since grant for the project was paid via CEC, the latter would have been fully aware of these conditions at the time they were imposed, and it then became a matter between CEC and TIE as to what extent those specific recommendations continued to be required after the change in governance.

82. Until TS withdrew from the Tram Project Board (TPB) in August 2007, we had a direct means of monitoring progress. After the change in the status of the project, TS could still withhold funding at any point if the revised grant conditions were not being met. TS thereafter managed its responsibilities for the project on the basis of evidence of spend. If TIE had demonstrated that they had spent money appropriately on the project then CEC was entitled to be paid that amount. That was the only direct control TS had going forward within the Scottish Ministers' commitment to fund the project to the extent of £500 million. If money was not being properly applied by TIE then that expenditure would not have been reimbursed by TS.
83. A Gateway 3 review was undertaken before contracts were awarded. There was evidence from TIE that it had been undertaken. TS was not party to that process although I recall that I was interviewed as part of the Gateway review. TS was aware that the review had been carried out but it was a matter for CEC to deal with any recommendations in the Gateway Review.
84. I have been shown an email Damian Sharp sent to Bill Reeve and others dated 19 December 2006 (**KPM00000135**). It included as an attachment the note that was intended to be sent the next day to the Transport Minister, Tavish Scott MSP. In his email, Damian stated that the latest possible date for entering pre-digest was 29 January 2007 but that would have required TS's paper to be non-controversial. It is my recollection that this was the usual terminology that was applied to distinguish between advice to a Minister that was purely routine, and advice that would require discussion with other Ministers. Because the paper put to the Transport Minister, Tavish Scott MSP, contained such issues, I would have expected that Mr Scott would have wished to discuss it first with Mr McCabe, the Minister for Finance and Public Service Reform, if it was to be submitted to Cabinet.
85. The paper dated 20 December 2006 submitted to the Minister for Transport demonstrates that TS was giving Ministers clear advice that aspects of the tram project needed more work. While TS felt that the information available at

that time was sufficient for the project to continue to the next stage, we were not then in a position to recommend commitment beyond that stage.

86. Alongside the paper prepared for the Transport Minister that I have just been discussing, TS prepared a draft memo for the Transport Minister to send to the Cabinet. I have been shown an email sent to me by Katie Beattie dated 29 December 2006 (**TRS00003412**) attaching a copy of this memo with one change marked by the Minister before circulating it. The change is shown in tracked changes (**TRS00003414**). I understand that the memo as amended was sent by Mr Scott to Cabinet colleagues. This memo noted that the tram project would cost £500 million (paragraph 5) and that the Minister had asked TS to review the risks in relation to the tram project to ensure that this funding release was accompanied by further improvements in project control as the scheme moved towards full implementation (para 12). The risks were all articulated in the papers I have already mentioned that went to the MIDMB, and the conditions that TS recommended should be imposed on any future grant for the tram project addressed those risks. There were deficiencies in project control and not all of those were the immediate responsibility of TIE. The fact that TIE's consultants were late in finalising designs meant that there was a significant risk exposure which needed to be managed. I have already referred to issues with the DFBC. The recommendation that the Scottish Ministers should approve the DFBC was cautiously and conditionally worded, and certainly did not say that everything was fine with the tram project for its entirety: the financial recommendation only extended to the next phase, the MUDFA contract and the analysis of tenders. The draft Cabinet memo noted that the Business Case was marginal (paragraph 2) and that risks remained in terms both of cost and benefits. The recommendation included a specific reference to the need to improve project control, and the grant conditions that had been prepared by Damien Sharp included measures that address that issue.
87. I have been shown two letters: the first is a letter from Willie Gallagher to the Cabinet Secretary for Finance and Sustainable Growth, John Swinney MSP, dated 28 June 2007, and the second was a reply from me to Willie Gallagher



dated 31 July 2007 (both at **TRS00004617**). In his letter, Willie Gallagher invited the Cabinet Secretary and the Transport Minister, Stewart Stevenson MSP, to make an official visit to TIE. I replied to that letter on behalf of the Cabinet Secretary and the Transport Minister, who did not consider it appropriate to conduct such a visit. I have been asked by the Inquiry whether Mr Gallagher's letter implied that TIE were the promoters of the tram project. It is my understanding that TIE were fulfilling that role on behalf of CEC. I have been asked to comment further on the role of TIE. TIE was a professional organisation, established by CEC with specific purposes in mind. These included managing projects other than the Edinburgh tram project, but the tram project was a very large part of what they were tasked to do. TIE was part of CEC and was subject to audit and the normal controls that exist for any public sector body. One was entitled to assume that TIE could be trusted as an organisation. I am not aware of any evidence that suggested that TIE was not presenting accurate information to funders.

88. I have been shown a letter that I wrote to David MacKay and Tom Aitchison on 2 August 2007 (**CEC01643223**). That letter set out TS's role going forward, and the conditions that had to be satisfied for the release of future grant funding. The letter explicitly stated that TS intended to relinquish its seat on the TPB and would not then attend future meetings in any capacity. I have also been shown Tom Aitchison's reply dated 16 August 2007 stating among other things that CEC accepted the revenue risk (**TRS00004704**). As I read his letter, I assume that this last point referred to the second bullet point in my own letter, which related to operational subsidy. During the preceding weeks the Cabinet Secretary, John Swinney MSP, had made it very clear that the tram project was CEC's project and that the project was at their financial risk beyond the £500 million that the Scottish Government had committed. Tom Aitchison's letter did not seek to challenge or alter that position.
89. TS did not simply "hand over £500 million". TS's authority from Ministers to release the balance of the £500 million grant for the tram project on a phased basis was dependent on the satisfaction of conditions by CEC. Ministers were fulfilling the terms of the resolution passed in the Scottish Parliament on 27

June 2007 that funding up to the level previously agreed would continue to be made available, and that the project should become the responsibility of CEC. That may not have been the initial wish of the new Government, but Ministers had accepted Parliament's decision, and that was what TS implemented. The conditions of future grant outlined within **(CEC01643223)** were intended to ensure the delivery of financial close on a robust basis so that the Scottish Ministers' investment would be protected going forward. I have been asked whether this was "normal". These were not "normal" circumstances: this was the only transport project of which I am aware where there was an explicit risk transfer from the Scottish Government to the local authority. TS had other joint projects with local authorities, but those retained a shared risk exposure. There is therefore no standard of "normality" to apply, other than the requirements of the Scottish Public Finance Manual, which continued to be met. I have not been made aware of any audit view that TS was not spending money appropriately on the tram project after the basis of that project changed.

90. The Scottish Ministers' clear intention was that from summer 2007 onwards the tram project would go forward at the risk of CEC, which wished the project to continue. It was an unusual situation for a project to go ahead when Ministers had indicated they wished to cancel it. The Scottish Ministers stopped the Edinburgh Airport Rail Link project later that summer. They subsequently cancelled the Glasgow Airport Rail Link project. The Scottish Ministers could stop projects despite their approval by a previous administration.
91. I have been asked to speculate from hindsight about what more might have been done in relation to oversight and protection of the funding for the tram project that TS was administering on behalf of the Scottish Ministers. Clearly such reflections can have little or no evidential value, but so far as I am aware Ministers' financial exposure to the tram project was not increased by the later problems that were encountered – their funding therefore continued to be protected. Beyond that, I consider that it was reasonable to expect that the second largest local authority in Scotland, well-resourced financially and

professionally, and with significant collateral at its disposal, would be very well equipped to provide all the necessary oversight of a project which it had promoted and which was being executed through its own subsidiary organisations. So, even with the benefit of hindsight, my conclusion is still that what was actually done was appropriate to the circumstances and requirements of the time when these decisions were being taken.

## **Project Governance Arrangements**

92. My understanding is that TIE, TEL and the TPB were all CEC entities, and exercised their respective functions under delegation from CEC. TS had no right or power to change those bodies - that would have been a matter for CEC. The oversight and delivery mechanism for the tram project in the form of the TPB, TIE, and TEL pre-existed TS. What TS therefore inherited was a set of governance arrangements that were already in place and which were primarily the responsibility of the other statutory party, CEC. Any influence that TS could exert was either through the partnership governance arrangements while they were in place or else indirectly through the conditions that were attached to the grant for the tram project. That was the extent of TS's ability to promote or require any change in the tram project.
93. I have also explained that when TS was established on 1 January 2006 the tram project was an existing partnership between the Scottish Executive and CEC. This arrangement had evidently achieved maturity and substance because CEC had succeeded in taking both Tram Bills to their final stages in the Scottish Parliament. I did not expect to review the governance of every partnership arrangement TS had inherited; that was the basis on which projects had been set up and on which they were being carried forward. As long as governance arrangements were working satisfactorily then there were greater immediate priorities for TS than carrying out a detailed reappraisal of such arrangements. The relationship with CEC was working well and the relationship between TS and TIE was part of that relationship. It was also convenient to have TEL in place alongside TIE as TEL was able to provide the

interface between the tram and Lothian Buses Ltd (LB), and to manage the revenue implications for LB from the creation of the tram network, matters which primarily affected CEC rather than the Scottish Government. One of the TS directors, Bill Reeve, was on the TPB and therefore part of the tram governance arrangements. That changed when the status of the project changed.

