

## **LEGISLATIVE COUNCIL BRIEF**

### **ENHANCED FINANCIAL ARRANGEMENT FOR THE WEST KOWLOON CULTURAL DISTRICT**

#### **INTRODUCTION**

At the meeting of the Executive Council on 13 December 2016, the Council ADVISED and the Chief Executive ORDERED that -

- (a) the Government should grant the development right of the entire hotel/office/residential (HOR) portion of the West Kowloon Cultural District (WKCD) (involving 366 620 square metres (sqm) gross floor area (GFA)) to the West Kowloon Cultural District Authority (WKCDA) at nominal premium, whereas WKCDA should pay Government upfront payments according to the financial arrangements to be specified in the Project Agreement<sup>1</sup> to be signed by both parties based on the following parameters (paragraphs 8 to 10 and 19 below) –
  - (i) WKCDA should be allowed to develop the HOR portion through Build-Operate-Transfer (BOT) and income sharing arrangements with private developers so as to provide WKCDA with a steady source of recurrent income;
  - (ii) in respect of sub-paragraph (a)(i) above, the upfront payments from private developers, to be determined through open and competitive tenders of the BOT arrangements with tender conditions set by WKCDA, should be attributable to the Government;

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<sup>1</sup> As the Land Grant will only cover land covenant matters and broad development parameters, when granting the WKCD site to WKCDA, the Government will sign a Project Agreement with WKCDA setting out the rights and responsibilities of both parties with regard to the facilities in WKCD and related interfacing issues including the integrated basement and public infrastructure works required for supporting the development of the whole WKCD.

- (b) notwithstanding the general disposal arrangement for the HOR portion in sub-paragraph (a) above, the Government should grant the development right of 81 066 sqm GFA of hotel and office sites (about 22% of the HOR portion GFA) to WKCDA at nominal premium without the need for an upfront payment to the Government. These sites should be packaged with the Exhibition Centre (EC) in WKCD for joint development (collectively known as Exhibition Hub Development Area (EHDA)) with private developers through BOT and income sharing arrangements (paragraphs 12 to 14 and 19 below); and
- (c) the Government should retain in the Project Agreement the right to share the income generated from the HOR and EHDA development packages upon expiry of the BOT period having regard to the funding requirements and financial position of WKCDA (paragraphs 18 to 19 below).

## **JUSTIFICATIONS**

### **Progress Update of the WKCD Development**

2. WKCD is being developed into an integrated arts and cultural district with a view to meeting the long-term infrastructural and development needs of Hong Kong's arts and culture, providing quality programmes with a must-visit appeal, fostering organic growth and development of cultural and creative industries (CCI), and becoming a hub for attracting and nurturing talents. Since the establishment of WKCDA in 2008, it has made great strides in advancing the planning, project delivery and cultural software for WKCD, with the key milestones set out below –

- (a) WKCDA conducted a three-stage public engagement exercise from 2009 to 2011 in preparing the Development Plan (DP) for WKCD. The draft DP, prepared on the basis of Foster + Partners' "City Park" Conceptual Plan, was gazetted under the Town Planning Ordinance (TPO) (Chapter 131) for public inspection in March 2012 and approved by the Chief Executive-in-Council (CE-in-Council) in January 2013;
- (b) To optimise the development potential of the WKCD site, WKCDA applied for minor relaxation of the maximum GFA and building height restrictions under section 16 of the TPO. The application was approved by the Town Planning Board (TPB) in November 2014 which yields additional GFA of 111 050 sqm (i.e. increase of 15%). The indicative distribution of GFA among different uses with the approved section 16 application is at **Annex A**;

- (c) Key infrastructure and building projects are moving full steam ahead. WKCD is making full use of the sites available for development, when other areas are being occupied by the Hong Kong section of Guangzhou-Shenzhen-Hong Kong Express Rail Link (XRL) project as construction sites for its West Kowloon Terminus and temporary works areas. Facilities that have been opened include the temporary Nursery Park (opened in 2015) where cultural and community events are organised for public enjoyment; and the M+ Pavilion (opened in July 2016) where small scale exhibitions are held prior to the opening of M+ Building. Facilities under construction include the Xiqu Centre (scheduled for opening in latter half of 2018), the Art Park (including the Freespace with a black box theatre and an outdoor stage) to be opened from 2018 in stages, as well as the M+ Building (scheduled to open in latter half of 2019). Foundation works for the Lyric Theatre Complex has also commenced. A table showing the batching and target completion dates of major WKCD facilities is at **Annex B** and a schematic plan is at **Annex C**; and
- (d) To prepare for the commissioning of the arts and cultural facilities, WKCD has devoted significant efforts to developing cultural software, such as programme development, audience building and professional development, as well as engaging the public especially the young people through community arts projects.

