

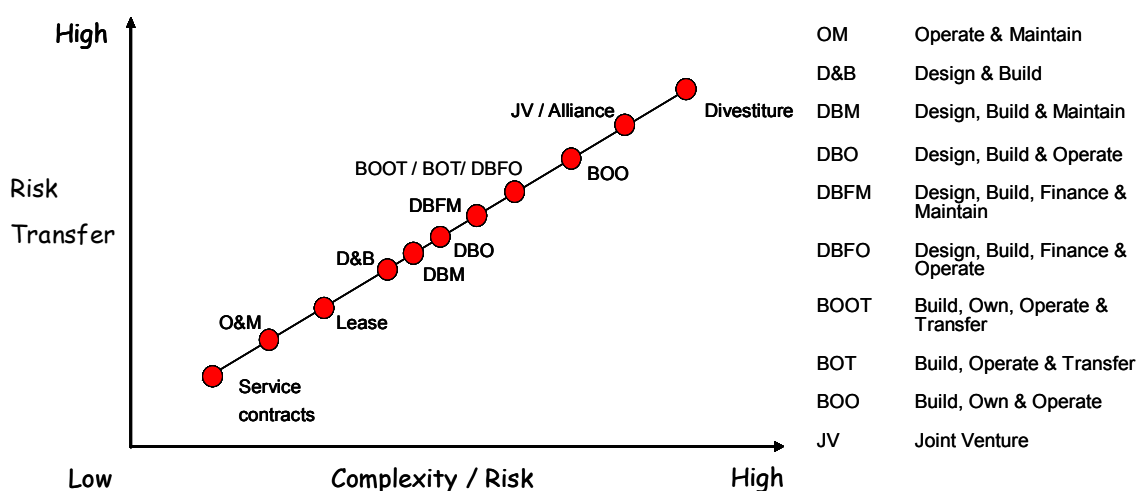
## EXECUTIVE SUMMARY

### Introduction

1. This Report examines the potential role of Public Private Partnerships (PPP) in the development and operation of the WKCD.
2. The analysis is undertaken for broad types of cultural and communal facilities which are categorised based on financial characteristics. The potential approaches examined are comprehensive and the Study Report recommends (i) a framework which will guide the formulation of scenarios for the financial analysis; (ii) an area based approach for development of the WKCD and (iii) analysis of the possible PPP options for the arts and cultural facilities recommended by the PATAG and the MAG.

### Private Sector Involvement and PPP

3. Involving the private sector in the delivery of what traditionally are seen as public services is a worldwide and ongoing trend and ranges from simple outsourcing of cleaning contracts to public floatation (divestiture) of former nationalised industries. What characterises and defines an approach is the allocation of risk between the public and private sectors. The diagram illustrates the spectrum of approaches.



4. PPPs are a subset of the spectrum of private sector involvement. Although there are slight variations in terminology between jurisdictions and between sectors, the key characteristics of PPP are **sharing of risk and responsibility**, a **contractual arrangement** between Government and the private sector, over a **medium to long term timescale** involving arrangements which take advantage of private sector management skills **incentivised by having private finance at risk** i.e. there is a potential for private sector investment funds to generate either positive or negative returns.

### Private Sector Involvement and PPP in WKCD

5. An analysis was undertaken of experience of private sector involvement and PPP in Hong Kong and internationally in the cultural and arts sectors. Experience demonstrates that nearly all of the types of cultural and associated communal facilities that are likely to be developed

and operated at the WKCD are loss making when measured in terms of the **market** revenue generated. Many cultural facilities do not cover the cost of operations and maintenance and very few are able to make any contribution to recovering the costs of construction. There has therefore been very limited scope for the private sector to take the lead in development or operation of facilities. In virtually all cases both the development and operation of facilities have involved significant levels of **public subsidy** in a wide range of different forms and at different levels – and where there is a minority contribution by the private sector it is unlikely to be at risk because it is in the form of a donation. Subsidy methods include capital expenditure, other grants and loans, land and property inducements, development packaging and planning gain, whereby lease conditions require the private sector to provide certain facilities or services. Most of these are already employed in Hong Kong. The issue is therefore the level, source and form of public subsidy which is most efficient and cost effective.

6. In terms of the facilities/ development at WKCD, three broad “classes” have been identified primarily based on the expected level of market financial viability of construction and operation but also considering (i) the relationship between broad capital and operating cost - specifically the need for a satisfactory level of capital **and** operating viability to be achieved for whole-life approaches and (ii) the existence of private sector players in the market with the right kind of experience and resources. The framework for recommended approaches is shown below. Potential options for private sector involvement in the delivery of facilities and services are shown on the following page.

Development Type	Possible Mechanisms
<b>Type 1</b> <i>Non-directly Revenue Generating Development</i>	Service/Operate and Maintain Design and Build Design Build Maintain/Design Build Finance Maintain Planning Gain
<b>Type 2</b> <i>Revenue Generating Development</i> <i>Not expected to cover operating costs</i>	Service/Operate and Maintain Design and Build Design Build Maintain/Design Build Finance Maintain Planning Gain Development Packaging
<b>Type 3</b> <i>Revenue Generating Development</i> <i>Cover Operating Cost</i> <i>Not determined as to extent of coverage of capital costs</i>	Service/Operate and Maintain Lease Operate and Maintain Design and Build Design Build Maintain/Design Build Finance Maintain Design Build and Operate BOOT/DBFO/BOT and hybrids BOO and hybrids Joint Venture Planning Gain Development Packaging

### Potential Options for Private Sector Involvement in CACF and Communal Facilities

PSI Capital Options														
PSI Operating Options														
CACF / Communal Facilities	Operating Profit / Deficit	Capital Costs	Planning Gain	Development Packaging	Build / D&B	DBM	DBO	DBFM	BOOT/ BOT / DBFO	BOO	JV / Alliance	Service Contracts	OMM	Lease
Mega Performance Venue	\$	\$		x	x	x	x	x	x	x	x	x	x	x
Great Theatres	\$	\$		x	x			x				x	x	x
Concert Halls	\$	\$		x	x	x		x				x	x	
Xiqu Centre	\$	\$		x	x	x	x	x				x	x	
Medium-sized Theatres	\$	\$	x	x	x			x				x	x	x
Blackbox Theatres	\$	\$	x	x	x	x	x	x				x	x	x
Piazzas	\$	\$	x	x	x	x						x	x	
M+	\$	\$		x	x	x						x		
Exhibition Centre	\$	\$		x	x	x	x	x	x	x	x	x	x	x
Automated People Mover	\$	\$	x	x	x	x	x	x	x	x	x	x	x	
Roads	\$	\$	x		x							x		
Public Open Spaces	\$	\$	x		x							x		
Other G/IC Facilities	\$	\$	x		x	x	x	x				x		

#### Notes:

- (i) Options in red are “true” PPP options
- (ii) The list of arts and cultural facilities covers those as recommended by PATAG and MAG. The communal facilities are those required under the IFP



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**List of Abbreviations**

ASD	Architectural Services Department
BLT	Build Lease Transfer
BRT	Build Rent Transfer
BOO	Build Own Operate
BOT	Build Operate Transfer (also Build Own Transfer)
BOOT	Build Own Operate Transfer
BTO	Build Transfer Operate
CACF	Core Arts and Cultural Facilities
CC	Consultative Committee
CEDD	Civil Engineering and Development Department
D&B	Design & Build
DBM	Design Build and Maintain
DBFM	Design, Build, Finance and Maintain
DBFO	Design Build Finance Operate
DBO	Design Build Operate
EU	Efficiency Unit
FA	Financial Advisor
F&B	Food and Beverage
FMAG	Financial Matters Advisory Group
G/IC	Government, Institution or Community
IFP	Invitation for Proposals
IMAX	Image Maximum
JV	Joint Venture
LCSD	Leisure and Cultural Services Department
MAG	Museums Advisory Group
MPV	Mega Performance Venue
MTRCL	Mass Transit Railway Corporation Ltd.
NGS	National Geographic Society
NOFA	Net Operating Floor Area
O&M	Operate & Maintain
PFI	Private Finance Initiative
PSI	Private Sector Involvement
PPP	Public Private Partnership
PATAG	Performing Arts and Tourism Advisory Group
QPAC	Queensland Performing Arts Complex
RBCM	Royal British Columbia Museum
URA	Urban Renewal Authority
WIP	Work in Progress
WKCD	West Kowloon Cultural District

# 1 INTRODUCTION

## 1.1 Scope of this Study Report

### *The Role of PPP in Meeting Cultural Objectives*

1.1.1 The basis of this Study Report lies in the concept that alternative approaches to traditional Government provision of public services could assist in meeting cultural objectives, as well as offer other efficiency and financial benefits. Advice of the Government to the FMAG<sup>1</sup> set out a clear role for the potential of PPP in meeting cultural policy objectives including:

- Fostering the principle of partnership between Government, the private sector and the arts and cultural community. This enables Government to be a facilitator for the development of the arts (rather than the principal provider)
- Enlarging the scope for market creativity and innovation through a financially self-standing non-Government operation mode
- Providing reliable streams of income to support the long term planning of arts and cultural programmes
- Limiting intervention by Government in cultural matters for a more liberal and open society
- Government does not plan to invite developers to develop the arts and cultural facilities - but the private sector could provide a funding source to develop and operate facilities

### *Approach to Study Requirements and Objectives*

1.1.2 Whilst the potential approaches examined are comprehensive and wide ranging, the objective of this Study Report was to recommend PPP scenarios which would be appropriate for the WKCD to be taken forward for testing under the financial analysis task. This Study Report provides a framework which will guide the formulation of scenarios and assessment of potential options for private sector involvement (PSI) for individual CACF and communal facilities.

1.1.3 The approach adopted focuses on the need for recommendations to be appropriate for:

- Cultural and arts facilities
- Operation as well as development of such facilities
- The legal and financial framework in Hong Kong
- The particular planning, development and market context of the WKCD

1.1.4 This involves analysis at two levels:

- Forms of PPP approaches that may be suitable for “developing and operating the WKCD as a whole” i.e. an area based approach involving establishment of a statutory body to take forward the development of the WKCD. This includes consideration of different roles for the statutory body such as development only, or operations of the CACF only

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<sup>1</sup> Note to FMAG on Public Private Partnerships and the Public Sector Comparator, 28 April 2006

- Forms of PPP approaches for “individual facilities in the WKCD” i.e. procurement arrangements for the development and ongoing operation, maintenance and management of the endorsed CACF and communal facilities

1.1.5 The analysis takes into account both local and overseas experience. However, the financial advisor (FA) recognises that:

- Experience is more limited in the arts/culture/entertainment sector than in the provision of public service goods and that the operation of such facilities is a distinctly different service to, for example, the operation of transport infrastructure, health or educational services
- Whilst most PPP experience has been in the funding of the development and operation of individual facilities, integrated approaches to groups of cultural and arts facilities and combined cultural and commercial development are particularly relevant and are examined

1.1.6 The analysis is undertaken for broad types of cultural and communal facilities which can be categorised based on financial and cultural characteristics as well as consideration of the potential of service providers in the relevant sector.

1.1.7 Integrated approaches will be considered to extend and improve the range of potential successful PPP approaches and facilitate the “fusion of activities” to increase visitor interest and participation.

## **1.2 Layout of the Study Report**

1.2.1 The Study Report is succinct and focuses on lessons learnt and recommendations. The main text is structured into five further chapters as follows:

- Chapter 2: Provides an overview of the wide range of PSI in the delivery of services<sup>2</sup>, some of which have been adopted in Hong Kong. It briefly sets out the characteristics of each approach and the overall lessons learnt
- Chapter 3: Sets out the policy context, considers and evaluates the lessons of private sector involvement including PPP in Hong Kong, drawing on all sectors in which it has been, or sought to be, applied
- Chapter 4: Specifically considers the applicability of PSI including PPP approaches to the cultural, arts and visitor destination sectors drawing on international experience
- Chapter 5: Considers area based approaches to planning and funding cultural and related development to consider the implications for potential project packaging and the procurement role of the proposed statutory authority
- Chapter 6: Discusses potential approaches for the particular circumstances of arts and cultural development and associated commercial development at WKCD. A framework is provided for PSI approaches for different types of development
- Chapter 7: Further applies and develops the framework to consider individual facilities and their potential for PSI

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<sup>2</sup> Note that the range available includes the whole range of private sector involvement from simple contracting out arrangements to divestiture, not just those which tend to be referred to as PPP in Hong Kong.

## 2 PPP: DEFINITION AND OVERVIEW OF EXPERIENCE

### 2.1 Introduction to PPP

2.1.1 Involving the private sector in the delivery of what traditionally are seen as public services is a worldwide and ongoing trend. Private sector involvement by definition is wide ranging, from simple outsourcing of cleaning contracts to public floatation (divestiture) of former nationalised industries. Each form of private sector involvement varies in the allocation of risk between the public and private sectors: simple outsourcing contracts involve low levels of risk transfer from the public to the private sector. Divestiture, where assets are sold and responsibility for service delivery is transferred to the private sector involves the highest level of risk transfer.

2.1.2 PPPs are a subset of the various forms of private sector involvement. Different jurisdictions and different sectors tend to have slightly different definitions and use slightly different terminologies; there is no hard and fast rule as to what is strictly a PPP and what is not, particularly given the myriad of variations on a basic form that could be incorporated into an individual contract.

2.1.3 Slight variations in definitions of PPP are not a problem. What is clear is that:

- PPP is about the **sharing of risk and responsibility** between the public and private sectors in service delivery
- PPP involves a **contract** between Government and the private sector, over a **medium to long term timescale**
- PPP involves arrangements which take advantage of private sector management skills **incentivised by having private finance at risk**<sup>3</sup>

2.1.4 A PPP approach is thus further up the spectrum of private sector involvement than simple outsourcing or management contracts, or where Government wholly finances projects up-front but it stops short of full (100%) divestiture.

2.1.5 What typically differentiates PPP type approaches from others is the degree of risk sharing, definition through contract, the relatively long timescale and the key point – **private finance is at risk**. These features are entirely consistent with the definition of PPP provided to Financial Matters Advisory Group (FMAG) – see box.