94. I met the Chief Executive of CEC on a formal basis only a few times after the governance arrangements for the project changed. The understanding that Tom Aitchison and I had was that we would leave the interface between TS and CEC in respect of the tram project to be managed primarily at working level, but that if any problems arose that could not be resolved they would then be escalated to Chief Executive level. During the time that I was at TS no issues were escalated to that level, so as far as I was aware the new arrangements were working effectively. Papers I have been shown by the Inquiry suggest that there may have been a degree of friction, and in particular that TIE seemed to feel that TS was being unduly intrusive. I was not aware of that as an issue at the time. From mid-2007 TS was dealing with CEC as the principal party responsible for the tram project and I had no indication of any difficulty in that relationship or in the working-level contacts with TIE. If there was an issue about the degree to which TS could properly require information of TIE and CEC, I was not made aware of that as a problem at the time, either by my own staff or by Mr Aitchison.
95. TS had no direct role in requiring or promoting the changes in the responsibilities of these bodies. The changes that took place in 2007 were as a result of the change of the Scottish administration and the change in the status of the project following the parliamentary resolution of 27 June that year. While the detailed implementation of these changes took some time to formalise, the broad intention was clear from the outset. The balance of responsibilities had altered so the basis of the relationship needed to be altered to reflect that.

96. I have mentioned that the TPB was in place before TS was established. While I have no knowledge of how it came to be set up, this was not an area in which Ministers would usually intervene. There were joint steering groups or boards for projects such as the Waverley Station upgrade and other projects where we were directly involved with a third party in delivering them. A joint oversight arrangement was a common way of working within Scottish Government when a project involved a partner elsewhere in the public sector. I have mentioned that there was a steering group for the Aberdeen Western Peripheral Route which was made up of TS and representatives from Aberdeen City Council and Aberdeenshire Council. There was a similar arrangement for the M74 extension where TS was in more of a supporting role.
97. The decision that an arm's-length company, TIE, should deliver the tram project was made before my time at TS. I have no direct knowledge of why that model was chosen, or by whom. The perceived advantages of having an arm's-length company undertake the tram project might have included having an organisation that was more commercially focused, with the ability to make quick decisions and with more flexibility within its pay structure in order to attract the calibre of staff that it would need. It was not, however, necessary for a project of that size to be delivered by an arm's-length company such as TIE. There were many examples of substantial projects being delivered in England by local authorities, but fewer examples in Scotland after local government reorganisation in 1996.
98. From my experience during my time at TS, TIE met the expectations of TS as an organisation with the capabilities to deliver the tram project. People with whom I had worked in the past and whose professional skills I respected were working for TIE. TIE had the right level of expertise and effective management, so I had no reason to doubt the competence of TIE. My immediate knowledge of TIE was fairly limited in the sense that I was not engaged at working level with the organisation, and I only visited their office once or twice. However, I knew both the first and second Chief Executives of TIE from previous professional contacts - Michael Howell in his earlier post as

Commercial Director of Railtrack and Willie Gallagher when he had been on the board of the Strategic Rail Authority - so I was well aware of the senior experience at the top of the organisation. I did not receive any negative feedback from TS colleagues who worked more closely with TIE. Where there were delays or difficulties, they seemed to be more down to TIE's suppliers than to TIE itself. I have already mentioned that the design contracts were running late and TIE was as frustrated about that as TS was. To my knowledge, TS did not recommend the employment of an established firm of professional project managers to run the project. It was not something I would myself have recommended, since TIE was already in existence for that purpose. TIE grew with the tram project because it was involved in taking the project through Parliament, and that in itself was a good learning curve for any organisation in terms of challenges and the need to prove itself. TIE being a new company was not an issue in my view.

99. I am aware that there were difficulties with the SAK project. TIE was involved in this project before TS was established, presumably because it provided a convenient resource for other projects and because it had recruited the appropriate expertise. The Auditor General's report of June 2008 (**CEC01318113**) raised some issues about the SAK Railway project, and the Transport Minister, Stewart Stevenson MSP, had also identified that there were problems. I was already aware from the monitoring being carried out by TS that there were deficiencies in the way the SAK project was operating, including supply chain weaknesses and issues of cost control. The contractors did not have the right resources at the right time and this came down to project management. Consequently there was a concern, not specifically about the TIE input, but about the overall effectiveness of the governance arrangements for SAK. I recall that I had discussions with Bill Reeve about the situation and whether the correct alignments of interest had been achieved. My concern was that the SAK project was going over budget and its governance arrangements did not seem at that point to provide TS with the level of leverage that was needed to address this and other underlying issues.

100. The Audit Scotland Report of June 2008, *Review of Major Capital Projects in Scotland* (**CEC01318113**), explained in case study 2 on page 24 that Clackmannanshire Council had appointed TIE to a management role in the SAK project. The project was being led by Clackmannanshire Council, the smallest local authority in Scotland. Even a relatively small project such as SAK could have imposed significant demands on the management resources that were directly available to Clackmannanshire. We reached the view within TS once we saw that there were difficulties with the project that it would be better to seek to reconstruct the oversight arrangements and to involve our staff more directly in the project and in the management of its grant support, rather than relying on TIE for these purposes. As the Audit Scotland report noted on page 24, TS took a direct role in the governance of the project in June 2007, and took over day-to-day project management in August that year.
101. I have already explained that TS was not involved in the establishment of the governance arrangements for the tram project, and that these were already in place when TS was set up and inherited the Transport Group's role in that structure. I refer to the Auditor General's report dated June 2007 (**CEC00785541**). At page 17, there is a governance diagram showing that TS was represented on the TPB. The TPB was chaired by TEL and involved TS's Director of Rail Delivery, Bill Reeve; the Executive Chair of TIE; CEC's Director of City Development; and the Chair and Chief Executive of TEL. Relevant organisations were therefore all represented in the top-level oversight of the tram project. Before the Scottish Parliament elections in May 2007, TS's expectations were that governance would continue on a similar basis, and that its involvement in the project would include direct participation in the TPB for as long as the tram project was under construction. However, we also expected that once the tram project was up and running that role would cease, since the operational undertaking would have become a TEL responsibility.
102. After the Scottish Parliament elections and the change of government in May 2007, the tram project became CEC's responsibility, to be taken forward at CEC's risk, for the reasons that I have described. At that stage it was



therefore appropriate for the TS representative (Bill Reeve) to step down from the TPB. The most important reason for TS no longer to remain on the TPB was that if TS had continued to influence TPB decisions then the accountability for those decisions would be blurred. Once the tram became entirely CEC's project, TPB decisions were being made wholly on behalf of CEC. If TS had had a director on the TPB and there had been a disagreement about the way forward and TS's representative had influenced a particular outcome, then CEC could rightly have argued to Scottish Ministers that they should also share the risk arising from such decisions.

103. I have been referred again to the Audit Scotland June 2007 Report **(CEC00785541)**. I agree in most respects with the statements made at page 9 under the heading 'Transport Scotland'. However, although there was a monthly slot in the meeting calendar for the MIDMB, it did not meet every month – it would only meet when required. At every main board meeting a report was provided which charted the financial progress of each budget area. We also considered on the same monthly basis our risk register which tracked the risk profile of TS's activities, including the capital investment projects. Normally we would only discuss projects by exception, if a project was going off budget or if additional risks were emerging. If we did not discuss a project that meant there was no fresh information to discuss.
104. I had sole responsibility as the agency accountable officer for TS and, in theory, I could make all necessary decisions relating to the activities of the organisation, subject to the wishes of Ministers and the limits of my own delegation and financial authority. However, I felt, and it was also agreed by Scottish Ministers, that it was appropriate for the Chief Executives of agencies such as TS to be supported and advised by a Board. This arrangement was set out in the framework document, which had been agreed with the Transport Minister during the establishment of TS. While I was Chief Executive, TS had a board of five functional directors and two non-executive directors, so there was a total board of eight including myself. Our Director of Rail Delivery was Bill Reeve and we had a Trunk Roads: Infrastructure and Professional Services Director, who oversaw the development and procurement of our

roads projects but also provided some corporate professional services. There was a Trunk Roads: Network Management Director, a Finance and Corporate Services Director, and a Strategy and Investment Director. They were the professional heads of departments within TS. In addition to that, TS had two experienced non-Executive Directors on the Board. That structure changed slightly after I left TS but it was the basic corporate structure I operated while I was Chief Executive. I chaired the TS Board which all executive and non-executive directors attended. Other senior officials would attend as necessary to discuss particular projects or issues.

105. Along with other major projects, the tram project was considered, as necessary, at the TS Board. It was not discussed at every meeting for the reasons I have already explained, but every Board meeting would have had oversight papers which would let the Directors see the progress of the tram project, both financially and in terms of any milestones that needed to be met. If an investment decision was to be taken, then that was generally done through the MIDMB, which allowed the necessary scope to consider the detail of a proposal. The TS Board oversaw corporate financial information and monitored that spending was in line with our budget. The Board also reviewed the risk register, and any risks in relation to the tram project that were not being contained or that it was otherwise felt necessary to draw to the Board's attention were discussed. Specific issues in relation to the tram were discussed as required by the TS Board and if any board paper was needed that would have been provided by Bill Reeve's Rail Delivery Directorate, because that was where the line management responsibility for the tram project lay. Normally Bill Reeve would present information or lead the discussion about the tram project at the TS Board, but Damian Sharp would also attend when appropriate. Depending on the nature of the information, if there was a risk to be managed or other action required, then that would be an action for the relevant director, Bill Reeve, to report back upon, usually within a monthly cycle but sometimes longer as required. In addition to the TS Board's role, the Audit Committee was an independent committee, chaired by one of the non-executive Directors and composed of the other non-executive Director and a third outside member. The risk register was one of the matters

that the Audit Committee kept under review. I and the Director of Finance and Corporate Services attended the Audit Committee meetings and reported as required on anything of concern to the Audit Committee. I cannot recall any particular issues coming up in relation to the tram project at the Audit Committee.

