

Legislative Council Finance Committee

Expansion and Development Plan of Hong Kong Disneyland Resort

*The Government's response to the follow-up actions raised
at the Finance Committee meetings on 21 and 22 April 2017*

PURPOSE

This paper sets out the Government's response to the follow-up actions raised at the Finance Committee meetings on 21 and 22 April 2017.

THE GOVERNMENT'S RESPONSE

(a) Depreciation

2. Depreciation of the assets of the Hongkong International Theme Parks Limited ("HKITP") is calculated in accordance with the relevant parts of the Hong Kong Financial Reporting Standards, and depreciation of property, plant and equipment is calculated using the straight-line method. The depreciation period of different asset types is shown in the following table –

Type of asset	Depreciation period
Buildings and improvements	3 – 40 years
Furniture, fixture and equipment	3 – 10 years
Machinery and equipment	3 – 40 years
Rides and amusements	8 – 25 years
Shows and parades	5 years

3. The above method for calculating depreciation is applicable to HKITP's existing assets and the new assets under the Hong Kong Disneyland Resort ("HKDL")'s expansion and development plan ("the Plan").

4. The Walt Disney Company ("TWDC") expects that, after the progressive launch of various new attractions under the Plan, HKDL's attendance would have a steady growth, with the total attendance in Fiscal Year 2025 ("FY25") at 9.0 million to 9.3 million, and that the incremental revenues brought about by the Plan would be higher than the annual depreciation of the new assets.

(b) Development restrictions in the vicinity of Sunny Bay

5. Please refer to paragraph 14 below.

- (c) *Base case scenario projection*
 (d) *The scenario without the Plan, and the scenarios with the Plan under different projections*

6. TWDC expects that without the Plan, HKDL's business would continue to benefit from factors such as HKDL's marketing and promotion, completion of various transport infrastructure projects, etc. in the next few years, and would show some growth. In this regard, the total attendance in FY25 would be comparable to the Government's respective projection made in 2009 when considering the expansion of the three new themed areas, i.e. at the level of around 7.3 million. However, in the medium to long term, amidst increasing competition among theme parks in the region, HKDL's attractiveness would diminish gradually due to the lack of new large-scale attractions, and its attendance would have slower growth or even drop slightly.

7. With capital injection into HKDL to take forward the Plan, new attractions and offerings will be launched in a continuous manner from 2018 to 2023. According to TWDC's projection, the Plan would enable HKDL's attendance and business to progress continuously with the total attendance in FY25 reaching 9.0 million to 9.3 million.

8. In our paper referenced FCR(2017-18)1 submitted to the Finance Committee, Enclosure 4 therein has set out the economic assessment of the Plan under different scenarios. Even if the projected incremental visitors under the more conservative Situation A is reduced by 15% as the sensitivity test, under this very prudent assumption, the Plan is, net of economic costs involved, still likely to bring about considerable net benefits to the economy. The results of the economic assessment of the Plan under Situation A, Situation B and the sensitivity test are extracted as follows –

	Total net economic benefits (HK\$2014 prices in present value)		Economic internal rate of return in real terms		Breakeven year @	Number of jobs created from additional spending (in terms of man-year)	
	Over the operation period of		Over the operation period of			FY25	FY30
	20 years	40 years	20 years	40 years			
Situation A	17.7 bn	38.5 bn	23.2%	24.3%	FY25	4 700	7 200
Situation B	18.7 bn	41.6 bn	22.9%	24.1%	FY25	5 600	7 900
Sensitivity test	14.0 bn	31.6 bn	20.1%	21.5%	FY26	4 000	6 100

Note:

@ "Breakeven year" refers to the year when the present value of the cumulative gross economic benefits just offset the cumulative economic cost.

