Private and confidential

Port Klang Authority

Position Review of
Port Klang Free Zone Project and Port Klang Free Zone Sdn Bhd

3 February 2009

PricewaterhouseCoopers

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Private & Confidential

Port Klang Authority
Jalan Pelabuhan
42005 Port Klang
Selangor Darul Ehsan

Attention: Chairman of Port Klang Authority
General Manager of Port Klang Authority

28 April 2009

Dear Sirs

Position Review of Port Klang Free Zone Project and Port Klang Free Zone Sdn Bhd

We refer to our letter dated 3 February 2009 enclosing our report on the Position Review of Port Klang Free Zone Project and Port Klang Free Zone Sdn Bhd and your letter dated 20 April 2009 confirming declassification of the JPPH letter (Reference JPPH:IP T(S)175/55/427-2/BO of 29 September 2000).

We are pleased to enclose our report dated 3 February 2009 incorporating the declassified information contained in the JPPH letter and information in the documents provided to us under your letters dated 13 April 2009 and 20 April 2009, as applicable.

Yours faithfully
PricewaterhouseCoopers Advisory Services Sdn Bhd

Lim San Peen
Senior Executive Director

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Port Klang Authority
Jalan Pelabuhan
42005 Port Klang
Selangor Darul Ehsan

Attention: YBhg Dato' Lee Hwa Beng, Chairman
Mr Lim Thean Shiang, General Manager

3 February 2009

Dear Sirs

Position Review of Port Klang Free Zone Project and Port Klang Free Zone Sdn Bhd

We refer to our letter of engagement dated 8 October 2008.

We are pleased to enclose our report on the position review of Port Klang Free Zone Project and Port Klang Free Zone Sdn Bhd. Kindly note that certain parts of our report may be subject to the Official Secrets Act 1972 and thus have been removed pending declassification by the relevant authorities.

We will be pleased to provide any clarification that you may require.

Yours faithfully
PricewaterhouseCoopers Advisory Services Sdn Bhd

Lim San Peen
Senior Executive Director

Table of Contents

Important Notice

This report is confidential to Port Klang Authority (PKA).

The report is not intended for general circulation or publication. It must not be reproduced, republished, copied, distributed, excerpted, disclosed, quoted, alluded or referred to, whether in whole or in part, to any other party in any way without prior written consent of PricewaterhouseCoopers Advisory Services Sdn Bhd (PwCAS). No other party may rely on the report for any purpose. To the extent that any other party gains access (with or without our consent) and chooses to rely on the report, then such other party does so entirely at its own risk. PwCAS does not and shall not accept any responsibility to such other party.

The report is limited in scope. It is restricted to a position review of Port Klang Free Zone and Port Klang Free Zone Sdn Bhd as set out in our Letter of Engagement dated 8 October 2008. We were not asked to and we have not advised on any strategy, valuation, legal implications, tax, operational effectiveness, staff competencies or process improvement. No investigation to detect any wrongdoing or audit to form an opinion on any financial information, including any forecasts and projections, has been undertaken. The completeness and accuracy of information contained in this report, including but not limited to financial information, forecasts and projections, is the responsibility of PKA and PwCAS shall expressly disclaim any liability to any party arising therefrom.

The report has been discussed with PKA management.

Section 1
Terms of Reference

Section 1 Terms of Reference

1.1 PricewaterhouseCoopers Advisory Services Sdn Bhd (PwCAS) was appointed by Port Klang Authority (PKA) to conduct a position review of the Port Klang Free Zone (PKFZ or the Project) and Port Klang Free Zone Sdn Bhd (PKFZSB) under the terms of a letter of engagement (the LoE) dated 8 October 2008. The LoE was accepted by PKA on 14 October 2008.

1.2 Under the LoE, our scope of work is limited to the following areas:

- Review of authority to enter into agreements pertaining to the Project, including acceptance of any variation and cost escalation covering the years 2002 to 2007;
- Review of financial implications of agreements;
- Review of current status of the Project;
- Review of PKA's ability to pay Kuala Dimensi Sdn Bhd (KDSB) and/or the Ministry of Finance (MOF); and
- Review of financial position of PKFZSB.

Key work steps undertaken for each of these areas are detailed in **Appendix 1**.

1.3 Information contained in this report has been gathered from a number of sources. The principal sources were the records (books, minutes, agreements, reports, memorandums, correspondences, calculations, plans, drawings, notices of payments, accounts, certificates, financial statements, forecasts and projections, valuations, print-outs) and the officers and directors, past and present, of PKA and PKFZSB. Some of these records were kept in the office of the Malaysian Anti-Corruption Commission (formerly the Anti-Corruption Agency). Other sources of information include the turnkey developer, KDSB; the quantity surveyors, QS4 Consortium (QS4); Jabatan Penilaian dan Perkhidmatan Harta, Kementerian Kewangan (JPPH); advocates and solicitors, Rashid Asari & Co; and the reports of the Auditor General. The Hansard (transcripts of Parliamentary debates) was another source of information, as was the officers of the Ministry of Transport (MOT). We were not required to and did not approach Jebel Ali Free Zone International (JAFZI) for information.

Appendix 2 lists out the records we have reviewed and the meetings we have conducted in the course of our work.

1.4 Where possible, we have cross checked the information contained in this report with other information that was provided to us. At the date of the report, we have yet to receive certain information requested. These are listed in **Appendix 3**.

Note: PricewaterhouseCoopers Taxation Services Sdn Bhd had served as tax agents of PKA from its corporatisation in 1990 to May 2006. In addition, our predecessor firm Price Waterhouse had served as previous auditors of Wijaya Baru Sdn Bhd and Wijaya Baru Holdings Sdn Bhd for the financial year ended 31 December 1996. We do not consider these roles as having an impact on our independence.

Section 2
Executive Summary

Chronology of key events

Conceptualisation phase

The Project was part of a strategic plan to transform Port Klang into a national load centre and regional transshipment hub. The project was modelled after the Jebel Ali free zone in Dubai.

See paragraphs 2.3 to 2.4

Execution phase

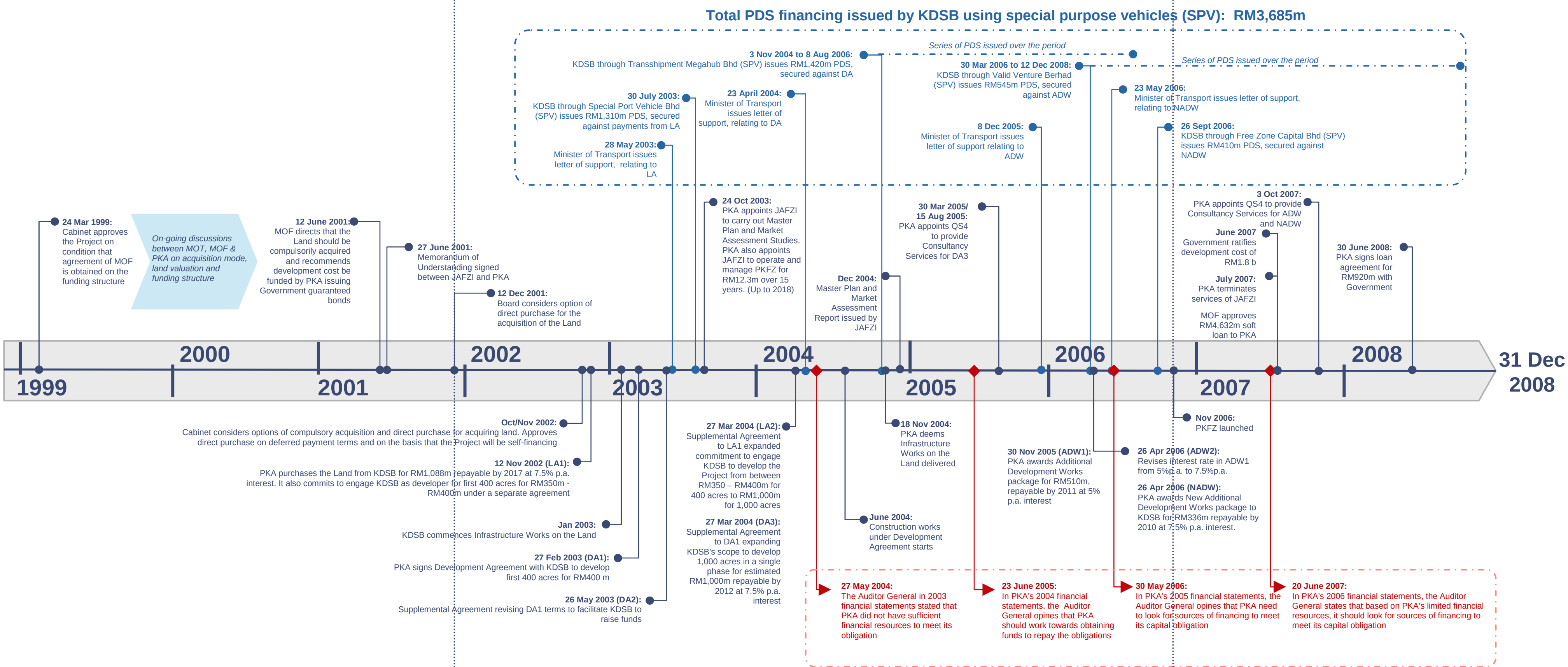
Cost escalations, weak governance and weak project management have severely undermined both the viability of the Port Klang Free Zone and the ability of PKA to meet its financial obligations to MOF. See paragraphs 2.5 to 2.18

Operational phase

Three key areas need immediate attention:

- All outstanding project-related issues to be satisfactorily resolved.
- The MOF soft loan need to be restructured to avoid a potential default in 2012
- A concerted effort needs to be undertaken to turn the Port Klang Free Zone into a financially viable venture.

See paragraph 2.19.



Section 2 Executive Summary

2.1 This section summarises the key issues and our conclusions resulting from the position review. Details of the key issues warranting the attention of the Board are set out in Section 4 of this report.

Main conclusion

2.2 The strategic intent of the Project was to transform Port Klang into a national load centre and regional transshipment hub. However, significant project costs, weak governance and weak project management have severely undermined the viability of the Project. It is imperative that PKA takes immediate actions to restructure the MOF soft loan of RM4.632 billion to avoid a potential default in 2012. The Government of Malaysia (the Government) would need to make a concerted effort to turn the Port Klang Free Zone into a viable venture.

The strategic intent of the Project

2.3 In 1993, the Government decided to transform Port Klang into a national load centre as well as a regional transshipment hub. Several strategies were outlined in the Seventh Malaysia Plan (1996-2000) leading to the creation of the Port Klang Free Zone.

2.4 The Project was modelled after the Jebel Ali Free Zone in Dubai. The Jebel Ali Free Zone was set up in 1985 and grew rapidly in the 1990s. Today, the Jebel Ali Free Zone spans an area of more than 12,000 acres. It has almost 6,000 tenants employing over 130,000 employees.

The Malaysian Cabinet approved the Project in March 1999. A chronology of key events that followed is shown on the opposite page.

