

For information

July 2015

**Legislative Council Panel on Transport
Subcommittee on Matters Relating to Railways**

**Hong Kong Section of the
Guangzhou-Shenzhen-Hong Kong Express Rail Link
Revised Programme to Complete and Cost to Complete**

INTRODUCTION

On 30 June 2015, the Government received the review results of the MTR Corporation Limited (“MTRCL”) regarding the revised Programme to Complete (“PTC”) and revised Cost to Complete (“CTC”) of the Hong Kong section of the Guangzhou-Hong Kong-Shenzhen Express Rail Link (“XRL”) project. This paper sets out the Government’s initial responses.

BACKGROUND

2. In May 2014, MTRCL proposed the PTC with commissioning of the XRL by end 2017. The Highways Department (“HyD”), with the assistance of its monitoring and verification (“M&V”) consultant, has completed its review on MTRCL’s proposed PTC. HyD considers that the PTC with commissioning by end 2017 could be attained provided that the target progress is met for the critical contracts and various major conditions¹ are satisfied. HyD notified the MTRCL of its assessment in writing on 23 October 2014. In the meantime, HyD continued to

¹ These conditions include whether the respective contractors had made their best endeavours in implementing the works; whether various assumed production rates have been met persistently, etc.

monitor closely how MTRCL followed up the issues raised by HyD which required attention in order for MTRCL to achieve the target of commissioning the XRL by end 2017.

3. In our quarterly report on the progress and financial situation of the construction of the Hong Kong section of the XRL for the period ending 31 March 2015 (“First Quarter Report”) (LC Paper No. CB(4)954/14-15(07)), we reported that according to information from MTRCL, the overall progress of the Hong Kong section of the XRL was 68.7% as at the end of March 2015, indicating a delay when compared to the planned progress of 73.7% in the PTC with commissioning by end 2017. Based on the progress figures in the first quarter of 2015, the overall delay of works has worsened and reached a very critical state. HyD was highly doubtful on whether MTRCL could achieve the target for commissioning of XRL in end 2017 and considered that there might be further delay. From March 2015 to May 2015, delay persisted and there was no improvement. As of end May 2015, the overall progress of the Hong Kong section of the XRL was 70.4%, indicating a delay of 5.8% when compared to the planned progress of 76.2%, or a further delay of 0.8% compared with the overall progress as at end March 2015 (5% delay).

4. As regards the overall project cost estimate, the Government received a letter from MTRCL on 24 July 2014 informing the Government that the CTC for the Hong Kong section of the XRL was \$71.52 billion. MTRCL also announced the CTC on 11 August 2014. Based on the information provided by MTRCL at that time and with the assistance of the M&V consultant, HyD had completed the assessment of MTRCL's CTC. Based upon this assessment², HyD and its M&V consultant considered MTRCL's CTC of \$71.52 billion tended to be on the low side. HyD also noted the second report of the MTRCL IBC reported a similar conclusion reached by its own appointed experts.

² HyD and its M&V consultant, in their assessment, identified certain items which had not been included in the CTC or which would need to be reviewed to ensure adequate coverage in the risk allowances.

HyD urged MTRCL in November 2014 to review again the CTC in view of HyD's review findings and the reports of the MTRCL IBC, and to advise how the identified items which had not been included in the CTC would be addressed and allowed for.

5. In the First Quarter Report, we reported that MTRCL is reviewing the PTC and CTC. In addition, MTRCL earlier on indicated that the CTC "may be revised significantly upwards". MTRCL planned to submit its revised PTC and CTC, as well as the associated details, to the Government within the second quarter of 2015. The revised PTC and CTC would first have to be confirmed by the MTRCL Board before submitting to the Government.

6. On 30 June 2015, the Government received the notification letter from MTRCL informing the review results of MTRCL regarding the revised PTC and revised CTC of the Hong Kong section of the XRL project. As requested by the Government, MTRCL submitted a paper the Subcommittee on Matters Relating to Railways ("RSC") to report the review results on the same day.

REVISED PTC AND CTC OF THE XRL

7. According to the MTRCL's latest assessment, the commissioning of the Hong Kong section of the XRL will have to be delayed further from the end of 2017 to the third quarter of 2018, which includes a 6-month contingency period. As regards the CTC, the MTRCL advised that the amount will have to be revised to \$85.3 billion, which includes a Revised Total Project Cost of \$83.2 billion and a sum of \$2.1 billion for contingency.

