For discussion
on 24 March 2017

FCR(2016-17)87

ITEM FOR FINANCE COMMITTEE

HEAD 186 – TRANSPORT DEPARTMENT
Subhead 700 General non-recurrent
New Item "Provision of Special Helping Measures for the Six Major Outlying Island Ferry Routes"

Members are invited to approve a new commitment of $412,140,000 for the continued provision of special helping measures for the six major outlying island ferry routes in the next three-year licence period (i.e. from mid-2017 to mid-2020).

PROBLEM

We need to continue to provide special helping measures (SHM) for the six major outlying island ferry routes[1] in the next licence period (i.e. from mid-2017 to mid-2020), to maintain the financial viability of the ferry services and alleviate the burden of fare increases on passengers.

/PROPOSAL …..

[1] Routes operated by the New World First Ferry Services Limited (NWFF):
(1) "Central – Cheung Chau";
(2) "Inter-islands" between Peng Chau, Mui Wo, Chi Ma Wan and Cheung Chau ; and
(3) "Central – Mui Wo" routes.

Routes operated by the Hong Kong & Kowloon Ferry Holdings Limited (HKK)'s three subsidiaries:
(4) "Central – Peng Chau";
(5) "Central – Yung Shue Wan"; and
(6) "Central – Sok Kwu Wan" routes.

PROPOSAL

2. The Commissioner for Transport, with the support of the Secretary for Transport and Housing, proposes to create a new commitment of $412,140,000 for the continued provision of SHM for the six major outlying island ferry routes during the new licence period starting from 1 April/1 July 2017[2].

JUSTIFICATION

Purposes and Effectiveness of SHM

3. It is the Government's established policy that public transport services should be run by the private sector in accordance with commercial principles to enhance efficiency and cost-effectiveness. There is basically no direct subsidy from the Government for public transport services save for the six major outlying island ferry routes. The Government provides SHM to these routes, because there is basically no alternative to the ferry services as a means of public transport[3], and short of the SHM, the ferry services cannot be maintained without periodic hefty fare increases. The SHM maintains the financial viability of the ferry services and alleviates the burden of fare increase on passengers.

4. The SHM was first launched in 2011 with funding approval from the Finance Committee (FC) of the Legislative Council (LegCo) on a three-year cycle, tying in with the three-year validity of a ferry service licence. For the licence period from mid-2011 to mid-2014, reimbursement made under the SHM was about $112 million, covering about 10% of the total operating costs of the six major outlying island ferry routes. For the current licence period from mid-2014 to mid-2017, FC approved a commitment of around $190 million in 2013 to provide the second round of the SHM for the six major outlying island ferry routes, also for a period of three years. Details are set out at Enclosure 1.

Encl. 1

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[2] The existing licence of "Central – Mui Wo" route will expire on 31 March 2017; the licences of the remaining five routes (i.e. "Central – Cheung Chau", "Inter-islands", "Central – Peng Chau", "Central – Yung Shue Wan" and "Central – Sok Kwu Wan") will expire on 30 June 2017. The new/extended licence for "Central – Mui Wo" route will start from 1 April 2017 and those for the remaining five routes will start from 1 July 2017. The licence period for all the six routes is three years.

[3] Only Mui Wo is also linked by an external road network, but its cross-district land-based public transport services are very limited.

5. For the 2011-14 licence period, with the assistance of the SHM, the weekday adult single journey and monthly ticket fares of the six major outlying island ferry routes were increased by about 10% and 7% respectively. For the 2014-17 licence period, the weekday adult single journey and monthly ticket fares of the six routes were increased by about 5% to 6% respectively in mid-2014[4]. Without the SHM, the rates for the two fare increases could have been as high as about 20% to balance the books of the operators. Judging from the above, the SHM has achieved the intended purpose of maintaining the ferry services while lowering the fare increase rates and alleviating the burden on passengers.

6. In early 2016, the two incumbent operators of the six major outlying island ferry routes (i.e. NWFF and three subsidiaries of HKK) approached the Transport Department (TD) for applying for licence extension. The Government consulted the LegCo Panel on Transport (the Panel) on this in April 2016. The Panel noted the operating difficulty of ferry services, and that there were not many service providers available in the market. The Panel also noted the experience that there had been no new service provider submitting bids[5] when the Government conducted the open tender for the operating right of the ferries. Taking these into account, to ensure a smooth continuation of ferry services when the current licence period expires in mid-2017, the Panel supported the Government to enter into direct negotiation with the two operators to discuss the terms of licence extension.