106. I have already explained that the purpose of the MIDMB was to assist me in my role as Accountable Officer and Investment Decision Maker for TS in reaching investment decisions. Its primary role was to provide the opportunity to consider the detail of an investment case outside the business of the main TS Board, where it might have been difficult to provide the necessary time for an extensive discussion. Generally no more than two projects at a time would be considered at an MIDMB, so that we could allow the time that was needed for full discussion of each investment decision. All the full-time TS Directors were invited to attend the MIDMB. They might not attend if the agenda items were not relevant to their function or had limited corporate impacts. Non-executive directors did not routinely attend but they had a standing invitation to attend any meeting that they wished. It was of course more difficult for non-executive Directors to make themselves available to attend additional meetings in the cycle, but all MIDMB papers would be shared with non-executive directors if requested. The Director of Strategy and Investment, Frances Duffy, would chair the MIDMB even if I was in attendance because I felt it was important that roles should be kept distinct. The purpose of the MIDMB was to advise me in my decision-making responsibilities, and if I was chairing a meeting then I might have unduly influenced the advice I was to receive. Therefore as a matter of practice I would only chair the MIDMB if Frances Duffy could not be present.
107. My role if I was present at a MIDMB meeting was to make my own contribution alongside that of all other participants to what was being discussed. It was part of the collegiate process to challenge and discuss any major project in order to add value and make sure there was proper scrutiny from every angle. If I was not present then I would see the report of the outcome and discuss with the chair any issues arising. I would usually see all

the papers for the MIDMB. As Chief Executive of an organisation such as TS I had to be available to Ministers at short notice whenever required, so it was important that a MIDMB meeting could take place in my absence.

108. Before my own involvement and TS's establishment, Scottish Ministers had decided that any significant expenditure on the tram project had to be approved by them. Therefore the role of MIDMB in relation to the tram project was to make recommendations on project expenditure to Scottish Ministers, rather than to approve the expenditure itself. I have explained why the tram project was not considered at every MIDMB meeting: it was only discussed there when a significant financial decision in relation to the tram project was necessary. In most instances when the tram project was discussed at the MIDMB Damian Sharp prepared and presented the required information, but I would expect Bill Reeve to be there in support of him. Arising from its consideration, the MIDMB would decide what course of action to recommend. An action in relation to the tram project would normally be a recommendation to the Transport Minister, supported by the necessary advice. Ultimately it was for me as accountable officer to take responsibility for each recommendation.
109. The project owner for the tram project was TIE. My understanding of the arrangement that I inherited, which was set up before my time at TS by the then Head of the Transport Group, was that for externally "owned" projects there would be a Senior Responsible Officer within TS in addition to the external project owner. This was a complex arrangement, which was essentially a hybrid form of project ownership. An example of this was the works on Waverley Station, where the project owner was the Scottish Director of Network Rail, who had no direct accountability to the Scottish Government. TS therefore had a parallel official who was effectively a shadow project owner and was the interface between an outside promoter and the Scottish Government's financial processes. This was done to accommodate the reality that public transport schemes were mostly being delivered by organisations outside the mainstream civil service structures, and provided a means of ensuring conformity with the requirements of the Scottish Government's Scottish Public Finance Manual. One important aspect of the Finance Manual

is that it is a live, on-line document which is frequently updated. I cannot therefore produce the relevant sections that applied during the period under discussion, but the current on-line version of the Scottish Public Finance Manual identifies the roles of project owner and SRO in a way which I believe reflects the arrangement we had in TS. As agency accountable officer for TS, I was held responsible for the expenditure and delivery of our project budget. In some instances, that expenditure was undertaken by an external body such as TIE, which was the project owner. For much of my time as accountable officer Damian Sharp was TS's designated Senior Responsible Officer for the tram project.

110. Apart from the TS Board and the MIDMB, there was a separate internal board led by Bill Reeve: the Rail Policy Board. This was another arrangement inherited by TS from the Transport Group, but which was adapted by Bill to reflect the corporate structures within TS by providing a single forum to discuss the management of the ScotRail franchise and all the major rail projects that were in his portfolio, together with rail policy and regulatory issues that were the responsibility of the Strategy & Investment Directorate and the handling of the rail budget within the Director of Finance & Corporate Services' overall responsibility for TS's finance. Part of that budgetary dimension was the development and maintenance of a comprehensive affordability model for all TS's rail responsibilities, including the projects. This was an extremely important "live" tool for managing and forecasting a major element of TS's budget. At meetings of the Rail Policy Board, Bill Reeve would be supported by the Director of Strategy & Investment and by the Finance & Corporate Services Director, or their representatives. Any actions from the Rail Policy Board that required the approval of the main TS Board were reported by the relevant functional Director, generally Bill Reeve, but it was not the practice to refer the Rail Policy Board's minutes to the main Board for noting or approval.
111. My own role in relation to the tram project was derived from my overall management responsibilities for TS, including that of agency accountable officer. In terms of the Scottish Public Finance Manual I could be neither the

project owner for the tram project nor the Senior Responsible Officer, since I was the person who ultimately determined the recommendation that would go to Ministers on any funding proposals that came from the project owner or the SRO. Bill Reeve reported to me on his entire rail portfolio and Damian Sharp, in his role as SRO for the tram project, would also report direct to me as necessary. My own accountability was then to the Transport Minister, although it was not unusual for Damian Sharp to prepare papers to the Minister and often to sign them after they had been seen and cleared by me.

112. It is my general recollection that during his time at TS Damian Sharp prepared most papers relating to the tram project that were required for formal consideration by the MIDMB. In many of those instances Damian Sharp, Bill Reeve and I would have a prior discussion about the contents of the report. Those discussions were conducted on an informal basis, but any actions arising out of them would be embodied either in correspondence or in the formal papers that were being prepared.
113. Bill Reeve's reporting line was to me. In common with other senior colleagues, he could, when appropriate, deal directly with the Transport Minister or other Ministers. Because of Damian Sharp's role as SRO he had direct access to me as necessary; in terms of management structure, however, Damian Sharp reported to Bill Reeve. In line with the budgetary procedures of the Scottish Government, Bill Reeve had to provide TS's Finance Director with a Certificate of Assurance at the end of each financial year for the management of the rail delivery budget, which included the tram project. As I have mentioned, Bill Reeve was on the TPB and the Edinburgh tram was one of several projects that he oversaw.
114. Damian Sharp was head of rail projects at TS. He had an overall responsibility under Bill Reeve for all the rail projects that I have listed earlier including Waverley Station, SAK and the Airdrie/Bathgate rail link. His deputy was Matthew Spence. For each project there was a project manager who reported through Damian Sharp to Bill Reeve.



115. John Ramsay was the project manager for the tram project, and he was the single point of contact with TIE at a working level. My general recollection is that John Ramsay had access to professional and administrative support from within Bill Reeve's team, but in organisational terms it was John Ramsay's responsibility to manage the tram project at his level.

### **Withdrawal of TS from the Project Governance Arrangements**

116. Before the Scottish parliamentary election in May 2007 there was a wide awareness that the SNP's manifesto indicated that they did not wish the Edinburgh tram project to proceed. I recall that one of the Cabinet Secretaries in the new administration, Kenny McCaskill MSP, represented an Edinburgh constituency and was quite strongly opposed to the tram project. I am not in a position to comment on how it became a manifesto commitment of the SNP to oppose the tram project. However, the new Government did not immediately withdraw support from the project. When the matter was raised in the Scottish Parliament on 31 May 2007 the First Minister gave assurances that he would bring a proper financial assessment to the Parliament. (*Official report, 31 May 2007, column 314.*)
117. I note that the Audit Scotland Report dated June 2007 (**CEC00785541**) states at page 4: *"On 4 June 2007, the Cabinet Secretary for Finance and Sustainable Growth asked the Auditor General for Scotland to carry out a high-level review of the arrangements in place for estimating the costs and managing the Edinburgh trams and Edinburgh Airport Rail Link (EARL) project"*. When transport was debated again in the Scottish Parliament on 27 June 2007 that Audit Scotland report had been produced, and an opposition motion was carried which demonstrated MSPs' support for retaining the tram project within the portfolio.
118. SNP Ministers had their own priorities and their own political commitments arising from their manifesto. As an executive agency within the Scottish Government, TS was accountable to the Scottish Ministers and was required

to deliver their objectives. We were working within the context of a budget that had been set by the previous administration and also of the cyclical review of the future Scottish budget. Many financial priorities were under discussion. As always in Government there were competing demands, and as officials we were being asked to see how the budget could be re-scoped to put some projects higher up the priority list. That of course required that some projects would have to go down in priority. During the first few months of the new administration that process involved me in a considerable amount of discussion with the Cabinet Secretary, John Swinney MSP, and the Transport Minister, Stewart Stevenson MSP. I was also heavily engaged with the Corporate Finance Department of the Scottish Government and with colleagues from the Transport Group who had responsibility for some of the portfolio spending commitments. TS also had a major technical issue to deal with in relation to the proposed new Forth crossing, because the incoming administration had indicated that they preferred a tunnel to a bridge. We had to review all the technical work that had already taken place, re-evaluate the options and eventually explain to Scottish Ministers why we still considered that a bridge was a better technical solution than a tunnel.