### **Strategic Importance of the WKCD Project**

3. The WKCD project has been generating cultural, economic, social and other benefits for Hong Kong. These include –

- (a) ***Driving growth of cultural and creative industries:*** The value added of the CCI sector in Hong Kong has increased by about 73% from \$63.3 billion in 2009 to \$109.7 billion in 2014 (annual average growth of 11.6%), as compared to a 39% increase in the Gross Domestic Product (GDP) at basic prices. In particular, the value added from the art, antiques and crafts sector has more than doubled from 2009 to 2014. The CCI sector in 2014 accounted for 5% of GDP, employing 213 060 persons. The WKCD project, which promotes the development of not only visual and performing arts but also that of design, film and art trading, has the potential of becoming a major CCI hub and providing a destination for CCI businesses.

- (b) ***Catalysing transformation of the local art scene:*** By making significant investment in WKCD, one of the world's largest cultural projects, the Government has sent a strong signal to the international art scene on its commitment to developing Hong Kong into an international arts and cultural metropolis. WKCD also assumes an institutional role for curatorial research, exchange, learning and participation, capacity building, and professional development of the arts and cultural sector. Its development thus catalyses the transformation of the local art scene and the development of art trading, as reflected in rapid growth in number and scale of international art fairs, auctions, art galleries, new art-themed clusters and public art projects. Hong Kong has now become one of the world's largest art trading markets in terms of auction sale.
  
- (c) ***Bringing intangible social benefits:*** Investment in arts and culture brings with it intangible social benefits. WKCD will play a critical role in giving Hong Kong new opportunities of developing artistic and cultural appreciation; enhancing community identity and expression; strengthening cultural institutions and exchange; increasing opportunities for community engagement and improving quality of life for Hong Kong's residents.
  
- (d) ***Strengthening Hong Kong's reputation as a world city and deepening its tourism offer:*** WKCD adds a new dimension to building Hong Kong's international reputation as a world city. In building WKCD as a cultural destination with a must-visit appeal, it has strong potential in attracting new mega events and creating new experience for different types of visitors.
  
- (e) ***Creating jobs:*** WKCD has created 1 500 construction-related jobs so far, and more jobs, particularly quality jobs for young people, will be created in a wide spectrum of economic sectors, including arts and culture, design and publishing, advertising and marketing, and tourism, as WKCD progresses to the operational phase. The latest estimate by WKCD's consultant reaffirms the results of the economic impact assessment in 2007 that upon full development, WKCD would create around 20 000 new jobs and contribute up to \$5.6 billion (in 2006 prices) to the Hong Kong economy annually in the operational phase.

## **The Existing Financial Arrangement for the WKCD Project**

4. The CE-in-Council decided on 29 January 2008 that the recommendations of the Consultative Committee on the Core Arts and Cultural Facilities of the WKCD (CC Case) should be adopted as the way forward for the development of WKCD. Among other things, an **upfront endowment of \$21.6 billion<sup>2</sup>** (in 2008 net present value), as subsequently approved by the Legislative Council (LegCo) in July 2008, would be given to WKCDA to implement the project; and the **Retail/Dining/Entertainment (RDE) portion** of WKCD would be vested with WKCDA at nominal premium to provide a steady source of recurrent income through rental proceeds to meet WKCDA's operating deficits, while the development rights of the HOR sites in WKCD belonged to the Government. Subsequently, WKCDA adopted the Foster + Partners' "City Park" Conceptual Plan. As the Conceptual Plan proposes the vertically integrated approach and the design with an integrated basement, the Government plans to grant the whole WKCD site, including the HOR portion, to WKCDA at **nominal premium**. The Land Grant and/or Project Agreement to be signed between the Government and WKCDA would specify clearly how the proceeds from the sale of the HOR sites (i.e. the land together with topside development rights) should be calculated and how they would be paid back to the Government.

## **WKCDA's Financial Difficulties**

5. As a result of various unforeseeable developments and changes after the upfront endowment was granted in 2008, including significant escalation in construction costs, lower than expected investment return of the upfront endowment, prolonged planning and public engagement exercise for the DP, additional GFA derived from the minor relaxation application approved by the TPB, expected recurrent income from RDE facilities not materialising in time, and changes in operational requirements not envisaged in the CC Case (a summary of the factors/developments is at **Annex D**), WKCDA is facing critical financial challenges in both capital and recurrent terms –

- (a) WKCDA currently estimates a capital funding of about \$11.7 billion in 2016 prices would be required for completing Batch 3 Core Arts and Cultural Facilities (CACF), two remaining black box theatres in Batch 2 as well as the remaining Other Arts and Cultural Facilities (OACF), RDE facilities and public open spaces (other than the Musical Theatre and the EC which are to be funded by private sector investment).

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<sup>2</sup> The capital costs of the WKCD project were estimated by the financial advisor for the CC Case based on a set of assumptions regarding the construction cost index, the rate of return in investment and other key parameters which formed the basis of the funding application to LegCo in 2008.

- (b) WKCDA will not have sufficient capacity to meet the operating deficit for reasons explained in Annex D. According to WKCDA's latest projection based on the Batch 1 and most of Batch 2 facilities which are completed or currently under construction, WKCDA will start to have operating deficit from 2017-18. The average operating deficit is estimated to be around \$500 million per annum from 2017-18 to 2026-27 in money-of-the-day (MOD) prices.

