

Extract

立法會

*Legislative Council*

LC Paper No. CB(4) /15-16

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by the Administration)

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**Panel on Economic Development**

**Minutes of meeting**

**held on Monday, 23 November 2015, at 9:30 am  
in Conference Room 1 of the Legislative Council Complex**

**Members present** : Hon James TIEN Pei-chun, GBS, JP (Chairman)  
Hon Jeffrey LAM Kin-fung, GBS, JP (Deputy Chairman)  
Hon CHAN Kam-lam, SBS, JP  
Hon Andrew LEUNG Kwan-yuen, GBS, JP  
Hon WONG Ting-kwong, SBS, JP  
Dr Hon LEUNG Ka-lau  
Hon Paul TSE Wai-chun, JP  
Hon Steven HO Chun-yin, BBS  
Hon Frankie YICK Chi-ming, JP  
Hon YIU Si-wing, BBS  
Hon Charles Peter MOK, JP  
Hon Kenneth LEUNG  
Hon Dennis KWOK  
Hon Christopher CHEUNG Wah-fung, SBS, JP  
Dr Hon Fernando CHEUNG Chiu-hung  
Ir Dr Hon LO Wai-kwok, SBS, MH, JP  
Hon CHUNG Kwok-pan  
Hon Tony TSE Wai-chuen, BBS

**Member attending** : Hon LEE Cheuk-yan

**Members absent** : Dr Hon LAM Tai-fai, SBS, JP  
Hon Albert CHAN Wai-yip  
Hon WU Chi-wai, MH  
Hon SIN Chung-kai, SBS, JP  
Dr Hon Elizabeth QUAT, JP  
Hon TANG Ka-piu, JP

**Public Officers  
attending**

: Agenda items IV and V

Mr WONG Kam-sing, JP  
Secretary for the Environment

Mr Vincent LIU, JP  
Deputy Secretary for the Environment

Mr Donald NG  
Principal Assistant Secretary for the Environment  
(Electricity Reviews)

Ms Esther WANG  
Principal Assistant Secretary for the Environment  
(Financial Monitoring)

Mr Alan CHOW  
Chief Electrical and Mechanical Engineer  
(Electricity Team)  
Environmental Bureau

Agenda item V

Miss Ada CHEN  
Senior Assistant Law Officer (Civil Law)  
Department of Justice

Agenda item VI

Professor Anthony CHEUNG, GBS, JP  
Secretary for Transport and Housing

Miss Joey LAM  
Deputy Secretary for Transport and Housing  
(Transport)5

Miss Joyce CHAN  
Assistant Secretary for Transport and Housing  
(Transport)11A

Agenda item VII

Ms Elaine HUI  
Assistant Director (Market and Competition)  
Office of the Communications Authority

Ms Helen LAI  
Head, Market and Competition 1  
Office of the Communications Authority

**Related  
organizations**

: Agenda item VI

Tricor Consulting Limited

Mr John NG  
Managing Director

Ms Rachel CARTLAND  
Contract Senior Consultant

Ms Ashley SEE  
Senior Consultant

Agenda item VII

Competition Commission

Hon Anna WU, GBS, SBS, JP  
Chairperson

Ms Rose WEBB  
Senior Executive Director

Mr Rasul BUTT  
Executive Director (Corporate Services and Public  
Affairs)

**Clerk in attendance :** Ms Debbie YAU  
Chief Council Secretary (4)5

**Staff in attendance :** Ms Shirley TAM  
Senior Council Secretary (4)5

Ms Zoe TONG  
Legislative Assistant (4)5

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**IV. Public consultation on the future development of the electricity market**

(LC Paper No. CB(4)217/15-16(03) — Administration's paper on future development of the electricity market

LC Paper No. CB(4)217/15-16(04) — Paper on future development of the electricity market prepared by the Legislative Council Secretariat (updated background brief))

**V. Proposed extension of two supernumerary posts to take forward the outcome of the public consultation on the future development of the electricity market**

(LC Paper No. CB(4)217/15-16(05) — Administration's paper on taking forward the outcome of the public consultation on the future development of the electricity market – extension of two supernumerary posts

LC Paper No. CB(4)217/15-16(04) — Paper on future development of the electricity market prepared by the Legislative Council Secretariat (updated background brief))

Members agreed to combine the discussion of agenda items IV and V as they were closely related.

