

A. Introduction

The Audit Commission ("Audit") conducted a review to examine the Environmental Protection Department ("EPD")'s planning and administration of land in EcoPark. The review focused on the following areas:

- planning of EcoPark;
- Phase 1 development;
- Phase 2 development; and
- administration of management contract.

2. At the beginning of the Committee's public hearing, **Dr Ellen CHAN Ying-lung, Assistant Director of Environmental Protection**, made a powerpoint presentation to report the up-to-date progress of the development of EcoPark since the completion of the Audit study at the end of February 2010. An information note provided by the Environment Bureau ("ENB")¹ and the EPD in May 2010 and a letter of 22 June 2010 from the Director of Environmental Protection on the up-to-date progress of the development of EcoPark are in *Appendices 6 and 7* respectively.

B. Planning of EcoPark

Delays in the planning of EcoPark

3. The Committee noted from paragraphs 2.2 to 2.13 of the Audit Report that there had been repeated delays in the planning of EcoPark. In September 2001, the ENB announced that the Government would build EcoPark to provide long-term land for the local recycling industries. The capital works were scheduled for completion by the end of 2004. In the same year, the EPD employed an engineering consultant ("Consultant A") to conduct a preliminary study of EcoPark. The consultant had spent almost one year to complete the study and submit the consultancy report in October 2002. Since the ENB informed the EPD in November 2002 that the operation of EcoPark should be self-financing, the EPD commissioned a financial consultant ("Consultant B") in March 2003 to further examine the financial arrangement and explore different contract options. In November 2003, Consultant B said that the EcoPark project would not be financially viable without the Government's financial support. In October 2004, in view of the lukewarm response from potential contractors, the ENB decided that the basic infrastructure at EcoPark should

¹ In 2001, the Environment and Food Bureau was responsible for the policy on environmental matters. In July 2002, the Environment, Transport and Works Bureau was formed to take up the environment portfolio from the Environment and Food Bureau. In July 2007, the ENB was formed to take up the policy on environmental matters. For simplicity, all the previous policy bureaux which had been responsible for the policy on environmental matters are referred to as the ENB in this Report.

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be provided under a public works project. In September 2005, the Government decided that a conventional management contract should be adopted and the management of EcoPark would be funded by the Government. In 2006, the EcoPark project was upgraded to Category A.

4. Against the above background, the Committee asked:

- whether the serious slippage between 2001 and 2005 before settling on a viable financial arrangement and contract option was due to a lack of commitment on the part of the ENB and the EPD as they considered the project infeasible or whether the delays were caused by negligence; and
- why it had taken the EPD almost three years to decide on the option of the management contract, although the ENB had already decided in November 2002 that the EcoPark project should be self-financing.

5. In response, **Mr Edward YAU Tang-wah, Secretary for the Environment**, and **Ms Anissa WONG Sean-ye, Director of Environmental Protection**, explained that:

- the EcoPark project was a completely new and innovative idea with the objective of supporting and further developing the local waste recycling industries by providing long-term land at an affordable price to promote more higher value-added waste processing operations in Hong Kong, instead of the commonly employed mode of bale-and-export process. As such, the Government could only feel their way forward cautiously based on its experience. Gradual adjustments were made to the project in the light of changes in market responses and economic situation, as well as the difficulties encountered during the process;
- the project had undergone important and substantial changes in its mode of development and operation between 2001 and 2005. The policy intent at the early planning stage of the project was to achieve a self-financing mode of operation as far as practicable. In 2002 and 2003, the EPD conducted two consultancy studies respectively to identify the types of recycling industries that were in line with the government policy on waste management and study the preliminary design of the project, and to examine the associated financial arrangement, including the response from potential investors and the commercial viability of the project in consultation with recycling traders. The general view was that the self-financing mode was infeasible and might not be able to achieve the policy objectives of encouraging the development of value-added environmental and recycling technologies that could help minimise waste generation. As such, the Government had decided to implement and manage EcoPark as a public project;

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- the EPD then needed to explore the arrangement for the management contract. It was considered that if EcoPark was to be operated strictly on commercial principles, the input of public funding might not be appropriate without policy support from the Government. On the other hand, the private investors expected the Government to provide financial support for the EcoPark's operation. Finally, it was decided that the management of EcoPark would be funded by the Government; and
- with hindsight, although it was not the Government's intention to make substantial changes during the planning and development of EcoPark, those changes were essential in order that the project could become feasible, but the cost was the loss of time.

6. The Committee queried:

- why the Administration had not explored the financial arrangement on recurrent expenditure and the contract arrangement concurrently so as to save time; and
- why the EPD had not consulted the Legislative Council ("LegCo") when it anticipated that the target date of the commissioning of the project could not be met, but only gave an explanation for the delays after the matter was raised by Audit.

7. The **Secretary for the Environment** and the **Director of Environmental Protection** responded that:

- in developing a project, some steps needed to be carried out first. The first step was to sort out the mode of development so as to estimate the resources required. Before that, it would be difficult to decide on the financial arrangement. Moreover, when there was a fundamental and substantial change in the mode of development, it would be difficult to proceed with other steps as originally planned; and
- the progress of the development of EcoPark had been reported to the relevant LegCo Panel and those who cared about the project. In 2005, the EPD had provided detailed analysis to the Panel on Environmental Affairs of the LegCo ("EA Panel") on the way forward after completion of the two consultancy studies.

