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**Joint Subcommittee to Monitor the Implementation of
the West Kowloon Cultural District Project**

Meeting on 1 June 2020

**Updated background brief on
the financial situation of the West Kowloon Cultural District project**

Purpose

This paper summarizes the major views and concerns expressed by members of the Joint Subcommittee to Monitor the Implementation of the West Kowloon Cultural District Project ("the Joint Subcommittee") on the financial situation of the West Kowloon Cultural District ("WKCD") project.

Background

Upfront endowment to the West Kowloon Cultural District Authority

2. On 4 July 2008, the Finance Committee ("FC") of the Legislative Council ("LegCo") approved a one-off upfront endowment of \$21.6 billion in money-of-the-day ("MOD") prices for the West Kowloon Cultural District Authority ("WKCDA") to implement the WKCD project. According to the relevant funding proposal ([FCR\(2008-09\)35](#)), the upfront endowment was intended to cover the capital costs of the WKCD project,¹ while the retail/dining/entertainment ("RDE") part of the WKCD development would be vested in WKCDA to provide a source of recurrent income through rental proceeds for meeting the operating costs of the arts and cultural facilities and

¹ The broad breakdown of the upfront endowment was as follows: (a) design and construction of various facilities (\$15.7 billion or 73%); (b) major repair and renovation of various facilities (\$2.9 billion or 13%); (c) collection costs and related costs for M+ (\$1.7 billion or 8%); and (d) planning of WKCD and project management (\$1.3 billion or 6%).

related facilities. Other communal and government facilities and related engineering works, such as roads, drainage and fire station, would be undertaken by the Administration, and funding approval for such works would be sought separately in accordance with the development programme.²

3. In July 2013, the Administration and WKCD advised the Joint Subcommittee that in view of the expansion in project scope and the significant escalation of construction costs, a pragmatic approach would be adopted to implement the WKCD project through, among others, rigorous cost containment of individual facilities. Furthermore, the Administration intended to fully fund the capital works of the integrated basement ("IB")³ as general enabling works to facilitate the development of the whole WKCD project.

4. In May 2014, the Administration and WKCD advised that the portion of the upfront endowment for the design and construction of facilities (i.e. \$15.7 billion) plus the apportioned interest income (i.e. \$2.1 billion) would only be sufficient to cover the costs of the design and construction of the Batch 1 and most of the Batch 2 facilities,⁴ while the implementation programme of the Batch 3 facilities would have to be reviewed. A table showing the batching, status and target completion dates of major WKCD facilities, and a schematic plan of these facilities are in **Appendices I and II** respectively.

² Funding proposals relating to the WKCD development, other than the integrated basement ("IB"), approved by FC included:

- (a) \$478 million for the design and site investigation of government infrastructure works in WKCD (approved in January 2013);
- (b) \$840.5 million, \$192 million and \$380 million respectively for the three packages of the construction of public infrastructure works in WKCD (approved in July 2015, April 2018 and March 2020 respectively, totalling \$1,412.5 million); and
- (c) \$981.2 million for the relocation of the supporting operational facilities of Tsim Sha Tsui Fire Station Complex, Fire Services Club and other Fire Services accommodations (approved in March 2020).

³ In respect of the construction of IB for WKCD, FC approved \$2,919.5 million for the first and second stages of design, site investigation and construction works, \$3,178.4 million for the third stage of construction works and \$17,472.3 million for the remaining works in July 2015, January 2018 and March 2020 respectively, totalling \$23,570.2 million.

⁴ In April 2019, WKCD advised that the capital costs of the Batch 1 and most of the Batch 2 facilities as well as related facilities were estimated to increase from \$17.8 billion in MOD prices to \$20.1 billion in 2019-2020, mainly due to adjustments to the contingency cost provision for the Xiqu Centre, M+ and Lyric Theatre Complex.

Enhanced financial arrangement

5. To provide WKCD with the financial capability to operate sustainably the various facilities in WKCD and continue to develop the remaining planned facilities, the Government agreed to provide an enhanced financial arrangement ("EFA") for WKCD, under which WKCD would be granted the development right of the entire hotel/office/residential ("HOR") portion of WKCD. The key components of EFA for WKCD are set out below:⁵

