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Panel on Transport

**Background brief on
toll increases by Tate's Cairn Tunnel Company Limited**

Purpose

This paper sets out the background to the toll adjustment mechanism for Tate's Cairn Tunnel (TCT) and summarizes Members' concerns about the toll increases of TCT and related matters.

Tate's Cairn Tunnel

2. Tate's Cairn Tunnel Company Limited (TCTC) was granted a franchise under the Tate's Cairn Tunnel Ordinance (Cap. 393) (TCTO) to build and operate TCT for 30 years starting from July 1988, inclusive of the construction period. The tunnel was built at a cost of \$1.96 billion and was opened to traffic in June 1991. The franchise granted to TCTC will expire in July 2018.

Toll adjustment mechanism

3. Section 36(3) of TCTO provides that the tolls specified in the Schedule to TCTO may be varied by agreement between the Chief Executive-in-Council (CE-in-Council) and TCTC. If an agreement cannot be reached, either party may resort to arbitration. TCTO 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 TCTC is reasonably but not excessively remunerated for its obligations under TCTO.

Considerations for toll increase

4. In considering TCTC's application for toll increase, the Administration would seek the views of the Panel on Transport (the Panel) and the Transport Advisory Committee (TAC) before seeking the approval of the CE-in-Council on TCTC's application for toll increase.

TAC's assessment

5. In the 2005 toll revision exercise of TCT, TAC considered that TCTC's application for toll increase was justified. In coming up with its recommendation, TAC had considered a basket of factors, including definition and interpretation of what amounted to "reasonable but not excessive remuneration", financial position of TCTC, the economic conditions of Hong Kong as well as any material changes in the economic conditions since the last toll increase, traffic impact of the proposed toll increase, and public acceptability.

Reasonable but not excessive remuneration

6. As to the definition and interpretation of what amounts to "reasonable but not excessive remuneration", the Administration pointed out that in considering TCTC's Base Toll Proposal in 1988, it agreed to the initial tolls but gave no undertaking in respect of subsequent toll adjustments. Neither was there any agreement on a targeted or expected internal rate of return (IRR). However, based on the Base Toll Proposal that accompanied its franchise bid, the Administration understood TCTC expected that it would achieve an IRR of 13.02% over the 30-year franchise period. This is in fact the lowest among the four Build-Operate-Transfer (BOT) tunnels in Hong Kong. The Route 3 (Country Park Section) aims at a targeted IRR of 15.18%, while the targets for the Eastern Harbour Crossing and the Western Harbour Crossing are both 16.5%.

Previous cases for arbitration of other BOT tunnels

7. Similar to TCT, the Eastern Harbour Crossing Ordinance (Cap. 215) (EHCO) does not set out the criteria for determining toll adjustments. It only stipulates that if the matter is submitted for arbitration, the arbitrators shall be guided by the need to ensure that the tunnel company is reasonably but not excessively remunerated for its obligations under EHCO, having regard to, among other things, any material changes in Hong Kong's economic conditions since the enactment of the Ordinance or since the tolls were last determined.

8. Since the commencement of the operation of Eastern Harbour Crossing (EHC), the New Hong Kong Tunnel Company Limited (NHKTC), the franchisee of EHC has sought arbitration on its toll increase applications in 1997 and 2005.

9. In 1995, NHKTC submitted their case to arbitration when the Government rejected NHKTC's first toll increase application in 1995. The arbitrator ruled in 1997 that the band of reasonable remuneration for NHKTC was an IRR between 15% and 17% over the life of the franchise. The arbitrator also concluded that to maintain a remuneration which is reasonable but not excessive, it would be necessary to prevent NHKTC's remuneration falling below an IRR on equity of about 15%.

10. In August 2003, NHKTC commenced arbitration against the Government's decision for rejecting its toll increase application. In January 2005, the arbitrators determined that the tolls for private cars and taxis should be increased by \$10 to \$25 with corresponding increases for other types of vehicles. The arbitrators' conclusion is that the level of reasonable but not excessive remuneration for the NHKTC is an IRR on equity after tax of between 15% and 17% over the life of the franchise.

