

For Information

**Legislative Council Panel on Transport
Subcommittee on Matters Relating to Railways**

**Hong Kong section of
Guangzhou – Shenzhen – Hong Kong
Express Rail Link**

INTRODUCTION

This paper provides Members with supplementary information on the pros and cons of the ownership and concession approaches in financing railway projects, the determination of on-cost payment in these projects, as well as the forecast of cross boundary traffic at various land crossings in 2016.

BACKGROUND

2. At the meeting of the Subcommittee held on 2 May 2008, we sought Members' support for a funding application to be made to the Public Works Subcommittee (PWSC) and the Finance Committee (FC) for the design and site investigation for the proposed Hong Kong section of the Guangzhou – Shenzhen – Hong Kong Express Rail Link (XRL). We undertook to provide the supplementary information set out in paragraph 1 above.

**FINANCING OF RAILWAY PROJECTS AND PROS AND CONS OF THE
“OWNERSHIP APPROACH” AND THE “CONCESSION APPROACH”**

3. Before the Rail Merger in December 2007, all railway projects were financed under the ownership approach. Under this approach, the railway corporations were responsible for the funding, design, construction, operation and maintenance of the railway, and ultimately own it. Since the two railway corporations operated on commercial principles, they would not take up financially non-viable railway projects unless some form of financial support was provided by the Government as appropriate. At present, the different forms of financial assistance provided / proposed by the Government include the granting of property development rights, waiver of dividends and provision of a lump sum capital grant. The form of funding support for each railway project is considered on a case-by-case basis.

4. Since the implementation of the Rail Merger, the MTR Corporation Limited (MTRCL) has been granted a service concession by the Kowloon-Canton Railway Corporation (KCRC) to operate the existing and new KCR railway lines under construction. The MTRCL is now responsible for the operation, maintenance and improvement of the KCR system, including the replacement of the concession assets, during the concession period. It exercises control over all the operational arrangements of the KCRC network in addition to its own network and is responsible for the performance of the

total system. Upon expiry or termination of the service concession, the MTRCL would be required to return to the KCRC an operating KCR system that meets the prevailing operating standards. In other words, the KCRC is not disposing of the railway system to the MTRCL, and the MTRCL is not acquiring the KCRC's railway assets (except for certain low value items such as spare parts and consumables).

5. It was also agreed in the context of the Rail Merger that for individual new railway projects which are not natural extensions of the MTRCL network, the Government has the discretion to determine whether to adopt the ownership approach or the concession approach. Under the concession approach, the Government will provide for the railway facilities of the new railway and the MTRCL will be granted a service concession to operate it.

6. Under the concession approach, as compared to the ownership approach, the Government bears the construction risk and shares the operational risk of the project. However, the ownership of the railway ultimately rests with the Government. Service concession payments, the amount of which depends on the profits arising from the operation of the railway, will be paid by the MTRCL to the owner of the railway in exchange for the right to operate it. If the railway turns out to be more profitable than projected, the Government would be able to share the upside by means of the concession payment, apart from sharing the profits indirectly in the form of dividends distributed by the MTRCL to its shareholders (the Government currently owns around 76% of the MTRCL's total shareholding).

7. The Administration briefed this Council on the two financing approaches (i.e. the ownership and concession approaches) of new railway projects during the Rail Merger consultation. There were detailed discussions on this subject in the Panel on Transport and the Panel on Financial Affairs in April 2006, followed by the discussion at the Bills Committee on the Rail Merger Bill. In June 2007, when this Council resumed Second Reading debate on the Bill, the concession approach and the reasons for adopting it were explained. Relevant papers were also issued to this Council for members' reference (Paper No.: CB(1)1291/05-06(01) and File Ref.: ETWB(T) CR 1/986/00).

