REPORT OF THE INTERNATIONAL ENERGY TRANSACTIONS COMMITTEE*

This Report summarizes two international arenas where important energy policy has emerged this year. The first section of this report discusses decisions by Canada's National Energy Board (NEB), addressing its policy on the export of natural gas and electric power to the United States. The NEB's decisions have a direct impact on domestic energy markets. The second section discusses steps the European Union (EU or the Union) is taking towards creating competitive energy markets among its member countries. The EU confronts many of the same regulatory issues that exist in the United States. Understanding the EU's models for creating and nurturing competitive markets can provide helpful guidance for managing domestic energy markets.

I. U.S.-CANADIAN ENERGY TRADE

Over two decades ago natural gas was discovered near Sable Island off the coast of Nova Scotia, one of the eastern Canadian provinces, and in 1999 natural gas began to flow from the Sable Offshore Energy Project (SOEP). More than half of the gas is exported to the northeastern United States. Early in 2002, the New Brunswick provincial government asked the NEB to reassess its policy for approving short-term exports of natural gas from the Scotian basin, arguing that a supply shortage was resulting and that Canadian natural gas purchasers were encountering difficulty in securing gas on the same terms and conditions as exports. In a September 2002 decision, the NEB rejected New Brunswick's call for greater regulatory control over short-term exports, but agreed to initiate closer monitoring of the operation of the maritime natural gas markets.¹

A. Background

Exports of natural gas from Canada must receive NEB approval, either by the granting of an export license or the making of a short-term export order. Section 118 of the National Energy Board Act (NEBA) requires the NEB upon application for a natural gas export license to "satisfy itself that the quantity of oil or gas to be exported does not exceed the surplus remaining after due allowance has been made for the reasonably foreseeable requirements for use in Canada having regard to the trends in the discovery of oil or gas in Canada."² Export licenses are issued for the export of natural gas for a period of more than

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^{1.} National Energy Board, Reasons for Decision, *Province of New Brunswick, Export Order Procedures*, MH-2-2002 (Sept. 2002) (Can.), *available at* https://www.neb-one.gc.ca/ll-eng/livelink.exe/fetch/2000/90466/94153/179387/179322/238312/238298/A0F7A5_-_Reasons_For_Decision. pdf?nodeid=238299&vernum=0 (last visited Sept. 12, 2003) [hereinafter NEB Decision].

^{2.} National Energy Board Act, R.S.C., ch N-7, § 118 (2003) (Can.).

two years. The NEB assesses applications for export licenses according to a Market Based Procedure (MBP), the fundamental premise of which is that the marketplace will generally operate in such a way that Canadian requirements for natural gas will be met at fair market prices. Procedures under the MBP enable Canadian natural gas purchasers to intervene in an application for a natural gas export license (via a complaints procedure) if they believe they have not been able to purchase natural gas on terms and conditions similar to those of the proposed export. No complaints have been made since the introduction of MBP in 1992. The MBP also includes an ongoing monitoring component through which the NEB undertakes periodic assessments of the long-term outlook for energy supply and demand in Canada.

Applications for the export of natural gas under short-term orders of less than two years follow a more streamlined procedure under the National Energy Board Part VI (Oil & Gas) Regulations (NEBR).³ The NEBR were designed to facilitate short-term trade in natural gas with a minimum of regulatory intervention. They permit the Board to include in short-term orders the terms and conditions respecting the point of exportation and "the maximum daily, monthly, annual and term quantities of the gas that may be exported."⁴ The NEB does not have the authority to place conditions with respect to pricing, nor does a complaint procedure exist for short-term exports. Since 1991 the NEB has approved blanket short-term export orders that provide natural gas exporters with the ability to export gas at multiple export points.

B. NEB Review of Natural Gas Export Policy

In February 2002, the Province of New Brunswick filed an application with the NEB requesting a hearing to establish more stringent rules for considering applications of short-term export orders for incremental supplies from the Scotian basin when those supplies cannot meet both Canadian and export requests for service.⁵ New Brunswick proposed that the NEB's MBP for longterm export licenses also apply to applications for short-term export orders and that procedures be implemented to allow any person to make a complaint against an application for a short-term export order for incremental Scotian gas. New Brunswick further advocated that the NEB reserve the right to "bump-up" any application for a short-term export order to a public hearing, as would be held in respect of a long-term license, and that the Board decide short-term applications in accordance with the same criteria it applies under section 118 of the NEBA for long-term natural gas export licenses.⁶ Contending that gas buyers in the Canadian maritime provinces were having difficulty accessing Scotian offshore natural gas because of tightness in supply and a regional market characterized by the dominance of a small handful of producers, New Brunswick argued that

^{3.} National Energy Board Act, Part VI (Oil and Gas) Regulations, S.O.R./96-244 (1996) (Can.).