#### Information Note to the FMAG

**PPP is defined as:** “any partnership approach, where the responsibility for the delivery of services is shared between the public and private sectors, both bringing their complementary skills to the enterprise”. This “usually” means Government defining the (level of) service and being involved in regulation and procurement to secure this service. The private sector is (usually) responsible for delivering the service using its innovation and flexibility. Risks are allocated to the party best able to manage them. It is assumed to be a long term relationship, typically between 10-30 years”

<sup>3</sup> i.e. there is a potential for private sector investment funds to generate either positive or negative returns

## 2.2 Development of PPP

2.2.1 Governments typically use PPPs for one or both of the following reasons:

- Improving **value for money** in service delivery by gaining access to experience, management skills and management flexibility that may not exist in the public sector
- Ability to finance the development of public service infrastructure with “off balance” sheet funding and thus, in budgetary terms, **spread the cost of such infrastructure over its economic life**

2.2.2 PPPs have been in existence for a long time. For example, France has extensive experience history of the provision of public services by private sector operators under long term concessions, including water supply and treatment and transport. The concessions operate under terms which have long been codified on the French legal system.

2.2.3 More recent evolution of PPPs has been driven by the UK. The process started in the early 1990's following on from the UK Government's privatisation programme. The overall driver was the need for major investment in public service infrastructure renewal within tight budgetary constraints and an inability to achieve this through privatisation, for practical and political reasons. The UK approach, codified in the form of the Private Finance Initiative (PFI) has sought to achieve a very clear allocation of responsibility and risk between the public and private sectors in order to maximise cost effective risk transfer to the private sector. This has resulted in relatively complex contractual terms.

2.2.4 PPPs are being pursued by an ever increasing range of countries as governments seek to find more cost effective ways of delivering public services within their budgetary constraints.

2.2.5 Despite the growing body of PPPs, there is relatively little PPP experience in the provision and operation of leisure and cultural facilities. The largest volume of PPPs has involved transport and utility provision (water and waste water). UK and Australia have also seen heavy use of PPPs for the provision of social infrastructure, such as hospitals, schools and government offices. Continental European governments are increasingly exploring the use of PPPs for social infrastructure e.g. hospitals, prisons and leisure related assets. The US has seen relatively limited application of PPPs to date, limited to the transport sector.

## 2.3 Spectrum of Private Sector Involvement and PPP Approaches for this Study

2.3.1 In considering appropriate arrangements for the WKCD, the FA has broadened the range of approaches to include all potential types of contract based private sector involvement, from outsourcing of service provision through to full divestiture. This broad range is appropriate given the wide variety of facilities and services to be provided in the WKCD and the potential need for different approaches to private sector involvement for different types of facilities. The focus, none-the-less is on identifying potential PPP approaches which involve the use of private finance in building and operating assets for a financial return over a lifecycle project period.

2.3.2 Table 2.1 describes the range of generic private sector involvement options and the typical split of responsibility of roles between the public and private sectors. Those potential PPP type approaches (or possible hybrids of which there are many) are shaded.

- 2.3.3 In addition to the contract based approaches set out in Table 2.1, the analysis in Chapters 3 and 4 shows that other planning and development approaches have been widely used between the public and private sectors such as “development packaging” to cross-subsidise private development of cultural and commercial facilities in one package and “planning gain” mechanisms using the statutory planning system to get developers to provide communal and other facilities. These are not included here as contract based PPP type approaches – and indeed may form part of the public or private contribution to a PPP approach – but are fully considered in the FA’s main report.

## **2.4 Types and Degree of Risk Transfer, Benefits and Disadvantages**

- 2.4.1 Identifying typical key features of private sector involvement, (including types of risk that may or may not be transferred) helps to map the type of approach and better understand its potential benefits or disadvantages. Six features have been identified:
- Design risk
  - Construction risk
  - Operational risk
  - Lifecycle approach
  - Demand risk
  - Private finance
- 2.4.2 Table 2.2 summarises the broad potential advantages and disadvantages for each of the features. In practise, each contract will have its specific advantages and disadvantages depending on the specific terms.

**Table 2.1: Private Sector Involvement and PPP Approaches, Roles and Responsibilities of the Public and Private Sectors**

Option	Typical Public Sector Role / Responsibility	Typical Private Sector Role/ Responsibility
<b>Service Contract</b>	<ul style="list-style-type: none"> <li>• Owns and finances underlying assets</li> <li>• Retains overall responsibility for operation and maintenance</li> </ul>	<ul style="list-style-type: none"> <li>• Provision of services to public sector as part of overall operation and / or maintenance</li> <li>• Responsible for providing services to the service levels specified</li> </ul>
<b>Operate and Maintain (O&amp;M)</b>	<ul style="list-style-type: none"> <li>• Owns and finances underlying assets</li> </ul>	<ul style="list-style-type: none"> <li>• Operation and maintenance to a specified condition / service level</li> <li>• Provision of services to the customer, possibly including collection of revenue</li> </ul>
<b>Lease</b>	<ul style="list-style-type: none"> <li>• Existing asset transferred from the public sector for a specified period</li> <li>• Public sector usually transfers on the basis of a lease for which it receives an up front capital payment and then makes a regular service payment to the private operator during the life of the lease.</li> </ul>	<ul style="list-style-type: none"> <li>• May need to refurbish or expand existing asset</li> <li>• Finance of up front capital payment and refurbishment/expansion costs</li> <li>• May include operation and maintenance to a specified condition / service level</li> </ul>
<b>Design and Build (D&amp;B)</b>	<ul style="list-style-type: none"> <li>• Specifies the asset required in terms of its functions and desired outcomes</li> <li>• Probably involves making stage payments during construction</li> <li>• Asset is transferred to public sector on completion</li> <li>• Operation, maintenance and management of completed asset</li> </ul>	<ul style="list-style-type: none"> <li>• Design and construction of the asset to agreed price and specification</li> <li>• Risk of time and cost overrun</li> </ul>

Option	Typical Public Sector Role / Responsibility	Typical Private Sector Role/ Responsibility
<b>Design Build and Maintain (DBM)/ Design Build Operate (DBO)</b>	<ul style="list-style-type: none"> <li>• Specifies the asset and services required</li> <li>• Purchases the asset on completion for a pre-agreed price and therefore finances the asset when it becomes operational</li> <li>• Takes all ownership risks following purchase</li> <li>• May provide management and operations</li> </ul>	<ul style="list-style-type: none"> <li>• Design and construction of the asset to agreed price and specification</li> <li>• Operation, management and maintenance to a specified condition/service level following completion or may just provide management</li> <li>• Provision of services to the customer, possibly including collection of revenue</li> <li>• Private sector incentive to design and build for long term quality operations/ or maintenance</li> </ul>
<b>Design, Build, Finance and Maintain</b>	<ul style="list-style-type: none"> <li>• Specifies the asset and services required</li> <li>• Purchases the asset throughout the agreed contract term</li> <li>• Provides management and operations</li> </ul>	<ul style="list-style-type: none"> <li>• Design, finance and construction of the asset</li> <li>• Maintenance of the asset to specified conditions/service level</li> <li>• Asset is returned to the public sector at the end of the contract</li> </ul>
<b>Build Own Operate Transfer (BOOT) / Build Operate Transfer (BOT)/ Design Build Finance Operate (DBFO)</b>	<ul style="list-style-type: none"> <li>• Specifies the services required and potentially the underlying asset required to deliver the services</li> <li>• Pays for the services and the cost of the underlying asset over the life of the contract</li> <li>• Takes ownership of the asset at the end of the contract, frequently at no cost</li> <li>• May provide front line services (e.g. teaching in a school or clinical services in a hospital)</li> </ul>	<ul style="list-style-type: none"> <li>• Design and construction of the asset to agreed price and specification</li> <li>• Finances project throughout contract period (construction and operation)</li> <li>• Operation and maintenance to a specified condition/service level following completion (extent of service provision dependent on the scope of the contract)</li> <li>• May provide services to the customer, possibly including collection of revenue (but service provision may be limited to building maintenance and possibly provision of soft facilities management or “hotel” services)</li> <li>• Takes full range of commercial risks associated with the project (excluding front line service provision provided by public sector)</li> <li>• Transfers asset to public sector at the end of the contract, usually with an obligation that the asset complies with minimum condition standards</li> </ul>

Option	Typical Public Sector Role / Responsibility	Typical Private Sector Role/ Responsibility
<b>Build Own Operate (BOO)</b>	<ul style="list-style-type: none"> <li>• Similar to BOOT projects but the public sector does not become the owner of the asset at the end of the contract</li> <li>• Commits to purchase services produced by the asset for a fixed length of time</li> </ul>	<ul style="list-style-type: none"> <li>• Similar to BOOT projects but retains ownership of the asset in perpetuity</li> </ul>
<b>Joint Venture / Alliance</b>	<ul style="list-style-type: none"> <li>• Sharing of benefits/costs associated with project risks</li> <li>• Pooling of assets, finance and expertise under joint management</li> <li>• Pre-agreed formula to benchmark pricing, timing, service levels and sharing of benefits / costs achieved</li> </ul>	<ul style="list-style-type: none"> <li>• Sharing of benefits/costs associated with project risks</li> <li>• Pooling of assets, finance and expertise under joint management</li> <li>• Pre-agreed formula to benchmark pricing, timing, service levels and sharing of benefits / costs achieved</li> </ul>
<b>Divestiture</b>	<ul style="list-style-type: none"> <li>• Sale of business, with potential to retain a shareholding</li> <li>• Regulation of business to ensure it does not unfairly exploit a market monopoly and continues to provide public services to the desired standard</li> </ul>	<ul style="list-style-type: none"> <li>• Ownership and management of the business</li> <li>• Full range of business risks</li> </ul>

Notes:

(i) Other hybrids/extensions of BOOT and BOO include: BLT/BRT: Build lease/rent transfer; BT: Build transfer and BTO: Build, transfer, operate and Design Build Finance Operate (DBFO) – DBFO tends to be used in Hong Kong and emphasises the “Finance” rather than “Ownership” but the former implies the latter and vice versa

(ii) Options may or may not include design depending on the nature of the facility

(iii) Options which include maintenance only – rather than full management and operations of facilities may be more appropriate for some arts and culture facilities. In other sectors such as water supply or environmental services there are more players likely to both operate and construct facilities

**Table 2.2: Typical Key Features of Private Sector Involvement and PPP Approaches, Potential Benefits and Disadvantages**

PPP Feature	Description	Potential Benefits	Potential Disadvantages
<b>Design risk</b>	<ul style="list-style-type: none"> <li>Private sector responsible for designing the asset</li> <li>Public Sector provides design specification based on outputs required as opposed to detailed design inputs</li> </ul>	<ul style="list-style-type: none"> <li>Maximises private sector scope for innovation</li> <li>Provides access to latest technology, through large companies operating in a global environment with access to design ideas not otherwise available to government</li> </ul>	<ul style="list-style-type: none"> <li>Public sector needs to be careful about its output specification to ensure that the underlying solution is robust.</li> <li>Private sector likely to value engineer design to lowest cost solution which may impact robustness of solution</li> </ul>
<b>Construction risk</b>	<ul style="list-style-type: none"> <li>Private sector responsible for delivering to time and cost</li> </ul>	<ul style="list-style-type: none"> <li>Private sector bears risk of cost and time overruns</li> </ul>	<ul style="list-style-type: none"> <li>Private sector will need to be able to control and thus manage the risk of time and cost overruns if is it to price such risks cost effectively</li> </ul>
<b>Operational risk</b>	<ul style="list-style-type: none"> <li>Private sector responsible for operating and maintaining the asset</li> <li>Likely to be a long term contract if significant long term maintenance risk is to be transferred</li> </ul>	<ul style="list-style-type: none"> <li>Private sector bears risk of cost overruns subject to pre-agreed price adjustment formulae</li> <li>Private sector bears performance risk through a payment mechanism which varies payments according to performance</li> <li>Private sector assumes long term maintenance and replacement risk in return for receiving a pre-agreed annual contribution to fund replacements</li> <li>Potential for better customer focus as a positive long term relationship with customers is essential to ensure good financial returns to the private sector and better service delivery to the customer</li> </ul>	<ul style="list-style-type: none"> <li>Private sector will need to be able to control and thus manage the risk of cost overruns and performance failures if is it to price such risks cost effectively</li> <li>A long term contract may be less flexible for the public sector than traditional shorter term outsourcing service contracts</li> </ul>
<b>Lifecycle approach</b>	<ul style="list-style-type: none"> <li>Transfer of design, construction and long term operating risk to the private sector</li> </ul>	<ul style="list-style-type: none"> <li>Gives the private sector maximum opportunity to come up with the lowest whole life cost approach</li> <li>Single party can be responsible for capital, maintenance, upgrade and operational aspects of the asset delivery enabling "trade offs" between investments at various life cycle stages to</li> </ul>	<ul style="list-style-type: none"> <li>Public sector needs to be careful about its output specification to ensure that the underlying solution is robust.</li> <li>Private sector likely to value engineer design to lowest cost solution which may impact robustness of solution</li> </ul>

