

For information

**Legislative Council
Panel on Development and Panel on Home Affairs
Joint Subcommittee to Monitor the Implementation of the
West Kowloon Cultural District Project**

Follow-up to Meeting on 21 February 2017

Following the meeting of the Joint Subcommittee to Monitor the Implementation of the West Kowloon Cultural District Project (Joint Subcommittee) on 21 February 2017, the Government and the West Kowloon Cultural District Authority (WKCDA/the Authority) provide supplementary information as requested below -

Monitoring the financial situation of the West Kowloon Cultural District (WKCD) Project

- a) **given that the income to be shared by WKCDA from the development packages under the enhanced financial arrangement would be subject to the result of the tendering process, how the Administration could ensure that WKCDA would be provided with sufficient but not excessive resources;**

According to the financial assessment conducted based on various assumptions, WKCDA estimated that the recurrent income it can share from the development packages during the Build-Operate-Transfer (BOT) period will only mitigate the operating deficits. However, upon expiry of the BOT agreements when the developments concerned would be reverted to WKCDA and the income sharing requirements with private sector partners would cease, WKCDA will have considerable cash inflow as it will capture all of the net income from these developments. It is envisaged that such strong cash inflow will provide WKCDA the necessary financial capability to operate WKCD in a sustainable manner.

As one of the major considerations in formulating the enhanced financial arrangement is to provide sufficient but not excessive resources to WKCDA to meet its financial difficulties, a mechanism will be built into the enhanced financial arrangement to give the Government the right to share with WKCDA the income generated from the developments, upon

expiry of the BOT agreements, having regard to the funding requirements and financial position of WKCDA. The Government will set out in the Project Agreement to be signed with WKCDA the principles for the sharing mechanism and will formulate the detailed arrangement with WKCDA in due course.

- b) **given that WKCDA would no longer need the funding approval of the Finance Committee for the development of the facilities in WKCD (except for the integrated basement) and its operational costs, how the Legislative Council (LegCo) could effectively monitor the financial situation of the WKCD project;**

As with the undertaking and arrangement in the past nine years since the Finance Committee (FC) approved the grant of \$21.6 billion upfront endowment to WKCDA, WKCDA will, in conjunction with the Government, continue to report regularly to LegCo (via the Joint Subcommittee) the progress of the WKCD project, including its hardware and software developments, the financial situation of WKCDA, as well as the implementation of the enhanced financial arrangement. Furthermore, the Government will continue to seek funding approval from the FC in the years to come for implementing the public infrastructure works and the Integrated Basement, during which LegCo will be updated on the development progress of WKCD and able to perform its monitoring role over the WKCD project.

Tendering of the development packages

- c) **how the Administration or WKCDA could ensure that the tendering of the hotel/office/residential (HOR) development packages would be conducted in an open and competitive manner and whether there were any relevant guidelines for WKCDA to follow;**

WKCDA will adopt open and competitive tendering in selecting private sector partners for the individual development packages. WKCDA will draw up a set of guidelines regarding the tendering of the HOR development packages, having regard to current market best practices. To this end, WKCDA has set up an internal task force to plan for the implementation of the enhanced financial arrangement and one of its tasks is to prepare the aforementioned tendering guidelines for WKCDA Board's approval. As the highest governing and executive body of the Authority, the WKCDA Board, chaired by the Chief Secretary for Administration and with three Principal Officials appointed as members, will closely monitor

the implementation of the enhanced financial arrangement.

Procurement of consultancy services

- d) **the justification for the WKCDA Management to appoint Rocco Design Architects Limited in June 2016 to provide advance consultancy services in a bundle, covering a preliminary technical study on the Mega Performance Venue/Exhibition Centre (MPV/EC) site (i.e. P46/P47 land parcels) for the integrated development of Exhibition Centre, hotels, offices and a proposed new museum, and to provide conceptual design for reference and cost estimation;**

Rocco Design Architects Limited (RDA) was engaged by WKCDA Management under its delegated authority in June 2016 to provide consultancy service including conducting a preliminary technical feasibility study of the integrated development of an Exhibition Centre, hotels, offices and a proposed new museum on land parcels P46/P47 (i.e. the MPV/EC site) and the adjoining U-shaped site, and to provide a conceptual design for the purpose of cost estimation and budgeting by WKCDA. This study was commissioned in response to the Board's advice in November 2015 that further studies on the future use of the P46/P47 site should be conducted given that the proposition of developing a MPV in WKCD might no longer be viable.

- e) **the procurement guidelines of WKCDA in relation to hire of consultancy services, including those related to direct appointments; and whether the financial advisor for the enhanced financial arrangement had been engaged by way of direct appointment;**

A set of the procurement policy, procedures and guidelines is available at the WKCDA website for public reference.

WKCDA Management has used "request for quotations" under its delegated authority to engage the financial consultant for preparing financial modelling for the Exhibition Hub development. The financial consultant was subsequently requested by the Management to extend the service to providing assessment on the business case analysis of the Exhibition Hub and financial projections and assumptions on commercial development through variation to contract, which is provided for under the established procurement procedures of WKCDA.

