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Panel on Development and Panel on Home Affairs

**Joint Subcommittee to Monitor the Implementation of
the West Kowloon Cultural District Project**

**Minutes of special meeting held on
Tuesday, 11 September 2018, at 9:00 am
in Conference Room 1 of the Legislative Council Complex**

Members present : Hon LAU Kwok-fan, MH (Chairman)
Hon Tanya CHAN (Deputy Chairman)
Hon Frankie YICK Chi-ming, SBS, JP
Hon YIU Si-wing, BBS
Hon CHU Hoi-dick
Hon Jimmy NG Wing-ka, JP
Hon Holden CHOW Ho-ding
Hon Tony TSE Wai-chuen, BBS

Member attending : Hon Jeremy TAM Man-ho

Members absent : Hon Abraham SHEK Lai-him, GBS, JP
Hon Claudia MO
Hon Steven HO Chun-yin, BBS
Hon MA Fung-kwok, SBS, JP
Hon CHAN Chi-chuen
Dr Hon Helena WONG Pik-wan
Dr Hon Junius HO Kwan-yiu, JP
Hon CHEUNG Kwok-kwan, JP

Public officers attending : Agenda item I

Mrs Cherry TSE LING Kit-ching, JP
Permanent Secretary for Home Affairs

Mrs Sorais LEE KWAN Siu-kuen, JP
Project Manager (Home Affairs Bureau)

Ms Alice PANG, JP
Project Manager (South)
Civil Engineering and Development Department

Attendance by invitation : Agenda item I

Mr Duncan PESCOD, GBS, JP
Chief Executive Officer
West Kowloon Cultural District Authority

Ms Suhanya RAFFEL
Executive Director, M+
West Kowloon Cultural District Authority

Mr Jeremy STOWE
Director, Project Control
West Kowloon Cultural District Authority

Mr Michael RANDALL
Senior Legal Counsel
West Kowloon Cultural District Authority

Clerk in attendance : Ms Doris LO
Chief Council Secretary (1)2

Staff in attendance : Miss Evelyn LEE
Assistant Legal Adviser 10

Mr Raymond CHOW
Senior Council Secretary (1)6

Ms Christina SHIU
Legislative Assistant (1)2

I M+ Main Works Contract

(LC Paper No. CB(1)1376/17-18(01) — West Kowloon Cultural District Authority's paper on M+ main works contract

LC Paper No. CB(1)1367/17-18(01) — Paper on the M+ project and the recent developments in relation to the M+ main works contract (Background brief))

Relevant papers

(LC Paper No. CB(1)1281/17-18(01) — Letter dated 16 July 2018 from the Chairman to the Chief Secretary for Administration

LC Paper No. CB(1)1333/17-18(01) — Letter dated 17 August 2018 from the West Kowloon Cultural District Authority on the M+ main works contract

LC Paper No. CB(1)1349/17-18(01) — Letter dated 21 August 2018 from Hon Tanya CHAN

LC Paper No. CB(1)1383/17-18(01) — Submission from Hsin Chong Construction Company Limited dated 7 September 2018 (Restricted to members))

The Chairman said that in the light of Hsin Chong Construction Company Limited ("HCC")'s request for its submission to be kept confidential, members were advised not to provide or make available the submission (or any part of it) or any copy of it to any party other than members of the Joint Subcommittee. However, HCC had given consent for members to raise questions at the special meeting based on the

submission and identify the source of the information upon which the questions were based.

(Post-meeting note: HCC provided a second submission which was tabled at the meeting/issued to members of the Joint Subcommittee under confidential cover.)

2. The Joint Subcommittee deliberated (index of proceedings in the **Annex**).

3. The Administration/the West Kowloon Cultural District Authority ("WKCDA") was requested to provide the following information:

- (a) the considerations of the Development Bureau for not removing HCC from the "List of Approved Contractors for Public Works" after HCC's employment under the M+ main works contract had been terminated by WKCDA;
- (b) the details, once available, of the impact of the termination of HCC's employment under the M+ main works contract on the works of M+, in particular the associated cost implications, together with an account of the claims from HCC and some subcontractors, and delay in the construction schedule taking into account the time required for the novation process, etc.; and
- (c) a copy of the general conditions of contract for building and civil engineering works of WKCDA.