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8. To ascertain the main cause of the delays between 2001 to 2005, the Committee asked whether, before announcing the EcoPark project in 2001, the Government:

- had conducted any feasibility study on the project, including the feasibility of the self-financing mode of operation;
- had conducted any research on overseas recycling technologies; and
- had consulted local expertise to understand the operation of the local recycling industries and the limitations of waste disposal in Hong Kong.

9. The **Secretary for the Environment**, the **Director of Environmental Protection** and the **Deputy Director of Environmental Protection** responded that:

- the Government had been conducting studies and planning on the management of municipal solid waste as a whole since the late-1990s. The introduction of the Waste Reduction Framework Plan in 1998 by the Government had a direct impact on EcoPark. The Framework Plan provided details of the measures which the Government would introduce for waste disposal, and the development of EcoPark was one of the measures announced by the Government in 2001; and
- apart from the local recycling trades, views of environmentalists and environmental organisations had also been sought. The introduction of EcoPark was to address their need for land.

10. The Committee further asked whether the change from the self-financing mode to funding the management of EcoPark by the Government was still considered viable at present.

11. The **Secretary for the Environment** and the **Director of Environmental Protection** replied that the consultant had identified in March 2003 four options of involving private-sector participation with a view to achieving self-financing. In view of the lukewarm response from potential contractors, the Government had decided to implement and manage EcoPark as a public project under which the Government provided land and essential infrastructure facilities in EcoPark for the recycling traders to operate their business. The management of EcoPark would also be funded by the Government. The current mode of operation and management would be more suitable for EcoPark nowadays.

Consideration of landfill cost in project evaluation

12. According to paragraphs 2.2(a) and 2.21 of the Audit Report, the annual recurrent cost of EcoPark was estimated to be \$10.6 million and the estimated saving on landfill disposal cost brought about by the recycling of waste in EcoPark was \$7.3 million a year. However, information about the landfill cost saving was not provided in the Public Works Subcommittee ("PWSC") paper of February 2006 on the EcoPark project. It appeared to the Committee that if the saving on landfill disposal cost was taken into account, the annual recurrent cost of the project could de facto be reduced to \$3.3 million, which would affect the assessment on the feasibility of the project as well as its financial and contract arrangements. The Committee asked:

- how the recurrent cost was determined;
- why the EPD had not provided the cost savings in the PWSC paper; and
- whether the EPD had provided information on such saving to the Financial Services and the Treasury Bureau ("FSTB") for consideration during the planning process of the project and the discussions on the associated financial arrangement and, if it had, whether the FSTB had:
 - (a) taken into account such saving during the process of financial evaluation, and
 - (b) requested the EPD to include the information in the PWSC paper.

13. **Prof K C CHAN, Secretary for Financial Services and the Treasury**, said at the public hearing and in his letter of 27 May 2010 (in *Appendix 8*) that:

- the capital cost and the annual recurrent cost were reported in the consultancy report in October 2002. The FSTB supported the original policy intent of achieving a self-financing mode of operation and involving the private sector in the development and operation of EcoPark. Subsequent to the change of the financial arrangement, the EPD absorbed the recurrent cost of EcoPark;
- in seeking to upgrade the EcoPark project to Category B, the ENB set out in its submission a number of reasons and data justifying the project. These included the point that there could be savings in the disposal cost of the materials that would be recycled/recovered instead of being dumped in the landfills. The FSTB believed that the information had been given due consideration, but the FSTB had no records as to what weight had been given to the point about savings in landfill disposal costs in the decision;

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- the FSTB had no records showing that the FSTB staff concerned had asked the ENB to include the point about savings in landfill disposal costs in the submission to the PWSC in 2006. It would seem that for the FSTB staff involved at that time, their analysis of the proposal and its justifications was such that savings in landfill disposal costs were not pertinent to the financial justification of the proposal;
- as could be seen from the "JUSTIFICATION" section of the PWSC paper, the justifications were mainly to provide an "outlet for locally recovered materials", "alleviate the heavy reliance on the export of these recyclable materials", "encourage the development of value-added environmental and recycling technologies", etc. Direct reduction in materials dumped in the landfills and savings arising from such reduction was not among the justifications;
- it was relevant to note that the materials in question could be exported instead of being sent to the landfills; and
- as for future PWSC/Finance Committee ("FC") submissions, the FSTB would as recommended by the Director of Audit continue to provide information on cost, benefits and cost savings arising from works projects in the PWSC/FC papers where appropriate.

14. The **Secretary for the Environment** said at the public hearing and the **Director of Environmental Protection** stated in her letter of 25 May 2010 (in *Appendix 9*) that:

- the Government had analysed the feasibility of adopting the self-financing mode through discussions with recycling traders. It was given to understand that the self-financing mode might only be feasible with positive economic outlook. As it transpired, the Government changed the self-financing mode to absorbing the recurrent cost of EcoPark by the EPD;
- the economic cost should be listed out and taken into consideration during the discussion of the policy behind public works projects, though it might not be totally relevant to funding application. The saving on landfill cost should have been taken into account during the planning process of the project and the discussions on the associated financial arrangement; and
- when assessing the economic effectiveness of EcoPark, the ENB and the EPD could not generalise a conclusion by simply equating the total quantity of recyclable waste materials processed at EcoPark to the total quantity of waste that would otherwise have been landfilled and then deducing from it the cost of landfilling so avoided because the saving on landfill disposal cost of the EcoPark project might only indicate notional savings. The main reason was that prior to the EcoPark project, some of the recyclable waste materials

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targeted for processing in EcoPark were already exported for recycling, albeit without going through any value-added processes, instead of being disposed of at landfills.