(e) Questions raised by Hon CHU Hoi-dick and ruled to be in order by the Chairman (letter dated 21 April 2017)

Deed of Restrictive Covenant (“DRC”)

9. As stated in the Legislative Council Brief on “Hong Kong Disneyland” dated 18 November 1999 issued by the Government, on 16 November 1999, the Executive Council advised and the Chief Executive ordered a series of arrangements to implement the development and operation of HKDL at Penny’s Bay, Lantau Island. The arrangements at that time included authorising the Director of Lands to enter into DRC whereby the future development of the land in the vicinity of HKDL would be subject to certain height, building and use restrictions, so as to maintain the aura of fantasy of HKDL and ensure the compatibility of the uses in the vicinity of HKDL. The said Legislative Council Brief also pointed out that DRC would not affect the rights of the concerned private lot owners which subsisted at the date of DRC, the existing developments as at the date of DRC and the approved developments as at the date of DRC. This DRC has been registered at the Land Registry (Memorial No.: IS278911) since January 2000 for public inspection.

10. The coverage of DRC includes the government land and private lots concerned, and the location of such government land concerned is shown on the relevant plans attached to DRC (including Chok Ko Wan Lots No. 2, 3, 4, 5, 6, and Yam O Lot No. 1). The purpose of creating new lot numbers is to facilitate registration of DRC at the Land Registry. As regards the areas of the private lots concerned under DRC, the Government needs more time to collate and verify the relevant data, and the requested information will be provided in writing later.

11. The purpose of the Land Resumption Ordinance (Cap.124, “the Ordinance”) is to resume private land for public purposes, while DRC is to restrict the Government’s interest in the government land concerned and the Government’s reversionary interest in the private lots concerned. DRC requires the Government, in so far as it has the legal right to do so, to ensure that the approval for future new development/redevelopment proposal on the government land and private lots concerned should comply with the development restrictions set out in DRC. As the purpose and nature of the Ordinance and DRC are different, the issue of one overriding another does not exist.

12. The idea of East Lantau Metropolis (“ELM”) was yet to be formulated when DRC came into place in 1999. As for the indicative alignments of transport infrastructures shown in DRC, they reflected the then planning intention of the relevant Outline Zoning Plan and the preliminary proposals in the related strategic or technical studies on the developments of ports, airport, railways and major roads, etc.. These proposals are constantly updated according to the latest

development needs and prevailing strategies. As regards the proposed ELM and the related traffic and transport network put forward in 2014, it will take into account the ongoing Hong Kong 2030+ study, the strategy for the development and conservation of Lantau to be announced later this year, and the strategic studies for artificial islands in the central waters to be conducted.

13. We wish to point out that TWDC's current agreement to explore relaxations to development restrictions is not a requisite nor prerequisite for the future development plan of ELM and around Sunny Bay. It would only enhance development and planning flexibility and allow greater flexibility and room for exploring the development potential of Lantau and its surroundings, including the vicinity of HKDL.

14. As regards the Sunny Bay reclamation proposal, as set out in the paper submitted by the Government to the Legislative Council Panel on Development (No. CB(1)578/16-17(07)), it is recommended that the Sunny Bay reclamation site can mainly be used for recreation and tourism-related developments. This site can be developed into a recreation and tourism gateway for Northeast Lantau by establishing new tourist attractions, recreational or leisure facilities, themed hotels, as well as retail, catering and entertainment facilities. These facilities (except internationally branded theme parks and casinos) are compatible with the permitted land uses for the Sunny Bay reclamation area under DRC. Detailed uses for the Sunny Bay reclamation will be explored in the subsequent planning and engineering studies.

