

立法會
Legislative Council

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**Background Brief on
Proposed privatization of Airport Authority**

Purpose

This paper sets out the background to the proposed privatization of Airport Authority (AA) and summarizes the major views and concerns expressed by Members at previous meetings of the Council.

Background

2. The AA is a statutory corporation established under the Airport Authority Ordinance (Cap. 483) ("the Ordinance") to provide, operate, develop and maintain an airport for civil aviation at and in the vicinity of Chek Lap Kok (known as Hong Kong International Airport), and also to carry out airport-related activities as permitted by the Chief Executive by order in the Gazette. The AA is currently wholly-owned by the Government.

3. The Financial Secretary announced on 6 August 2003 that the Government would commence work immediately in preparation for the proposed privatization of AA.

4. In pursuing partial privatization of AA, the Administration has advised that the key objectives are to

- (a) strengthen market discipline in the running of the airport for greater efficiency and more commercial opportunities;
- (b) enhance AA's access to the capital market;
- (c) introduce an additional quality stock to add diversity to the local financial markets;
- (d) offer an opportunity for Hong Kong people to participate in the success of a well-managed company with strong growth potential; and

- (e) proceeds from privatization will help to strengthen Government finance in the short to medium term.

Privatization is in line with the Government's philosophy of "big market, small government". As a matter of principle, the Administration is of the view that it should be pursued whenever the market is well placed to provide the service.

Previous discussions

Consultation with Panel

5. On 23 February and 2 March 2004, the Administration briefed the Panel on Economic Services (the Panel) on the preparatory work for the proposed privatization of AA. The Administration advised that it was mindful of the concerns over certain issues relating to the proposed privatization, and therefore had decided to take more time to further consult stakeholders on the specific issues as set out in **Annex A** before putting a privatization bill to the Council.

Proposal to optimize AA's capital structure

6. However, in order to lower the overall costs of AA's capital, the Government intended to ask AA to return to it about \$6 billion of equity capital prior to privatization. According to the Administration, while AA would have to finance such return of equity by borrowing, it was estimated that an amount of about \$6 billion should not unduly affect its financial strength and credit rating, subject to the continuation of appropriate Government credit support mechanism, e.g. a majority Government ownership. The additional borrowing by AA to finance a capital restructuring would increase its interest expenses and lower the amount of its net profits in the next few years. But the capital structure optimization would in the long term help improve AA's return on equity and make it more attractive to potential investors.

7. On 9 June 2004, the Council passed the Airport Authority (Amendment) Bill 2004 which sought to provide a mechanism for the reduction of AA's capital and the return of AA's equity capital to Government in cash or in kind. On 16 June 2004, the Administration moved a resolution to effect the proposed reduction of \$6 billion in the capital of AA and to require AA to distribute an amount equivalent to the reduction to the Government. Payment received by the Government would be credited to the Capital Investment Fund. The Resolution would also give effect to the cancellation of shares in the AA held by the Government to an equivalent value. The resolution was passed by the Council.

Members' concerns

8. The primary concerns expressed by Members in previous meetings over the proposed privatization of AA are set out below:

- (a) the impact of privatization on staff working on the airport island;
- (b) the mechanism to govern the adjustment of airport charges;
- (c) the mechanism to upkeep the service standards and efficiency of AA after privatization;
- (d) the scope of AA's business and competition and mechanism to prevent AA from abusing its monopolistic power after privatization;
- (e) the residual Government controls over AA after privatization;
- (f) the need for the Government to balance the conflicting interests of various stakeholders after privatization;
- (g) the need for the Government to take back the land on the airport island not already earmarked for airport operational and support facilities before privatizing AA; and
- (h) the pros and cons of various privatization options.

9. Members may wish to refer to the minutes of the Panel meetings on 23 February 2004 (LC Paper No. CB(1)1321/03-04) and 2 March 2004 (LC Paper No. CB(1)1685/03-04) for details.

Overseas duty visit

10. The Panel conducted an overseas duty visit in April 2004 to study overseas experience in airport privatization amongst other things.

11. During their stay in London, the delegation met with the Head of the Economic Regulation Group of the UK Civil Aviation Authority and exchanged view with him over the economic regulatory framework for designated UK airports upon privatization. The delegation also received a briefing by the Ministry of Transport, Public Works and Water Management of the Netherlands Government on the proposed privatization of the Amsterdam Airport Schiphol.

12. A report on the overseas visit was published in June 2004 (LC Paper No. CB(1)2216/03-04).
13. A list of relevant papers is in **Annex B**.

