

ITEM FOR FINANCE COMMITTEE

LOAN FUND

NEW HEAD – “Private Hospital Development”

New Subhead – “Loan for the CUHK Medical Centre Development Project”

Members are invited to approve a commitment of \$4,033 million for the provision of a loan to the CUHK Medical Centre Limited, a wholly-owned subsidiary of the Chinese University of Hong Kong, for the purpose of developing a non-profit making private teaching hospital, to be named the CUHK Medical Centre.

PROBLEM

The Chinese University of Hong Kong (CUHK), a statutory body incorporated under the Chinese University of Hong Kong Ordinance (Cap. 1109), requires the Government’s financial support in the form of a loan to implement the CUHK Medical Centre Development Project.

PROPOSAL

2. The Secretary for Food and Health recommends the creation of a new commitment of \$4,033 million, and the provision by the Government to the CUHK Medical Centre Limited, a wholly-owned subsidiary of CUHK, of a loan of \$4,033 million under the Loan Fund. The proposed loan is to finance the development costs of a non-profit making private teaching hospital, to be named the CUHK Medical Centre, by CUHK and is for a period of 15 years with interest-free for the first five years from the first drawdown in 2016-17 and on a floating interest rate equivalent to the interest rate of the Government’s fiscal reserves placed with the Exchange Fund from 2021 onwards.

/JUSTIFICATION

JUSTIFICATION

The Development Proposal

Encl. 1

3. CUHK proposes to develop a non-profit making private teaching hospital, i.e. the CUHK Medical Centre, on part of the Sha Tin Town Lot No. 437 and the extension thereto (the Site as shown on the plan at Enclosure 1). The Site is adjacent to the MTR University Station. The proposed Medical Centre will be managed and run by its wholly owned subsidiary, the CUHK Medical Centre Limited, on a self-financing basis.

4. The CUHK Medical Centre aims to provide quality private healthcare services at affordable and transparent prices. The CUHK Medical Centre will consist of 516 beds (with an expansion potential of an additional 90 beds) covering a range of specialties, services and facilities including general medicine, general surgery, orthopaedics & traumatology, gynaecology, paediatrics, radiology, obstetrics, cardiology, a 24-hour outpatient clinic and teaching venues.

5. CUHK Medical Centre will also be operated as a teaching hospital contributing to the training of healthcare professionals in Hong Kong. With strong input from the experienced professors and medical professionals in CUHK, CUHK Medical Centre can supplement the Prince of Wales Hospital (PWH) and Queen Mary Hospital as an additional teaching hospital in Hong Kong.

6. The CUHK Medical Centre is required to commence operation no later than 60 months from the date of approval of modification of the Conditions of Grant (Land Lease) by the Government.

Supporting the dual-track healthcare system

Alleviating pressure on public healthcare

7. Apart from providing quality private healthcare services and training of healthcare professionals, CUHK has committed to help alleviate the current pressure on the public healthcare sector by taking up referrals of specialist

/outpatient

outpatient (SOP) and day procedure cases from the Hospital Authority (HA). The CUHK Medical Centre has agreed to receive from HA up to 17,600 new SOP cases and 6,600 new day surgery cases each year on an ongoing and long term basis from the fifth year of operation of the Hospital onwards¹. HA patients referred to CUHK Medical Centre will continue to be charged at HA fees. This partnership arrangement with HA will help shorten waiting time for public services while helping to ensure a comprehensive and diverse case mix for the CUHK Medical Centre on the other hand and the quality of training it offers.

Enhancing price transparency of private healthcare services

8. The CUHK Medical Centre will use packaged prices extensively for its services to enhance price transparency. It will provide 50% of its inpatient bed-days for services provided through standard beds at packaged charges upon commencement of the operation of the Hospital, and the percentage will rise progressively up to 70%. The extensive use of packaged charges will provide patients with a reasonable level of confidence on the total costs of hospital services they can expect, thereby encouraging the use of private hospitals services. These commitments undertaken by the CUHK Medical Centre are summarized at Enclosure 2.

Encl. 2

9. The above commitments undertaken by CUHK as set out in paragraphs 7 and 8, together with a set of minimum requirements related to private hospital development accepted by CUHK (which cover aspects of land use, scale of development, date of commencement of operation, service scope, price transparency, provision of standard beds at packaged charges, service standards or hospital accreditation, and reporting obligations), will be reflected in the modified Land Lease and/or Service Deed to be signed between CUHK and/or CUHK Medical Centre Limited and the Government.