119. The nature of my duties meant that I continued to have frequent contact with the Cabinet Secretary, John Swinney MSP, after it had been decided to retain the tram project. It was of course not my role to question political positions, either the political view of the incoming administration on the Edinburgh tram project as expressed in their manifesto or the political decision taken by Parliament in favour of continuing that project. Those two conflicting objectives were resolved in the wording of the parliamentary resolution on 27 June 2007 and by statements Ministers made in the aftermath of that parliamentary vote. Ministers had made it clear that if CEC wanted the project then it became CEC's project. All that the parliamentary resolution asked of Ministers was that the Scottish Executive funding that had been available previously for the tram project should continue to be available, noting explicitly that it was the responsibility of TIE and CEC to meet the balance of the funding costs. Mr Swinney's response to the Parliament's decision was to make it clear that this was indeed now CEC's project. As an official, my role

was therefore to implement the decision that funding for the Edinburgh tram scheme should continue but on the basis that responsibility for the project had changed. It was central to that change of responsibility for the project that future financial risk would now lie with CEC.

120. I have been shown an email chain dated 17 and 18 July 2007 in which I participated, together with Bill Reeve, Damian Sharp and others **(TRS00004547)**. In that email chain, we discussed some of these issues. In my response to Damian Sharp dated 18 July 2007, I stated: *"I am getting very strong signals from the Cabinet Secretary that TS should not be on the project board - he reiterated this at the Portfolio Meeting on Tuesday morning"*. I made that comment in reference to a meeting the previous day with the Cabinet Secretary, John Swinney MSP. That meeting must therefore have been on the morning of 17 July 2007. The portfolio meeting was a roundtable management meeting that John Swinney MSP held frequently with all the senior officials who were responsible for delivering his area of Cabinet responsibilities. I note that I used the word *"reiterated"* which clearly suggests that the Cabinet Secretary must previously have expressed the view that he did not want TS to continue on the TPB. That would be consistent with the timeline of the various papers that have been shown to me on this matter, in particular **(TRS00004523)** of 6 July 2007, which I discuss subsequently, noting that it was a response to an email from Mr Swinney's office dated 2 July 2007.
121. The decision to limit the Scottish Government's funding for the tram project to £500 million was in effect made by the Scottish Parliament, although no specific figure appeared in the parliamentary motion. However, the round number of £500 million was already in play when the matter was debated on 27 June, since it was quoted in the Audit Scotland Report dated 20 June 2007 **(CEC00785541)**. The TS paper mentioned above and discussed further below contained a technical discussion about how that commitment was derived in policy and in monetary terms **(TRS00004523)**. While the ballpark figure that was being quoted as the cap for the Government's expenditure was generally

understood to be £500 million, TS recognised that it was important that there should be a clear understanding of the basis for that figure.

122. I was aware that Scottish Ministers envisaged TS's role in the tram project changing to that of being a banker rather than a partner in the project. Other than the high-level indication from Mr Swinney that TS should withdraw from participation in the TPB, neither he nor Mr Stevenson sought to specify the details of how we should implement that change. That was my responsibility, and the change was effected through a straightforward grant arrangement with provisions for releasing future funding on a phased basis. TS could not remain a part of the governance arrangements and on the TPB because of the change in risk management responsibilities. I have been shown an email sent by Damian Sharp to myself dated 30 August 2006 (**TRS00011024**). The fifth paragraph of his email summed up the issues: *"Full participation would also expose us to later questions in the event of any challenge to the procurement process when City of Edinburgh Council or TIE is the procuring authority for EU law. It might also expose us to pressure from CEC if there were subsequent problems on the lines of 'it would all have been all right with contractor X but you made us choose contractor Y so you should share the cost of putting it right'"*. The parallel that I would draw would be with a Companies Act company board, where directors of a company are liable for the decisions of that board. If you influenced the decision of a board, even if not formally a member of it, you could be regarded as a shadow Director and therefore as still participating in the decision-making process. This requirement for clarity of future roles was my fundamental reason for agreeing with the Cabinet Secretary's view that TS should not be represented at the TPB, in any form, and I would have recommended that course of action even if Mr Swinney had not so clearly expressed his view.
123. I have been shown an email from John Ramsay to Matthew Spence dated 4 July 2007 (**TRS00004510**). Attached to that email was a paper which John Ramsay produced on TS's involvement in the tram project (**TRS00004511**). At section 4 of the paper (page 2), he listed three options for TS's ongoing involvement in the project. That paper did not come to me. It went through the

management chain to Matthew Spence and to Damian Sharp amongst others and it was the addressees who provided the advice that I sent to Scottish Ministers. I have been asked if the three options listed by John Ramsay were ever put to Ministers, and if not, why not. That question appears to relate only to the options for future engagement on page 2 of his paper. In terms of TS's own internal processes, the paper from John Ramsay would have been seen by Matthew Spence and discussed with the copy addressees. The proposals that were put to Scottish Ministers in respect of future engagement were those prepared by Matthew Spence after that discussion and set out in his note dated 25 July 2007 (**TRS0004581**). His proposals within paragraphs 8-11 on page 1 reflected one of the options defined by John Ramsay. I was not aware at the time of John Ramsay's views. He was one member of staff providing his input to an internal management process and it is in the nature of such processes that some views may be considered but not accepted. I would regard the fact that one member of staff's recommendations were not put to me as part of the normal sifting process within the Rail Projects management line that John Ramsay reported to. I am also referred to section 8(b) of John Ramsay's paper: "*We argue that the recent clearance on project governance etc by Audit Scotland is a clear reflection of the project oversight and management that Transport Scotland has maintained to date*", and to the similar comment by Bill Reeve in (**TRS00004547**) (his email of 18 July 2007). I agree with the first part of statement, that the Auditor General had concluded that the governance arrangements were effective; however, what John Ramsay's paper did not reflect was the fact that the status of the tram project had changed fundamentally with the Ministerial decision that the financial risk for the project should lie entirely with CEC. What this paper argued for was a status quo in governance when actually the status of the tram project itself had changed. I do not disagree that sound financial control and public probity should be the priority. Within the Scottish Public Finance Manual there were adequate controls and measures to protect the public financial interest through a purely grant aided mechanism, and that was what TS's involvement in the tram project evolved into. It was moving from being a project jointly funded by Scottish Executive and CEC with shared risk to a project where, as Ministers had made very clear, all the financial risk lay with CEC. John

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Ramsay's paper did not reflect the risk transfer that Scottish Ministers expressly required following the Parliamentary decision. Towards the end of paragraph 8(b) of the paper, I note that it is suggested that future participation in the TPB might be a decision that could be made within TS, and it is recommended that Ministers should be advised accordingly. Effectively, that amounted to saying that, regardless of what Scottish Ministers wished, TS should decide to remain on the TPB. Because of the direct engagement I had already had with the Cabinet Secretary on this question, I would not have recommended to Mr Swinney that TS should continue to have a presence on the TPB, partly because he had already made it clear that he did not want it, but equally because my own professional view was also that it would be imprudent for TS to continue to be on the TPB in the new circumstances.

124. I have been shown a memo dated 6 July 2007 which I sent to the Cabinet Secretary, John Swinney MSP, on 9 July 2007 (**TRS00004523**). That memo outlined the different funding options for the tram, but also dealt with matters relating to the EARL project and the proposed upgrade of the Edinburgh-Glasgow line. The appendices and annexes reflected the more detailed consideration that had taken place within TS, and there was complete alignment between what was put to Mr Swinney and what had been recommended to me in the papers that came from the Rail Projects management team. There is reference in the memo to an e-mail dated 2 July 2007 from the Cabinet Secretary's office, which I have not been shown. It is however apparent that the memo sent to the Cabinet Secretary on 6 July 2007 was in response to a request in that 2 July email, so we were evidently working to a tight timescale.
125. Returning to the paper that John Ramsay produced and emailed to Matthew Spence on 4 July 2007 (**TRS00004511**), as I have mentioned he referred in section 8(b) to Audit Scotland's clearance of the governance arrangements for the tram that were then in place. I have been referred again to an email chain dated 17 and 18 July 2007 (**TRS00004547**). I note that Bill Reeve similarly expressed concern in his email of 18 July 2007 that TS's withdrawal from the project's governance might undermine the arrangements that had been



cleared by Audit Scotland. I am asked whether Ministers were reminded of the Auditor General's view on this matter. Given that the Audit Scotland report dated June 2007 had been requested by the Cabinet Secretary, John Swinney MSP, and that it was available before the parliamentary debate on 27 June 2007 and referred to in that debate, I saw no need for me to remind the Transport Minister or the Cabinet Secretary of what was that report. There were differences of view within TS, and Bill Reeve had written to me in quite forceful terms in his email. However I took the view that while Bill was of course entitled to offer his advice to me, I did not consider that it was the correct way for me to advise the Minister. The third paragraph of Bill Reeve's memo refers to the "*nuclear option*", which was for me to seek direction from the Cabinet Secretary that TS should withdraw from the TPB. I would only have sought such a direction from a Minister if there were grounds for questioning fundamentally what the Minister had decided. I did not disagree with what the Cabinet Secretary was requesting.

