

**For discussion
on 21 February 2001**

EC(2000-01)31

**ITEM FOR ESTABLISHMENT
SUBCOMMITTEE OF FINANCE COMMITTEE**

**HEAD 145 - GOVERNMENT SECRETARIAT : ECONOMIC SERVICES
BUREAU**

Subhead 149 General departmental expenses

**HEAD 42 - ELECTRICAL AND MECHANICAL SERVICES
DEPARTMENT**

Subhead 001 Salaries

Members are invited to recommend to Finance
Committee -

- (a) the non-civil-service appointment of an
Electricity Advisor at the equivalent rank of
D2/D3 (\$116,650 - \$123,850/\$127,900 - \$135,550)
to the Economic Services Bureau for three years;
and
- (b) the creation of a permanent post of Chief
Electrical and Mechanical Engineer (D1) (\$98,250
- \$104,250) in the Electrical and Mechanical
Services Department,

with effect from 1 April 2001, to work out the post-
2008 regulatory regime for the electricity supply sector.

PROBLEM

The Scheme of Control Agreements (SCAs) signed between the
Government and the two power companies will expire in 2008. The Economic
Services Bureau (ESB) and the Electrical and Mechanical Services Department
(EMSD) need dedicated professional input at the directorate level to work out the
post-2008 regulatory regime for the electricity supply sector.

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PROPOSAL

2. We propose to create a non-civil service post of Electricity Advisor (EA) (at the equivalent rank of D2/D3) in ESB for three years and a permanent post of Chief Electrical and Mechanical Engineer (CEME) (D1) in EMSD, both with effect from 1 April 2001.

JUSTIFICATION

3. We need to take early action to devise an appropriate post-2008 regime for the regulation of the electricity supply sector, to ensure continued investment in the provision of an adequate and reliable electricity supply and a smooth transition should there be a new regime.

4. In examining the options for a post-2008 regulatory regime, we need to consider both technical (primarily engineering) and economic regulation issues. The technical issues include system stability, reliability, planning and logistics for meeting the needs of different market structures, and parameters for power systems under an increased interconnection scenario. In considering these issues, the Administration needs to commission consultancy studies, discuss with the power companies and work out mutually acceptable arrangements.

5. On economic regulation, we need to study the electricity market restructuring experience in other places while taking into account local circumstances, and to evaluate different market design and implementation arrangements, which may include unbundling generation, transmission, distribution and/or retail facilities. We will need to consider practical ways of modifying the market structure, the size and number of players in different market segments, the institutional framework, the market rules, and the economic costs and benefits of the different options. To this end, we intend to visit and maintain liaison with relevant regulatory authorities and other players in electricity markets overseas, and to examine their market rules and practices. We will also maintain liaison with the Mainland authorities on developments across the border. We need to think through the implications for Hong Kong taking into account the characteristics of the current Hong Kong market and its future prospects.

6. In examining the above issues, we need to consult a wide range of stakeholders including the Legislative Council Panel on Economic Services, the power companies, advisory committees and the community at large. If changes are to be made to the current arrangements, we would need to work out

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transitional arrangements with the existing power companies. We would also need to put in place the necessary market rules, regulatory and institutional structure, etc. in good time.

7. For the above mammoth and complex tasks which involve considering the restructuring of one of the most important economic sectors of Hong Kong, we need a multi-disciplinary team comprising administrators, engineers, economists and accountants. We also need outside support in the form of consultancy studies and a strengthening of in-house experience and expertise.

Existing staffing support in ESB and EMSD

8. At present we have very limited staffing resources for dealing with electricity supply policy and monitoring of the two power companies. In ESB, there is one Administrative Officer Staff Grade C (D2) (designated as PAS(ES)B), supported by one Senior Administrative Officer (designated as AS(ES)5), overseeing a number of policy areas including electricity supply, and one Assistant Director of Accounting Services (D2) heading a team of three accountants to monitor the financial affairs of electricity and gas companies and keep track of prices of major fuels. In EMSD, there are only one Senior Electrical and Mechanical Engineer (SEME) and two Electrical and Mechanical Engineers (EMEs) overseeing planning issues and monitoring the technical performance of the power companies.

9. All these officers are already fully occupied with on-going work which includes handling policy issues arising from the implementation of the SCAs, following up on issues relating to the Financial Plans of the power companies, such as reviewing demand forecasts and capacity addition schedules, reviewing and auditing their financial and technical performance, conducting annual tariff reviews etc. There is therefore no spare capacity for taking on the complex and detailed development work relating to the post-2008 regulatory regime. Besides, the considerable expertise and technical skills required for the tasks outlined in paragraphs 4 to 6 above are currently not available within ESB and EMSD.