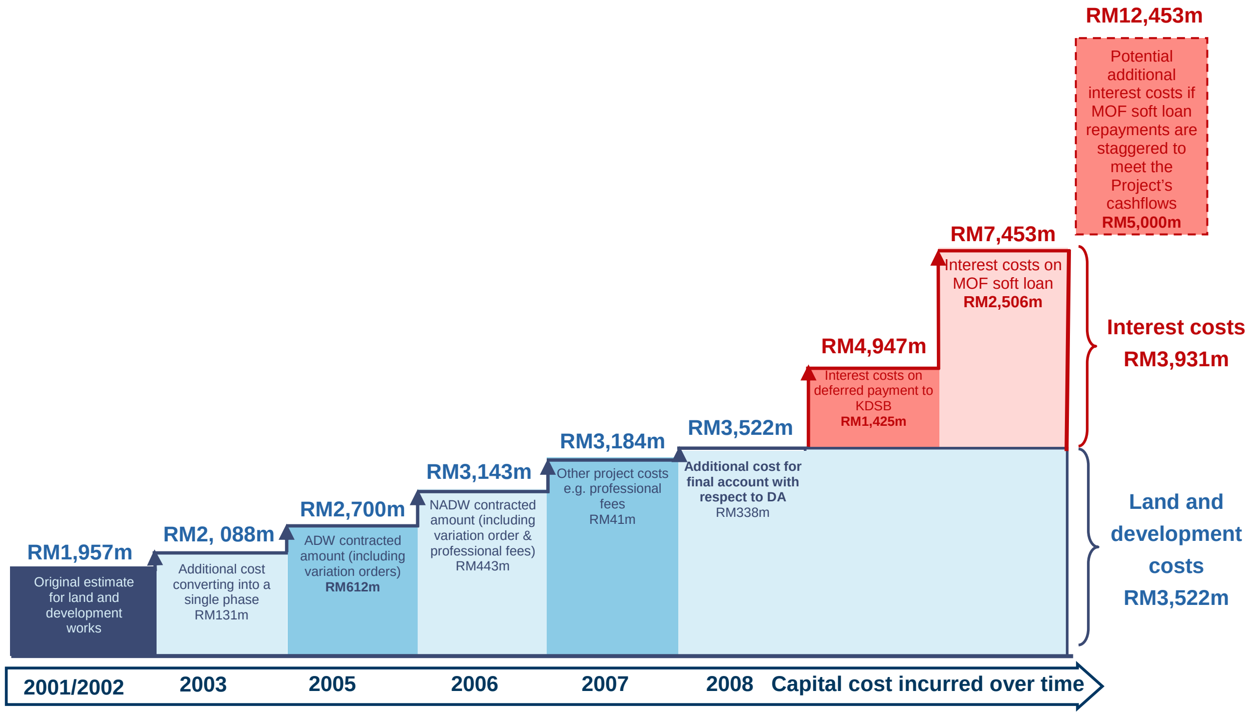
Project outlay has escalated from RM1.957 billion to RM3.522 billion, excluding interest cost. Including interest cost, the Project outlay increases to RM7.453 billion

2.5 PKA entered into several agreements with KDSB to purchase the Land and develop the Project on a turnkey basis. The original estimated cost for the land purchase and development works in 2001 was RM1.957 billion. As shown in the chart on the next page, Project outlay has escalated to RM3.522 billion as at 31 December 2008. Interest cost of the deferred payments to KDSB amounted to RM1.425 billion resulting in a total Project outlay of RM4.947 billion.

2.6 PKA was unable to fund its obligations to KDSB from its own resources when the first scheduled payment was due in 2007. PKA secured a 20-year soft loan of RM4.632 billion from MOF, of which RM4.382 billion is available for draw down. This loan would impose an additional interest cost of RM2.506 billion resulting in a total Project outlay of RM7.453 billion.

PKA must restructure the MOF soft loan to avoid a potential default in 2012

2.7 Cashflow projections prepared by PKA management show that PKA would be in a cumulative cash deficit position between 2012 and 2041, after paying two instalments to MOF. Should PKA fail to meet the MOF soft loan instalments as scheduled and if these instalments are deferred to match its projected cashflows, it would incur additional interest cost of approximately RM5 billion. This would further increase the outlay of the Project to RM12.453 billion.



PKA may not have received value for money due to its heavy reliance on KDSB as turnkey developer

2.8 It cannot be ascertained with any degree of certainty whether PKA has received value for money for the amount spent on developing the Project. PKA's approach to the Project was that, this being a turnkey development, the onus was on KDSB to deliver the completed works to PKA, with minimal supervision. Furthermore, it relied heavily on its quantity surveyors, QS4, to verify cost estimates based on completed designs submitted by KDSB.

PKA could have better managed the Project by, inter alia, appointing a qualified supervising officer; ensuring the JAFZI/TSG Masterplan and detailed building / infrastructure specifications were available before commencing works; undertaking open tenders for award of development contracts; and using its own quantity surveyors (QS4) more effectively.

Potential savings on financing cost

2.9 MOT / PKA could have benefitted from lower cost of funding had they issued government-guaranteed bonds to finance the Project. For example, PKA could have issued bonds at 4.27% as enjoyed by Syarikat Prasarana Nasional Berhad (SPNB) to purchase the Land outright at RM21 psf (cash basis) instead of RM25 psf (deferred payment basis). As such, the total estimated outlay for the Land could have been RM1.276 billion compared to RM1.808 billion i.e. a potential savings of RM0.532 billion.

In addition, PKA could have achieved further savings in financing costs had it developed the LIU over eight years as recommended in the JAFZI/TSG Masterplan, instead of over two years.

The Land was acquired at special value

2.10 The Land was purchased by PKA at a price of RM25 psf on the basis that the Land was of special value (as referred to in paragraph 4.33).

2.11 According to the Hansard, there were differing views on the mode of acquisition of the Land, namely compulsory acquisition as against outright purchase. The Hansard mentioned that the Cabinet had deliberated on the differing views and decided that, in the best interest of the country and to avoid any complication, the Land be purchased outright.

JPPH had in August 2001 placed a value of RM10.16 psf on the basis of compulsory acquisition with land partly reclaimed and no infrastructure works. Compulsory acquisition, had it been possible, would have cost a total of RM442 million compared to the purchase price of RM1,088 million (that is RM25 psf including Infrastructure Works with land fully reclaimed).

Weak governance

2.12 The proposal to purchase the Land was approved by the Cabinet. However, subsequent development proposals were not tabled to the Cabinet for approval prior to the execution of the DA, ADW and NADW even though the total development costs under the DA, ADW and NADW of RM1.846 billion (excluding interest) exceeded the cost of the Land of RM1.088 billion (excluding interest). We have been informed by PKA that the Government ratified development costs of RM1.8 billion on 27 June 2007. This sum combined with the cost of the Land (RM1,088m), additional amount agreed in the final acccount of the DA (RM216m), VO for ADW and NADW (RM169m) and professional fees paid to KDSB and other consultants (RM203m) adds up to a total project outlay of RM3,522m (excluding interest).

2.13 PKA/MOT also failed to alert the Cabinet in a timely manner about PKA's inability to pay for the Project out of its own funds. In May 2004, PKA was aware that it was not able to meet the Cabinet's condition on self-financing. PKA should have alerted the Cabinet of this important fact. To compound the issue, PKA entered into other very significant development agreements thereafter.

2.14 There was a general lack of Board oversight and governance over the Project. Several matters indicated that the Board had limited involvement in implementing the Project:

- Key agreements were not submitted to the Board for approval. The agreements were signed under Common Seal without prior authorisation;
- Variation Orders (VOs) totalling RM 62.5 million have been accepted to-date by PKA management, without reference to the Board;
- Appointment of key project consultants were made by PKA management without the prior approval of the Board; and
- The Board was not consulted on acceptance of the Land without KDSB completing the Infrastructure Works and how price adjustment was to be effected.

2.15 Several Government checks and balances were bypassed. For example:

- The agreements were not vetted by the Attorney General despite the significant amounts involved and PKA's lack of experience in projects of this nature;
- Treasury guidelines on vetting of agreements by the Attorney General and approval of VOs by MOF were not adhered to;
- Letters of support, which could be construed as guarantees, were issued by the Minister of Transport without MOF approval; and

- PKA did not adhere to MOF's stipulation to issue government guaranteed bonds for the development of the Project.

2.16 As an important statutory body, the Board of PKA is expected to demonstrate good corporate governance. In the words of the Auditor General, a statutory body is set up to implement government policies through programmes and activities in a professional and effective manner.

Any failure to be seen to operate with exemplary corporate governance, for example, in the way the Board exercises its oversight of the Project including managing any potential conflicts of interest, can damage the reputation of not only PKA but also the Government.

2.17 We should also mention PKA's apparent reliance on approvals by senior government offices such as the Cabinet, Ministry of Transport and Prime Minister. Whilst such approvals are important, the Board still retains the overall responsibility to run PKA in a professional and sustainable manner. This would include the responsibility to not enter into agreements which may threaten PKA's long term financial viability.

Weak project management

2.18 The Project was poorly executed with several lapses in project management. Key amongst them were:

- Contracts were entered into on the basis of estimated amounts and without detailed building plans. The development agreement DA3 was entered into based on an estimated amount of RM1 billion and without detailed plans. Therefore, PKA did not have the benefit of a fixed sum contract or detailed specifications of what the turnkey development would entail.

- The development contracts totalling RM1.846 billion were all awarded to KDSB without competitive bids.

- The entire Project was completed in two years, contrary to the JAFZI/TSG Masterplan which recommended a mixed development strategy – a single phase for infrastructure works and multiple phases over eight years for the Light Industrial Units (LIU) (which represented 42% of total construction cost of RM1 billion under the JAFZI/TSG Masterplan). As at 31 December 2008, only 77 units out of a total of 512 units of the LIU are rented.

- The QS4 quantity surveyor consortium was only appointed nine months after construction works commenced. Thus, PKA did not have the benefit of the advice of its own quantity surveyor from the beginning of construction works.

The way forward

2.19 Moving forward, there are three areas which merit the Board's immediate attention:

(i) Governance and project management

PKA should strengthen its Board oversight and governance over significant projects of this nature.

In addition, PKA should take immediate steps to address the issues arising from the Land purchase and the development agreements with KDSB. These issues would include:

- the non deduction for value of Infrastructure Works not done under LA1 and other potential adjustments;
- the potential interest overcharge of between RM51 million to RM309 million in connection with the purchase of the Land. KDSB may have wrongly compounded its interest from PKA using

a half-yearly compounding method instead of a “simple” (i.e. non-compounded) annual basis;

- adjustment to the final account of DA3 for value of work (and associated interest charge) not carried out on three infrastructure components as stated in the Land purchase agreement. These charges had already been included in the purchase price of the Land.

- delay in issuance of Certificate of Fitness (CF), and outstanding defect rectification works.

PKA should ensure that outstanding construction works are completed to its expectations and that the final accounts of DA, ADW and NADW are reflective of work done.

(ii) Financing structure

PKA must restructure the MOF soft loan to avoid a potential default in 2012. Some of the restructuring options that it may wish to consider could involve a combination of loan rescheduling, government grant and privatisation.

(iii) Making the Port Klang Free Zone viable

The Project’s actual occupancy of 14% is low and is not generating sufficient revenue to cover its operating expenses.

The Project faces many commercial challenges to achieving viability, including:

- Marketing
- Current economic climate
- Domestic and regional competition
- A multi-agency approval environment

The Government will need to undertake a concerted effort involving a number of agencies in order to turn the Port Klang Free Zone into a financially viable venture.

Section 3
Project Overview and Status

Section 3 Project Overview and Status

(A) General

3.1 The Project was undertaken by PKA, a statutory body under the Port Authorities Act 1963. The core functions of PKA are as follows:

- port planning and development
- regulatory oversight of privatised facilities
- trade facilitation
- asset management
- free zone authority.

The members of the Board of PKA for 2001 to 2007 are set out below.