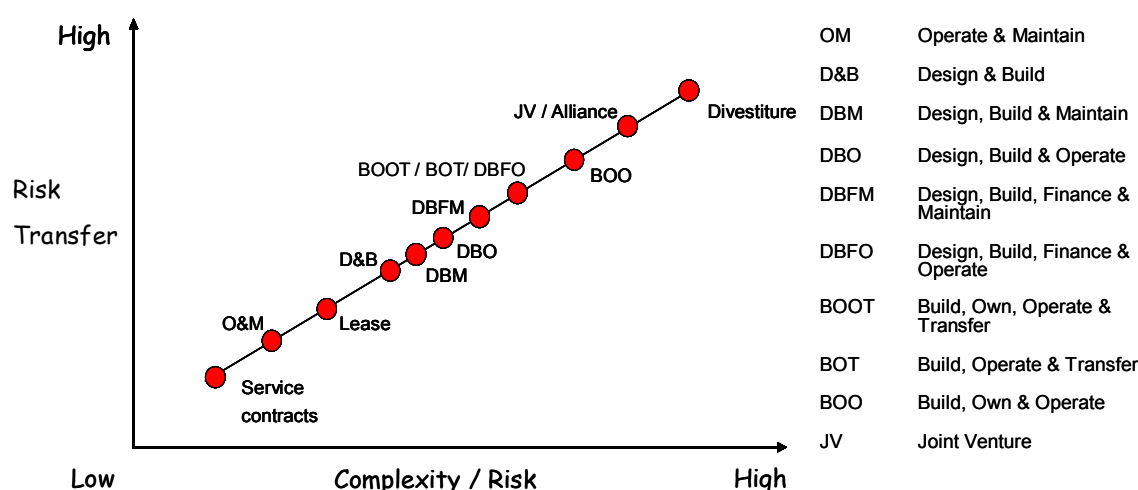
PPP Feature	Description	Potential Benefits	Potential Disadvantages
		be considered	<ul style="list-style-type: none"> <li>Private sector will need to be able to manage the risk of time and cost overruns if is it to price such risks cost effectively</li> <li>Private sector will need to be able to control and thus manage the risk of cost overruns and performance failures if is it to price such risks cost effectively</li> <li>A long term contract may be less flexible for the public sector than traditional shorter outsourcing service contracts</li> <li>The more complicated the contract the longer and more complicated the procurement process is likely to be</li> </ul>
<b>Demand risk</b>	<ul style="list-style-type: none"> <li>Transfer of risk of revenue generation and/or service use to the private sector</li> </ul>	<ul style="list-style-type: none"> <li>Private sector assumes significant financial risk against the success of the overall project</li> <li>Potential for better customer focus as a positive long term relationship with customers is essential to ensure good financial returns to the private sector and better service delivery to the customer</li> <li>Demand risk transfer will increase government's ability to treat finance as off balance sheet</li> </ul>	<ul style="list-style-type: none"> <li>Private sector will only accept demand risk that it can control or easily predict</li> <li>Demand risk transfer may be expensive</li> </ul>
<b>Private Finance</b>	<ul style="list-style-type: none"> <li>Private sector funds the creation of the asset and its ongoing operation for some form of return</li> </ul>	<ul style="list-style-type: none"> <li>Potential for earlier project delivery unrestricted by public funding constraints</li> <li>Financial disciplines of the private sector can enhance the efficiency of the project and ensure a practical balance between risk and cost savings Private finance helps ensure economically sound decision making rather than potentially popular decision making</li> </ul>	<ul style="list-style-type: none"> <li>Additional cost of private finance compared to the cost at which governments can borrow – this needs to be offset by efficiency savings by the private sector</li> <li>Potentially high cost of early termination of private sector's involvement may lead to inflexibility.</li> <li>Low cost but highly geared private finance structure may make contract changes costly and time</li> </ul>

PPP Feature	Description	Potential Benefits	Potential Disadvantages
		<ul style="list-style-type: none"><li>• Potential for private finance to be treated as off the government's balance sheet</li></ul>	<p>consuming</p> <ul style="list-style-type: none"><li>• The more highly geared the finance structure the longer and more costly the procurement process is likely to be as lenders need to be satisfied that risks have been mitigated</li></ul>

## 2.5 Risk Transfer, Finding the Right Balance

- 2.5.1 As discussed and illustrated in Table 2.1, the type of approach is defined by the degree of risk transfer to the private sector. Figure 2.1 illustrates the spectrum of approaches mapping them in terms of risk transfer against complexity/ risk.

**Figure 2.1: Finding the Balance of Risk Transfer, a Comparison of Approaches**



- 2.5.2 The lower the level of risk transfer, the less complex the contractual arrangement is likely to be and thus the more straightforward the procurement process.
- 2.5.3 In theory, the more risk that is transferred to the private sector, the greater the scope of the private sector to come up with more innovative forms of service delivery to improve value for money. However, such risk transfer will need to be clearly thought through and defined by the public sector. The private sector will need to satisfy that it is able to manage such risks in order to price them on a cost effective basis. The higher levels of risk transfer to the private sector are therefore usually associated with increasing levels of deregulation and, ultimately, higher levels of irreversibility of services and assets back to the public sector.
- 2.5.4 The maximum degree of risk transfer will be achieved through privatisation, transferring all the business risk associated with the relevant public service provision. However, this option will only be practical for a stand alone, largely deregulated, business that has the ability to control all aspects of its business and where there are no expectations of reversion back to the public sector.

## 2.6 Approaches to Private Sector Involvement, Risk Transfer to Private Sector

- 2.6.1 Combining Figure 2.1 and Table 2.2 provides an appreciation of why certain approaches have advantages and disadvantages and may be more suitable for some facilities/services than others. It is because of the different allocation of risk.
- 2.6.2 Figure 2.2 summarises the strengths of each feature for each of the approaches. A high score means that the risk transfer to the private sector is higher. The strength of feature is ranked into five levels from high to low. Demand risk is included as one of the risk transfers, assuming the main source of revenue is directly from the end user. From a conceptual point of view, consideration of demand risk will depend on the nature of the

revenue stream (end user/ public subsidy or both) and as such will depend on the terms of an individual contract.

#### **Risk Transfer in the UK Private Finance Initiative (PFI)**

In the UK, the contractual package of risk transfer and performance incentives included in a PFI contract has resulted in a significant improvement in the delivery of infrastructure capital investment on time and to budget. The terms of the PFI contract also encourage the private sector to focus on value for money over the lifetime of an asset. A well structured performance and payment mechanism ensures that the private sector contractor is aligned with its public sector client and incentivised to deliver service outputs which are consistent with its client's objectives.

However, the PFI has also been a high procurement cost option due to the complexity and length of procurement. For PFI projects to be value for money, the additional costs of this process have to be exceeded by the savings that the private sector can achieve through better design, procurement and asset management. The other key concern over PFI is the inflexibility of PFI contracts due to their length and the difficulty of changing service requirements during the life of the contracts.

**Figure 2.2 Features of Approaches to Private Sector Involvement, Risk Transfer to Private Sector**

PPP Option	Risk transfer to private sector					
	Design risk	Construction risk	Operational risk	Lifecycle approach	Demand risk	Private finance
Service contract						
Operate & Maintain (O&M)						
Lease						
Design & Build (D&B)						
Design Build Maintain (DBM)						
Design Build Operate (DBO)						
Design Build Finance Maintain (DBFM)						
Build Own Operate Transfer (BOOT) / Hybrid						
Build Own Operate (BOO)						
Joint Venture / Alliance						
Divestiture						

**Note:****Key:**

- No risk transfer
- Weak transfer
- Reasonable degree of risk transfer
- Strong risk transfer
- Full risk transfer

**Lease**

Private finance risk transfer is only "strong" because limited risk transfer of other risks will make off balance sheet finance more difficult to achieve

**DBO**

Weak private finance because public sector pays on completion - this reduces scope for operational and lifecycle

**DBFM**

Provides potential for facilities where private finance are contract but operations are separately managed

**BOOT / Hybrid**

Risk transfer is slightly higher in BOO than BOOT as private sector retains ownership under BOO and therefore has more

incentive to maintain asset (assuming it continues to have an economic value). Demand risk transfer depends on terms of contract

Joint Venture / alliance Degree of risk transfer can cover a wide spectrum depending on nature on contract.

## **2.7 Lessons Learnt**

2.7.1 There is an increasing body of practical experience of PPP contracts that have been operational for some years in the UK, Australia and an increasing range of other countries, including Hong Kong.

2.7.2 This experience has generated a number of key lessons that governments procuring PPPs need to consider in the procurement and operating phases of these contracts. These include:

### **2.7.3 Procurement phase**

- The public sector should have an experienced procurement team, with high quality advisory support to develop the scope of the contract to be tendered and to manage the overall procurement process
- The terms of the tender should be clearly specified to ensure that tenderers have a clear understanding of what they are bidding for and bids can be compared on a like for like basis
- Bidders should be provided with as much information on the project as possible to ensure that they do not apply an unnecessary pricing premium for uncertainty
- The public sector should ensure that there will be sufficient interested bidders to ensure a competitive market for the bid. This may require the project to be structured to reflect likely market demand and capacity
- The project should be structured with appropriate risk transfer to enable bidders to price risk on a cost effective basis and the project to be financed efficiently in the market
- The public sector should ensure that the contractual terms, including the performance and payment mechanisms, are drafted to ensure that its public policy objectives (which in this case include cultural and artistic objectives) are met by the successful bidder

### **2.7.4 Implementation phase**

- The public sector should ensure that it develops an operational management team with the appropriate competencies to manage a complex long term PPP agreement to ensure enforcement of the provisions of the contract
- A PPP contract should contain appropriate value testing mechanisms (e.g. benchmarking of market testing provisions for facilities management services) to ensure that the public sector pays an appropriate market based price for long term service provision
- Highly geared PPP contracts i.e. those with high levels of risk transfer, are relatively inflexible and changes to the contract can be expensive

### 3 PRIVATE SECTOR INVOLVEMENT AND PPP IN HONG KONG

#### 3.1 Introduction

- 3.1.1 This section sets out the background and policy context in Hong Kong for alternative approaches to development for the WKCD. It discusses the experience of private sector involvement in procurement of services including leisure and cultural services, recent PPP and specialist lease conditions for land grant potentially relevant to WKCD in particular. Lessons learnt are highlighted.

#### 3.2 PPP: Policy and Legislative Framework in Hong Kong

- 3.2.1 Traditional Government provision of facilities involves Government allocation of land to the relevant department, Government design and construction primarily through Architectural Services Department (ASD) (and Civil Engineering and Development Department (CEDD) for major projects) for leisure and cultural services. However, in many cases, the actual construction work (and design work in some cases) is contracted out to the private sector. Government facilities are run by relevant departments or, for some services such as cleaning and security, are outsourced to the private sector.
- 3.2.2 Government direction in the provision of services is clear<sup>4</sup>:
- The Government's goal is to meet community needs in the most efficient and effective manner
  - Government policy is that consideration should always be given to involving the private sector in the provision of new services and opportunities should be sought to improve private sector involvement in existing activities
- 3.2.3 Continued public sector reform since the late 1980's, value for money and efficiency objectives and fiscal constraints has led to further consideration of outsourcing possibilities and alternative approaches to capital procurement, which involve a greater sharing of responsibility and risk between public and private sectors – PPP. The Efficiency Unit (EU) has issued a series of guidance documents including guides which focus on (i) outsourcing<sup>5</sup> and (ii) PPP's which involve the use of private finance<sup>6</sup>.
- 3.2.4 Subject to relevant legislation in any given situation, the Government has extensive constitutional and common law powers to make commercial contracts including PPP contracts.

#### 3.3 Experience of Private Sector Involvement and PPP in Hong Kong

##### **Scope**

- 3.3.1 Hong Kong has a varied experience in private sector involvement, particularly in considering projects for PPP and other approaches, as well as in implementation. As part

<sup>4</sup> Serving the Community By Using the Private Sector – Policy and Practice, Efficiency Unit, January 2007

<sup>5</sup> Serving the Community, By Using the Private Sector, A General Guide to Outsourcing, Efficiency Unit, October 2003

<sup>6</sup> Serving the Community, By Using the Private Sector, An Introductory Guide to Public Private Partnerships, Efficiency Unit, October 2003

of this assignment, the FA has discussed relevant experience and lessons learnt with Government officials and representatives of other organisations, and undertaken specific research on case study projects.

- 3.3.2 Some trends emerge from the consideration of PPP and other private sector involvement in the provision of public services in Hong Kong. At one end of the spectrum are the less commercially viable sectors, including leisure, cultural and most arts facilities, as well as sectors where there are difficulties in finding appropriate financial incentives i.e., reliable income to attract private sector interest. At the other end are more commercially viable sectors or where existing practice provides financial incentives through an accepted mechanism.

***Current Private Sector Involvement in the Leisure and Culture Sectors***

- 3.3.3 There are many leisure facilities in Hong Kong provided by the private sector such as sports and recreational clubs etc. However, some leisure services and the majority of performing arts venues and museums in Hong Kong, including the two indoor stadia, are provided by the Government and managed by the Leisure and Cultural Services Department (LCSD) - although many activities have been out-sourced. Examples of outsourcing include:

- Revenue contracts for retailing, catering, car-parking
- Expenditure contracts include cleaning, security, horticulture maintenance, backstage technical support
- Maintenance contracts include sound operations with PCCW and electrical and mechanical services with EMSD

- 3.3.4 There is only one truly private performing arts venue in Hong Kong – the Sunbeam Theatre. There are other private venues that receive/ received at the outset, some form of Government or other external support including the Hong Kong Fringe Club, the Hong Kong Arts Centre, venues in tertiary institutions including the Hong Kong Academy for Performing Arts and venues in exhibition centres. Non-LCSD museums, which are significantly smaller than LCSD museums, include museums in tertiary institutions, museums of other Government departments, museums of not-for-profit organizations and one very small private museum which is part of a wider visitor destination. Whilst the Government provided the cost of buildings, plus the LCSD and the Hong Kong Arts Development Council funded some of their programmes, the Hong Kong Arts Centre and the Hong Kong Fringe Club are privately run, self-financed facilities with no direct funding from the government. They have relied on property rental, venue hiring, donations and sponsorships for their income to subsidise their arts and education programmes.

- 3.3.5 The operation of cultural facilities in Hong Kong has also been funded primarily by the Government. Government funding is vital since the level of private sponsorships and donations to the cultural sector is low given Hong Kong's philanthropy traditions. It should also be noted that the Government has been subsidizing the operation of non-LCSD performing arts venues indirectly through subsidizing their users (performing companies, arts organizations, education institutions or other tertiary organisations). The Hong Kong Jockey Club is the main source of subsidy for arts and culture outside the Government. To achieve its social objectives rather than commercial investments, it has funded the provision of cultural facilities and activities such as the construction of the Hong Kong Academy for Performing Arts, the maintenance and repair costs of the Hong Kong Arts Centre, the programmes of the Hong Kong Arts Festival and the Hong Kong Youth Arts Festival. In general, commercial entities have limited involvement in the provision and operation of cultural facilities in Hong Kong.

- 3.3.6 In leisure services, the private sector is involved in the management of sports centres, security, cleaning services and horticulture maintenance.