Need for the proposed EA

10. In order to acquire the necessary expertise and technical skills, we propose to appoint a specialist who has rich experience in electricity market restructuring and a good understanding of the electricity supply industry to serve as an in-house EA for three years. This person will provide expert advice and assist in mapping out the future directions for the post-2008 regime, laying the

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Encl. 1 foundation for future implementation and contributing to policies that affect the future electricity supply infrastructure of Hong Kong. The job description of the proposed EA is at Enclosure 1.

11. Given that the advice of the EA may significantly affect the business and the future of the two existing utilities, we must ensure no conflict of interest between the EA and the existing shareholders. We will therefore consider both local and overseas candidates. As the EA is expected to deal with the two existing electricity utilities at a senior level, he should be of sufficient seniority. We therefore propose that the EA be remunerated at the equivalent rank of D2/D3 on the Civil Service Directorate Pay Scale, depending on the experience and qualification of the successful candidate.

12. We propose to appoint the EA on contract terms for an initial period of three years. We hope that once the electricity market restructuring framework and roadmap are set out, the follow-up implementation can be carried out by the support team headed by a CEME (see paragraphs 14 and 15 below). We will nevertheless review the appointment of the EA nearer the time in the light of experience gained, and having regard to the actual progress and circumstances at that time.

13. The proposed EA will report to the Deputy Secretary for Economic Services (DS(ES)1) who, among other things, oversees policy issues relating to an adequate, safe and reliable electricity supply. The EA will also need to liaise closely with PAS(ES)B as we expect there will be a lot of linkage between the present and future if changes are to be made to the present regulatory and market arrangements.

Need for the proposed CEME

Encl. 2 14. We also propose to create a permanent CEME post in EMSD to provide technical support to the proposed EA and the bureau, and continuity in taking forward the post-2008 regime. The job description of the proposed CEME post is at Enclosure 2. In view of the significance of the task and the level of responsibilities involved, a permanent CEME post at D1 rank is needed.

The support team

15. To provide support to the proposed EA and CEME, in particular in the technical aspects, we shall set up a support team of two SEMEs, two EMEs, one Senior Economist, and additional secretarial and clerical staff. Members of
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the team may also be attached to regulatory authorities and other players in the electricity supply sector overseas to acquire first hand regulatory and other experience in different restructured markets.

16. The proposed CEME post and the support team will be created as part of EMSD's establishment but will be attached to ESB to form part of the multi-disciplinary team after a period of familiarization in EMSD. The CEME and his team will be responsible to PAS(ES)B but will provide support to the EA. The existing and proposed organisation charts of ESB before and after the appointment of the EA and the creation of the proposed CEME and other supporting posts are at Enclosures 3 and 4 respectively.

Encls.3&4

17. Our plan is to map out the broad directions before 2003 to allow adequate time to take forward any proposed change. We propose to create the EA and CEME posts on 1 April 2001. Actual appointment of the EA, taking into account the time required for recruitment, is expected to be made in the second quarter of 2001.

Alternatives

18. Since this exercise will involve major policy considerations and regular discussion with the power companies and other stakeholders, we do not consider it a viable alternative to commission a consultancy firm to undertake the tasks. Besides, we need to build up expertise and a core group in-house for regulating the electricity supply sector in the future. As explained in paragraphs 8 and 9 above, the existing staff in ESB and EMSD do not have the capacity or the necessary expertise and skills required for the tasks. Therefore, there is no alternative to the current proposal.

FINANCIAL IMPLICATIONS

19. The additional notional annual salary cost of this proposal at MID-POINT is -

New Post	\$	No. of Posts
Electricity Advisor (D2/D3)	1,511,700	1
CEME (D1)	1,213,200	1
Additional cost	<u>2,724,900</u>	<u>2</u>

/20.

20. The full annual average staff costs of the proposal, including salaries and staff on-cost, is \$4,600,000.

21. In addition, the proposal will necessitate the creation of seven non-directorate posts at a total notional annual mid-point salary cost of \$4,247,340 and a full annual average staff costs of \$8,636,000 respectively.

22. We have included sufficient provision in the 2001-02 draft Estimates under Head 145 Government Secretariat - Economic Services Bureau and Head 42 Electrical and Mechanical Services Department to meet the cost of this proposal.