6. WKCDA has given a full account of the project's financial difficulties to LegCo and the public on various occasions. In mid-2013, the Government and WKCDA announced the adoption of a pragmatic approach for implementing the WKCD project, including delivering the major facilities in three batches, rigorous cost containment and emphasis on content rather than form. In the same year, the Government also announced that it was prepared to fund the integrated basement in full in addition to the associated public infrastructure works as general enabling works to support the development of the whole WKCD project subject to LegCo's funding approval. Furthermore, the Government indicated that it had no plan for additional injection to WKCDA before the completion of the development of Batch 1 facilities, and would carefully review the development plan of the Batch 3 facilities. Subsequently, WKCDA had stated that the upfront endowment of \$21.6 billion, together with the investment return, was only adequate to complete Batch 1 and most of Batch 2 facilities. In mid-2015, the Government and WKCDA informed LegCo that they were exploring various options to address WKCDA's financial difficulties which include granting WKCDA the development right of some or all of the commercial developments in WKCD so as to generate income to implement the rest of the project. As WKCD has started building up a promising brand for Hong Kong as an international arts and cultural hub, and making useful and impactful contributions not only in supporting the development of arts and culture of Hong Kong, but also in diversifying the economic development of Hong Kong as well as creating jobs and performing opportunities for young people, the Government agrees to introduce the enhanced financial arrangement to enable the successful implementation and the sustainable operation of WKCD for achievement of its public missions and realisation of its strategic values elaborated in paragraph 3 above.

## ENHANCED FINANCIAL ARRANGEMENT

7. The enhanced financial arrangement for the WKCD has the following considerations –

- (a) To provide **sufficient but not excessive resources** to WKCDA to meet its financial difficulties so that it can deliver and sustainably operate WKCD in particular its arts and cultural facilities;
- (b) To adopt **open and competitive tendering** in selecting private sector partners for the development of WKCD facilities and HOR sites such that **WKCDA will not play a developer role**;
- (c) To let private developers shoulder **development risks** (including construction, financing and marketing risks) of the development packages as much as possible in accordance with commercial considerations;
- (d) To **retain ownership** of the HOR developments in the hands of WKCDA to produce stable recurrent rental income during the BOT period, and ensure design and management of the entire district in a more **holistic and integrated manner**; and
- (e) To **protect Government's interests** by obtaining revenue from the development packages where possible, **a mechanism** will be devised to enable **sharing of income** with WKCDA upon expiry of BOT period and having regard to its funding needs.

### Key Components of the Enhanced Financial Arrangement

*(A) Grant of development right of entire HOR portion of WKCD to WKCDA with upfront payment to Government*

8. Taking into account the considerations in paragraph 7 above, the Government plans to grant the development right of the entire HOR portion of WKCD to WKCDA at nominal premium so that it may tender out the development packages of HOR together with the RDE embedded therein (embedded RDE), develop these commercial developments under the BOT model and receive rental income. Meanwhile, upfront payments should be paid to the Government according to the financial arrangements to be specified in the Project Agreement and the result of the tendering. With the 15% increase in total GFA under the approved planning application, the maximum GFA for HOR uses is 366 620 sqm (around 43% of total GFA of WKCD), of which no more than 170 280 sqm GFA (20% of total GFA of WKCD) could be designated for residential use (see Annex A).

9. Key features of the HOR development packages under the enhanced financial arrangement include –

- (a) WKCDA should adopt open and competitive tendering in selecting private sector partners for the development packages;
- (b) The tenderers need to indicate an upfront payment they propose to pay given the tender conditions set by WKCDA and that payment will be attributable to the Government;
- (c) To ensure that private developers would offer a reasonable price for the BOT arrangements involving development right in a prime location, WKCDA is required to come up with its own assessment of the full market value of the upfront payment the market is willing to pay for the development package concerned under specified tender conditions (pre-determined Full Market Value (FMV)), prepare pre-tender estimates, and retain the power to cancel the tender if the offer on upfront payment, in respect of sub-paragraph (b) above, is unreasonably low vis-à-vis the pre-determined FMV;
- (d) The private developers will bear all the costs for the planning, design, construction, management, maintenance, marketing and leasing of the development packages (including the embedded RDE facilities) and be solely responsible for any possible losses which might arise from the operation of the development packages;
- (e) WKCDA will share rental income from the development packages with private developers at a pre-determined ratio prior to the tender during the term of the BOT agreements;
- (f) The term of the BOT agreements will have to be reasonably long to be commercially attractive, but should not exceed the term of the Land Grant to WKCDA; and
- (g) WKCDA will retain ownership of the concerned land and premises in WKCD during the term of the BOT agreements, i.e. the private developers will have no claim on the land titles and have to hand over the control of the premises to WKCDA upon expiry of the BOT agreements.