^{4.} Id. §16(g).

^{5.} Province of New Brunswick, Application under Paragraph 12(1)(b) and Subsection 21(1) and 24(3) of the National Energy Board Act, (2002) (Can.), available at https://www.neb-one.gc.ca/lleng/livelink.exe/fetch/2000/90466/94153/179387/179322/191872/193720/application_(AOEOC2)

[.]pdf?nodeid=193721&vernum=0 (last visited Sept. 12, 2003) [hereinafter Application].

^{6.} Id. at 2-3.

exports from the maritime supply basin required a more stringent level of scrutiny to ensure that Canadian natural gas purchasers enjoyed the same access as exporters to such supplies.⁷

The Scotian basin is a relatively new gas field. A consortium of producers, the SOEP, began production from fields in late 1999. Maritimes & Northeast Pipeline Management Ltd. (M&NP) received regulatory approval to construct natural gas transmission lines from the Scotian basin (through Nova Scotia and New Brunswick to the Maine border where the gas continues on to the Boston market). Of the total firm contracted load on M&NP's transmission system, approximately 65% is contracted to the New Brunswick/Maine border export point. Efforts to construct a local distribution system in Nova Scotia have stalled, but M&NP has constructed a number of lateral lines in New Brunswick for delivery of natural gas to the local franchised distributor. New Brunswick argued before the NEB that some developers of gas-fired electricity generation projects in northern New Brunswick had been unable to procure long-term commitments of gas from the Scotian basin because of tightness of supply.⁸

In its September 2002 decision, the NEB stated that an adequate supply of Scotian gas exists to maintain the current level of deliveries to the domestic and export markets for approximately thirteen years.⁹ In the NEB's view, however, the outlook for incremental supply remains very uncertain. Although, gas from the recently discovered Deep Panuke field could double current production rates from the Scotian basin, a short flat life and steep production decline are projected for the field.¹⁰ Nevertheless, the Board noted that maritime gas consumption has been increasing and that Canadian gas buyers have been reselling natural gas in excess of their requirements into the export market. In the Board's view, this fact provided a strong indication that Canadians had adequate access to natural gas supplies in current gas markets and suggested that short-term export orders have provided Canadians with a suitable means to manage their purchases of natural gas.¹¹

While the NEB stated that New Brunswick did not produce any direct evidence that Maritime gas buyers failed to have access to Scotian natural gas supplies on terms and conditions similar to those in the export market, it did share New Brunswick's concerns about several unique difficulties associated with the Scotian basin market. These concerns included the fact that: buyers do not have the option of purchasing gas from a wide range of selling agents; no access exists to an upstream hub in the Maritimes that would provide high liquidity and price transparency; a mismatch exists between the expected production profile of incremental gas supply and domestic market requirements for a secure long-term source of supply; and the expansion economics of the mainline appear to favor incremental sales of gas to the U.S. over the construction of new laterals in Canada. Nonetheless, the NEB expressed the

8. NEB Decision, *supra* note 1, at 6.

- 10. NEB Decision, supra note 1, at 16.
- 11. Id. at 31.

^{7.} Application, supra note 5, at 2.

^{9.} Id. at 11.

view that, the fact that Canadians pay fair market prices for natural gas in the context of the North American market is a key indicator that Canadian public interest is being served.¹² The NEB reiterated its policy to develop regulatory procedures that are both compatible with and support market-oriented trade and energy policies, and emphasized that its regulatory approach must not impede the development of new gas supplies.¹³ Consequently, the NEB "decided that it would be inappropriate at this time to implement procedures that would unduly interfere with the normal operations of the market."¹⁴ The NEB therefore rejected New Brunswick's efforts to change the procedures and criteria for the approval of short-term export orders.

While the NEB was not prepared to change its procedures for short-term export orders, it did agree to enhance its ongoing monitoring of the Maritime gas market in light of the market's unique characteristics. The NEB intends to publish public reports on the state of the market before July 31, 2003. In addition, to improve price transparency in Maritime Canada, the Board will publish additional data gathered from the reports it receives on a monthly basis from export order holders.¹⁵

C. NEB Policies on Electricity Exports

The NEB's commitment to relying on market mechanisms to ensure the adequacy of energy supplies to Canadian consumers has also been reflected in its recent approach to electricity exports. The NEB requires an electricity export permit applicant to meet a "fair market access" test. Under this test the applicant must demonstrate that it has afforded to Canadian producers (with transmission access), who have demonstrated an intention to buy electricity for consumption in Canada, an opportunity to purchase electricity on terms and conditions as favorable as those offered to an export customer.¹⁶ On May 1, 2002, the Province of Ontario implemented a competitive power market under which an independent system operator, the Independent Electricity Market Operator (IMO), directs the operation of the province's transmission systems and administers a bid-based, security constrained real-time energy market that includes the import and export of electricity. Prior to market opening an issue arose as to which entities would have to secure electricity export permits from the NEB for any power exported from Ontario to the United States through the IMO-administered market. The NEB accepted the argument that the IMO should be the licensed exporter because its bid-based real time energy market would satisfy the "fair market access" test for market-based price signals by providing the opportunity for any Ontario power consumer to bid for its required energy through the IMO-administered market. Accordingly, the NEB appears committed to relying on market mechanisms to ensure that Canadian energy

^{12.} NEB Decision, *supra* note 1, 31-32.