Presentation by the Administration

2. At the invitation of the Chairman, Secretary for the Environment ("SEN") briefed members of the views received during the public consultation on the future development of the electricity market conducted from 31 March to 30 June 2015 ("the Consultation"). He said that in addition to having received views from the some 16 000 submissions, the Administration had also attended over 25 engagement sessions and held a public forum to solicit views. Having regard to views received, the Administration planned to put forward improvement proposals to the future contractual arrangement between the Government and the two power companies, such as reducing the permitted rate of return ("RoR"), enhancing the promotion of energy efficiency and conservation ("EE&C") and renewable energy ("RE"), improving the incentive and penalty scheme to enhance power companies' performance, increasing information transparency of the power companies and conducting studies to pave the way for introducing competition in the long run.

3. On permitted RoR, SEN highlighted that taking into account views received through different channels, the prevailing economic environment as well as comparable investments overseas, the Administration considered that there was room for reduction in the permitted RoR. The Administration would commission a further study to revise the permitted RoR to the appropriate level having regard to the current global market conditions. SEN said that the level of the permitted RoR would be considered together with other improvement proposals of the new contractual arrangement.

4. SEN also sought members' views on the Administration's proposal to extend two supernumerary posts which were created in 2014 in the Environment Bureau ("ENB") and the Department of Justice ("DoJ") respectively to undertake the review of the electricity market. The said posts would continue to head a dedicated team each in ENB and DoJ to undertake the negotiation with the power companies and implement the outcome. As the negotiation with the power companies was expected to be lengthy and intensive, dedicated teams were necessary to ensure that adequate resources would be provided to undertake the highly-demanding and complicated tasks involved. Further details of the Consultation outcome and the staffing proposal were set out in the Administration's papers (LC Paper Nos. CB(4)217/15-16(03) and (05)).

## Discussion

### *Introduction of competition*

5. Mr Tony TSE relayed the responses of his constituencies in the architectural, surveying and planning sectors to the Consultation that reliability of electricity supply was of utmost importance followed by affordability, and the power supply in Hong Kong was performing well on these areas. While the sectors were open to the idea of introducing competition to the electricity market, they suggested that changes could be made based on the existing regulatory framework.

6. Noting that the business sector was in general less positive about the introduction of competition, Mr Frankie YICK opined that the sector was more concerned about the stability and affordability of power supply, and their support for the introduction of competition would depend on the strategy to be adopted.

7. Mr CHAN Kam-lam considered that the Administration should study in detail the public views received in response to the Consultation, and address the public concerns about the natural monopoly of the electricity supply market. For example, the power companies should maintain reliability of power supply at affordable tariff level, and source fuels used for electricity generation at reasonable prices etc. He remarked that the power companies, being public utilities, should shoulder social responsibility on environment protection and market development in order to obtain a reasonable return.

8. SEN said that the Consultation had achieved a high response rate and views received were generally in line with the Administration's four energy policy objectives of safety, reliability, affordability and environmental protection. He said that the Consultation outcome had provided a good basis for formulating improvement proposals to the new Scheme of Control Agreements ("SCAs"), and the Administration would take into account views received when negotiating with the two power companies the future contractual arrangement.

9. Mr Frankie YICK suggested that the power companies could increase their interconnection to enable a reduction of their reserve margins and hence the electricity tariff. He also requested the Administration to provide written information on the pros and cons of increased interconnection between the two power companies' facilities, including an analysis on the level of tariff reduced over a longer term as a result of the estimated cost of investment, and the reduction of reserve margins etc.

10. SEN advised that the existing interconnection between the two power companies had already served the function of reducing the reserve capacity each power company required, and enhancing the interconnection could not help further reduce each of their reserve margin. Deputy Secretary for the Environment ("DSEN") elaborated that enhancing interconnection would incur additional substantial upfront investment equivalent to the installation cost of several gas generation units amounting some tens of billion dollars which would have tariff implications. Besides, the reserve margin of the two power companies was expected to reduce to a percentage between 20% and 30% at the end of this SCA period. The Administration's current assessment was that enhancing interconnection at this stage might not bring concrete benefits to the consumers in the near term. The consideration might however be different in the longer term. If it was decided that electricity from the Mainland should be imported in future to allow more choices for consumers, the two existing local power grids would have to be better connected, and it would be more cost-effective to consider how to strengthen the interconnection between the two existing power companies in that context. He undertook to provide further supplementary information on this matter afterwards.

