

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 Our Ref. THB(T) CR 20/1016/99
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Tel. No.: 3509 8188
Fax No.: 2868 5261

Council Business Division
Legislative Council Secretariat
Legislative Council Complex
1 Legislative Council Road
Central, Hong Kong
(Attn: Ms Macy NG)

(Fax no.: 2978 7569)

25 January 2017

Dear Ms NG,

**Request for Arranging a Joint Meeting between
the Panel on Transport and
the Panel on Administration of Justice and Legal Services**

Regarding the captioned suggestion made by Hon. Holden CHOW, which was relayed in your letter of 14 December 2016 to our Bureau, our reply is set out below.

The Shatin to Central Link (“SCL”) project is implemented under the “concession approach”. The Government is responsible for funding the construction and will have the ownership of the railway. The MTR Corporation Limited (“MTRCL”) is entrusted with the design and construction of the railway. Upon completion of the railway, the Government may vest the SCL in or lease it to the Kowloon-Canton Railway Corporation (“KCRC”). The KCRC will in turn include the SCL into the service concession granted to the MTRCL and receive service concession payments. In 2012, the Government and the MTRCL entered into an agreement for entrusting the construction, testing and commissioning of the main works of the SCL to the latter. The MTRCL, as a trustee, has to provide management and monitoring service to the SCL project. According to the agreement for the main works of the SCL, the original target commissioning date

for the “Tai Wai to Hung Hom Section” is December 2018 and that for the “Hung Hom to Admiralty Section” is December 2020. The main works commenced in July 2012.

Works Progress of SCL

Since July 2014, we have submitted quarterly reports on the SCL to the Subcommittee on Matters Relating to Railways (“RSC”) of the Panel on Transport of the Legislative Council (“LegCo”). In addition to the detailed progress in various sections of the project, the works delayed and the relevant delay recovery measures, the reports also set out the expenditures of the works, the situation of substantiated claims from contractors, and the progress of the major civil, and electrical and mechanical works contracts for the reference of Members and the public, and their monitoring of the implementation of the project.

As mentioned in the quarterly reports submitted to RSC and discussed at its meeting held on 9 December 2016, the MTRCL is currently conducting a detailed cost review of the main works of the SCL. Issues covered include the delay of at least 11 months and the additional cost of at least \$4,100 million arising from the archaeological and conservation works at To Kwa Wan Station, the increase in the cost of the enabling works for the topside development at Exhibition Station, the additional expenditure involved due to the deferred site handover, and the increase in construction cost arising from the difficulties and challenges encountered at different works sites.

The MTRCL also pointed out at the meeting of RSC held on 9 December 2016 that the SCL project was complicated and only about 40% of the “Hung Hom to Admiralty Section” had been completed as at the end of October 2016, coupling with the fact that the remaining 60% of the section would still be affected by various difficulties and challenges. To provide a relatively accurate estimate for the cost of the main works, it was necessary to wait until the second half of 2017 in order to have a more practical assessment. As regards the latest project cost estimate for the SCL as reported by the media in November 2016, the MTRCL could not confirm the information concerned.

It is anticipated that the contingencies for the main works of the SCL will not be sufficient to meet the additional expenditures of the main works. Therefore, upon receiving the final assessment on the additional cost from the MTRCL in the second half of 2017, the Highways Department (“HyD”) and its monitoring and verification (“M&V”) consultant will conduct a detailed and stringent scrutiny of such assessment. After completion of the scrutiny, we will seek additional funding from the LegCo in the 2017/18 legislative session for the continuation of the main works.

Entrustment Agreement of Main Works of SCL

In January 2010, the Government and the MTRCL entered into an agreement for entrusting the construction, testing and commissioning of the Hong Kong section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link (“XRL”) to the latter. After discussion with the MTRCL, we submitted to the LegCo in early January 2016 with a copy of the entrustment agreements of the XRL. On the other hand, the Government and the MTRCL entered into an entrustment agreement (“EA”) of the main works of the SCL in May 2012. Apart from the particulars of the SCL project, the terms of the EA of the SCL are generally identical to that of the XRL.

The Government has put in place a three-tiered monitoring mechanism¹ to closely oversee the work of the MTRCL since the commencement of the SCL works. The HyD has also employed a M&V consultant to assist in the monitoring work and undertake regular audits. The M&V consultant will review the works progress and notify the HyD of any potential risk of delay. It will also offer comment to the HyD on the appropriateness of MTRCL’s proposed mitigation measures (for delay recovery).

According to the EA for the main works, the MTRCL is responsible for the overall management of the SCL project. It shall use its best endeavours to complete, or procure the completion of, the Entrustment Activities in accordance with the Entrustment Programme; and to minimise any delay or other effect which any modifications may have on the Entrustment Programme. In this connection, the MTRCL shall act in accordance with its management systems and procedures. Moreover, the Government shall be entitled to appoint an appropriate consultant to verify MTRCL’s compliance with its obligations under the EA. At any time the MTRCL is in material or persistent breach (or the Government, acting reasonably, suspects that the MTRCL is in material or persistent breach) of any of MTRCL’s material obligations under the EA, the Government shall be entitled to verify MTRCL’s compliance with MTRCL’s obligations under the EA.

