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Finance Committee of the Legislative Council

**Notes of the Briefing
held at the Legislative Council Chamber
on Friday, 25 February 2005, at 4:45 pm**

Members present:

Hon Emily LAU Wai-hing, JP, Chairman of the Finance Committee (Convenor)
Hon Albert HO Chun-yan
Ir Dr Hon Raymond HO Chung-tai, S.B.St.J., JP
Hon Fred LI Wah-ming, JP
Hon Margaret NG
Hon James TO Kun-sun
Hon CHEUNG Man-kwong
Hon SIN Chung-kai, JP
Hon Howard YOUNG, SBS, JP
Hon Andrew CHENG Kar-foo
Hon TAM Yiu-chung, GBS, JP
Hon Abraham SHEK Lai-him, JP
Hon Tommy CHEUNG Yu-yan, JP
Hon Frederick FUNG Kin-kee, JP
Hon LEE Wing-tat
Hon Andrew LEUNG Kwan-yuen, SBS, JP
Dr Hon Fernando CHEUNG Chiu-hung
Hon TONG Ka-wah, SC
Hon Albert Jinghan CHENG

Public officers attending:

Miss Elizabeth TSE, JP	Deputy Secretary for Financial Services and the Treasury (Treasury) 1
Mr Alfred FOK	Principal Executive Officer (General), Financial Services and the Treasury Bureau (The Treasury Branch)
Mr Stephen FISHER, JP	Deputy Secretary for Home Affairs
Miss Esther LEUNG	Principal Assistant Secretary for Home Affairs

Mr Y S LEE

Chief Project Manager
Architectural Services Department

Clerk in attendance:

Ms Pauline NG

Assistant Secretary General 1

Staff in attendance:

Miss Becky YU
Mrs Mary TANG
Ms Caris CHAN
Mr Frankie WOO

Chief Council Secretary (1)1
Senior Council Secretary (1)2
Senior Legislative Assistant (1)1
Legislative Assistant (1)2

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Progress Report on the Centre of Youth Development Project

The Chairman said that the purpose of the briefing was for the Administration to apprise members of the latest proposal on the management and operation of the Centre of Youth Development (CYD) project as well as the related financial responsibility. Members were invited to express their views on the proposed management and operation mode but their views should not be regarded as the stance of the Finance Committee (FC).

2. Mr Tommy CHEUNG, Chairman of the Panel on Home Affairs (HA Panel), said that the proposal of adopting a Public Private Partnership (PPP) approach for operating and maintaining CYD under a single contract was discussed by the Panel. Youth organizations and interested parties were also invited to the special meeting held on 3 January 2005 to express views on the subject. While most of the deputations attending the meeting did not object to the CYD project, many of them considered it necessary for the Administration to provide further details to substantiate the propriety of the proposed PPP approach in taking forward the CYD project. Concerns were also raised on the ability of the single operator to coordinate with youth service providers on the future use of CYD and whether the latter could have fair access to the facilities in CYD. They asked how the performance of the operator would be effectively monitored and whether youth service providers could afford the rental charges of the facilities if CYD were to be run predominantly on commercial principles. To achieve youth development objectives, some deputations suggested that CYD should be operated by a non-profit youth organization experienced in youth development work. Consideration should also be given to relaxing the restriction that CYD should operate on a self-financing basis as this could increase the flexibility in drawing up an appropriate management and operation arrangement for CYD.

3. The Deputy Secretary for Home Affairs (DS(HA)) said that having regard to the views of youth organizations and the HA Panel, the Administration intended to adopt the following arrangements -