The Need for Continued Provision of the SHM in the Next Three-year Licence Period (2017-20)

7. The existing licences of the six ferry routes will expire in mid-2017. Based on the financial data of the first operating year, it is anticipated that the existing provision of $190,359,000 under the SHM should be exhausted within the current licence period. Based on the revenue and cost situation in the first two years (i.e. 2014-15) of the current licence period and the industry outlook (including the projections of patronage, oil price, wages and other operating costs in the coming three-year licence period (i.e. 2017-20)), we have conducted an assessment on the financial performance of the six outlying island ferry routes in the next licence period. The assessment results show that without the SHM and fare increase, the NWFF and HKK would suffer a significant financial loss in the

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[4] Not yet taking into account the time-limited and one-off fare concession subsequently offered by the two operators due to "profit-sharing" (please refer to footnote 9 for details).

[5] When the TD conducted the open tenders for the six major outlying island routes in 2007-08 and 2011, only the NWFF and the subsidiaries of HKK submitted bids.

next three-year licence period 2017-20. To achieve breakeven alone, a substantial fare increase of around 30% would be needed for the two operators. To moderate the fare increase, there is clearly a case for continued provision of the SHM and the subsidy amount will also need to be suitably adjusted upwards due to the increase in costs.

8. We have examined the scope of the SHM. To encourage the operators to introduce new vessels or improve services, facilities or equipment, we now propose the addition of a new item, to reimburse the depreciation expenses of the abovementioned capital investments. The depreciation costs should only be reimbursed by half, having considered that the ownership of assets with depreciation cost subsidy would rest with the operators. Based on the current information, the operators have already planned to introduce two new vessels and a series of ferry fleet upgrading projects in the next licence period (such as replacement of air-conditioning and ventilation systems and refurbishment of passenger cabins/washrooms).

9. The SHM is intended to maintain the financial viability of the ferry services and alleviate the burden of fare increase on passengers. Despite the continued provision of SHM by the Government, the ferry operators express that there has been pressure for fare increase, owing to the substantial increase in operating cost, particularly the significant pay rise of ferry crew members in recent years. Therefore, when the two ferry operators applied for licence extension, they requested for a fare increase of about 10% upon the commencement of the new licence period. After careful consideration, fares of the six routes would be increased by an average rate of around 4%[6], which would take effect on commencement of the new licence period. In other words, the new fares will take effect gradually[7] along the commencement date of the licence period of the six routes in mid-2017, which would be three years from the last fare increase in 2014 (fare increase rates were around 5% to 6% at that time). The proposed fare increase rate is lower than the projected cumulative increase in the Composite Consumer Price Index (7.4%) in the current licence period (i.e. during the period from July 2014 to June 2017).

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[6] Having considered the different patronage and operating modes of the six routes, as well as the different financial situations of the two ferry operators, the Government intends to approve an overall average fare increase of around 3.9% for "Central – Cheung Chau", "Inter-islands" and "Central – Mui Wo" routes operated by the NWFF while the overall average fare increase rate for the "Central – Peng Chau", "Central – Yung Shue Wan" and "Central – Sok Kwu Wan" routes operated by the HKK is around 4%.

[7] Except for the "Central – Mui Wo" route of which the licence after extension will take effect from 1 April 2017, the licences of the other five routes will be effective from 1 July 2017 after extension. The licence duration of the six routes is of three years.

10. We have projected the various major items of operating costs (including fuel, staff cost, repairs and depreciation, etc.) and farebox revenue, non-farebox revenue and the SHM proposed in paragraph 12 below for the two ferry operators in the next three-year licence period. Having regard to these projections, the projected profit margin for the NWFF is around 6.0%, while that for the HKK is around 6.2%, which are lower than the actual profit margin in the first licence period[8] and that in the first 18 months of the current licence period[9]. The projected profit margins are overall projection for the entire three-year licence period rather than on an annual basis. In projecting the profit margins, we have also taken into consideration the impact of the fare increase and SHM starting from the commencement of the licence in 2017 on operation. It should be noted that, the above projected profit margins are only for drawing up the implementation details of the SHM during the licence extension, processing fare increase applications and working out the profit-sharing mechanism for the next licence period. The projections concerned are neither guaranteed profit nor profitability caps. Instead, they are a projection tool for assessing the financial viability of the operations.

11. In early 2016, the Government conducted a mid-term review on the provision of SHM for the six major outlying island ferry routes in the current licence period (2014-17) and set up a profit-sharing mechanism. Under the mechanism, the operators would share any "windfall profit" (i.e. the profit exceeding the projected profit margin at the time of licence extension) with passengers on a 50:50 basis through offering fare concession. The same profit-sharing mechanism will be applicable to the next licence period 2017-20, which will share the "windfall profit" earned in the first half of the licence period with passengers on a 50:50 basis in the second half of the licence period, while the "windfall profit" earned in the second half of the licence period will be shared with passengers on a 50:50 basis in the next licence period.

/**Proposal** …..

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[8] The profit margin of the NWFF and HKK in the first licence period (2011-14) was 7% and 8.1% respectively.