10. Instead of selling the HOR sites and attributing the proceeds being land premium assessed at full market value to the Government under the original financial arrangement, WKCDA will retain ownership of the HOR sites and fetch for the Government upfront payment offered by the successful developers reflecting the price the market is willing to pay having regard to the development conditions attached to the BOT packages as set out in the tender documents. The retention of ownership of the HOR sites will help ensure that the entire district would be designed in a more holistic and integrated manner to complement the overall organic growth of WKCD and the phased commissioning of the arts and cultural facilities. While this requirement and the other development conditions as set out in paragraph 9 above would inevitably render the upfront payment received by the Government to be lower than the FMV that can be fetched under normal land disposal arrangements, we consider that the arrangement is justifiable on policy grounds given the strategic importance of WKCD as mentioned in paragraph 3 above, particularly in arts and cultural development.

11. WKCDA's current plan is to develop the major portion of the GFA of the HOR sites into rental offices and a small portion for rental residential units, the GFA of which will be lower than the approved upper limit. The major considerations for this plan include: additional office GFA can help alleviate the acute shortage of offices, especially Grade A offices, in core business districts; the DP prescribes only the maximum (20%), but not minimum, GFA for residential uses, and provision of rental residential units can satisfy the requirement for residential element in HOR sites; and under the enhanced financial arrangement, WKCDA's proposed development plan does not envisage selling of land and premises in WKCD (including rental residential units) to any other parties during the term of the BOT agreements. This will help remove the complications and uncertainties arising from multiple ownerships of different strata of the HOR buildings.

***(B) Grant of development right of the EHDA to WKCDA without upfront payment to Government***

12. The original intention of the WKCDA was to develop the co-located EC and Mega Performance Venue (MPV) when private sector funding is available. It had reserved a site of about 77 045 sqm GFA in the western part of the WKCD for these developments. WKCDA has completed a review and came to the view that the original proposal to build a MPV in WKCD was no longer suitable and has decided to consider developing the EC into a medium-sized, multi-purpose venue for exhibition, convention and performance purposes through private sector investment. Subsequently, WKCDA has decided to develop the Hong Kong Palace Museum on part of the site concerned.

13. Notwithstanding the general disposal arrangement proposed in paragraphs 8 to 10 above for the HOR portion, the Government plans to grant the development right of 81 066 sqm GFA of hotel and office uses (about 22% of the total GFA of the HOR sites) in the U-shaped site adjacent to the EC to WKCDA at nominal premium without the need for WKCDA to pay an upfront payment to the Government. WKCDA should tender out a BOT development package of the EHDA comprising the EC, rental offices and hotel(s) together with the embedded RDE facilities. Instead of setting a pre-determined ratio for income sharing with WKCDA as a tender condition, tenderers are required to indicate the **percentage of income** from the operation of the BOT development package that they will share with WKCDA having regard to the tender conditions set by WKCDA. The key features of the HOR development packages set out in paragraphs 9(a), (d), (f) and (g) above will also apply to the EHDA BOT package. Furthermore, similar to paragraph 9(c) above, WKCDA will be required to come up with its own assessment of the pre-determined FMV of the development package concerned under specified tender conditions, prepare pre-tender estimates, and retain the power to cancel the tender if the income to be shared with WKCDA offered is unreasonably low vis-à-vis this pre-determined FMV.

14. The proposed packaging of EC with hotel(s) and rental offices has taken into account the following considerations –

- (a) there will be synergy in the design, construction and management of the EC, hotel and office facilities as a package, e.g. the accommodation and catering facilities of hotels can serve the needs of events at EC;
- (b) packaging hotels and rental offices with EC in WKCD will allow the investor(s) to capture positive externalities that could be generated by EC (e.g. Meetings, Incentive Travels, Conventions and Exhibitions, tourism, catering, hospitality, etc.);
- (c) the EC in WKCD will be uniquely positioned to serve the exhibition and conference needs of the CCI such as art fairs/exhibitions, art-related auctions/trading and performances, which currently have to face keen competition with other hirers; and
- (d) different financial models involving public and/or private sector funding were adopted for the development of convention and exhibition facilities in Hong Kong in the past years, and there are cases where Government support was given in the development of such facilities.

*(C) WKCDA to raise funds to finance the development of the remaining CACF and OACF*

15. Apart from the EC which will be delivered through the BOT arrangement, among the remaining CACF, WKCDA will give priority to the delivery of the Music Centre (a Batch 3 CACF) so as to provide a much-needed, purpose-built concert hall with appropriate acoustics, and up-to-date facilities to address the performance needs of the music community. As for the Great Theatre, Medium Theatre I, two black box theatres, M+ Phase II and Xiqu Small Theatre, they will be implemented by WKCDA having regard to demand and in line with the organic growth approach of WKCD. WKCDA will also tap market interest in developing the Musical Theatre through public-private partnership (PPP). In addition to allocating some of the OACF space to CCI for office use, WKCDA is also considering the case of providing an artist hostel and more arts education facilities in the WKCD through PPP.