- (a) The Government would directly take up the responsibility of managing and operating CYD by funding the necessary recurrent expenditure. In other words, the Government would bear all commercial risks arising from the operation and management of CYD. In the event that CYD incurred an operating deficit, this would be covered through redeployment of resources under the operating expenditure envelope of the Secretary for Home Affairs (SHA).
- (b) In order to reduce the operating costs, the day-to-day management and operation of the CYD premises and the various facilities such as cafeteria and hostel would be contracted out to one or different service providers, depending on the market situation. The Government would collect all incomes generated from facilities/programmes and would be responsible for funding the recurrent expenses on the operation and maintenance of CYD, including the fees for the management services provided by the contractors.
- (c) The Government would administer the management contracts, as well as organize and co-ordinate youth development programmes in CYD.
- (d) The Government would continue to extensively consult youth organizations and the Commission on Youth (COY) on the objectives and contents of the youth development programmes in CYD.
- (e) A management advisory committee would be set up to advise the Government on the overall strategy and objectives of CYD, the themes and contents of youth development programmes, as well as the use and allocation, the leasing and charging arrangements of various facilities. The advisory committee would consist of representatives from Government bureaux/departments, non-governmental organizations (NGOs), youth organizations and other interested parties involved in youth development work. The advisory committee would regularly meet with COY and youth organizations to seek their views on matters relating to CYD.

DS(HA) said that the above arrangements had the support of youth organizations which agreed that CYD should be constructed, financed, operated and maintained by the Government on its own rather than a PPP approach.

4. Mr Albert CHENG noted that the CYD project had been a cause of controversy at the outset, in particular the setting up of a limited company to assume the responsibility for the management and operation of CYD on a self-financing basis. Nevertheless, funding for the capital works of the project had been approved. As the

economic situation had changed, the CYD project under the original management and operation mode was considered not sustainable and the Administration now proposed to take up the responsibility of managing and operating CYD by funding the necessary recurrent expenditure. Given that the new management and operation mode for CYD was substantially different from the original model, he could not support such changes, including those related to the project scope of CYD where video production and editing studios would be converted to retail area, dance studios to cafeteria and arts gallery to multi-purpose area etc. He considered that such changes were for commercial reasons and would change the nature of the project. They would indeed defeat the main purpose of the CYD project, that is, to serve as a focal point for territory-wide youth development activities in Hong Kong. His views were shared by Mr CHEUNG Man-kwong.

5. DS(HA) said that the need for CYD stemmed from the study on youth development conducted by COY in 1997 which recommended, among other things, the setting up of a central facility to provide a focal point for territory-wide youth development activities in Hong Kong. Youth organizations and NGOs also supported the provision of CYD. A site at the junction of Chai Wan Road and Wan Tsui Road (adjacent to the Chai Wan MTR station), which included the former Chai Wan Community Centre site plus its surrounding open space, was then identified for CYD. As regards the proposed revision of project scope of CYD, DS(HA) explained that this was to take account of the changing needs in youth development. According to a recent survey, many of the facilities originally proposed for CYD had already been provided for in different youth centres. In order for CYD to serve its purpose as a focal point for territory-wide youth development activities and to attract the critical mass, greater flexibility had to be provided for in the mix of facilities and equipment within CYD to cater for the changing demands in the market. Besides, the proposed multi-purpose areas could be easily converted back to the original facilities if needs arose.

6. Mr CHEUNG Man-kwong said that he was not opposed to the provision of CYD but to the use of public funding on a luxurious youth centre, which was to be completed with hostel and cafeteria, and the operation and management of which was to be taken up by a limited company on a self-financing basis. Under such mode of operation, the Administration would not be accountable to the Legislative Council (LegCo) for the performance of the operator. The limited company could make use of the profits generated from the operation of CYD in whatever means, thereby setting a dangerous precedent for future operation of publicly-funded projects. Nevertheless, the funding for CYD was eventually approved by FC. He said that it was no surprise to him that the initial self-financing operation model was considered financially non-viable as stated in the progress report. However, he was disappointed that the Administration was trying to downplay the proposed changes in the management and operation mode for CYD whereby Government would directly take up the responsibility of managing and operating CYD by funding the necessary recurrent expenditure, claiming that these were only minor changes. In fact, such changes were unusual and could be very substantial in nature, bearing in mind the Government's extent of responsibilities. He then enquired about the causes leading

to the changes and whether any parties should be held responsible for have made a wrong judgment on the initial mode for the management and operation of CYD.

