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For information on
30 December 2011

Legislative Council Panel on Economic Development

Latest Development of Power Companies' 2012 Tariff Reviews

PURPOSE

This Paper reports to Members the latest development of the Administration's negotiation with the power companies on the 2012 tariff adjustment since the meeting of Panel on Economic Development (the Panel) on 13 December.

PUBLIC REACTION TO TARIFF INCREASE

2. CLP Power Hong Kong Limited (CLP) and The Hongkong Electric Company Limited (HEC) announced on 13 December 2011 their tariff adjustment for the coming year. The Administration indicated reservations and raised a number of queries. Having regard to the views of the Executive Council, HEC reduced the tariff increase to 6.3% on the same day. HEC announced further improvement to its progressive tariff structure on 16 December. As a result, the actual net tariff for 90% of HEC's domestic consumers would increase by 4.97% or less, which is lower than inflation.

3. On the other hand, CLP announced the net tariff increase of 9.2% on 13 December. The Legislative Council, the Energy Advisory Committee, many organisations and the community at large expressed grave concern over the tariff increase. CLP revised downwards the tariff increase to 7.4% on 21 December. However, at both the meetings of Legislative Council on the same day and the Panel meeting on 23 December, Members remained discontent with the revised tariff increase. The Panel also passed a motion, requesting for the deferral of tariff increase by two months. CLP was also requested to lower the tariff increase by reducing the operating costs, taking out the capital investment projects not agreed by the Administration and making use of the Tariff Stabilisation Fund (TSF); and lower the tariff immediately upon receipt of rent and rates refund. In the past week, the Environment Bureau

continued the negotiation with CLP and requested CLP to respond positively to the requests made by Members and the Administration.

CLP'S LATEST RESPONSE

4. CLP announced the revised tariff increase this morning (30 December). The Net Tariff increase is further reduced from 7.4% to 4.9%. The Basic Tariff increase is lowered from 6.3% to 5.3%. For details, please refer to CLP's Media Release at the Annex.

5. Regarding the four queries raised by the Environment Bureau in respect of CLP's tariff proposals this year, the latest development following further negotiation is set out below -

Query	Response
(i) Operating costs would increase by 11.2%, which is far above inflation. CLP was requested to exercise better cost control.	CLP now reduces the increase in operating costs upon review. Together with measures in (ii) and (iii) below, Basic Tariff would increase by 4.2 cents/kWh in the coming year, down from 5 cents/kWh originally.
(ii) CLP has included in its capital investment "Preparatory work" and "Stage 1 works" for increasing generation capacity. These premature capital investment items have yet to be fully vetted or included in the current Development Plan and must be taken out.	CLP has agreed to take out the related capital expenditure.
(iii) CLP may mitigate the tariff increase by reducing the TSF balance.	The projected TSF balance has been reduced from the original forecast of $300 million to about $100 million. This is the lowest level ever recorded under the current Scheme of Control Agreement (SCA).

Query	Response
(iv) In anticipation of refund of rent and rates in coming years, it is suggested that CLP provide rebates to customers as early as possible, with a view to relieving the tariff increase pressure.	CLP will alleviate the tariff increase impact through a special rebate of 3.3 cents/kWh.

6. On 21 December, CLP had proposed to reduce the tariff increase from 9.2% to 7.4% by increasing the deficit balance in the Fuel Clause Recovery Account (FCA) from about $800 million to about $1,400 million. However, adopting this measure alone to relieve tariff increase may increase the pressure of tariff increase in the future. Having listened to the views of different sectors of the community, CLP will adopt other measures as set out above to reduce the tariff increase, while maintaining the deficit balance at the original level of about $800 million.

7. Some Members expressed concerns at earlier meetings over the impact of CLP’s tariff structure adjustment on the operating costs of the commercial sector. CLP indicates that, with regard to the views of different sectors of the community received, it has decided to retain the current tariff structure for commercial customers, and will continue to review and consult users on changes to the tariff structure in the coming year, with a review to encouraging energy conservation on one hand while addressing users’ needs and concerns on the other.

BACKGROUND

8. The SCAs signed between the Government and the power companies in 2008 provide a framework for regulating the supply of electricity. The Government has all along been undertaking strictly the scrutiny duties at two levels, including the five-year Development Plans and annual tariff adjustment proposals. In scrutinising the tariff proposals submitted by the power companies annually, the Administration focuses on five areas, including capital expenditure, operating costs, FCA, TSF and other income, with a view to avoiding investments or expenditure that are excessive, premature, unnecessary or unreasonable, and performing its gate-keeping role in the tariff review with the power companies.

9. In the current tariff review, it is the first time that the Government could not come to terms with the power company on the extent of tariff increase. The Government raised a number of queries against the tariff increase, and the Executive Council, the Legislative Council and the public also expressed concerned. Since 13 December, the two power companies have revised their original tariff proposals by reducing the tariff increase and improving the tariff structure.