Table 1: Board members of PKA

Name of board member		2001/ 2002	2002/ 2003	2003/ 2004	2004/ 2005	2005/ 2006	2006/ 2007
1)	Dato' Dr. Ting Chew Peh – Pengerusi	X	X	X*			
2)	Abdul Rahman Bin Mohd. Noor – Wakil Ketua Setiausaha, Kementerian Pengangkutan	X	X	X*			
3)	Datin Paduka O.C Phang – Pengurus Besar	X	X	X	X	X	X
4)	Zubir Bin Abdul Aziz – Wakil Ketua Pengarah, Unit Perancang Ekonomi, Jab. Perdana Menteri	X	X	X	X*		
5)	Dato' Mohd. Sinon Bin Mudzakir – Wakil Setiausaha, Kerajaan Negeri Selangor	X					
6)	Mohd. Bashir Bin Maskijo – Wakil Kesatuan Sekerja Pel. Klang	X*					
7)	Tan Sri G. Gnanalingam	X	X	X	X	X	
8)	Dato' Abd. Rahman Bin Palil	X	X	X*			
9)	Mohammad Bin Ismail – Wakil Ketua Setiausaha, Perbendaharaan Malaysia (diganti oleh En. Abdul Rahim Bin. Mokti)	X*					
10)	Choong Tow Chong	X	X	X*			
11)	Abdul Rahim Bin. Mokti – Wakil Ketua Setiausaha, Perbendaharaan Malaysia	X*	X	X	X	X*	
12)	Dato' Dr. Abdul Munip Bin Kasmin – Wakil Setiausaha, Kerajaan Negeri Selangor		X	X	X	X*	
13)	Ahmat Bin Abu – Wakil Kesatuan Sekerja Pel. Klang	X*	X	X	X	X	X
14)	Dato' Yap Pian Hon – Pengerusi			X*	X	X	X*
15)	Chandrasekaran D – Wakil Ketua Setiausaha, Kementerian Pengangkutan (diganti olehY.B. Dato' Muhd. Safaruddin Bin Muhd. Sidek)			X*	X*		
16)	Dato' Haji Ahmad Bhari Bin Abd. Rahman			X*	X	X	X
17)	Loh Chew June			X*	X	X	
18)	Dato' Muhd. Safaruddin Bin Muhd. Sidek – Wakil Ketua Setiausaha, Kementerian Pengangkutan				X*	X	X*
19)	V. Ravindran – Wakil Ketua Setiausaha, Perbendaharaan Malaysia					X*	X*
20)	Nor Rizan Bin Mohd. Thani – Wakil Ketua Pengarah, Unit Perancang Ekonomi, Jab. Perdana Menteri				X*	X	X*
21)	Shamsul Azri Bin Abu Bakar – Wakil Setiausaha Kerajaan Negeri Selangor (diganti oleh Y.Bhg. Dato' Noordin Bin Sulaiman)						X*
22)	Tan Boon San @ Tan Hock Guan						X
23)	Dato' Chor Chee Heung – Pengerusi						X*
24)	Dato' Haji Zakaria Bin Haji Bahari – Ketua Setiausaha, Kementerian Pengangkutan						X*
25)	Mohamad Nor Bin Taib – Wakil Ketua Pengarah, Unit Perancang Ekonomi, Jab. Perdana Menteri						X*
26)	Noordin Bin Sulaiman – Wakil Setiausaha, Kerajaan Negeri Selangor						X*
27)	K. Tarmalingam						X
28)	Mohd Zainuddin Bin Ahmad Rashidi, Wakil Ketua Setiausaha - Perbendaharaan						X

** appointed / replaced during the year*

3.2 The Project is an integrated 1,000-acre free commercial and industrial zone offering facilities for international cargo distribution and which acts as a consolidation centre. It is situated next to Westport of Port Klang in Pulau Indah, and is accessible by the Kesas Highway. Another access route is planned via the South Klang Valley Expressway. The map below shows its current and future access routes.

3.3 The Project is modelled after Dubai's Jebel Ali Free Zone and has been gazetted as a free zone incorporating both manufacturing and commercial activities. The zone is developed with the view of promoting entreport trade and export-oriented manufacturing industries. In addition, it has been planned to attract regional distribution and international procurement centres.

3.4 The Project is a mixed development comprising several components as follows:

- **Prepared/Open land** - open plots of various sizes complete with basic infrastructure for long-term lease of 10-30 years with option to extend

- **Commercial centre (4 blocks of leased office building)** - office space, showroom, retail outlets, training centre for short/long-term lease

- **Light industrial units (512 units)** - suitable for light-manufacturing, trading and logistics activities for short/long-term lease

- **Exhibition and trade centre -** for exhibitions and international trade fairs

- **Business class hotel (135 rooms)** - suitable for business accommodation

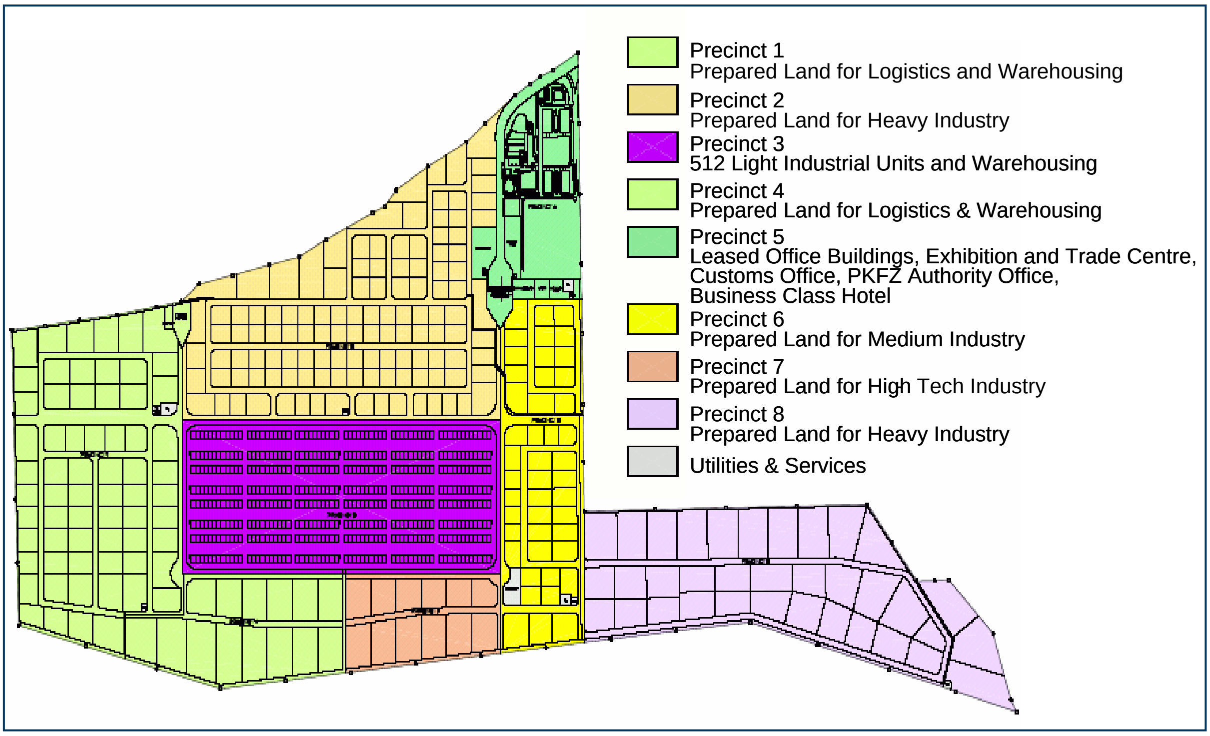
- **PKFZ Authority office**

3.5 The development is zoned into eight precincts. A summary of the precincts and facilities are in the table below:

Table 2: Summary of precincts and facilities

Precinct	Facilities	Area	
		Acres	Square feet
Precinct 1 & Precinct 4	Prepared Land for Logistics and Warehousing		
Precinct 2 & Precinct 8	Prepared Land for Heavy Industry (Manufacturing)	788	34,325,280
Precinct 6	Prepared Land for Medium Industry (Automotive & Others)		
Precinct 7	Prepared Land for High Tech Industry		
Precinct 3	512 Light Industrial Units and Warehousing	165	7,187,400
Precinct 5	Leased Office Buildings (LOB), Business Class Hotel, Exhibition and Trade Centre, Customs Office, PKFZ Authority office	47	2,047,320
TOTAL		**1,000**	**43,560,000**

The layout of the eight precincts is shown below:



3.6 The total lettable area is 31,187,744 square feet of which 14% or 4,460,021 square feet is currently tenanted. These tenancies have an annual rental of RM14 million. A further RM32 million in rental income is expected from expand-options given to tenants and from bookings and enquiries received from interested parties. Details are in the table below:

Table 3: Lettable area and tenancies

	LIU	LOB	Open Land	Total
Available lettable area (sf)	2,809,344	500,000	27,878,400	31,187,744
(A) Confirmed tenants				
(i) area occupied (sf)	423,871	93,579	3,942,571	4,460,021
(ii) area occupied (%)	15%	19%	14%	14%
(iii) annual rental revenue (RM'000)	6,091	1,158	6,771	14,020
(B) Potential tenants				
(i) area to be occupied (sf)	504,804	35,686	12,975,227	13,515,717
(ii) area to be occupied (%)	18%	7%	47%	43%
(iii) annual rental revenue (RM'000)	8,247	572	23,030	31,849

(B) Development of the Project

3.7 PKA appointed KDSB as the turnkey developer to design, construct and finance the Project. KDSB was also the former owner of the land on which the Project is developed.

3.8 KDSB was incorporated on 22 April 1994 with share capital as follows:

Authorised share capital	:	RM50 million comprising 50 million ordinary shares of RM1.00 each
Issued and paid up capital	:	RM30 million comprising 30 million ordinary shares of RM1.00 each.

3.9 According to its audited financial statements for FYE 2007, the principal activities of KDSB are construction and property development. KDSB is a wholly-owned subsidiary of Wijaya Baru Holdings Sdn Bhd (WBHSB). WBHSB and its group of companies are involved in land and sea reclamation, construction, dredging, property development and marine transport activities.

3.10 As at 16 January 2009, the shareholders and directors of WBHSB are as follows:

Table 4: Shareholders and directors of WBHSB

Name of Shareholders / Directors	Shareholding	Appointment date
Dato' Seri Tiong King Sing	70%	20 March 1995
Idris Bin Mat Jani	10%	20 March 1995
Omar Bin Abdul Latip	20%	20 March 1995

Source: Companies Commission Malaysia search dated 16 January 2009

3.11 The directors of KDSB as at 11 September 2008 were as follows:

Table 5: Directors of KDSB

Name of Directors	Appointment date
Dato' Seri Tiong King Sing	21 July 1994
Idris Bin Mat Jani	16 August 1994
Omar Bin Abdul Latip	21 July 1994
Dato' Seri Abdul Azim Bin Mohd Zabidi	18 July 2003

Source: Companies Commission Malaysia search dated 11 September 2008

3.12 KDSB issued four sets of private debt securities (PDS) to finance the development of the Project. These PDS were secured against repayments from the various agreements entered into between KDSB and PKA. The PDS were issued under four special purpose vehicles as follows:

Table 6: Summary of PDS issued by KDSB

Special purpose vehicle	Amount raised (Bonds/MTN/ CP) RM million	Date/Period of issue	Secured against repayments from these agreements*
Special Port Vehicle Berhad	1,310	30 July 2003	LA
Transshipment Megahub Berhad	1,420	3 November 2004 to 8 August 2006	DA
Valid Ventures Berhad	545	30 March 2006 to 12 December 2008	ADW
Free Zone Capital Berhad	410	26 September 2006	NADW
Total	**3,685**		

** Please refer to Table 8 for more details*

Note: *MTN: Medium Term Notes; CP: Commercial Papers*

(C) Administration of the Project

3.13 The day to day administration of the Project is carried out by a wholly owned subsidiary of PKA, PKFZSB. PKFZSB is the administrator of PKFZ under a Service and Operation Agreement dated 8 September 2005. This agreement is for 88 years until 2093.

3.14 The scope of services provided by PKFZSB is as follows:

(i) to deal with land matters in PKFZ in relation to leasing, sub-leasing and renting land and facilities in PKFZ, including:

- to solicit clients, negotiate, enter and execute lease/rental agreements;
- to enforce terms and conditions of the lease/rental agreements;
- to obtain consent to lease from the authority; and
- to arrange prompt payment for all outgoings related to the land due to the authority.