7. Mr Tommy CHEUNG recapped the historical development of the CYD project, and highlighted that the approval given by FC for the construction of CYD under the Capital Works Reserve Fund (CWRF) in 2001 was made on the understanding that no recurrent expenditure would be incurred since CYD would be operated on a self-financing basis during the initial 10-year period. However, the outlook of CYD under the original financial assessment was much less optimistic as a result of the changes in the economic environment since 2001. Based on the original staffing and operating costs, CYD could incur a significant shortfall in recurrent expenditure over the first 10 years of operation if it were implemented according to the initial plan. The Administration consulted the Steering Committee in August 2003 and floated the idea of contracting out the management and operation rights of all the facilities of CYD. The Steering Committee had expressed concern about the possible domination of the use of the CYD by one single well-established organization, and decided to commission a consultancy study to review the project scope and to assess the feasibility of constructing, financing, operating and maintaining the CYD through an appropriate PPP approach. The findings and recommendations of the consultant were presented to the HA Panel at its meeting on 10 December 2004, during which youth organizations were also invited to express their views on CYD. The Eastern District Council (EDC) had also expressed views on the subject. The Administration had taken into account all these views and come up with the revised proposal that Government should directly take up the responsibility for managing and operating CYD by funding the necessary recurrent expenditure under SHA's envelope. In order to reduce the operating costs, it was suggested that some of the day-to-day management and operation of the CYD facilities such as hostel should be contracted out. Mr CHEUNG also declared interest as a member of EDC.

8. Mr Ronny TONG questioned why the Administration did not submit the changes to FC for approval. While he noted that the Legal Adviser (LA) of the Legislative Council Secretariat had given views on the matter, he considered that the principles of when the Government should seek FC's approval for changes to original approvals ought to be carefully examined. In this connection, the Chairman advised that to clarify this point, the Clerk had written to the Administration and to LA for additional information and advice. According to LA, the planned mode of management and operation of CYD and the use of its facilities were not part of FC's approvals for the capital costs of CYD. The Clerk supplemented that to assess the financial implications of the changes, the Secretariat had sought clarification on how the proposed changes would be funded. The Administration's explanation was that since the PPP approach no longer applied, CYD would be financed in the same way as other government-run facilities. The Government would seek recurrent funding in the context of the Appropriation Bill as and when required. In the light of LA's advice members might wish to consider whether, in future, important matters such as Government's recurrent financial liabilities should be specified as conditions or limitations in an approval given for funding capital projects under the public works programme which involved private sector participation.

9. Ms Margaret NG could not agree with LA's legal opinion. She said that FC's previous approvals for the project were made on the basis that CYD would be a self-financing project in its first 10 ten year of operation. The revised arrangement seemed to suggest that there would be deficits and the Government would be meeting the deficits through internal redeployment of resources. The new recurrent financial commitment had changed the basis of FC's earlier approvals. As the present case might set a precedent, she considered it necessary for FC to discuss how proposed changes made by the Administration to matters which formed the basis for FC's approval given to publicly-funded projects should be dealt with. Expressing similar concern, Mr Ronny TONG said that he would need to obtain more information about the proposed changes before deciding on the way forward.

10. DS(HA) said that according to a preliminary financial viability study carried out in 2000-2001, CYD should be able to remain financially sustainable during the first 10 years through incomes generated from the management of hostel and leasing of retail areas. The economic conditions in Hong Kong had gone through significant changes and in mid-2003, the updated financial assessment results indicated that the outlook was much less optimistic. Taking into account the latest views of the youth organizations and the Panel on Home Affairs regarding the Administration's previous proposal to manage CYD through a PPP approach, consideration had been given to relaxing the self-financing mode and allowing Government to directly manage and operate CYD instead.

11. Mr Ronny TONG questioned the basis upon which the financial assessment results made in 2003 was arrived at. He said that if funding approvals for the provision of CYD given by FC were based on wrong assumptions provided by the Administration, such approvals should no longer be valid. He added that the Administration should learn from this lesson and avoid making the same mistake in future, in particular when the public consultation on West Kowloon Cultural District Development Project was still underway.

12. DS(HA) said that the financial viability study conducted in 2001 was based on statistical figures around 1999 and 2000 which were very different from today's. In mid-2003, the Administration updated the financial assessment and the results indicated that the outlook was much less optimistic. The IBM Business Consulting Services was subsequently commissioned in early 2004 to conduct a study to review the project scope, and to assess the feasibility of constructing, financing, operating and maintaining CYD through an appropriate PPP approach. The purpose was to devise a model which could both effectively achieve the youth development objectives of CYD, and maintain CYD's financial sustainability. At members' request, the Administration undertook to provide reports of all the relevant studies on and details of the approval for the CYD project.