As for the expenditures of the works, the Government and the MTRCL conducted risk assessments at the planning and budgeting stages of the project to minimise claims arising from the works. Nevertheless, there were often unforeseeable situations in the course of works. For instance, the foundation or excavation works might encounter a larger amount of or more complicated obstructions than expected. As this would add difficulties to the works, the contractors might have to use more machines or switch to other machines that were more suitable and employ more staff to cope with these situations. The contractors would submit claims in accordance with the contract terms to cover the additional expenditures. Upon receipt of claims from contractors, the MTRCL would

¹ That is, the Project Supervision Committee chaired by the Director of Highways, the Project Coordination Meetings held by an officer at the Assistant Director level of the HyD with MTRCL’s General Managers and Project Managers, and the Contract Review Meetings held by an officer at the Chief Engineer level of the HyD with site supervision staff of the MTRCL.

examine the reasonableness of such claims and assess the amount concerned based on the contract terms, justifications submitted by the contractors, the relevant records, etc. In assessing such claims, the MTRCL has to seek comments from the HyD through its Project Control Group. In this connection, the HyD will critically examine each claim assessment report involving public funds, offer professional comments in respect of the analysis of claim assessment, and review the justifications, principles and culpabilities of all the claims, with a view to safeguarding the interest of the Government as the owner of the SCL project and ensuring the proper use of public funds.

The MTRCL warrants the Government that Entrustment Activities relating to the provision of project management services shall be carried out with the skill and care reasonably expected of a professional and competent project manager whose role includes coordination, administration, management and supervision of the design and construction of works. Should the delay in question involve a breach of the MTRCL of any of its warranties, the Government may have a claim against the MTRCL for breach of warranties. Besides, the EA has also set out a dispute resolution mechanism, inter alia, by means of mediation or even arbitration to settle disputes.

In the light of the delay in the construction of the XRL, the Chief Executive appointed an independent expert panel (“IEP”) in May 2014. The IEP, chaired by the Hon Mr Justice Michael J HARTMANN, comprised two other overseas engineering experts, namely Dr. Peter HANSFORD and Professor Andrew J WHITTLE, to review the delay and cost overrun problems of the XRL. The report of the IEP was released on 30 January 2015. It stated the review results on the delay and cost overrun problems of the XRL, including the deficiency of the EA of the XRL, and put forward recommendations aiming to improve the systems, processes and practices for implementing and monitoring the XRL as well as future new railway projects.

Enhancement of Monitoring of the SCL

Since the SCL project and the XRL project are both implemented under the “concession approach”, taking into account the advice of the IEP, the HyD started to implement the following measures to enhance the monitoring of the progress and financial status of the SCL project in mid-2014.

- (i) an increase in the number of staff in the SCL project team under the Railway Development Office of the HyD to enhance the monitoring role;
- (ii) submission of monthly progress reports to the Transport and Housing Bureau (“THB”) for the SCL project with the adoption of “traffic light” system to facilitate THB’s understanding of current project status;
- (iii) liaising more closely with MTRCL’s project team and requesting the

MTRCL to provide more detailed information;

- (iv) arranging the M&V consultant appointed by the HyD to attend the PSC meetings; and
- (v) establishment of a working group amongst the HyD, the M&V consultant and the MTRCL with members from the respective specialised teams to review the programme and progress of the SCL project in detail on a regular basis with all aspects and levels of works covered.

We understand the Members' concerns on the SCL project. However, we have reservations about the suggestion of the captioned joint meeting to discuss the terms and legal matters of the EA.

As regards the spirit of the EA, the Government and the MTRCL should fulfil their responsibilities in accordance with the terms of the EA. The HyD together with its appointed M&V consultant are closely monitoring the progress and expenditure status of the SCL, etc. If necessary, they would request the MTRCL to provide supplementary information and the MTRCL is proactively fulfilling its responsibility according to the EA.

If at this stage, the Government and the MTRCL jointly discuss with Members about the terms of the EA at any panel meetings, it may give rise to unnecessary disputes to both contracting parties while implementing the EA. At the moment, the construction team of the MTRCL and the contractors has spared no effort to mitigate part of the delay arising from the archaeological works at To Kwa Wan Station earlier on. If the terms of the EA for the SCL are to be discussed publicly at this stage, the focus of the construction team would be shifted and the progress of the SCL may be affected. Besides, if the Government discloses its understanding and stance on the terms concerned upon request of Members, it will affect the Government in the possible negotiations with the MTRCL on obligations regarding such issues as works delay or project cost overrun in the future.

We consider that the immediate imperative is to focus on recovering part of the delay, with a view to enabling the early commissioning of the SCL to serve the public. In view of the delay of 11 months arising from the archaeological works, discoveries and conservation options for the archaeological features at To Kwa Wan Station earlier on, the "Tai Wai to Hung Hom Section" would be deferred to end 2019. The HyD has always been coordinating and overseeing the construction of the SCL with a view to recovering part of the delay. With the efforts of the construction team, the delay recovery measures implemented at the "Tai Wai to Hung Hom Section" take effects progressively. Hence, the target commissioning date of this section is advanced to about mid-2019, while that of the "Hung Hom to Admiralty Section" remains at 2021. We will continue to coordinate and oversee the construction of the SCL, with a view to commissioning the project in accordance with the above revised targets. We will also continue to fully support

the work of the RSC, submit quarterly reports on the SCL, and discuss the latest works progress and financial status of the SCL project at RSC meetings.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Rli' with a small mark above the 'i'.

(Ralph LI)
for Secretary for Transport and Housing

c.c.:

Director of Highways (Attn.: Mr Frankie CHOU) Fax no.: 2714 5297