(ii) to administer PKFZ including to co-operate, communicate and to work with JAFZI in implementing and enforcing rules and regulations.

3.15 In October 2003, PKA entered into a Management Agreement with JAFZI to operate and manage PKFZ. This agreement was mutually terminated in July 2007.

3.16 PKFZSB employs 25 people. Current and past members of its Board of Directors are set out in **Appendix 4.**

Section 4
Matters for the Attention of the Board

Section 4 Matters for the Attention of the Board

4.1 In accordance with our scope of work set out in Section 1, we have identified a number of issues warranting the attention of the Board. These issues are summarised in the table below:

Table 7: Summary of issues

Summary			Paragraph
(A)	**Authority to Enter into the Agreements**		
	Issue 1:	The proposal to purchase the Land was approved by the Cabinet. However, subsequent development proposals were not tabled to the Cabinet for approval	4.5
	Issue 2 :	PKA failed to alert the Cabinet in a timely manner of its inability to finance the Project from its internal funds	4.8
	Issue 3:	The Board did not exercise oversight and adequate governance over the implementation of the Project	4.10
	Issue 4:	Advice of the Attorney General was not sought and certain MOF regulations were not complied with	4.17
	Issue 5 :	There could be potential conflicts of interest arising from the involvement of parties who had prior association with either the Land or KDSB	4.19
(B)	**Financial Implications of the Agreements**		
	Issue 6 :	Interest on the MOF soft loan will increase the Project outlay from RM4.947 billion to RM7.453 billion. Unless the MOF soft loan is restructured, total outlay for the Project will increase to RM12.453 billion	4.24
	Issue 7 :	PKA could have reduced its funding costs had it complied with MOF's recommendation to issue government-guaranteed bonds and developed the Project in phases	4.28
	Issue 8 :	The Land was acquired at special value which exceeded market value	4.33
	Issue 9 :	KDSB may have overcharged PKA for interest by between RM51 million and RM309 million in connection with the purchase of the Land	4.41
	Issue 10:	DA3 was not a 'fixed sum' contract and did not stipulate a rate for professional fees claimable by KDSB	4.42
	Issue 11 :	PKA incurred claims of RM95.256 million for general preliminaries cost not expressly specified in the DA	4.46
	Issue 12 :	The final account for DA3 did not include any deduction for value of work not done on three infrastructure components in the Land purchase agreement	4.51
(C)	**Project Management and Status**		
	Issue 13:	The RM1 billion development contract was awarded to KDSB before a project masterplan was finalised	4.57
	Issue 14:	PKA may not have received value for money due to its heavy reliance on KDSB as the turnkey developer	4.61
	Issue 15:	Project management and control over the Project was weak	4.63

Summary		Paragraph
Issue 16:	Project status as at 31 December 2008 - only the LIU have been issued with CF; defect liability period has expired and certain defects remain to be rectified	4.64
(D)	**Ability to Meet Financial Obligations**	
Issue 17:	PKA has projected that it will be in a cumulative cash deficit position in 2012 and will not be able to repay the MOF soft loan instalments from that time on	4.74
Issue 18 :	Letters of support issued by MOT could be construed as a guarantee that PKA would meet its obligations on a full and timely basis	4.78
Issue 19:	The Project's actual occupancy of 14% is low and it is not generating sufficient revenue to cover its operating expenses	4.81
(E)	**Financial Position of PKFZSB**	
Issue 20:	PKFZSB has incurred losses since its incorporation and has negative shareholder's funds as at 30 September 2008	4.87

The above mentioned issues are discussed in the paragraphs that follow.

(A) Authority to Enter into the Agreements

4.2 PKA has entered into the following key agreements in relation to the Project:

Table 8: Key agreements entered into by PKA in relation to the Project

Agreement	Date of agreement	Description	Signed under common seal and authenticated by
LA1	12 Nov 2002	This agreement with KDSB was for the purchase of the Land and the Infrastructure Works to be carried out by KDSB for RM1.088 billion. In addition, PKA committed to engage KDSB as developer for the first 400 acres for RM350 to RM400 million under a separate agreement. On a deferred payment basis, RM1.808 billion is payable over 15 years. The first two years are interest free and the interest on the remaining 13 years is calculated at 7.5% p.a. Repayments commence from 2007 to 2017. The Land including the Infrastructure Works has been deemed delivered to PKA on 18 Nov 2004.	General Manager and Chairman
DA1	27 Feb 2003	This agreement appointed KDSB as turnkey developer for 400 acres of the Project at RM400 million on deferred payment basis. Total of RM585 million including interest payable in yearly instalments over 9 years (up to 2012) at 7% p.a. subject to repayment-free period for first two years. The terms of this agreement have since been varied by DA2 and DA3.	General Manager and Manager (General Services)
DA2	26 May 2003	This supplemental agreement revised the terms of DA1 to facilitate KDSB to raise funds.	General Manager and Manager (General Services)
JAFZI Consultancy Agreement	24 Oct 2003	This agreement appointed JAFZI to carry out master plan and market assessment studies at a fee of USD0.21 million. JAFZI has since submitted a report under the title “Master Plan and Market Assessment Study” in December 2004.	General Manager and Chairman
JAFZI Management Agreement	24 Oct 2003	This agreement appointed JAFZI to operate and manage PKFZ for 15 years (up to 2018) for total fee of USD12.3 million. This agreement has since been terminated in 2007.	General Manager and Chairman
DA3	27 Mar 2004	This supplemental agreement to DA1 expanded the scope of work of KDSB as turnkey developer of the Project from 400 acres to 1000 acres for RM1billion on deferred payment basis. Total of RM1.303 billion including interest is payable over	General Manager and Chairman

Agreement	Date of agreement	Description	Signed under common seal and authenticated by
		8 years (up to 2012) at 7.5% p.a. interest subject to repayment-free period for first 2 years. Development has since been completed and final cost agreed at RM1.216 billion. Estimated total amount including interest and professional fees is RM1.85 billion.	
LA2	27 Mar 2004	This supplemental agreement to LA1 expanded the commitment to engage KDSB to develop the Project from RM350 million to RM400 million (for 400 acres) to RM1 billion (for 1,000 acres).	General Manager and Chairman
LA PMU	2 Nov 2004	This agreement was for the purchase of a parcel of land measuring 9.37 acres for PMU and water tank for RM5.395 million from CSSB.	General Manager and Manager (General Services)
QS4 Agreement 1	15 Aug 2005	This agreement appointed QS4 to provide consulting services for DA3 for RM4.31 million.	General Manager and Manager (General Services)
ADW1	30 Nov 2005	This supplemental agreement to DA1 appointed KDSB to design, construct, finance and complete additional development works on turnkey basis for RM510.38 million involving junction improvement, business class hotel and electrical infrastructure on a deferred payment basis. Total of RM726.49 million including interest, is payable over 5 years commencing July 2007 (up to 2011) at 5% p.a.	General Manager and Manager (General Services)
ADW 2	26 Apr 2006	This supplemental agreement to ADW1 revised interest rate from 5% p.a. to 7.5% p.a.	General Manager and Assistant General Manager (Administration)
NADW	26 Apr 2006	This supplementary agreement to DA1 appointed KDSB to design, construct, finance and complete new additional development works on turnkey basis for RM335.8 million involving concrete trenching, electrical works for precincts 2 and 8, civil and infrastructure works to PMU, direct access road and link road to Westport Container Terminal 4 on a deferred payment basis. Total of RM522.58 million including interest, is payable over 3 years commencing July 2008 (up to 2010) at 7.5% p.a.	General Manager and Assistant General Manager (Administration)
QS4 Agreement 2	3 Oct 2007	This agreement appointed QS4 to provide consultancy services for ADW and NADW for RM5.04 million.	General Manager and Assistant General Manager (Administration)

4.3 As a result of PKA's inability to meet the first scheduled payment due to KDSB on 30 June 2007, PKA entered into an agreement with the Government for a soft loan of RM4.632 billion. PKA drew down the first tranche of RM0.92 billion on the same day. This was the first of four tranches. The soft loan is repayable over 20 years from each drawdown date, commencing from the fourth year onwards. The soft loan carries interest of 4% p.a.

Copies of the agreements mentioned are enclosed as **Appendix 5**.

4.4 From our review of the agreements and other documents made available to us, we have identified the following issues regarding limits of authority and the way in which the Project was managed and governed by the Board and management of PKA.

Issue 1 The proposal to purchase the Land was approved by the Cabinet. However, subsequent development proposals were not tabled to the Cabinet for approval

4.5 In 2002, following the endorsement by the Board for PKA to purchase the Land from KDSB for RM1.088 billion, the proposal was tabled to the Cabinet by MOT. The Cabinet approved the proposal, on condition that PKA was able to finance the purchase from its own funds, including from future returns of the Project. The condition imposed by the Cabinet is contained in a letter from MOT to PKA dated 20 November 2002, a copy of which is enclosed as **Appendix 6**.

4.6 PKA purchased the Land and subsequently entered into several significant development agreements with KDSB as follows:

(i) February 2003: PKA entered into a development agreement (DA1) to develop the first 400 acres of the Land for RM400 million

(ii) March 2004: PKA entered into a supplemental agreement (DA3) to vary DA1 for the purpose of developing the entire 1,000 acres for an estimated RM1 billion

(iii) November 2005: PKA entered into an additional development works agreement (ADW) involving junction improvement, a business class hotel and electrical infrastructure for RM510.38 million

(iv) April 2006: PKA entered into a new additional development works agreement (NADW) involving concrete trenching, electrical works for precincts 2 and 8, civil and infrastructure works to the PMU, direct access road and link road to Westport Container Terminal 4 for RM335.8 million

The contracts under (ii), (iii) and (iv) above were awarded to KDSB after the Prime Minister had agreed to recommendations from the Minister of Transport. We have been informed by PKA that the Government ratified development costs of RM1.8 billion on 27 June 2007.

4.7 We are of the view that MOT/PKA should have tabled their Land development plans to the Cabinet for the following reasons:

(i) Prior approval of the Cabinet had been obtained for the purchase of the Land, as mentioned in paragraph 4.5, and therefore subsequent proposals to develop the Land should also be tabled to the Cabinet; and

(ii) The total value of the development agreements in paragraph 4.6 of RM1.846 billion (excluding interest), is more than the Land purchase price of RM1 billion, and thus would warrant deliberation by the Cabinet.

Issue 2 PKA failed to alert the Cabinet in a timely manner of its inability to finance the Project from its internal funds

4.8 As mentioned in paragraph 4.5, the Cabinet had approved the proposal on the condition that PKA would be able to finance the purchase from its own funds, including returns from the Project. However, in his audit report on PKA for the FYE 31 December 2003, the Auditor General stated that PKA did not have sufficient funds to finance the Project. Excerpts from the audit report are reproduced below.

> *"A review for the year 2001 to 2003, showed that the Authority (PKA) does not have sufficient financial resources to meet this obligation. The Authority (PKA) income before tax was between RM0.50 million and RM21.19 million whilst income after tax was between a deficit of RM1.52 million to a surplus of RM16.31 million."*
>
> *"The Authority (PKA) needs to look for sources of financing to meet the capital obligation of RM2.90 billion from the year 2007 to 2017".*

Source: Certificate of the Auditor General on the Financial Statements of Port Klang Authority for the Year Ended 31 December 2003 dated 27 May 2004

4.9 Hence, PKA was aware in 2004 that it was not able to meet the Cabinet's condition on self-financing. PKA should have alerted the Cabinet of this important fact. To compound the issue, PKA entered into other very significant development agreements thereafter.

Issue 3 The Board did not exercise oversight and adequate governance over the implementation of the Project

4.10 With the exception of (i) the initial proposal to develop the Project in two phases and (ii) the proposal to appoint JAFZI to undertake masterplan/market assessment studies and provide management services, key matters were not tabled to the Board for approval.