10. CUHK has taken into account the above commitments when preparing their financial projections, and expects that CUHK Medical Centre can breakeven within five years from its commissioned operation.

/Financing

¹ For reference, according to the Controlling Officer's Report, the number of Hospital Authority's (HA's) specialist outpatient new attendances (clinical) for 2014-15 is estimated to be 691,000. The number of day surgery cases handled by HA per year is not available.

Financing Arrangements

Considerations

Encl. 3

11. Private hospital development is a very long term investment involving a huge capital outlay upfront, given the high cost of medical equipment and the heavy capital investment required for construction of hospital buildings. According to CUHK's development plan, the total project cost for the CUHK Medical Centre is estimated to be \$6,333 million² (in 2014 prices). Details of the breakdown of the estimated project cost are at Enclosure 3. CUHK has applied for a Government loan of \$4,033 million to fund part of the development costs of the Project. The sources of funding for the Project are summarized in the table below –

CUHK's equity injection	(in HK\$ million)
- CUHK's reserve	500
- Donation by the Hong Kong Jockey Club Charities Trust	1,300
- Donation by other donors	500
	2,300
Government loan	4,033
Total project cost	6,333

12. Indeed, the huge initial capital investment required for private hospital development and the constraint that conditions for land granted to bona fide Non-governmental organisations (NGOs) often do not permit the grantees to mortgage the land for the purpose of seeking loans from commercial banks provide major hurdles for bona fide NGOs, like CUHK, from providing affordable private healthcare services through development of private hospitals.

13. The difficulty for a non-profit making organization such as CUHK in meeting the capital costs for developing a private hospital on its own will mean that it has to collaborate with a third party to act as its financier for the project. The profit-sharing arrangement with the financier will defeat the purpose of operating a non-profit making hospital and is not conducive to lowering private hospital charges and providing affordable private hospital services to the community.

/14.

² The \$6,333 million includes the development cost of \$39.2 million for an off-site medical clinic which will also be operated by Chinese University of Hong Kong (CUHK)'s wholly owned subsidiary.

14. With a view to facilitating financing of the necessary capital cost for private hospital development and considering that CUHK's proposed development of the Hospital is in line with our health policy, we consider it appropriate to provide financial support to CUHK and/or its wholly owned subsidiary in the form of a Government loan of \$4,033 million for developing the CUHK Medical Centre.

15. CUHK will exercise due care to control the overall project cost. With a view to containing the Government's financial exposure, the loan amount provided for the development will be fixed at \$4,033 million. In the event that the actual project cost exceeds the estimate, the Government will provide no further loans to CUHK Medical Centre Limited, who will be responsible for covering the extra costs incurred without compromising the service commitments it has undertaken.

Encl. 4 16. The terms and conditions of the proposed Government loan are summarized in Enclosure 4.

Interest to be charged on the Government loan

17. There will be a continuous and significant outflow of cash in the initial years following the commencement of construction works of the CUHK Medical Centre until the Hospital is set up under the relevant legislation and starts generating a stable income stream. To assist CUHK Medical Centre with its cashflow during the construction and initial stage of the operation of the Hospital, the proposed loan would be interest-free for the first five years from the first drawdown of the loan. Thereafter, interest will be charged on the outstanding amount at a floating rate equivalent to the interest rate of the Government's fiscal reserves placed with the Exchange Fund. The five-year interest-free period is well-justified with the service commitments undertaken by CUHK.

Economic benefits

18. The proposed loan will facilitate the development of a non-profit making private hospital by CUHK, which will increase the overall capacity of the healthcare system in Hong Kong. This would help cater for the rising demand for healthcare services arising from an ageing population and provide the public with more choices of high quality private hospital services. The proposal would also be conducive to the growth of medical professions and related businesses and create more job opportunities in the medical sector.

/FINANCIAL

FINANCIAL IMPLICATIONS

19. The interest forgone by the Government in the five-year interest-free period is estimated to be \$533 million (at 2014 prices). This amount will be fully offset by the cost saving of HA by referring SOP and day procedure cases to the CUHK Medical Centre, which is projected to be about \$1,058 million in total or about \$51 million in a full year from the fifth year of hospital operation onwards (both figures at 2014 prices)³. Taking into account the above estimated saving as well as the increased capacity for treating public patients, overall speaking, the net benefit of the proposed loan to the public would outweigh the interest foregone by the Government arising from the provision of the loan.