16. According to the enhanced financial arrangement, WKCDA will share rental income with private developers under the BOT packages for the HOR and EHDA, providing it with additional recurrent income source for WKCDA. Yet, although the enhanced financial arrangement will help improve the long term financial situation of WKCDA, given its operating deficit in baseline scenario (paragraph 5 above), it is projected that WKCDA will continue to face a mitigated deficit until the BOT agreements gradually begin to expire and the developments concerned are reverted to WKCDA, bringing an enhanced recurrent income stream and achieving an operating surplus.

17. To fund the development of the Music Centre and its embedded OACF and RDE facilities as early as possible, and to tide over the interim operating deficit, WKCDA needs to explore various financing options (e.g. issuing bonds or raising bank loans) pursuant to the WKCDA Ordinance (Chapter 601)<sup>3</sup> by leveraging against its development right of HOR sites and long-term income stream. WKCDA will engage a financial consultant to draw up a comprehensive and affordable external borrowing plan taking into account the interest risks involved and cash flow requirements. The Government will continue to closely monitor WKCDA's financial position, requesting it to exercise stringent cost containment and deliver higher efficiency gains.

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<sup>3</sup> Section 24(1) provides that the WKCDA may borrow from the Government, or otherwise raise, moneys as may be required for the performance of its functions on such terms and conditions as may be approved by the Financial Secretary. Section 24(2) provides that subject to section 24(3), the WKCDA may borrow moneys from any person other than the Government for performing its functions while section 24(3) provides that the Chief Executive may issue a direction in writing for the purposes of this section of the WKCDA Ordinance (Chapter 601) to the WKCDA that it is not to borrow or raise any sum (or its equivalent in a currency other than Hong Kong dollar) which exceeds an amount specified in the direction without the prior written approval of the Financial Secretary.

### *(D) Sharing of surplus*

18. As mentioned in paragraph 7 above, one of the considerations of the enhanced financial arrangement is to provide sufficient but not excessive resources to WKCD A to meet its operating deficit in delivering and running arts and cultural facilities. It is projected that the enhanced financial arrangement will generate considerable cash inflow for WKCD A upon expiry of the BOT agreements and repayment of all external borrowing. It is therefore pragmatic and reasonable to build into the enhanced financial arrangement a mechanism that allows the Government to share the income generated from the HOR and EHDA development packages, upon expiry of the term of the BOT agreements, having regard to the funding requirements and financial position of WKCD A. The Government will retain, in the Project Agreement to be signed with WKCD A, the right to share such income with WKCD A upon expiry of the term of the BOT agreements. Such arrangement gives due recognition to the grant of development right of valuable HOR sites to WKCD A by the Government at nominal premium with or without the need for upfront payments.

### **Land Grant and Project Agreement**

19. The Government will enter into a Project Agreement with WKCD A to set out the legal rights and responsibilities of both parties, including the financial arrangements on upfront payments and on the right to share income generated from the HOR and EHDA development packages.

20. Pursuant to section 6 of the WKCD A Ordinance (Chapter 601), the WKCD A is governed by a Board comprising three public officers<sup>4</sup>. They will closely monitor the work of WKCD A to protect the Government's overall interests. In addition, Home Affairs Bureau, as the bureau responsible for overseeing WKCD A, will assist WKCD A in enhancing its corporate governance in respect of the formulation and management of BOT agreements, implementation of a sustainable charging policy for the WKCD venues and exercise of control over its capital and recurrent expenditures.

### **IMPLICATIONS OF THE PROPOSAL**

21. The enhanced financial arrangement has financial, economic and sustainability implications as set out at **Annex E**. The proposal is in conformity with the Basic Law, including the provisions concerning human rights. It has no civil service, productivity, family, environmental and gender

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<sup>4</sup> Under section 6 of WKCD A Ordinance (Chapter 601), the WKCD A Board consists of, among other members, three public officers and the Chairman who may or may not be a public officer. At present, the Chief Secretary for Administration serves as the Chairman and the Secretary for Home Affairs, the Secretary for Financial Services and the Treasury and the Secretary for Development serve as Board members.

implications.

## **PUBLIC CONSULTATION**

22. The existing financial approach of providing an upfront endowment (which was subsequently approved by LegCo in 2008) and vesting RDE facilities in WKCD to provide a source of recurrent income was the outcome of thorough deliberations of the CC Case. The enhanced financial arrangement is an extension of the existing financial approach and can be justified given the host of unforeseeable developments since 2008 as set out in Annex D.

23. Since 2009, the Government and WKCD have regularly reported the progress of the WKCD project and other related matters to LegCo Joint Subcommittee to Monitor the Implementation of the WKCD Project (Joint Subcommittee). The WKCD Board Chairman has presented annual updates on the financial situation of the WKCD project at the Joint Subcommittee since 2013. At the Joint Subcommittee meetings on 7 July 2015 and 30 May 2016, the Board Chairman informed Members of the financial challenges faced by WKCD due to escalation in construction costs and lower than expected investment returns, and that WKCD was exploring with the Government various options for enhancing the financing arrangements which include granting WKCD the development right of some or all of the commercial developments in WKCD, so as to enable WKCD to generate income to implement the rest of the project. Members were in general supportive of providing further financial support to the WKCD project. We will explain the enhanced financial arrangement in detail at the meeting of the Joint Subcommittee in February 2017.