11. Echoing Mr Frankie YICK's views that a detailed analysis on the matter of increased interconnection between the two power companies could help Members to decide whether to pursue the subject, Mr CHAN Kam-lam considered that to enhance its bargaining position, the Administration should have a stance on the matter before entering into negotiation for the next SCAs with the two power companies.

*(Post-meeting note: The Administration's response was issued to Members vide LC Paper No. CB(4)351/15-16(01) on 14 December 2015.)*

12. Mr LEE Cheuk-yan was very disappointed about the Administration's work to increase interconnection between the two power companies undertaken by former bureau directors, namely, Mr Stephen IP Shu-kwan and Dr Sarah LIAO Sau-tung, since more than a decade ago. As no progress had been made so far, the objective of introducing competition to the electricity supply market appeared as an empty promise. Now, the focus was shifted to the promotion of RE which, in his opinion, would be implemented in small scale, and could not bring any real competition and benefit the customers. Mr LEE expressed grave concern about the status quo of maintaining the monopoly of the electricity supply market. He cautioned the Administration not to use the outcome of the Consultation as an excuse to continue the current contractual arrangement by SCAs. As regards the Consultation, Mr LEE commended the work of the public relation teams of the two power companies, but urged the Administration

to consult the 18 newly-elected District Councils. In response, SEN said that views received during the Consultation were very clear and largely in line with the Administration's four energy policy objectives. The Administration would take into account views received through different channels when charting the way forward. Noting the Administration's response, Mr LEE requested to put on record his dissatisfaction that the Administration had no intention to consult the District Councils.

*Future regulatory and contractual arrangements – permitted RoR*

13. Given the public concern on environmental protection, Mr Tony TSE suggested allowing the power companies to reap returns on their investment in promoting RE and EE&C as an incentive to encourage better environmental performance. DSEN remarked that there was a clear consensus that future contractual arrangement should be crafted to better help promote energy saving and conservation. Some respondents suggested that an incentive and penalty scheme should be in place to encourage energy saving by power companies. The Administration would take into account these views in negotiating the new SCAs with power companies.

14. Mr YIU Si-wing urged that, given the power supply in Hong Kong was already quite sophisticated in terms of its safety, reliability and affordability, it was important to make Hong Kong a more advanced city in the environmental performance, and EE&C on electricity supply. To this end, he agreed that the permitted RoR for power companies could be maintained at the current level of 9.99% in exchange for better environmental performance. SEN said that while the current electricity supply was safe and reliable at affordable price, the Administration would consider how to move forward to further enhance the environmental performance. The Administration would consider the permitted RoR together with other improvement proposals in totality and ensure that the four energy policy objectives would continue to be achieved.

15. Mr Frankie YICK enquired if there were other ways to reduce the tariff level apart from reducing the permitted RoR. SEN responded that apart from the permitted RoR, the tariff level could be affected by a host of factors. For instance, enhanced efforts on EE&C might reduce electricity consumption, while adoption of RE might have higher tariff implications. There were also views suggesting that the tariff approval mechanism should be tightened by extending the tariff approval to cover fuel costs.

16. Mr LEE Cheuk-yan expressed grave concern that the electricity customers had long been suffering from a high tariff level arising from the power companies' seeking to maximize their profits by yielding the permitted



RoR of 9.99%. He was very concerned whether the permitted RoR would be reduced in the new SCAs. SEN said that it was worth noting that the electricity tariff of Hong Kong was lower than that of many major cities in the world. Nevertheless, the Administration considered that there was a case to lower the permitted RoR in view of the current market conditions.

17. The Chairman remarked that the reason for a low tariff level in Hong Kong was due to its much lower investment on electricity distribution facilities since it had the highest density with the smallest geographical area among the major cities in the world. He recalled that the permitted RoR had been set in 15% in 1998 when the rates of interest and inflation were both double-digit high. However, it had not been reasonable for the permitted RoR to be set at 9.99% for the SCAs commencing in 2008. He shared Mr LEE Cheuk-yan's concern that the power companies sought to yield 9.99% of return as permitted to maximize their profits, and opined that reducing the permitted RoR was the most effective way to lower the tariff level.