(Post-meeting note: The supplementary information provided by the Administration/WKCDA was circulated to members vide LC Paper No. CB(1)131/18-19(01) on 2 November 2018.)

II Any other business

4. There being no other business, the meeting ended at 11:06 am.

Panel on Development and Panel on Home Affairs

**Proceedings of special meeting of the Joint Subcommittee to Monitor
the Implementation of the West Kowloon Cultural District Project
held on Tuesday, 11 September 2018, at 9:00 am
in Conference Room 1 of the Legislative Council Complex**

Time marker	Speaker(s)	Subject(s)/Discussion	Action required
Agenda Item I – M+ Main Works Contract			
000516-000829	Chairman	<p>Opening remarks</p> <p>The Chairman reminded the representatives of the West Kowloon Cultural District Authority ("WKCD") attending the meeting that they were not protected by the Legislative Council (Powers and Privileges) Ordinance (Cap. 382) for what they said at the meeting.</p>	
000830-003026	Chairman Administration WKCD	<p>Briefing by the Administration and powerpoint presentation by WKCD</p> <p>[LC Paper Nos. CB(1)1376/17-18(01) and CB(1)1385/17-18(01)]</p>	
003027-003656	Chairman Mr Tony TSE WKCD	<p>Mr TSE asked about:</p> <p>(a) when deciding to award the M+ main works contract to Hsin Chong Construction Company Limited ("HCC") in 2015, whether WKCD had considered the financial position of HCC with due regard to the correlation of which with the financial position of its parent company, Hsin Chong Group Holdings Limited ("HCG");</p> <p>(b) the circumstances that gave rise to the decision to terminate HCC's employment under the M+ main works contract; and</p> <p>(c) whether HCC should be held accountable for the delay in the M+ project.</p> <p>WKCD replied that:</p> <p>(a) WKCD had investigated the financial situation of both HCG and HCC before entering into the M+ main works contract with HCC in 2015, but there had been no indication that they had any financial issues;</p>	

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		<p>(b) the course of events that had eventually led to WKCDA's decision to terminate HCC's employment included the announcements HCG made to the stock exchange and its consequent implication on HCC, including HCG's announcement in May 2018 about the default on their US\$300 million 8.75% senior notes due 2018 ("2018 Notes") and the cross-default of its US\$150 million 8.5% senior notes due 2019 ("2019 Notes") to which HCC was a guarantor, etc.; and</p> <p>(c) due to HCC's deteriorating financial situation, in particular its cash flow, WCKDA made direct payments to the key subcontractors from February 2017 (hereinafter referred to as "direct payment arrangement") to ensure that the works continued. While the works delay remained substantial up to date, it was expected that it might be partly caught up as the new management contractor took over the project.</p>	
003657-004230	Chairman Mr Jeremy TAM WKCDA	<p>Mr TAM queried that, when responding to his enquiries relating to the financial position of HCC and the payment arrangements to the workers of its subcontractors at the Finance Committee ("FC") meetings on 8 December 2017 and 5 January 2018:</p> <p>(a) whether the Chief Executive Officer ("CEO") of WKCDA was lying to or misleading the Legislative Council ("LegCo") Members that all the workers were being paid on time; and</p> <p>(b) why CEO of WKCDA did not mention about the financial difficulties of HCG/HCC or the measures taken by WKCDA, such as the establishment of Blue Poles Limited ("BPL").</p> <p>CEO of WKCDA responded that:</p> <p>(a) he denied that he was a liar and he did not mislead the LegCo;</p> <p>(b) at the above FC meetings, he made it clear that he would not comment on the financial stability of a listed company (i.e. HCG), and WKCDA had aimed to ensure that the employees of both the contractor and the subcontractors were paid; and</p>	