## **PUBLICITY**

24. A press briefing will be arranged after the delivery of the 2017 Policy Address by the Chief Executive to introduce the details of the enhanced financial arrangement.

## **ENQUIRIES**

25. Enquiries on this brief can be directed to Mr Eric Cheng, Principal Assistant Secretary for Home Affairs (West Kowloon Cultural District) at 3102 3341.

**Home Affairs Bureau**  
**19 January 2017**

**Indicative distribution of GFA by uses in WKCD**

<b>Uses</b>	<b>Indicative distribution (sqm)</b>	<b>As percentage of total GFA</b>
Arts and Cultural Facilities (Including CACF and OACF)	337 340	40%
RDE Facilities	138 360	16%
HOR <sup>note</sup>	366 620	43%
Government/Institution/ Community Uses	9 080	1%
<b>Total</b>	<b>851 400</b>	

Notes:

According to the approved section 16 application with 15% increase in total GFA of WKCD, the maximum GFA for HOR uses is 366 620 sqm (around 43% of total GFA), of which no more than 170 280 sqm (i.e. 20% of total GFA) for residential use. There is thus flexibility in the exact distribution among HOR uses and the distribution in the table above.

**Batching and target completion timeframe of  
major WKCD facilities**

<b>Batching</b>	<b>Facilities</b>	<b>Status and target completion date</b>
<b>Batch 1</b>	Temporary Nursery Park	Opened in July 2015
	M+ Pavilion <i>(previously called Arts Pavilion)</i>	Opened in July 2016
	Xiqu Centre <i>(including Tea House)</i>	Main works in progress Target for completion in late 2017 and opening in latter half of 2018
	Art Park	Construction works in progress Target for completion in 3 phases and opening in stages starting from 2018
	Freespace <i>(including Outdoor Stage and Black Box Theatre)</i>	Construction works in progress Target for completion in 2018 and opening in 2019
	M+ Building	Main works in progress Target for completion in 2018 and opening in latter half of 2019
<b>Batch 2</b>	Lyric Theatre Complex <i>(including a Lyric Theatre, a Medium Theatre and a Studio Theatre)</i> <sup>note 1</sup>	Foundation works in progress Detailed design substantially completed
	Centre for Contemporary Performance (CCP) <i>(including two Black Box Theatres)</i>	Mode of development of the remaining two Black Box Theatres to be reviewed as one of the three Black Box Theatres in CCP have been incorporated into the Lyric Theatre Complex
	Medium Theatre II <sup>note 1</sup>	Incorporated into the Lyric Theatre Complex