20. The forecast drawdown of the proposed Government loan is as follows –

Financial Year	2016-17	2017-18	2018-19	Total
Drawdown amount (\$million)	1,815	1,492	726	4,033

CONSULTATION

21. CUHK consulted the Health and Environment Committee of the Shatin District Council on 12 March 2015. While members in general are supportive of the development, they raised concerns over the possible impact on the road traffic in the vicinity. CUHK will look into this with due care and work with relevant Government departments to ensure the concerns are properly addressed during the development.

22. We consulted the Legislative Council Panel on Health Services on 16 March 2015. Members supported the proposed loan and our submission of the proposal to the FC for approval, whilst making the following comments –

/(a)

³ Since CUHK Medical Centre's commitment to take up referrals from HA is on an on-going and long term basis, the cost savings to the Government is computed using the perpetuity formula. A perpetuity is an annuity in which the periodic payments begin on a fixed date and continue indefinitely. The value of the perpetuity is finite because receipts that are anticipated far in the future have extremely low present value (present value of the future cash flows). The saving of \$1,058 million is a conservative estimate as HA's unit cost of a day procedure is not readily available. We have used HA's unit cost per patient day (general) in 2014-15, which is \$4,590, as a proxy to estimate HA's cost savings for referring day procedure cases to the CUHK Medical Centre. The figure of \$4,590 is significantly lower than the mean price of day procedures of private hospitals, e.g. the mean price of colonoscopy which is one of the most common types of day procedure in private hospitals in Hong Kong is \$11,042.

- (a) some Members asked if the proposed Hospital will drain the teaching manpower of CUHK Faculty of Medicine. Currently, full time clinical professors employed by CUHK can engage in private clinical practice only with the approval of his or her department and for limited sessions per week in accordance with existing rules and regulations prescribed by CUHK. This rule will be maintained with the development of CUHK Medical Centre. Therefore, teaching resources of CUHK should not be jeopardized. Moreover, CUHK Medical Centre will employ its own staff for the operation of the hospital, including a majority of its doctors. Despite the fact that they will not be employed by CUHK, they will serve as additional workforce contributing towards the teaching and research activities of CUHK. CUHK Medical Centre will therefore strengthen the teaching capacity of CUHK Faculty of Medicine as a whole.
- (b) some Members enquired if the access to services for existing patients at the PWH would be affected with CUHK diverting resources to the operation of the CUHK Medical Centre. Despite the establishment of the CUHK Medical Centre, CUHK will continue to use PWH as a teaching hospital without cutting back on or diluting its involvement in it. Not only will patients' access to public healthcare services remain the same, they might even have additional access to services provided by the CUHK Medical Centre at HA fees given CUHK's commitment to provide SOP consultation services and day surgery to public patients referred by HA as detailed in paragraph 7 above.