[9] In the first 18 operating months of the current licence period, the two operators benefitted from oil price adjustment and recorded respectable profits exceeding the original projections. After negotiation between the Government and the operators, the two ferry operators agreed to share "windfall profit" with passengers on a 50:50 basis through a time-limited and one-off fare concession. The amount of fare concession concerned is around $22 million. The fare concession is to reward to passengers the entire amount attributed to the profit sharing, under a 50:50 basis. The two ferry operators both offered an overall fare concession of around 10-20% off for around half a year for the various routes. The actual profit margin for the first 18 months of the current licence period (after sharing with passengers the "windfall profit") was around 7.5% and 13.5% for the NWFF and HKK respectively.

Proposal

12. Considering the financial projections of the ferry operators, the SHM subsidy and an average fare increase rate of around 4%, the funding required for the SHM for the next three-year licence period would be around $340 million. In line with the practice in the current licence period, a buffer of 20% would be budgeted for contingency, and therefore bringing the SHM amount up to $412,140,000 (see paragraph 16 below for details).

13. The SHM will be implemented through the reimbursement of actual expenses of designated items (items set out in paragraph 16 below). Operators will be required to submit audited financial statements to the TD at the end of each financial year for substantiating the actual expenditure incurred. In addition, they are also required to submit their quarterly management accounts so that the TD can monitor their financial position. Besides, we will conduct a mid-term review during the three-year licence period.

14. The SHM amounts to around $190 million (with the 20% contingency funding included) for the current licence period. The substantial increase in the SHM sum is attributable mainly to the introduction of the new item of reimbursing half of the depreciation expenses under the SHM, the substantial increase in repair and maintenance cost, the increase in other costs that could be reimbursed under the SHM, and the increase in contingency provision in proportion to the total, now expanded, SHM amount required. In other words, apart from creating the new depreciation expense item, this increase in subsidy mainly seeks to meet escalating operating costs so as to alleviate the fare burden on passengers. Details are at Enclosure 2. SHM reimbursement is subject to actual usage and TD would carefully verify invoices to avoid abuse.

Encl. 2

Maintaining the Long-term Financial Viability of Outlying Island Ferry Service

15. The Government first introduced the SHM arrangement for the six major outlying island ferry routes in 2011. The next three-year licence period (i.e. 2017-20) is the first time where the Government subsidises operators' depreciation expense to encourage the operators to introduce new vessels and upgrade facilities or equipment, and the Government will also formally incorporate the profit-sharing mechanism into the terms of licence extension of the ferry services. It will take time to see what the actual effectiveness of the above new arrangements will be in enhancing ferry service and maintaining the long-term financial viability of ferry service. We will look into this in a holistic

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manner in the next mid-term review (in the first half of 2019). At that time, the Government will review in one go whether the currently proposed SHM would be the most desirable long-term operation model for maintaining the service quality and financial viability of ferry services. Details of relevant issues are in Enclosure 3.

Encl. 3

FINANCIAL IMPLICATIONS

Non-recurrent Expenditure

16. We estimate the expenditure of providing the SHM for the six major ferry routes to be $412,140,000 in the next three-year licence period, with the breakdown as follows –

		2017-18 $'000	2018-19 $'000	2019-20 $'000	2020-21 $'000	Total $'000
(a)	reimbursing the operators of the ferry services concerned for the annual vessel survey fee and private mooring charge	154	510	526	356	1,546
(b)	reimbursing the pier electricity, water and cleansing charges	1,652	5,448	5,614	3,798	16,512
(c)	reimbursing the balance of revenue foregone due to provision of elderly fare concessions after netting off the amount of pier rental reimbursement and vessel licence fee exemption under the established arrangement	3,515	11,598	11,950	8,084	35,147
(d)	reimbursing the vessel maintenance cost	24,044	79,344	81,749	55,301	240,438

		2017-18 $'000	2018-19 $'000	2019-20 $'000	2020-21 $'000	Total $'000
(e)	reimbursing the revenue foregone due to provision of child fare concessions	2,149	7,093	7,308	4,943	21,493
(f)	reimbursing the vessel insurance cost	910	3,003	3,094	2,093	9,100
(g)	reimbursing the depreciation cost of vessel and fleet improvement	1,620	5,345	5,506	3,725	16,196
(h)	implementing "Visiting Scheme to Outlying Islands"	302	996	1,026	694	3,018
(i)	**Estimated Commitment [Total of (a) to (h)]**	34,346	113,337	116,773	78,994	343,450
	Total Commitment including a 20% Buffer Provision [i.e. 120% of (i)]	**41,215**	**136,004**	**140,128**	**94,793**	**412,140**

17. On paragraph 16(a) above, the estimated expenditure of $1,546,000 is for reimbursing the ferry operators for the annual vessel survey fee and private mooring charge during the next licence period. The estimated expenditure is the anticipated actual fee level of these items.