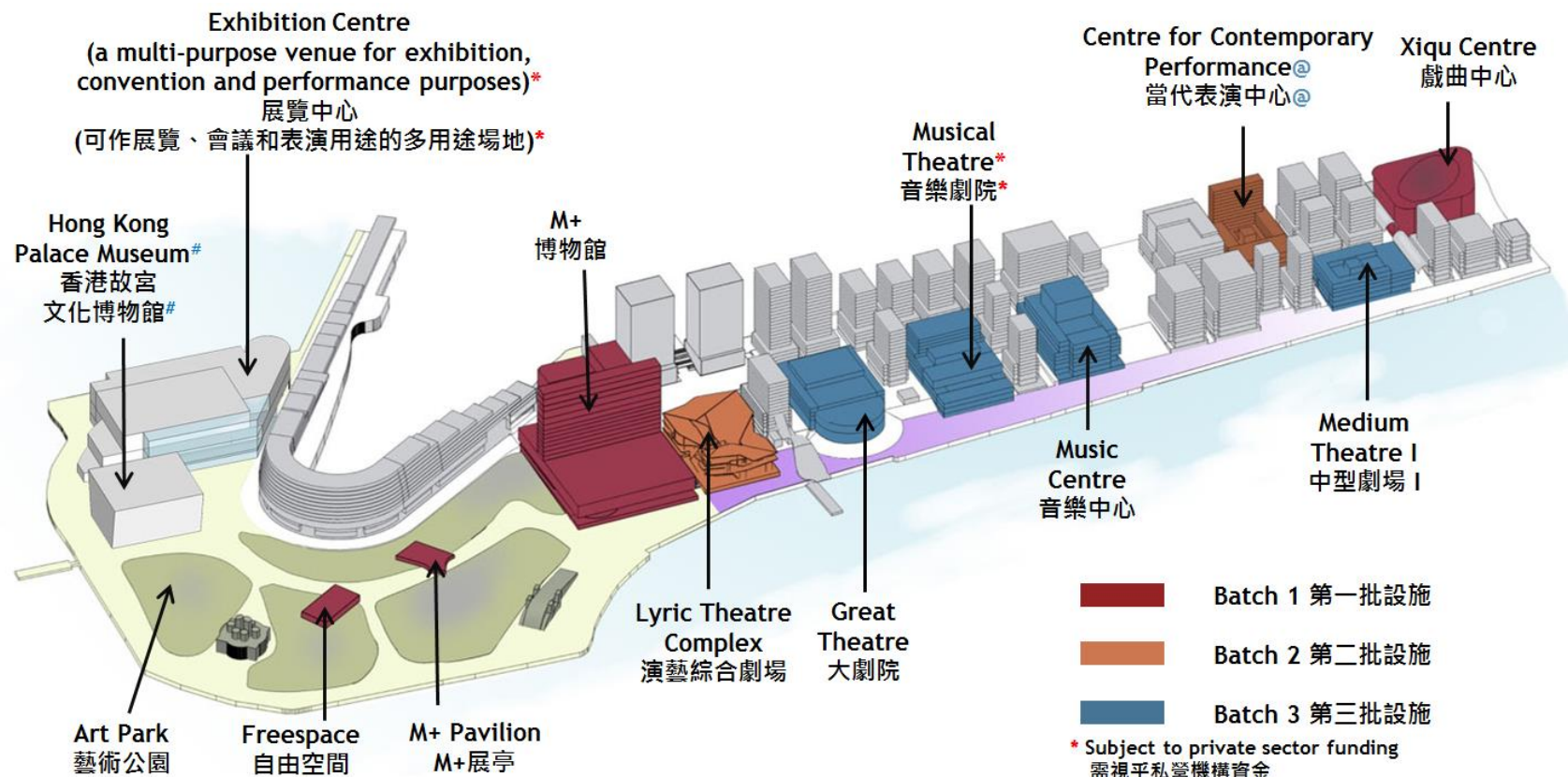
<b>Batching</b>	<b>Facilities</b>	<b>Status and target completion date</b>
<b>Batch 3 facilities</b>	Music Centre <i>(including Concert Hall and Recital Hall)</i>	High priority under the enhanced financial arrangement
	Musical Theatre	To be developed through public-private partnership subject to private sector funding
	Great Theatre	To be reviewed by WKCDA and delivered gradually having regard to demand in line with the organic growth approach of WKCD
	Medium Theatre I	
<b>Not phased</b>	EC <sup>note 2</sup>	To be developed through public-private partnership subject to private sector funding
	M+ Phase II	To be reviewed by WKCDA and delivered gradually having regard to demand in line with the organic growth approach of WKCD
	Xiqu Small Theatre	

Notes:

1. The originally proposed Medium Theatre II and one black box theatre (now called Studio Theatre) of the CCP were incorporated into the original Lyric Theatre to form the Lyric Theatre Complex to advance their provision.
2. In September 2016, the Board of WKCDA agreed that the original proposal to build a MPV co-located with the EC in WKCD was no longer a suitable proposition and that the EC should be developed into a medium-sized, multi-purpose venue for exhibition, convention and performance purposes. Furthermore, the Board of WKCDA has approved the proposal for the development of the Hong Kong Palace Museum in November 2016 and the public consultation for this project is currently in progress.



**Schematic plan of major WKCD facilities**



\* Subject to private sector funding  
需視乎私營機構資金

@ Future development to be reviewed due to partial incorporation into Lyric Theatre Complex  
由於部分設施已納入演藝綜合劇場，未來發展需再研究

# Development funded by donation;  
public consultation underway  
由捐款資助發展；相關公眾諮詢進行中

**Summary of factors/developments leading to  
WKCD's financial difficulties**

The financial difficulties faced by WKCD in terms of capital cost are the result of a combination of developments and changes since the adoption of the CC Case in 2006 –

- (a) There has been significant **escalation of construction costs** since the approval of the \$21.6 billion upfront endowment in 2008 (by 136% from Q3 2006<sup>1</sup> to Q2 2016 or by average increase of 9% per annum compounded since 2006 as opposed to 2% per annum assumed in the CC Case);
- (b) For a sustained period, the global investment markets have experienced high volatility and a significant **decline in investment return**. The actual investment return from the endowment (3.2% per annum from 2008-09 to 2015-16) is significantly lower than the assumed rate of 6.1% per annum in the CC Case;
- (c) The **prolonged planning and public engagement process** (about four years including the three-stage public engagement exercise) had resulted in approval of the submission of the DP by the CE-in-Council only in January 2013, and cost for delivering the CACF escalated significantly during this period; and
- (d) The **complexity** involved in implementing the “City Park” design concept, which makes construction of an integrated basement a pre-requisite of any topside developments, as well as the vertical integration of different uses within a building have increased construction costs and extended the delivery timeframe of CACF.