^{13.} *Id.* at 40.

^{14.} NEB Decision, *supra* note 1, at 40

^{15.} Id. at 42.

^{16.} National Energy Board, Reasons for Decision, *Ontario Hydro*, EW-3-90, (April 1991) (Can.); National Energy Board Decision, *PowerEx*, File No. 6200-B007-5 (Sept. 1996) (Can.).

II. EUROPEAN UNION LIBERALIZATION DEVELOPMENTS

In the last several years, EU and its Member States have taken major steps towards instituting an open-access transportation regime for both electricity and natural gas. In Europe, this process of opening markets to competition is frequently termed "liberalization," a usage that will be followed here. The liberalization process began many years ago. However, the pace of change has accelerated in recent years, due in part to the European Council's adoption in 2000 of the goal of making the EU economy "the most competitive . . . economy in the world" by the year 2010.¹⁷

Liberalizing the energy markets in Europe is being accomplished by implementation of the electricity and natural gas restructuring directives adopted in 1996 and 1998 respectively.¹⁸ In addition, the EU has institutionalized the reform process through the so-called Florence and Madrid Forums, which have led to proposals to adopt an amended energy Directive in 2003 that would seek to harmonize and enhance the restructuring of the two industries in an overtly parallel and coordinated fashion.

This restructuring process has distinct political, legal, and institutional dimensions. The political dimension defines the overall context within which the decisions governing restructuring policies take place. The legal dimension consists of the legal rules governing restructuring. In the case of the EU this refers principally to: the Directives adopted by the European Commission; the implementing legislation adopted and implemented by each of the Member States "transposing" the EU directives into national statutory law; regulatory changes adopted by the national governments under the new statutes (including regulations issued by the newly created regulatory authorities); and tariff and contractual changes implemented by transmission entities.

The institutional dimension consists of various new institutions created or adapted to fill roles required by a restructured industry. These new institutions arise along a continuum that ranges from entities that are entirely governmental (e.g., regulatory commissions or authorities), to entirely private (e.g., trade associations), with various combinations of the two (e.g., a power grid manager owned by, but separated from, a governmentally owned utility, or a power exchange jointly owned by a governmentally controlled independent system operator together with a private clearing exchange services provider). Developments in each of these areas are discussed in turn.

^{17.} PRESIDENCY CONCLUSIONS, LISBON EUROPEAN COUNCIL (Mar. 23-24, 2000) ¶ 5, available at http:// ue.eu.int/newsroom/LoadDoc.asp?MAX=1&BID=76&DID=60917&LANG=1 (last visited Sept. 12, 2003). At Lisbon, the European Council explicitly called for the EU and its Member States to speed up liberalization in areas such as gas and electricity. *Id.* at ¶ 17.

^{18.} Council Directive 96/92/EC 1996 O.J. (L 27), available at http://europa.eu.int/smartapi/cgi/sga_doc? smartapi!celexapi!prod!CELEXnumdoc&lg=en&numdoc=31996L0092&model=guichett (last visited Sept. 12, 2003) [hereinafter Power Directive]; Council Directive 98/30/EC 1998 O.J. (L 204), available at http://europa.eu.int/eur-lex/pri/en/oj/dat/1998/1_204/1_20419980721en00010012.pdf (last visited Sept. 12, 2003) [hereinafter Gas Directive].

A. The Political Dimension

The EU has undergone enormous changes over the last few years that are being reflected in equally fundamental changes in its size, composition, and institutional arrangements. While these changes are far outside the scope of this report, the most salient must at least be mentioned since the changes in energy regulation cannot be properly understood without reference to them.