Environment Bureau
December 2011

CLP 中電

新聞稿
Media Release

中華電力有限公司
CLP Power Hong Kong Ltd

30 December 2011

CLP Finalises Tariff Package with Government
2012 Tariff Increase Narrowed To 4.9%

CLP Power Hong Kong Limited (CLP) today announced that it has finalized with Government a revised package for its electricity tariff for 2012, following thorough discussions with Hong Kong Government.

Tariff for 2012 is 98.7 cents, an increase of 4.9% from the current year.

The new package has significantly narrowed the increase of 9.2% as announced on 13 December, taking into account a number of measures, namely:

- Savings from the removal of planned capital expenditure on additional generating capacity, and further efforts to reduce operating costs.
- A deeper draw-down on our Tariff Stabilisation Fund (“TSF”).
- A Rent and Rates Special Rebate.

Details are explained as follows:

1. **On Basic Tariff**:

   Our Basic Tariff will be increased by 4.2 cents, compared with a 5-cent increase in our announcement two weeks ago. The adjustment is attributable to savings from the removal of planned capital expenditure on additional generating capacity and extra efforts in enhancing cost control measures on operation.

   In addition, drawing down the TSF to a projected level of $100 million also allows buffer to reduce the impact of tariff increase.   This is the lowest TSF balance ever recorded and represents just one day of electricity sales for CLP.

2. **On Rent and Rates Special Rebate:**

   CLP has made a commitment to return to customers any repayments made by Government upon the final resolution of the Court in our favour in respect of CLP's claim against Government's overcharging of our rent and rates over the past decade.

   While the case is still continuing, our latest discussion with our lawyer has increased our confidence of possible refund from the Government on this case. We have therefore taken the initiative to provide a special rebate of 3.3 cents per unit, which in effect offsets part of the tariff increase.

3. **On Fuel Clause Charges:**

   Global fuel costs are moving on a trajectory of significant increases with high volatility and Hong Kong is competing with many economies for cleaner fuels, in particular, gas to generate cleaner electricity. The challenges that we face are only becoming more serious going forwards in the context of rising costs and increasing use of gas to meet Government's regulatory requirements, including tightened emissions caps on our operations.

   CLP is already carrying a deficit Fuel Clause Account (FCA) on behalf of the customers and the deficit is deteriorating. There are concerns that our earlier proposal to carry a bigger FCA deficit would increase the pressure of tariff increase in the future. To address these concerns, we consider it prudent to increase the Fuel Clause Charges by 3.7 cents per unit in order to smooth out the impact of fuel costs in future. There remains a forecast deficit of over $800 million in the FCA by the end of 2012.

   CLP will continue to monitor the fuel market and its implications to our tariff carefully.

In addition, as opinions on the tariff structure change for our commercial customers are divided, we will defer the implementation of this energy efficiency driven initiative until a wider public acceptance is reached. This means that the current tariff structure for commercial customers will remain unchanged.

CLP Power's Vice Chairman, Mrs Betty Yuen, said, "the new package represents a balanced outcome that meets Government's objectives without compromising the quality of our service to our customers in Hong Kong. At the same time, our ability to exercise strict discipline for a prudent and long-term financial management on behalf of our customers and our shareholders can also be upheld."

"CLP has critically reviewed options to help reduce the tariff increase. This final package is a result of extensive discussions with Government and has addressed their concerns. We believe Government will find it acceptable," said Mrs Yuen.

<u>Details of the 2012 tariff are as follows:</u>

Components (¢/u)	**Current**	**Effective 1 Jan 2012**
Average Basic Tariff	80.0	84.2 (+4.2)
Fuel Clause Charge *	14.1	17.8 (+3.7)
Rent & Rates Special Rebate	- -	- 3.3
Average Net Tariff	94.1	98.7 (+4.6)

*** Fuel Clause Charge is the cost of fuel used to generate electricity which is directly passed through to customers. CLP makes no profit on fuel.**

With the adjustment, 30% of our domestic customers will have no impact from the tariff package while 50% will have a monthly increase of no more than $3.4 and 90% of our customers will see electricity bills increase of $40.7 or less per month.

50% of our commercial customers will have no more than $27.5 increase monthly.

CLP will continue to work with the Government on the delivery of quality electricity service to customers, at a competitive price and in an environmentally friendly manner, to meet the demand of our customers. We also pledge to continue complying with the Hong Kong Government's regulatory and policy requirements.

- Ends -

About CLP Power Hong Kong Limited

CLP Power Hong Kong Limited ("CLP Power") is the Hong Kong utility subsidiary wholly owned by CLP Holdings Limited, a company listed on the Hong Kong Stock Exchange and one of the largest investor-owned power businesses in Asia. CLP Power operates a vertically integrated electricity supply business in Hong Kong, and provides a highly reliable supply of electricity and excellent customer services to 5.7 million people in its supply area.

- ENDS -

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