

Legislative Council Panel on Transport Review on Ferry Services for Outlying Islands

Purpose

This paper informs Members of the progress of the review on the ferry services for outlying islands since the meeting of the Legislative Council Panel on Transport (the Panel) on 23 April 2010, and provides further information on the issues raised by Members at the meeting.

Background

2. In May 2008, the Government committed to conduct a review on the outlying island ferry services with a view to enhancing the long-term financial viability of these services and maintaining fare stability. The review covers 14 outlying island ferry routes which are regular passenger services licensed under the Ferry Services Ordinance (the routes and their patronage are at Annex A).

3. On 23 April 2010, we briefed the Panel on the progress of the review on the ferry services for outlying islands and the Administration's proposals. We explained that during the review, we had carefully examined and analyzed the chronic problems faced by the outlying island ferry services, which are essentially two-fold : lack of growth in demand and highly volatile fuel cost. On the demand side, patronage has been relatively small. The average daily patronage of the 14 outlying island routes is about 64,000, accounting for 0.6% of the total public transport ridership. The population projection of up to 2012 does not support much growth in demand. On the cost side, the major components are staff remuneration, maintenance cost and fuel cost. Whereas fuel cost constitutes a significant portion of the total operating expenditure, it is outside the operators' control and putting the business at high risk. These are the long-term structural problems faced by the outlying island ferry services. There is not much room for cost cutting and revenue generation or cost containment. At the same time, we recognize the increasing expectation and demand on these services of the community and the public. While fare increases could help sustain the financial viability of these services, such increases would need to be above general inflation and would be subject to residents' criticism.

4. Despite Government's continuous efforts to help ferry services by providing various measures to enable ferry operators to reduce operating cost and to allow them to sublet pier premises in order to increase non-fare box revenue, in view of the characteristics and the chronic problems of the ferry services and having

examined their financial situations, we consider that there is a need to step up the measures. We propose to share some of the burden of the commuters of the six major trunk routes¹ so that the rate of fare increase could be reduced by half (after netting of the rate of general inflation) by reimbursing to the operators the vessel maintenance cost that has been incurred. Therefore, when there is a need to increase the fare, passengers will bear the fare increase up to the rate of general inflation since the previous fare increase as well as half of the residual rate of the fare increase. The other half will be subsidized by the Government (details of the proposal are at Annex B).

5. We launched a series of consultations immediately after our briefing for the Panel on 23 April 2010. During April to June 2010, we held over 20 meetings to consult the Transport Advisory Committee, Traffic and Transport Committee of the Islands District Council as well as relevant Rural Committees, organizations and the trade etc on our proposals. We also held public forums on the outlying islands concerned to gauge the views of residents directly. In addition, the Transport Department (TD) has uploaded information of the review and proposals onto its website for the public to express their views.

6. During the consultations, most respondents supported the Government to help the major outlying island ferry services and generally welcomed the helping measures to be provided to the six major trunk routes. They considered that the proposal would help alleviate the operating difficulties of the ferry operators and the pressure on fare increase. Other views collected during the consultations include : the fares of some major trunk routes were already too high and should not be increased further; the holiday fare differential should be totally removed; the Government should extend the proposed helping measures to other ferry routes; and the Government should further consider other measures as the proposed ones could not solve the problem completely. Nonetheless, a small number of respondents considered that the Government should not provide financial assistance to the ferry services. Furthermore, some members of the public also commented on the quality and level of the ferry services for outlying islands. TD will consider such views in the next tendering exercise for relevant routes.

7. We understand the public's expectation on outlying island ferry services and that as ferry services are the only means of transport for some of these outlying islands, we have to ensure that such essential services for the residents could be maintained. Therefore, we have to provide special measures. In view of the uniqueness of ferry services, not only do we have to ensure that these essential

¹ The six major trunk routes are: Central - Cheung Chau route; Inter-Islands route serving Peng Chau, Mui Wo, Chi Ma Wan and Cheung Chau; Central - Mui Wo route; Central - Peng Chau route; Central - Yung Shue Wan route; and Central - Sok Kwu Wan route.

services could be provided to the residents, we also have to ensure that the fare could be maintained at a stable level. However, we need to consider the existing policy and strike a balance when formulating proposals. Our basic premise is to follow as far as possible the existing policy of allowing the private sector to operate public transport services on commercial principles. At the same time, we have borne in mind the need for prudent use of public funds. We have also struck a balance between the need to support essential services which otherwise would not be financially viable and the need to let those individuals shoulder the appropriate responsibility for choosing to live on the outlying islands. Therefore, we propose to provide further support to the six major trunk routes when such a need arises in order to share some of the burden of the commuters when there is a fare increase.