18. On paragraph 16(b), (d) and (f) above, the estimated expenditures of $16,512,000, $240,438,000 and $9,100,000 are for reimbursing the ferry operators for the pier electricity, water and cleansing charges, vessel maintenance cost and vessel insurance cost. The estimated expenditures are financial caps derived from the projected expenses of the ferry operators in the next three-year licence period, with reference made to the actual expenses of the six ferry routes in the first 18 months of the current three-year licence period and the projected changes in the Composite Consumer Price Index.

/19. …..

19. On paragraph 16(c) and (e) above, the estimated expenditures of $35,147,000 and $21,493,000 are for reimbursing the ferry operators for the revenue foregone due to the provision of elderly and child fare concessions. The estimated expenditures are financial caps derived from the projected patronage of the six ferry routes in the next licence period, taking account of the fare adjustment mentioned in paragraph 9 above and the total actual revenue foregone of the six ferry routes owing to the provision of elderly and child fare concessions. Reference has also been made to the patronage in the current three-year licence period.

20. On paragraph 16(g) above, the estimated expenditure of $16,196,000 is for reimbursing the ferry operators for half of the depreciation expenses they incurred in introducing new vessels or capital items for improving services, facilities or equipment. The estimated expenditure is derived from the ferry operators' plans of introducing new vessels or improving their fleet in the next three-year licence period.

21. On paragraph 16(h) above, the estimated expenditure of $3,018,000 is a financial cap intended for the implementation of the Visiting Scheme to Outlying Islands. The scheme provides free ferry rides to eligible persons from schools, non-governmental organisations, community and local groups, etc. to encourage them to organise activities to the outlying islands served by the six ferry routes.

IMPLEMENTATION PLAN

22. As mentioned in paragraph 6 above, with the support of the Panel and the Islands District Council (DC), the Government has completed its negotiation with the two ferry operators to ensure a smooth continuation of ferry services when the current licence period expires in mid-2017. The period of the existing licences of the six ferry routes would be extended for another three years in accordance with section 29(2)[10] of the Ferry Services Ordinance. Subject to the funding approval of the FC, the TD will continue to provide the SHM on an actual reimbursement basis in the next licence period.

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[10] In accordance with section 29(2) of the Ferry Services Ordinance, "[t]he Commissioner [for Transport] may, at the request of the licensee, during any period while the licence is in force, extend the period of the licence for a further period or periods not exceeding 3 years at any one time, so that the period for which the licence was granted together with all extensions thereof shall not in any case exceed in the aggregate a period of 10 years". As the current licences of the six ferry routes started from mid-2011, further extension of these licences for three years will still meet the ten-year aggregate period rule.

23. In the event of a sudden, steep and sustained oil price hike during the next licence period, we may, if necessary, consider a one-off additional SHM provision and/or fare increase during the licence period.

PUBLIC CONSULTATION

24. We consulted the LegCo Panel (on 18 November and 2 December 2016), the Islands DC's Traffic and Transport Committee (T&TC) (on 21 November 2016) and the Transport Advisory Committee (TAC) (on 29 November 2016) on the SHM proposal. They were all supportive of the proposal and accepted the proposed fare increase of around 4%.

25. On the front of the Panel, two meetings were held, primarily because of the need to arrange for a deputation, a request made by Members during the first Panel meeting. Some Members were of the view that there should be no fare increase or at most an increase which was lower than the proposed 4%, in particular when the Government was prepared to double the SHM subsidy in the next licence period. The Government explained clearly at the meetings that, the operators originally requested a fare increase of around 10%, mainly due to the significant increase in operating cost in the next licence period. The Government already proposed to lower such fare increase to a modest rate of 4% through the SHM, and passengers should shoulder a fair share of fare increase burden. There were also views that the Government should set up a fuel stabilisation fund and enhance manpower supply in the ferry trade. Members were advised that in determining the SHM amount, we had already taken into account the overall financial performance of the ferry routes in the next licence period, including the fuel and staff costs. As to manpower, Members were advised that the Government had been providing financial incentives to encourage talents to attain necessary ferry crew qualifications. The enhanced remuneration packages offered by the ferry operators would also help attract more new blood to join the industry. In addition, Members requested for information on the patronage of the "Central – Cheung Chau" route and the estimated SHM amount for the HKK in the next licence period. The Government submitted the requested supplementary
Encl. 4 information (see Enclosure 4) to the Panel on 9 January 2017.

26. The Panel also raised some route-specific matters. Some Members showed objection to the operator's tentative plan of the proposed introduction of single-vessel type operation (by replacing the two existing slow ordinary ferries with two fast ferries to have four fast ferries operating that route in total) for the Peng Chau route[11], mainly out of the concern that fares for fast ferries were higher

/than …..