13. Mr CHEUNG Man-kwong opined that the initial management and operation mode might have constituted a transfer of benefits to a small group of people who wished to profiteer from the operation of CYD, which was a publicly-funded capital project. Given that the initial proposal was flawed from the start, remedial measures

had to be taken to rectify the situation. Hence, the Administration should account for the proposed changes to the CYD project. He also did not agree that approval need not be sought on grounds that the operation mode was not a condition for approval.

14. The Deputy Secretary for Financial Services and the Treasury (Treasury)1 (DS(Tsy)1) explained that under the existing mechanism, government capital works were funded under CWRF subject to approval by the Public Works Subcommittee (PWSC) and FC. Operating expenditure for them would be met by resources within the Government to be approved by FC on an annual basis in the context of the Appropriation Bill. As for the CYD project, while funding for the capital works under CWRF had already been approved by FC, funding for the operating expenditure would not be needed until nearer its completion which was expected to be included in the Appropriation Bill for the financial year of 2007-08. DS(HA) supplemented that under the original proposal, CYD would be operated and managed by a limited company through a team of staff employed under the terms and conditions similar to that of civil servants. Meanwhile, under the revised proposal, Government would directly take up the responsibility of managing and operating the CYD by funding the necessary recurrent expenditure. Efforts would be made to achieve full cost recovery but in the event of an operating deficit, this would be covered through internal redeployment of resources within SHA's envelope or by seeking public donations.

15. Mr Fernando CHEUNG expressed concern that the Administration had failed to take heed of members' concerns. The present case reflected a series of misjudgements which needed to be remedied. It was not possible to scrap the project at this stage as the piling and basement works for CYD had already been completed. Any changes in land use of the site would incur additional resources to reinstate the site to its original form. Meanwhile, a sum of \$200,000 a month had to be paid to the contractor for the purpose of maintaining the site in proper conditions. Besides, there was a need to provide a replacement for the Chai Wan Community Centre in the Eastern District which had been demolished to give way to CYD. Given the constraints and the opportunity costs that would be involved, there was no turning back and the CYD project had to proceed. However, the Administration should endeavour to increase the transparency in the management and operation of CYD and to regularly report progress to LegCo.

16. The Chairman asked if the site could be put up for land auction at its present form as one of the conditions of the land grant, thereby obviating the need for the resources to reinstate the site. DS(HA) said that one of the constraints of the site was that there would be a turnaround of MTR within CYD making it unsuitable for other land uses. Furthermore, approval from the Town Planning Board had to be sought if there was a change of land use. Besides, public expectation on CYD as a focal point for youth and replacement for the former Chai Wan Community Centre could not be met.

17. As regards the progress on the tender for the superstructure works, the Chief Project Manager, Architectural Services Department, by making reference to the supplementary information tabled at the meeting, explained that tender for the

superstructure works was invited on 2 May 2003. He said that the tender validity date which was originally scheduled to expire on 24 October 2003 had been extended several times until 1 May 2005. The number of tenders had been reduced from seven to five as two of them had declined to extend the tender validity period. The Architectural Services Department (ASD) Tender Price Index had been dropped from 723 in the second quarter of 2003 to 705 in the second quarter of 2005, representing a decrease of 2.49%. He assured members that the reduction in Tender Price Index would not affect the quality of works, and that ASD would review the necessity to negotiate with the contractors for a lower tender price for CYD in view of the adjustment in Tender Price Index.

Lessons learnt

18. Mr CHEUNG Man-kwong said that the public welcomed the development of youth centres and funding should not be a problem if it had followed the established practice. The Administration should have learnt a hard lesson from the present case where some non-subvented organizations tried to bypass the usual funding mechanism under COY to manipulate proceeds from the operation of CYD to subsidize their own activities. It should avoid making the same mistakes in future and should adhere to the established mechanism. DS(HA) admitted that the Administration might have relied too heavily on the original financial assessment made by the consultant that CYD could be operated on a self-financing basis. In future, findings of assessment would be subject to further examination.