LegCo's power to amend the toll levels of TCT

11. After an agreement on revision to toll levels reached between the CE-in-Council and TCTC or arbitration award, the Commissioner for Transport (C for T) shall amend the Schedule to TCTO by notice in the Gazette as soon as is practicable. Such notice is subsidiary legislation which is subject to the negative vetting procedure of LegCo. However, the power of C for T to make such notice does not cover the determination of toll levels and the timing for implementation of the new tolls. According to section 34(2) of the Interpretation and General Clauses Ordinance (Cap. 1), LegCo's power to amend subsidiary legislation has to be consistent with the power to make such subsidiary legislation. In other words, there is little room for LegCo to amend such notice other than making minor technical amendments. Similarly, LegCo cannot repeal the notice as the exercise of such power is also inconsistent with the power of the C for T to make the notice.

Alternative routes to TCT

12. Tsing Sha Highway section between Sha Tin and Cheung Sha Wan was open to traffic on 21 March 2008. The toll charge for all vehicles using the tunnels along the Tsing Sha Highway is \$8. The Administration has anticipated that there would be a diversion effect to ease the increasing traffic flow in the Lion Rock, TCT and Shing Mun Tunnels as well as along Tai Po Road.

13. The Lion Rock Tunnel provides a road link from north Kowloon to Sha Tin and north-eastern New Territories. It was used on average by 89 200 vehicles daily in 2006. The toll is \$8.

14. The Shing Mun Tunnels link up Tsuen Wan to Sha Tin. They were used on average by 52 800 vehicles each day in 2006. The toll is \$5.

15. The latest traffic flow of TCT and alternative routes are set out in **Appendix A**.

Toll increases for TCT

16. So far, Tate's Cairn Tunnel has had four toll increases that came into effect in May 1995, November 1996, January 2000 and August 2005 respectively.

Previous discussions by the Council on the toll increase for TCT in 2005

17. The Panel last discussed the application for toll increase by TCTC on 2 February 2005. Members were worried that the proposed toll increase would aggravate the traffic congestion at Lion Rock Tunnel and induce other public transport operators to increase their fares. They called on the Administration to request the tunnel company to defer the toll increase. Views were also expressed that the Administration should expeditiously make a decision on its position regarding the application for toll adjustments by the tunnel company and hold discussions with the company in accordance with section 36 of TCTO and it should refer the matter for arbitration as soon as possible if an agreement could not be reached.

18. On 2 February 2005, the Panel passed the following motion:

"In view of the gradually improving financial position of the Tate's Cairn Tunnel Company Limited, this Panel considers it inappropriate to increase the tunnel tolls at this stage."

19. On 10 June 2005, the Government published in the Gazette the new Schedules to reflect the toll increases of TCT and Tai Lam Tunnel and Yuen Long Approach Road. The Panel was disappointed that the Administration did not consult the Panel prior to gazettal of the notices. The Panel held a meeting on 15 June 2005 to discuss the matter with the Administration and the tunnel companies.

20. At the meeting on 15 June 2005, the Panel reiterated its concern about the tunnel toll increases and their impact on traffic and the general public, and the request that the tunnel companies should defer the toll increases or offer concessionary tolls to motorists. The Panel also urged the Administration to review the decision of allowing the tunnel companies to increase their tolls. Whilst recognizing the inherent problems associated with BOT tunnels whereby tunnel operators would only aim at maximizing their profit, the Panel called on the Administration to review the effectiveness and appropriateness of using BOT approach in taking forward infrastructure projects.

21. The Panel passed a motion at the meeting on 15 June 2005, urging the Administration to withdraw the Gazette notices on the toll increases of TCT (L.N. 93 of 2005) and Route 3 (Country Park Section) (L.N. 95 of 2005).