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		<p>(c) the incorporation of BPL was a precautionary measure internally resolved to be taken for the purpose of protecting the interests of WKCDA.</p>	
004231 004750	Chairman Mr CHU Hoi-dick WKCDA	<p>Based on the submission from HCC (LC Paper No. CB(1)1383/17-18(01)) that was confidential and restricted to members of the Joint Subcommittee to Monitor the Implementation of the West Kowloon Cultural District Project ("Joint Subcommittee" only), Mr CHU asked whether:</p> <p>(a) the causes of the delay of the M+ project were mainly the responsibility of WKCDA, but not HCC, and involved the following issues: underground water at the site being in excess of that envisaged due to inadequate design, more than 180 000 design clashes being identified between the drawings and specifications, re-submission of plans to the Building Authority for approval due to revised designs, but the contract administrator failed to issue extension of time beyond the date for practical completion despite the submission of many notices by HCC; and</p> <p>(b) WKCDA had allegedly hacked into HCC's computer servers at the project site and retrieved information that was HCC's property as well as personal data of HCC's staff, but refused to halt accessing such confidential and personal information despite protestations from HCC.</p> <p>WKCDA indicated that it could not comment on the specific matters raised in HCC's submission that was not disclosed to WKCDA. WKCDA stressed that there were provisions under the M+ main works contract for contractor to submit claims for delay which were resolved by the independent Contract Administrator ("CA"). The actions taken by WKCDA to terminate HCC's employment under the M+ main works contract (including securing the project site and seizing of equipment at the site) was fully in accordance with the contract terms.</p>	
004751- 005330	Chairman Deputy Chairman WKCDA	<p>The Deputy Chairman enquired about:</p> <p>(a) whether BPL was limited by guarantee/by share;</p>	

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		<p>(b) the debenture arrangement for BPL; and</p> <p>(c) the progress of the novation process undertaken by BPL, i.e. the number of subcontractors engaged in the works of the M+ project and the number of novations agreed among them.</p> <p>WKCDA replied that:</p> <p>(a) while two to three other subsidiaries of WKCDA were companies limited by guarantee, WKCDA decided to set up BPL as one limited by shares given the shorter time required thereby such that BPL could be readily available in the event of failure of the main contractor;</p> <p>(b) debenture arrangement enabled WKCDA to have first priority of claims as the debenture holder in the event of liquidation of BPL, hence providing protection to the assets of WKCDA; and</p> <p>(c) about 30 subcontractors, including 14 to 15 major ones, were engaged in the M+ main works. BPL had started the novation process for selected subcontractors, excluding those which had already completed their works and those for some other reasons, with about 15 novations agreed so far.</p>	
005331-005940	Chairman WKCDA	<p>The Chairman was disappointed that WKCDA was acting in hindsight to terminate HCC's employment under the M+ main works contract only after implementing the direct payment arrangement for months. He opined that the decision making of WKCDA lacked transparency and was wavering, and he asked:</p> <p>(a) whether it was a dereliction of duty of WKCDA misjudging the financial situation of HCC;</p> <p>(b) whether and why, as HCC had claimed in its submission to the Joint Subcommittee, WKCDA rejected HCC's earlier proposals of entering into joint venture arrangement with other companies to continue taking forward the M+ project;</p> <p>(c) the progress of WKCDA in calling on the on-demand performance bond (at about</p>	

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		<p>\$297 million) procured by HCC as required under the M+ main works contract and provided by AIG Insurance Hong Kong Limited ("AIG"); and</p> <p>(d) whether and how WKCDA would claim against HCC for any additional cost incurred and works delay in respect of the M+ main works.</p> <p>WKCDA responded that:</p> <p>(a) it was not until May 2018 when HCG made an announcement on the default of 2018 Notes that the insolvency of HCC was irrefutably clear;</p> <p>(b) in light of HCG's statements about its attempts to secure potential investors, WKCDA implemented the direct payment arrangement from February 2017 until it became clear that no new investment to HCG could be secured; and</p> <p>(c) HCC was still unable to pay its subcontractors after WKCDA ceased the direct payment arrangement in July 2018, and failed to advance the project in line with the agreed timetable. WKCDA then decided to call and demand payment of the performance bond, and applied for the issue of a writ of execution. Given that legal proceedings were in progress, it was not appropriate for WKCDA to comment further.</p>	
005941-010624	Chairman Mr Holden CHOW WKCDA	<p>Mr CHOW asked why WKCDA was being passive and terminated HCC's employment under the M+ main works contract as late as in August 2018 despite having aware of its financial difficulties and implemented the direct payment arrangement for as long as 18 months. He also asked whether and when WKCDA had sought advice from external advisers on the actions to be taken.</p> <p>WKCDA advised that it had sought advice from external legal and financial advisers since October 2016 but WKCDA was not at liberty to disclose the details of the advice. WKCDA took the series of actions leading to the termination of HCC's employment based on the advice sought and the decision of the Board.</p>	