Other relevant information

8. At the Panel meeting on 23 April 2010, Members generally welcomed the Government's support for outlying island ferry services. However, they also reminded the Government that the maintenance cost of ferry operation should be carefully monitored in order to prevent abuse of government subsidy. In view of Members' request, we will provide safeguards to prevent abuse when applying for relevant funding. Members asked the Government to list out the financial implications of the existing helping measures. The relevant information is at Annex C. Members also requested the Administration to provide further information on other options explored but found not acceptable. In the course of the review, we have explored the following options which we found to be not feasible :

(a) Reducing cost through route and service rationalization

We have examined whether some of the routing could be combined or if a hopper service could be provided so that patronage could be strengthened by channeling passengers to a couple of main routes. The geographical location of the islands, however, makes such options infeasible. It would either require the use of extra vessels or would result in longer journey time. The present routing has evolved over many years and passengers may not prefer major changes which would affect their traveling patterns, particularly journey time.

We have also looked into the possibility for service rationalization for those sailings with patronage less than 35%. While there are sailings at off-peak hours in the morning, mid-afternoon and late evening which contain room for frequency reduction, the only savings that could be achieved are the fuel cost from reduced sailings. Such savings account for only about 1% to 3% of the total operating cost of the relevant routes, and cannot therefore improve the long-term financial viability of the ferry services.

- (b) Replacing ferry service licence with franchise to extend the licensing period

There have been suggestions that as franchises have a longer tenure, franchisees could find more lucrative tenants thus generating more rental from subletting pier premises. We have examined the financial situations of ferry operators, including non-fare box revenue currently generated from subletting pier premises. While we have been providing helping measures to increase non-fare box revenue of the ferry operators, non-fare box revenue still only comprises a small percentage of the total revenue. As such, the long-term financial viability of the ferry services could not be improved by a longer tenure of franchises and the higher non-fare box revenue so generated.

- (c) Government to purchase vessels for operators

We have looked into the option of the Government providing hardware. The option involves huge capital expenditure. If the Government is to purchase new vessels, this involves purchasing vessels for the six major trunk routes at a capital cost of almost \$1.7B, based on the information provided by vessel builders in the market. On the one hand, this option involves huge capital expenditure. On the other hand, the option could not reduce pressure on fare increases because it would not help enhance revenue or reduce operating cost except for depreciation. Moreover, the Government will also need to take up the management and maintenance fees for the vessels which involve a huge expenditure. Therefore, we consider this option not feasible.

- (d) Contracting out

In the course of the review and formulation of the proposals, our basic premise is to follow as far as possible the existing policy of allowing the private sector to operate public transport services on commercial principles as this is the best way to provide efficient public transport services. If the ferry services are to be taken over by the Government and re-provisioned as Government contracted-out services, it would be against our policy that public transport services should be run by the private sector or public corporations in accordance with commercial principles and would have wide read-across implications. In addition, the option means that operators will have little incentive to provide effective and efficient service. Moreover, the financial implications for the Government under this option could be infinite.

(e) Fuel-related mechanisms

We have also considered various fuel-related mechanisms including fuel surcharge or fuel subsidy. As it is difficult to predict the fluctuation in oil price, we do not wish to see a complete and direct shift of the fluctuation onto the public. A fuel subsidy would violate the principles of free market economy and have wide read-across implications.

Conclusion

9. Among the five options above, options (a) to (c) could not help the operators to improve the long-term financial viability of the ferry services. Moreover, option (c) would require huge capital expenditure. As regards options (d) and (e), these two options would violate the Government's policy and have wide read-across implications. As such, all the above options are considered infeasible. Given the characteristics and chronic problems of the ferry services, there is a need to step up the helping measures. At the same time, we have to strike a balance between the need to support essential services which otherwise would not be financially viable and the need to let those individuals shoulder the appropriate responsibility for choosing to live on the outlying islands. We therefore suggest implementing the proposed measures detailed at Annex B.

10. We will seek funding approval from the Legislative Council Finance Committee before the next tendering exercise begins for implementing the proposals.