4.11 For example, no approval of the Board was sought in the following instances:

(i) when the Common Seal of PKA was affixed to all the agreements mentioned in Table 8;

(ii) when delivery of the Land was accepted without KDSB completing the Infrastructure Works specified in LA1;

(iii) when RM45 million was set as the benchmark for deeming the incomplete Infrastructure Works (specified in LA1) as completed by KDSB for the purpose of delivery of the Land;

(iv) when variation orders under ADW and NADW totalling RM62.6 million to date were accepted;

(v) when Rashid Asari & Co were appointed legal advisers; and

(vi) when PKA management appealed for Perunding BE Sdn Bhd to be appointed as the sole quantity surveyor for the Project, despite MOF's instruction to appoint a consortium of four quantity surveyors.

4.12 In addition, all the agreements mentioned in Table 8 were not submitted to the Board for prior approval. Therefore, PKA management did not have the benefit of the views of the Board on various terms contained in the agreements. This conflicts with good corporate governance.

4.13 The implementation of the Project was led by the General Manager and the Steering Committee. The General Manager provided progress reports to the Board as and when Board meetings were convened.

4.14 The Steering Committee was set up in December 2002. Members of the Steering Committee appointed by the General Manager at inception are set out in **Appendix 7**.

4.15 The Steering Committee was not established by a resolution of the Board nor was it subject to supervision by the Board (although it provided periodic progress updates to the Board). The General Manager and the Steering Committee did not have formal terms of reference nor did they have specified limits of authority. The General Manager had only an operational authority limit of RM50,000. We have not noted any evidence that the Board gave authority to the General Manager or the Steering Committee to implement the Project. Therefore, roles, responsibilities and accountability were not defined.

4.16 We would also mention PKA's apparent reliance on approvals by senior government offices such as the Cabinet, MOT and Prime Minister. Whilst such approvals are important from a corporate governance standpoint, it would appear to us that the Board still retains the overall responsibility to run PKA in a professional and sustainable manner. This would include the responsibility not to enter into agreements which PKA cannot afford, or which may threaten its long term financial viability. This is a wide issue and it may benefit corporate governance in the statutory body sector in the country if all statutory body Board members were made aware of their duties and responsibilities when faced with approvals from senior government offices.

Issue 4 Advice of the Attorney General was not sought and certain MOF regulations were not complied with

4.17 The views of the Attorney General were not sought before the agreements mentioned in Table 8 were entered into. In his "Laporan Ketua Audit Negara Mengenai Badan Berkanun Bagi Tahun 2006", the Auditor General reported that:

(i) given the scale of the Project, advice from the Attorney General Office should have been obtained to safeguard the interests of PKA and the Government.

(ii) several key matters had been omitted from the agreements entered into with KDSB:

- defect liability in the LA; and
- performance bond in the DA, ADW and NADW.

(iii) the commitment made in the LA1 to appoint KDSB as contractor for the development of the Project did not comply with financial regulations and was made without approval of the MOF.

(iv) VOs were not contracted according to the provisions of Arahan Perbendaharaan 202, which stipulates that a statutory body is only able to approve VOs up to 20% of the contract sum or RM4 million, whichever is lower. Any higher amount must be approved by the MOF.

4.18 PKA management did not seek the views of the Attorney General in accordance with Arahan Perbendaharaan 204 but instead relied on the advice of Rashid Asari & Co for all the contracts entered into with KDSB. Rashid Asari & Co is a firm comprising two partners and 12 legal assistants as of November 2002.

Issue 5 There could be potential conflicts of interest arising from the involvement of parties who had prior association with either the Land or KDSB

4.19 We noted a number of parties with prior association to either the Land or KDSB which may give rise to potential conflicts of interest:

Dato' Abdul Rahman Palil

Dato' Abdul Rahman Palil was a member of the Board from 1997 to 2003.

At one Board meeting, Dato' Abdul Rahman Palil declared his position as the President of KPPLB and queried a proposal for compulsory acquisition of the Land over direct purchase. KPPLB was the original owner of part of the Land.

Given that compulsory acquisition would have benefitted PKA, the rationale for Dato' Abdul Rahman Palil raising the query is unclear.

Dato' Chor Chee Heung

Dato' Chor Chee Heung was non-executive Deputy Chairman of Wijaya Baru Global Berhad (WBGB) from April 2004 to July 2007, and Chairman of PKA from April 2007 to March 2008.

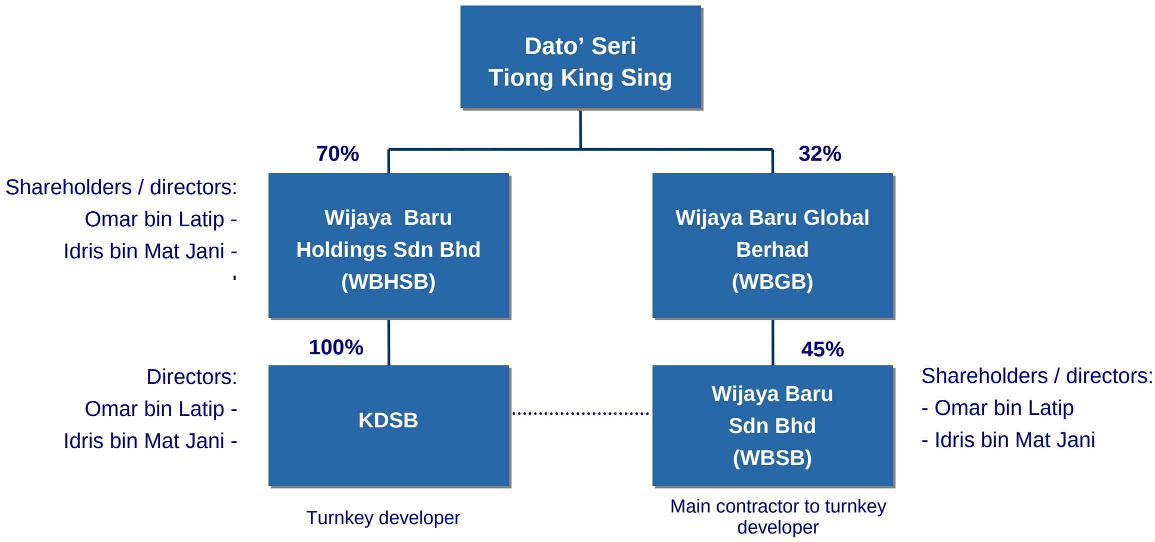
In February 2008, the final account for the DA3 of RM1.216 billion was approved by the Board. KDSB carried out the construction works under the DA3 during the period from July 2004 to November 2006, during which time Dato' Chor Chee Heung was the non-executive Deputy Chairman of WBGB.

Minutes of the Board did not indicate that Dato' Chor Chee Heung either declared his previous involvement in WBGB to the Board or withdrew himself from the deliberations.

WBGB and KDSB are related through a common shareholder and director. WBGB and the parent company of KDSB, Wijaya Baru Holdings Sdn Bhd (WBHSB), share a common shareholder and director, Dato' Seri Tiong King Sing.

In addition, two directors of KDSB, Omar bin Latip and Idris bin Mat Jani, are also shareholders and directors of Wijaya Baru Sdn Bhd (WBSB). WBSB is a 45% associate of WBGB and is the main contractor of KDSB for this Project.

A diagram showing the relationships of the parties referred to above is set out below.



Perunding BE Sdn Bhd

Perunding BE Sdn Bhd is a member of QS4, the consortium of quantity surveyors appointed by PKA to, among others things, assess the final cost for the Project. Perunding BE Sdn Bhd had acted as the quantity surveyor for KDSB in relation to the Infrastructure Works under LA1.

Given its prior involvement as KDSB's quantity surveyor, Perunding BE Sdn Bhd may have put itself in a position of conflict of interest when it was appointed as a member of QS4.

Rashid Asari & Co

Rashid Asari & Co acted as legal adviser for PKA in all the agreements mentioned in Table 8 except for LA PMU and QS4 Agreement 1 and 2. Prior to its involvement with the agreements, Rashid Asari & Co had acted in the sale and purchase of part of the Land between Koperasi Pembangunan Pulau Lumut Berhad (KPPLB) and KDSB in 1995. Good practice would require this earlier involvement to be declared to the PKA Board prior to the firm's appointment as PKA's legal advisers.

Whilst PKA does not have a written policy of using only members of its legal panel, we noted that Rashid Asari & Co was not on the panel of legal advisers of PKA at the time of their appointment.

(B) Financial Implications of the Agreements

4.20 This section deals with the financial implications of the agreements mentioned in Table 8.

4.21 As at 31 December 2008, the contracted outlay (including interest) of the Project is estimated to be RM4.947 billion. A summary is set out in the table below:

Table 9: Project outlay as at 31 December 2008 (RM million)

	Land	Development			Total
	LA	DA	ADW	NADW	
Land & development costs	1,088	1,216	510	336	3,150
Variation orders			102	67	169
Professional fees		122		40	162
Contracted costs to KDSB	**1,088**	**1,338**	**612**	**443**	**3,481**
CSSB					17
QS4					10
JAFZI					7
Rashid Asari & Co					4
Others (plan fees)					3
Contracted costs to others					**41***
Total contracted costs as at 31 December 2008	**1,088**	**1,338***	**612**	**443**	**3,522**
Interest cost on deferred payments to KDSB	720	512	114	79	1,425
Total Project Outlay	**1,808***	**1,850**	**726**	**522**	**4,947**

Note: The ADW and NADW contract sums of RM726 million and RM522 million shown respectively in the table assume VOs of 20% and professional fees of 10% (for NADW only) as provided in the two agreements.

** This represents costs which have been finalised with KDSB and other parties.*

4.22 Of the total outlay of RM4.947 billion, RM3.187 billion or about 64% are final costs - Land cost RM1.808 billion; DA cost RM1.338 billion; and other contracted costs RM41 million. All other costs are pending finalisation.

4.23 In addition, the RM4.947 billion total outlay excludes potential adjustments which may increase or reduce the final total outlay of the Project. At this juncture, PKA management is not able to determine the quantum of the potential adjustments, details of which are set out in **Appendix 8**.

Issue 6 Interest on the MOF soft loan will increase the Project outlay from RM4.947 billion to RM7.453 billion. Unless the MOF soft loan is restructured, total outlay for the Project will increase to RM12.453 billion

4.24 PKA management has estimated total payments due to KDSB to be RM4.841 billion. As at 31 December 2008, PKA has paid a total of RM1.378 billion leaving an outstanding balance of RM3.463 billion. The RM1.378 billion is funded by a combination of PKA's own funds (RM0.458 billion) and draw down of RM0.920 billion from the MOF approved soft loan of RM4.632 billion. The approved amount of RM4.632 billion has since been revised to RM4.382 billion as PKA has paid KDSB RM250 million from its own funds in 2007.

4.25 The MOF soft loan is repayable with interest over 20 years from the date of drawdown. Interest at 4% p.a over this 20-year period is estimated to be RM2.506 billion if the soft loan is drawn down as and when repayments to KDSB fall due. The total amount repayable to MOF by the end of the repayment period is expected to be RM6.888 billion:

	RM billion
Total loan to be drawn down (principal amount)	4.382
Interest on loan	2.506
Total amount repayable to MOF	6.888

The letters from MOF dated 25 July 2007 and 29 January 2008 approving the soft loan are enclosed as **Appendix 9**.

4.26 The RM2.506 billion soft loan interest will increase total outlay of the Project to RM7.453 billion, as follows:

	RM billion
Outlay related to land and development	3.522
Interest on deferred payments to KDSB	1.425
Total Project outlay	4.947
Interest on the MOF soft loan	2.506
	7.453

4.27 The Project outlay of RM7.453 billion has not taken into account potential additional interest which would arise if PKA cannot meet the instalments on MOF soft loan as scheduled. Potential additional interest cost could amount to RM5 billion if the loan repayments to MOF are deferred to match PKA's projected cashflows. If this were to happen, the Project outlay would increase from RM7.453 billion to RM12.453 billion.

