

LEGISLATIVE COUNCIL PANEL ON TRANSPORT

Application for Toll Increase by Tate's Cairn Tunnel Company Limited

PURPOSE

Tate's Cairn Tunnel Company Limited (TCTC) has applied for an increase in tolls. This paper seeks Members' views on the application.

BACKGROUND

2. TCTC was granted a franchise under Tate's Cairn Tunnel Ordinance (Cap. 393) (the Ordinance) to build and operate the Tate's Cairn Tunnel for 30 years starting from July 1988, inclusive of the construction period. The tunnel was opened to traffic in June 1991. TCTC's franchise will expire in July 2018.

3. Section 36(3) of the Ordinance provides that the tolls specified in the Schedule to the Ordinance may be varied by agreement between the Chief Executive-in-Council and the tunnel company. If an agreement cannot be reached, either party may resort to arbitration. The Ordinance has not set out the criteria for determining toll adjustments. It only stipulates that if the matter is submitted for arbitration, the Arbitrator shall be guided by the need to ensure that the company is reasonably but not excessively remunerated for its obligations under the Ordinance.

TCTC'S APPLICATION FOR TOLL INCREASE

4. So far, Tate's Cairn Tunnel has had four toll increases which came into effect in May 1995, November 1996, January 2000 and August 2005 respectively. TCTC applied for its fifth toll increase in December 2006.

5. The existing tolls and new tolls proposed by TCTC are as follows –

	Motor-cycles	Private car & taxi	Light bus and light goods vehicle	Medium and heavy goods vehicle	Single-decker bus	Double-decker bus	Extra axle
Existing Tolls	\$10	\$12	\$18	\$23	\$24	\$26	\$15
Proposed Tolls	\$12	\$15	\$23	\$26	\$30	\$33	\$19
Increase %	20%	25%	28%	13%	25%	27%	27%

CONSIDERATIONS

(A) Guiding Principle – Reasonable but not Excessive Remuneration

6. On the basis of the Base Toll Proposal which accompanied its franchise bid, TCTC expected that it would achieve an Internal Rate of Return (IRR) of 13.02% over the 30-year franchise period. In considering TCTC's franchise bid in 1988, the Government agreed to the initial tolls but gave no undertaking in respect of subsequent toll adjustments. Neither was there any agreement on a guaranteed rate of return.

7. TCTC's target IRR is the lowest among the four Build-Operate-Transfer tunnels in Hong Kong. Route 3 (Country Park Section) aims at a target IRR of 15.18%, while the targets for the Eastern Harbour Crossing and the Western Harbour Crossing were both 16.5%. TCTC projects that with the toll increases (including the current application and five subsequent projected increases during the remainder of the franchise), it will be able to achieve an IRR of 8.47% over the 30-year franchise period. If no toll increase is to be made before the end of the franchise, TCTC will only achieve an IRR of 5.72%.

(B) Traffic Implications

8. Currently, Tate's Cairn Tunnel has an average daily throughput of 56,400 vehicles, against its design capacity of 78,500 vehicles. TCTC has estimated that with its proposed toll increases, about 1,300 and 400 vehicles will be diverted to Lion Rock Tunnel (LRT) and Tai Po Road (TPR) respectively per day. Nevertheless, Route 8 between Cheung Sha

Wan and Shatin, which was commissioned in March 2008, will help relieve the traffic congestion at LRT and TPR. According to TCTC, one of the key assumptions in planning the franchise bid in 1988 was that the tolls for LRT would be increased broadly in line with inflation. This scenario has not materialized.

(C) Public Affordability and Acceptability

9. The magnitude of TCTC’s proposed toll increases for different vehicle types ranges from 13% to 28%. Public affordability and acceptability would have to be carefully taken into account.

(D) Arbitration

10. As mentioned in paragraph 3 above, if an agreement on the toll increase cannot be reached between the Government and TCTC, either party may resort to arbitration under the Arbitration Ordinance. Therefore TCTC has the right to resort to arbitration if its application for the toll increase is rejected by the Executive Council.

TCTC’S FINANCIAL POSITION

11. By the end of June 2007, TCTC had accumulated losses of \$53 million, representing a shortfall of \$2,343 million as compared with the expected cumulative profit of \$2,290 million in the base case projection. The difference between the actual profit/losses of TCTC and base case projections over the years is set out below –

Profit & Loss (in \$million)			
Year¹	Base Case Projection (A)	Actual Profit/Losses (B)	Difference (B-A)
1991/92	(149)	(176)	(26)
1992/93	(148)	(159)	(11)
1993/94	(147)	(147)	0
1994/95	(69)	(143)	(74)
1995/96	(56)	(94)	(38)
1996/97	41	(71)	(112)
1997/98	66	(43)	(109)
1998/99	88	(41)	(129)

¹ TCTC’s financial year is from 1 July to 30 June of the following year.

1999/2000	194	(10)	(204)
2000/01	212	18	(194)
2001/02	265	92	(173)
2002/03	356	103	(253)
Deferred tax adjustment²	-	120	120
2003/04	371	97	(273)
2004/05	372	112	(260)
2005/06	448	141	(307)
2006/07	447	146	(301)
Cumulative	2,290	(53)	(2,343)

12. TCTC started to make an operating profit in 2000/01. It repaid its bank loan in October 2004, and shareholders' loan in 2004/05 after repayment of the bank loan. According to TCTC, at the current toll levels, it will be able to wipe off the accumulated loss by 2007/08, with an accumulated profit of \$93 million at the end of the year. TCTC also forecasts that it will start to pay dividends in 2007/08.

13. The financial underperformance was mainly attributable to lower toll revenue caused by lower-than-expected traffic volume through the tunnel as compared to the franchise bid. TCTC attributes the lower-than-expected traffic volume to the following –

- (a) increasing toll disparity between LRT and TCT;
- (b) relocation of the airport;
- (c) diversion effect due to an increase in transportation modes and road choices, for instance, the opening of Route 3 (Tai Lam Tunnel) and Ma On Shan Railway; and
- (d) migration of industrial/manufacturing activities to the Mainland.

² The deferred tax adjustment was a result of the adoption of a revised accounting standard.

ADVICE SOUGHT

14. Members' views are invited on the toll increase application submitted by TCTC.

**Transport and Housing Bureau
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