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Issues for Further Consultation with Stakeholders

A. Economic Regulation

1. Basic principles – fair, user pays; predictable and stable; clear, simple and transparent; allow reasonable return; provide incentives for efficiency, service quality and investment; minimize administrative costs.
2. Scope of regulated activities – only those activities in the “monopolistic bottleneck”, i.e. those core airport activities which are necessary for the operation of airlines, but cannot be economically duplicated or produced outside the airport perimeter.
3. Permissible return – the return from regulated activities is to be capped, the exact level to be further determined. As AA would be free, subject to market conditions and statutory prohibitions (see item 9 below), to adopt any target return for the non-regulated activities, the AA’s overall return as a company could be above the cap.
4. Price setting – AA to draw up a set of price caps for airport charges for 3 to 5 years taking into account projected costs, revenues and capital expenditure relating to regulated activities and following consultation with airlines. The price caps could be set in different ways, e.g. with specific numbers, an inflation-linked formula, etc.
5. Service standards – AA to draw up a set of service standards at the same time as setting price caps for airport charges. Consideration could be given to a financial reward and penalty system to link the actual service standards to the level of airport charges.
6. Qualitative factors – notwithstanding the price caps, AA would have to explain how it has taken into account some qualitative factors such as competitiveness of the airport or general economy of Hong Kong before implementing any adjustment to airport charges.

7. Dispute resolution – an independent body would be established to adjudicate on any complaint from airlines against the setting of price caps by AA.

B. Scope of AA's business and competition

8. Subject to applicable laws, restrictions in the Land Grant and other Government regulations, the AA would be allowed to conduct any airport-related activities both on and outside the airport island.
9. Statutory provisions would be included in the privatization bill to prohibit AA from engaging in anti-competitive activities and abuse of its dominant position, modeling on similar provisions in the Telecommunications Ordinance (Cap. 106) and Broadcasting Ordinance (Cap. 562). The same independent body responsible for adjudicating on airport charges could also be tasked to deal with any complaints against AA's alleged breaches of these provisions.

C. Other Controls on AA

10. Government to appoint a minority number of members to the Board of AA to represent Government's interests, on top of any rights Government may have as a shareholder.
11. More than half of the members of the AA Board, excluding Government appointed directors, should be ordinarily resident in Hong Kong. The existing requirement for the AA Chairman to be a Hong Kong Permanent Resident would be retained.
12. Material interests in shares by any single shareholder (including associates), other than HKSAR Government, would be limited to not more than 10% of the issued shared capital.
13. The exercise of voting rights by shareholders who are not ordinarily resident in Hong Kong would be limited to not more than 49% of votes cast at a general meeting of shareholders.

14. Government to be empowered to obtain information from AA for the purpose of enforcing relevant laws and regulations.
15. AA would be required to submit capital investment plans to the Government as a regulator of the airport.
16. Government to be empowered to give directions to AA in the public interest, with compensation to AA under specified circumstances.
17. Government to be empowered to take over AA's assets in case of AA's default, with compensation to AA under specified circumstances.
18. Government to retain powers to revoke the aerodrome licence of AA in case of substantial breakdown of services at the airport or under other prescribed conditions.

Privatization of Airport Authority

List of relevant papers

Council/Committee	Date of meeting	Papers
Economic Services Panel	23 Feb 2004 2 Mar 2004	<p>Information paper on the privatization of Airport Authority (LC Paper No. CB(1)1017/03-04(05)) http://www.legco.gov.hk/yr03-04/english/panels/es/papers/es0223cb1-1017-5e.pdf</p> <p>Response to questions raised by the members at the meeting on 23 February 2004 (LC Paper No. CB(1)1154/03-04(01)) http://www.legco.gov.hk/yr03-04/english/panels/es/papers/es0302cb1-1154-1e.pdf</p> <p>Response to questions raised by the members at the meeting on 2 March 2004 (LC Paper No. CB(1)1749/03-04(01)) http://www.legco.gov.hk/yr03-04/english/panels/es/papers/es0302cb1-1749-1e.pdf</p>
Bills Committee on Airport Authority (Amendment) Bill 2004	7 May 2004	<p>LegCo Brief on Airport Authority (Amendment) Bill 2004 (File Ref.: FIN CR 4/2/951/00) http://www.legco.gov.hk/yr03-04/english/bills/brief/b43_brf.pdf</p>
Council Meeting	9 June 2004	<p>Report of the Bills Committee on Airport Authority (Amendment) Bill 2004 to the Council on 9 June 2004 (LC Paper No. CB(1)1930/03-04) http://www.legco.gov.hk/yr03-04/english/bc/bc07/reports/bc070609cb1-rpt-e.pdf</p>