Issue 7 PKA could have reduced its funding costs had it complied with MOF's recommendation to issue government-guaranteed bonds and developed the Project in phases

4.28 In a letter dated 12 June 2001, MOF stipulated the following financing structure for MOT/PKA to implement the Project:

(i) the Land to be compulsorily acquired and paid for by MOT from its allocation;

(ii) the Land to be leased to PKA for development at a rate to be determined; and

(iii) the cost of development could be funded by government guaranteed bonds to be issued by PKA, subject to certain conditions including the award of development contracts by open tender.

A copy of the letter from MOF to MOT dated 12 June 2001 is set out in **Appendix 10**.

4.29 MOT/PKA did not implement this financing structure. Hence, had PKA issued government guaranteed bonds to finance the development cost, these bonds could have been issued at rates reflective of their government-guaranteed status. As an indication, Syarikat Prasarana Negara Berhad (SPNB), a company owned by MOF Inc., issued 8-year and 13-year bonds in 2003 at coupon rates of 3.80% and 4.27%, respectively. PKA could have benefitted from this lower cost of funding compared to the 7.5% p.a. interest charged under the terms of the LA, DA, ADW and NADW.

4.30 PKA is charged interest at 7.5% p.a. on deferred payments under the Land purchase and development agreements. Due to the length of the repayment periods, moratorium and interest-free periods built into the repayment schedules of the aforementioned agreements, the effective interest rate is lower than 7.5%. In the case of the LA and the DA which has been finalised, the effective interest rates for the LA and DA are 5.83% and 7.3% respectively which are significantly higher than government-guaranteed bond rates.

4.31 MOT/PKA could have further benefitted from lower cost of funding had they issued bonds for the purchase of the Land. For example, PKA could issue bonds at 4.27% as enjoyed by SPNB to purchase the Land outright at RM21 psf instead of RM25 psf per JPPH's valuations (as shown in Table 10 below). As such, the total estimated outlay for the Land could have been RM1.276 billion compared with RM1.808 billion i.e. a potential savings of RM0.532 billion.

4.32 In addition, PKA could have achieved further savings in financing costs had it developed the LIU over eight years as recommended in the JAFZI/TSG Masterplan.

Issue 8 The Land was acquired at special value which exceeded market value

4.33 The Land was purchased at a price of RM25 psf on the basis that the Land was of "special value" to PKA and because PKA would enjoy deferred payment terms.

4.34 In arriving at the special value, JPPH considered that:

(i) KDSB was reluctant to sell the Land;

(ii) MOT/PKA required the Land for future development; and

(iii) there was no other suitable land adjacent to Westport

4.35 Standard 2 of the Malaysian Valuation Standards states that, "Special Value is the term relating to an extraordinary element of value over and above Market Value (as defined in the Malaysian Valuation Standards)…It is an increment of value that could be applicable to a particular owner or user, or prospective owner or user, of the property rather than to the market at large; that is, Special Value is applicable only to a purchaser with special interest."

A copy of the letter from JPPH to the MOT dated 29 September 2000 setting out the special value valuation is enclosed as **Appendix 11** and a copy of Malaysian Valuation Standards - Standard 2 is enclosed as **Appendix 12**.

4.36 Before this, JPPH had valued the Land in November 1998 and May 2000 at the market value of RM17 per square feet (psf) and RM18 psf, respectively.

4.37 In September 2000, JPPH assessed the Land at a special value of RM21 psf on cash basis after taking into account the Infrastructure Works to be undertaken by KDSB as listed in **Appendix 13**.

4.38 In addition, JPPH was of the view that a higher price could be considered if payment terms were deferred. JPPH placed a special value of RM25 psf, assuming the following deferred payment terms:

- Deposit in first year of 5%
- Coupon rate of 6.5%
- Interest waiver for 1st and 2nd years
- Interest repayment only in 3rd and 4th years
- Annual repayments inclusive interest for 6 years and repayment period of 10 years.

4.39 The table below summarises JPPH's valuations in relation to the Land:

Table 10: Summary valuations by JPPH

Date	Details of transaction/valuation	Acres	Total RM mil	RM psf
Nov 1998	Valuation: – on basis of reclaimed land but with no access road and infrastructure – on basis of reclaimed land with access road and infrastructure Land status - development and approved for industrial and commercial use.	 400 400	 235 296	 13.50 17.00
May 2000	Updated valuation on market value basis of reclaimed land with access road and basic infrastructure. Land status - development and approved for industrial and commercial use.	830	651	18.00
Sep 2000	Valuation on special value basis including certain additional basic infrastructure to be undertaken as listed in **Appendix 13** – assumption of cash payment . – RM25.00 per sq ft with the assumption of deferred payment terms of 10 years Land status – industrial	 830 830	 760 904	 21.00 25.00
Aug 2001	Valuation on open market value for compulsory acquisition purposes. Land is partly reclaimed but no infrastructure. Land status – industrial	1,000	442	10.16

4.40 According to the Hansard, there were two view points expressed on the mode of acquisition of the Land, namely (i) that the Land could be compulsorily acquired according to the Attorney General and MOF and (ii) that compulsory acquisition was not suitable according to the Selangor State Government. It is further mentioned in the Hansard that:

(i) compulsory acquisition was not possible because:

(a) PKFZ is not a public interest project; and

(b) the Land had been issued with a development order in 1995; and

(ii) the Cabinet had deliberated on the differing views and decided that, in the best interest of the country and to avoid complications, the Land be purchased outright.

JPPH had placed a value of RM10.16 psf on the basis of compulsory acquisition with land partly reclaimed and no infrastructure works. Compulsory acquisition, had it been possible, would have cost a total of RM442 million compared to the purchase price of RM1,088 million (that is RM25 psf including Infrastructure Works with land fully reclaimed).

Issue 9 KDSB may have overcharged PKA for interest by between RM51 million and RM309 million in connection with the purchase of the Land

4.41 Interest on the LA1 is chargeable at the rate of 7.5% p.a. calculated on a yearly basis on the 'Balance Consideration Price' or such part thereof remaining due. Balance Consideration Price is defined in the LA1 as "*the sum of Ringgit Malaysia Nine Hundred Seventy Nine Million Six Hundred Ten Thousand and Four Hundred (RM979,610,400-00) only*." We understand, therefore, that interest is to be calculated each year on the remaining portion of the Balance Consideration Price without compounding.

Based on a set of computations provided to PKA by KDSB, the interest has been compounded on a 6-monthly basis instead of non-compounded yearly basis. In addition, the agreement does not specify whether the yearly repayment should be applied against principal or interest. Depending on whether the yearly repayment is applied against interest or principal, interest has been potentially overcharged by between RM51 million and RM309 million.

KDSB disagrees with this interpretation of the interest computation in LA1. We have informed PKA management to refer the matter for legal advice.

Issue 10 DA3 was not a 'fixed sum' contract and did not stipulate a rate for professional fees claimable by KDSB

4.42 The DA3, which did not contain detailed specifications and scope of work required of KDSB, was not a 'fixed sum' contract. The development cost in DA3 is described as follows:

> *Development Cost - "Means the proposed cost properly and reasonably incurred, paid or reimbursed by KDSB for the Development estimated about Ringgit Malaysia One Billion (RM 1,000,000,000.00) only excluding the Professional Fee, the Variation Order (if any) and the Interest Charged subject to the final costing to be prepared by KDSB and agreed by PKA and subject further to the needs and requirement of the Development upon the terms and conditions herein mention."*

4.43 The final amount that was eventually agreed for DA3 in respect of Builder's Works and Preliminaries was RM1.216 billion, which is 21% higher than the original estimate of RM1 billion.

4.44 In addition, KDSB claimed professional fees of RM121.592 million calculated as a single 10% of the final amount of RM1.216 billion. The professional fee of 10% was not stipulated in DA3 and thus could have been a subject of negotiation between PKA and KDSB. As a minimum, PKA should have asked for a breakdown of professional fees claimed.

4.45 The open-ended nature of DA3 has increased the final development cost by 33%, from the original estimated sum of RM1 billion to RM1.337 billion.

Issue 11 PKA incurred claims of RM95.256 million for general preliminaries cost not expressly specified in the DA

4.46 PKA approved a final cost of RM1.216 billion (excluding professional fees of RM121.592 million) for the DA3, compared with RM1.269 billion claimed by KDSB and RM1.118 billion assessed by QS4. Details are shown in the table below:

Table 11: Comparison of final cost (RM'000)

	Claim by KDSB	QS4 assessment	Final amount approved
Builder's Works	1,120,659	1,054,977	1,120,659
Preliminaries	148,665	63,298	95,256
Total development cost	**1,269,324**	**1,118,275**	**1,215,915**

4.47 The final cost approved of RM1.216 billion (excluding professional fees of RM121.592 million) is 8.7 % above the assessment by QS4 and 21% above the original estimated contract sum of RM1 billion. This 21% increase is partly attributable to Preliminaries which had not been specified in the DA.

4.48 In the absence of a detailed breakdown of KDSB's claim for Preliminaries, QS4 allocated 6% or RM63.299 million of Builder's Works as Preliminaries, which it deemed broadly consistent with industry practice. KDSB subsequently submitted a revised claim for Preliminaries at 11%.

4.49 On 5 February 2008, the Board approved the final account of RM1.216 billion (excluding professional fees of RM121.592 million) which included Preliminaries of RM95.256 million, a sum equivalent to 8.5% of Builder's Works. The latter amount is RM32million higher than the amount of RM63.298 million assessed by QS4. It appears that the final account approved by the Board was based on the following:

- Builder's Works as claimed by KDSB (RM1.120 billion as compared with RM1.054 billion assessed by QS4)

- Preliminaries of RM95.256 million based on the average of KDSB's revised claim of 11% and QS4's assessment of 6%.

4.50 Under normal practice, Preliminaries are awarded as a percentage of the cost of Builder's Works and expressly written into development agreements. In this case, the Preliminaries claimed were not expressly provided in the DA and therefore the Board had to arbitrate in respect of this claim by KDSB.

Issue 12 The final account for DA3 did not include any deduction for value of work not done on three infrastructure components in the Land purchase agreement

4.51 KDSB commenced work on the Infrastructure Works in January 2003. Under the terms of the LA, the Land with completed Infrastructure Works was to be delivered to PKA within 24 months from commencement. However, certain components of the Infrastructure Works were not completed when the Land was delivered to PKA:

(i) monsoon drain system
(ii) water supply system
(iii) two bridges.

4.52 The monsoon drain and water supply systems could not be completed because of changes in specifications that necessitated more time and cost. The bridges were no longer required after reclamation works and they were replaced by two box culverts. With PKA management's agreement, the monsoon drain system and water supply system with the revised specifications were included as part of the works under the DA.

4.53 On 3 November 2004, PKA management agreed to deem the construction of Infrastructure Works under the LA as 100% completed when the value of work done on the components based on revised specifications exceeded RM45 million. A copy of the letter dated 3 November 2004 from PKA to KDSB on this matter is enclosed in **Appendix 14**.

4.54 Delivery of the Land to PKA was considered effective from 18 November 2004 upon confirmation by KDSB's quantity surveyor, Perunding BE Sdn Bhd, that works on the revised specification had exceeded RM45 million. A copy of KDSB's letter dated 25 November 2004 to PKA stating the effective date for Delivery of the Land is enclosed in **Appendix 15**.

4.55 We draw attention to the following matters:

- the basis for adopting RM45 million as the point at which construction of the Infrastructure Works could be deemed completed is unclear;
- KDSB did not reduce the Land purchase price to take account of the value of work not done on the three components which would have the effect of reducing PKA's interest cost in respect of the LA. Instead, PKA agreed to KDSB's request to make that deduction out of the contract sum of DA3 – the basis for PKA agreeing with KDSB's request is not clear; and
- No deduction for the value of Infrastructure Works not done under the LA was made in the final account of DA3 submitted by KDSB.