[11] The Panel put forward a motion that the Panel should not support the subsidy for the Peng Chau route unless the HKK submits the details of proposed ferry types and fares for the next licence period to the Panel for scrutiny. The motion was defeated.

than that of ordinary ferries[12]. We explained to the Panel that the operation mode of the Peng Chau route would not affect the SHM funding[13] required for the next licence period. The Government has also consulted the Islands DC on the operators' tentative plan of the single-vessel type operation. Subsequently, having regard to the local's views, the operator decided to shelve such plan (see paragraph 28 below for details). For the Cheung Chau route, individual Members requested a priority passageway for Cheung Chau residents and pier improvements (including constructing a new pier in Cheung Chau). In response, we advised the Panel that, having consulted the Islands DC, the operator already planned to launch a monthly ticket passage, which should be able to benefit frequent passengers of the "Central – Cheung Chau" route. As to the request for the operator to provide multi-ride tickets for passengers of the "Central – Cheung Chau" route and expanding the monthly ticket passage to cover such multi-ride ticket holders, the operator responded positively but would need time to sort out the technical details of implementation. The operator aimed to complete the task before the commencement of the next licence period. The Government was also looking into the necessary pier improvement in Cheung Chau.

27. Regarding the arrangements beyond 2020, Panel members requested the Government to actively look into the possibility of lengthening the duration of the licence period, currently three years only, to facilitate necessary long-term planning and investment on the part of the operators. They also clearly expressed the view that the SHM should be extended to cover the other eight outlying island ferry routes, in particular the Discovery Bay and Ma Wan routes. On the option of using rental income from additional floors on Central Piers Nos. 4-6 to cross-subsidise ferry operation, Members noted the demerits of going down that route, while expecting the Government to come to a definitive answer on whether to adopt this cross-subsidy model in the coming mid-term review due for completion in early-2019.

28. At the T&TC meeting on 21 November 2016, Members expressed no dissenting views on our SHM proposal after deliberation and found the fare increase understandable. The TAC, at its meeting on 29 November 2016,

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[12] For the "Central – Peng Chau" route, the fare for an adult single journey ticket for fast and ordinary ferries now is $28.5 and $15.3 respectively during Mondays to Saturdays, and $41.8 and $21.9 respectively on Sundays and public holidays. If single vessel type operation mode is implemented, the ferry operator expects that the fares will fall in between those for ordinary ferry service and fast ferry service.

[13] The operation mode adopted for the Peng Chau route, be it single-vessel type or mixed-fleet operation mode, will have little impact on the overall costs involved and hence no significant impact on the overall SHM funding required.

supported the Government's proposal. As regards the operator's proposal on adopting the single-vessel type operation for the "Central – Peng Chau" route, the Islands DC invited the TD to a residents' meeting to collect more views. TD and HKK attended the Peng Chau residents' meeting on 30 December 2016 to collect views. The majority view of the residents who attended was to maintain the existing mixed fleet operation for the "Central – Peng Chau" route. Having regard to the local's views, HKK decided to continue to run the route under mixed fleet operation.

BACKGROUND

29. It is the Government's established policy that public transport services should be run by the private sector in accordance with prudent commercial principles to achieve operating efficiency. However, ferry services for outlying islands are unique in that they are the only means of transport for outlying islands[14]. As there has been a lack of growth in patronage and given the escalating operating costs, the Government has been providing various measures to reduce the operating costs of the ferry services, and allow ferry operators to sublet the piers in order to increase non-fare box revenue to cross-subsidise their operations. The implementation of these measures (other than SHM) aims to maintain the financial viability of the ferry services and alleviate the burden of fare increases on passengers. Details of these measures are at Annex II of Enclosure 1.

Transport and Housing Bureau
March 2017

[14] Only Lantau Island is linked also by a road network, but its cross-district land-based public transport services are limited.

Details of the Special Helping Measures

Their average daily patronage of the six routes was around 50 000 passenger trips in 2015. The total sum of 14 outlying island ferry routes, including the six major routes, together with their patronage information are at Annex I.

Annex I

2. We sought approval from Finance Committee of the Legislative Council in July 2013 of a commitment of around $190 million for implementation of the following package of the Special Helping Measures (SHM) to the six major ferry routes –

	SHM	**Reimbursement cap for the current 3-year licence period ($ Million)**	**Actual amount reimbursed in the first two operating years ($ Million)**
(a)	Reimbursing the vessel survey fee and private mooring charge	**34**	31.8
(b)	Reimbursing the pier electricity, water and cleansing charges		
(c)	Reimbursing the balance of revenue foregone due to provision of elderly fare concessions after netting off the amount of pier rental reimbursement and vessel licence fee exemption under the established arrangement		
(d)	Reimbursing the vessel maintenance cost	**96**	81.2
(e)	Reimbursing the revenue foregone due to provision of child fare concessions	**23**	12.5