GOVERNMENT'S INITIAL RESPONSES

8. The Government has grave concern about the further delay and cost overrun of the Hong Kong section of the XRL. The latest CTC of \$85.3 billion submitted by MTRCL is 31.23% more than the January 2010 original entrustment fee of \$65 billion, and 19.3% more than

MTRCL's revised CTC of \$71.5 billion announced last August, just a year ago.

9. Although we understand that major infrastructure projects may face different kinds of challenges or unforeseen difficulties, the Government is of the view that MTRCL, being the entrusted project manager of the Hong Kong section of the XRL project, bears the greatest responsibility and duty to control project cost and manage risks. It has to fulfill its role in supervising and coordinating its various contractors, spare no efforts in cost control and completing the project as scheduled.

10. The Government has serious concern about the drastic deviations of the project from the original commissioning schedule and approved funding. We will critically examine the performance of MTRCL as the project manager and look into its responsibility for project delay and cost overrun.

11. HyD's initial responses to the paper MTRCL submitted to the RSC on 30 June are set out in the following paragraphs.

(i) MTRCL has not in its paper carried out an analysis and given an account of the liability issues on the programme delay and cost overrun. In fact, the major causes of delay as mentioned in the MTRCL's paper including the challenges brought by the tunnel boring machines, fast-tracked front end, design variations, low production rates, etc. are all related to the liability issues of MTRCL as the project manager, its design consultants and/or contractors. We consider that ascertaining the liabilities of the major stakeholders of the project, including MTRCL, its design consultants and contractors, in the programme delay, cost overrun and contractors' claims in accordance with the contracts is very critical for the Government to assess and secure adequate funds to take forward the project.

(ii) MTRCL has mentioned in its paper that a contingency of \$2.1 billion is allowed on top of the Revised Total Project Cost of \$83.2 billion to account for future risks and uncertainties. According to

the experience in implementing large scale projects, and particularly in view that the XRL works has been more than 70% completed, we consider that a majority of the risks, especially those related to ground conditions, design and construction sequence etc., have become clear and materialized, and that the Revised Total Project Cost of \$83.2 billion should have allowed funds to account for these materialized risks. As such, MTRCL should explain the details of this contingency amount, and the risks, the uncertainties and the unclear factors this contingency amount is to account for. In the absence of this information, we have reservation on the reasonableness of the contingency of \$2.1 billion.

- (iii) Similar to (ii) above, MTRCL has not in its paper explained the risks, the uncertainties and the unclear factors the contingency time of 6 months is to account for. We also have reservation on the reasonableness of the contingency time of 6 months. MTRCL, as entrusted by the Government as the project manager for the XRL Project, bears the greatest responsibility and duty to manage and control the project cost, and complete the project on schedule. As such, MTRCL should review the future risks and uncertainties in details, put in place a comprehensive risk management plan to mitigate these risks, and use its best endeavors to avoid the use of the proposed contingency amount and time.
- (iv) MTRCL should be clearly aware the basic conditions to be met in order to achieve the target completion date, including the need for MTRCL and its contractor to use best endeavors to implement the project in accordance with the Entrustment Agreements. Since May 2014 when MTRCL revised the target completion date to end 2017, there has been persistent delay and the difference between the actual progress and the planned progress based on the PTC with commissioning by end 2017 has been ever-increasing. In scrutinizing the latest review results submitted by MTRCL, we will ascertain whether MTRCL and its contractors have continued to use their best endeavors to deliver the remaining critical and other works of the XRL project. In processing the contractors' claims, MTRCL will have to demonstrate that it has used its best endeavors to protect

the best interests of the Government as the entrusted party of the project.

NEXT STEP

12. HyD, assisted by its M&V consultant, will critically scrutinise MTRCL's review results, and will not accept any revised project completion date and cost estimate without substantiation. As for the revised CTC submitted by MTRCL, we will critically assess the basis of the underlying assumptions of the figure, including the \$2.1 billion for contingency, in accordance with the established practice in assessing Government's public works projects. Upon completion of review, we will report the outcome to the public and the Legislative Council as soon as possible.

13. The above-mentioned review of MTRCL's revised CTC only focuses on the engineering estimate of the cost required to complete the whole XRL project. Apart from that, obligations regarding project cost overrun will have to be ascertained. The Government will assess MTRCL's obligations regarding project implementation, works delay and project cost overrun, and will reserve all the rights to pursue the warranties and obligations from MTRCL.

Transport and Housing Bureau
Highways Department
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