We have raised this omission with the new management of PKA which has in turn sought clarification from KDSB. At the date of this report, PKA has not received a response from KDSB.

(C) Project Management and Status

4.56 This section describes issues in project management together with the status of the Project as at 31 December 2008.

Issue 13 The RM1 billion development contract was awarded to KDSB before a project masterplan was finalised

4.57 The JAFZI/TSG Masterplan which addressed, among other things, market demand, development approach and financial projections, was finalised in December 2004. In essence, the JAFZI/TSG Masterplan recommended a mixed development strategy – a single phase for infrastructure works and multiple phases over eight years for the LIU. This staggered development for the LIU was recommended for cashflow considerations and to match expected future demand.

4.58 However, PKA had earlier entered into a single phase RM1 billion development contract with KDSB on 27 March 2004, nine months before the JAFZI/TSG Masterplan was finalised. By December 2004, KDSB had already completed six months of construction works.

4.59 The entire Project including the LIU was completed within 24 months, resulting in excess LIU capacity. As at 31 December 2008, occupancy rate of the LIU was only 15%. We understand that this single phase development was adopted based on an earlier letter dated 8 November 2003 from JAFZI. A copy of this letter is enclosed in **Appendix 16**.

4.60 Significant financing cost could have been avoided had PKA adhered to the JAFZI/TSG Masterplan and its recommendation for phased development. In addition, sound project management would suggest the Project should commence after the finalisation of the JAFZI/TSG Masterplan and not before.

Issue 14 PKA may not have received value for money due to its heavy reliance on KDSB as the turnkey developer

4.61 It cannot be ascertained with any degree of certainty whether PKA has received value for money for the amount spent on developing the Project on a turnkey basis. PKA's approach to the Project was that, this being a turnkey development, the onus was on KDSB to deliver the completed works to PKA, with minimal supervision. Instead, PKA relied heavily on its quantity surveyors, QS4, to verify cost estimates based on completed designs submitted by KDSB.

4.62 PKA could have better managed the Project by:

- appointing a suitably qualified supervising officer as provided for in the development agreement, to safeguard its interest including ensuring construction was carried out in accordance with building plans
- ensuring that detailed building / infrastructure specifications were submitted with the agreement
- undertaking competitive tenders for development contracts
- adhering to the JAFZI/TSG Masterplan for phased development
- complying with JKR standard terms for Design and Build Contracts
- appointing independent quantity surveyors, QS4 early in the development; PKA should have utilised QS4's services more effectively, especially in checking the progress billings submitted by KDSB.

Issue 15 Project management and control over the Project was weak

4.63 The Project suffered from weak project management and control on the part of PKA as illustrated in the examples below:

(i) PKA did not require:

- DA3 to specify:
  (a) detailed building/infrastructure specifications and
  (b) scope of work required of KDSB as the turnkey developer
  (c) a fixed contract price

- KDSB to submit preliminary cost estimates for all development works

- Quantity surveyors QS4 to be appointed prior to commencement of construction works in July 2004. QS4 was only appointed nine months later

- KDSB to submit plans and drawings to QS4 on a timely basis for QS4 to perform their scope of work effectively.

In addition, PKA did not appoint a suitably qualified Supervising Officer despite having the contractual right to do so.

(ii) Development agreements were inconsistent with Jabatan Kerja Raya's (JKR)'s standard contract terms for design guarantee and defect liability. The JKR Standard Form of Design and Build Contract stipulates that a contractor shall take full and unequivocal responsibility for the safety of the design and for the adequacy, stability and safety of all site operations and methods of construction. No expiry period is specified. In addition, the contractor is required to deposit a design guarantee bond of 5% of the cost of works for a period of 5 years commencing from the date of practical completion. For defect liability, a 24-month period from date of completion is stipulated.

However, DA, ADW and NADW limited KDSB's design guarantee and defect liability periods to 12 months from the completion date. In addition, these agreements did not require KDSB to deposit a design guarantee bond.

(iii) None of the Notices of Payment (NOP) presented by KDSB were forwarded to QS4 for their independent verification. PKA management accepted the NOPs solely on the basis of certificates issued by KDSB's architect. This has resulted in potential overbillings such as:

- NOPs for cable cost in relation to 33KV works under ADW and NADW when the cables in question had not been laid.

- NOPs of RM69.6 million for the business class hotel which QS4 had preliminarily valued at RM43.5 million (without furniture and electrical items in the rooms).

(iv) PKA twice agreed to accept higher interest rates than those originally contracted:

- 7% p.a. in the DA1, increased to 7.5% p.a. under DA3. We have not sighted any rationale on record for the increase.

- 5% p.a. in the ADW1, increased to 7.5% p.a. in ADW2. The rationale given was that KDSB would be exposed to interest rate increases given that payments would only end in 2011. PKA agreed with the increase despite KDSB having issued bonds at rates of 5.25% to 6.15%. Therefore, KDSB was not exposed to interest rate risk.

(v) The basis for PKA agreeing the final account with KDSB for DA3 was the cost assessment prepared by QS4. In assessing the cost, QS4 relied on a combination of as-built drawings and construction drawings instead of only as-built drawings. Therefore, the final account agreed by PKA may not be fully reflective of the actual works delivered by KDSB under DA3.

(vi) PKA paid for a link road to Westport Container Terminal 4 under the NADW of RM57.50 million. This was constructed to ease traffic from Klang / Kuala Lumpur entering into Westport. The road is not directly beneficial to the Project. It is open to question whether the cost of this link road should be accounted as part of the cost of the Project.

Issue 16 Project status as at 31 December 2008 - only the LIU have been issued with CF; defect liability period has expired and certain defects remain to be rectified

4.64 As at 31 December 2008, all components have been completed and accepted by PKA with the exception of the following:

- Electrical Infrastructure (ADW)
- Concrete Trenching (NADW)
- Electrical work for 33KV supply to Precinct 2 and 8 (NADW)
- Civil and infrastructure work to PMU (NADW)
- Link Road to Westport Container Terminal 4 (NADW)

In respect of the business class hotel, the construction of its car park and swimming pool is pending. However, PKA had accepted the business class hotel in March 2008.

4.65 The LIU are the only buildings in the Project to have been issued with CF. We noted that PKA has let out a number of units in the LOB which have not been issued with CF. The main PKFZ Authority office is also being occupied without CF. We understand that CF applications for the other buildings have not been processed mainly because penalty fees due to late submission of building plans have yet to be paid. The status of completion and CF approvals for each development component is set out in **Appendix 17**.

4.66 The defect liability period of all the building components under DA3 (excluding the ancillary buildings and the exhibition centre), expired on 7 November 2007. The defect liability period for the ancillary buildings and exhibition centre will expire on various dates in 2009.

4.67 As at 31 December 2008, a number of defects remained unrectified. A summary of defects not yet rectified is set out in **Appendix 18**. KDSB continues to carry out rectification works on these defects notwithstanding it is no longer contractually obliged to do so.

4.68 The matters raised under Issues 13, 14, 15 and 16 lead us to conclude that the Project has been poorly executed, which has resulted in:

- higher Project outlay;
- significant financing costs;
- weak control over KDSB's billings / NOPs;
- LIU which are surplus to current demand; and
- delays in the issuance of CF.

4.69 PKA should take immediate steps to address the issues arising from the land purchase and the development agreements with KDSB. These issues would include:

- the non deduction for value of Infrastructure Works not done under LA1 and other potential adjustments mentioned in **Appendix 8**;
- cable cost in relation to 33KV works under ADW and NADW (PKA management has since initiated discussions with Tenaga Nasional Berhad and KDSB to resolve this issue);
- cost of the business class hotel as compared to the value assessed by QS4;
- interest computation under LA1 and DA; and
- issuance of CF and defect rectification works.

4.70 In addition, PKA should strengthen its project management to complete outstanding construction works and ensure that the final accounts of DA, ADW and NADW are based only on as-built drawings.

(D) Ability to Meet Financial Obligations

4.71 This section covers PKA's ability to meet its obligations for the period 2009 to 2046 under the terms of the MOF soft loan.

4.72 PKA's cashflow projections for the period 2009 to 2046 are shown in Table 12 below.

Table 12: PKA's cashflow projections 2009 to 2046 (RM'000)

Year	Projected cash surplus from operations	Repayment to MOF	Yearly excess /shortfall of cash	Accumulated excess / shortfall of cash
	Cash balance brought forward		82,826	82,826
2009	15,350	-	15,350	98,176
2010	39,079	(24,040)	15,039	113,215
2011	46,398	(85,065)	(38,667)	74,548
2012	58,662	(146,090)	(87,428)	**(12,880)**
2013	78,214	(212,902)	(134,688)	(147,568)
2014	90,765	(257,942)	(167,177)	(314,745)
2015	100,912	(325,751)	(224,839)	(539,584)
2016	112,869	(341,470)	(228,601)	(768,185)
2017	115,473	(357,188)	(241,715)	(1,009,900)
2018	115,301	(372,907)	(257,606)	(1,267,506)
2019	127,485	(388,625)	(261,140)	(1,528,646)
2020	128,063	(405,234)	(277,171)	(1,805,817)
2021	141,925	(405,234)	(263,309)	(2,069,126)
2022	150,567	(405,234)	(254,667)	(2,323,793)
2023	151,197	(405,234)	(254,037)	(2,577,830)
2024	169,489	(405,234)	(235,745)	(2,813,575)
2025	179,281	(405,234)	(225,953)	(3,039,528)
2026	180,191	(405,234)	(225,043)	(3,264,571)
2027	201,100	(381,194)	(180,094)	(3,444,665)
2028	212,207	(320,169)	(107,962)	(3,552,627)
2029	213,452	(259,144)	(45,692)	**(3,598,319)**
2030	238,200	(192,332)	45,868	(3,552,451)
2031	250,808	(147,292)	103,516	(3,448,935)
2032	252,466	(79,483)	172,983	(3,275,952)
2033	277,418	(63,764)	213,654	(3,062,298)
2034	291,746	(48,046)	243,700	(2,818,598)
2035	297,816	(32,327)	265,489	(2,553,109)
2036	326,780	(16,609)	310,171	(2,242,938)
2037	344,760	-	344,760	(1,898,178)
2038	347,548	-	347,548	(1,550,630)
2039	381,168	-	381,168	(1,169,462)
2040	404,425	-	404,425	(765,037)
2041	407,977	-	407,977	(357,060)
2042	447,004	-	447,004	**89,944**
2043	468,189	-	468,189	558,133
2044	472,679	-	472,679	1,030,812
2045	523,612	-	523,612	1,554,424
2046	547,816	-	547,816	2,102,240
Total	**8,908,392**	**(6,888,978)**	**2,102,240**	

4.73 Key assumptions used by PKA management for the projections are as follows:

(i) PKFZ will achieve full tenancy in 2018;

(ii) Repayments to KDSB will follow the schedule shown in **Appendix 19**.

(iii) MOF soft loan will be used to meet KDSB's repayments;

(iv) There will be no changes in rental rates for the year 2009 to 2020. The rental rates will escalate by 15% at the interval of three years, commencing year 2021;

(v) All rentals will be collectable in the year billed; and

(vi) Power supply to the LIU will be upgraded to allow for power exceeding 60 amp.

Detailed cashflow projections complete with underlying assumptions as prepared by PKA management are enclosed in **Appendix 19**.

Note: In conducting our review of the cashflow projections, we have accepted and relied on information and representations made by PKA and PKFZSB management. No audit was performed by us. We have presumed that all information and representation provided to us is reliable, complete and accurate and our review is therefore subject to these limitations. No responsibility, whether legal or otherwise, is assumed on our part for their accuracy, and any projections cannot be guaranteed as being certain and achievable. PKA and PKFZSB management remains responsible for the projections provided to us including the underlying bases and assumptions. Projections, by their very nature, are subjected to uncertainties and unexpected events, many of which are outside the control of PKA and PKFZSB and their management. In addition, events and circumstances often do not occur as projected and therefore actual results are likely to differ from the projections, and the differences may be material.