	SHM	Reimbursement cap for the current 3-year licence period ($ Million)	Actual amount reimbursed in the first two operating years ($ Million)
(f)	Reimbursing the vessel insurance cost	**3**	4.4
(g)	Implementing "Visiting Scheme to Outlying Islands"[Note]	**2**	1.6
(h)	20% Buffer	**32**	N/A
	Total	**Around 190**	131.5

Other helping measures

Annex II

3. A list of other helping measures now provided to ferry services (other than SHM) is at Annex II.

Note The "Visiting Scheme to Outlying Islands" provides free ferry rides to eligible persons who come from institutions such as schools, non-governmental organisations, community and local groups, to facilitate them to organise activities on the outlying islands served by the six ferry routes. The ferry operators are reimbursed with the revenue foregone from the Government. The application for the scheme for the current licence period was closed in mid-2016. It is anticipated that the sum reserved for the scheme will be largely used up.

Annex I

Patronage of the 14 outlying island ferry routes in 2015

Outlying Island Ferry Routes	Average Daily Patronage in 2015
Routes covered by the SHM	
1. Central – Cheung Chau[Note 1]	26 315
2. Inter-islands (Peng Chau – Mui Wo – Chi Ma Wan – Cheung Chau)[Note 1]	1 059
3. Central – Mui Wo[Note 1]	5 865
4. Central – Peng Chau[Note 2]	6 860
5. Central – Yung Shue Wan[Note 2]	9 111
6. Central – Sok Kwu Wan[Note 2]	1 257
Routes not covered by the SHM	
7. Aberdeen – Cheung Chau[Note 3]	539
8. Aberdeen – Yung Shue Wan via Pak Kok Tsuen	845
9. Aberdeen – Sok Kwu Wan via Mo Tat	642
10. Tuen Mun – Tung Chung – Sha Lo Wan – Tai O	1 102
11. Discovery Bay – Mui Wo	264
12. Discovery Bay – Central	11 707
13. Ma Wan – Central	3 039
14. Ma Wan – Tsuen Wan	302

Note:

1. Operated by New World First Ferry Services Limited (NWFF).
2. Operated by the subsidiaries of Hong Kong & Kowloon Ferry Holdings Ltd (HKK).
3. The route was inaugurated on 8 August 2015.

Annex II

Ordinary helping measures for ferry services (other than SHM)

The Government has been providing various ordinary helping measures to all routes (other than SHM) to enhance the viability of ferry services. These measures include –

(a) taking over pier maintenance responsibility;

(b) waiving fuel duty;

(c) reimbursing pier rentals and exempting vessel licence fees for ferry services under the Elderly Concessionary Fares Scheme; and

(d) streamlining the pier subletting approval procedures to help generate non-fare box revenue for cross-subsidising the ferry operation so as to alleviate pressure for fare increase.

Enclosure 2 to FCR(2016-17)87

Details of implementation of the SHM in the 2017-20 licence period

The substantive increase in SHM amount from $190 million for the current licence period (2014-17) to around $410 million for the next licence period (2017-20) is mainly attributable to the following factors –

Items	Cap of subsidy amount in the 2014-17 licence period (a) ($ million)	Cap of subsidy amount in the 2017-20 licence period (b) ($ million)	Additional subsidy amount in the 2017-20 licence period (b-a) ($ million)
Introduction of a new SHM item – depreciation cost	Not applicable	16	16
Repairs and maintenance cost of NWFF and HKK	96	240	144[Note]
Reimbursement of vessel survey fee and private mooring charge, pier electricity, water and cleansing charges, and revenue foregone due to provision of elderly fare concessions	34	53	19
Reimbursement of vessel insurance cost	3	9	6
Contingency provision	32	69	37

Note The some $144 million increase in reimbursement of repairs and maintenance costs for the two operators is mainly attributable to the following –

(a) the operators' plan to spend around $57 million to upgrade ferry fleets in the next licence period;

(b) some of the key major vessel maintenance and survey costs of around $13 million in a four-year maintenance cycle of vessels would fall within the next licence period;

(c) an increase of around $42 million in operators' standard repairs and maintenance costs; and

(d) part of the operators' repairs and maintenance costs in the current licence period cannot be fully subsidised. We intend to fully reimburse repairs and maintenance costs of the next licence period to operators in the next licence period and hence a larger provision is required.

Enclosure 3 to FCR(2016-17)87

Maintaining the long-term financial viability of outlying island ferry services

For maintaining the long-term financial viability of outlying island ferry services, the Government will study the various issues below.

2. The Ferry Service Ordinance (Cap. 104) stipulates that a licence period for ferry service should be three years at the maximum. We are of the view that this requirement hampers the operators' capability for longer-term planning and investment for ferry services. We will take the opportunity of the next mid-term review to explore extending the effective period of a licence, through legislative amendments.