126. I have been shown a letter sent by Willie Gallagher to me dated 3 July 2007 (**CEC01582956**). This was sent after the Parliamentary vote. He wrote (page 2): *"We have an opportunity to review the working arrangements between tie and Transport Scotland... We will of course also maintain the tight project governance through the Tram Project Board"*. I refer back to the email chain dated 17 and 18 July 2007, and specifically to Damian Sharp's email of 17 July 2007 (**TRS00004547**). This email provided feedback from the most recent TPB meeting. Damian indicated that Willie Gallagher did not appear to support the continuation of TS on the TPB (paragraph 6). As I read Willie's letter, it appears to me to be focused primarily on the opportunity to **review** the existing working arrangements (my emphasis). The remark about maintaining the tight project governance through the TPB seems to have been made as an aside, and does not offer any view about the TPB's future composition. This letter was written on 3 July 2007, shortly before the memo to Mr Swinney that I have already referred to. I cannot recall whether I had seen that letter before sending the requested advice to Mr Swinney, but Willie Gallagher's letter did not contain anything which would have led me to change the advice that went to Ministers at that time.

127. I have been referred back to the memo dated 6 July 2007 which I sent to the Cabinet Secretary, John Swinney MSP (**TRS00004523**). That memo stated at paragraph 11 that funding should be capped and that TS should scale back its direct involvement in the project. The Scottish Parliament had asked the Scottish Government to continue funding the tram project to the full extent envisaged by the previous administration. Therefore (**TRS00004523**) was seeking to provide advice to Mr Swinney as to how that funding decision should be defined and taken forward. As stated on page 7 there was some ambiguity about how the Scottish Ministers' existing £375 million funding commitment should be rebased to an outturn amount. We identified five options, noting that when the commitment was made the outturn contribution was then estimated at £450 to £500 million. But that was in 2003, and from our latest calculation that figure would equated to £492 million in 2011 (page 7). Of the five options TS offered, the first one was to keep the funding at £375 million and index it to an outturn, which would still be indefinite because it would be dependent on the actual indexation at the time the final contribution was made, but potentially would reach a final figure of £492 million. The second option was a variation on that, where £375 million was indexed but funding capped at £500 million. The third option was to recalculate on the revised baseline programme, because by that stage some slippage was anticipated and if the project programme was completed over a longer period the final figure would go to about £500 million. The fourth option was to recalculate the £375 million on the prevailing programme at Financial Close, and TS's view was that on that basis the final figure would be likely to exceed £500 million. The fifth option was to restate £375 million as an already out-turned fixed and capped sum of £490 or £500 million. We gave the Cabinet Secretary explanations of the advantages and disadvantages of each option and we concluded that option 3 would be the fairest, with a slight modification by capping funding at £500 million. The advice set out alternatives transparently and logically, and recommended an option. If Mr Swinney wished the settlement to be less generous then we provided a case for limiting the contribution to £492 million. The Cabinet Secretary chose to allow more headroom and the fixed £500 million option, the sum that TS had recommended, was what he agreed. That defined the Scottish Government's

total financial contribution to the tram project, and I am not aware of any suggestion in the documents I have seen that TIE or CEC were unhappy with either the quantum of the offer or the basis of it. CEC accepted that £500 million was the limit of Minister's future funding commitment.

128. As I have already explained, if a senior member of TS staff had been sitting on the TPB and had been party to a decision which subsequently led to a cost overrun, CEC could argue that because someone from TS was involved in the process then the Scottish Government should also share any financial risk arising from such decisions. That was why the recommendation was made at the end of Annex C of the memo that TS staff should withdraw from active governance of the project once grant conditions had been agreed with CEC.
129. I have been shown an email that Jerry Morrissey sent to TS staff on 9 July 2007 (**TRS00004522**), enclosing the final version of my memo to the Cabinet Secretary. In the email, he wrote: *"We need to define and discuss our level of involvement in trams. It may be slightly different to what we proposed"*. At that time TS had a high level understanding with the Cabinet Secretary that we would withdraw from active participation in the project. TS had then to define its future level of involvement in the tram project following the first piece of advice we had provided to Mr Swinney on 6 July 2007, which primarily related to the financial commitment of the project (**TRS00004523**). The second piece of advice, which was Matthew Spence's memo dated 25 July 2007 (**TRS00004581**), set out the detail of how we proposed to give effect to our changed involvement. In terms of substance, no new information was provided. As I have explained, I did not see John Ramsay's original proposals but they had been discussed within the Rail Projects management line before the eventual recommendations emerged. I cannot comment further on what other alternatives had been considered because I am not aware of who within Bill Reeve's division was recommending which particular course of action.
130. I have been shown an email exchange dated 11 July 2007, which includes an email from Shauna Cranney (**TRS00004536**). In her email, Shauna confirmed that the Cabinet Secretary, John Swinney MSP, had agreed that TS should

“scale back” involvement in the tram project. Jerry Morrissey forwarded this email, stating: *“We need to define and agree “scale back” for the tram project”*. At the point the broad framework for that scale back had already been defined and agreed with the Cabinet Secretary as TS’s withdrawal from the TPB, so it is not correct to state that no-one knew what it meant. It was simply a question of shaping a new working relationship with CEC and TIE, to be expressed through revised conditions of grant. That process was quickly taken forward, as is shown by Matthew Spence’s subsequent memo of 20 July 2007 (**TRS0000459**), discussed subsequently. I have already explained why I considered such scale back to be appropriate: it was a corollary of the changed responsibility for financial risk in the tram project.

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131. I have been shown an email chain dated 12 July 2007, which included an email sent by Julie Thompson, PA to Willie Gallagher at TIE, to various people at TS (**TRS00004540**). Attached to Julie’s email was a letter dated 12 July 2007 addressed to me from David Mackay (**TRS00004541**). In that letter, David sought confirmation of funding and governance issues, and suggested that TS should continue to attend TPB meetings. The email chain includes another email by Jerry Morrissey at TS, in which he suggested that a one page definition of ‘scale back’ should be produced. By that stage, the Cabinet Secretary’s view about TS’s continuing to attend TPB meetings was known. David Mackay was proposing alternative measures, but as is shown by the documents that were passing between the Cabinet Secretary’s office and mine that I have discussed above, the process to withdraw from the TPB was well in hand. As I have already explained, I saw no justification for seeking to reopen that question with Mr Swinney. If David Mackay felt that strongly about the matter, he would have been able put his concerns directly to the Cabinet Secretary.
132. The decision to withdraw TS from the governance arrangements was a political decision because ultimately any significant decision in Government is political. It was the outcome of not one but two political decisions: the political position of the incoming administration that they did not want the tram project and the political decision by the Scottish Parliament that it wished the project

to continue on defined terms. Both of those decisions affected the nature of the outcome. I was the agency accountable officer, accountable both to Parliament and to the Cabinet Secretary, John Swinney MSP. I saw no reason to disagree with the views that the Cabinet Secretary had expressed to me. The position that he had reached was one which conformed completely with the Scottish Parliament's resolution of 27 June 2007, protected the financial interests of the Scottish Government, and gave CEC the scope to deliver the tram project as it had asked. I would certainly have spoken to the Permanent Secretary at the time and sought his advice if I had been uncomfortable with that proposition or what was being asked of TS in delivering it. But I was not in that position.

133. I have been shown the papers prepared for the TPB Meeting on 9 August 2007 (**CEC01566662**). They include the minutes of the TPB meeting on 12 July 2007 at pages 5 - 9. My previous knowledge of what had been said at that meeting was based on Damian Sharp's note in his email dated 17 July 2007 which I have already considered (**TRS00004547**). I did not routinely see the minutes of the TPB: those went to Bill Reeve who was TS's representative on the TPB. I was aware in general terms from Damian Sharp's note from the meeting that James Stewart was among those who expressed a wish that Bill Reeve should continue on the TPB. I do not disagree with the first statement in paragraph 5.4 of the minutes, where it is stated: *"TS would remain responsible to assure prudent spending of taxpayers' money."* However, it then states: *"This should require continued attendance at the TPB, although less detailed scrutiny outwith the board"*. I find that quite a strange statement. That arrangement seems to me to be the wrong way round if careful spending of public money was to be ensured: I would consider detailed scrutiny to be more relevant than high-level oversight in achieving that objective. I note however from the minutes of the next TPB meeting on 9 August, included at pages 5 to 12 of the papers for the TPB meeting on 5 September 2007 (**CEC01561047**), that Mr Stewart seems to have modified his position: he is noted as having said that TS's withdrawal from the TPB was the same approach as that applied by Department for Transport (DfT) in England. PUK was a partnership between the public and private sectors, and although the

Treasury was the major public sector shareholder, the Scottish Government was also a shareholder in PUK. Again, if James Stewart felt strongly about the composition of the TPB then as PUK's Chief Executive he would have access to his Scottish shareholder in the person of the Cabinet Secretary for Finance and Sustainable Growth, John Swinney MSP.