Land value of the development packages

f) the estimated land value of the HOR portion and the retail/dining/entertainment (RDE) portion of WKCD;

The financial advisor who assisted the Financial Matters Advisory Group of the Consultative Committee on the Core Arts and Cultural Facilities of the West Kowloon Cultural District estimated in 2007 that the land sale value of the RDE sites in WKCD, with a total Gross Floor Area (GFA) of 119 000 m² and the HOR sites with a total GFA of about 308 940 m², would be about \$3.2 billion and \$18.9 billion respectively in 2006 Net Present Value. This estimation was made prior to the formulation of the Development Plan for WKCD, i.e. before the adoption of Foster + Partners' "City Park" Conceptual Plan. With the approval of the Development Plan and the subsequent application made to the Town Planning Board under section 16 of the Town Planning Ordinance (Cap. 131) for minor relaxation of development intensity of WKCD (which included a 15% increase in total GFA), the previous estimated land sale value is no longer valid as the GFA for RDE facilities has increased to 138 360 m² while the GFA for HOR developments has also increased to 366 620 m².

It has always been the Government's plan to vest the RDE part of the commercial sites in WKCD in WKCDA at nominal premium to provide it with a steady source of recurrent income through rental proceeds to meet the operating deficits of the core arts and cultural facilities and related facilities. As such, WKCDA has not re-evaluated the land sale value of the RDE facilities since the estimation was made in 2007.

As for the HOR portion, the land sale value will depend on the specific tender conditions, the prevailing market situation and the GFA distribution ratio among the three uses which has yet to be determined. WKCDA's current plan is to develop the major portion of the GFA of the HOR sites into rental offices and a small portion into rental residential units. In other words, the GFA of rental residential use will be lower than the upper limit permitted under the approved Development Plan (i.e. not more than 20% of the total GFA of WKCD). Since there is no land sale under the enhanced financial arrangement, it will be inappropriate to estimate and apply the present-day value of the HOR sites through normal land disposal to that under the enhanced financial arrangement.

Financial analysis for the enhanced financial arrangement

- g) detailed financial projections for the enhanced financial arrangement, including estimates on the upfront payment for the Government and income shared by WKCDA, whether the income generated for WKCDA could cover the shortfall in the funds for developing and operating the arts and cultural facilities to be provided in WKCD, how long a 'build-operate-transfer' contract would last, the yearly discounted cash flows for WKCDA, and the financial model adopted for making the projections/analysis, if any;**

The enhanced financial arrangement would allow WKCDA to share the rental income from the HOR developments during the BOT period to sustain the operation of WKCD under pre-determined ratios. The amount of income to be shared by WKCDA would depend on the prevailing market situation and the development parameters set by WKCDA for the individual development packages.

On the other hand, the Government will receive upfront payment from the successful bidder (except for the Exhibition Hub Development Area (EHDA)) to be selected by WKCDA through open tendering. The total amount of upfront payment to be received by the Government will depend on the amount the market is willing to offer having regard to the specific tender conditions of the individual development packages.

The BOT period will have to be reasonably long to be commercially attractive, e.g. 30 years, but should not exceed the term of the Land Grant to WKCDA.

In preparing the proposal for the enhanced financial arrangement, WKCDA has conducted a financial assessment based on a set of assumptions and market information. As the assumptions adopted in the financial assessment involve commercially sensitive information the disclosure of which will affect relevant tendering process, the details of the financial projections cannot be provided to the Joint Subcommittee at this stage.

According to the financial assessment conducted based on various assumptions, WKCDA estimated that the recurrent income it can share from the development packages during the BOT period will only mitigate the operating deficits. However, under the enhanced financial arrangement, WKCDA can leverage against its development right of HOR sites and long-term income stream to explore different financing options. Moreover,

upon expiry of the BOT agreements when the developments concerned would be reverted to WKCDA and the income sharing requirements with private sector partners would cease, WKCDA will have considerable cash inflow as it will capture all of the net income from these developments. As such, it is anticipated that the enhanced financial arrangement will provide WKCDA with the financial capability to operate sustainably the various facilities in WKCD and continue to develop WKCD under an organic growth approach, in particular a world-class Music Centre.

h) whether minimum upfront payment and ratios of income sharing between WKCDA and the developer would be worked out before tendering the development packages, and whether there were initial formulations for the sharing of surplus between WKCDA and the Government.

For the EHDA, instead of setting a predetermined ratio for income sharing with WKCDA as a tender condition, tenderers will be required to indicate the ratio 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. For the remaining HOR development packages, the tenderers will need to indicate an upfront payment that they propose to pay given the tender conditions (including a predetermined ratio for income sharing with WKCDA) set by WKCDA. The offer on the income sharing ratio for the EHDA development package and the offer on the upfront payment for the remaining HOR development packages will be a factor for consideration in the tender assessment by WKCDA. To ensure that private sector developers would propose a reasonable offer, WKCDA is required to come up with its own assessment of the income sharing ratio under full market value for the EHDA development package as well as the full market value of the upfront payment for the remaining HOR development packages. WKCDA may cancel the tender if the offer on income sharing ratio and the upfront payment is unreasonably low vis-à-vis the prior assessment of the full market values mentioned above. WKCDA will further study the details of the tendering arrangement for individual development packages to ensure the offer on upfront payment or income sharing ratio is reasonable while taking into account the commercial viability of the development packages.

As one of the major considerations in formulating the enhanced financial arrangement is to provide sufficient but not excessive resources to WKCDA to meet its financial difficulties, a mechanism will be built into the enhanced financial arrangement to give the Government the right to

share with WKCDA the income generated from the developments, upon expiry of the BOT agreements, having regard to the funding requirements and financial position of WKCDA.

The Government will set out in the Project Agreement to be signed with WKCDA the principles for the sharing mechanism and will formulate the detailed arrangement with WKCDA in due course.

Home Affairs Bureau
West Kowloon Cultural District Authority
April 2017