23. The proposal would have no impact on fees and charges as we have no intention to recover any cost in relation to the proposal from any persons or companies in the market and the community.

BACKGROUND INFORMATION

24. Electricity in Hong Kong is supplied by two power companies, namely CLP Power Hong Kong Limited (CLP Power) and Hongkong Electric Company, Limited (HEC). They are investor-owned and do not operate on a franchise basis, but are regulated by their respective SCAs with Government for the purpose of profit control. The existing SCAs for CLP Power and HEC will expire in 2008.

25. The Government commissioned a consultancy in 1998 to conduct an independent Study of Interconnection and Competition in the Electricity Supply Sector in Hong Kong (the Study) as a first step to exploring future directions for the local electricity supply market with reference to the global and regional trends. The main objective of the Study was to establish whether additional interconnection between Hong Kong's two electricity supply companies and encouragement of competition in the electricity supply sector would be in the interests of consumers. The Study was completed in November 1999.

26. We invited public comments on the findings and recommendations of the Study and received written comments from the power companies, the Consumer Council, other organisations and individuals. For the long term, nearly all commentators supported reviewing the market structure and the regulatory regime for Hong Kong's electricity supply sector. They were generally of the view that deregulation and introduction of competition was a global trend. They

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suggested that the Government should examine all relevant issues, including reliability of supply, operation of the future market, role of the regulatory authority and interests of stakeholders when considering the way ahead. Some also highlighted the complexity of transforming the electricity supply market and emphasised the need to map out the post-2008 arrangements well before expiry of SCAs in 2008.

27. To take forward the issue of increased interconnection, we are in the process of commissioning a detailed investigation study on a number of planning, reliability and logistics issues and the time-frame required for the construction of additional interconnectors between the two power companies. At the same time, we are also examining market restructuring experience in other places with a view to identifying practicable options for the Hong Kong market in future. In view of the complexity of the issue involved in mapping out the post-2008 regulatory regime, we need additional manpower. The requirements are set out in the current proposal.

28. We consulted the Legislative Council Panel on Economic Services on 16 January 2001 on the current proposal. Members unanimously supported the proposal.

CIVIL SERVICE BUREAU COMMENTS

29. The ESB has considered carefully various means to provide the required directorate and professional support to meet the service need. Noting that it is a major policy initiative of ESB to map out the future regulatory regime for the electricity supply sector in Hong Kong and having regard to the reasons detailed in the paper, Civil Service Bureau considers the proposal justified, and the grading and ranking of the proposed posts appropriate.

ADVICE OF THE STANDING COMMITTEE ON DIRECTORATE SALARIES AND CONDITIONS OF SERVICE

30. The Standing Committee on Directorate Salaries and Conditions of Service has advised that the grading proposed for the post of Chief Electrical and Mechanical Engineer would be appropriate if the post were to be created.

Proposed Job Description of Electricity Adviser

Major Duties and Responsibilities

To report to Deputy Secretary for Economic Services (1) on the following main duties -

- (a) To provide expert advice and proposals to both ESB and EMSD for the formulation of electricity supply policies and market restructuring strategies.
- (b) To provide expert advice on the following areas:
 - (i) appropriate regulatory regime;
 - (ii) appropriate market structure and ways to achieve it;
 - (iii) rules and arrangements required for different market and regulatory options;
 - (iv) detailed plan and time frame for different market and regulatory options;
 - (v) mechanism to ensure reliability and security of electricity supply under different market options; and
 - (vi) transitional arrangement necessary for a smooth transition where changes are to be made to the current regulatory arrangement.
- (c) To attend meetings of Legislative Council, Energy Advisory Committee and other groups to explain market options and government's plans for the post-2008 regime.
- (d) To attend meetings with power companies and relevant parties on issues relating to any proposal for change to the existing market and regulatory regime.
- (e) To train and transfer market restructuring knowledge and expertise to permanent in-house staff.