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		<p>The direct payment was a request from HCC and WKCDA believed that the direct payment arrangement was appropriate to allow the construction to continue at a very critical point when the trusses were still being erected.</p>	
<p>010625-011420</p>	<p>Chairman Mr Tony TSE WKCDA</p>	<p>Mr TSE asked about:</p> <ul style="list-style-type: none"> (a) the signs and indications that had led WKCDA to believe that HCG/HCC was in financial difficulties, hence the need for implementing the direct payment arrangement; and (b) the role and responsibilities of HCC and/or HCG in relation to the default on the M+ main works contract and any relevant claims made. <p>WKCDA replied that:</p> <ul style="list-style-type: none"> (a) HCG did not have a direct role under the M+ main works contract, which was between HCC and WKCDA. HCG's announcement in May 2018 about the default of the 2018 Notes and the cross-default on the 2019 Notes, of which HCC was a guarantor made the insolvency of HCC irrefutably clear. The chronology of events that had led to WKCDA's decision to terminate HCC's employment under the M+ main works contract was set out in Annex 1 to the Administration's paper (LC Paper No. CB(1)1376/17-18(01)); (b) an independent CA had been appointed to manage matters related to the M+ main works contract, including handling the claims made by HCC and its subcontractors; and (c) HCC was in dispute with WKCDA over the termination of its employment under the contract and the dispute would be resolved in accordance with the dispute resolution mechanism provided under the contract. 	
<p>011421-012814</p>	<p>Chairman Mr Jeremy TAM Assistant Legal Adviser 10 ("ALA10") WKCDA</p>	<p>Mr TAM enquired about:</p> <ul style="list-style-type: none"> (a) how substantial was the amount of payments HCC owed to its subcontractors, and whether the system of independent contract management of WKCDA had failed to check and avoid such substantial default payments; and 	

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		<p>(b) the amount of direct payments made by WKCDA to these subcontractors.</p> <p>WKCDA responded that:</p> <p>(a) WKCDA was not informed of the amount of payments HCC owed to its subcontractors under the contract terms. The system of independent contract management of WKCDA had been functioning well in ensuring the funding requests submitted by HCC based on the works carried out by the subcontractors were all checked and verified. Yet, HCC's failure to pay its subcontractors in a timely manner went beyond the scope of the system; and</p> <p>(b) WKCDA made direct payments of about \$1.609 billion in total to about 20 subcontractors.</p> <p>Mr TAM doubted why WKCDA did not know the amount of default payments by HCC to its subcontractors under contract terms, and requested for legal advice. On the suggestion of ALA10, the Senior Legal Counsel of WKCDA was invited to give further explanations.</p> <p>WKCDA further responded that:</p> <p>(a) WKCDA had previously made payments to HCC ranging from \$50 million to \$200 million each month in relation to the works carried out by the subcontractors, but WKCDA was not informed of the exact amount passed on to the subcontractors by HCC; and</p> <p>(b) at the request of WKCDA, HCC provided a list of subcontractors which they owed money. The new management contractor recently appointed by WKCDA would be tasked to ascertain the amount then owed.</p>	
012815-013516	Chairman Mr Holden CHOW WKCDA	<p>Mr CHOW asked about:</p> <p>(a) why WKCDA had not taken earlier action to terminate HCC's employment, knowing that HCC was a guarantor of the defaulted 2019 Notes; and</p>	