15. The Committee understood that Hong Kong was experiencing economic downturn in 2001 when the Government announced the EcoPark project. Apart from environmental protection considerations, the project was introduced to boost the economy of Hong Kong. Paragraph 1.6 of the Audit Report also mentioned the three objectives of the development of EcoPark. They were:

- to provide land for processing of recovered materials at affordable rents with a target throughput of 58,600 tonnes per year;
- to provide basic infrastructure (including a marine frontage) and environmental control facilities to reduce tenants' operating cost; and
- to create job opportunities for recycling and related industries.

The Committee asked whether the above objectives had been achieved.

16. The **Secretary for the Environment** said at the public hearing and the **Director of Environmental Protection** stated in her letter of 4 June 2010 (in *Appendix 10*) that:

- the three objectives were generally achieved and some of the results had exceeded the target;
- the average rental cost offered at EcoPark was as low as \$1/feet. The throughput had exceeded the target with a wider scope of recycling materials to be processed;
- the basic infrastructure and environmental control facilities provided at EcoPark were better than that in other industrial estates. For example, the area for loading and unloading activities at EcoPark was located along the coast, which could hardly be provided by other industrial estates and those which offered short-term leases. The Visitor Centre and the Product Gallery could also attract buyers of recycled products. Furthermore, the Government had also assisted tenants in building recycling plants and designing the flow of production; and
- as at April 2010, there were about 120 permanent staff employed by the EcoPark Operator and the tenants who had already started operations. It was anticipated that the target of creating 750 permanent jobs could be achieved upon full commissioning of both Phase 1 and Phase 2 of EcoPark.

C. Administration of management contract

Management contract for EcoPark

17. As mentioned in paragraph 5.2 of the Audit Report, the EPD awarded a seven-year contract, commencing in May 2007, to the Operator to provide management and maintenance services. Paragraphs 5.6 to 5.8 further revealed that the scheduled payments for operation fees were planned to increase with the commissioning of different phases of site handover and the number of lots ready for occupation. Because of the adoption of a front-loaded pricing strategy by the Operator, the operation fees with the commissioning of both Phase 1 and Phase 2 were \$14 million a year, which was only \$0.9 million higher than that for Phase 1 alone in operation. The operation fees for Phase 1 seemed to be disproportionately high. Notwithstanding the fact that Phase 1 had not yet commenced operation and the services required of the Operator had been substantially lower than scheduled, up to December 2009, the EPD had paid the Operator operation fees of \$32 million.

18. In the above circumstances, the Committee asked:

- whether it had occurred to the EPD that the project might be subject to further delays before awarding the management contract, having regard to the experience gained from the planning of EcoPark between 2001 and 2005;
- whether the EPD had negotiated any adjustments to the front-loaded pricing strategy submitted by the Operator in its tender before awarding the management contract; and
- whether the contract had prescribed the level of services required of the Operator in each year of the contract and if it had, given that the level of activity on site so far had been lower than expected, whether the contract allowed the EPD to re-schedule the services for the earlier years to the latter years of the contract.

19. In response, the **Assistant Director of Environmental Protection** said at the public hearing and the **Director of Environmental Protection** stated in her letter of 4 June 2010 that:

- the management contract prescribed the services to be provided by the Operator during the contract period and the payment to be made to the Operator in phases in accordance with the portions of the site of EcoPark which would be handed over to the Operator (as set out in Table 6 and Table 7 of the Audit Report). The services required were in response to the operational circumstances at EcoPark. The tenderers submitted their

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quotations for each item of service as required under the tender document. The EPD followed the standing regulations to assess the tenders;

- the EPD had negotiated with the Operator on a proposal for reducing the monthly operation fees in the light of the actual level of activities in mid-2008. The EPD's proposal was not accepted by the Operator for the reason that management duties were still required to maintain the site. In this case, the EPD had to comply with the terms of the management contract;
- the management and maintenance services, such as security, cleaning, repairing and landscaping, were required immediately after site formation. With the commencement of recycling operations in some of the Phase 1 lots and the two waste processing centres in Phase 2 as well as the opening of the Visitor Centre, the Operator had been required to deploy higher level of resources for delivery of the necessary services in accordance with the terms of the management contract; and
- apart from managing the common parts of EcoPark, the Operator was required to provide marketing services including promotion of EcoPark to local stakeholders, developing a dedicated website for EcoPark, and preparing promotional flyers and leaflets, and to provide assistance to tenants in identifying sources of recyclable materials and in submission of building plans. In January 2010, the Operator also assisted in organising a recruitment exercise for hiring manpower for one of the tenants and itself.

20. The Committee further enquired the reason why the contract period was set at seven years and whether such a relatively long contract period was common for other government service contracts.

21. The **Director of Environmental Protection** replied in the same letter that:

- the management contract was a multi-disciplinary services contract on facility management, infrastructure maintenance, tenant support, tenancy management and marketing. A seven-year contract period was adopted to attract sufficient commercial interest in pulling together the necessary multi-disciplinary forces to provide the integrated services, and at the same time allowing the operator of the second contract to gain sufficient experience before dealing with the renewal or re-tendering of the tenancy lots in the tenth year; and
- contract periods in the public sector were determined according to the service requirements and relevant operational considerations. There were contracts on facility management, for example, those on tunnel management, that covered periods longer than three years.