1. The Reunification of Germany, the Dissolution of the Soviet Union, and the Integration of Eastern Europe into the West

These three developments over the last decade frame the future of the EU and underlay the organizational restructuring that is just beginning and whose outcome is still unclear.

a. German Reunification

The demographic change from reunification (Germany's population rising from less than sixty, to more than eighty million) suddenly made Germany much larger than Italy, France, or Britain, disrupting the traditional demographic parity among this group. While reunification promised in the long-run to expand significantly the role of Germany within the EU, the economic difficulties of integrating East Germany (coupled with political and intellectual focus on reunification), have tended to push in quite the opposite direction.

b. Dissolution of the Soviet Union and the Integration of the East

The dissolution of the Soviet Union and the collapse of the Soviet empire in Eastern Europe created a huge economic and political vacuum. The Member States of the EU have moved to fill this vacuum by expanding the Union to include nearly all of the former Eastern Bloc countries, as well as the former Soviet Baltic republics. Pursuant to decisions taken during 2002, the EU will expand in 2004 to include some ten additional countries, creating a political and economic entity of some twenty-five nations and roughly 450 million people.

It is rather astonishing that the fifteen Member States of the existing EU have invited ten sovereign nations to join the Union before the incumbent members have even agreed among themselves on the governing structure of that expanded union. This is a wager of continental proportions. Presumably, the EU nations reasoned that, however great the risks of bringing the new members into the Union with so much left undecided, the risks of allowing a political and economic vacuum to develop (along the EU's eastern frontier and the frontier with the former Russian Soviet Socialist Republic) were greater. At the same time, this expansion process has had a tendency to shift the geographic, economic, and intellectual center of the EU to the east and the south, reducing the transatlantic element that had played such a large role in the post WW II era. These new Member States are sometimes called "New Europe" because they are joining the EU decades after the founding six countries. As seen below, this shift of focus east, and to the Mediterranean world, is already beginning to have very concrete consequences for European energy policy, particularly with regard to infrastructure.

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2. The European "Constitutional Convention"

The expansion of the Union is expected to require changes in the underlying governing structure. It is widely recognized, for example, that the existing requirement of unanimous consent of all Member States for most decisions will be largely unworkable in a Union of twenty-five States. Similarly, questions arise with regard to the role of the executive power, which is currently exercised essentially by committee in the form of the European Commission, not to mention "foreign policy" will be developed and implemented.

Consequently, in late 2001, the EU instituted the European Convention (often referred to as the "Convention on the Future of Europe"). The purpose of the Convention is to propose a new constitution for the Union that will simplify and supersede the existing treaties.¹⁹ The Convention is more of a consultative committee than the one-time convention in Philadelphia that drafted the U.S. Constitution in 1789. It is headed by former President of the French Republic, Valéry Giscard d'Estaing, and includes approximately 102 representatives (including representatives from the candidate countries expected to join in 2004).

A preliminary draft of the Constitution was published for public comment in October of 2002.²⁰ This draft was indeed preliminary and discussions are continuing with regard to a host of fundamental issues such as: the nature of the Union's executive power; whether it will be exercised by one or more individuals (or a group); and how (and by whom) the executive leadership will be chosen. While there is no formal deadline for proposing a new constitution, the expectation is that a text will be proposed to the heads of state and governments at their meeting in June of 2003. This will leave time for the Member States to reach final agreement prior to the entry of the new Member States in early 2004.

With regard to the implications for the legal structure governing liberalization of the gas and electricity industries, the new Constitution is not expected to have any direct impact or to modify any of the existing EU openaccess directives. Nonetheless, the creation of new political institutions, or voting and representational arrangements, may lead to significant changes in the manner in which these rules are interpreted and applied. In addition, the new Member States, because of their desire to make up for the economic gap resulting from decades of relative economic isolation (e.g., Spain and Portugal), or Soviet and Communist Party control (as in the case of the former Eastern Bloc countries), may be more open to market-based solutions for energy networks than some of the founding Member States. They may perhaps be more inclined than some of the major incumbent states to take risks in order to gain the

20. The October 2002 draft is available at http://register.consilium.eu.int/pdf/en/02/cv00/00369en2.pdf (last visited Sept. 12, 2003).

^{19.} The homepage of the Convention is available online at http://european-convention.eu.int (last visited Sept. 12, 2003). The European Council took the decision in December of 2001 in the LAEKEN DECLARATION ON THE FUTURE OF THE EUROPEAN UNION (Belgium, Dec. 15, 2001), available 'at http://europa.eu.int/futurum/documents/offtext/doc151201_en.htm (last visited Sept. 12, 2003). A useful gateway to a large number of the pertinent Convention documents (including the many comments submitted by various organizations, companies and individuals) is found at http://europa.eu.int/futurum/documents/contrib/c onv en.htm (last visited Sept. 6, 2003).

promised benefits of more flexible and competitive markets. The revised political and institutional arrangements under the new Constitution are likely to give a larger voice to these Members States. Consequently, expansion could tend to alter the political dynamics with regard to liberalization of energy markets and favor greater reliance on competitive, market-based approaches.