- (a) *grant of development right of entire HOR portion of WKCD to WKCD with upfront payment to the Government:* the Government will grant the development right of the entire HOR portion of WKCD (involving 366 620 square metres ("m²") gross floor area ("GFA")) to WKCD at nominal premium so that the Authority may tender out the development packages of HOR together with the RDE embedded therein, develop these commercial developments under the Build-Operate-Transfer ("BOT") model and receive rental income. Meanwhile, upfront payment should be paid by WKCD to the Government according to the financial arrangements to be specified in a Project Agreement to be signed between the Government and WKCD⁶ as well as the relevant tendering results;
- (b) *grant of development right of the Art, Commerce and Exhibitions ("ACE") development package (formerly known as the Exhibition Hub Development Area) to WKCD without upfront payment to the Government:* the Government will grant the development right of 81 066 m² GFA of hotel and office uses (i.e. about 22% of the total GFA of the HOR sites) in the U-shaped site adjacent to the Exhibition Centre to WKCD at nominal premium without the need for paying an upfront payment to the Government. WKCD should tender out a BOT development package of ACE comprising the Exhibition Centre, a hotel and rental offices together with the embedded RDE facilities;

⁵ Sources: [Legislative Council Brief on Enhanced Financial Arrangement for WKCD](#) and [LC Paper No. 559/17-18\(01\)](#)

⁶ According to the Administration, the Project Agreement will set out the legal rights and responsibilities of the Government and WKCD, including the financial arrangements on upfront payment and on the right to share income generated from the HOR and Art, Commerce and Exhibitions development packages.

- (c) *WKCD A to raise funds to finance the development of the remaining core arts and cultural facilities ("CACF") and other arts and cultural facilities ("OACF")*: WKCD A will explore various financing options (e.g. issuing bonds or raising bank loans) pursuant to the WKCD A Ordinance (Cap. 601)⁷ by leveraging against its development right of the HOR sites and long-term income stream. WKCD A 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; and
- (d) *sharing of surplus*: the Government will share the income generated from the HOR and ACE development packages, upon expiry of the term of the BOT agreements, having regard to the funding requirements and financial position of WKCD A.

Financial position of the West Kowloon Cultural District Authority reported in April 2019

6. At the meeting of the Joint Subcommittee in April 2019, the Administration and WKCD A briefed members on the financial position of WKCD A. According to them, the original endowment of \$21.6 billion was expected to have generated an estimated accumulated return on investment of \$7.1 billion by the end of the financial year 2018-2019, and the balance of the endowment by then was estimated to stand at \$13.6 billion. The forecast/estimated income, expenses and operating deficit before depreciation of WKCD A in the financial years from 2018-2019 to 2021-2022 provided by WKCD A are set out below:⁸

⁷ Under the WKCD A Ordinance (Cap. 601), section 24(1) provides that WKCD A 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 ("FS"); section 24(2) provides that subject to section 24(3), WKCD A may borrow moneys from any person other than the Government for performing its functions; and section 24(3) provides that the Chief Executive may issue a direction in writing for the purposes of this section to WKCD A that it is not to borrow or raise any sum (or its equivalent in a currency other than Hong Kong dollars) which exceeds an amount specified in the direction without the prior written approval of FS.

⁸ Source: [LC Paper No. CB\(1\)914/18-19\(01\)](#)

(\$ million)	2018-2019 forecast	2019-2020 estimates	2020-2021 estimates	2021-2022 estimates
Estimated income	631	412	515	682
Estimated expenses	658	1 259	1 622	1 868
Estimated operating deficit before depreciation	(27)	(847)	(1 107)	(1 186)

7. WKCDA also advised that among the Batch 3 CACF, it would give priority to the delivery of the Music Centre to address the performance needs of the music community and the estimated capital cost of the Music Centre project would be around \$6 to \$7 billion in MOD prices.

Major views and concerns of members

8. Issues relating to the financial situation of the WKCD project were discussed at meetings of the Joint Subcommittee. The major views and concerns expressed by members are summarized in the ensuing paragraphs.

Adequacy of the upfront endowment

9. Members expressed grave concern over the serious cost overrun of the WKCD project as well as the uncertainty about the extent of the cost overrun problem. Some members were worried whether, with the spiralling cost of the WKCD project, the Administration was planning to shelve the development of the Batch 3 facilities or cut down on the resources to be allocated for the WKCD development. Some other members, however, expressed the view that given the huge cost overrun of the WKCD project, the Administration and WKCDA should critically examine the scope of the project and come to an early decision on which facilities would and would not be taken forward.

10. The Administration and WKCDA explained that the increase in the capital costs of the WKCD project was attributed to a number of factors, including the significant escalation of construction costs in Hong Kong in recent years, the inclusion of IB as an integral part of the approved Development Plan ("DP") of WKCD, enhanced project scope to meet public aspirations reflected during the public engagement exercise on DP (such as adding space for education facilities in different venues), and longer time taken to complete the master planning and planning approval process for WKCD.

