Scheme of Control Statement

CLP Power Hong Kong Limited and Castle Peak Power Company Limited

Overview

In Hong Kong, CLP Power Hong Kong Limited (CLP Power Hong Kong) operates a vertically integrated electricity generation, transmission and distribution business. The generating plants in Hong Kong are owned by Castle Peak Power Company Limited (CAPCO), which is 40% owned by CLP Power Hong Kong and 60% owned by ExxonMobil Energy Limited. CLP Power Hong Kong builds and operates CAPCO's power stations under contract and is the sole customer for CAPCO's electricity which CLP Power Hong Kong transmits and distributes to its customers in Kowloon and the New Territories. CLP Power Hong Kong owns the transmission and distribution network.

Since the financial year 1964, the electricity-related operations of CLP Power Hong Kong and CAPCO (the SoC Companies) have been governed by a Scheme of Control (SoC) Agreement with the Hong Kong Government. The SoC specifies the SoC Companies' obligations to supply adequate and reliable electricity supplies to customers at the lowest reasonable cost and the mechanism for the Government to monitor their financial affairs and operating performance. In return, CLP Power Hong Kong is allowed to charge tariffs designed to recover the operating costs (including tax) and allowed net return of the SoC Companies. The current agreement, which took effect from 1 October 1993, covers the period to 30 September 2008.

Permitted and Net Return

The permitted and net return that the SoC Companies are allowed under the SoC are calculated as follows:

- The annual permitted return is 13.5% of the SoC Companies' average net fixed assets relating to the electricity business in Hong Kong; plus a further 1.5% on the average net fixed assets financed by shareholders' investments and acquired after 30 September 1978.

- Any difference between the permitted return and the profit for SoC operations is transferred to or from a Development Fund. The Development Fund does not form part of distributable shareholders' funds and is, in effect, a liability owing to customers carried in CLP Power Hong Kong's books.

- Four charges are deducted from the permitted return. First, shareholders of the SoC Companies pay interest up to a maximum of 8% per annum on borrowed capital arranged for financing fixed assets. Second, shareholders of CLP Power Hong Kong pay a charge of 8% per annum on the sum of the average balances of the Development Fund and special provision account. This charge is credited to a rate reduction reserve in CLP Power Hong Kong's books and is applied as rebates to customers. By a Supplemental Agreement which took effect from 1 October 1998, two more charges have been introduced. Third, shareholders of the SoC Companies pay an excess capacity adjustment of 13.5% on the average excess capacity expenditure less an allowed interest charge up to 8% per annum on the average excess capacity expenditure. This excess capacity adjustment will only apply to additional generating units installed after the SoC Companies' Black Point Units 7 and 8 are commissioned. Fourth, shareholders of CLP Power Hong Kong pay interest up to 8% per annum on the increase in average balance of the customers' deposits in excess of the balance as at 30 September 1998.

- The net return is the permitted return less the deductions. The rate of return on average net fixed assets of the SoC Companies for the year ended 31 December 2004 was 13.05% (2003: 12.87%).

The net return is divided between the SoC Companies in accordance with the provisions of the agreements between the SoC Companies and ExxonMobil International Holdings Inc. These provisions state that each company will receive that proportion of the total net return represented by the net return that company would receive if it were the only company under the SoC and the net return were calculated solely on the basis of its own accounts. In year 2004, 60% (2003: 59%) of the net return was allocated to CLP Power Hong Kong and 40% (2003: 41%) to CAPCO. If the actual profit for the SoC, when added to the amount available for transfer from the Development Fund is less than the permitted return, the share of any such deficit to be borne by CAPCO is limited to 20%.

The calculations shown below are in accordance with the SoC and the agreements between the SoC Companies. The calculations are extracted from the audited accounts of CLP Power Hong Kong for the year ended 31 December 2004, upon which the auditors have expressed an unqualified opinion.

	2004 HK$M	2003 HK$M
SoC Revenue	**26,773**	25,739
Expenses		
Operating costs	**3,166**	2,817
Fuel	**3,482**	2,901
Purchases of nuclear electricity	**4,763**	5,134
Depreciation	**3,452**	3,439
Deferral premium	**176**	494
Operating interest	**415**	459
Taxation	**1,967**	1,652
	17,421	16,896
Profit after taxation	**9,352**	8,843
Interest on increase in customers' deposits	**–**	–
Interest on long-term financing	**679**	679
Adjustments required under the SoC (including share of profit on sale of electricity to the Chinese mainland attributable to the SoC Companies)	**35**	367
Profit for SoC	**10,066**	9,889
Transfer to Development Fund	**(219)**	(572)
Permitted return	**9,847**	9,317
Deduct interest		
On increase in customers' deposits	**–**	–
On long-term financing as above	**679**	679
On Development Fund and special provision account transferred to rate reduction reserve	**253**	287
	932	966
Net return	**8,915**	8,351
Divisible as follows:		
CLP Power Hong Kong	**5,363**	4,895
CAPCO	**3,552**	3,456
	8,915	8,351
CLP Power Hong Kong's share of net return		
CLP Power Hong Kong	**5,363**	4,895
Interest in CAPCO	**1,425**	1,386
	6,788	6,281