2. WKCD suffers from **serious delay in the receipt of RDE income**, which is intended to be a steady recurrent income source to meet the operating deficits of CACF. Due to the extended development timeframe of WKCD, the deferred possession of site being occupied as construction sites/works areas of the XRL, as well as the priority given to developing CACF, the majority (over 65%) of the RDE facilities will only be completed beyond 2022.

3. As the WKCD project enters into the operational phase, WKCD needs to **increase its operating budget** for additional manpower and/or expenses on the following areas –

- (a) **Project delivery and management:** The “City Park” design concept which requires a high degree of integration of various facilities in WKCD and involves the development of an integrated basement, coupled with the encroachment of the West Kowloon Terminus of the XRL into WKCD, have made project delivery far more complex than was originally envisaged. A strong project delivery and management team staffed by experienced professionals has to be set up in WKCD to plan and coordinate the work;

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<sup>1</sup> The estimated costs in the CC Case were prepared by the Financial Advisor in 2006. The Architectural Services Department's tender price indices for building works in the public sector has gone up from 751 in Q3 2006 to 1 776 in Q2 2016.

- (b) **Cultural software development:** In recognition that the development of cultural software is important for promoting the development of the district, strengthening connection between WKCD and the public, and building audiences for WKCD, WKCDA has taken on new missions in programme development, audience building and professional development to enhance the profile, interest and capacity of arts and culture in Hong Kong;
- (c) **Commercial operations, marketing and fundraising:** The need for WKCDA to ensure the financial sustainability necessitates the recruitment of staff with strong background and attributes in operation, management and leasing of commercial facilities (such as RDE), marketing and ticketing as well as solicitation and management of donation and sponsorship; and
- (d) **Facilities management:** As WKCD progresses from the planning phase to the operational phase, it has to review and adjust the budget for facilities management based on actual operational needs.

**Implications of the proposal**

**Financial Implications**

Government has provided substantial financial support to the development of WKCD through an upfront endowment of \$21.6 billion to finance the capital costs of the project, and a commitment to construct the integrated basement and the related public infrastructure works. The Executive Council decided in 2008 that the RDE sites in WKCD would be vested in WKCDA at nominal premium to provide a steady source of recurrent income.

2. Regarding the development of the HOR sites, the current proposal of granting the development right of the sites to WKCDA at nominal premium and allowing WKCDA to seek upfront payments from private developer(s) for the BOT packages having regard to tender conditions pursuant to an open and competitive bidding process would result in land revenue forgone for the Government. While the upfront payments payable by the developer(s) to WKCDA would be attributable to Government, given the rental income sharing arrangements between the developer(s) and WKCDA and the retention of ownership of the HOR sites by WKCDA under the BOT arrangement, the upfront payments to be received by Government will inevitably be lower than the full market value land premium that can be fetched under normal land disposal arrangements. The magnitude of revenue forgone and the actual amount of payment received by the Government depend on the result of the open and competitive tendering.

3. The development right of the office and hotel portion in the EHDA package will be granted to WKCDA at nominal premium for it to develop the sites under a BOT package with rental income sharing arrangements between the developer(s) and WKCDA. Developer(s) is not required to make any upfront payment to WKCDA (which is in turn attributable to Government) but is required to share rental income with WKCDA.

4. To give due recognition to the substantial financial support provided by Government to WKCDA through the grant of development right of HOR sites to WKCDA at nominal premium with or without the need for upfront payments, Government will retain the right to share the income generated from the HOR and EHDA development packages, upon expiry of the BOT period, having regard to WKCDA's funding requirements and financial position.

5. Should the external borrowing to be entered into by WKCDA require any guarantee involving financial liability upon Government, approval from the LegCo Finance Committee should be sought.

## **Economic Implications**

6. The enhanced financial arrangement, which transfers some of the potential income stream generated from the development right of HOR sites in WKCD to WKCDA, will help improve WKCDA's financial capability to develop WKCD in accordance with the integrated development design concept and organic growth approach, and to operate the WKCD in a sustainable manner. The successful development of the WKCD would help foster vibrant cultural activities, thereby raising the people's quality of life. Through supporting the development of a creative economy, nurturing local talents, attracting and retaining investors and talents, it could also facilitate the development of Hong Kong as a knowledge-based economy and a world city.

7. As the proposed upfront payment, by its nature, will inevitably be lower than the full market value land premium that can be fetched under the normal land disposal practice (paragraph 2 above), the enhanced financial arrangement may be perceived as giving the eventual developments of rental office, hotel and rental residential units within the WKCD a development cost advantage over other similar developments. Nonetheless, this advantage will be offset by the requirement for developers to share income and hand over the control of the premises to WKCDA under the BOT packages. So long as the tendering process is and competitive, the tender result would reflect the price the market is willing to pay taking into account all conditions attached to the tender. As such, there should be minimal effect on competition in the overall rental HOR markets.

## **Sustainability Implications**

8. The proposal will provide WKCDA the financial capacity to develop the remaining WKCD facilities which could not only support the development of arts and culture in Hong Kong but also add impetus to and diversify economy as well as create opportunities for young people.