11. In view of the above, the Administration considered it a pragmatic arrangement for WKCDA to make efficient use of the endowment fund and the associated investment return to complete the Batch 1 and Batch 2 facilities for early public enjoyment. As for the Batch 3 facilities, WKCDA had been working with the Administration to identify alternative approaches to take forward the development of the Exhibition Centre through BOT and the Musical Theatre through public-private partnership.

12. Members had asked about the feasibility of some options to bridge the funding gap in the delivery of the remaining CACF, such as providing additional funding or loans by the Government to WKCDA, or taking back the sites leased to WKCDA for the remaining facilities for developing performance arts venues by the Leisure and Cultural Services Department ("LCSD").

13. The Administration advised that it had no plan to provide further funding to WKCDA for the construction of CACF, and considered it not conducive to the integrated development of WKCD if part of the district was resumed for development by LCSD. In April 2019, WKCDA informed members that the Authority would commence a consultancy to provide financial advisory services in Q2 2019 to review its budget and draw up an external borrowing plan expected to be completed in Q3/Q4 of 2019 subject to the progress of the consultancy study.

Operating deficit faced by the West Kowloon Cultural District Authority

14. Some members expressed worry on the huge operating deficit faced by WKCDA. They asked about the measures to reduce the deficit and whether WKCDA would expedite the commercial developments in WKCD to generate income in a timely manner.

15. WKCDA advised that it had suffered from a serious delay in the receipt of sustainable sources of income expected to be generated from the topside commercial developments above IB to underpin the operation of the arts and cultural facilities. While the income received from business activities, ticketing and sponsorships following the progressive opening of various facilities in WKCD in the coming years could help improve the short-term financial situation of WKCDA, the long-term financial situation of WKCDA would be significantly improved by the cash inflow from the ACE project and HOR developments in WKCD under the BOT arrangement.

16. According to WKCDA, it had adhered to the fiscal principle of "spending where necessary and saving where possible". The Authority had also widened its income sources (such as launching public fundraising campaigns via the newly established WKCD Foundation Limited) and exercised stringent cost control over the years. In addition, with the implementation of cost control measures, WKCDA's estimated operating deficit before depreciation in financial year 2018-2019 had significantly improved from \$312 million (February 2018 estimate) to \$27 million (April 2019 estimate).

Details of the enhanced financial arrangement

17. Some members enquired about the details of the financial projections for EFA, including the estimates on the upfront payment to be paid to the Government and the income to be shared by WKCDA, and whether the income generated for WKCDA could cover the shortfall in the funds for developing and operating the arts and cultural facilities in WKCD. They also queried if a financial advisor had been engaged to examine EFA.

18. WKCDA indicated that in preparing the EFA proposal, it had engaged a financial advisor to conduct a financial assessment based on a set of assumptions and market information. As the assumptions adopted in the financial assessment involved commercially sensitive information the disclosure of which would affect relevant tendering process, the details of the financial projections could not be provided to the Joint Subcommittee at that stage.

19. The Administration advised that EFA would allow WKCDA to share the rental income from the HOR developments during the BOT period to sustain the operation of WKCD under predetermined 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. 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 would have considerable cash inflow as it would capture all of the net income from these developments.

20. Some members further pressed for information including the terms of the BOT agreements, the estimated land value of the HOR and RDE portions of WKCD and the return on the rentals of the HOR portion, etc. They opined that in the absence of such relevant information, it was doubtful whether it

was appropriate to grant the HOR and RDE portions of WKCD to WKCDA at nominal premium. Some members were worried that the granting of the HOR and RDE portions of WKCD to WKCDA under EFA would amount to making WKCDA an "independent kingdom".

21. The Administration clarified that it had always been the Government's plan to vest the RDE portions of 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 CACF and related facilities. An estimation of the land sale value of the RDE facilities had been made in 2007. As for the HOR portion, the land sale value would depend on the specific tender conditions, the prevailing market situation and the GFA distribution ratio among the HOR uses which had yet to be determined. WKCDA's plan was to develop the major portion of GFA of the HOR sites into rental offices and a small portion into rental residential units together with the embedded RDE facilities in phases under the BOT model.

22. The Administration further advised that certain terms and conditions would be imposed in the BOT tenders to protect the Government's interests under EFA. For instance, WKCDA would be required to tender out the relevant sites through multiple BOT development packages to increase competition so that contracts would not be awarded to a single developer. WKCDA would also retain the right to cancel the tender if the tender price offered by tenderers was unreasonably low.

