Statement by SFST on Merger of MTR and KCR Systems
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Following is the English translation of the statement by the Secretary for Financial Services and the Treasury, Mr Frederick Ma, at the press conference today (April 11) on the Merger of MTR and KCR Systems:

Transaction structure

In deciding upon a means to effect the rail merger, our primary objective was, first, to realise the benefits of the rail merger for the community, which Dr Liao has touched upon, and, in delivering these, to balance the interests of the different stakeholders, including the people of Hong Kong who own the assets of KCRC, the passengers of the railways, the staff of the two corporations, and the shareholders of MTRCL.

In the light of these considerations, the Government and MTRCL have agreed that it would be most appropriate to effect the rail merger by means of a service concession arrangement.

Our recommendation is for KCRC to grant a service concession to MTRCL to operate the existing and new railway lines and other transport-related businesses of KCRC. After the rail merger, MTRCL will retain its listing status and the post-merger franchise will be expanded to include provision of the KCRC services.

During the term of the service concession, the post-merger corporation would be responsible for operating the two integrated railway networks. This would include undertaking and funding maintenance, improvement, and replacement of assets of the KCR system.

Our recommendation is for the service concession to have a term of 50 years, and it would be co-terminus with the franchise of the post-merger corporation.

Under the service concession arrangement, KCRC would retain the ownership of KCR system and its own financial obligations.

In other words, under the proposed rail merger, the Government is not disposing of the assets of the KCR system. Upon expiry or termination of the service concession, the post-merger corporation is obliged to deliver back to KCRC a railway system that meets the prevailing operating standards.

On this basis, the financial terms which we have agreed focus on the cashflow generating potential of the KCR system.

Financial terms

Under our current proposal, KCRC will receive from the post-merger corporation the following payments for the service concession -

* An upfront payment of $4.25 billion on the Appointed Day of the merger;

* Fixed annual payments of $0.75 billion; and

* Starting from the fourth year of the service concession, an annual share of the actual revenue generated from the KCR system based on a pre-agreed set of sharing ratios. The sharing ratios are -

- 10% for revenue exceeding $2.5 billion and up to $5 billion;

- 15% for revenue between $5 billion and $7.5 billion; and

- 35% for revenue beyond $7.5 billion.

This revenue-sharing arrangement will ensure that the public, which owns KCRC, will enjoy the upside when the revenue from the KCR system increases. At the same time, the post-merger corporation will be encouraged to operate the KCR system efficiently. At the moment, many parts of the KCR system are newly commissioned or under construction, and these parts will see an increase in patronage and revenue some time after they are commissioned and in operation. In that event KCRC will enjoy the upside under the revenue-sharing mechanism.

Property package

As an integral part of the package, we will sell property interests to MTRCL for $7.79 billion. These would include the property development rights, investment properties and property management business, but not include the land premium to be paid by the developers to the Government. In the course of the negotiation, we have made reference to the advice of our independent professional property valuer.

As the Government is both the sole shareholder of KCRC and the majority shareholder of MTRCL, the proposed service concession arrangement will be subject to the approval of the minority shareholders of MTRCL. We will not take part in the voting on this proposal.

I will now pass this briefing back to Dr Liao.

Ends/Tuesday, April 11, 2006