134. I have been referred back to an email which I sent to Damian Sharp and Bill Reeve and copied to others, dated 18 July 2007 and which is part of a chain of emails that I have already considered (TRS00004547). The reference to scaling back appears only once in this chain as a progress item, so I am unclear of the basis for the further questions on this topic in relation to these particular items of correspondence. I have already explained that, as I saw it, Mr Swinney's views on TS's future involvement in the governance of the tram project were entirely consistent with the decision that the Parliament and he had reached: that responsibility for the project should lie with CEC. It is correct that Bill Reeve was expressing a view which differed from the Cabinet Secretary's about future governance arrangements, but that does not provide any evidence of a widespread divergence of views within TS. It was certainly not my style of management to impose decisions without considering other views, but if I felt the logic pointed in a particular direction I would make that clear. I am sure that Bill Reeve was well aware of my views just as I was aware of his. However, what Bill had failed to articulate in his email response was the substance of his grounds for considering that the course of action proposed was not in accordance with the Scottish Public Finance Manual. Others besides Bill Reeve would have pointed out very quickly if I had been proposing any course of action that was outwith the provisions of the Scottish Public Finance Manual.
135. There was nothing inconsistent in the advice that TS gave to the Cabinet Secretary, John Swinney MSP and Minister for Transport, Stewart Stevenson MSP, about the future of the tram project. Colleagues within Bill Reeve's directorate developed the grant conditions which were to be the basis of the future working relationship with TIE. I believe TS staff accepted that the world had moved on and TS should adjust to having a pure grant funding



relationship. Then, entirely professionally, the staff set about the means of giving effect to that. Some members of staff within TS may have been individually concerned about withdrawal from the previous governance arrangements, but apart from a few documents I have been shown no systematic evidence of such concerns. The Scottish Ministers had expressed their intention to change the basis on which the tram project would be carried forward, and I was not aware of anyone within TS complaining about the new arrangements once the situation was understood. None of TS's other Directors expressed any concern about the changes as they emerged. In particular I considered that both the Director of Finance and Corporate Services, Guy Houston, and the Director of Strategy and Investment, Frances Duffy, each of whom had a stake in what was happening, would have expressed very strong concerns if they felt that what TS was doing was not appropriate.

136. TS was very busy as an organisation over the whole summer of 2007 after the change of administration. This was not just because of the political change, but also because we were running into the new spending review. TS was also taking forward an entirely unexpected major project, the second Forth road crossing at Queensferry, for which we were not then fully resourced. Potentially there might have been advantage in being able to withdraw some TS staff from one project to help with other projects, but that certainly did not influence any parts of our recommendation to Scottish Ministers as to the form of TS's withdrawal from the tram project, nor did it materialise to any significant extent.
137. The Scottish Public Finance Manual is a live document, so what is online at present was not the document as it stood in 2007. It would require archival research to find out what the exact provisions were at that time, and I certainly can no longer recall the detail. In general terms, specific processes applied to ongoing projects which were "owned" within the Scottish Government to ensure that they were being properly managed and that funding was being correctly applied. However, other provisions dealt expressly with grant-aided projects, and in my view at the time was that those provided the necessary

assurance for the Scottish Government's changed financial interests in the project.

138. I have been shown an email that Matthew Spence sent to me on 20 July 2007 (**TRS00004558**). Attached was a memo on the role of TS (**TRS00004559**). The purpose of the memo was to define the scaled back role of TS. I have been asked why the position reached in Parliament required the existing arrangements to be modified. I have already referred to the revised allocation of financial risk as defined in the parliamentary resolution of 27 June 2007 and as accepted by the Cabinet Secretary, John Swinney MSP. As detailed in paragraph 6 of the memo, the existing arrangements contained detailed project management requirements which it would no longer be appropriate for TS to apply once CEC accepted complete responsibility for the management of the project. A simple statement that no more money would be available from the Scottish Government would have left these otiose conditions in place. I have been asked why the key points stated in paragraph 8 of the note were being used as "reasons" for the revised role, since they were existing circumstances. The new circumstance was stated in the first indent: the explicit capping of Scottish Government funding at £500 million. I do not consider that they were being advanced as "reasons"; they were simply stating the underlying conditions of grant moving forward. I am asked whether these new arrangements were requested by Parliament. They were not requested, but they were necessary in order to implement the Scottish Parliament's explicit wishes that existing committed Government funding should be continued but that responsibility for the project would transfer wholly to CEC.

139. I have been shown an email dated 26 July 2007 which was sent on my behalf to the Cabinet Secretary, John Swinney MSP (**TRS00004580**). Attached was a memo prepared by Matthew Spence dated 25 July 2007 and cleared by me (**TRS00004581**). The memo informed the Cabinet Secretary of the proposed redefined role of TS. I have been shown an email sent to my office dated 30 July 2007 sent on the Cabinet Secretary's behalf (**TRS00004595**). This email confirmed that the Cabinet Secretary was content with the proposed redefined

role. As far as I was aware, I was the only one who had direct meetings with Mr Swinney about TS's redefined role in the project, but others within TS were contributing to the formulation of advice to the Cabinet Secretary and some of that written advice and information went direct from senior TS officials to the Cabinet Secretary. As I have explained, I was fully aware of the Cabinet Secretary's clear view that TS should withdraw from active engagement in the management of the tram project.

140. I have been referred to the papers for the TPB meeting on 5 September 2007 (**CEC01561047**). Included at pages 5 to 12 were the minutes from the TPB meeting on 9 August 2007. I note that at paragraph 3.9.2 of the minutes (page 8), it is recorded that the Board considered whether the decision to withdraw from the TPB was politically motivated. As I have explained, the decision to withdraw TS from the TPB was the outcome of political decisions by the Scottish Government and the Scottish Parliament. Equally the decision of CEC to continue with the project was a political decision.
141. I have been shown an email sent to me and Bill Reeve by Damian Sharp dated 23 August 2007 (**TRS00004742**). Attached (amongst other documents) was a document he had prepared entitled 'Tram Issues' (**TRS00004745**). The purpose of this document was summarised at paragraph 18 of the email (page 3). The document stated that the role instructed by Scottish Ministers meant that TS should no longer act on some of the information provided by TIE or CEC (paragraph 9 on page 2). I agreed with Damian's very clear distinction between financial information, and management information. TS needed to have the former, it needed to be aware of cash flow and to ensure that funds were disbursed properly. However, under the new arrangements it would no longer be appropriate for TS to act on management information by intervening actively in the operational delivery of the project. That was now the responsibility of CEC. I am asked if I agree that Damian's note shows that Ministers instructed TS's withdrawal from the governance arrangements and its new role. I see nothing in his note to indicate that, other than his reference in paragraph 2 to the Minister's point on CEC's ownership of the project – a matter which had effectively been determined by the Parliament rather than

Ministers. TS was accountable to the Scottish Ministers and we applied the Scottish Government's policies. Ministers were not following every interaction TS had with TIE or CEC. Ministers had set the broad principles and TS was implementing those broad principles.

142. I have been referred to a briefing note headed 'TIE - Governance Arrangements, Briefing Paper for the Chief Executive' dated 20 July 2007 and prepared by Jim Inch, CEC's Director of Corporate Services (**CEC01566497**). I note that at paragraph 3.1 it stated that the then current governance arrangements were "*complex*", at paragraph 4.1 (page 8) that it was "*vital that more rigorous financial and governance controls are put in place by the Council*", and at paragraph 4.2 (page 8) that "*TS have previously urged the Council to implement a more robust monitoring of TIE's activities in delivering the project*". I have been asked when, how, and by whom TS had urged that more robust monitoring. That imperative was clearly expressed in TS's comments on the DFBC prepared by Damian Sharp and dated 30 March 2007, and already discussed (**TRS0004145**). It was also evident from the conditions of grant that were applied in March 2007 with Ministers' agreement. I have previously discussed the background to these concerns, and the effectiveness of CEC's response would have been monitored under the previous governance arrangements until the status of the project changed in the summer of 2007. I do not recall being advised of any further issues in relation to monitoring during that time. This report suggests to me that CEC took its governance responsibilities for the tram project very seriously.