3. In 2013, the Government proposed taking forward the construction of additional floors at Central Piers Nos. 4, 5 and 6, to provide shop rental income to cross-subsidise the operation of the six routes. When the proposal was submitted to the Public Works Sub-committee under the FC for consideration, the Sub-committee raised various concerns over the rental income and operations and management issues[1], and voted down the proposal of upgrading the construction project to Category A. Subsequently, we re-considered this proposal in detail. Given the construction cost involved of such proposal (estimated to be around $610 million in 2013), the uncertainty of rental income, and the complex contractual relationship among stakeholders (namely the Government, ferry operators, the lease agency as well as shop tenants), and that the fees to be charged by the lease agency will reduce the eventual rental income for the cross-subsidy purpose, preliminarily, we are of the view that this proposal may not be the most feasible and desirable model.

4. Separately, there are views that the Government should procure vessels for the operators to reduce their operating costs, as ferry operators have been facing a sustained and difficult operating environment. It is the Government's established policy that public transport services should be run by the private sector in accordance with commercial principles to enhance efficiency and cost-effectiveness. This proposal deviates from that established public transport policy. However, in order to encourage operators to introduce new

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[1] Members' major concerns included opining that the Government under-estimated the projection of rental revenue, and should work out a business model of the piers that could maximise rental income. There were also suggestions that the Government should re-consider the design of the exterior appearance of the piers.

vessels or improve services, facilities or equipment, the Government now proposes the introduction of a new item in the next three-year licence period so as to reimburse half of the depreciation expenses of the abovementioned capital investment. Accordingly, two new vessels will be introduced to the fleet. In fact, the major pressure faced by the ferry operators are from the continuously escalating operating expenses, of which around 70% are attributable to fuel and staff costs. Even if the Government were to procure vessels for the operators to reduce operating cost, this would only lower the expenditure arising from capital investment. It could not solve the problem of recurrent deficit in daily operation. Therefore, the SHM would still need to be maintained.

5. Another similar idea is for the Government to procure and own ferries, and to outsource the service operation. Our preliminary assessment shows that the "management, operation and maintenance" business model has the merits of enabling the Government to use public funds to upgrade/replace existing ferries with new ones from time to time. It can also give the Government full control of ferry services. But, the "management, operation and maintenance" model deviates from the Government's long-standing policy to let public transport services run by the private sector on commercial principles, in the interest of maximisation of operational efficiency and cost-effectiveness. Besides, fare adjustment arrangement will also need to be handled suitably.

The eight remaining outlying island ferry routes

6. Currently, apart from the six major outlying island ferry routes, there are eight other outlying island ferry routes[2]. There are views that the SHM should be expanded to these eight outlying island ferry routes. We will examine this matter. Specifically, we will consider a whole host of factors, including the principle of prudent use of public money, whether there are any alternative public transport service of each of the eight routes, the operating environment of each of the eight routes (for example, some of the routes were launched in support of the new residential development projects at that time) and the different financial situation (some of the routes are suffering financial loss but there are routes that are relatively financially manageable for the time being) and patronage of the eight routes, etc. The current data on these issues are in the table enclosed.

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[2] The eight other outlying island ferry routes include:

(1) "Aberdeen – Cheung Chau";
(2) "Aberdeen – Yung Shue Wan via Pak Kok Tsuen";
(3) "Aberdeen – Sok Kwu Wan via Mo Tat";
(4) "Tuen Mun – Tung Chung – Sha Lo Wan – Tai O";
(5) "Discovery Bay – Central"
(6) "Discovery Bay – Mui Wo";
(7) "Ma Wan - Central"; and
(8) "Ma Wan – Tsuen Wan".

The profit-sharing mechanism has become the terms of licence renewal for 2017-20 for the six major outlying island ferry routes. Whether it should be applicable to the other eight routes needs to be studied. Besides, the duration of the licence periods of those eight routes is not the same (the existing licence periods range from one to three years; details are in table enclosed at Annex). Whether the future licence periods should be rationalised or unified also needs to be studied. When the Government makes a decision on the long-term operation model of the existing six major outlying island ferry routes in the first half of 2019, it will decide in one go whether and how the long-term operation model to be selected at that time should be applicable to the other eight routes. We will then consult the LegCo.

Annex

7. We will look into the matters in paragraphs 2 to 6 above carefully. The studies are expected to be completed in tandem with the mid-term review of the implementation of the SHM in the 2017-20 licence period in the first half of 2019.

