

## **LEGISLATIVE COUNCIL BRIEF**

### **UPDATE ON THE DEVELOPMENT OF A NEW CRUISE TERMINAL AT KAI TAK**

#### **INTRODUCTION**

This note informs Members of the Government's plan to design and build the new cruise terminal at Kai Tak for leasing to a cruise terminal operator (the Government Design, Build and Lease (DBL) approach), in view of the recent escalation of construction cost and latest market feedback.

#### **LATEST ASSESSMENT OF THE RE-TENDER APPROACH**

2. We last informed Members in July 2008 of our plan to re-tender the cruise terminal project with the Government funding the works for the site formation and Government Facilities<sup>(1)</sup> subject to approval by the Legislative Council (LegCo); and that should re-tender fail, the Government would proceed with the DBL approach. We have since then engaged relevant stakeholders including the cruise and travel trade, as well as the property and construction industry, on the re-tender approach. We have also updated the construction costs for the project. Taking into account the recent developments as set out in paragraphs 3 to 6 below, our assessment is that it is highly unlikely that a re-tender would meet the objective of developing a new cruise terminal as soon as possible.

#### **Unpredictable escalation of construction cost**

3. The construction cost in general has surged significantly. The May 2008 material indices for galvanized mild steel, sand and steel reinforcement have risen by 60%, 104% and 137% respectively as compared to those in January 2007. In the first five months of 2008 alone, these material indices have risen by 25%, 42% and 41% respectively. In addition, diesel fuel prices are expected to remain volatile. Coupled with the increased volume in building construction works, the tender price

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Note<sup>(1)</sup> Government Facilities include Customs, Immigration, Health Quarantine and Police Facilities, a Government radar tower, support area for cross boundary heliport passengers and a Landscaped Deck.

index<sup>(2)</sup> for Government building works for the first quarter in 2008 has risen by 36% over the past 12 months and 12% over the fourth quarter in 2007. These recent developments in the local construction sector would give rise to considerable risks in cost estimates and hence dampen market interest in the re-tender for the cruise terminal.

4. Taking into account the latest cost increase, the overall construction cost of the new cruise terminal (excluding the commercial Gross Floor Area (GFA) of 50 000 m<sup>2</sup> which forms part of the tender) is now estimated to be \$5.6 billion at September 2008 price. This estimate is based on the assumption that the private sector will only be required to adopt the minimum standards that can be enforced by the Government and are necessary to meet statutory requirements and functional needs. Members were last informed that the Government would seek to fund the works for the site formation and Government Facilities should we decide to proceed with a re-tender. The estimated cost for these works then was about \$1.8 billion - \$2 billion at September 2007 price. The updated cost estimate has escalated to \$3 billion at September 2008 price.

5. When we last reported to Members, our intention was for the Government to seek approval from the Finance Committee (FC) to entrust the works for the site formation and Government Facilities to the successful tenderer. The cost of these entrusted infrastructure works would be reimbursed to the tenderer subject to a project estimate cap as approved by FC. Given the uncertainty in construction cost, there is a possibility that the actual construction cost to be shouldered by the tenderer may be much higher than the approved cap. This would in turn increase the risks of private sector involvement in the project. Also we are concerned that the latest financial market turbulence might add further uncertainty to the financing costs and resulting in no conforming tenderer for the project. Another abortive tender would discourage cruise operators from deploying cruise vessels to Hong Kong and dampen cruise market development.

### **Market feedback**

6. Since announcement of the Government's plan to re-tender on 9 July 2008, we have been engaging the market on the proposed re-tender. The cruise industry and travel trade would like to see the earliest commissioning of the terminal and have questioned why the Government does not develop the terminal itself. There was indication from the market, especially the property development and construction sector, that even with the proposed Government funding support, the market might not respond positively due to remote access of the cruise terminal site, the

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Note<sup>(2)</sup> The tender price index is compiled by the Architectural Services Department (ArchSD) based on cost data from accepted tenders and on a quarterly basis.

long time required for the Kai Tak Development to mature, and the prospect of operating the terminal at a loss in the initial years.

### **THE DBL APPROACH**

7. In view of the uncertainty and the time required in pursuing the re-tender approach, the Government now proposes to proceed with the DBL approach, keeping the target of commencing the operation of the first berth in mid 2013, as under the re-tender option.