***Private Sector Involvement (PSI) and PPP in Hong Kong***

- 3.3.7 In Hong Kong PSI approaches have been used for the procurement of G/IC facilities as an alternative to the traditional Government model.
- 3.3.8 There have been a few PPP trial schemes incorporating sports and leisure facilities but none of the projects have gone ahead. Potential alternatives remain under study in a bid to find a workable business model to overcome legislative constraints, public acceptability and also to meet land use planning requirements. Elsewhere PPP approaches have been adopted for prisons but in a recent case the Correctional Services Department was unable to find an appropriate PPP solution and the project was undertaken using traditional Government funding through the Capital Works Reserve Fund and operations remain the responsibility of the Department. Reasons for not adopting a PPP approach included lack of comparable examples, lengthy lead time to determine an appropriate approach, and an absence of sufficient financial incentives.
- 3.3.9 More successful PSI examples include approaches that have been used for the procurement of G/IC facilities as an alternative to the traditional Government model. Although the type of land transaction varies, for example, land exchange, land grant and land sales, the process is relatively simple and similar – the lease requires facilities to be built which are paid for by Government on completion and which revert to Financial Secretary Incorporated ownership. Where not all the cost of the facility is reimbursed, it is assumed that the developer would bid a lower land premium or in the case of land exchange accept less reimbursement. Either way, the full cost of the facility is borne out of the public purse.
- 3.3.10 The “planning gain” approach is used quite extensively for major developments in the UK for example, in Hong Kong this PSI approach tends to be used for relatively small “gains” such as open space provision or reprovisioning of some community facilities. In this approach the lease requirement specifically requires that the redevelopment and subsequent operations fits with Government policy. For this “gain”, the bid land premium would be lower than would have been expected had these requirements not been in place and the financial supporting mechanism is thus land premium forgone.
- 3.3.11 Of the remaining examples, most are supported financially through some form of land or property incentive. Government contribution in the form of land or access is also used extensively elsewhere in the world to support development initiatives, where returns may fall short of those required by the private sector for investment.
- 3.3.12 The “railway and property” development model in Hong Kong is well known internationally. In the case of the MTR Tseung Kwan O Line, private sector investment is supported through the granting of property development rights above the stations for which there are significant returns. Under this business model, MTRCL is able to recoup some of the economic gain seen in land and property prices from rail development and support the major cost of capital investment.
- 3.3.13 There is far less experience of PPP approaches with direct payment of service/availability payments in Hong Kong. Environmental services which do not lend themselves well to support through the land/property market tend to use this model, do show that if provided with the right financial incentives – primarily a reasonably reliable stream of income - then the private sector will be interested and able to participate. However, in Hong Kong, payment for services such as municipal solid waste is some way behind full cost recovery

pricing and as such, the Government either needs to provide an adequate service fee rather than tariffs being paid direct to the supplier or at least Government must “top up” any direct tariff revenue to allow adequate returns to be made.

### **3.4 Lessons Learnt**

#### **3.4.1 Key lessons relating to Hong Kong’s experience include:**

- Adequate financial incentives are required for the private sector to finance. This can be undertaken through a range of support mechanisms including land and property as well as service payments and cash injection. Where appropriate business models could not be found, private sector funding arrangements have not been implemented
- The more commercial a service in terms of achieving adequate revenues to cover costs, the easier it is to find a business model that can work. Flexibility in fees and charges can help improve “commercialism” but for public/community services issues of affordability, competition with Government service provision etc need to be taken into consideration
- Public sentiment suggests that the relative balance between public service and private return needs to be established if land premium/ property development rights are used as a financial incentive for new sectors such as leisure and cultural sectors
- Flexibility is needed within a PPP contract where a life cycle approach is undertaken to accommodate changing market conditions and technology over the period of the contract term
- Lead time is longer to develop new PPP approaches than traditional procurement
- Facilities procured under a PPP approach require a project “champion” to take the project forward and manage the inevitable difference of views about the adopted approach. Similarly leadership is seen as important in developing partnerships between the public and private sector

## 4 PRIVATE SECTOR INVOLVEMENT AND PPP IN THE CULTURAL AND ARTS SECTORS: INTERNATIONAL EXPERIENCE

### 4.1 Introduction to the Cultural and Arts Sectors

- 4.1.1 As is clear in Chapter 2 there is now a wide range of international experience in private sector involvement and PPP approaches – which has been applied to an equally wide range of services and social, transport and other infrastructure. Most of these had been public services which had been free at the point of delivery or had been subsidised from the public purse. Relatively few of the successful PPP programmes have been used to procure or operate arts and cultural facilities. In practice facilities for culture and the arts have usually been subsidised – mainly by the public sector but also through private philanthropy – not only for the development of facilities but also for their operation and maintenance. The revenues raised direct from the users of facilities rarely cover the costs of anything other than the most commercial of cultural performances and presentations.
- 4.1.2 As Chapter 3 illustrated virtually all existing cultural facilities in Hong Kong are provided and operated by LCSD or funded through other public or tertiary organisations. Apart from service contracts to the private sector, no PPP approaches have been adopted in the arts and cultural sector. This chapter therefore examines the extent of various forms of PPP in the cultural and arts sectors by considering **international** experience. This chapter examines international experience of private sector involvement which varies in three main areas:
- The museums and galleries sector
  - The performing arts sector
  - Other visitor destination facilities
- 4.1.3 The analysis draws on international case studies for these three groups undertaken as part of this Assignment. Table 4.1 summarises some of the most relevant cases.

### 4.2 The Museums and Galleries Sector

- 4.2.1 Museums worldwide are characterized by tremendous diversity in their funding and governance. There is a wide continuum from those that can be described as fully public (e.g. the “line department” museum owned and operated by a government agency) and those that are fully private (e.g. a corporate museum or a museum that is owned and operated by a private (often wealthy) individual with the majority are somewhere in between. In the United States and Canada and increasingly in Europe, most museums are operated by either a trust, a board-governed not-for-profit private organization, or as a board-governed “arm’s length” government organization. The other key variable in determining the nature and form of a partnership in which a museum organization may be involved is whether the partnership is an operating partnership, a partnership to facilitate initial construction of a new museum, or a combination of both.
- 4.2.2 As noted in introduction however, the most fundamental reality shaping museum partnerships is the fact that museums and cultural centres rarely survive on self-generated revenue alone; that is, they virtually always require an operating subsidy from contributed (private donors, for example) and especially government sources. In the U.S. and Canada the operating subsidy averages about 70% of the museum’s total operating requirement; in other countries (such as Hong Kong) the subsidy level is usually higher.

**Table 4.1: International Case Studies, Summary of Selected Examples**

Example	Approach	Ownership	OMM	Govt Finance	Private Sector Finance	Land / Property Incentive	Govt Payment of Service Fee	Direct Fees and Charges
The Royal Armouries Museum, UK	BOT after 60 years. BOT revoked after 3 yrs	Royal Armouries (Public body)	Royal Armouries International (Private sector)	£20.8m contribution to construction costs. Government took back the museum following large losses	£14m contribution to construction costs	Not known	None	Entrance fees and shop sales
Wembley National Stadium, UK	BOO	Wembley National Stadiums Ltd	Wembley National Stadiums Ltd	£161m from three different public sector bodies	£148m private sector cash with a £433m of debt	Redevelopment of existing site		All revenues generated by the stadium, with 1% to be spent on sports education
Millennium Dome, UK	Built and operated by a public-sector owned co. Failed BOT	New Millennium Experience Company	New Millennium Experience Company	£400m plus including covering operational losses	£160m in sponsorship from commercial bankers but less than expected	Land contributed by national government agency	Government covered construction costs and operational losses	Ticket sales and sponsorship
Melbourne Convention Centre, Australia	BOT after 25 years	Private sector consortium	Govt owned authority	AUS\$410	AUS\$590	Not known		Revenues derived from convention and additional facility operations
Singapore Sports Hub	DBFO for 25 years	To be confirmed	Private sector	To be confirmed	To be confirmed	Redevelopment of existing site	Govt to pay an ongoing fee in form of an annual Unitary Payment.	Revenue from commercial, sporting and non-sporting events. Revenue-sharing mechanism will be put in place
Walt Disney Concert Hall, LA, USA	Design and Build Lease	County of LA, leased to the Music Centre	Music Centre (not for profit organisation)	US\$80m - \$110m for landscaping and car park	US\$100m plus contribution from Walt Disney	Land contributed by County of Los Angeles	County of LA funds maintenance, upkeep, security and ushers	Revenues from earned income, investments and contributions

Example	Approach	Ownership	OMM	Govt Finance	Private Sector Finance	Land / Property Incentive	Govt Payment of Service Fee	Direct Fees and Charges
The Sage, Gateshead, UK	Design and Build Lease	Gateshead council, leased to North Music Trust	North Music Trust (a charitable trust)	£70m from assorted public bodies	None	Land contributed by Gateshead Council		Revenues from the council, earned income as well as private sector donors
Lowry Centre, Salford, UK	Design and Build Lease	Salford Council, leased to the Lowry Trust	The Lowry Trust (a charitable trust)	Almost £120m from assorted public and cultural bodies	£2.25m	Land contributed by national government agency		Earned income, sponsorship, donations and cultural grants
Milton Keynes Theatre and Gallery, UK	Design and Build Lease	Milton Keynes Borough Council, leased to MK Theatre and Gallery Co Ltd.	Sub-let to the Ambassador Theatre Group (private sector)	£23m from public sector bodies	£10m from corporate and private sector grants	Land contributed by national government agency and Milton Keynes Council	Annual grant from assorted public bodies of c£350,000 towards running costs	Earned income from theatre, rental and commercial activities. 30% of profits go to MK Theatre and Gallery Company Ltd.
Baltic, Gateshead, UK	Design and Build/ Conversion Lease	Gateshead Council, leased to Baltic Trust	Baltic Trust (a charitable trust)	Almost £43m from assorted public bodies	£500,000 from private sector donations	Land contributed by Gateshead Council	National Lottery endowment to underwrite first five years of operations	Income from public sector, ACE and private sector. Sponsorship, donations, corporate membership c. 1/3 of running costs
Guggenheim Bilbao	Franchise (Govt being franchisee)	State ownership	Guggenheim Bilbao Foundation	US\$100m construction costs	None		Govt pays operational expenses	Entrance fees, shop sales
Royal British Columbia Museum	BOT with 30 year land lease	Unclear	National Geographic Society	None	National Geographic Society paid capital costs			Seat sales with payments made to RBCM

- 4.2.3 Obviously this fact has a determining effect on the kinds of partnerships that can be pursued, and the types of partners that are willing to become involved.
- 4.2.4 Where they occur, public-private partnerships are typically intended to harness up-front private sector capital investment in return for the opportunity to secure returns based on the subsequent income stream including end user charges, public subsidy or other sources. Since most museums and cultural centres produce no such income streams from operations and in fact usually require a subsidy, their application to such institutions is different than for entities with commercial potential. This of course limits the scope of such partnerships.
- 4.2.5 The case studies provide illustrations of the way public-private partnerships can work for the initial construction and ongoing funding and operation of museum-related organizations. The experience of nearly all of these international examples illustrates the constraints on the scope for private sector participation:
- In the museum and gallery sector it is common for virtually all of the construction cost of facilities to be met by the public sector. For the development of the Guggenheim Bilbao, the Basque and the regional governments financed 100% of the new museum at total cost of US\$250 million. In the UK the availability of Public Lottery Funding for Arts facilities has seen an increase in major publicly funded projects such as the Baltic at Gateshead where the £46 million construction cost was met 75% from Lottery funds and virtually all of the balance from a cocktail of local, regional, national and European Union funding
  - Free land is also a key public sector contribution – often as part of an industrial regeneration package through which sites have been reclaimed and assembled. The City of Bilbao donated the land on which the Guggenheim Museum was built and Gateshead Council donated the Baltic site and unconverted building - approximately 10% of the cost
  - It is not uncommon for public authorities to make grant towards the start up and establishment or collection costs. The City of Bilbao made a US\$20-million donation to the SRGF called a "rental fee" in reference to the future use of the Guggenheim's collection and "brand name." – in effect an availability payment. A one off endowment fund to the Baltic was also made by the UK Lottery used to subsidise start up and operation for 5 years
  - Museum partnerships with other public entities are common. These are often public educational institutions (such as school districts or universities and colleges), other museums, or not-for-profit government agencies. Often such partnerships relate to programme delivery but can also extend to training initiatives or other services such as conservation or collection management
  - The most common example of the involvement of commercial entities is in the day-to-day operation of museums - typically the operation of the museum's food outlet and, less commonly, retail outlets – usually through a concession arrangement. There has been a move towards more creative use of commercial concessions at for example the Royal British Columbia Museum (RBCM) in Canada where a major PPP project is the addition of an IMAX large format theatre. The IMAX theatre partnership, is with the not-for-profit National Geographic Society (NGS). In addition, the formation of the RBCM Corporation – an arms length public corporation has provided the incentive and the legal right to pursue more entrepreneurial activities

- Commercial organizations often contribute in-kind services or make one-time donations for specific museum projects. It is also not uncommon for them to fund a particular programmatic initiative related to their philanthropic goals
- In return for this very high level of public funding in the museum sector the Government has been able to secure relatively high levels of regulation through agreements and Board participation by local government representatives. For example, the Guggenheim agreement with Bilbao includes programmatic safeguards; the contract asks that SRGF supply Bilbao with at least three exhibitions per year of equal calibre to those taking place in its New York venues
- The main return for the public sector however has been a higher cultural visibility nationally and internationally – often in cities which have lacked such a profile in the past - and a beneficial economic impact for the visitor economy of the city. Guggenheim Bilbao has achieved the Museum's success, and higher visibility of Bilbao with visitors of nearly 1 million per annum and the Baltic has more than doubled expected visitor numbers at over 500,000

4.2.6 An interesting exception to the significant scale of public funding of museums and galleries has been the UK's PFI initiative for the Royal Armouries Museum relocation from the Tower of London and new development of facilities at Leeds and subsequent operation for 60 years by a private company, RAI. Royal Armouries contributed its collection and some curatorial and marketing costs. The construction was completed on budget in 1996 with RAI funding 33% of the building cost only, but taking a commercial risk on visitor income which never reached 60% of the break-even operating figure. By 1999 the PFI agreement had to be revised and the Armouries took back responsibility for running the museum and RAI retained some profit making services such as catering, parking and hospitality to pay off its debts. This was one of the first PFI agreements made and, according to the UK National Audit Office, it is unlikely that a similar project would now be approved without the clearer demonstration of viability which museums find hard to make.