8. The form of funding support for railway projects should be project specific. The Government will consider the most viable options for providing funding support for each railway project on a case-by-case basis, having regard to the following considerations:

- (a) whether the Government should take a longer term view on investment in railway infrastructure and would like to retain the ownership of the railway, thereby retaining the residual value of the railway;
- (b) whether the Government would be prepared to input more resources, including staff and cash outlay, to implement the railway under the

concession approach;

- (c) whether the Government would be prepared to bear the construction risks and operating risks under the concession approach, e.g. lower revenue as a result of patronage being lower than anticipated;
- (d) the financial implications for the Government;
- (e) whether the selected approach would allow the MTRCL to effectively co-ordinate the planning and implementation of the railway and the above station/depot property development; and
- (f) whether the ownership of the new railway by the Government will facilitate the smooth implementation of the railway networks.

9. As regards new projects which are natural MTR-extension projects, the ownership approach will be adopted.

ON-COST

10. Under the concession approach, the MTRCL will be entrusted with the design and construction of the new projects, subject to the Government's formal approval process, and the MTRCL and the Government agreeing on the fee of such entrustment. In the case of the XRL, services to be provided by the MTRCL for the management and supervision of the design and construction works of the project will be covered by an on-cost, which includes, but is not limited to, staff cost for the MTRCL's dedicated project management team and the headquarters for providing support for the project; accommodation costs for the dedicated project management team and consultants; and corporation costs (e.g. legal, financial, human resources, public relations, operating support, insurance, corporate governance and other relevant overheads).

11. The on-cost payable to the MTRCL could be settled in two different ways. The first is to pay the MTRCL on a reimbursement basis, i.e. the MTRCL will be paid back the actual on-cost expenses incurred during the course of the work. The second is to pre-determine a certain percentage (known as on-cost rate) of the actual expenditure of the design and construction works undertaken to be the on-cost payable to the MTRCL. The first way will require tremendous administrative efforts in verifying the MTRCL's on-cost expenditure and will not be desirable in view of the scale of the construction works of the XRL. The second way is the one usually adopted as it provides better financial control, and is more practicable from the resources point of view.

12. At present, the on-cost rate for the XRL has yet to be agreed with the MTRCL. The determination of a reasonable on-cost rate takes time. We would need to, for example, examine the MTRCL's audited accounts of previous projects and ascertain the actual on-cost apportioned to individual

projects, and would also need to further negotiate with the MTRCL. Pending an agreement on the on-cost rate, payment of the on-cost for design work to the MTRCL will have to be made on a reimbursement basis according to the actual expenses incurred by the MTRCL for such services. The sum will be off-set in the final on-cost payable to the MTRCL for the design and construction of the whole project. Hence the design on-cost now shown in item (a)(IV) of paragraph 11 of the PWSC paper of XRL (Paper No.: PWSC(2008-09)22) is only an indicative figure. Purely for the purpose of providing an estimate, we have adopted a percentage of 16.5% in the cost breakdown. This should not, however, be taken to mean that we would be paying design on-cost to the MTRCL on this basis; nor should it be taken as the Government's agreement to adopting the same percentage as the actual on-cost rate for both design and construction. We will seek independent consultancy advice in assessing the reasonableness of the on-cost rate to be proposed by the MTRCL for the XRL project.

CROSS-BOUNDARY TRAFFIC FORECAST IN 2016

13. The two-way daily passenger forecast at various cross-boundary control points in 2016 is given in the table below.

Two-way Daily Passenger Forecast For Cross-Boundary Public Transport in 2016

Transport Modes	Types/Control Points	Two-way daily passenger forecast in 2016
Trains	Boundary Trains (Lo Wu/ Lok Ma Chau)	285 000
	XRL	99 000
	East Rail Line Intercity Trains (Hung Hom)	10 000
	Sub-total for Trains	394 000
Buses/Coaches	Hong Kong - Zhuhai - Macao Bridge	47 000
	Lo Ma Chau	118 000
	Shenzhen Bay Bridge	55 000
	Man Kam To/Sha Tau Kok	20 000
	Sub-total for buses/coaches	240 000