BACKGROUND

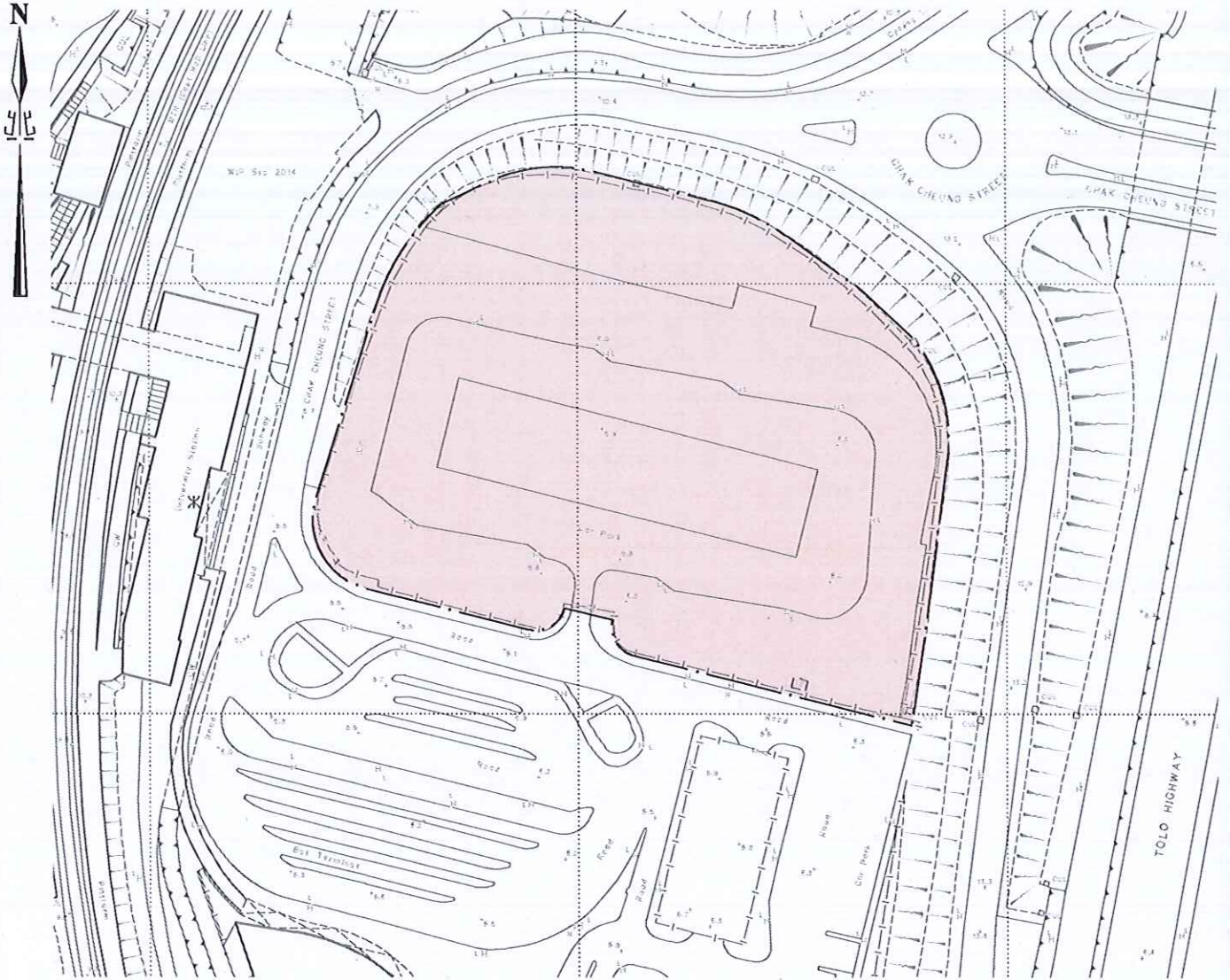
23. The healthcare system of Hong Kong runs on an effective dual-track basis encompassing both public and private elements. The public healthcare sector serves as the cornerstone of Hong Kong's healthcare system and the safety net for all while the private healthcare sector provides personalized and more accessible services for those who are willing and can afford to use its services.

24. The Chief Executive's manifesto pledges that the Government should examine measures "to encourage non-profit making organisations to establish hospitals and operate them on a self-financing basis". In the 2013 Policy Address, the Government reaffirmed its commitment to the twin-track system for public and private healthcare sectors. To achieve this, we will reinforce the public healthcare system by enhancing its services and effectiveness while facilitating the development of the private healthcare sector and improving the regulatory mechanism. Facilitating private hospital development will help increase the overall capacity of the healthcare system in Hong Kong which should assist in addressing the rising demand for healthcare services arising from an ageing population and provide the public with more choices of high quality private hospital services.

25. In parallel with continued investment in the public healthcare sector, the Government is developing and consulting the public on detailed proposals for the implementation of the Voluntary Health Insurance Scheme (VHIS). The VHIS is a voluntary and government-regulated private health insurance scheme and is intended as a supplementary financing arrangement and one of the turning knobs for adjusting the balance of the public-private healthcare sectors. By enhancing the accessibility, quality and transparency of health insurance products, the VHIS aims to encourage those who are willing and able to make greater use of private healthcare services to use such services, thereby indirectly alleviating the pressure on the public healthcare sector and enhancing the long-term sustainability of our healthcare system. The successful implementation of the VHIS hinges on having in place the necessary supporting medical infrastructure, including a private hospital sector with sufficient capacity to serve the community demand.

26. At the same time, we are expanding and redeveloping a number of existing public hospitals to increase the overall capacity of the healthcare system. Construction of new ones in the Kai Tak Development Area is also in the pipeline. The works expenditure of public hospital projects already under construction or planning is estimated at \$81 billion. It is therefore important to facilitate the development of more private healthcare facilities in tandem; otherwise the over-reliance on the public sector for inpatient service will be further aggravated.