### 4.3 The Performing Arts Sector

4.3.1 As with museums, PPP procurement arrangements designed to harness private sector capital investment up-front in return for the opportunity to secure returns based on the subsequent income stream from operations has not occurred in the performing arts venues field – excluding commercial cinemas, theme parks and sports stadia – because most of these facilities operate at a loss and there is no expectation of a return to drive private sector's involvement. Although revenues from the performing arts typically cover a higher proportion of operating costs than museums and galleries, virtually all performing arts venues require public funding for operations as well as their construction.

4.3.2 The level of private funding contributions varies significantly across regions and countries, depending on the area's cultural and philanthropic traditions. In Europe and Australia, it is usual for Government to meet most or all of the costs of performing arts facilities. In the US, the private sector often contributes a higher proportion. The case studies also provide illustrations of the scope of public-private partnerships for the construction and operation of a range of different types and locations of performing arts venues:

- In these examples public funding has met most of the costs of development. In the UK the availability of Public Lottery Funding for Arts facilities has been a major funder of performing arts venues. The UK Lottery funded 60 – 70% of the capital costs of three of the most recent and successful major theatre developments in the UK - the Milton Keynes Theatre and Gallery, the Sage,

Gateshead and the Lowry at Salford. In each of these cases virtually all of the balance of the funding came from a cocktail of local, regional, and national and European Union Funding

- Private sector contributions are more likely to be made in the form of donations and sponsorships rather than commercial investments. These typically take the form of:
  - Commercial entities, seeking naming rights or other benefits
  - Commercial entities with a philanthropic wing for making donations including individuals or commercial entities providing sponsorships and donations to the facility or its programmes and other activities
  - Trusts and foundations, seeking to fulfil social responsibilities charters – including international foundations and individuals
- In the UK only Milton Keynes attracted a 10% development cost donation from the private sector. In Los Angeles, the Walt Disney Concert Hall attracted private donations for more than 50% of the capital costs – principally from the Disney family. In the US donations are more common than risk capital
- A more common form of private sector participation in the development of performing arts venues has been in their construction as part of a mixed commercial development for which they can provide an attractive anchor. The Orleans Arts Centre in Ottawa is being developed as part of arrangement between City of Ottawa government and a private consortium. The Arts Centre will be the centrepiece of a larger Orleans Town Centre development, and will also include hotels and other retail/commercial and residential developments. In this case the incentive for the private-sector firms to be involved is the profit-making potential in the development of retail, office/commercial and residential properties at the Orleans Town Centre site. Similarly the Lowry has been developed as part of a mixed retail and media/technology development and commercial rents make a contribution to theatre operating costs
- In the case of the Orleans Arts Centre, a PPP procurement arrangement was made between the City of Ottawa government and a private consortium based on a design, construction, finance, operation and maintenance contract with ownership reverting to the City after the agreement expires in 25 years
- Perhaps the most common form of private sector participation in performing arts venues, particularly theatres, is for a commercial entity to operate the facility or its ancillary commercial activities (restaurants, bars, shops, car parks etc.) on a service contract or lease. In this case performing companies or presenters are sharing the commercial risk on presentations with the theatre management. In Milton Keynes and Richmond the theatre is owned or leased to a charitable Theatre Trust and the theatre then leased to the private Ambassador Theatre Group Ltd, a commercial theatre and production company

#### 4.4 Other Visitor Destinations Sector

- 4.4.1 The analysis of museums and performing arts venues funding strategies suggests that risk sharing PPP arrangements are uncommon in both construction and operation because of the limited market revenue generated by cultural facilities compared with the capital and operating high costs. However the more commercial the “cultural” activity the more revenue generated and other visitor destination facilities such as sports and events stadia and arenas, convention and exhibition centres do provide multi-purpose

accommodation for commercial entertainment and cultural events. The review of international cases has included visitor destination facilities of this type and indicates that risk sharing PPP arrangements such as DBO and DBFO contracts are increasingly being used by public agencies to provide these facilities. The main features of these arrangements include:

- The increasing use of risk sharing PPP arrangements such as DBO and DBFO contracts based on the builder /operator retaining all or most of the revenue receipts. In some cases the public agency commissioning the facility also shares in any operating profit. However, in the case for the DBO for the new Wembley National Stadium in the UK, the Football Association is providing annual income guarantees – a form of availability payment – and the terms of the DBFO contract for the proposed Singapore Sports hub includes an annual “Unitary Payment” by the Government together with a revenue sharing mechanism to incentivise the contractor to increase use of the site for commercial events
- In each of these cases, unlike dedicated cultural facilities, the capital funding has come primarily from the private sector – though in all cases there has still been some public capital contribution. As for cultural facilities in the UK, the Lottery Fund has been widely tapped for this type of facility for Wembley (£120 million – nearly 20% of capital costs) with other public sector grants taking the total over 25%. At the Melbourne Convention Centre the City will contribute around 6% of the total capital and operating costs
- Some of these subsidies recognise the risks shared by the private sector which are still relatively high for this type of signature architecture / market driven visitor facility. At Wembley, there have been significant cost overruns as a result of time cost penalties in the construction contract as the project has gone up to 2 years overrun. The experience of the UK Millennium Dome exhibition and events arena illustrates the risks of over estimating visitor numbers. The project was originally conceived as a DBO but by 1996 it became apparent that the private sector would not accept the risks of the short term visitor expectations (for year 2000) of 12 million visitors. The £700 million Dome was eventually mainly public sector funded using Lottery Funds and other Government grants with only 15 -20% coming from private donations. It attracted only around 6 million visitors and a loss of around £200 million was made by the government-owned private sector company set up to build, operate and dispose of it
- For these types of projects there is now a widely experienced group of international contractors, financiers and consortiums of other skills which have bid for and implemented PPP contracts. The combination of skills is wide and usually includes marketing, maintenance, and real estate skills to assess and manage the risks. Consortiums with these skills do not exist to the same extent in the cultural and arts sectors
- The level of regulation sought and achieved by the public sector organizations commissioning this type of facility is relatively low, compared with what might be expected in the cultural sector. At Wembley the contractor is required to make a minimum amount of seats at events publicly available, has no naming rights and cannot take on an anchor tenant or resident company / club. Most other conditions relate to pricing and are compensated through service payments

## 5 PRIVATE SECTOR INVOLVEMENT AND PPP IN AREA BASED DEVELOPMENT

### 5.1 Area based Approaches for Cultural Districts

5.1.1 Some cultural districts in the major international cities have developed organically over a long period of time. However it is now more common - as in many of the examples above and as proposed for the WKCD – for them to be created through an area-based regeneration and planning process where the Government provides the lead for a range of public and private partners in delivering a complex mix of cultural and commercial facilities and associated infrastructure for the wider public benefit. Many of the most successful international cultural projects have formed part of such an area based initiative. WKCD is distinctive in that it is a new reclamation site – rather than having the problems of a brown-field regeneration site – and because of the number, scale and range of cultural facilities being considered. However, international experience shows that the opportunity to plan and develop the area comprehensively – an “area based” approach – will be important to the use of PPP approaches.

5.1.2 Area based development case studies were undertaken as part of this Assignment. They include a rich mix of different types of development and cultural facilities are often the centre pieces of the districts, such as the Guggenheim Museum in Bilbao, the Baltic and the Sage in Gateshead, and the Australian Centre for the Moving Image and the Ian Potter Centre at Federation Square in Melbourne.

5.1.3 Key features of these cultural development led districts include:

- The economic and financial success and urban vibrancy of this type of area-based development is based on mixed use development including high and lower value uses which complement each other and ensure that there is all-day and evening activity. Culture and leisure are usually an important component of this mix. It also means that incomes from commercial uses can be used to cross-subsidise cultural uses
- The objective of much of this type of mixed area-based development is to use the new investment and development as a driver for change in the economy and quality of life in the city as a whole by boosting the visitor economy, providing opportunities for the “Live and Work City” and adding a new dimension to the image of city, nationally and internationally. Many cities have required the regeneration of relatively large areas of former industrial or port/waterfront sites that required comprehensive mixed use development to transform the environment and economy of the area
- All the international experience shows that mixed use area-based development is most effectively implemented through the establishment of an independent dedicated development authority, or not-for-profit corporation, for the planning, development and, in some cases the subsequent operation and maintenance of the district and its facilities. Most of these are partnerships of public agencies with an interest in the area with, in many cases, the participation of representatives of the private sector including landowners and developers – in effect they are public / private partnerships
- Area-based agencies may be public authorities formed under statute or may be incorporated as private entities. The key is their status as independence of

(local and national) government with an independent Board and, critically, an independent budget with the ability to retain income from land disposals and other receipts, engage in PPP and service contracts and package and prepare sites for development using independent master planning and development control powers

- In areas with a strong cultural and entertainment focus to development, continuing festival and public event programming are the key to success. The Harbourfront Centre has set the world standard in this regard, but, while operated by a private not-for-profit organization, it requires significant government operating support every year to maintain operations. Other authorities have been able to enter into long term operation and maintenance contracts or incorporate whole-life servicing arrangements into PPP type contracts

## 5.2 Area Based Agency Approaches for WKCD

5.2.1 The main lesson of this international experience in some of the most successful and transformational regeneration areas and cultural districts has been the importance of creating a dedicated area-based agency with wide public sector and private sector representation and dedicated resources and powers to plan develop and operate facilities and infrastructure in the area. The WKCD is such an area albeit with a unique scale and challenge to provide a wide range of cultural facilities and a world class environment. It was proposed to create a statutory authority for the development and management of WKCD.

5.2.2 The FA believes that the role of this authority – and the dedicated powers and resources it will have at its disposal - will be central to the success of the WKCD and to effective PPP arrangements. Previous developers' proposals (assuming their proposed development mix<sup>7</sup>) indicated that – across the area as a whole - the return from commercial development was capable of supporting the costs of cultural and communal facility provision. The ability of a dedicated agency to cross subsidise development, subsidise and cross subsidise operations through project packaging and PPP agreements will be an important part of the public / private funding strategy.

## 5.3 Three Relevant Cases

5.3.1 The above research suggests that there are relatively few area based development initiatives or development agencies which have the primary objective of the provision and operation of cultural facilities and are of a similar scale to that proposed for West Kowloon. Most of the cultural facilities exemplified above are relatively free standing and many of the area based development agencies have a primary objective of regenerating and promoting an area for business, leisure or housing.

5.3.2 Of the case studies cited in section 5.1 above however, three cases are clearly culturally led developments of multiple cultural and commercial facilities and have been planned and developed and/or operated by dedicated area based agencies – and each in waterfront locations. As such they provide a useful reference and comparator for the WKCD for alternative area based agency approaches to development and operation of cultural facilities. The three agency cases presented here are:

<sup>7</sup> Note, that the overall return estimated for these proposals were based on different plot ratios and the results of this assignment will depend on the development parameters and assumptions adopted and will not necessarily show an overall financial return

- *The South Bank Corporation, Brisbane* – responsible for the South Bank Precinct on Brisbane waterfront in Queensland, Australia.
- *Bilbao Ria 2000* – responsible for the Abandoibarra area regeneration on Bilbao riverfront in northern Spain including the Guggenheim, Bilbao
- *Harbourfront Centre, Toronto* – responsible for the operation of the Harbourfront Centre district, a revitalisation project on Toronto waterfront.

#### ***South Bank Corporation, Brisbane***

- 5.3.3 The South Bank Corporation was responsible for remodelling **Brisbane's South Bank cultural and recreation precinct** after World Expo 1988. The precinct encompasses an area of 125.5 hectares across the Brisbane River from the city's CBD. When selected as the site for World Expo 88, South Bank was a near-derelict port but was already home to the Queensland Performing Arts Complex (QPAC) as the lone new development. In 1989, South Bank Corporation, a Queensland Government statutory body was established to oversee the development and management of a new South Bank.
- 5.3.4 Over the next three years the South Bank Precinct and surrounding areas underwent ongoing urban renewal. The Corporation's initial project was South Bank Parklands, which opened in 1992, consisting of a man-made beach and lagoon, rainforest and garden walks, more than 20 restaurants and cafes, free picnic and barbecue areas and some paid tourist attractions. Development was subsequently completed on:
- Rydges South Bank Hotel,
  - Griffith University,
  - Park Avenue residential apartments and
  - Brisbane Convention, Exhibition and Entertainment Centre.
- 5.3.5 Although the original development of QPAC preceded the creation of the Corporation, subsequent cultural development clustered around the site and, today, South Bank is also Brisbane's principal arts, cultural and higher education precinct including:
- Queensland Performing Arts Centre
  - Queensland Art Gallery
  - Queensland Museum
  - Opera Queensland
  - Queensland Theatre Company
  - State Library
  - South Bank Institute
  - Griffith University's Queensland Conservatorium and Queensland College of Art
  - University of Canberra, Brisbane Campus
- 5.3.6 However, rather than being funded by the Corporation, these cultural facilities have been developed primarily by the State, Federal and City Governments. They continue to grow and expand with the state government committing Aus\$250 million in capital expenditure from 2000 – 2005 through its *Millennium Arts Project*. This involves the redevelopment of the State Library, State Art Gallery and Museum and the addition of a Modern Art Gallery, which will be the largest modern art gallery in Australia. The project also includes a new entrance for the Queensland Museum, a new public plaza with improved access

throughout the Queensland Cultural Centre and a range of outdoor, recreational and open spaces.