B. The Legal Dimension

1. The Original Electricity and Gas Directives

The transition to open-access in Europe actually began very shortly after the policy initiatives of the Federal Energy Regulatory Commission (FERC) in 1985. Thus, in May 1989 the United Kingdom (U.K.) energy regulator, acting pursuant to the Gas Act of 1986, issued its first direction requiring a transporter to provide open-access transportation service.²¹

By the mid to late 1990s, a sufficient consensus had developed among EU members to support the adoption of the current legal foundation for open-access transportation, the Electricity and Gas Directives, issued in 1996 and 1998 respectively.²² Both Directives adopted a general policy of moving towards an open-access regime on a gradual, phased basis. Both Directives left the individual Member States considerable flexibility as to the implementation of the new policies within a framework of broadly defined objectives and principles. In essence, the Directives required each Member State to "transpose" the general EU rules and policies into binding national law by certain deadlines (in general, February 1999 for electricity and August 2000 for natural gas). Certain aspects of the Directives, however, have binding legal force on their own, even without transposition into national law. For example, the basic grant of grid access to certain categories of end-users falls into this category. Ultimate implementation is effected through administrative regulations pursuant to the newly enacted statutes.

This transposition and implementation process has proceeded reasonably smoothly, albeit with some noteworthy exceptions. In Germany, for example, the necessary statute was adopted, but successful entry of competitive new suppliers was significantly delayed due to provisions in implementing agreements that were unfavorable (and the absence of a regulatory commission

22. The European Commission on Energy homepage for internal electricity market is found at http://europa.eu.int/comm/energy/electricity/index_en.htm (last visited Sept. 15, 2003). The European Commission on Energy homepage for internal natural gas market is found at http://europa.eu.int/comm/energy/gas/index_en.htm (last visited Sept. 15, 2003).

^{21.} COMPETITION COMMISSION, GAS AND BRITISH GAS PLC: VOLUME 2 OF REPORTS UNDER THE GAS AND FAIR TRADING ACT, 120 (1993), available at http://www.competition-commission.org.uk/rep_pub/reports/ 1993/fulltext/337c5.pdf (last visited Sept. 15, 2003); COMPETITION COMMISSION, GAS AND BRITISH GAS PLC: VOLUME 2 OF REPORTS UNDER THE GAS AND FAIR TRADING ACT, APPENDIX 5.1, 345 (1993), available at http://www.competition-commission.org.uk/rep_pub/reports/1993/fulltext/337a5.1.pdf (last visited Sept. 15, 2003). This 1993 Competition Commission report provides an exhaustive review of early efforts to implement open-access for natural gas in the United Kingdom. The full text of the report may be found at http://www.competition-commission.org.uk/rep_pub/reports/1993/337gas.htm (last visited Sept. 15, 2003). Interestingly, the application was made by AGas, the U.K. affiliate of the American marketing company, Hadson Gas Systems, Inc., providing an indication of how the open-access paradigm spread.

tasked to oversee successful implementation of an open-access policy). In France, as well, there was considerable delay in adopting the necessary transposing statutes.²³ In these, and a few other instances, the European Commission commenced so-called "infringement" procedures against certain Member States for failure to implement the Directives, at least two of which (Germany and France for noncompliance with the Gas Directive) were still unresolved in late 2002.²⁴

2. Benchmarking Reports on Implementation to Date

At the 2002 European Council meeting in Barcelona, the EU Commission Staff presented an initial benchmarking report on the progress in implementing the open-access policies.²⁵ The Council welcomed the first benchmarking report and called for it to become an annual review conducted prior to each spring meeting. A second benchmarking report was drafted in the second half of 2002 and is now available as a staff working paper.²⁶

These reports are likely to become an indispensable reference for anyone interested in tracking the evolution of European energy restructuring. Consistent with the move towards harmonizing the access policies for the two industries, the benchmarking reports track developments for both natural gas and electricity, and present the results in a comparable format. The reports thus present detailed statistics on the percentage of customers eligible for competitive supply, and the percentage that have switched to a competitive supplier (or renegotiated their arrangements with the traditional supplier), as well as data on the evolution of prices. Of particular interest are the tables that provide a concise snapshot of the policy judgments made by each of the Member States on ten separate issues, nearly all of which have been faced by U.S. state and federal regulators.

In general, the reports show that a relatively large percentage of large industrial and commercial users had taken advantage of competitive supply

^{23.} The law transposing the Electricity Directive was adopted in February of 2000, about one year after the deadline, while the law transposing the Gas Directive was adopted in January of 2003, nearly two and a half years after the deadline.