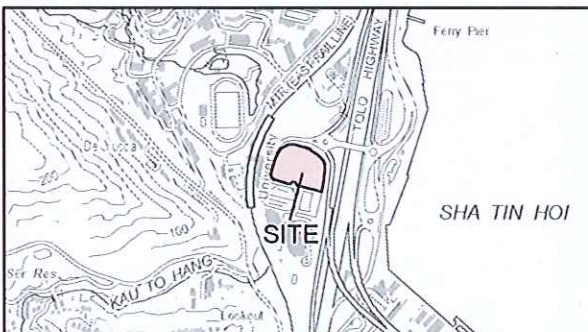
SITE PLAN



SCALE 1:1 500



LOCATION



SCALE 1:20 000

FOR IDENTIFICATION PURPOSES ONLY



District Lands Office, Sha Tin
Lands Department

Plan Prepared by District Survey Office, Sha Tin

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File No. ----

Survey Sheet No. 7-NE-22C/D

O.Z.P. No. ----

Reference Plan No. ----

PLAN No. STM9638

Enclosure 2 to FCR(2015-16)3

Extra Commitments Undertaken by CUHK

(I) Provision of inpatient services at packaged charges beyond the Minimum Requirements

CUHK undertakes that the CUHK Medical Centre shall use packaged prices extensively for its services.

2. CUHK undertakes that the CUHK Medical Centre shall offer inpatient services at packaged charges at a level of commitment exceeding the minimum requirement of 30% of inpatient bed-days and shall increase the percentage in a progressive manner. The CUHK Medical Centre shall provide 50% of its inpatient bed-days for services provided through standard beds at packaged charges for Eligible Persons upon commencement of operation of the Hospital, and the level of commitment will rise progressively, reaching 60% by the sixth year of operation of the Hospital and 70% by the tenth year of operation of the Hospital.

(II) Offer SOP and day procedures services to public patients referred by HA

3. CUHK also undertakes that the CUHK Medical Centre shall provide SOP consultation services and day surgery to patients referred by HA in the following four specialties: gynaecology, orthopaedics, gastroenterology cum colorectal surgery and urology. Patients referred to the CUHK Medical Centre for treatment shall continue to be charged at HA's standard fees and charges. CUHK also undertakes that the CUHK Medical Centre shall attend to a minimum of 3,520 new SOP cases and 1,320 new day surgery cases in the first year of operation of the Hospital, and the number of cases will increase progressively. From the fifth year of operation of the Hospital onwards, the CUHK Medical Centre will receive 17,600 new SOP cases and 6,600 new day surgery cases each year.

Enclosure 3 to FCR(2015-16)3

**Breakdown for Estimated Project Cost
for the Development of the CUHK Medical Centre
(as at November 2014)**

Items	Cost Estimates (HK\$ million)
Construction costs	4,060
Equipment	1,461.1
Pre-opening commissioning charge	509.4
Pre-opening staff cost	23
Working capital	162
Interest capitalised	117.5
Total: (at 2014 price level)	6,333 ^{Note}

^{Note} Includes the development cost of \$39.2 million for an off-site medical clinic which will also be operated by CUHK's wholly owned subsidiary.

Enclosure 4 to FCR(2015-16)3

Proposed terms and conditions of the Government Loan for the Chinese University of Hong Kong Medical Centre Development Project

- Amount: \$4,033 million
- Lender: The Government (new Head of “Private Hospital Development” under the Loan Fund Account)
- Purpose: To finance the development costs of the CUHK Medical Centre
- Drawdown: Tentative drawdown schedule is as follows^{Note} –

<u>Financial Year</u>	<u>Drawdown amount</u>
2016-17	\$1,815 million
2017-18	\$1,492 million
2018-19	\$726 million
Total	\$4,033 million

- Loan Term: 15 years
- Interest:
- First 5 years from first drawdown: Interest-free
 - From 6th year onwards: a floating rate equivalent to the interest rate of the Government’s fiscal reserves placed with the Exchange Fund
- Repayment:
- Repayment in ten annual instalments (i.e. annual repayment of principal in ten equal instalments plus interest charged on the amount of outstanding loan)
 - First repayment instalment to be made in the sixth year from the first drawdown, subsequent repayment instalments to be made within 15 years as from the first drawdown
- Safeguards: If CUHK fails to comply with the modified Land Lease, the Government may re-enter and take possession of the Site. If CUHK and/or its wholly-owned subsidiary fails to comply with the Service Deed, the Government may terminate the Service Deed. This would trigger co-termination of the modified Land Lease and the Government may re-enter and take possession of the Site. The Site includes the buildings and structures erected thereon and all the fixtures permanently affixed to the land. We also intend to impose as security for the loan, a floating charge over the assets (including all equipment) which the CUHK Medical Centre owns for managing and operating the hospital.

^{Note} The drawdown schedule is set on the basis that the modification of the Land Lease will be approved in 2015-16.