- 5.3.7 The **South Bank Corporation** oversees the precinct development and operations and is a body corporate established by the Queensland Parliament through a dedicated “South Bank Corporation Act”. Significant amendments to this Act in October 1991 and December 1993 reflect the changing role of the Corporation towards **the ongoing management** of South Bank.
- 5.3.8 The vision of the Corporation is to plan and facilitate the development and operation of a successful, world-class cultural, leisure, business and residential precinct for the enjoyment of South Bank visitors and the economic benefit of Brisbane's community and investors. The Corporation's primary activities include:
- Maintaining and administering the South Bank Corporation Area Approved Development Plan
  - Coordinating the development of land within the Corporation Area
  - Disposing via lease land vested in or under the control of the Corporation
  - Promoting, organising and conducting tourist, education, recreational, entertainment, cultural and commercial activities within the Corporation Area
  - Marketing and promoting South Bank as an appealing and entertaining precinct for leisure, tourism and convention activities for Queensland residents and interstate and international visitors
  - Promoting South Bank as an attractive and viable residential and commercial address to investors, financiers and business operators
- 5.3.9 South Bank Corporation Board is chaired by a leading private sector businessman and has representatives from both state and local government, as well as commerce, the arts and culture.
- 5.3.10 The Corporation's primary asset has been the 125.5 hectares site. Following the 1988 Expo there was public objection to the Queensland Government's intention to sell land to a single development Consortium which led to the creation of the Corporation and an investment by the Government, through the Corporation, of over Aus\$100 million in the Parklands project. The Corporation owns the freehold of the land under its control and is also the Planning Authority. Land has been parcelled for the subsequent commercial development on long term development leases to private or state developers. Sites are normally tendered in packages in a three stage process – (1) a development agreement, where deposit paid and plans made, (2) a limited life development phase with sunset clause (if development does not happen as agreed the Corporation can cancel the agreement), followed by (3) issuing of a lease when development is completed.
- 5.3.11 The Corporation uses receipts earned from leasing land and buildings to repay Government investment in Parklands and the major master planning and infrastructure works it undertook in the late 1990's. The Convention Centre is an independent business unit of the corporation with any profits going back into Convention Centre and not used to offset other costs and debts.
- 5.3.12 Cultural programming forms an important part of the Corporation's area management role. The Corporation sponsors and partners the major cultural organisations to deliver events in the area and provides low cost or no-cost spaces for smaller scale arts events – including use of the 3000 seat Suncorp (sponsored) piazza owned and operated by the Corporation. South Bank also continues to be funded for this important area management

and programming role (a turnover of approximately Aus\$20 million which is expected to be expanded) by a combination of Government grant (c.60%) and from rents from Corporation owned properties and joint ventures (c.40%).

- 5.3.13 It is therefore apparent that in the case of the South Bank Corporation their key tasks have been planning and securing the redevelopment of the area, its infrastructure and communal facilities and preparing and packaging sites for commercial development – not for the development or operation of cultural facilities. This has provided a setting for the development and expansion of the cultural facilities in the area by the State Government and gives the Corporation an important continuing area management and marketing of the South Bank as a cultural and business district. In this case it is the presence of the cultural facilities that have been used as an anchor for the area and as a magnet for revenue generating commercial development and as an economic driver for the city.

#### ***Bilbao Ria 2000***

- 5.3.14 The success of the Bilbao Ria 2000's cultural development and urban **redevelopment of the Abandoibarra riverfront district** of Bilbao is well known. The impetus for the plan, which features a branch of the Guggenheim Museum as its centrepiece, was deindustrialisation in Bilbao which created high unemployment and left many industrial sites and buildings derelict. In 1987 Bilbao City Government drew up the first General Urban Plan for development of areas such as Abandoibarra and in December 1992 a non-profit making entity was created, owned equally by Basque Administration and the State Administration - Bilbao Ria 2000 - to coordinate and manage the economic recovery of Bilbao.

- 5.3.15 Abandoibarra is the most prominent of all the area based projects carried out by Bilbao Ria 2000. This area at the heart of the city on the riverfront covers 35.8 hectares and is destined to become the new cultural, administrative and business centre of the new Bilbao. The development encompasses mixed use waterfront development including:

- Zubiarte Shopping Mall - opened in November 2004 as a themed shopping centre of 25,000 square metres
- Hotels and Restaurants – including the Sheraton Hotel with 215 guest rooms, opened in July 2004
- 78,000 sq.m of office development including a 165 metre office tower of 50,000 sq.m designed by César Pelli, as a company headquarters. There will also be two residential/commercial buildings of 20,000 sq.m on each side of the tower
- Residential development of approximately 600 units – 78,000 sq.m
- Riverfront Parks comprising 11.6 hectares of the total area. This was the first completed structure along 800 metres of the waterfront as a facility to connect existing promenades. The park also features the collection of sculptures, "Paseo de la Memoria," to commemorate the industrial activity of the area with works by well-known Basque artists and others from overseas
- Other communal facilities including playgrounds, sculpture gardens, and a recently restored historic bridge

- 5.3.16 However Abandoibarra is now also Bilbao's principal arts, cultural and higher education district including:

- Guggenheim, Bilbao
- Bilbao Ria Maritime Museum

- Duesto University facilities of 15,000 sq. m. including a library
  - Restored and renovated Museum of Fine Arts
  - Euskalduna concert hall and convention centre
- 5.3.17 **Bilbao Ria 2000** is a non-profit making limited liability company, owned equally by the central government administration through public companies (SEPES - a public land management company, the Bilbao Port Authority and the rail companies) and the Basque regional and local administrations (Basque Government, the Provincial Council of Bizkaia, and Bilbao and Barakaldo local authorities). The Board of Directors comprises 20 senior representatives of the public authorities, chaired by the Mayor of Bilbao.
- 5.3.18 The organization identifies and assembles sites for expanding economic activities and for the physical upgrading of derelict land. It also has the authority to develop urban renewal strategies within the metropolitan areas of Bilbao and was given access, management authority and control over public resources while remaining an autonomous private entity.
- 5.3.19 Its functions include:
- Coordinating and implementing urban planning, transport and environmental action
  - Determining a project development programme
  - Preparing sites and parceling them for commercial development by the private sector
  - Searching for investors and other sources of finance
- 5.3.20 Bilbao Ria 2000 was created with an initial share capital of 1.8 million euros. The public shareholders transfer their land in the area to the agency who invests in site preparation – funded by private bank loans - and sell off the resultant development plots to finance its activities. As a non-profit making entity, the capital gains generated are reinvested in the regeneration of Abandoibarra and other former industrial areas and projects. Bilbao Ria 2000 also receives European Union subsidies, which in recent years have accounted for 14% of its investment budget.
- 5.3.21 This approach has enabled the Abandoibarra area based project to be self financing without any further direct investment by the public sector. Revenues from the sale of commercial sites are retained by the agency enabling the agency to **part** fund cultural and communal developments that are not self financing, including the Guggenheim Museum. All of the cultural facilities have received significant levels of direct public funding from other sources however. The private Duesto University will finance the development of and operate a library as part of a planning gain-type arrangement.
- 5.3.22 In the case of Bilbao Ria 2000's development of the Abandoibarra therefore the agency's primary role has been as a public development agency assembling, funding the preparation and disposing of sites for commercial development and cultural and communal facilities. Revenues from commercial disposals are used to cross subsidise their financial contribution to cultural developments - which also receive funding from other public sources. Cultural facilities have not been directly packaged with commercial sites but some planning gain projects have been secured. At this stage the agency has had no role in the operation of cultural facilities or cultural programming of the area.

**Harbourfront Centre, Toronto**

- 5.3.23 Harbourfront Centre is a non profit making cultural organization which manages cultural facilities, events and activities in the four hectare **Harbourfront Centre on Toronto's waterfront** encompassing York Quay and John Quay (south of Queens Quay West). The site attracts over 12 million visits each year.
- 5.3.24 Original ownership of land and initial ownership and operation of the Centre was in the purview of the federal government. Construction was financed entirely by the Government of Canada, through the "Harbourfront Corporation", a federal Crown Corporation established in 1972.
- 5.3.25 The Centre includes a variety of cultural facilities including:
- Premier Dance Theatre (proscenium style), 446 seats
  - Du Maurier Theatre Centre (black box style), 357-425 seats
  - Studio Theatre (proscenium style), 196 seats.
  - Power Plant Gallery, 10,000 net sq. ft. of exhibition space
  - York Quay Gallery, 2,275 net sq. ft. of exhibition space
  - An additional 3,500 net sq. ft. of temporary exhibition space
- 5.3.26 The Harbourfront Centre includes relatively little commercial development. It has a 120 sq.m gift shop and a 380 sq.m food service area, which is concessioned out. There is also a Craft Studio, housed in a multipurpose building that includes a craft gift shop, lecture theatre, café, multipurpose halls, galleries, and programme spaces. The Centre also operates two marinas and five parking lots.
- 5.3.27 The Harbourfront Centre is now therefore primarily an operating organisation for both the cultural facilities and for the site of the centre as a whole. Festival and public event programming are a key part of the operation and Harbourfront Centre has set the world standard in this regard. The Centre is:
- Creator and presenter of over 4,000 events annually
  - Partner to more than 450 community and cultural groups
  - A multi-disciplinary artistic and cultural promoter showcasing works in contemporary visual arts, crafts, literature, music, dance and theater for adults and children
  - Host to 30,000 children at School by The Water and 4,500 children at camps annually
- 5.3.28 From its beginnings as the "Harbourfront Corporation", a federal Crown Corporation established in 1972, **Harbourfront Centre** was formed in January 1991 as a non-profit charitable organization with a mandate to organize and present public events and to operate the 10-acre site. Harbourfront Centre is now a private not-for-profit organization with operations supported by government, private sector contributions and earned revenues. It is governed by a 26-person community based volunteer Board of Directors.
- 5.3.29 In the 1990s the Government of Canada, wishing to divest itself of responsibility for Harbourfront, gifted the land over to the present landowner, the City of Toronto, which is now the owner of the site. The Crown Corporation was empowered to manage development. Development rights were given to the Corporation for a wider area of the waterfront to build residential and some commercial facilities and to generate funds for

communal facilities and for park and cultural programming. This development generated sufficient income to support the building of the Harbourfront Centre's cultural venues.

5.3.30 In 1997 the City entered into 99-year lease with the Harbourfront Centre organisation to operate the cultural facilities and manage and programme the Centre as a whole. The Centre is funded by:

- government grants and contributions which constitute about one-third of its annual operating budget
- generated revenues to support two-thirds of the annual operating budget
- all events and programmes are offered at reasonable prices with many completely free of charge
- assistance by approximately 2,000 volunteers who contribute their efforts and time

5.3.31 Whilst operated by a private not-for-profit organization, Harbourfront requires significant government operating support every year to maintain operations. In May 2006 the Government of Canada announced new funding for the Harbourfront Centre to enable it to continue operations and to repair its aging infrastructure.

5.3.32 The Harbourfront Centre is therefore primarily a facility operating and area programming organisation funded from facility and event operating revenues, leasing ancillary commercial space to concessionaires, but also from City government subsidies. The cultural facilities themselves were developed by a preceding Crown Corporation using income generated from land gifted by the federal Government and parcelled by the Corporation for residential and commercial development by private developers.

#### **5.4 Key Features of Cultural District Agencies and Indicators for the Proposed Statutory Authority**

5.4.1 Table 5.1 summarises and compares the main features of each of the cultural district agencies including the nature of the area developed and operated, facilities provided, their main development and operating objectives and characteristics and financing arrangements. Where appropriate these are compared with the same features of the WKCD and provide a series of key indicators for the role of a proposed statutory authority.

5.4.2 This analysis suggests that even where the main objective of the area based agency has been to develop and operate a "cultural district" the approaches of the agencies have differed in respect of their development role and their operating role. The lessons of these alternatives are taken up for the proposed statutory authority in section 6.3.

**Table 5.1: Key Features of Cultural District Agencies and Indicators for the Proposed Statutory Authority**

Case Study	Location	Site Area	Organisation Status	Area Development Objectives	Cultural Facilities	Commercial / Other Facilities	Development / Operating Approach	Development Financing	Land Assembly / Disposal
<b><i>The South Bank Corporation, Brisbane</i></b>	South bank of Brisbane River - opposite the city's CBD	125.5 ha	Body corporate established by Queensland Parliament through a dedicated "South Bank Corporation Act"	Regeneration of Brisbane's South Bank as a cultural and recreation precinct after World Expo	Queensland Performing Arts Centre Queensland Art Gallery Queensland Museum Opera Queensland Queensland Theatre Company State Library South Bank Institute Griffith University - Conservatorium and College of Art University of Canberra -Brisbane Campus	South Bank Parklands Rydges South Bank Hotel Griffith University Residential apartments Convention, Exhibition and Entertainment Centre Suncorp Piazza	Plan making and site assembly / disposal for commercial development to subsidise continuing area management and cultural programming  No role in development of cultural facilities or their operation	Arts and cultural facilities are financed by direct public funding only. No funding by corporation  Proceeds from commercial development leases and other commercial operations fund area management and programming	State Govt transferred land at no cost to Corporation  Long term development leases on sites for commercial development
<b><i>Bilbao Ria 2000</i></b>	Riverfront site on edge of City Centre – former industrial sites	38.5 ha	Non-profit making limited liability company, owned by governments	Regeneration of former industrial area for mixed use cultural and commercial development	Guggenheim Bilbao Bilbao Ria Maritime Museum Duesto University facilities inc. library Restored Museum of Fine Arts Euskalduna concert hall and convention centre	Zubiarte Shopping Mall Hotels and Restaurants Office devpt. - 78,000 sq.m Residential - 600 units Riverfront Parks Other communal facilities	Plan making and site assembly / disposal for commercial development to subsidise cultural / communal development.  Limited area management role. No cultural operations	Arts and cultural facilities are part financed by proceeds from sale of commercial development sites. Also other direct public funding	Public sector shareholders transfer land at no cost to the agency  Sale of freeholds for development

Case Study	Location	Site Area	Organisation Status	Area Development Objectives	Cultural Facilities	Commercial / Other Facilities	Development / Operating Approach	Development Financing	Land Assembly / Disposal
<b>Harbourfront Centre, Toronto</b>	Waterfront site – former quayside	4 ha	Non profit making cultural organization (preceded by Crown Corporation responsible for development of facilities)	Cultural led development to regenerate former dock and quayside area	Premier Dance Theatre Du Maurier Black Box Theatre Studio Theatre Power Plant Gallery York Quay Gallery Temporary Exhibition space	120 sq.m. gift shop 380 sq.m. food service area Craft Studio 2 marinas 5 parking lots.	Centre mainly responsible for cultural facility operation and area programming Centre preceded by Crown Corporation responsible for development of cultural facilities	(By preceding Crown Corp.)  Cultural facilities financed by proceeds from sale of commercial development sites.	(By preceding Crown Corp.)  Federal Govt transfer land at no cost to Corporation  Sale of freeholds for development
<b>West Kowloon Cultural District</b>	Reclaimed waterfront site at West Kowloon	40 ha		Cultural led development to enhance World City status	Major Performance Venue, 2 Great Theatres Concert Hall, Chamber Music Hall, Xiqu Centre 4 Medium Size Theatres, 4 Black Box Theatres, Piazzas, M+, Exhibition Centre	Residential and Commercial Development  Automated People Mover Roads Car parking  Public Open Space Other G/IC Facilities			