Issue 17 PKA has projected that it will be in a cumulative cash deficit position in 2012 and will not be able to repay the MOF soft loan instalments from that time on

4.74 As shown in Table 12, PKA has projected that it will be in a cumulative cash deficit position from 2012 to 2041. The actual combined cash balance of PKA and PKFZSB based on their unaudited management accounts for FYE 31 December 2008 was RM143.666 million compared to RM82.826 million as projected. Had the actual cash balance been taken into account, PKA will be in a cash deficit position in 2013 instead of 2012.

4.75 As projected by PKA management, PKA will continue to be in cumulative cash deficit position until 2041. The cumulative cash deficit peaks in 2029 at RM3.598 billion.

4.76 PKA has not developed a solution to address the projected cash deficit commencing from 2012. Assuming that the cash shortfall will be addressed by deferring the MOF repayments period, and that interest will be maintained at 4% p.a., the MOF loan is projected to be fully repaid in the year 2051* instead of 2036. If this were to happen, the additional financing cost is estimated to be in the region of RM5 billion.

** Note: Based on extrapolated cashflow projections using the same assumptions as used by PKA management.*

4.77 The PKA Board should address this funding shortfall immediately. Some of the options it should consider may include loan restructuring involving a combination of rescheduling, grant and privatisation.

Issue 18 Letters of support issued by MOT could be construed as a guarantee that PKA would meet its obligations on a full and timely basis

4.78 The repayments to KDSB as assumed by PKA in its cashflow projections are backed up by four letters of support issued by the MOT to various parties as follows:

(i) Malaysian International Merchant Bankers Bhd and Pacific Trustees Berhad dated 28 May 2003, relating to the LA1

(ii) Malaysian Rating Corporation Berhad and the Trustees (OSK Trustees Berhad) dated 23 April 2004, relating to DA

(iii) Malaysian Rating Corporation Berhad and the Trustees (OSK Trustees Berhad) dated 8 December 2005, relating to ADW

(iv) Malaysian Rating Corporation Berhad and the Trustees (OSK Trustees Berhad) dated 23 May 2006, relating to NADW.

Copies of these letters of support are enclosed in **Appendix 20**.

With the exception of the letter dated 28 May 2003, all the letters of support stated that “the MOT shall at all times in the future ensure that PKA is in the position to meet (and do meet on a full and timely basis) their liabilities in respect of the Repayment Amount / Sum for so long as an amount in respect of the Repayment Amount / Sum remains outstanding”. The Repayment Amount / Sum refers to the amount payable by PKA to KDSB under the terms of the DA, ADW and NADW.

These three letters also stated that “there is no express or implied guarantee with regards to the Repayment Amount / Sum.”

4.79 Subject to legal interpretation, these letters of support could be construed as guarantees given that MOT has stated it will ensure that PKA will be able to meet all its obligations on a timely basis. If this is the case, MOT has breached Treasury regulations which require that such letters be approved by MOF.

4.80 Because of the potential significance of the letters of support, PKA would not have the option to default on its obligation to KDSB.

Issue 19 The Project’s actual occupancy of 14% is low and it is not generating sufficient revenue to cover its operating expenses

4.81 To date, only 14% of the total available lettable area is occupied. The following table shows confirmed tenancies against total lettable area.

Table 13: Lettable area and tenancies

	LIU	LOB	Open Land	Total
Available area space (sf)	2,809,344	500,000	27,878,400	31,187,744
(i) area occupied (sf) (ii) area occupied (%)	423,871 15%	93,579 19%	3,942,571 14%	4,460,021 14%

Source: PKFZ tenancy listing as at 31 December 2008

4.82 The Project's operational income and expenses, since PKFZSB commenced operations are as follows:

Table 14: Project's operational income and expenses (RM'000)

	(16 Months) FPE* 2006	(12 Months) FYE** 2007	9 Months to Sept 08
Rental income	-	3,136	5,260
Maintenance and other fees	117	560	486
Total revenue	117	3,696	5,746
Less:			
Operating Expenses (net of depreciation)	(14,224)	(12,836)	(6,867)
Operational Deficit	**(14,107)**	**(9,140)**	**(1,121)**

** FPE – financial period ended*
***FYE – financial year ended*

To date, the Project has yet to generate enough revenue to sustain its operating expenses. However, it has been able to reduce its operational deficit from RM14.107 million for FYE 2006 to RM1.121 million for FPE Sept 2008.

4.83 Based on current rental rates, PKA has projected that the Project will achieve full tenancy by 2018 with an estimated gross rental income of RM112 million with a net income after tax of RM61 million. On this basis the Project on its own will not be able to recoup its development cost of RM3.522 billion (excluding interest cost).

4.84 The Project faces many commercial challenges to achieving viability, including:

- Marketing
- Current economic climate
- Multi-agency approval environment
- Domestic and regional competition

4.85 The Government will therefore need to undertake a concerted effort involving a number of agencies in order to turn PKFZ into a financially viable venture.

(E) Financial Position of PKFZSB

4.86 This section deals with the financial position of PKFZSB as at 30 September 2008.

Issue 20 PKFZSB has incurred losses since its incorporation and has negative shareholder's funds as at 30 September 2008

4.87 PKFZSB has been recording losses since the day of its incorporation. The results of PKFZSB from Financial Period End (FPE) 2006 to FPE 30 September 2008 are as follows:

Table15: Audited and unaudited income statements (RM'000)

	16 months audited 31.12.2006	12 months audited 31.12.2007	9 months unaudited 30.9.2008
Revenue – Service and Operation Fee from PKA	15,026	12,800	7,333
Administrative Expenses	10,411	5,901	1,634
Finance Expenses	1	4	4
Sales and Marketing Expenses	3,562	3,065	2,017
Property Expenses	1,070	4,720	3,875
Total Operating Expenses	(15,044)	(13,690)	(7,530)
Loss Before Tax	**(18)**	**(890)**	**(197)**

4.88 PKFZSB's only source of income is the Service and Operation Fee payable by PKA pursuant to the Service and Operation Agreement. This Service and Operation Fee is meant to fund PKFZSB's operating expenses.

4.89 The table below sets out PKFZSB's audited balance sheets as at 31 December 2006 and 31 December 2007 together with its unaudited balance sheet as at 30 September 2008:

Table 16: Audited and Unaudited Balance Sheets (RM'000)

	Audited 31.12.2006	Audited 31.12.2007	Unaudited 30.9.2008
Property, Plant and Equipment	2,419	2,862	2,428
Deferred Taxation	0	107	107
Current Assets			
Other receivables	90	262	900
Fixed deposits	6,360	3,471	2,421
Cash and bank balances	160	523	751
Amount owing by PKA	0	0	3,771
	6,610	4,256	7,843
Less:			
Current Liabilities			
Trade payables	1,102	997	812
Other payables and accruals	280	2,645	10,063
Amount due to PKA	7,165	3,883	0
	8,547	7,525	10,875
Net Current Liabilities	(1,937)	(3,269)	(3,032)
Non Current Liabilities - Deferred Taxation	(40)	0	0
Net Assets / (Liabilities)	**442**	**(300)**	**(497)**
Shared Capital	500	500	500
Accumulated Loss	(58)	(800)	(997)
Shareholder's Funds	**442**	**(300)**	**(497)**

4.90 Shareholder’s funds turned negative in Financial Year End (FYE) 2007. PKFZSB has been in net current liabilities position since its first financial period, FPE 2006. Therefore, without continuing support from PKA, PKFZSB would be insolvent.

Definitions and abbreviations

Except when the context otherwise requires, the following definitions and abbreviations shall apply throughout this report:

ADW	Collectively ADW1 and ADW2 signed between PKA and KDSB
ADW1	Supplemental Agreement signed between PKA and KDSB dated 30 November 2005 in respect of Additional Development Works
ADW2	Supplemental Agreement signed between PKA and KDSB dated 26 April 2006 in respect of Additional Development Works
Board	The Chairman, General Manager and appointed members of Port Klang Authority
CF	Certificate of Fitness
CSSB	Central Spectrum Sdn Bhd, a subsidiary of PKNS (Company number 183136-D)
DA or Development Agreement	Collectively DA1, DA2 and DA3 signed between PKA and KDSB
DA1	Development Agreement signed between PKA and KDSB dated 27 February 2003
DA2	Supplemental Agreement to DA1 signed between PKA and KDSB dated 26 May 2003
DA3	Supplemental Agreement to DA1 signed between PKA and KDSB dated 27 March 2004
FYE	Financial Year End
FPE	Financial Period End
Government	Government of Malaysia
Infrastucture Works	List of infrastructure works as listed in **Appendix 13**
JAFZI	Jebel Ali Free Zone International
JAFZI Consultancy Agreement	The Consultancy Agreement signed between JAFZI and PKA dated 24 October 2003
JAFZI Management Agreement	The Management Agreement signed between JAFZI and PKA dated 24 October 2003
JAFZI/TSG Masterplan	The Master Plan and Market Assessment Study dated December 2004 prepared by JAFZI and The Services Group Inc (TSG)
JKR	Jabatan Kerja Raya
JPPH	Jabatan Penilaian dan Perkhidmatan Harta, Kementerian Kewangan
KDSB	Kuala Dimensi Sdn Bhd (Company No. 297068-V)
KPPLB	Koperasi Pembangunan Pulau Lumut Berhad
LA or Land Agreement	Collectively LA1 and LA2 signed between PKA and KDSB
LA1 or SPA	Sale and Purchase Agreement signed between PKA and KDSB dated 12 November 2002
LA2	Supplemental Agreement to LA1 signed between PKA and KDSB dated 27 March 2004
LA PMU	Agreement signed between PKA and CSSB dated 2 November 2004

Land	The parcel of land held under Pajakan Negeri 7324, Lot 67894, Daerah Klang, Mukim Klang, State of Selangor (formerly H.S. (D) 42378, No. PT 43656, Mukim Klang, State of Selangor) measuring 404.4 hectares or 999.5 acres or 43,538,200 sq ft.
LIU	Light Industrial Units
LOB	Lease Office Building
LoE	Letter of Engagement dated 8 October 2008 signed between PwCAS and PKA
MOF	Ministry of Finance
MOF soft loan	MOF soft loan of RM4.632 billion extended to PKA in 2007
MOT	Ministry of Transport
NADW	Supplemental Agreement signed between PKA and KDSB dated 26 April 2006 in respect of New Additional Development Works
NOP or NOPs	Notice of Payment or Notice of Payments issued by KDSB in relation to DA, ADW and NADW
PDS	Private Debt Securities
PKA	Port Klang Authority or Lembaga Pelabuhan Kelang
PKFZ	Port Klang Free Zone
PKFZSB	Port Klang Free Zone Sdn Bhd (Company No. 708970- U)
PMU	Pencawang Masuk Utama
Project	Port Klang Free Zone
PwCAS	PricewaterhouseCoopers Advisory Services Sdn Bhd (Company No. 573259-K)
QS4 Agreement 1 and 2	Agreements for Consultancy Services signed between PKA and QS4 Consortium dated 15 Aug 2005 and 3 October 2007
QS4 Consortium or QS4	Consortium comprising Perunding BE Sdn Bhd, Jurukur Bahan H&A, ASA-CM Jurukur Bahan Sdn Bhd & RK Partnership
WBGB	Wijaya Baru Global Berhad (Company No. 8184 – W)
WBHSB	Wijaya Baru Holdings Sdn Bhd (Company No. 334418-T)
WBSB	Wijaya Baru Sdn Bhd (Company No. 205953 - X)
VO	Variation Order

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