Monitoring of the Operator's performance

22. Noting that the Operator was required to manage the site according to the service performance requirements under the management contract, the Committee asked how the EPD monitored the performance of the Operator to ensure that the Operator had fulfilled the requirements in the management contract, before paying the operation fees to the Operator.

23. The **Director of Environmental Protection** said that the EPD monitored the Operator's performance by holding regular meetings with the Operator, conducting at least two surprise checks on the Operator's performance monthly, and requiring the Operator to submit a monthly report on the work it planned to do.

24. According to the information note provided by the ENB and the EPD, the EcoPark Visitor Centre at Phase 1 had begun to receive visitors since mid-March 2010 and had so far received more than 50 group visits with over 1,500 visitors. However, the Committee noted from paragraph 5.14(a) of the Audit Report that the Administration Building of the Centre had been completed as early as November 2007. The Committee asked why the Visitor Centre had not been put into use for a long period of time.

25. The **Assistant Director of Environmental Protection** responded that in view of the delay in the Phase 1 development, the EPD had adjusted the commissioning of the Visitor Centre to tie in with the estimated time of commencement of the tenants' operation, since the message to be delivered by the Visitor Centre was related to the recycling activities in EcoPark.

D. Phase 1 development

Land allocation of Phase 1 of EcoPark

26. As reflected in Table 1 and Table 2 of paragraph 3.6 of the Audit Report, there were delays in the land allocation of Phase 1 of EcoPark. As at December 2009, the EPD had entered into tenancy agreements for all the six Phase 1 lots with the recycling traders. However, none of the recycling traders had commenced operation and produced any throughput. The Committee questioned:

- whether the ENB and the EPD had accorded sufficient attention to monitoring the progress of the recycling traders in commencing operation;
- the reasons the recycling traders had not promptly commenced their operation; and

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- whether there were any tenants who occupied the land only to prevent their competitors from operating in EcoPark but had no intention to develop any environmental and recycling trades; if there were, what measures would be taken by the EPD to tackle this problem.

27. The **Secretary for the Environment** and the **Director of Environmental Protection** replied that:

- it would be difficult to judge whether a tenant had no intention to develop any environmental and recycling trades after being awarded a tenancy. There were many traders in the recycling industry who adopted the traditional simple mode of collecting waste materials for export. Such traders might encounter difficulties when they were required to build recycling plants for higher value-added waste processing operations. A much longer lead time and larger initial capital investment were required for setting up a recycling plant in EcoPark than a plant for the simple bale-and-export process. Besides, the recycling traders also faced other difficulties, leading to late commencement of operation. These difficulties were:
 - (a) the specified waste types to be processed for individual lots might not be viable due to fluctuating market conditions;
 - (b) the majority of tenants were small-to-medium-sized recycling companies which were inexperienced in handling planning and approval seeking processes in connection with designing and building their waste processing facilities. As such, a longer lead time was required to commence operation as they needed to re-submit the plans for approval by the relevant authorities. Even if the plans were approved, the tenants also needed to spend time on following up logistics such as application for electricity supply, etc;
 - (c) the small-to-medium-sized recycling companies might have difficulties in making substantial investments in hiring professional services and in funding the capital costs during the difficult market situation prevailing in the past few years; and
 - (d) tenants might have problems relating to cash flow, market volatility and unstable price of waste materials due to economic downturn, etc; and
- the EPD would try to assist tenants in tackling the problems. At the same time, it would take appropriate contract enforcement measures which included termination of tenancy, if there was any serious and significant breach of tenancy conditions.

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28. Given the difficulties encountered by some small-to-medium-sized companies, the Committee enquired whether the EPD would consider setting up an inter-departmental group with relevant authorities to assist tenants in submitting applications to meet statutory requirements or adopting other modes of operation.

29. The **Secretary for the Environment** responded that:

- the EPD had maintained close communication with relevant authorities, such as the Buildings Department and the Fire Services Department, to assist tenants in submitting applications to meet statutory requirements;
- other measures had been taken to address the difficulties encountered by some tenants in the Phase 1 development, including exercising flexibility when the tenants experienced cash flow problems, and on the types of materials to be processed and the requirement of building recycling plants; and
- the EPD was still exploring other modes of operation, such as the feasibility of partnership arrangements with relevant organisations, according to the experience gained during the development process of the project.

30. The Committee further enquired:

- the reasons why re-tendering was needed for three of the six lots in Phase 1 of EcoPark;
- whether a pre-qualification exercise had been conducted to ensure that the successful tenderer would be capable of operating the business; and
- whether the EcoPark Advisory Committee ("EAC") set up in December 2006 had provided advice on the development and operation of EcoPark.

31. The **Assistant Director of Environmental Protection** replied that:

- the three lots had to be re-tendered due to the following reasons:
 - (a) tenancy terminated due to default in rent payments;
 - (b) tenancy terminated due to failure to submit performance bond; and
 - (c) successful tenderer repudiated the tenancy after the award of tenancy as it did not understand that there was no subsidy from the Government;

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- no pre-qualification exercise had been conducted before tendering. However, the EPD had conducted an expression-of-interest exercise to obtain information about the recycling traders' preference before tendering; and
- the EAC performed a consultancy role in the EcoPark project. It provided advice on the types of recycling industries to be invited for tendering. Views from the potential tenants on the letting of lots were also discussed at the EAC meetings.

32. At the request of the Committee, the **Director of Environmental Protection** provided in her letter of 25 May 2010 the terms of reference and membership of the EAC, as well as the discussion items of the EAC meetings since its establishment.