8. Under the DBL approach, the Government would proceed to develop the new cruise terminal with two parallel contracts, i.e. a site formation works contract and a cruise terminal building works contract. The new cruise terminal would be leased to a cruise terminal operator. As a tenant, the cruise terminal operator would pay the Government a rental for the right to operate the cruise terminal. The Government intends to –

- (a) expedite the construction process by conducting the site formation works<sup>(3)</sup> and the cruise terminal building works through two parallel tracks; and
- (b) commence operation of the first berth for cruise vessels with temporary facilities<sup>(4)</sup> in mid 2013, pending the completion of the full-fledged cruise terminal building in 2014/15.

9. Drawing reference from the ancillary commercial facilities in other cruise terminals overseas, we intend to scale back the commercial GFA from a maximum of 50,000 m<sup>2</sup> to about 10,600 m<sup>2</sup>. The displaced 39,400 m<sup>2</sup> of commercial GFA will be redistributed to other sites earmarked for commercial development in the Kai Tak Development. The design of the Landscaped Deck would have to be adjusted accordingly to ensure it is proportional to a smaller commercial area.

10. A comparison of the facilities to be developed on the cruise terminal site under the re-tender and the fast-tracked DBL approach is at Annex A. The capital cost of the new cruise terminal under the DBL approach is estimated to be about \$ 7.2 billion (at September 2008 price). The estimate has taken into account the necessary allowance for price fluctuation payment and contingencies, and the necessary compliance with Government standards and provisions for projects undertaken by the Government.

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Notes <sup>(3)</sup> Site formation works include setting-back of seawall to avoid triggering the Protection of the Harbour Ordinance, dredging of sea-bed to accommodate vessels with deep draft, and provision of piled quay deck including mooring and fender systems for berthing of cruise vessels.

<sup>(4)</sup> These temporary facilities will include essential road access, parking area, transport loading and unloading facilities, etc.

### **Earlier commissioning with temporary facilities**

11. When we last reported to Members, we estimated that the first berth and the supporting facilities would be ready for operation in 2014/15 according to an all-in-one DBL programme (i.e. a tender exercise covering the works of both the site formation and cruise terminal building). We have since then critically reviewed the development programme with a view to compressing the timetable. We believe that it would be feasible to proceed with the works for the site formation and the cruise terminal building through two parallel tracks. The site formation works can therefore commence earlier, by early 2010. Leasing of the terminal facilities could proceed in advance, for the facilities to be operated by the lessee as early as in mid 2013.

12. As soon as the site formation and the quay deck are ready, the first berth would be able to receive cruise vessels with temporary facilities. The works for the full-fledged cruise terminal building will continue while the first berth is in temporary operation. The temporary facilities would be similar to those at the Container Terminals and China Merchants Wharf at Kennedy Town, which the cruise industry has been using for cruise vessels unable to berth at Ocean Terminal due to their large sizes or conflict of schedules. The use of such facilities for berthing cruise vessels is also not uncommon in overseas ports. While the temporary facilities would not be fully satisfactory, the industry in general is prepared to accept such interim arrangements, which are better than mid stream berthing. This fast-tracked DBL approach would enable us to commence the operation of the first berth in mid 2013.

### **THE NEXT STEP**

13. We intend to proceed in accordance with the following timetable –

<b>Key tasks</b>	<b>Date</b>
Brief the LegCo Panel on Economic Development	24 October 2008
Seek LegCo funding approval for the extension of a supernumerary directorate post to head a designated Cruise Terminal Task Force in the Tourism Commission (See Annex B)	2008/ 2009
Seek LegCo funding approval for the site formation works upon finalisation of tender documents, and commence the site formation works thereafter	2009

<b>Key tasks</b>	<b>Date</b>
Seek LegCo funding approval for the cruise terminal building works upon finalisation of design and build tender documents and prequalification of tenderers, and commence the building works thereafter	Early 2011
Commence leasing work of the cruise terminal	2011/12
Commission the first berth by using temporary facilities	Mid 2013
Commission the new cruise terminal	2014/15

### **IMPLICATIONS OF THE PROPOSAL**

14. The proposal is in conformity with the Basic Law, including the provisions concerning human rights. Other implications are set out in Annex B.

### **PUBLICITY**

15. We shall brief the LegCo Panel on Economic Development. A press release will be issued. A spokesman will be available to handle enquiries. A list of Frequently Asked Questions will be uploaded to Tourism Commission's website. We shall also update the relevant professional and trade bodies, and engage the local and international cruise industry and the travel trade.

### **BACKGROUND**

16. We last issued a LegCo Brief on the development of a new cruise terminal at Kai Tak on 9 July 2008. We informed Members of the Government's plan to re-tender the cruise terminal project with Government funding for site formation and Government Facilities. Should the re-tender fail, the Government would proceed with the DBL approach.