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		<p>(b) whether WKCDA had considered other options to enable continuation of the works of the M+ project, such as accepting HCC's proposals of entering into joint venture arrangement with other companies.</p> <p>WKCDA reiterated/added that:</p> <p>(a) WKCDA could only ascertain HCC's insolvency after the announcement of HCG in May 2018 about the default of their 2018 Notes; and</p> <p>(b) HCG/HCC had put forward at least three proposals regarding the possibility of bringing in new investment, but none of the proposals had materialized.</p>	
013517-015454	Chairman Deputy Chairman Administration WKCDA	<p>The Deputy Chairman enquired about:</p> <p>(a) whether HCC had put forward concrete proposals of entering into joint venture arrangement with other companies;</p> <p>(b) whether the ground for terminating HCC's employment due to its insolvency caused by the severe financial troubles of its parent company (i.e. HCG) could stand;</p> <p>(c) as it did not take long setting up BPL, why WKCDA still paid the subcontractors for 18 months, and whether such payments were by nature loans to HCC and if so, whether WKCDA was statutorily authorized to provide such loans;</p> <p>(d) whether WKCDA had withheld information about the critical events relating to the progress of the M+ works project, for example, it was not until June 2018 had WKCDA stated its press release that the M+ construction works had seen some slippage, and it had not mentioned about the cessation of the direct payment arrangement until a media stand-up on 17 July 2018; and</p> <p>(e) the considerations of the Development Bureau for not removing HCC from the "List of Approved Contractors for Public Works" after HCC's employment under the M+ main works contract had been terminated by WKCDA.</p>	Administration (paragraph 3(a) of the minutes refers)

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		<p>The Administration indicated that:</p> <ul style="list-style-type: none"> (a) the Home Affairs Bureau would relay the question regarding HCC's place on the "List of Approved Contractors for Public Works" to the Development Bureau for follow-up; (b) the role of public officers on the Board of WKCDA was to ensure that the actions taken by WKCDA were in the best interest of the WKCD project. The Board of WKCDA had considered terminating HCC's employment under the M+ main works contract in late 2016, but decided to put this on hold given that the insolvency of HCG/HCC was not evidenced and it would take about 6 to 8 weeks to secure a new management contractor thus leading to delay in the M+ project. Furthermore, HCG's auditors advised in 2016 and 2017 that the company's directors had undertaken measures to improve the liquidity and financial position of HCG; (c) having considered all the information available then, the Government was of the view that WKCDA had exercised due diligence to protect the interests of WKCDA, which included taking precautionary measures such as setting up BPL. While the financial solvency of a parent company would generally have an impact on its subsidiaries, it was inappropriate to take actions on HCC's employment simply based on media reports or unsubstantiated allegations; (d) the Government's main objective was for the construction of the WKCD project to be completed in good quality and timely manner. WKCDA had carefully considered HCC's proposals of entering into joint venture arrangement with other companies but did not accept the proposals upon conducting internal analysis. As potential new investors to the project failed to materialize, the Board of WKCDA eventually decided to terminate the HCC's employment under the M+ main works contract after thorough deliberation. <p>WKCDA responded that:</p> <ul style="list-style-type: none"> (a) a joint venture proposal of HCC suggested that 	

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		<p>the company entering into the agreement with HCC would subcontract the M+ main works to HCC. WKCDA considered this arrangement not feasible;</p> <p>(b) WKCDA had not made any advance payment to HCC or granted any loan to it. On the contrary, WKCDA had only made payments to HCC and its subcontractors based on the actual works done. When the direct payment arrangement was being implemented, WKCDA had closely reviewed the situation and made conscious decisions to continue the arrangement; and</p> <p>(c) members and the public had been kept informed of the target completion date of the M+ building in a transparent manner. The Joint Subcommittee was advised in February 2017 that the M+ building was targeted for completion by end 2018, and in November 2017 that the target completion date had been revised to 2019. Since February 2018, CEO of WKCDA had informed the Board members and the public of the WKCDA's concern over the progress of the M+ project during the open sessions of the Board meetings.</p>	
015455-015837	Chairman Mr Frankie YICK WKCDA	<p>Mr YICK asked about:</p> <p>(a) whether any extra payment was made under the direct payment arrangement; and</p> <p>(b) whether the process of appointing the new management contractor and novating the subcontractors had proceeded smoothly, as well as the cost implications on the project costs.</p> <p>WKCDA responded that:</p> <p>(a) the amount paid by WKCDA was based on the actual works carried out by HCC and its subcontractors. The funding requests were vetted by HCC first, and then checked and re-certified by the independent CA; and</p> <p>(b) WKCDA had quickly secured a management contractor to oversee the M+ project. As the management contractor was still assessing the</p>	