33. The Committee noted that only four EAC meetings were held from December 2006 to May 2010, with an interval as long as 19 months between the second meeting in May 2007 and the third meeting in December 2008.

Change in throughput of recycling materials

34. According to paragraphs 3.20 and 3.21 of the Audit Report, Consultant A estimated that EcoPark could process 648,780 tonnes of recycling materials. However, according to the PWSC paper of February 2006, the annual throughput was substantially reduced to 58,600 tonnes. The Committee enquired why there had been such a significant reduction of throughput, especially on the throughput of metals between the estimates by the Consultant A and the minimum quantity required under tenancy agreement.

35. The **Director of Environmental Protection** and the **Assistant Director of Environmental Protection** responded that:

- the throughput estimates provided in the consultancy study included waste metals and waste paper. These materials, however, were excluded when the PWSC paper was prepared in consideration of the waste management policy as a whole; and
- although waste metals were excluded from the PWSC paper estimate, they were eventually included in the Phase 1 development in the light of market changes. Apart from collecting waste metals, the tenant planned to build a steel furnace to reproduce the metals. This would contribute to an annual throughput of 160,000 tonnes.

36. The **Secretary for the Environment** supplemented that:

- as waste paper made up a considerable amount of throughput (i.e. 136,000 tonnes), the exclusion of it had a great impact on the total amount. Another trade, tyres, was originally included in the PWSC paper but was eventually excluded from the Phase 1 development as it was considered that exporting this kind of materials for recycling in other countries would be more viable; and
- while the actual throughput had exceeded the target set out in the PWSC paper, the annual throughput might not be able to reflect the real situation of EcoPark. The ENB's concern was whether the types of recycling industries could tie in with the government policy on waste management. For example, used cooking oil was selected as one of the recycling materials to be processed at EcoPark as it was in line with the legislation regarding biodiesel, even though the throughput of used cooking oil was not very large. Another example was the electronics/electrical appliances trade which was at present operated by non-governmental organisations ("NGOs"). If the collection of these appliances had become satisfactory, it would pave the way for the future Producer Responsibility Scheme for waste electrical and electronic equipment ("WEEE").

37. The Committee referred to Audit's comments in paragraph 3.22 of the Audit Report that in view of the market changes since 2006, the EPD needed to update the target materials throughput of EcoPark. The Committee asked:

- whether the change in recycling materials to be processed had been reported to the EA Panel; and
- about the measures that the EPD would take in response to Audit's recommendation.

38. The **Secretary for the Environment** and the **Director of Environmental Protection** said that the EPD reported to the EA Panel the progress of the development of the EcoPark project, including the types of recycling materials to be processed, at least once a year. The EPD would also update the target materials throughput of EcoPark in the next regular report to the EA Panel.

Consolidation of experience gained from the Phase 1 development

39. According to paragraph 3.29(g) and (h) of the Audit Report, in the light of the experience of the Phase 1 development and the views from stakeholders, the EPD would continue to explore appropriate measures and arrangements to ensure the early setting up of waste recycling operations at EcoPark following the award of tenancies, and the EPD would work with relevant parties to review the tenancy arrangements for Phase 2. The Committee asked:

- how the land allocation in Phase 2 would be arranged; and
- when the EPD would report the experience gained from Phase 1 to the EA Panel.

40. The **Secretary for the Environment** and the **Assistant Director of Environmental Protection** replied that having regard to the experience gained from the Phase 1 development, the ENB and the EPD would consider taking the following measures in the Phase 2 development:

- to exercise flexibility in determining the size and operation of the lots to be leased out in light of the market situation and the government policy on waste management;
- to set up some government-funded waste recycling centres to be operated by NGOs in order to tie in with the government policy on waste management;
- to invite traders to bid for lots for a wider scope of land uses, including conducting researches for waste-management technologies;
- to provide basic plant infrastructure and facilities, e.g. working sheds and fire services facilities, to tenants; and
- to provide flexibility in the tenancy agreements, including a longer tenancy period, such as 20 years, as reflected by some tenants.

41. The **Director of Environmental Protection** said that the EPD was studying the feedback from the Phase 1 tenants with the FSTB with a view to encouraging investment in more advanced technologies and value-added processes. The EPD would report the progress of the review to the EA Panel in the coming months once recommendations were generated.

E. Phase 2 development

Waste processing centres operated by NGOs in Zone A

42. In February 2009, in response to the demand for short-term use of land by logistics trades in Tuen Mun and the slowing down of the recycling industries due to the economic downturn, the EPD divided Phase 2 of EcoPark into three zones, namely Zones A to C, for different uses. Zone A was allocated for government-funded projects. The EPD planned to set up some waste recycling centres at the lots to be operated by NGOs. Zone B was allocated for recycling-related environmental industries. Zone C was used by other government departments on a temporary basis for storage of empty containers. According to paragraph 4.6 of the Audit Report, the plastic waste processing centre and the WEEE processing centre would be commissioned in the first and second quarters of 2010 respectively. Paragraph 4.10 of the Audit Report stated that Phase 2 should have been available for leasing by the end of 2009, but infrastructure works for Phase 2 were still in progress as at February 2010. The Committee asked:

- whether the two waste processing centres could be commissioned on time; and
- about the actions that would be taken by the ENB and the EPD to expedite the Phase 2 development of EcoPark.