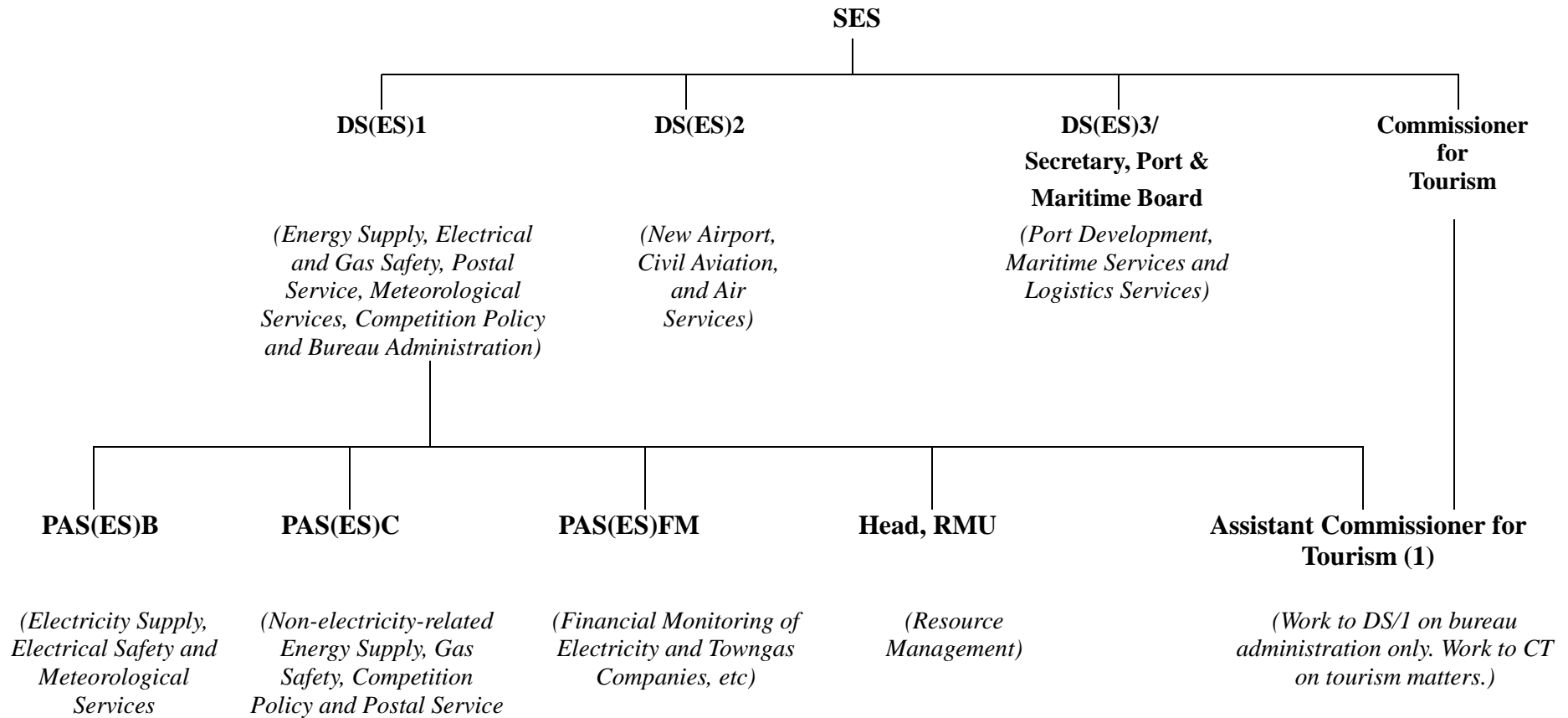
**Proposed Job Description of
Chief Electrical and Mechanical Engineer (D1)**

Major Duties and Responsibilities

To report to Principal Assistant Secretary for Economic Services (B) on the following main duties -

- (a) To direct the operation and management of the division for review of the electricity supply sector.
- (b) To work with the Electricity Adviser to provide professional advice and proposals for the formulation of policies and strategies relating to the post-2008 regime.
- (c) To plan the necessary institutional set up for, and implementation of, the post-2008 regime taking into account the advice of the Electricity Adviser.
- (d) To co-ordinate with relevant government departments, utilities and relevant parties for the formulation of the post-2008 regime.
- (e) To attend meetings of Legislative Council, Energy Advisory Committee and other groups to explain government's objectives and proposals.
- (f) To deputise the Electricity Adviser in chairing working group meetings with the power companies and relevant parties in making arrangement for the post-2008 regime.
- (g) To attend meetings with existing power companies on transitional arrangements if necessary.
- (h) To manage consultancy studies on relevant issues.
- (i) To assist in liaising and co-ordinating with South China regulatory agencies and electricity supply organisations on issues related to the development of South China electricity supply market and supply reliability in the region.

**Existing Organisation Chart
of Economic Services Bureau**



**Proposed Organisation Chart
of Economic Services Bureau**

