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For discussion on 11 May 2015

Public Consultation on the Future Development of the Electricity Market

PURPOSE

This paper informs Members of a 3-month public consultation on the future development of the electricity market that the Administration launched on 31 March 2015. A copy of the consultation document is at **Annex**.

DETAILS

Background

2. The Scheme of Control Agreements (SCAs) entered into between the Government and the two power companies^[1] will expire in 2018. As provided in the SCAs, the Government has an option to extend the term of the SCAs for five more years, i.e. till 2023 either (a) on existing terms; or (b) on such amended terms as may be mutually agreed by the Government and the power companies before the expiry of the SCAs in 2018. The Government may introduce changes to the electricity supply regulatory framework after the expiry of the SCAs. Before implementing any changes to the electricity supply regulatory framework, the Government will take into account all relevant factors and discuss with the power companies market readiness, potential future changes to the electricity supply regulatory framework, and transition issues before 1 January 2016.

3. The Administration launched a public consultation on 31 March 2015 on the future development of the electricity market, which also sets out our plan to implement the fuel mix for electricity generation in 2020 having regard to the views received in the public consultation conducted in March – June 2014.

¹ The power companies are CLP Power Hong Kong Limited and Castle Peak Power Company Limited, as well as The Hongkong Electric Company Limited.

Our electricity market

4. **Chapter 1** of the consultation document gives a brief background of electricity supply in Hong Kong and highlights its performance against the four energy policy objectives of safety, reliability, affordability and environmental protection, as well as the current regulatory framework.

The review

5. **Chapter 2** sets out the background of the present review. In conducting the review of the future development of the electricity market, we are not only guided by the four energy policy objectives, but have also paid due regard to our goal to introduce competition to the electricity market when the requisite conditions are present. The present review builds on the various reviews and public consultations conducted over the past few years relating to electricity supply, including the mid-term review of the SCAs conducted in 2013, and the public consultation on the future fuel mix for electricity generation launched in 2014.

Readiness to introduce competition in 2018

6. **Chapter 3** sets out our observation of the experiences of Australia, Singapore, the United Kingdom and the United States in introducing competition to the electricity markets. Market liberalisation is a long, complex and evolving process, and delivered mixed outcomes when evaluated against our energy policy objectives. While we should not expect that introducing competition to the market would naturally lead to tariff reduction, it would allow consumers to have more choices. We consider that we should not change our goal to introduce competition to the electricity market.

7. **Chapter 4** gives an analysis of our readiness to introduce competition to the electricity market in Hong Kong in 2018. While a key determining factor is the availability of stable and reliable sources of new supply, there will unlikely be any substantial new source of electricity supply after the expiry of the current term of the SCAs in 2018. However, to pave the way for Hong Kong to introduce competition in the longer term, we plan to conduct the necessary preparatory work, which includes conducting a joint study with the power companies on grid access arrangements by new players, and a study on the detailed arrangements required to enhance the interconnection with the Mainland grid and between the local power grids.

Future regulatory arrangement

8. We have reviewed the regulatory arrangement, and set out in **Chapter 5** our views on the regulatory tool, the price setting mechanism to be adopted, and the features of the future contractual arrangement, including the permitted rate of return, tariff approval process, promotion of information transparency, incentive and penalty scheme to enhance power companies' performance, measures to promote energy saving and renewable energy, etc..

The future fuel mix

9. **Chapter 6** sets out our plan to implement the fuel mix for electricity generation in 2020 having regard to the views received in the public consultation conducted in March – June 2014. We plan to increase the percentage of natural gas generation to around 50%, and maintain the current interim measure to import 80% of nuclear output from the Daya Bay Nuclear Power Station such that nuclear import would account for around 25% of the total fuel mix. Subject to public views on the tariff implications, we are prepared to develop more renewable energy, and we will also enhance our efforts to promote energy saving. The remaining demand will be met by coal-fired generation. This will help us achieve the environmental targets for 2020.

10. **Chapter 7** provides a summary of the above and sets out the consultation questions to solicit public views. A response form is also provided in the consultation document, together with a report of the fuel mix consultation as the **Annex**.

PUBLIC CONSULTATION

11. The public consultation will last for three months until 30 June 2015. The Government keeps an open mind on the various issues, and would engage different stakeholder groups, including the academia, green groups, professional bodies and the business community to solicit their opinions.

ADVICE SOUGHT

12. Members are invited to provide comments on the public consultation on the future development of the electricity market.

Environment Bureau
May 2015