43. The **Secretary for the Environment** said at the public hearing, and the Committee noted from the information note provided by the ENB and the EPD that:

- the plastic waste processing centre located in Zone A had already commenced operation;
- the views from potential tenants were being taken into account in the review of the tenancy arrangements for Phase 2. The site formation and road works for Phase 2 had been substantially completed and the lots would be available for leasing by the end of 2010. In the light of the lessons learnt from Phase 1 as well as the feedback from project stakeholders from time to time, the EPD was reviewing the lot allocation arrangement in consultation with the FSTB. While the ENB and the EPD would continue to uphold the principle of open, competitive and fair process in the selection of tenants, they were prepared to make appropriate necessary adjustments to:
 - (a) increase the attractiveness of EcoPark to the recycling industry; and

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- (b) facilitate early commencement of recycling operation on site so that the objectives of setting up EcoPark to provide long-term land at affordable costs for the development of the recycling and environmental industry with a view to encouraging investment in more advanced technologies and value-added processes were fulfilled; and
- the EPD would take into account the views from Audit, the Public Accounts Committee and the FSTB in developing a set of revised lot allocation arrangement for the Phase 2 lots. Subject to follow-up consultation with relevant stakeholders and the EA Panel, the ENB and the EPD aimed to commence the tendering process by the end of 2010.

Temporary land allocation for open storage of empty containers in Zone C

44. The Committee noted Audit's recommendation in paragraph 4.23(c) of the Audit Report that the EPD should liaise with the Secretary for Development and the Director of Lands regarding the time-frame for handing back the Phase 2 lot temporarily allocated for container storage. The Committee asked what progress had been made.

45. The **Secretary for the Environment** replied that:

- Zone C was used by other government departments on a temporary basis for storage of empty containers;
- the financial downturn in late 2008 resulted in a significant drop in import/export trade and a massive return of empty containers to Hong Kong. There was an acute shortage of temporary sites for open storage of empty containers. In response to the request of the Development Bureau and in consideration that the EPD was still resolving the problems encountered in the Phase 1 development, the EPD agreed to set aside some areas under Phase 2 of EcoPark for the storage of empty containers; and
- so far, the ENB and the EPD had not received any request for extension of the usage of the land. Since the Phase 2 tenancy arrangement should be decided as soon as possible and the import/export trade had gradually recovered, the EPD would take back the land for letting upon expiry of the one-year short-term tenancy in October 2010.

Funding arrangements of waste processing centres

46. According to paragraphs 4.18 to 4.22 of the Audit Report, although the infrastructure works of the plastic waste processing centre and the WEEE processing centre under a pilot scheme in Phase 2 of EcoPark were general and common in nature and within the scope of the EcoPark project, the EPD had adopted different funding arrangements for the capital cost of the two centres, with the former being charged to the EcoPark project vote under the Capital Works Reserve Fund ("CWRF") and the latter to a separate item under the CWRF block allocation. The Committee also noted that under Financial Circular No. 8/2001 of August 2001 on Delegated Authorities of CWRF block allocations, which was currently in force, government departments should not use block allocations to cover increased expenditure on a project or part of a project that was already funded under the CWRF. Also, block allocations must not be used to hide cost overruns on projects. The Committee asked why the EPD had adopted different funding arrangements.

47. The **Secretary for the Environment** and the **Director of Environmental Protection** explained that:

- different financial arrangements had been adopted to reflect the different purposes and background of the two projects;
- the plastic waste processing centre was developed as a short-term measure to address the poor market situation of plastic waste since the financial tsunami in 2008. Upon the revival of the plastic waste recycling market, the processing centre's infrastructure works and ancillary facilities could be released for other short-term waste recycling operations. The Administration hoped that the involvement of NGOs in the development of the processing centre would continue to foster the work of source separation of municipal solid waste;
- given the success of the Kowloon Bay WEEE processing centre and the physical constraints there for capacity expansion, the WEEE processing centre at EcoPark was developed to provide additional space to process WEEE collected by NGOs. Since the WEEE processing centre was an extension of the Kowloon Bay WEEE processing centre which was funded under a separate item of the block allocation in 2005, the ENB and the EPD considered that the same source of funding should be used; and
- the financial arrangements were in compliance with the government guidelines and the EPD had no intention to hide any cost overruns. In fact, as at March 2010, the unspent balance of \$21.67 million under the EcoPark project vote was sufficient to cover the capital costs of the WEEE processing centre at \$19 million.

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48. The Committee further enquired whether the FSTB considered that it would be more appropriate for the EPD to charge the EcoPark WEEE processing centre capital cost to the EcoPark project vote than the block allocation.

49. **Ms Alice LAU, Deputy Secretary for Financial Services and the Treasury (Treasury)**, said at the public hearing and the **Secretary for Financial Services and the Treasury** stated in his letter of 27 May 2010 that:

- in March 2010, the EPD consulted the FSTB about whether the funding arrangement for the WEEE processing centre at EcoPark was in order. The FSTB noted the rationale of the ENB and the EPD in adopting different financial arrangements. The FSTB had also reviewed the funding arrangement with reference to the Financial Circular No. 8/2001 on Delegated Authorities of CWRF block allocations;
- the capital cost of a works project was chargeable to a subhead (be it a project vote created under Public Works Programme or a block allocation) if it fell within the ambit of the subhead concerned. In the present case, the EcoPark WEEE processing centre fell within the scope of both the EcoPark project vote and the relevant block allocation; and
- based on the information the ENB provided to the FSTB earlier in 2010, the FSTB did not find it improper for the ENB to use the block allocation to cover the expenditure of the EcoPark WEEE processing centre as it was not the increased expenditure of the EcoPark project. The FSTB therefore considered that both funding routes were appropriate.

