

## **British Chamber of Commerce in Hong Kong**

### **Response to the Government's Consultation Paper on the – *Future Development of the Electricity Market in Hong Kong, Stage II Consultation***

**Submitted to the Economic Development and Labour Bureau, March 31<sup>st</sup>, 2006**

This paper has been submitted to the Economic Development and Labour Bureau in response to the Government's consultation paper of December 2005: *Future Development of the Electricity Market in Hong Kong*. It has been compiled by the Business Policy Unit of the British Chamber of Commerce in Hong Kong, the Chamber's think tank and advisory group on Government policy, and represents the views and concerns of the Chamber's members.

The British Chamber is one of Hong Kong's largest international business organisations. The Chamber comprises major multinational companies and institutions, as well as a substantial number of SMEs and represents a broad spectrum of British, Hong Kong, international and Chinese companies. Collectively, this membership makes a significant contribution to the Hong Kong economy and to employment, and constitutes a representative cross-section of business opinion in the SAR. Whilst the membership includes major stakeholders in the electricity market in Hong Kong, in drafting this response the Chamber has sought to include a broad spectrum of views and care has been taken not to simply reflect the position of a single company or group. Furthermore, as this is a Stage II consultation, the Chamber has limited its comments to the recommendations outlined in the paper, and has not referred to additional issues already covered in Stage I of the consultation.

#### **1. Policy Objective**

The Chamber supports the Government's policy objective for the future development of the electricity market. The high degree of reliability achieved in Hong Kong is viewed as a cornerstone of the city's strength as a regional financial centre. Given Hong Kong's continued poor air quality, the Chamber also fully endorses the Government's aim to minimise the environmental impact caused by power generation.

#### **2. New Supply Sources**

Whilst the Chamber views market competition as desirable, concern has been raised as to the effects of opening the electricity market to new supply sources. Hong Kong is a small market in which security and reliability of electricity supply are critical to

its continued success as an international centre for business. The Chamber would like to see a scheme of control for the electricity market that:

- i) creates a structure for 'best in class' delivery of electricity, whereby the existing 99.99% reliability rates are maintained
- ii) provides incentives to the electricity companies to enact world class standards on renewable energy and the use of 'clean' fuel
- iii) has appropriate safeguards to ensure that consumers continue to be protected and provided with electricity at reasonable cost

Due to its geographical location, should the electricity market be opened to new supply sources, these would necessarily derive from Mainland China, or more specifically Guangdong Province. Over the long term, Hong Kong is likely to become more fully integrated with Guangdong, and ultimately it is conceivable that a single market for the provision of power throughout the Greater Pearl River Delta region could be created. It is important, if such a market is to be opened, that a level playing field for all companies entering the market should be created. This needs to be achieved at the same time as guaranteeing reliability of supply, achieving targets for renewable energy and controlling the cost of electricity to the consumer.

The Chamber does not believe that the timing is right to open Hong Kong's electricity market to supply from the Mainland and does not believe that the introduction of new supply sources from the Mainland would assist in achieving the three key objectives outlined above. For this to be possible, significant research and monitoring would first be required. In order to ensure fair competition and to ensure that the policy objectives of the future scheme of control are met, companies from the Mainland would have to be able to prove themselves able to adhere to the same legal, technical and environmental standards imposed on the current Hong Kong providers. Supply from the Mainland also raises the questions of whether the same market access to the Mainland would be allowed to Hong Kong's electricity companies, and whether the Government should allow the entry of new players into the Hong Kong market that are supported heavily by subsidies given by Mainland authorities.

The idea of opening up of Hong Kong's electricity market to new supply sources creates a great deal of uncertainty and this uncertainty casts doubt over the reliability of electricity supply. A high-rise, energy-dependent place like Hong Kong would

cease to function in the event of prolonged power failure. Even short-term interruptions are unacceptable. The Chamber welcomes further research into alternative sources of power, but would like to see the Government first formulate a strict set of conditions that would carefully define criteria for allowing entry to Hong Kong by Mainland supply sources. These conditions for market access would form the basis for future discussion with Mainland authorities, and it is only on achievement of these criteria that the Government should consider allowing new supply sources to access the Hong Kong market. In setting these criteria, there should be no compromise on the Government's stated objectives with regard to reliability, safety, efficiency, price and environmental impact.

Measures outlined in the Government consultation paper to open grid access and increase interconnection both between the two existing power companies and with Guangdong should only be undertaken once doubts regarding the impact on the reliability of electricity supply can be sufficiently allayed. Given the investment and the time required to make such changes, a full cost/benefit analysis of such arrangements to cater to new supply sources should first be undertaken.

### **Proposed Regulatory Arrangements**

The Chamber supports continued safety regulation of the electricity market. The Chamber also fully supports the application of world class environmental standards to the electricity generation industry in Hong Kong. With regard to this, the Chamber would also like to see the consumer taking some responsibility for the efficient use of power and the Government providing support through the development of public education programmes to promote energy efficiency and conservation. This encouragement should also be extended to the construction industry and apply to building standards. The aim of economic regulation should be to set an agenda that creates the desired behaviour by Hong Kong's electricity companies.

The Chamber supports the Government's use of a balance between regulation and incentives to ensure that policy objectives are met. There are concerns, however, that some regulations may lead to increased uncertainty for investors and, therefore, have the potential to adversely impact investment decisions. The Chamber feels that a 15 year term should be maintained, particularly if the Government's intention is to encourage long term resource allocation with targets for renewable energy.

The Chamber feels that the 'rate of return' should be a matter for negotiation between the Government and the electricity companies. The Chamber would like to stress, however, that in order to attract investment, this should be a fair rate for the industry and comparable with rates of return in other business sectors. Transparency on this issue and effective benchmarking against other jurisdictions and sectors should ensure a rate that is acceptable to investors and fair to consumers.

The Chamber agrees that in determining tariff levels the future scheme of control should include the costs of making available supply and the agreed return to the company. The Chamber is also in favour of the maintenance of the Fuel Clause Account and the Tariff Stabilisation Fund. However, whilst transparency of pricing and the continued provision of information to the public are important, the Chamber does not regard it as necessary or desirable for the Government to approve all tariff adjustments made by the electricity companies. The Chamber does not believe that increased bureaucracy and micro-management by Government in this way would go anyway to enhancing the efficient operation of the electricity market.

The Chamber supports the maintenance of the current institutional set up and does not feel that a separate regulatory authority is necessary at this stage. The Chamber would, however, support enhanced consumer protection through a Government operated mechanism to deal with customer concerns that have failed to be addressed by existing services provided by the electricity companies.

Finally, the Chamber would like to see the development of a comprehensive environmental policy that would provide focus for the future development of the electricity market in Hong Kong. This would encompass, for example, targets for renewable energy, educational measures, and incentives for investors, as well as incentives for power companies and consumers to save electricity, use energy-efficient devices and employ 'clean' energy. In this way, Government could greatly enhance energy efficiency and provide the leadership necessary to reach world-class standards for environmental protection related to the use of power in Hong Kong.

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