^{24.} Procedures were commenced for failure to adequately transpose both the Electricity Directive (against Belgium and France) and the Gas Directive (against Luxembourg, Portugal, Germany, and France). An "infringement" proceeding is a process by which the European Commission may seek to encourage Member States to comply with Directives. The process has several phases that commence with an official warning letter and can lead eventually to formal action to compel compliance before the European Court of Justice. The status of infringement proceedings involving the internal market may be followed at http://europa.eu.int/comm/internal_market/en/update/infr/index.htm (last visited Sept. 15, 2003). In addition, the Secretariat General of the European Commission keeps a register of infringement cases, which is available online, *at* http://europa.eu.int/comm/secretariat_general/sgb/droit_com/index_en.htm (last visited Sept. 15, 2003).

^{25.} EUROPEAN COMMISSION STAFF, FIRST BENCHMARKING REPORT ON THE IMPLEMENTATION OF THE INTERNAL ELECTRICITY AND GAS MARKET (Commission of the European Communities, Working Paper, Dec. 3, 2001); *available at* http://europa.eu.int/comm/energy/en/internal-market/library/reports/report-amended_en.pdf (last visited Sept. 15, 2003).

^{26.} EUROPEAN COMMISSION STAFF, SECOND BENCHMARKING REPORT ON THE IMPLEMENTATION OF THE INTERNAL ELECTRICITY AND GAS MARKET (Commission of the European Communities, Working Paper, Apr. 7, 2003), 1038, *available at* http://europa.eu.int/comm/energy/electricity/benchmarking/doc/2/sec_2003_4 48_en.pdf (last visited Sept. 12, 2003) [hereinafter SECOND BENCHMARKING REPORT].

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alternatives as of mid-2002, but that effective competition among smaller users remained very limited or non-existent (outside of the U.K.).²⁷ For natural gas, the extent of large customers switching to competitive suppliers was equally modest, with smaller customers simply not being eligible to purchase competitive supply in all but three countries.²⁸

3. The Madrid and Florence Forums on Implementation

Both Directives contemplated further reports to the Council of the EU (Council) and European Parliament, and potential changes and improvements in the regulatory structure. To assist in this ongoing process, the Commission instituted parallel consultative forums, which are known as the Florence and Madrid Forums (Florence for electricity; Madrid for gas).

Both forums convene twice a year in the respective cities. In attendance are representatives from national regulatory authorities, Member States, the European Commission, Transmission System Operators, gas suppliers and traders, consumers, network users, and gas exchanges. The forums are intended to complement the reforms required by the Directives and to focus on how, in practice, the Member States can ensure competition and nondiscrimination. In addition, they tend to address issues associated with cross-border trade in electricity and natural gas, rather than the retail issues that are the focus of many Directives.²⁹ For example, the October 2002 Florence Forum focused largely on issues of congestion management and locational pricing mechanisms that would not be unfamiliar to most FERC electricity practitioners.³⁰

4. The November 2002 Agreement and Amended Directives Proposed for 2003

In light of the experience of the past half-dozen years, the EU has been considering revisions to the Electricity and Gas Directives to complete the restructuring of the two industries. An initial draft was presented to the European Parliament and the Council in March of 2001.³¹ Following formal and informal consultation and comment procedures, which included, among other things, the European Parliament's adoption of a series of recommended amendments, the Commission issued a revised proposal in the summer of

30. See, e.g., THE CONCLUSIONS OF THE NINTH MEETING OF THE EUROPEAN ELECTRICITY REGULATORY FORUM ROME (2002), available at http://europa.eu.int/comm/energy/electricity/florence/doc/flor ence9/conclusion/draft conclusions.pdf (last visited Sept. 5, 2003).

31. PROPOSAL FOR A DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL AMENDING DIRECTIVES 96/92/EC AND 98/30/EC CONCERNING COMMON RULES FOR THE INTERNAL MARKET IN ELECTRICITY AND NATURAL GAS (2001), available at http://europa.eu.int/comm/energy/en/internal-market/library/directive_en_acte.pdf (last visited Sept. 5, 2003).

^{27.} Id. at 8, Table 4, Switching Estimates for the Period 1998-2001.

^{28.} SECOND BENCHMARKING REPORT, supra note 26, at 8.

^{29.} Each forum maintains a website, each of which contains a very useful collection of materials presented at the forums, contributions by interested participants, and conclusions and recommendations for further reform initiatives. The website for the Florence Forum on electricity is http://europa.eu.int/comm/energy/electricity/florence/index_en.htm (last modified July 16, 2003). The website for the Madrid Forum on natural gas is http://europa.eu.int/comm/energy/gas/madrid/index_en.htm (last modified July 16, 2003).