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## Procurement and Contracts

143. I have been referred to an email sent by Damian Sharp to me dated 30 August 2006 (**TRS00011024**). In that email, he set out the proposed TS role in the procurement of contracts for the tram project. The view that Damian Sharp expressed was that TIE had adequate professional and technical resources to undertake this process, and he was questioning whether our direct involvement would add value. He went on to say that if TS participated fully in

decision-making on the award of contract then TS was a party to that contract, and beyond the obvious issue about protecting Ministers' financial interests, there was also the issue of where TS would have stood in terms of EU procurement law if TS was construed as the contracting party. His recommendation was that TS should restrict its role to defining criteria for the evaluation of tenders, agreeing the evaluation process, and checking for compliance with that process. I agreed with that view, and my understanding was that TS's engagement with the procurement process was on that basis until the summer of 2007, when the status of the project changed

144. I am referred to the TIE response dated 8 February 2007 (**ADS00017**) to TS queries which noted that both Infraco bidders were protecting their risk position pending receipt of more detailed design information and completion of due diligence. I was not aware of that document at the time, nor was I involved in any consideration of the issues raised within it. It is not therefore within my direct knowledge. Likewise, I have no previous recollection of the Design Due Diligence report produced by BSC in February 2008 (**DLA00006338**) which was shown to me, and I cannot comment from direct knowledge of TS's awareness of it at the time, or how, if at all, it was handled within TS. I note however that it is dated after the change in status of the project in 2007 and CEC's assumption of full financial risk.
145. I have been asked about the letting of the MUDFA contract early in 2007. The framing of this question appears to be based upon a misapprehension. The MUDFA contract was a TIE contract, and it is my understanding that it had been let in October 2006. Its letting was not therefore an issue. The question appears to relate more to TS's recommendation to Ministers that funding for draw-down against that contract should be released early in 2007. We were aware that this was a sensitive issue because of the forthcoming Scottish Parliament elections and the SNP's known lack of support for the tram project. However, as I have already explained, the urgency of the release of funds for MUDFA works was not created by the forthcoming election; it was necessary to maintain the delivery programme for the tram project, which had received the approval of the Scottish Parliament and the then coalition administration. I

have also explained that the Scottish Ministers had instructed that any decision to authorise further expenditure on the project should be made by them. The necessary advice was provided well in advance of the “purdah” limitations on potentially-sensitive Ministerial announcements during pre-election periods.

146. TS was aware of problems with delays to the design programme in April 2007, but I am unclear about the connection that appears to be being drawn with the release of funding for the final phases of the project under the new arrangements that took effect later that year. The grant release that was authorised in March 2007 was to provide funding for the MUDFA contract and the evaluation of bids, and included conditions designed to strengthen project management to address issues such as design delays. It was also made clear that a further Gateway review and the preparation of the FBC were necessary preconditions before the release of further funding. These were all measures that were being taken specifically to address remaining issues with the project, of which TS was aware and Ministers had been advised. I do not understand the question that has been put to me about “handing over the money”. As I have repeatedly explained, Scottish Government funding was only released, whether before or after the change in the status of the project, against evidence that expenditure was being properly incurred.

147. I have previously explained that I retired from the Civil Service on 17 February 2009, when I left TS after an agreed overlap period of about a week with my successor as Chief Executive, David Middleton. From the day he took up his appointment I ceased to be the agency accountable officer. I was not aware at that time that TIE was in dispute with its contractors nor of any factors which led to that dispute. I therefore cannot comment on the dispute and its budgetary or other implications, nor on the options that might have been available to TS or Ministers after the dispute had emerged.

## Grant Funding

148. I have been referred to a number of emails between TIE and CEC dated 8 October 2007 and which form part of a longer chain of emails (**CEC01565313**). The emails of 8 October related to the fact that a grant letter had not been issued. I cannot comment from memory on the details, but the change in the status of the project required negotiation and agreement with CEC, and the drafting of revised terms and conditions of grant. It is evident from the emails that significant amendments had been proposed by CEC. These required consideration by the Scottish Government's lawyers, and it is noted in the email of 8 October 2007 from Lorna Davis (TS) that TS was still in the process of consulting its legal advisers. I recall that this was part of a wider problem at that time of obtaining timely legal advice, and around the same time we were experiencing similar delays on one of the major roads contracts which required detailed contractual drafting.

## TS Involvement and Progress Reporting

149. I have been shown an email sent by Dave Anderson at CEC to John Ramsay and copied to me, dated 2 May 2008 (**CEC01222014**). In that email Dave Anderson referred to the Cabinet Secretary's, John Swinney MSP's, concerns about financial close. I was not personally aware of any concerns the Cabinet Secretary had about Financial Close and I have no recollection of any advice being sent to Ministers on this matter.
150. I have been referred to an email from Stewart McGarrity to Graeme Bissett dated 24 May 2008, which is at pages 1 - 3 of a longer email chain (**CEC01342332**). Stewart stated that Scottish Ministers had asked TS to be *"more involved/informed re what's going on in the Tram project"*. This was an internal CEC document and I was not aware of any request from Ministers for TS to become more involved in the tram project. After TS withdrew from direct participation in the governance arrangements, we maintained the monthly reporting and quarterly reconciliation of expenditure on the tram project. TS



submitted regular financial statements to Ministers about the progress of all the capital schemes. The Scottish Government's grant support for the tram was part of a budget portfolio for which the Cabinet Secretary, John Swinney MSP, and the Transport Minister, Stewart Stevenson MSP, were responsible and accountable. It was therefore necessary and appropriate for them to be assured that spending was proceeding to budget and that funds were being properly applied, and for TS to carry out the financial monitoring that was needed to provide that assurance.

151. My attention has been drawn to **(CEC01786920)** as an example of a monthly progress report. However, that report is dated 2006, before the governance arrangements for the tram project changed in 2007. A report in that level of detail was entirely appropriate when Scottish Ministers shared risk on the project. A report to TS in that depth and coverage would not have been necessary after responsibilities were altered in 2007.
152. I have been referred to the notes of a meeting on 2 August 2007 between TIE and TS, which are at pages 18 to 23 of a larger document file **(TRS00026730)**. I note however that this meeting note was to be the subject of intra-organisational agreement (page 21, paragraph 29) and that the arrangements were to be formalised in a subsequent letter from the Chief Executive of CEC to myself (page 18, paragraph 1). It is unclear, therefore, whether this meeting note reflects the detail of the arrangements that were eventually adopted, and I have not been shown the subsequent letter that is mentioned.
153. I refer in particular to the reporting format described in section 3 of that note in **(TRS00026730)**. I have been asked whether that format was followed, and whether senior TS staff such as Bill Reeve participated in the proposed monthly meetings, which were to be with CEC rather than TIE. I do not recall seeing, and would not have expected to see, the monthly reports and the documentation relating to the monthly meetings that were proposed, so I cannot comment on whether that format of reporting was adhered to in those respects or who from TS attended such meetings. I would have expected

John Ramsay, as the relevant TS project manager, to have handled routine monthly contacts, reporting anything that required action by TS through Bill Reeve's team. So far as the proposal that there should be a quarterly meeting at Chief Executive level between TS and CEC is concerned, I do not recall that Tom Aitchison proposed such an arrangement to me. We met with each other or spoke by telephone as necessary rather than on a specific cycle, and the understanding we had was that our respective teams would handle any issues relating to the tram project between themselves, only escalating to Chief Executive level matters which could not otherwise be resolved. No matters were raised by Tom with me on that basis while I was at TS, and I did not find it necessary refer any issues to him. My routine awareness of tram project progress was provided through Board monitoring papers; any specific issues would have been raised with me by exception by Bill Reeve, but after this passage of time I cannot recall any particular instances. Colleagues across TS had access to TS Board minutes and papers, so anything that came up at the Board relating to the tram project would have been available to other colleagues. As previously described, other directorates were represented on Bill Reeve's management meetings for the rail portfolio, so that provided a mechanism for the sharing of more fine-grained information within TS. I have already explained that the MIDMB did not have a monitoring role in relation to the tram or other projects.

154. After the governance of the tram project changed in 2007, the Scottish Ministers were kept advised of the progress of that project through normal portfolio reporting processes and specific briefings when required for parliamentary purposes or external engagements. So long as conditions of grant were being met, TS had no locus to require detailed information on the management of the project: that was a matter for CEC. My own role in relation to the tram project remained that of Chief Executive of TS and the accompanying responsibility of accountable officer for the Scottish Government's financial contribution to the scheme. I do not recall any requests from Scottish Ministers to me for more specific information about the tram project than was being provided through existing reporting and liaison channels.

## Reviews and Reports

155. It has been put to me that a number of 'Panel Reviews of Major Projects' in relation to the Edinburgh tram project took place in 2005 and 2006 and were attended by representatives from TIE and TS. Any meetings before 2006 could not have been attended by TS representatives, because the organisation only commenced operations on 1 January 2006. I have been referred specifically to the minutes of the Panel Review of Major Projects: Edinburgh Tram meeting dated 24 November 2006 (**CEC01642265**). This did take place after I was in post and TS had been established. As I have previously explained, this was an inherited management arrangement which had been established when these projects formed part of a portfolio that was the responsibility of the Scottish Executive's Transport Group. It was adopted by Bill Reeve as part of the departmental management of his rail project portfolio, and chaired entirely properly by Bill Reeve. It was not my role to attend such departmental meetings, where Bill was, in effect, managing his clients. Necessary actions were noted at the meeting and I expected Bill Reeve to deal with them as part of the normal progress of his meeting cycles, reporting matters to Chief Executive or Board level only when necessary.
156. I have been asked about an Audit Scotland review into the Tram project carried out in February 2007. I am not aware of any such review. I have previously referred to the report by the Auditor General which was issued in June 2007 (**CEC00785541**). Paragraph 1 of the report states: *"On 4 June 2007, the Cabinet Secretary for Finance and Sustainable Growth asked the Auditor General for Scotland to carry out a high-level review of the arrangements in place for estimating the costs and managing the Edinburgh trams and Edinburgh Airport Rail Link (EARL) projects. The Auditor General had already made a commitment that Audit Scotland would undertake a review of major capital projects in Scotland in its current work programme. On this basis, the Auditor General agreed to bring forward a more focused review of Edinburgh trams and EARL as part of the planned work"*. It is possible that the question I have been asked refers to the existing commitment to review

major capital projects that is mentioned in the second sentence of that quotation. But it would be for Audit Scotland to comment on that. The 2007 Audit Scotland report provided input to Scottish Government decision making on the EARL project, and was available before the Scottish Parliament resolution of 27 June 2007 which effectively determined the future of the tram project. I am not aware whether CEC used this report or gave weight to it in their decision-making. Equally, I am not in a position to comment on how the Scottish Ministers viewed this report, nor on what they saw as its purposes and on how much weight they attached to it.