Transport and Housing Bureau (Transport)
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Annex A

Patronage of the 14 outlying island ferry routes in 2009

Outlying island ferry routes	Average daily patronage in 2009
1. Central - Cheung Chau	20,458
2. Inter-islands (Peng Chau - Mui Wo - Chi Ma Wan - Cheung Chau)	985
3. Central - Mui Wo	5,828
4. Central - Peng Chau	5,290
5. Central - Yung Shue Wan	7,815
6. Central - Sok Kwu Wan	997
7. Hei Ling Chau - Peng Chau	451
8. Aberdeen - Yung Shue Wan via Pak Kok Tsuen	749
9. Aberdeen - Sok Kwu Wan via Mo Tat	523
10. Tuen Mun - Tung Chung - Sha Lo Wan - Tai O	461
11. Discovery Bay - Central	12,122
12. Discovery Bay - Mui Wo	276
13. Ma Wan - Central	3,829
14. Ma Wan - Tsuen Wan	4,173

The Administration's Proposals

(a) Six major trunk routes

We will support the six major trunk routes (namely Central - Cheung Chau route; Inter-Islands route serving Peng Chau, Mui Wo, Chi Ma Wan and Cheung Chau; Central - Mui Wo route; Central - Peng Chau route; Central - Yung Shue Wan route and Central - Sok Kwu Wan route) when such a need arises. In effect, this would mean one route for each of the major islands except for Lamma Island where we propose to support two routes because of the geographical distance between Yung Shue Wan and Sok Kwu Wan.

(b) Maintaining the existing service level

We will maintain the existing service levels of the six major trunk routes in the next tender. However, in view of the responses received, we will consider slight adjustments to the service levels and arrangements of individual routes in order to enhance the existing services and meeting residents' needs.

(c) Reducing holiday fare differential

We will narrow the holiday fare differential to a maximum of 20% in the next tendering exercise to address calls by residents for reducing such differential.

(d) Extending the special helping measures introduced in 2008

We will extend the special ad hoc helping measures currently provided to the four routes (see paragraph (b) of Annex C) to all the six routes.

(e) Reducing the magnitude of fare increases

When a fare increase is still justified, we will share some of the burden of the commuters so that the rate of fare increase could be reduced by half (after netting of the rate of general inflation) by reimbursing to the operators the vessel maintenance cost that has been incurred.

Therefore, when there is a need to increase fare, passengers will bear the fare increase up to the rate of general inflation since the previous fare increase as well as half of the residual rate of the fare increase. The other half will be subsidized by the Government.

(f) Mid-term review

In order to monitor the proper spending of public funds and ensure that fare levels should be appropriately adjusted when operating cost is projected to be reduced, a mid-term review will be conducted during the 3-year licensing period on the routes whose rate of fare increase has been reduced by reimbursing the vessel maintenance cost.

Existing Government helping measures and financial implications

The Government has been providing various helping measures to enhance the financial viability of the ferry services, including –

Existing helping measures	Financial implications
(a) for all ferry routes –	
(i) taking over pier maintenance responsibility;	about \$30.8M per year
(ii) waiving fuel duty;	-
(iii) reimbursing pier rentals and exempting vessel licence fees for ferry services under the Elderly Concessionary Fares Scheme;	revenue foregone of about \$3.8M per year
(iv) obtaining the Town Planning Board's approval to relax land uses at Central Piers No. 4, 5 and 6 so that the operators can sublet the upper deck of these piers for commercial activities such as restaurants, fast food shops, retail shops and service trades; and	-
(v) streamlining the subletting approval procedures to help generate non-fare box revenue for cross-subsidizing the ferry operation so as to alleviate pressure for fare increase;	-
(b) for the Central - Mui Wo route, Central - Peng Chau route, Central - Yung Shue Wan route and Central - Sok Kwu Wan route, special helping measures have been offered for the licensing period from July 2008 - June 2011 –	
(i) waiving annual vessel survey fee and private mooring fee;	revenue foregone of about \$0.3M per year
(ii) reimbursing pier water charge;	capped at about \$0.1M per year

- (iii) reimbursing pier cleansing and electricity charge subject to a cap prescribed by the Government; capped at about \$2.24M per year
 - (iv) reimbursing the balance of revenue forgone due to provision of elderly fare concessions after netting off the amount of pier rental reimbursement and vessel licence fee exemption under the current arrangement subject to a cap prescribed by the Government; and capped at about \$3.33M per year
 - (v) a one-off \$2 million scheme of providing free ferry tickets to encourage organizations such as schools, non-government organizations and community and district groups to organize activities to these outlying islands; actual amount spent about \$1.4M
- (c) we have retrofitted Central Piers No. 4 and 6 with fire prevention facilities so that ferry operators can sublet pier premises for more diversified commercial and retail activities. The project has been completed in February 2010. project cost at about \$16.4M