22. A Subcommittee was subsequently formed at the House Committee meeting on 17 June 2005 to study the above Gazette notices. The Subcommittee was gravely concerned whether the toll increases for TCT and Route 3 were justified, and the impact of the toll increases on the public and traffic flow. To better protect the interests of the public, the Subcommittee also examined a member's suggestion that the Administration should set up a task force to monitor the toll levels of the various tunnels in Hong Kong, in particular the three road harbour crossings, and to collect views on how the toll adjustment

mechanisms could be improved.

23. The Administration advised the Subcommittee that toll adjustments for various tunnels were made in accordance with the requirements set out in the relevant ordinances and Project Agreements. Given that there were on-going discussions between the Administration and the operators of the three road harbour crossings and Route 3 on possible improvements to the existing toll adjustment mechanism, the Administration did not see the need for the setting up of a task force as suggested.

24. The Council passed a motion on BOT tunnels at its meeting on 6 July 2005. The wording of the motion is in **Appendix B**.

25. The the Panel has been following up on measures to rationalize utilization of BOT tunnels. Research reports were also prepared by the Research and Library Services Division on "Operation of Toll Roads, Bridges and Tunnels in Selected Places" (RP03/05-06) and "Adoption of the Build-Operate-Transfer Model and its Variants in Developing Transport Infrastructures in Selected Places" (N13/05-06).

Relevant papers

26. A list of relevant papers is in **Appendix C**.

Council Business Division 1
Legislative Council Secretariat
23 April 2008

Tate's Cairn Tunnel - Traffic

Year	Traffic (Vehicles)			
	South-bound	North-bound	Total	Daily Average
1997	-	-	25,819,035	70,737
1998	11,492,923	12,227,753	23,720,676	64,988
1999	11,319,975	12,112,627	23,432,602	64,199
2000	11,171,193	11,986,211	23,157,404	63,272
2001	11,287,397	12,079,799	23,367,196	64,020
2002	11,047,518	11,851,262	22,898,780	62,736
2003	10,772,350	11,464,759	22,237,109	60,924
2004	10,842,069	11,508,288	22,350,357	61,067
2005	10,180,063	10,736,088	20,916,151	57,305
2006	9,784,153	10,340,727	20,124,880	55,137

Lion Rock Tunnel - Traffic

Year	Traffic (Vehicles)			
	South-bound	North-bound	Total	Daily Average
1997	17,457,723	18,118,150	35,575,873	97,468
1998	16,958,567	17,619,355	34,577,922	94,734
1999	16,070,872	16,761,170	32,832,042	89,951
2000	16,503,581	17,207,341	33,710,922	92,106
2001	16,268,870	16,900,276	33,169,146	90,874
2002	16,109,459	16,663,433	32,772,892	89,789
2003	15,741,179	16,389,769	32,130,948	88,030
2004	15,698,881	16,405,189	32,104,070	87,716
2005	15,594,722	16,379,422	31,974,144	87,600
2006	15,834,595	16,710,903	32,545,498	89,166

Shing Mun Tunnels - Traffic

Year	Traffic (Vehicles)			
	South-bound	North-bound	Total	Daily Average
1997	9,963,876	10,123,429	20,087,305	55,034
1998	9,752,478	9,841,764	19,594,242	53,683
1999	9,705,336	9,762,548	19,467,884	53,337
2000	9,903,248	9,933,616	19,836,864	54,199
2001	9,840,354	9,794,316	19,634,670	53,794
2002	9,972,093	9,941,663	19,913,756	54,558
2003	9,652,610	9,688,391	19,341,001	52,989
2004	9,724,351	9,792,780	19,517,131	53,325
2005	9,665,724	9,730,936	19,396,660	53,142
2006	9,648,578	9,631,553	19,280,131	52,822

Motion on BOT tunnels passed by the Council on 6 July 2005

"That, in view of the toll increases by the operators of a number of transport infrastructures delivered through the Build-Operate-Transfer ('BOT') mode, which not only directly increase the burden of transport expenses on the public and lead to a rise in transportation costs for the business and industrial sectors, but also greatly aggravate the traffic congestion at other lower-toll tunnels or toll-free routes, thereby defeating the intended purpose of diverting traffic flows to various tunnels, this Council urges the Government to expeditiously put up, in six months' time, specific proposals for improvement regarding the following:

- (a) actively exploring with the tunnel companies which own the franchises of the tunnels ways to achieve effective distribution of traffic among various tunnels and to relieve the pressure on various tunnels to increase their tolls, such as extending the franchise periods, standardizing and reducing the tolls or adopting other feasible measure;
- (b) conducting a comprehensive review of the BOT mode and drawing conclusion from the relevant experience to serve as guidance in the financing, construction, toll charging and operation, etc, of future transport infrastructures, so as to avoid the above pitfalls and safeguard the interests of the public;
- (c) reviewing whether the current toll increase mechanisms under the Tai Lam Tunnel and Yuen Long Approach Road Ordinance and the Western Harbour Crossing Ordinance are in the public interest, and avoiding the introduction of similar mechanisms for future transport infrastructures; and
- (d) negotiating common ownership of the three road harbour crossings with the consortium which owns the franchises of both the Eastern Harbour Crossing and the Western Harbour Crossing, and presenting to this Council reports on the progress of the negotiations."

Appendix C

Tate's Cairn Tunnel Company Limited

Meeting date	Committee	Papers/Items
2 Feb 2005	Transport Panel (TP)	Administration's paper on Application for Toll Increase by Tate's Cairn Tunnel Company Limited http://www.legco.gov.hk/yr04-05/english/panels/tp/papers/tp0202cb1-786-3e.pdf
2 Feb 2005	TP	Tate's Cairn Tunnel Company Limited - Toll Increase Application Briefing Paper for Legislative Council Panel on Transport http://www.legco.gov.hk/yr04-05/english/panels/tp/papers/tp0202cb1-786-4e.pdf
2 Feb 2005	TP	Powerpoint presentation materials provided by Tate's Cairn Tunnel Company Limited http://www.legco.gov.hk/yr04-05/english/panels/tp/papers/tp0202cb1-854-1e.pdf
2 Feb 2005	TP	Minutes of meeting http://www.legco.gov.hk/yr04-05/english/panels/tp/minutes/tp050202.pdf
15 June 2005	TP	Application for Toll Increase by Tate's Cairn Tunnel Company Limited http://www.legco.gov.hk/yr04-05/english/panels/tp/papers/tp-etwb_t_cr1465194-e.pdf
15 June 2005	TP	Minutes of meeting http://www.legco.gov.hk/yr04-05/english/panels/tp/minutes/tp050615.pdf
6 July 2005	Council	Motion debate on "Reviewing the mode of construction and operation of transport infrastructure" http://www.legco.gov.hk/yr04-05/chinese/counmtg/floor/cm0706ti-confirm-c.pdf
14 Oct 2005	House Committee	Report of the Subcommittee to Study Tate's Cairn Tunnel Ordinance (Replacement of Schedule) Notice 2005 and Tai Lam Tunnel and Yuen Long Approach Road Ordinance (Replacement of Schedule 1) Notice 2005 http://www.legco.gov.hk/yr05-06/english/hc/papers/hc1014cb1-31-e.pdf

Meeting date	Committee	Papers/Items
		<p>Research Report on Operation of Toll Roads, Bridges and Tunnels in Selected Places</p> <p>http://www.legco.gov.hk/yr05-06/english/sec/library/0506rp03e.pdf</p> <p>Information Note on The Adoption of the Build-Operate-Transfer Model and Its Variants in Developing Transport Infrastructures in Selected Places prepared by Research and Library Services Division</p> <p>http://www.legco.gov.hk/yr05-06/english/sec/library/0506in13e.pdf</p> <p>Information Note on Toll Increase of the Eastern Harbour Crossing prepared by Research and Library Services Division</p> <p>http://www.legco.gov.hk/yr05-06/english/sec/library/0506in14e.pdf</p> <p>Information Note on Nottingham Express Transit prepared by Research and Library Services Division</p> <p>http://www.legco.gov.hk/yr05-06/english/sec/library/0506in15e.pdf</p>