18. In considering the basis for a reasonable return for the power companies, the Chairman highlighted the sluggish global economy with a decreasing investment return and a low interest rate. For example, the current 30-year United States Treasury yield was only 2% to 3% and the investment return of the Exchange Fund managed by the Hong Kong Monetary Authority was only 1.4% in 2014. In light of this, he considered that the permitted RoR in the new SCAs should be reduced to the level lower than the range of 6% and 8% as suggested by the Administration's consultant. He added that the permitted RoR should be reviewed once every five years.

19. SEN said that the electricity tariff in Hong Kong had been maintaining at a reasonable level and was significantly lower than that of other comparable cities like Singapore. The Administration would commission a consultancy study to revise the permitted RoR to the appropriate level having regard to the current global market conditions, as well as the return level of comparable power utilities in overseas jurisdictions. In response to the Chairman's enquiry, DSEN said that for the power utilities in Macao and some of the cities in Australia and the United States, their return rates in respect of power generation and distribution businesses ranged from 6% to 10%.

*Future regulatory and contractual arrangements – duration*

20. Mr Tony TSE enquired about the duration of the new SCAs which, in his opinion, was a crucial factor in determining the permitted RoR for the power companies. DSEN advised that the duration of the current SCAs was ten years, with an option exercisable by the Government to extend the term for five more

years to provide flexibility for making changes as necessary. The majority of the respondents in the Consultation supported maintaining the current arrangement. The Administration would take into account public views when negotiating the new SCAs with the power companies.

21. The Chairman considered that the duration of the new SCAs should be shortened to five years with an option to extend five years, given that the power companies had made huge investments and hence would continue to provide electricity supply service anyway. He also enquired about the duration of contractual agreements for electricity utilities in other jurisdictions. DSEN advised that the electricity markets in many overseas cities were liberalized and the power utilities did not enter into contractual agreements with the governments. On new investments by the existing two power companies, DSEN said that new generating units would need to be constructed to replace the retiring coal-fired generating units and to improve the fuel mix for electricity generation.

*Promotion of RE and demand side management*

22. Mr YIU Si-wing asked the Administration to give more information about the RE development and Mr Kenneth LEUNG enquired about the edge of Hong Kong in the use of solar power. Mr LEUNG also asked in addition to providing a higher permitted RoR for RE infrastructure investment (i.e. 11% instead of 9.99% for non-RE infrastructure investment), what other measures would be undertaken by the Administration to further promote the development of RE. Noting that before the introduction of the Public Consultation on the Future Fuel Mix for Electricity Generation in 2014, the Administration proposed a strategy of increasing the share of RE in the fuel mix to about 3%, Mr LEUNG considered such percentage too low, in particular if waste-to-energy was also included. He asked whether the Administration would consider requiring the power companies to adopt certain percentage of RE in their fuel mix in the new SCAs. In addition, he noted that while CLP Power Hong Kong Ltd. and Castle Peak Power Company Ltd. (collectively referred as "CLP") was willing to explore the introduction of smart metering, The Hongkong Electric Company Ltd. ("HEC") was not keen to the proposal. He urged the Administration to require both companies to install smart meters for their customers under the new SCAs. SEN took note of Mr LEUNG's request for consideration.

23. DSEN responded that developing large-scale solar energy might not be cost-effective due to the high capital cost and the geographical constraints of Hong Kong. The Administration considered it more effective to promote small-scale distributed RE generation. Based on the outcome of the Consultation, the community in general supported the development of

small-scale distributed RE generation. The Administration would draw up specific proposals for the new SCAs in respect of this area. With regard to the various waste-to-energy facilities completed or being planned, the RE generated was estimated to be able to meet about 1% of Hong Kong's total electricity demand by the early 2020s.

24. Mr LEE Cheuk-yan expressed concern about the grid access arrangement by RE generators. In response, SEN said that under the current SCAs, the power companies should allow grid access by distributed RE facilities to the existing power grids. However, the Administration considered that the existing arrangements should be improved to better facilitate grid connection for distributed RE generators to encourage their development, and the Administration would pursue this when negotiating with the power companies the future contractual arrangement. In response to Mr LEE's concern on the scale of such grid connection under the current SCAs, SEN said that such arrangement applied to the installation of solar panels on the roofs of multi-storey buildings and the scale of such connection could be large.

25. Mr YIU Si-wing requested the Administration to provide, in respect of a total of 15 762 submissions received in the Consultation, a summary of views categorizing respective views and concerns such as promotion of RE and energy saving, the nature and number of respondents providing such views for members' reference and follow-up. DSEN undertook to provide a written response after the meeting.