The Government's investment and expenditure in the HKDL project

15. Details of the Government's investment, capital expenditure, etc. in the HKDL project in the past are shown in the following table (the relevant figures were disclosed in past Legislative Council papers) –

Government investment on HKDL	
Equity	\$10.7 billion
Loan	\$1.15 billion
Subordinated shares	\$3.6 billion
Capital expenditure (in money-of-the-day prices)	
Reclamation and infrastructure works	about \$8.0 billion
Land acquisition and clearance	about \$1.5 billion
Others	
Waiver of cash dividends receivable from the MTR Corporation Limited to support the construction and operation of the Disneyland Resort Line	about \$0.9 billion

Economic assessment

16. We have provided details of the methodology of economic assessment in Enclosure 4 of our paper submitted to the Finance Committee referenced FCR(2017-18)1. Specifically, our economic assessment studies the economic costs and benefits of the Plan, the quantifiable economic benefits of which arise from the additional spending in Hong Kong by incremental visitors to HKDL brought about by the Plan. The methodology involves, based on the number and type of incremental visitors projected by TWDC, estimating the additional spending brought about by these incremental visitors (including spending both inside HKDL and at other parts of Hong Kong), and then assessing the total value added and employment that can be generated by such additional spending.

17. According to the Government's economic assessment in 2009 for considering the expansion of the three new themed areas, HKDL's cumulative attendance up to FY16 was projected to reach 54 million. HKDL's actual cumulative attendance from its opening in 2005 up to FY16 exceeded 64 million, which is already above the Government's projection in 2009. Furthermore, the HKDL project achieved economic breakeven in FY12.

Waste management and green buildings

18. HKDL is committed to protecting environment, saving energy and minimising the burden of its operation on the environment, as one of its corporate social responsibilities. In this connection, the management company of HKDL requires its construction contractors to ensure, where possible, that the construction waste from HKDL's works can be minimised and relevant materials can be reused and recycled. Also, the contractors have to put in place measures for proper disposal of construction waste and comply with such measures in a stringent manner. The management company of HKDL will, following the above environmental protection principles, implement the works projects under the Plan and ensure environmental sustainability.

Basis of induced tourists

19. When conducting the economic assessment of the Plan as mentioned in paragraph 16 above, we further break down HKDL's non-local visitors into base tourists (i.e. who would have visited Hong Kong even without HKDL) and induced tourists (i.e. tourists whose main purpose of coming to Hong Kong is to visit HKDL) for assessment. We have also taken into account the surveys conducted inside the resort by HKDL and the Hong Kong Tourism Board ("HKTB"), which indicate that in recent years, about half of HKDL's non-local visitors' main purpose of coming to Hong Kong is to visit HKDL. By making reference to these surveys and taking into account the breakdown of the projected

incremental visitors, we assume that about 31% of the total incremental attendance (i.e. including local visitors and tourists) brought about by the Plan would be induced tourists.

Analysis of tourism industry

20. The Government's tourism policy objective is to pursue a balanced, healthy and long-term growth. Our focuses of tourism planning are to highlight the unique elements of Hong Kong, expand Hong Kong's market reach and draw more high-spending overnight visitors. In this regard, apart from the development of the two theme parks, namely HKDL and Ocean Park, we are also committed to increasing the diversity of tourism products, including tourism activities showcasing Hong Kong's local characteristics, green tourism, etc.. Every year, HKTB prepares projections on various tourism performance indicators (including total visitor arrivals) for the coming year and report to the Legislative Council Panel on Economic Development ("ED Panel"). HKTB's projection will take into account different factors in the macro environment, including risks and opportunities, tourism-related policies, developments in visitor source markets, and the analyses and forecasts by international organisations. However, the number of visitor arrivals will be affected by many uncertain factors such as exchange rate and the overall economic environment.

TWDC's information

21. TWDC, which is listed in the United States, is required to disclose its financial information in accordance with applicable laws and regulations in the United States, and the financial information related to HKDL has been set out in the relevant financial statements.

Profit and loss of HKDL

22. As stated in the Government's paper submitted to the Finance Committee in 2009 regarding the arrangements for HKDL's expansion of the three new themed areas and capital realignment (FCR(2009-10)39), TWDC agreed that, from FY09 onwards, HKDL would disclose its key operating and financial results on an annual basis. During the discussion at ED Panel in 2009, the Government also pointed out that both the Government and TWDC were subject to confidentiality provisions, and should not disclose any commercially sensitive information. Nevertheless, the Government and TWDC have agreed to disclose HKDL's key operating and financial results on an annual basis starting from FY09.