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In November of 2002, the Energy Ministers of the EU took up the matter, announcing an agreement on accelerating the opening of natural gas and electricity markets. Under the November 2002 ministerial agreement, both electricity and gas markets will in general be fully liberalized by July of 2004 for all non-residential customers, with residential customers gaining at least the formal right of access to competitive supply by July 1, 2007 at the latest.³³ With regard to the degree of unbundling between the competitive and the regulated functions, the ministerial agreement rejected calls for mandating divestiture, choosing instead to require at least a legal separation of the competitive and the regulated functions.³⁴ This legal separation requirement means that the transportation and distribution functions will be required to be conducted through an affiliate that is legally separate from the competitive generation or The obligation to implement legal unbundling at the supply function. transmission level will go into effect by July of 2004, while the obligation to unbundle at the distribution level will be imposed in July of 2007.³⁵

The accord also endorsed retail labeling requirements as to fuel source and carbon dioxide emissions that are roughly analogous to those adopted by a number of U.S. retail regulatory schemes.³⁶

Also of particular note to the American practitioner is the fact that the revised Directive will address changes in both the electricity and the gas industries in a single document. The EU Commission has been fairly adamant in maintaining an integrated policy towards liberalization of the two industries. Thus, in June of 2002, the EU Commission had justified its rejection of some two dozen amendments sought by the EU Parliament on the grounds that they implied the splitting of the proposed Directive into separate Directives for each industry.³⁷

The electricity and gas markets are increasingly interdependent and should

33. LOYOLA DE PALACIO, EUROPEAN ENERGY MARKET REVOLUTIONIZED, IP/02/1733, 1 (2002), available at http://europa.eu.int/rapid/start/cgi/guesten.ksh?p_action.getfile=gf&doc=IP/02/1733|0|AGED&lg= EN&type=PDF (last visited Sept. 9, 2003) [hereinafter ENERGY MARKET]. Exceptions are expected to be available for certain cases (such as in those countries with very limited development of natural gas, and for small distributors (with fewer than 100,000 customers)). In addition, a report on the experience under the revised Directive is to be provided in 2006. This report could lay the predicate for further revisions to the Directive prior to the 2007 date for opening access to all customer classes. For a summary of the evolution of the proposed revised Directive see Christopher Jones and Nathalie Vande, *Commission Proposals on Completing the Internal Market*, Workshop on the Internal Market for Gas for the Candidate Countries – Brussels (2002), available at http://europa.eu.int/comm/energy/gas/workshop_2002/doc/external_commission/ 01.pdf (last visited Sept. 12, 2003).

36. ENERGY MARKET, supra note 33, at 1.

^{32.} AMENDED PROPOSAL FOR A DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL AMENDING DIRECTIVES 96/92/EC AND 98/30/EC CONCERNING RULES FOR THE INTERNAL MARKETS IN ELECTRICITY AND NATURAL GAS; AMENDED PROPOSAL FOR A REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL ON CONDITIONS FOR ACCESS TO THE NETWORK FOR CROSS-BORDER EXCHANGES IN ELECTRICITY (2002), *available at* http://europa.eu.int/comm/energy/en/internal-market/2002-06-14/reg110_en.pdf (last visited Sept. 5, 2003) [hereinafter AMENDED PROPOSAL].

^{34.} ENERGY MARKET, supra note 33, at 1-2.

^{35.} Id.

^{37.} AMENDED PROPOSAL, supra note 32, at 10.

therefore be treated in parallel. The majority of new power generation plants are gas fired. Confronting actors working on both markets with two separate sets of rules would severely hamper the efficient functioning of the internal market. Furthermore, there is a risk that the splitting of the proposal would lead to a divergence in the dates of adoption.

This is the approach followed by the November 2002 ministerial accord. If the new Directive is approved is should become final during 2003.

5. Cross-Border Trade and the Trans-European Networks

The November 2002 meeting also produced agreement on a draft regulation on cross-border electricity exchanges. The cross-border tariff rules are to address rate "pancaking," seams issues, and congestion management for electricity.

A summary of the EU developments would not be complete without at least mentioning the significant efforts underway to expand the gas and electricity infrastructure to support inter-State commerce and trade (the Trans-European Energy Networks project).³⁸ The EU authorities have designated a list of "priority projects" that will benefit from EU level financial support. Seven of these projects address critical bottlenecks to electricity flows, while the remaining five are deemed essential to natural gas supply.

C. The Institutional Dimension

1. Creation of Regulatory Bodies

Both of the original Directives from 1996 and 1998 required Member States to "designate a competent authority... independent of the parties, to settle"³⁹ disputes relating to the terms and conditions of access, as well as to establish "appropriate and efficient mechanisms for regulation, control and transparencey" so as to avoid any abuse of a dominant position and any predatory behavior.⁴⁰

The prospect of creating fifteen new regulatory bodies obviously posed issues of choice of law and conflicting jurisdiction. The Gas Directive provided that in the event of a cross-border dispute, the dispute will be settled by the regulatory authority covering the gas system that has refused access.⁴¹ In the event of refusals from systems in more than one Member State, the authorities of the respective States are directed to consult with each other "with a view to ensuring that the provisions of [the] Directive are applied consistently."⁴²

Both Directives allow for a member State to temporarily take "necessary

^{38.} The gateway to documentation on the Trans-European Energy Networks is found at http://europa.eu.int/comm/energy/ten-e/en/index.html (last visited Aug. 19, 2003).