Annex

Operating situation of the eight outlying island routes without SHM

The eight Outlying Island Routes without SHM [Current Licence Period]	2015 Average Daily Patronage	Remarks
Discovery Bay – Central [One year：1.5.2016 - 30.4.2017]	11 707	• Certain cross-district non-franchised residents' bus services are available[1]
Aberdeen – Pak Kok Tsuen – Yung Shue Wan [Three years：15.8.2014 - 14.8.2017]	845	• No alternative public transport service
Discovery Bay – Mui Wo [Two years：10.2.2016 - 9.2.2018]	264	• Road network connecting other places is available, but routing is very inconvenient.
Aberdeen – Cheung Chau [Three years：8.8.2015 - 7.8.2018]	539	• Cheung Chau relies on ferries for transmuting. This route is to moderate the heavy loading of the Central – Cheung Chau route.
Tuen Mun – Tung Chung – Sha Lo Wan – Tai O [Three years：2.9.2015 - 1.9.2018]	1 102	• No alternative public transport service
Ma Wan – Central [Three years：14.12.2015 - 13.12.2018]	3 039	• Certain cross-district non-franchised residents' bus services are available[2]
Ma Wan – Tsuen Wan [Three years：8.6.2016 - 7.6.2019]	302	
Aberdeen – Mo Tat – Sok Kwu Wan [Three years：1.6.2016 - 31.5.2019]	642	• No alternative public transport service

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[1] Details of routes are as follows:
- DB01R Discovery Bay – Tung Chung
- DB02R Discovery Bay – Airport
- DB03R Discovery Bay – Sunny Bay

[2] Details of routes are as follows:
- NR330 Ma Wan (Tung Wan Bus Terminus) – Tsing Yi Station
- NR331 Ma Wan (Pak Yan Road) – Tsuen Wan (Sai Lau Kok Road)
- NR331S Ma Wan (Pak Yan Road) – Tsuen Wan West Station
- NR332 Ma Wan (Tung Wan Bus Terminus) – Kwai Fong (Metroplaza)
- NR334 Ma Wan (Tung Wan Bus Terminus) – Hong Kong International Airport
- NR338 Ma Wan (Tung Wan Bus Terminus) – Central (Central Ferry Pier No.2) (All Night Service)

(Translation)

政府總部
運輸及房屋局
運輸科
香港添馬添美道 2 號
政府總部東翼

Transport and Housing Bureau
Government Secretariat
Transport Branch
East Wing, Central Government Offices,
2 Tim Mei Avenue,
Tamar, Hong Kong

本局檔號 :THB(T)CR 2/5482/00
來函檔號 :

電話號碼 : 3509 8159
傳真號碼 : 2537 5246

Secretary General
Legislative Council Secretariat
Legislative Council Complex
1 Legislative Council Road
Central, Hong Kong
(Attn: Ms Sophie LAU)

[Fax no: 2978 7569]

9 January 2017

Dear Ms LAU,

Legislative Council Panel on Transport
Special Helping Measures for six major outlying island ferry routes
for the next three-year licence period 2017-20

The Government consulted the Legislative Council Panel on Transport on the arrangements of Special Helping Measures ("SHM") for the six major outlying island ferry routes[1] in the next three-year licence period (2017-20) on 18 November and 2 December 2016. We now provide a reply to Members' enquiries raised at the meetings, concerning the average daily patronage of the "Central – Cheung Chau" ferry route operated by the New World First Ferry Services Limited, as well as the

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[1] Routes operated by the New World First Ferry Services Limited :
(1) "Central – Cheung Chau";
(2) "Inter-islands" between Peng Chau, Mui Wo, Chi Ma Wan and Cheung Chau ; and
(3) "Central – Mui Wo" routes.

Routes operated by the Hong Kong & Kowloon Ferry Holdings Limited's three subsidiaries :
(4) "Central – Peng Chau";
(5) "Central – Yung Shue Wan"; and
(6) "Central – Sok Kwu Wan" routes.

projected amount of SHM to be provided by the Government to the Hong Kong & Kowloon Ferry Holdings Limited ("HKK") for operating the three outlying island ferry routes in the next three-year licence period.

Patronage of the "Central – Cheung Chau" ferry route

The average daily patronage of the "Central – Cheung Chau" ferry route in the past five years are detailed as follows –

Year	Average daily patronage (passenger trips)
2011	22 943
2012	23 610
2013	25 244
2014	25 767
2015	26 315

Projected amount of SHM to be provided by the Government to HKK in 2017-20

Having regard to the financial projections of the three outlying island ferry routes operated by HKK (i.e. "Central – Peng Chau", "Central – Yung Shue Wan" and "Central – Sok Kwu Wan" routes) in the next three-year licence period, the Government projects that there is a need to provide SHM of around $122 million (without accounting for any contingency provision) for those three routes. It should be noted that SHM reimbursement on specified costs is subject to actual usage. Invoices would be carefully verified by the Transport Department to ensure there would not be any abuse. Operators are required to submit audited financial statements to the Transport Department at the end of each financial year to prove the actual paid expenses. Besides, operators are also required to submit quarterly management accounts, to enable the Transport Department to monitor their financial situations.

Yours sincerely,

(Vivian HO)
for Secretary for Transport and Housing