Monitoring the financial situation of the West Kowloon Cultural District project

23. Some members enquired how the Administration could effectively monitor the financial situation of the WKCD project under EFA. There was also a concern on whether the approach for bridging the capital funding gap by external borrowing was a means for bypassing the scrutiny of LegCo over the spending for the WKCD project.

24. The Administration advised that three directors of bureaux or their alternates, being members of the WKCDA Board, were responsible for, among others, monitoring the financial situation of WKCDA. A mechanism would also be built into EFA to give the Government the right to share with WKCDA the income generated from the developments upon expiry of the BOT agreements. The Administration would set out in the Project Agreement to be signed with WKCDA the principles for the income sharing mechanism and would formulate the detailed arrangement with WKCDA in due course. Moreover, the Administration had no intention to bypass LegCo's scrutiny

over the WKCD project. The Administration would, in conjunction with WKCDA, continue to report regularly to 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 EFA.

Latest development

25. At the meeting of the Joint Subcommittee to be held on 1 June 2020, the Administration and WKCDA will update members on the latest financial situation of the WKCD project.

Relevant papers

26. A list of the relevant papers on the LegCo website is in **Appendix III**.

Council Business Division 1
Legislative Council Secretariat
26 May 2020

Appendix I

Status and target completion date of major West Kowloon Cultural District facilities

Facilities	Status and target completion date
<i>Batch 1</i>	
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>	Opened in January 2019
Art Park	Phase 1 of the Art Park and a section of the waterfront promenade was opened in early 2018. Phases 2A and 2B of the Art Park were opened in March 2019. The remaining Phase 3 will be opened by the end of 2019
Freespace	Construction works in progress Target to be in use in June 2019
M+ Building	Main works in progress Target to secure the Occupation Permit in Q1 2020, with opening of the Museum approximately a year later
<i>Batch 2</i>	
Lyric Theatre Complex ("LTC") <i>(including a Lyric Theatre, a Medium Theatre and a Studio Theatre)</i> ^(note)	Main work in progress Target to secure the Occupation Permit in 2023
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 has been incorporated into the LTC
Medium Theatre II ^(note)	Incorporated into the LTC

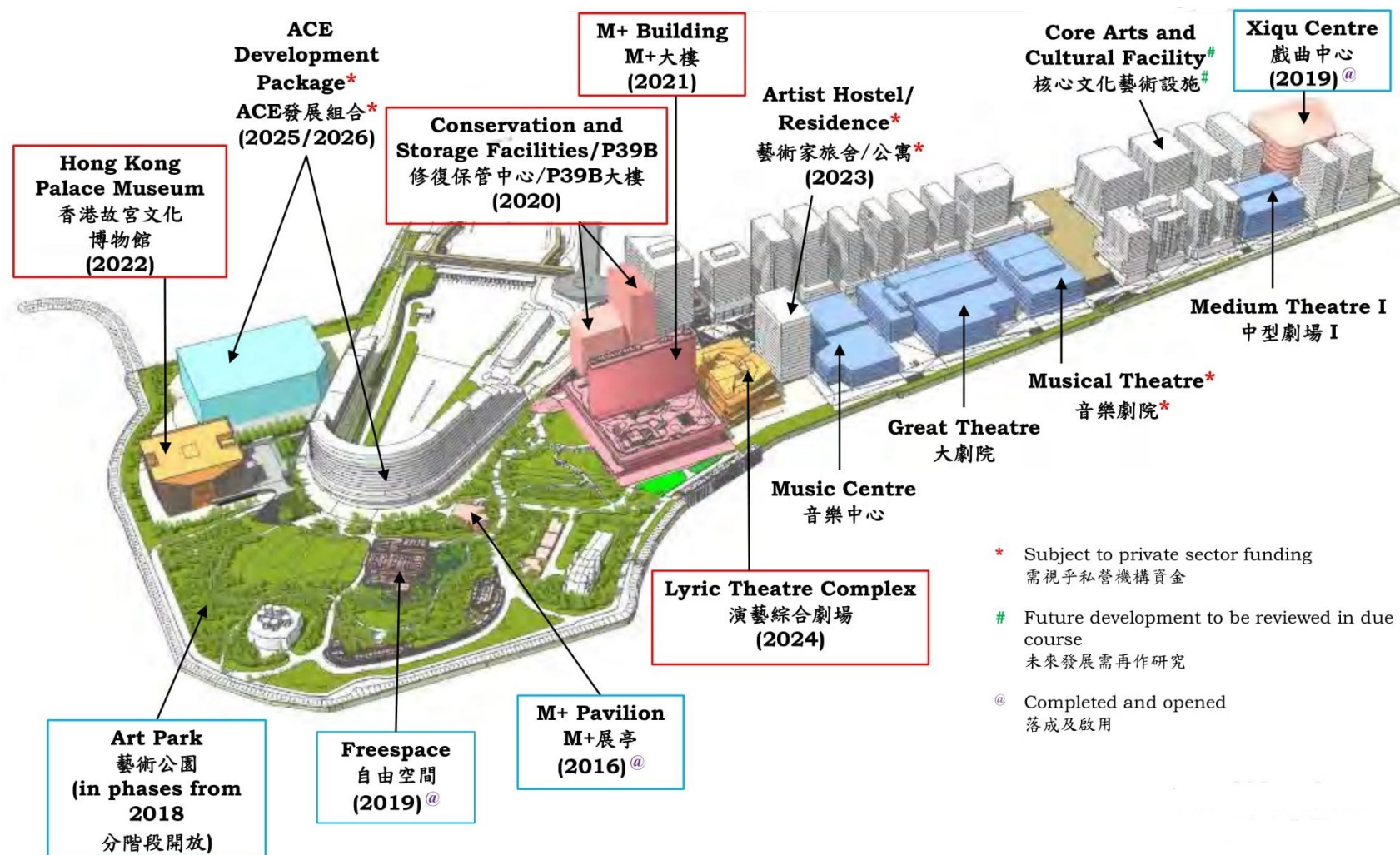
Facilities	Status and target completion date
<i>Batch 3</i>	
Music Centre <i>(including Concert Hall and Recital Hall)</i>	High priority under the enhanced financial arrangement
Musical Theatre	To be developed through public-private partnership subject to private sector funding
Great Theatre	To be reviewed by WKCDA and delivered gradually having regard to demand in line with the organic growth approach of WKCD
Medium Theatre I	
<i>Others</i>	
Exhibition Centre	To be developed through BOT arrangement packaged with hotel/rental offices of the adjacent U-shaped site (ACE Project)
Hong Kong Palace Museum	Construction of superstructure commenced in April 2019, with the Occupation Permit targeted to be granted in mid-2021, with opening one year later
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	