157. I have been shown a document entitled 'Audit Scotland Review' which was circulated to TIE staff in June 2007 (**CEC01677283**). It told them how to prepare for the Audit Scotland review, and stated that all documents released to Audit Scotland would be approved by Stewart McGarrity or Graeme Bissett before being released (page 1). Internal policy within TIE would of course have been a matter for its Board, but this memorandum appears to me to have been primarily focused on ensuring consistency and effective document control during a necessarily tight period of information gathering by Audit Scotland. There is nothing in that document that appears to me to suggest any restrictive intent on the part of TIE, and it acknowledges the scope for Audit Scotland to speak to other parties.
158. I have been referred back to paragraph 30 on page 10 of the Audit Scotland June 2007 report (**CEC00785541**). It recorded that, although the rail transport projects had been delivered by third parties to which the OGC guidance did not apply with the same force, TS had agreed that Gateway reviews should be extended to projects which were being delivered by third parties such as the tram and Network Rail projects. I would have expected that the primary addressee of such Gateway review would have been the organisation which requested it. If reports were copied to TS, I would have expected them to be considered first in TS within Bill Reeve's directorate, and I would have expected them to draw to my attention any particular issues. If a review was asked for by CEC or TIE, I would have expected that the report would in the

first instance have been addressed to the chief officer of whichever organisation had requested it.

159. The results of Gateway reviews involving TS were generally reported to me and I certainly did see Gateway review reports on a number of TS projects during my tenure as Chief Executive. However, at this distance in time I cannot recall specifically which Gateway review reports I saw. As I have explained, the normal practice within TS was for a review to be handled by the Directorate responsible for the project in question. I would then be provided with a summary of the key findings and of any recommended actions, accompanied if appropriate by a copy of the full report. I considered the Gateway review system to be a good discipline and TS was well used to it.
160. Gateway reviews were set up by the Office of Government Commerce. Their purpose was as the name implied: they provided checkpoints as projects evolved through various stages of development and commitment. A Gateway review was intended to provide an independent audit of the health of a project: and in particular whether it was still on target in terms of programme and budget.
161. Though I accept that the quality of a Gateway review would be dependent on the quality of information available to the reviewers, any inadequacy in the information made available ought itself to attract an adverse report. In the case of a review of the tram project, the main responsibility for providing information would be TIE, although other bodies could have been involved: I recall that I was myself interviewed as part of the October 2007 review of the tram project. I have not been made aware of any inadequacies in the information provided by TIE for Gateway reviews.
162. Panels of reviewers were available to undertake Gateway reviews, and all parts of Government were asked to nominate staff to go onto those panels. The Gateway reviews were undertaken primarily for the project owner's benefit when taking the project forward. However, in a case such as the tram

project the reviews were of value to the funders as well as the people who were delivering the project. The reviews were a part of good governance.

163. I am not personally aware of any instance where a Gateway review has stopped a project. I was aware of situations where a Gateway review had found issues that needed urgent attention, resulting in delays. The reviews were more about establishing readiness to proceed to the next stage rather than cancelling a project completely. It was the responsibility of the project owner to implement the recommendations from a Gateway review. For example, if one of the TS in-house projects had received an adverse Gateway review then I would have expected the project owner to report on that and to advise me and if necessary the Board on how they proposed to resolve it, as part of the overall project management process within TS.
164. If TS became aware of any Gateway review issues identified for externally-owned rail projects then I would have expected Bill Reeve's team to address these directly with the organisation concerned, and to raise at TS Board level any aspects which were not being resolved. In general terms, however, another check was usually available, in that Gateway reviews tend to be staged at different key points in a project. If there had been an adverse Gateway review at one point, then the next set of reviewers would inevitably want to question the outcome and establish what the project owner had done to put right the issues that were identified in the previous Gateway review. If they were not satisfied then I am sure that would have resulted in strong remarks in the subsequent Gateway review report. How recommendations from Gateway reviews were managed depended on the internal processes of each organisation. Within TS, any significant issue which had budgetary or programme implications would be incorporated in the corporate risk register and therefore visible to the main Board and the Audit Committee until it was resolved.
165. I have been referred to an Office of Government Commerce (OGC) Readiness Review of the tram project which was carried out in May 2006. A report of the review was delivered to the Chief Executive of TIE on 25 May

2006 (**CEC01793454**). The overall status of the project was assessed as Red (page 4), which meant that to achieve success the project had to take action immediately. I have been referred to the report from a second OGC review dated 28 September 2006 (**CEC01629382**). That resulted in an Amber rating (page 4).

166. Though I have explained that I cannot now recall the details of specific Gateway reviews that were referred to me, I would have been concerned to be advised of these Red and Amber ratings. I note that a follow up review was carried out in November 2006 and a report dated 22 November 2006 issued (**CEC01791014**). I note that this follow-up review was commissioned on my behalf to check on progress. This indicates that TS acted directly when the second review failed to show an improvement beyond Amber status, and the report of the follow-up review, while noting that challenges still remained, showed that most outstanding recommendations had by then been implemented.
167. I have been referred to the report from a third OGC Review was carried out in October 2007 and issued on 9 October 2007 (incorrectly recorded on the cover page as 2006) (**CEC01562064**). That resulted in a Green rating (page 3), which indicated that the project was on target to succeed provided that the recommendations were acted upon. I have also been referred to an email dated 4 October 2007 from Duncan Fraser at CEC (**CEC01567494**). This provided an informal summary of the third, October 2007 review. The 2007 Gateway review of the tram project was required as a condition of grant under the new arrangements that resulted from the change in the project's status. As I have previously stated, I recall that I was interviewed as part of that review, but I do not recall seeing either the eventual report, or the CEC summary that has been mentioned to me (**CEC01567494**). Noting that the review assigned a "green" rating, I would have expected that review to be considered within Bill Reeve's team in TS as discharging the relevant condition of grant, and that I would have been advised of the detail of its findings only if there were issues that I required to discuss with the Chief Executive of CEC.



168. I have been asked about STAG. The 2006 Audit Scotland Report (**ADS00078**), page 22, paragraph 3.19 gives a very good summary of the STAG process, which is amplified in Appendix 2 and compared with other appraisal methodologies. That appendix also lists the degree of appraisal all of the projects under review, including the tram scheme, had undergone at the time of that report. STAG was introduced in 2001, and applied only to new schemes coming forward after July 2003. Appendix 2 notes that the tram scheme had been identified by CEC through a STAG review of its overall transport strategy. It adds that the route options were appraised individually through a STAG 2 stage, but the preferred option, an amalgam of two lines, had not been subject to the full STAG process (**ADS00078**, pp 48-9). However, the Auditor General's subsequent 2007 report identified that a further STAG2 report for the tram project was commissioned in 2006 (**CEC00785541** page 11). The initial stages of the STAG process involved specifying the transport problem to be addressed, and identifying options for dealing with it. More detailed evaluation of options was carried out in the STAG 2 phase, leading to the identification of a preferred option and a more rigorous appraisal of the expected costs and benefits to support that selection. The sequential nature of this process meant that as the project developed, parameters such as cost and outputs would be refined. The STAG process was intended to provide a means of appraising different schemes on a reasonably even footing. What each project was ultimately being assessed against was how it was expected to deliver against the Scottish Ministers' transport objectives in terms of efficiency and in addressing their then policy criteria. The latter included economic development, protecting the environment, social inclusion, and integration. The appraisal process allocated a score against each of these objectives so that a project which might do very well, for example, on protecting the environment might not be so strong in terms of its effects on social inclusion. The process was designed to be a sequential process to give decision-makers an across-the-board methodology for assessing very different attributes and outcomes on a common basis. However, in common with all such processes it could not be totally objective. Information and guidance on STAG was available online, and the methodology continues to be developed and refined. In my view, STAG

provides a robust and reasonable methodology for identifying options and assessing one scheme against another. It includes monetary aspects, such as affordability and return on investment, but it also weighed less tangible aspects. I was professionally familiar with the STAG process, which was something I had worked with previously and which continued to inform our consideration of new projects after Transport Scotland was established.

169. I do not recall seeing the STAG appraisal reports relating to the tram project, some of which were commissioned and acted upon before I was in office. I subsequently saw references to elements of them.

I confirm that the facts to which I attest in this witness statement, consisting of this and the preceding 78 pages are within my direct knowledge and are true. Where they are based on information provided to me by others, I confirm that they are true to the best of my knowledge, information and belief.

Witness signature...  .....  
Date of signing..... 23 June 2017 .....