(f) Questions raised by Hon CHU Hoi-dick and ruled to be in order by the Chairman (letter dated 22 April 2017)

Project cost of the Plan

23. The nature, positioning, construction and operation model of HKDL and Ocean Park are different, and the project costs of their development plans cannot be directly compared. As regards the Plan of HKDL, the new themed areas and attractions will bring imaginary scenes and buildings in the movies to the real setting which, apart from usual machinery, will integrate with high-quality visual and audio effects brought about by the latest technology to enrich guest experiences. When we consider the project cost of the Plan, we have compared the project costs of similar theme park development projects in recent years. For example, the Tokyo Disney Resort announced in April 2016 a development plan with one new themed area at a project cost of 75 billion Japanese yen (around \$5 billion to \$6 billion Hong Kong dollars), and there would be eight new entertainment offerings, less than the 20 offerings under the Plan of HKDL.

24. When the Plan was discussed at ED Panel in November 2016, some Panel members requested more details of the project cost. As such, we provided a more detailed breakdown of the project estimate to ED Panel in February 2017, and the same is also included in Enclosure 1 of our paper submitted to the Finance Committee (FCR(2017-18)1).

25. According to the information provided by the management company of HKDL, over 90% of the project cost of \$10.9 billion would be spent on local operations or construction works/materials by third-party companies not related to TWDC. Any fees to be paid to TWDC's related companies for the design and technology development would be charged on cost recovery basis without making any profit by TWDC from the construction cost, and there is no element of royalties and management fees in the construction cost. Moreover, the management company of HKDL will, in line with its past practice, select its suppliers/contractors under the Plan through open and fair tenders, so as to obtain high-quality and value-for-money services and materials.

Capital Investment Fund

26. The Capital Investment Fund ("CIF"), established by Resolution of the Legislative Council on 1 April 1990, is part of the fiscal reserves of the Government. CIF was established for the purpose of financing investments in the MTR Corporation Limited, the Kowloon-Canton Railway Corporation, the Hong Kong Housing Authority, the New Hong Kong Tunnel Company Limited and such other bodies as the Finance Committee may specify.

27. The Government will consider the need to transfer funds from the General Revenue Account to CIF with regard to the commitments and the cashflow projections of CIF. If the balance of the CIF could not fully meet its expenditure, transfers from General Revenue Account to CIF will be required. The balance of CIF remains to be part of the fiscal reserve of the Government. Payment of CIF will become expenditure of the Government when made. Transfers from General Reserve Account to CIF are for meeting the estimated expenditure of CIF, but not provisions for losses.

28. In the past five years (i.e. 2012-13 to 2016-17), the Government made a transfer of HK\$9 billion from the General Revenue Account to CIF in 2016-17 for meeting the estimated expenditure of that year. The Government has no relevant forecast for the year 2018-19 and afterwards.

29. The Government proposes to inject \$5,450 million from CIF as equity to HKITP to support the Plan at the Phase 1 site of HKDL. The capital injection schedule will be determined having regard to the cashflow requirements of the Plan.

Basis of implementing the HKDL project

30. In early November 1999, the Government briefed the Legislative Council Panel on Economic Services on the HKDL project and the proposed implementation arrangements, and listened to the views of Members and relevant sectors. Subsequently, the Government issued the Legislative Council Brief on “Hong Kong Disneyland” on 18 November 1999, which stated that on 16 November 1999, the Executive Council advised and the Chief Executive ordered a series of arrangements to implement the development and operation of HKDL at Penny’s Bay, Lantau Island. The arrangements at that time included authorising the Director of Lands to grant the site for Phase 1 development of HKDL to HKITP and to enter into DRC, etc.. The relevant land documents have been registered at the Land Registry for public inspection. On 26 November 1999, the Government also obtained the Finance Committee’s approval for injection into HKITP for the HKDL project.

Tourism Commission
Commerce and Economic Development Bureau
April 2017