Note:

The originally proposed Medium Theatre II and one black box theatre (now called Studio Theatre) of the Centre for Contemporary Performance were incorporated into the building of the original Lyric Theatre to form the Lyric Theatre Complex to advance their provision.

Source: Annex 2 to [LC Paper No. CB\(1\)914/18-19\(01\)](#)

西九文化區主要設施示意圖
Schematic plan of major West Kowloon Cultural District facilities



資料來源：[立法會 CB\(1\)149/19-20\(02\)號文件的附件](#)
Source: Annex to [LC Paper No. CB\(1\)149/19-20\(02\)](#)

Appendix III

Financial situation of the West Kowloon Cultural District project

List of relevant papers

Council/Committee	Date of meeting	Paper
Public Works Subcommittee	18.6.2008 Item 1	Agenda Minutes
Finance Committee	4.7.2008 Item 2	Agenda Minutes
Council meeting	26-27.6.2013	Official Record of Proceedings — Motion on "Concern about the expenditure of the West Kowloon Cultural District project" (p.14119-14141, 26.6.2013) and (p. 14148-14235, 27.6.2013)
Former Joint Subcommittee to Monitor the Implementation of the West Kowloon Cultural District Project formed in the Fifth Legislative Council	3.7.2013 Item II	Agenda Minutes
	24.1.2014 Item II	Agenda Minutes
	28.3.2014 Item II	Agenda Minutes
	28.5.2014 Item I	Agenda Minutes Response of the Administration/WKCDA to members' concerns raised at the meeting
	24.11.2014 Item II	Agenda Minutes

Council/Committee	Date of meeting	Paper
	12.1.2015 Item III	Agenda Minutes
	19.5.2015 Item III	Agenda Minutes
	7.7.2015 Item I	Agenda Minutes
	30.5.2016 Item I	Agenda Minutes
—	19.1.2017 (Issue date)	Legislative Council Brief on Enhanced Financial Arrangement for the West Kowloon Cultural District
Joint Subcommittee to Monitor the Implementation of the West Kowloon Cultural District Project	21.2.2017 Item II	Agenda Minutes Response of the Administration/WKCDA to members' concerns raised at the meeting
	9.2.2018 Item II	Agenda Minutes
	11.5.2018 Item II	Agenda Minutes
	14.1.2019 Item II	Agenda Minutes
	29.4.2019 Item III	Agenda Minutes
	10.6.2019 Item IV	Agenda Minutes