## 5.5 Lessons Learnt from International Experience

5.5.1 The following key points can be drawn from the analysis of international experience in Chapters 4 and 5 above:

- All international experience indicates that cultural facilities are typically loss making in operating terms – museums typically cover only 30% of operating costs – and rarely make any contribution to capital costs. This severely restricts risk sharing PPP arrangements which must offer sufficient financial incentives to the private sector. The more revenue generating the facility such as visitor destination facilities, sports and events stadia and exhibition or convention centres, the more potential there is for risk sharing PPP arrangements
- In these circumstances nearly all construction of cultural facilities has been directly public sector funded or heavily subsidised. A wide range of public sector arts, local, regional and national funding programmes have been developed for the capital funding of facilities and have been used as a cocktail of public funding. Even more commercial visitor destination and events facilities have attracted public capital grants
- Where government initiated projects have sought private partners to help them deliver the projects, such private partners are rarely for-profit commercial organizations. Most often, they are other not-for-profit private organizations such as trusts and foundations. Museums in particular need an independent Trust or Foundation Board and the ability to retain their own revenue to facilitate philanthropic donations and attract collections and exhibitions
- Where private capital is contributed it is usually in the form of donations and with a few exceptions makes up only a small proportion of total capital costs
- Where there is private sector participation it is usually in the form of service contracts or leases – most frequently for the operation of ancillary facilities such as catering, but, in the case of theatres, some other performance and events venues the contracting of specialist operating or production companies is common
- The other form of PPP in common use for capital development is through “planning gain” or other cross subsidisation arrangements with commercial development on the same site or in the same area. This most commonly occurs in mixed use development areas
- Many of the most successful cultural developments are located in area-based projects involving a mix of commercial, residential and community uses which complement the arts and cultural uses functionally and financially
- In many cases a statutory body has been established as an autonomous entity to oversee the planning, development and operation of the mixed use area. This arrangement offers the flexibility and efficiency required and balances the interests of the Governments and their private sector partners
- Even where the main objective of an area based agency has been to develop and operate a “cultural district” the approaches of the agencies have differed in respect of their development role and their operating role
- In return for a very high level of public funding of cultural development Governments have been able to secure relatively high levels of regulation through programming agreements and Board participation by councillors. The more commercial the facility the less the level of regulation which is achieved

- These projects are carried out to meet policy objectives such as cultural development, urban renewal, economic and tourism development objectives, and the projected public benefit of the projects is used to justify the high levels of public spending

## 6 PRIVATE SECTOR INVOLVEMENT IN WEST KOWLOON CULTURAL DISTRICT

### 6.1 Public Funding of Cultural and Communal Facilities

- 6.1.1 The basis of the objective of this Report lies in the concept that alternative funding approaches to traditional Government provision of public services could assist in meeting cultural objectives, as well as offer other efficiency and financial benefits. It is clear from the analysis of Hong Kong and international experience that nearly all of the types of cultural and associated communal facilities that are to be developed and operated at the WKCD are loss making when measured in terms of the **market** revenue generated. Many cultural facilities do not cover the cost of operations and maintenance and very few are able to make any contribution to recovering the capital costs. There has therefore been very limited scope for the private sector to take the lead in development or operation of facilities. In virtually all cases both the development and operation of facilities have involved significant levels of **public subsidy** in a wide range of different forms and at different levels – and where there is a minority contribution by the private sector it is unlikely to be at risk. In the few cases where public sector subsidy has not been sufficiently available the facility has fallen into bankruptcy or been taken back into public ownership.
- 6.1.2 The issue for governments has therefore been the level, source and form of public subsidy which is most efficient and cost effective. The wide range of subsidy methods used by government and other public agencies in the cultural sector includes:
- Government's main spending programmes and public works funds
  - Grants or soft loans from dedicated arts, heritage, economic development, regeneration funds or lotteries funds etc.
  - Free or below market value land and buildings, rent or premium reductions etc.
  - Service payments (including availability payments, usage payments, performance payments) made by the public sector to private partners as part of risk sharing PPP contracts
  - Assembly and parcelling of development site packages by public development and planning agencies to combine high value commercial and low or negative value cultural uses to secure an overall viable development package
  - "Planning gain" schemes in which private developers will construct and transfer back to the public sector communal infrastructure and other (cultural, community or social) facilities as part of the terms of a planning / development consent
- 6.1.3 All of these are forms of public subsidy delivered in different ways – most of which are already employed in Hong Kong (as seen in chapter 3) in a wide range of public services, infrastructure and facility development arrangements with the private sector.
- 6.1.4 The analysis has clearly shown that in determining appropriate methods of involving the private sector it is important to also consider the appropriate method to involve and incentivise the private sector. Thus the key consideration issue is the broad level of market financial viability. In theory, if the public sector financial inducement is high enough then the private sector will be incentivised, but in practice there are limitations.

One such limitation particularly relevant for the cultural sector is the lack of private sector players with the right skills and resources<sup>8</sup>.

6.1.5 In terms of the facilities development at WKCD therefore, this chapter adopts a framework of three broad “classes” of development which are expected to require some form of subsidy as set out below. This does not preclude individual facilities being grouped together to form a different “type” such as through cross subsidisation:

- **Type 1:** Non-directly revenue generating – such as refuse collection points<sup>9</sup>
- **Type 2:** Revenue generating but insufficient to cover ongoing operation, maintenance and management costs, such as virtually all museums
- **Type 3:** Revenue generating, sufficient to cover ongoing operation maintenance and management costs but coverage of capital costs is not yet determined, such as the Mega Performance Venue (MPV)

## 6.2 Private Sector Involvement Approaches for the WKCD

6.2.1 This Report has identified and assessed a range of approaches to private sector involvement – including risk bearing PPP approaches – and their application in Hong Kong and to arts and cultural projects internationally. Based on this assessment it is possible to suggest a series of general criteria for selecting alternative approaches to each of the three types of WKCD development above – see Box below. With reference to these criteria, potential private sector involvement mechanisms are proposed for each of the above category (types 1-3) – together with a brief outline of how such a mechanism might be applied to different types of cultural and communal development.

### ***Criteria for Selecting Private Sector Involvement Approaches***

- **Financial-** Is it likely that a partnership between government and the private sector will be able to carry out the project under financial terms which are acceptable?
- **Technical -** Is it reasonable to expect that a technical solution to the project can be found using private sector involvement mechanisms?
- **Operational -** Are there operational hurdles that prevent a PPP approach or other private sector involvement mechanism from being used?
- **Acceptability-** Will the public accept the involvement of the private sector in implementing the project?
- **Implementation -** Are there implementation barriers that prevent the use of a PPP approach or other private sector involvement mechanisms?
- **Timing -** Are there time constraints that would pre-empt consideration of private sector procurement?

### ***Type1: Non-directly Revenue Generating Development***

6.2.2 Non revenue generating development at the WKCD is expected to include most of the communal services and infrastructure services in the area. Communal facilities can be

<sup>8</sup> For example, museum operators are unlikely to have the experience, capacity or resources to undertake museum construction

<sup>9</sup> This assumes existing Government policies for “free at the point of delivery” for these services is adopted

packaged as one package of projects or as a number of individual projects. More specifically this category may include some of the following types of communal facilities being considered:

- Access roads
- Fire station
- Refuse collection points
- General, public realm, open space

### 6.2.3 Potential private sector involvement in Type 1 projects might include:

- **Service Contracts (Expenditure) / O&M** - paid for through budget expenditure. There are two potential means of applying this mechanism. As an outsourcing mechanism this approach is widely adopted for projects such as greening and security. However in practice many of these services are provided by Government departments such as roads, refuse collection points etc. and there is little reason to adopt a different approach for these services in WKCD
- **Design and Build** – paid for through budget expenditure and differs from standard procurement approach in that ASD would not be the designer. This is similar to the existing practice where ASD contracts out their design work to the private sector
- **Design Build and Maintain** - paid for through budget expenditure and may or may not be to ASD design. The difference is that the construction and maintenance are undertaken by the same party and thus creates an incentive for quality and long term maintenance consideration in construction. Government retains control of the management and operations and owns the asset
- **Design Build, Finance and Maintain** – it may be that there would be developer interest in also financing a type 1 development in return for payments over the life of the contract. Market sentiment for individual facilities would need to be tested. Government retains control of the management and operations and the asset is returned to Government at the end of the contract
- **Planning Gain** – the sale of a development land parcel with lease conditions to provide a facility. This is also a common practice at present. Most appropriate where the required facility is linked to a commercial development, e.g. residential and fire station, and retail and open space. Arrangements could include ownership, operation and maintenance of facilities or be returned to the contracting authority on completion. Paid for through reduction in land premium

### ***Type 2: Revenue Generating Development – Not expected to cover operating costs***

### 6.2.4 It is to be expected that, as in many other countries, most of the core arts and cultural facilities are unlikely to generate sufficient sales revenue to cover operating costs and will not be able to make any contribution to capital development costs. More specifically this category may include some of the following types of cultural and communal facilities being considered by the PATAG and MAG:

- Virtually all museums
- Exhibition Centre with a high proportion of cultural programming
- Concert Halls

- Theatres (may exclude those primarily used for long run musicals / dramas / Chinese operas, and small black box theatres)
- Piazzas
- Automated People Mover (APM) depending on expected patronage - to be determined

6.2.5 Potential private sector involvement in these Type 2 projects might include:

- **Service Contracts (Expenditure and Revenue) / O&M** - similar to Type 1 but it includes revenue contracts such as catering and retailing etc. Service contracts could also be adopted for the servicing, operation and maintenance of museums and theatres, but it is possible that not all of the costs of service provision would be subsidised but only a portion in order to motivate recovery of the remainder from user charges, donations, ticket prices etc and to be retained by the operator
- **Design and Build** – similar to Type 1. The contract would likely require the contractor to include potential operators/those with knowledge of operations in the design team for the cultural facilities. For the construction of signature buildings of the highest design standards it is possible that a contractor might also finance the construction (DBF) in order to benefit from the exercise of close control over the design and construction process
- **Design Build and Maintain** – as with Type 1
- **Design Build, Finance and Maintain** – as with Type 1
- **Planning Gain** – as with Type 1
- **Development Packaging** – a contract to build a facility with a contract clause providing for development rights in linked higher value commercial development to subsidise the viability of developing lower value facilities. May or may not also include operation. May or may not also require service payments

***Type 3: Revenue Generating Development – Expected to cover operating cost but not determined as to extent of coverage of capital costs***

6.2.6 Evidence has shown that some more commercial cultural facilities are capable of covering their operating costs but not servicing capital development debts. This category may also include revenue generating infrastructure. More specifically this category may include some of the following types of cultural and communal facilities being considered by the PATAG and MAG:

- Mega Performance Venue (MPV)
- Some theatres (may include those primarily used for long run musicals or dramas / Chinese operas, and small black box theatres)
- Exhibition Centre with a high proportion of commercial programming such as marketing exhibitions, product launches

6.2.7 All mechanisms are potentially possible, depending on commercial viability and policy towards financial incentives. Examples include:

- **Service Contracts (Expenditure and Revenue) / O&M** – similar to type 2. However, if the service is considered able to cover its operation and maintenance costs, without a service payment then the contract may simply include the rights to provide the service and collect and retain revenues

through ticket prices, admissions, private service functions, education services etc; the private operator can also obtain revenues from 3<sup>rd</sup> party sources including donations and sponsorships etc.

- **Lease, Operate and Maintain** – as above, service contracts could be adopted but it is possible that not all of the costs of service provision are subsidised but only a portion, with the remainder recovered from user charges, donations, ticket prices etc and retained by the operator. Most appropriate for some theatres that come reasonably close to covering their running costs
- **Design and Build** – as with Type 2
- **Design Build and Maintain** – as with Type 1 and 2
- **Design Build Operate** – with a facility that is able to meet its operating costs and potentially make some contribution towards capital costs, there is more likelihood of a private sector player existing in the market that may be interested in both the capital and operational aspects – such as for a major performance venue. However, under this option, the private sector would not be expected to finance the construction from its own sources
- **Design Build, Finance and Maintain** – as with Type 1 and 2
- **BOOT/DBFO/BOT and hybrids** – as with DBO except that under these options the operator is expected to finance the construction and would expect to earn a return over the period of the contract – or the period for which he has financed the cost depending on the terms of the contract. The private sector player therefore needs to have the resources to raise capital through borrowing, resources etc such as may be applicable to exhibition spaces; or at the other end of the spectrum, the capital cost needs to be low in comparison to operating costs – as for a small black box theatre for example - such that incorporation of construction of the facility into the overall contract does not prohibit operators from bidding for both aspects. Under this option the facility is returned to the public sector at the end of the contract. It may or may not require support through development rights or service payments as a subsidy in order to meet financial returns
- **BOO and hybrids** – as with above but under this type of contract the assets are not returned to the public sector. This is probably only applicable to a very few facilities such the EC and possibly the MPV. It may or may not require support through land /property development rights or capital injections at the outset in order to meet financial returns
- **Joint Venture** – this option involves the creation of a new company with joint ownership of assets and a sharing of returns. This is probably only applicable to a very few facilities such as the EC and possibly the MPV. It may or may not require support through land /property development rights or capital injections at the outset. Service payments as a subsidy are unlikely to be appropriate under this option
- **Planning Gain** – similar to type 2. If the lease requirement is for operations as well then the impact on the loss of land premium is likely to be less
- **Development Packaging** – as with type 2