19. Mr Fernando CHEUNG asked if the Administration would consider specifying, in future PPP projects, both the capital commitment and recurrent implications in the proposal statement of each paper for approval by FC. In this way, any changes to the approval statement would require further approval by FC. DS(Tsy)1 said that there could be different forms of private sector participation but where a works project involved the private sector financing the construction works and Government paying for such and for the future running of the project on a recurrent basis, the Administration was indeed inclined to sort out the full financial implications in clear terms and to seek FC's approval as appropriate. She however clarified that CYD was not a typical "private financing initiative" and was in fact quite uncommon. Mr CHEUNG Man-kwong took a different view. He pointed out that it was not uncommon for the Government to make loans to institutions such as the Hong Kong Polytechnic University for the construction of premises to conduct sub-degree courses. As institutions were expected to operate these courses on a self-financing basis, they might not be able to repay the loans if they had difficulties in recruiting sufficient students, particularly when the demand for sub-degree courses was declining. The problem of non-viability would recur.

The way forward

20. The Chairman sought members' views on whether there was a need for the Administration to seek FC's approval for the proposed changes to the management and operation of CYD, and whether a further meeting should be held to follow up on

the subject. Mr CHEUNG Man-kwong said that members would not object to the construction of CYD, but the Administration would need to account for the changes. Mr Ronny TONG said the Administration should provide more information, such as exchanges of correspondences and undertakings between the Government and the relevant youth organizations regarding the initial proposal on CYD, to facilitate understanding on the subject. He also agreed to hold another meeting.

21. DS(HA) responded that there were no exchanges of correspondence with youth organizations on the provision of CYD. The provision of CYD was included in the 1998 Policy Address. While the Administration would be pleased to provide the consultancy reports and to account for the changes as requested by members, he would have to seek clarification on the need to seek FC's approval. He reminded members that in the event the CYD incurred an operating deficit, this would be met by internal redeployment within SHA's envelope. Mr CHEUNG Man-kwong was not convinced that it was not due to the consideration of the interest of certain groups that the Government had decided to proceed with CYD. He recalled that there were two youth organizations which had indicated interest in operating CYD. The deliberations on the subject were clearly set out in the verbatim transcript of the PWSC meeting on 16 June 1999. He considered that the subject should be followed up at a future FC meeting.

22. As regard the anticipated operating deficit under the proposed management and operation mode, DS(HA) said that with the contracting out of the day-to-day management and operation of CYD premises and its various facilities, the operating costs could be much reduced and the estimated annual operating deficit of around \$2 million could be absorbed within SHA's envelope. DS(Tsy)1 clarified that all relevant project expenditure on CYD, be it capital or recurrent in nature, and whether absorbed within SHA's envelope, would be subject to the scrutiny and approval of the Legislature under CWRF or through passage of the Appropriation Bill. Recurrent expenditure for CYD for meeting deficits incurred under the proposed mode of management and operation was expected to be included in the Appropriation Bill for 2007-08.

23. In response to the Chairman's question on whether FC could require the Government to submit the proposed changes for approval, the Clerk clarified that it was Government's responsibility to take the initiative. Any proposed changes which would involve the expenditure of public funds not already approved by LegCo or FC ought to be submitted to FC for approval. She also pointed out that although the Government might be able to absorb the recurrent costs through internal redeployment of resources, the new expenditure would still have impact on the Approved Estimates. In relation to the proposed changes to the CYD project mentioned by the Administration, it had the obligation to explain to members the extent of the financial commitment resulted from these changes was likely to be. Such information would enable members to assess whether the proposed changes were significant or not. Given that details of recurrent expenditure of CYD were expected to be included in the relevant head of expenditure in 2007-08, the Administration might consider providing a forecast of the funds expected to be redeployed from SHA's current

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expenditure envelope at this stage without having to wait till the introduction of the Appropriation Bill in 2007-08.

24. At the request of members, the Chairman agreed to hold a special meeting on 11 March 2005 to continue discussion on the CYD project.

(*Post-meeting note:* As the Administration had to seek legal advice on whether FC's approval was required for the proposed management and operation mode for CYD, the meeting on 11 March 2005 had been postponed to 18 March 2005.)

25. The meeting was adjourned at 6:20 pm.

Legislative Council Secretariat

17 March 2005