### **ENQUIRIES**

17. Enquiries on this Brief can be addressed to Miss Patricia So, Assistant Commissioner for Tourism (Tel: 2810 3137).

Commerce and Economic Development Bureau  
30 September 2008

**Comparison of the Key Components under Re-tender and Government  
Design, Build and Lease (DBL) Approach**

Approach Component	Re-tender	DBL approach
Berthing facilities such as fender system	✓	✓
Apron facilities such as passenger gangways	✓	✓
Customs, immigration and health quarantine clearance	✓	✓
Commercial Area	50,000 m <sup>2</sup>	10,600 m <sup>2</sup>
Landscaped Deck	22,000 m <sup>2</sup>	Adjusted scale
Access Road (from Cheung Yip Street at Kowloon Bay)	✓	✓

## IMPLICATIONS OF THE PROPOSAL

### Financial and Civil Service Implications

1. To proceed with the DBL approach, the Administration will require capital expenditure of about \$ 7.2 billion (at September 2008 price), including the capital cost for site formation works, cruise terminal building works, 10,600 m<sup>2</sup> Gross Floor Area for ancillary commercial purposes, and the costs for temporary facilities for the berthing of cruise vessels such as road access, parking area and transport loading and unloading facilities, etc. We shall secure the necessary capital and recurrent funding through established resource allocation procedures.

2. We have created in the Tourism Commission (TC) from April 2007 one supernumerary Directorate (D2 level) post for two years. Under the DBL approach, we consider that this post would have to be extended until end 2014 to oversee the completion of the construction works, leasing of the cruise terminal and the commencement of operation of the cruise terminal. We shall seek approval for extension of the supernumerary directorate post until end 2014 according to the established mechanism.

3. TC will also establish a dedicated Cruise Terminal Task Force to oversee the DBL approach, ensure strict adherence to the compressed timetable, and conduct the subsequent enforcement and monitoring of the lease. It will be charged with the overall co-ordination of the project, resolving inter-departmental and interface issues, preparing and overseeing the lease agreement, and continuously engaging the cruise industry to ensure that the end product would meet the market need. Apart from redeployment of existing resources, TC will seek additional staff resources through established mechanism. The other relevant bureaux/departments would also apply for additional time-limited staff resources to take up the extra workload arising from the implementation of the DBL approach, and recurrent staff resources for the provision of Government services including Customs, Immigration, Health Quarantine and Police services and management of the Landscaped Deck after the new cruise terminal commences operation.

### Productivity Implications

4. The Administration's plan to implement the DBL approach in lieu of re-tender will unlikely have any productivity implications.

### **Economic Implications**

5. According to the cruise market consultancy studies commissioned earlier by TC, Hong Kong would require an additional berth between 2009 and 2015, and one to two further berths beyond 2015. The timely development of new cruise terminal facilities is critical for developing Hong Kong into a regional cruise hub in Asia. This will also have positive impact on land premiums of the Tourism Node nearby and of the commercial area in the vicinity to be developed in phases, as well as favourable spill-over effects on the whole South East Kowloon where higher land value will be fetched. For the economy as a whole, more cruise vessels visiting Hong Kong will boost our tourism industry, which in turn will add impetus to the overall economic growth and create additional employment opportunities. Based on updated assumptions, with the availability of new cruise terminal facilities and appropriate market strategies, it is estimated that the economic benefits brought by the cruise industry may range from \$1.5 billion to \$2.6 billion per annum and the additional jobs generated may be around 5 300 to 8 900 by 2023, depending on different growth scenarios. The DBL approach will provide greater certainty on the timing of the development of the new cruise terminal and achieving the related economic benefits.

### **Environmental Implications**

6. The dredging works associated with the cruise terminal are a designated project under Schedule 2 of the Environmental Impact Assessment (EIA) Ordinance. The Civil Engineering and Development Department had completed the EIA study report which was approved in December 2007 by the Director of Environmental Protection. Based on the approved Schedule 2 EIA report, an Environmental Permit can be applied for carrying out the concerned works.

### **Sustainability Implications**

7. A sustainability assessment report has been conducted, which shows that the cruise terminal would bring in a range of benefits, particularly direct economic benefits in terms of port charges and passengers spending,



and employment opportunities in related industries. It would also help establish Hong Kong as a regional cruise hub and boost our tourism industry. Nonetheless, there are potential impacts in the environmental and natural resources aspects. In particular, dredging of seabed and setback of existing seawall would generate substantial solid waste and cause marine water pollution, noise and ecological damage. There would be vehicle exhaust emission along the proposed new roads and cruise emissions, as well as potential odour emission generated from the sewage pumping station. Mitigation measures and operation control have to be implemented to minimize the adverse environmental impact during the construction and operation stages.