### 6.3 An Area Development Approach for West Kowloon

#### *Area Development Approaches to Private Sector Involvement*

- 6.3.1 The analysis of international experience, and the case studies of three cultural district agencies in Australia, Spain and Canada set out in Chapter 5 has shown that the potential for all of these mechanisms of private sector involvement - including PPP options – would be increased by the establishment of a dedicated, area-based development and/or operating authority for the WKCD. The Government has already considered the creation of the proposed statutory authority. However it is clear that almost all of the above options for private sector involvement would be made more effective where the public sector partner – in this case, the future statutory body has a dedicated area-based role and can enter into development packaging, service, PPP and other agreements with developers and operators on behalf of the Government and other public partners.
- 6.3.2 To achieve this it is important to create a dedicated area-based agency with wide public sector and private sector representation and dedicated resources and powers to plan, develop and operate facilities and infrastructure in the area. The analysis of international experience has shown that area-based institutions are more effective in:
- Masterplanning the development of the area (within the government's statutory planning framework) in order to optimise the pattern of development packaging so as to secure the right financial, technical and cultural balance of arts, commercial and communal infrastructure development across the area as a whole
  - Development site and use parcelling and packaging of commercial, cultural and communal facilities in order to best manage the expenditures and revenues generated. A dedicated agency is best able to cross-subsidise development, subsidise and cross-subsidise facility operation through a range of “planning gain”, project packaging and risk sharing PPP agreements which will be an important part of the public / private funding strategy
  - Developing business propositions to be offered to the private sector, whilst ensuring the public interest is met, both financially and culturally. An agency with an area-based focus and dedicated purpose is best placed to create market interest and understand public and arts community interests and objectives. The agency should be responsible for identifying public sector development options for comparison with private sector alternatives and thereby setting the relevant public sector comparator (PSC)
  - Being the public party which enters into joint venture and other risk sharing PPP contracts on behalf of the public sector ensuring the public interest is maintained but at the “arm's length” from Government which may be required for both contractual and artistic purposes
  - Making use of public revenues from the leasing and development of sites, the operation of revenue generating facilities to allow effective **revolving** of funding within the area in support of the area's development – including non-revenue generating communal facilities – and operation of cultural facilities. This would minimize the need for seed monies and reduce the need for further public capital injections
  - Representing public sector involvement in the management structures of facilities. A dedicated area agency could be instrumental in establishing and participating in Foundations, Trusts, and other not-for profit organisations essential for the ownership and operation of many cultural facilities. This would facilitate the important process of getting the right type of arrangements for

individual cultural institutions in place first before development and operational decisions are taken

***Alternative Area Based Approaches for the Proposed Statutory Authority***

6.3.3 The analysis of international examples of area based cultural district agencies shows that different approaches have been adopted to key aspects of their statutory status, funding and organisation and powers – and, most importantly, to their differing roles in developing and/or operating cultural facilities and developing communal and commercial facilities. Although each of the area based agencies has delivered successful cultural districts their role in doing so, has varied. Thus:

- *The South Bank Corporation, Brisbane* has been responsible for the commercial and communal development of the South Bank Precinct on Brisbane waterfront and is an active area manager and cultural programmer but has had no role in the development or operation of the area's cultural facilities
- *Bilbao Ria 2000* has also been responsible for the commercial and communal development of the Abandoibarra area regeneration on Bilbao riverfront and has used revenues generated from this development to subsidise the development of cultural facilities and achieve planning gain - but has had no role in the operation of the area's cultural facilities or cultural programming
- *Harbourfront Centre, Toronto* by contrast is now responsible only for the operation of cultural facilities at the Harbourfront Centre district on Toronto waterfront and is an active area manager and cultural programmer. Responsibility for development of the cultural facilities using revenues generated from commercial development was with a preceding public corporation set up for that purpose only

6.3.4 Based on the scale and type of development and operational challenge faced at WKCD this experience suggests that **three alternative approaches** might be adopted by the proposed statutory authority and the strengths and weaknesses of each are summarised in Table 6.1 below:

- Development of cultural and commercial facilities – no operational responsibility
- Development of cultural and commercial facilities and operating responsibility for cultural facilities
- Development and operation of cultural facilities only

**Table 6.1 Strengths and Weaknesses of Area Based Agency Approaches**

Agency Approach	Strengths	Weaknesses
<b>1. Development of cultural and commercial facilities – no operational responsibility</b>	<p>Focus on comprehensive planning &amp; development skills</p> <p>Ability to cross subsidise between commercial and cultural developments – cross funding / packaging / planning gain</p> <p>Potential for overall development viability if operational losses are excluded</p> <p>Reduced seed and continuing public funding requirements</p> <p>Simplification of powers and responsibilities for development only</p>	<p>Limits range of PSI approaches to capital funding only</p> <p>Inability to cross subsidise operation of cultural facilities from development revenues</p> <p>Lack of participation in long term management and operation of a primarily cultural district</p> <p>Impacts on existing Government land grant and premium system for commercial development</p>
<b>2. Development of cultural and commercial facilities and operating responsibility for cultural facilities</b>	<p>Extends range of PSI approaches to combined capital and operational funding</p> <p>Ability to cross subsidise between commercial and cultural developments – cross funding / packaging / planning gain</p> <p>Ability to cross subsidise operation of cultural facilities from development revenues</p> <p>Participation in long term management and operation of a primarily cultural district</p> <p>Maximises prospect of long term sustainability of cultural facilities</p>	<p>Compromises agency focus on comprehensive planning &amp; development skills</p> <p>Compromises overall development viability if operational losses are included</p> <p>Increases need for seed and continuing public funding</p> <p>Extends range of powers and responsibilities required to both development and operation</p> <p>Impacts on existing Government land grant and premium system for commercial development</p>
<b>3. Development and operation of cultural facilities only</b>	<p>Simplification of powers and responsibilities for cultural sector only</p> <p>Limits impact on existing Government land grant and premium system for commercial development</p> <p>Participation in long term management and operation of a primarily cultural district</p>	<p>Maximises need for seed and continuing public funding</p> <p>Inability to cross subsidise operation of cultural facilities from commercial development revenues - no cross funding / packaging / planning gain</p> <p>Maximises overall development non-viability if all capital and operational losses of cultural facilities are borne by agency</p> <p>Inability to cross subsidise operation of cultural facilities from development revenues</p> <p>Limits range of PSI approaches to combined capital and operational funding of (non-viable) cultural facilities only</p>

- 6.3.5 Based on the analysis above it is recommended that the statutory body should be responsible for the development of both cultural and commercial facilities (and area communal facilities) and have a role in the subsequent operation of (some) cultural facilities – i.e. Option 2 above. However it would be preferable for the status and powers of the proposed statutory authority to be changed between the initial development and subsequent operational phases of its existence.

## **6.4 A Framework for Private Sector Involvement in the WKCD**

- 6.4.1 Based on the above recommendations for the use of private sector involvement – including a range of PPP approaches and other mechanisms – and on the creation and role of the proposed statutory authority as an area-based development and operation agency, it is possible to set out a broad framework of mechanism options and the appropriate role of the proposed statutory authority in delivering these for each broad type of facility – see Table 6.2.

**Table 6.2 Summary of Potential Private Sector Involvement**

<b>Development Type</b>	<b>Possible Mechanisms</b>	<b>Relevant Roles of the Proposed Statutory Authority</b>
<b>Type 1</b>  <b><i>Non-directly Revenue Generating Development</i></b>	Service/Operate and Maintain  Design and Build  Design Build Maintain/Design Build Finance Maintain  Planning Gain	The proposed statutory authority has responsibility for: <ul style="list-style-type: none"> <li>▪ Preparation of development briefs and contract management</li> <li>▪ Service contracting</li> <li>▪ Specification/negotiation of Planning Gain terms</li> </ul>
<b>Type 2</b>  <b><i>Revenue Generating Development</i></b>  <b><i>Not expected to cover operating costs</i></b>	Service/Operate and Maintain  Design and Build  Design Build Maintain/Design Build Finance Maintain, Planning Gain  Development Packaging	The proposed statutory authority has responsibility for: <ul style="list-style-type: none"> <li>▪ Development Packaging</li> <li>▪ Specification/negotiation of Planning Gain terms</li> <li>▪ Preparation of development briefs and contract management</li> <li>▪ Service contracting</li> </ul>
<b>Type 3</b>  <b><i>Revenue Generating Development</i></b>  <b><i>Cover Operating Cost</i></b>  <b><i>Not determined as to extent of coverage of capital costs</i></b>	Service/Operate and Maintain  Lease Operate and Maintain  Design and Build  Design Build Maintain/Design Build Finance Maintain, Design Build and Operate  BOOT/DBFO/BOT and hybrids  BOO and hybrids  Joint Venture  Planning Gain  Development Packaging	The proposed statutory authority has responsibility for: <ul style="list-style-type: none"> <li>▪ Development Packaging</li> <li>▪ Specification/negotiation of Planning Gain terms</li> <li>▪ Preparation of development briefs and contract management</li> <li>▪ Service contracting</li> <li>▪ Joint Venture</li> <li>▪ Developing business propositions / identifying and contracting PPP partners</li> </ul>

## 7 PRIVATE SECTOR INVOLVEMENT IN CACF AND COMMUNAL FACILITIES

### 7.1 Applying the Framework

7.1.1 The framework set out in the preceding chapter adopts three broad classes of facilities and communal services based on:

- The expected level of market financial viability of construction and operation
- The relationship between broad capital and operating cost – specifically the need for a satisfactory level of capital **and** operating viability to be achieved for whole-life approaches
- Existence of private sector players in the market with the right kind of experience and resources.

7.1.2 The framework clearly shows that the more commercially viable a facility/service is likely to be, the more appropriate it is for potential PPP approaches and the more likely it is that a workable solution combining market returns and public subsidy will be found to incentivise the private sector to become involved. It is used as a basis to examine and make recommendations on options and scenarios for individual CACF and communal facilities.

### 7.2 PSI in CACF and Communal Facilities

7.2.1 The framework is applied to the list of arts and cultural facilities as recommended by PATAG and MAG, and the IFP's requirements for communal facilities (see Attachment A). Making use of initial information available at this stage on each of the main groups of cultural and communal facilities proposed, Figure 7.1 presents the set of potential PSI options against facilities. Those coloured in red show potential "true" PPP options as defined in chapter 2. The figure also demonstrates the likely order of magnitude (indicated by the number of dollar signs) of costs and revenues associated with such facilities.

7.2.3 There are a limited range of options for many of the facilities. Of those that demonstrate more commercial viability, it is possible for them to also be procured in a traditional public procurement manner but preference will be for involvement of the private sector and the sharing of risk, consistent with Government policy.

7.2.4 It should be noted that where more than one facility of a type is planned it is not necessarily the case that the recommendations will be the same. Recommendations will depend on demand for the facility which if considered to be spread more thinly for example, the degree of financial viability for two such facilities may be different to that for one. It is also the case that development packaging may be possible for some facilities, particularly where there are synergies in developing the two together such as performing arts facilities and commercial development but there are limitations on the level of commercial development, and therefore the number of packages, that can be used to cross subsidise CACF and communal facilities.

**Figure 7.1: Potential Options for Private Sector Involvement in CACF and Communal Facilities**

PSI Capital Options														
PSI Operating Options														
CACF / Communal Facilities	Operating Profit / Deficit	Capital Costs	Planning Gain	Development Packaging	Build / D&B	DBM	DBO	DBFM	BOOT/ BOT / DBFO	BOO	JV / Alliance	Service Contracts	OMM	Lease
Mega Performance Venue	\$\$	\$\$\$\$		x	x	x	x	x	x	x	x	x	x	x
Great Theatres	\$	\$\$\$		x	x			x				x	x	x
Concert Halls	\$\$\$	\$\$\$		x	x	x		x				x	x	
Xiqu Centre	\$\$	\$\$\$		x	x	x	x	x				x	x	
Medium-sized Theatres	\$\$	\$\$	x	x	x			x				x	x	x
Blackbox Theatres	\$	\$	x	x	x	x	x	x				x	x	x
Piazzas	\$	\$	x	x	x	x						x	x	
M+	\$\$\$\$	\$\$\$\$		x	x	x						x		
Exhibition Centre	\$	\$\$		x	x	x	x	x	x	x	x	x	x	x
Automated People Mover	\$	\$\$	x	x	x	x	x	x	x	x	x	x	x	
Roads	\$	\$	x		x							x		
Public Open Spaces	\$	\$\$	x		x							x		
Other G/IC Facilities	\$	\$	x		x	x	x	x				x		

**Notes:**

- (iii) Options in red are “true” PPP options
- (iv) The list of arts and cultural facilities covers those as recommended by PATAG and MAG, and the IFP’s requirements for communal facilities

## **ATTACHMENT A – LIST OF CACF AND COMMUNITY FACILITIES**



## List of CACF and Communal Facilities

### Core Arts and Cultural Facilities

1. Mega Performance Venue
2. Great Theatre 1
3. Great Theatre 2 (Phase 2)
4. Concert Hall
5. Chamber Music Hall
6. Xiqu Centre
  - a. Theatre
  - b. Small Theatre
  - c. Xiqu Tea House Type Venue
7. Medium Sized Theatre 1
8. Medium Sized Theatre 2
9. Medium Sized Theatre 3 (Phase 2)
10. Medium Sized Theatre 4 (Phase 2)
11. Blackbox Theatre 1
12. Blackbox Theatre 2
13. Blackbox Theatre 3
14. Blackbox Theatre 4
15. Piazzas, including a small canopy
16. M+
17. Exhibition Centre

Performing arts  
facilities as  
recommended by  
PATAG

M+ and exhibition  
centre as  
recommended by  
MAG

### Infrastructure and Communal Facilities

1. Automated People Mover
2. Roads and Pedestrian Connections
3. Public Pier
4. Public Carparks
5. Public Open Space
6. Reprovisioning of Tsim Sha Tsui Fire Station Complex
7. Electrical Substation Structure
8. Police Post
9. Refuse Collection Point
10. Public Toilets
11. Decking Over Part of the Tunnel Portal of Western Harbour Crossing
12. Decking Over Kowloon South No.2 Salt Water Pumping Station
13. Utilities
14. Building Over and Around Existing Ventilation Buildings

These are primarily  
based on the IFP's  
requirement