*(Post-meeting note: The Administration's response was issued to Members vide LC Paper No. CB(4)351/15-16(01) on 14 December 2015.)*

#### *Implementation of the new fuel mix in 2020*

26. Ir Dr LO Wai-kyok noted that the new fuel mix for electricity generation in 2020 would increase the percentage of natural gas to around 50%, and maintain the current interim measure to import additional 10%, i.e. from 70% to 80% of the nuclear output from the Daya Bay Nuclear Power Station ("DBNPS") so that nuclear import would account for around 25% of the total fuel mix. He enquired about the measures to be taken in the coming five years to tie in with the new fuel mix target, such as investment on new gas-fired generating units and/or infrastructure for importing the additional nuclear output from DBNPS.

27. DSEN said that both CLP and HEC would need to construct new generating units to meet the fuel mix target of increasing the proportion of

natural gas generation to around 50% in 2020. The Administration had given approval to HEC the construction of a new gas-fired unit which would be available in 2020. CLP was conducting an Environmental Impact Assessment on its new gas-fired unit, and it was estimated that CLP would submit its proposal for the Administration's consideration in 2016. He also understood that CLP had started negotiation with DBNPS on maintaining the current arrangement of importing 80% of the nuclear output from DBNPS after 2018.

28. Mr Kenneth LEUNG enquired if the Administration would adopt measures to encourage the installation of floating liquefied natural gas ("LNG") storage in Hong Kong by the power companies. DSEN advised that one of the power companies was studying the feasibility of installing a floating LNG terminal. The Administration would access the feasibility and cost effectiveness of such project as well as its implications on the environment and marine safety etc. upon receipt of the power company's proposal. Mr LEUNG urged ENB to take initiative, which might involve different bureaux and departments, to provide facilitation as early as possible in implementing the project. DSEN advised that other relevant departments were involved in the said study conducted by the power company, and the Administration would evaluate the project's feasibility when the final proposal was received.

29. Given that the existing gas supplies from Yacheng had been fast-depleting and the piped gas through the Mainland's Second West-East Natural Gas Pipeline ("WEPII") which was relatively more expensive would become the major gas source afterwards, Ir Dr LO Wai-kiwok enquired if the Administration would encourage power companies to explore other gas sources so as to address the long term need of gas for Hong Kong. DSEN replied that apart from gas supply via WEPII, the power companies were also exploring other new gas sources, with a view to diversifying the sources of gas supply.

### *Staffing proposal*

30. Noting that the supernumerary post of the Administrative Officer Staff Grade C in ENB proposed to be extended mainly focused on negotiating for a new set of SCAs, Mr Tony TSE expressed concern that the scope of duties might be too narrow. DSEN advised that apart from undertaking the negotiation with the power companies, the post proposed to be extended would also work with other teams in ENB on policy matters relating to promotion of RE and EE&C etc.

31. Mr YIU Si-wing opined that the staffing proposal would only be justified if new changes would be introduced to the electricity market with a view to making Hong Kong a more advanced city in terms of environmental

protection, and EE&C. In response, SEN remarked that while the current electricity supply had generally achieved the four energy policy objectives, the Administration would consider how to further improve the regulatory regime and draw up improvement proposals for the new SCAs on such areas of RE promotion and EE&C taking into account views received during the Consultation.

*Way forward*

32. Both the Chairman and Mr CHAN Kam-lam enquired about the timing for briefing Members the finalized terms of SCAs, in particular the level of permitted RoR before negotiating with the power companies. The Chairman cautioned that as it was running up to the expiry of the current SCAs in 2018, the Administration should speed up its work to finalize the proposed terms for the new SCAs without further delay. SEN replied that the Administration would take into account views received during the Consultation and the updated findings of the consultancy study on the permitted RoR when deciding the level of the permitted RoR. He also remarked that when negotiating with the power companies a new set of SCAs, the Administration would consider the permitted RoR together with other elements in the new regulatory arrangement as a package, having regard to the four energy policy objectives.

Conclusion

33. The Chairman concluded that the Panel was generally supportive of the Administration's staffing proposal. He also drew the Administration's attention to Members' concerns which should be taken into consideration for preparing the final proposal for the coming negotiation with the power companies.

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