F. Conclusions and recommendations

50. The Committee:

- expresses serious concern and finds it unacceptable that:
 - (a) the Environment Bureau ("ENB") and the Environmental Protection Department ("EPD") had failed to exercise due diligence and had demonstrated a lack of commitment in handling the EcoPark project, as evidenced by the spate of problems from its inception to the Phase 1 development, causing the project not only to stall between 2001 and 2005 before finally settling on a viable financial arrangement and contract option after serious slippage, but also to progress slowly in awarding tenancies after its commissioning due to the failure to critically assess market demand before tendering and that despite the problems, the EcoPark Advisory Committee ("EAC") was only set up as late as December 2006;

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- (b) progress in the development of EcoPark has become notable only after the completion of Audit Commission ("Audit") review at the end of February 2010, which further demonstrates that the ENB and the EPD had not accorded sufficient attention to the EcoPark project before the Audit review; and
- (c) the ENB and the EPD had not found it necessary to consult the Legislative Council ("LegCo") on the proposed financial arrangement for EcoPark, i.e. implementing and managing EcoPark as a public project with the Government taking on all financial risks instead of a self-financing project;

Planning of EcoPark

- is surprised and expresses serious concern that:
 - (a) notwithstanding the fact that the ENB had decided in November 2002 that the EcoPark project should be self-financing, the financial arrangements on recurrent cost and the contract option to be adopted were only resolved in September 2005; and
 - (b) information about the landfill cost saving of \$7.3 million a year, brought about by the recycling of waste in EcoPark, was not provided in the Public Works Subcommittee ("PWSC") paper of February 2006 on the EcoPark project;
- does not agree with the Secretary for Financial Services and the Treasury and the Director of Environmental Protection that the landfill cost saving is only notional and not pertinent to the financial justification of the project. If the saving had been taken into account, the estimated annual recurrent cost of EcoPark could de facto be significantly reduced from \$10.6 million to \$3.3 million, which might affect the financial and contract arrangements of the project;
- acknowledges that the Secretary for the Environment and the Director of Environmental Protection agree with the recommendations in paragraph 2.22 of the Director of Audit's Report ("Audit Report");
- urges the Secretary for the Environment, the Secretary for Financial Services and the Treasury and the Director of Environmental Protection, in evaluating the financial justification of a project in future, to take into account all the relevant costs and benefits, including de facto cost savings, and provide such information to the LegCo;

Administration of management contract

- expresses dissatisfaction and finds it unacceptable that the management contract for operating EcoPark had been designed in such a way that it failed to align the payment schedule with the occupancy of the lots at EcoPark. Although the EPD was well aware that the project was to be implemented in two phases, and its planning had already experienced delays between 2001 and 2005 with possible further slippage, it had not tried to negotiate any adjustments to the front-loaded pricing strategy submitted by the Operator in its tender before awarding the management contract in November 2006. Consequently, although Phase 1 had not yet commenced operation and the services required of the Operator had been substantially lower than scheduled, up to December 2009, the EPD had paid the Operator operation fees of \$32 million;
- expresses dismay that in administering the management contract, the Director of Environmental Protection had failed to exercise sufficient vigilance and prudence, in that:
 - (a) while the Operator was required under the management contract to ensure that a mix of industries was established and operated at EcoPark and to minimise the number of vacant lots, the EPD had not instructed the Operator to provide any marketing services for promoting EcoPark from November 2006 to November 2009; and
 - (b) the EPD had not compiled assessment reports on the Operator's performance;
- acknowledges that the Director of Environmental Protection agrees with the recommendations in paragraph 5.17 of the Audit Report;
- urges the Director of Environmental Protection to:
 - (a) in designing future management contracts of EcoPark and other projects, take into account the special circumstances of each project, including the possibility that the project may not be able to proceed on schedule; and
 - (b) implement expeditiously the above Audit recommendations;

Phase 1 development

- expresses serious concern and finds it unacceptable that:
 - (a) there was delay in the implementation of Phase 1 of EcoPark, which was planned to be commissioned by 2006 according to the 2005 Policy

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Address. Up to February 2010, Phase 1 had not yet commenced recycling operation;

- (b) the EPD did not have sufficient understanding of the actual demand, capabilities and profiles of the recycling trade and its operators in Hong Kong not only in the planning stage but also after EcoPark has been launched, as reflected by the following:
 - (i) re-tendering of tenancy for three of the six lots was required and the types of recycling materials for two lots had to be revised to meet the market demand;
 - (ii) of the six Phase 1 tenants, four had not complied with the tenancy requirements to commence recycling operations within 12 months from the date of site possession. The EPD had not provided timely support to tenants which were small-to-medium-sized companies to assist them in handling the planning and approval seeking processes in connection with the design and building of their waste processing facilities; and
 - (iii) there was significant variation between the original planned annual throughput of EcoPark in 2002 (i.e. 648,780 tonnes) and that as stated in the PWSC paper of 2006 (i.e. 58,600 tonnes) due to the exclusion of waste metals and waste paper from the recycling materials; and
 - (c) the Director of Environmental Protection only held four EAC meetings from December 2006 to May 2010, with an interval as long as 19 months between the second meeting in May 2007 and the third meeting in December 2008;
- notes that concerns had been expressed at a meeting of the Panel on Environmental Affairs of the LegCo ("EA Panel") held in June 2008 as to whether the modus operandi of EcoPark could attract tenants;
 - acknowledges that:
 - (a) the Director of Environmental Protection agrees with the recommendations in paragraph 3.28 of the Audit Report;
 - (b) the Secretary for Financial Services and the Treasury agrees with the recommendation in paragraph 3.28(f) of the Audit Report;
 - (c) the EPD has maintained close communication with relevant authorities to assist tenants in submitting applications to meet statutory requirements;