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		<p>additional costs, and it would take time for WKCDA to work out the payment arrangement with the subcontractors after novation, the final cost of the M+ main works could not be ascertained at this stage.</p>	
015838-020154	Chairman Mr CHU Hoi-dick WKCDA	<p>Mr CHU was concerned about:</p> <ul style="list-style-type: none"> (a) the impact on the progress of the M+ project in case HCC sought to reverse WKCDA's decision to terminate HCC's employment under the M+ main works contract; and (b) when WKCDA had put the dispute with HCC over the M+ main works contract to arbitration. <p>WKCDA reiterated/added that:</p> <ul style="list-style-type: none"> (a) Clause 73.1 of the general conditions of contract for building and civil engineering works of WKCDA provided that if the contractor became insolvent, WKCDA could terminate the contractor's employment under the contract. The actions taken by WKCDA to terminate HCC's employment was fully in accordance with the contract terms; and (b) the dispute with HCC would be resolved in accordance with the dispute resolution mechanism (including arbitration) set out in the M+ main works contract and the process might take a long time. As the contract provided that arbitration over the dispute on the contract could only be proceeded with after the completion of the M+ project, the arbitration process had not yet commenced. 	
020155-020843	Chairman WKCDA	<p>The Chairman asked:</p> <ul style="list-style-type: none"> (a) how WKCDA would judge and decide whether or not a matter should be reported to the Joint Subcommittee, and in hindsight, whether the Administration/WKCDA considered it more preferable reporting or making public about the direct payment arrangement at an earlier stage; and (b) whether WKCDA had taken proper steps to terminate HCC's employment under the M+ 	

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		<p>main works contract and secure the project site in August 2018.</p> <p>The Administration advised that:</p> <p>(a) WKCDA had been cautious in taking the series of actions that led to the termination of HCC's employment under the M+ main works contract, taking into account various factors and circumstances, including that any comments and actions might cause fluctuations in the share price of HCG and actions from their creditors, which might in turn give rise to litigation by HCG/HCC against WKCDA; and</p> <p>(b) it would be difficult for WKCDA to inform LegCo of its decisions much earlier than it had as information provided to LegCo would be released in the public domain before the insolvency of HCC was irrefutably clear and might trigger the aforementioned reaction carrying litigation risk for WKCDA.</p> <p>WKCDA added that:</p> <p>(a) the written notice of termination of HCC's employment under the M+ main works contract had been delivered to HCC's office by hand in an appropriate manner and in accordance with the terms of the contract; and</p> <p>(b) to protect its interests, WKCDA could not notify HCC in advance of its plan to take over the project site, but it had held a press conference to announce its decision to terminate HCC's employment as early as possible.</p>	
020844-021002	Chairman Deputy Chairman WKCDA	<p>The Chairman requested WKCDA to provide the details, once available, of the impact of the termination of HCC's employment under the M+ main works contract on the works of M+, in particular the associated cost implications, together with an account of the claims from HCC and some subcontractors, and delay in the construction schedule taking into account the time required for the novation process, etc..</p> <p>The Deputy Chairman requested WKCDA to provide a copy of the general conditions of contract</p>	WKCDA (paragraph 3(b) and (c) of the minutes refer)

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		for building and civil engineering works of WKCDA.	
Agenda Item II – Any other business			
021003- 021004	Chairman	Closing remarks	

Council Business Division 1
Legislative Council Secretariat
19 March 2019