

(Translation)

**Meeting of the Finance Committee of
the Legislative Council on 26 February 2016**

**Hong Kong Section of the
Guangzhou-Shenzhen-Hong Kong Express Rail Link**

Opening remarks by the Secretary for Transport and Housing

Chairman,

Regarding the application for additional funding for the Hong Kong Section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link (“XRL”) project, six Public Works Subcommittee meetings and six sessions of Finance Committee (“FC”) meetings have been held since it was discussed at the two meetings of the Subcommittee on Matters relating to Railways in December 2015, representing a total discussion time of 29.5 hours. As at yesterday (25 February), the Government has provided 15 supplementary papers or written replies to the Legislative Council (“LegCo”) in response to Members’ requests.

2. As at the end of January 2016, more than 77% of the entire XRL project was completed. Any uncertainty with the construction has gradually diminished. The MTR Corporation Limited (“MTRCL”) is confident that the target completion and commissioning of XRL in the third quarter of 2018 can be attained. The total expenditure under the Entrustment Cost is expected to reach \$60.2 billion in March this year. As about \$4.8 billion has to be reserved for the various expenses required for the suspension of works or even termination of the works contracts in case approval for the additional funding

was not obtained from the LegCo, we are now approaching a critical point where we need to consider if we have to suspend works temporarily.

3. The Government will discuss the matter with MTRCL in a highly prudent manner. It is because once a decision is made to trigger suspension of works, there will be a series of undesirable outcomes. They include workers being out of job, further delay of works schedule, additional claims from contractors and the “capping” of the Entrustment Cost as agreed with MTRCL being non-applicable.

4. We understand that the community has strong views on the serious delay and cost overrun of the XRL project. The Government deeply regrets the matter and would like to apologise to the public. The Government is dissatisfied with the performance of MTRCL as the project manager of the XRL. Therefore, the Government reserves all of its right to pursue the warranties and obligations from MTRCL and will commence the arbitration proceedings after the completion and commencement of the XRL.

5. The Government appointed the Independent Expert Panel (“the Panel”) chaired by Hon Mr Justice Michael HARTMANN in 2014. The Panel made a number of criticisms about the performance of MTRCL on XRL project management. It also suggested some improvement measures regarding Highways Department’s (“HyD”) monitoring work in accordance with the “check the checker” approach under the Entrustment Agreement. The Government has accepted and implemented the new measures, including providing enhanced access for the Monitoring and Verification Consultant to perform its duties and more frequent and focused verification on critical contracts, strengthening HyD’s monitoring of the progress and cost of the XRL project according to key milestones of the programme, and requiring MTRCL to enhance progress reporting.

6. To control the expenditure, the Government has agreed with MTRCL on “capping” the revised Cost to Complete at \$84.42 billion. HyD will not relax its monitoring over the cost. Under the Entrustment Agreement, MTRCL has to manage its contracts with various contractors and handle the related claims having regard to the best interest of the XRL project.

7. We have learnt the lesson and enhanced our monitoring work, and will continue to pursue the warranties and obligations from MTRCL. Right now the most pressing need is to provide additional funding to avoid leaving the XRL works “unfinished”, which will result in “double loss” to the community - the waste of the original Entrustment Cost of \$65 billion plus an additional cost of no less than \$10.6 billion to undertake the remedial works. The expected economic and social benefits to be brought about by the XRL project will also become unrealized.

8. We must not leave the XRL project “unfinished”, and need to endeavour to ensure that the XRL can bring out its maximum transport, economic, and social benefits. As the world has entered into a high speed railway era, the XRL can become a strategic infrastructure project that can consolidate and enhance the competitiveness and hub status of Hong Kong. To implement the co-location of CIQ arrangement under “one country, two systems” is the best way to maximise the benefits of the XRL. Some international experiences (such as between the United Kingdom and France or between the United States of America and Canada) have proved that co-location is feasible.

9. Chairman, for the past two months and more, the Government has endeavoured to answer the questions raised by Members, including those on works progress and reasons for delay and cost overrun, economic benefits of the XRL project and projections of operating return. Regarding the claims under individual work contracts, as these ultimately relate to negotiation by

MTRCL with its individual contractors constituting sensitive commercial information and affecting the interest of the public coffer, we find it difficult to provide full details. Nevertheless, we have, in one of the latest papers submitted to FC, provided Members with some relevant information about the 42 major contracts of the XRL project by category of percentage of estimated increase over the contract cost.

10. Concerning the future operation of the XRL, we estimate that there will be reasonable return. As we have pointed out in the supplementary paper (paper no. FC122/15-16(01)) submitted at the last FC meeting, the operating margin (as expressed in EBITDA, i.e. operating revenue minus operating cost, and divided by operating revenue) in 2012 and 2013 will range from 42% to 58% on the assumption that the XRL is commissioned in Q3 of 2018. The operation of the XRL will not be in deficit. Of course, we have to discuss the related planning with the mainland railway operating authorities in order to work out the frequency, fare, sharing of fare revenue and other details of train service of the Hong Kong section. The Government also has to discuss with MTRCL the various provisions of the arrangement on service concession.

11. On the issue of co-location arrangement, I have already reiterated the views of the Government on a number of occasions: (i) implementation of the co-location arrangement is the best choice in order to realise the maximum social and economic benefits of the XRL and full convenience to passengers, which is also the goal of the SAR Government; (ii) the proposal on the co-location arrangement to be implemented must be in conformity with the Basic Law provisions and the principle of “one country, two systems”; (iii) the co-location arrangement involves rather complicated constitutional, legal and specific operational issues, the discussion of which with the relevant authorities of the Central Government has been taking more time because we have to carry out in-depth studies on related problems to ensure that we will eventually come up with a proposal that conforms to the provisions in the

Basic Law and is practicable.

12. While there has been intensive discussions between the SAR Government and the Central authorities, we are not yet ready to announce the full details of the proposal on implementing the co-location arrangement. As I have said before, FC's approval for additional funding for the XRL project now does not amount to its approval of a co-location arrangement. These are two different procedures. In due course we will present the proposal in detail to the community for consultation and the relevant arrangements will need LegCo's clearance. Therefore, LegCo Members will definitely be given the opportunity to fully examine the proposal on co-location arrangement to be put forward by the Government.