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- (d) four tenants (waste cooking oil, waste metals, waste wood and waste computer equipment) of Phase 1 of EcoPark have commenced their operations or will have done so by July 2010; and
 - (e) in the light of the Phase 1 development and the views from stakeholders, the EPD will continue to explore appropriate measures and arrangements to ensure the early setting up of waste recycling operations at EcoPark following the award of tenancies;
- urges the Director of Environmental Protection to:
- (a) seek advice from the EAC more frequently;
 - (b) critically review whether the modus operandi of EcoPark can attract tenants in consultation with experts in the field, the EA Panel and other stakeholders, and report the outcome to the EA Panel; and
 - (c) expeditiously follow up the above Audit recommendations and take specific measures to assist all tenants of Phase 1 of EcoPark to commence operation as soon as possible;

Phase 2 development

- expresses serious concern and finds it unacceptable that:
- (a) Phase 2 of EcoPark could not be made available for leasing by the end of 2009 as originally planned. As at February 2010, infrastructure works for Phase 2 were still in progress;
 - (b) by mid-2010, of the 12 hectares of land formed under Phase 2, only 5.2 hectares would be available for allocation to recycling traders; and
 - (c) although the EPD has indicated that it will draw on the experience gained from the Phase 1 development in reviewing the tenancy and lot allocation arrangements for Phase 2, the EPD has yet to formulate a concrete strategy to ensure that EcoPark will achieve its objectives of encouraging the development of value-added and higher-end environmental and recycling technologies and activities;
- acknowledges that:
- (a) the Director of Environmental Protection agrees with the recommendations in paragraph 4.23 of the Audit Report;
 - (b) the Secretary for Development agrees with the recommendations in paragraph 4.23(c) of the Audit Report; and

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- (c) the EPD is reviewing, in consultation with the Financial Services and the Treasury Bureau ("FSTB"), the lot allocation arrangement for Phase 2 as well as other supporting measures, with a view to increasing the attractiveness of EcoPark to the recycling industry and facilitating early commencement of recycling operations on site. It aims to commence the process for the allocation of the Phase 2 lots by late 2010;
- urges the Director of Environmental Protection to:
 - (a) formulate a concrete strategy to ensure that EcoPark will achieve its objectives of encouraging the development of value-added and higher-end environmental and recycling technologies and activities, and seek the views of the experts in the local recycling trade and other stakeholders in the process; and
 - (b) set measurable performance targets for Phase 2 of EcoPark with milestone dates for their achievement, and report progress to the EA Panel;

Funding arrangements of waste processing centres

- notes that under Financial Circular No. 8/2001 of August 2001 on Delegated Authorities of Capital Works Reserve Fund ("CWRF") block allocations, which is currently in force, government departments should not use block allocations to cover increased expenditure on a project or part of a project that is already funded under the CWRF. Also, block allocations must not be used to hide cost overruns on projects;
- expresses concern that:
 - (a) although the infrastructure works of the plastic waste processing centre and the waste electrical and electronic equipment ("WEEE") processing centre under a pilot scheme in Phase 2 of EcoPark were general and common in nature and within the scope of the EcoPark project, the EPD had adopted different funding arrangements for the capital cost of the two centres, with the former being charged to the EcoPark project vote under the CWRF and the latter to a separate item under the CWRF block allocation; and
 - (b) while it may not be the intention of the EPD to charge the WEEE processing centre capital cost to the CWRF block allocation for the purpose of covering increased expenditure or hiding cost overruns of the EcoPark project, the fact that it did not charge the cost of the works of the same project to the project vote will leave room for manipulation and under-reporting of the total project cost. This is undesirable from the financial control point of view;

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- urges the Secretary for Financial Services and the Treasury to review Financial Circular No. 8/2001 and consider issuing guidelines on the charging of the cost of the works of the same project to different votes, with a view to removing any room for manipulation and under-reporting of the total cost of a project; and

Follow-up actions

- wishes to be kept informed of:
 - (a) the actions taken by the Director of Environmental Protection to seek advice from the EAC more frequently;
 - (b) the EPD's decision on whether to review if the modus operandi of EcoPark can attract tenants, and any progress made;
 - (c) the specific measures taken by the EPD to assist all tenants of Phase 1 of EcoPark to commence operation as soon as possible;
 - (d) the progress made by the EPD in formulating a concrete strategy to ensure that EcoPark will achieve its objectives of encouraging the development of value-added and higher-end environmental and recycling technologies and activities;
 - (e) the progress made by the EPD in setting measurable performance targets for Phase 2 of EcoPark with milestone dates for their achievement;
 - (f) the FSTB's decision on whether to review Financial Circular No. 8/2001 and issuing guidelines on the charging of the cost of the works of the same project to different votes, with a view to removing any room for manipulation and under-reporting of the total cost of a project, and any progress made; and
 - (g) the progress made in implementing the various Audit recommendations.