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From: [REDACTED]
Transport Scotland Ferries Unit
20 August 2015

Cabinet Secretary for Infrastructure Investment and Cities

VESSEL REPLACEMENT – PROCUREMENT OF 2 NEW MAJOR VESSELS

Purpose

1. In the absence of the Minister for Transport and Islands on leave, your approval is sought for CMAL to award shipbuilding contracts of a total cost of £96m for 2 new major ferries for the CHFS network to Ferguson Marine Engineering Ltd (FMEL).

Priority

2. **Urgent.** Given procurement deadlines, Caledonian Maritime Assets Ltd (CMAL) are required to issue a notification of contract award letter to FMEL, and ‘Alcatel’ letters to the 5 unsuccessful bidders no than Monday 31 August – after that date the tenders will no longer be valid: the original 3 month validity period has already been extended for 2 months with the agreement of all the bidders. Subject to consideration by the CMAL Board on Tuesday 25 August and feedback from CalMac Ferries Ltd, Ministerial approval in principle is sought by **Thursday 27 August**.

Background

3. The Vessel Replacement & Deployment Plan 2014 (VRDP), approved by Mr Mackay on 14 July (and to be published shortly) set out the case for the procurement of 2 new major vessels for the Clyde & Hebrides Ferry Service (CHFS) network. On the basis of the initial analytical work behind the VRDP, and the indicative vessel replacement proposals set out in the 2012 Ferries Plan, you announced the start of the procurement process for these 2 new vessels by CMAL on 15 October 2014.

4. Following consideration of Pre-Qualification Questionnaire responses, CMAL issued Invitations to Tender to the following shipyards on 10 December 2014:

- [REDACTED]
- [REDACTED]
- [REDACTED]
- [REDACTED]
- [REDACTED]
- [REDACTED]

Tender evaluation

5. 7 tenders from these 6 shipyards were submitted by the deadline of 31 March 2015. After detailed consideration of the quality and costs submissions by the CMAL vessels team, with technical input from CalMac Ferries Ltd, the CMAL executive team are recommending the award of the contracts to FMEL.

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6. It was made clear to tenderers that the quality/price ratio for assessment of proposals was 50:50. FMEL was the highest quality bid received but also the highest price. Taken together, the FMEL tender achieved the highest overall evaluation score.

7. Although CMAL are responsible for vessel procurement, under the tripartite arrangements in place CalMac have been consulted extensively at technical level to achieve their endorsement of the detailed specification and designs which will form part of the shipbuilding contract. Intensive exchanges between CMAL and CalMac on the one hand and CMAL and FMEL on the other have resolved the vast majority of the issues identified by CalMac. CalMac are currently carrying out a final review of documentation, due to complete on 25 August.

8. On the basis of discussions at the project steering group today, we anticipate that CalMac will not be in a position to fully endorse the shipbuilding documentation by the required deadline. However, under agreed procedures this does not prevent CMAL from awarding the contract and further efforts will be undertaken during the detailed design of the vessel by FMEL to address any outstanding points. These issues largely concern the access of the vessels to the various ports that they may serve during their working lives and the potential requirement for modifications at some ports. However, on the basis of the information available to us at this point, the risk of major infrastructure requirements to accommodate these vessels – such as those at Stornoway and Ullapool to accommodate the MV Loch Seaforth – is considered to be low. That said, the CHFS port infrastructure as a whole, which was largely designed for a very different size and type of vessel – requires ongoing investment in order to continue to support safe and reliable ferry services which can meet the growing demand for travel to and from the islands.

9. The vessels have been designed as 'dual-fuel' so they can operate on LNG and marine diesel. LNG is significantly cleaner and is being adopted increasingly by ferry operators in northern Europe largely in response to tighter sulphur regulations which will apply on the west coast from 2020. LNG brings some logistics challenges, which CalMac are looking into, and may require some additional fuelling infrastructure. The benefit of 'dual-fuel' is that the vessels can be run on conventional fuel if there is any interruption in LNG supply. When the initial business case for this project was drawn up, the forecast price of LNG compared to marine diesel made a compelling case for its adoption. Since then, the fall in oil prices has, at this point in time, removed the price benefit of LNG; however, historically gas prices follow oil prices and over the long-term we would expect a financial as well as an environmental benefit from using gas.

Delivery timetable

10. Under the draft contracts, the first vessel will be delivered in January 2018 and the second in March 2018, subject to final clarification and permissible delays. As previously announced, these ships are earmarked for Ardrossan-Brodick and the Uig Triangle although the final decision on vessel deployment rests with the operator and will be informed by further analysis of demand on all major routes.

Financial issues

11. The contract value is £96m. This is higher than the £80m included in the VRDP – which will be updated prior to publication – and the revised estimate of £90m included in CMAL's 3-year Corporate Plan, which has already been published.

12. This capital funding commitment will fall over 3 financial years to 2017-18 and has been submitted to Scottish Government Finance for consideration. The cost in 2015-16 can be covered from within the capital allocation to the Ferries Budget. The cost in 2016-17 will however require an increased capital allocation of around £20m.

13. Capital funding will be provided by loans from Transport Scotland to CMAL, repaid with interest over an agreed period, usually 25 years. An initial business case was drawn up by CalMac to inform the recommendation to initiate the procurement by CMAL. This is currently being updated to reflect the increased capital cost. Over the estimated 30-year lifetime of these ships, the capital cost represents a small share of overall costs.

Presentational issues

14. Subject to Ministerial approval and the clearance by SG Finance of the in-year and future funding commitments, CMAL will formally offer the contract to FMEL on 31 August which will be confirmed following the statutory 10 day standstill period. An initial announcement can be made to coincide with the formal offer, in agreement with the shipyard, rather than waiting for the 10 days.

15. Given the significance of the award in respect of Scottish Government investment in the ferry fleet, retention and creation of jobs at a resurgent Ferguson shipyard and the scale of the costs, we will work with Press TS colleagues and CMAL to ensure maximum positive publicity from this significant announcement. We will ask Press TS to lead on a Communications Plan.

16. It would be appropriate for Mr Mackay as Minister for Transport and Islands to lead on this announcement, highlighting the benefits to the islands as well as the jobs and training opportunities in Inverclyde.

17. As with any procurement, a legal challenge from one of the unsuccessful shipyards cannot be discounted. CMAL have not identified any particular risks in this regard and, in any case, are confident that any challenge can be defended. That said, the relationship between Scottish Ministers and Ferguson's owner is well known.

Recommendation

18. We recommend that you approve the award of the two shipbuilding contracts by CMAL to Ferguson Marine Engineering Ltd.

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Copy List:	For Action	For Comments	For Information		
			Portfolio Interest	Constituent Interest	General Awareness
Minister for Transport and Islands			X		

DG Enterprise, Environment and Innovation
PS/Transport Scotland
David Middleton, CE, Transport Scotland
TS Directors

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Alexander Anderson, Special Adviser