^{39.} Gas Directive, supra note 18, at Article 21 \P 2 (requirement to settle such disputes "expeditiously"); Power Directive, supra note 18, at Article 20 \P 3.

^{40.} Gas Directive, *supra* note 18, at Article 22; Power Directive, *supra* note 20, at Article 22. See also Gas Directive, *supra* note 18, at Article 23 (requiring an independent authority to settle disputes relating to access to upstream pipeline networks).

^{41.} Gas Directive, *supra* note 18, at Article 21 ¶ 3.

^{42.} Id.

safeguard measures" in the event of a sudden crisis in the energy market or where the physical safety or security of persons, apparatus or installations, or system integrity is threatened.⁴³

As of year-end 2002, all of the Member States, except for Germany, had fulfilled this aspect of the Directives and created a regulatory authority. While the American practitioner is apt to assign the mental tag Public Utility Commission (PUC) to these new entities, in fact the responsibilities and powers may vary materially from the typical American PUC and from one authority to another. While the regulatory authority is required to be independent of the industry it regulates, there is no requirement that it be independent of the executive branch. This allows for Member States to craft varying roles for the regulator. For example, the executive branch of the French government may make known government policies to the regulator, the Commission de Régulation de l'Énergie (CRE). Indeed, the executive branch representative may even put items on the CRE's agenda and the statute provides that the Commission is required to address such matters. On the other hand, the statute is equally clear in stating that the executive branch representative may not participate in the deliberations of the CRE and that the commissioners themselves must act entirely impartially, and without any instructions from the administration.44

2. Creation of the Council of European Energy Regulators (CEER)

One of the intriguing differences between implementation of "liberalization" in the EU and "deregulation" or "restructuring" in the U.S. is the lack of an "interstate" regulator in the EU. At present, all of the energy regulators are creatures of a national government, each being a Member State of the EU. Hence, there is no EU regulator of "inter-state" transmission with "local distribution" left to the "states." Rather, each of the Member State regulators may regulate high-pressure/high-voltage transmission assets, *as well as* low-pressure/low-voltage distribution lines. This lack of EU wide regulation of inter-State transmission and sales clearly puts a premium on coordination among the Member State regulators. The EU authorities have addressed this need through a consultative organization known as the Council of European Energy Regulators (CEER), created in March of 2000.⁴⁵ By the end of 2002, all regulatory authorities of the EU Member States (except for Germany) were members of the CEER, as well as authorities of some of the candidate countries.

Among its top objectives are the promotion "of efficient electricity and gas

^{43.} Gas Directive, supra note 18 at Article 24; Power Directive, supra note 18, at Article 23.

^{44.} Compare Article 29, with Article 35 of the LOI No. 2000-108, J.O. No. 35 (2000), available at http://www.legifrance.gouv.fr/WAspad/UnTexteDeJorf?numjo=ECOX9800166L (last visited Sept. 12, 2003). This balance is in substance quite similar to the approach taken in the U.S. Department of Energy Organization Act, which allows for the Energy Secretary to propose rules that the FERC may then decide to issue, based on its independent rulemaking record and deliberations. Compare 42 U.S.C. § 7171(d) (2003) (FERC commissioners and staff not subject to supervision or direction of any officer or employee of the Department of Energy), with 42 U.S.C. § 7173(b) (2003) (FERC required to act on any rulemaking proposed by the Secretary within reasonable time limits prescribed by the Secretary).

^{45.} The CEER homepage is found at http://www.ceer-eu.org/ (last visited Sept. 12, 2003).

markets in Europe" and cooperation among the regulators to achieve competitive European markets in electricity and gas in order to "reinforce and follow up the processes of liberalisation in the electricity and gas markets."46 Thus, the CEER differs fundamentally from U.S. National Association of Regulatory Utility Commissioners (NARUC) in that the CEER's very purpose is to help implement the basic political objectives of opening electricity and gas markets to competitive, nondiscriminatory access. In contrast, the NARUC was formed decades before the development of the open-access paradigm and has no institutional responsibility to implement national energy policy, whether that policy is developed by the executive branch (i.e., the Department of Energy) or by the national regulatory commission, (i.e., the FERC). This political structure means that while the EU may have taken longer to adopt an open-access policy than did the U.S., it may be able to implement that policy more easily than can the FERC because the governments of each of the component States have already committed themselves to the policy (subject to whatever compromises may have been made at the political stage in order to obtain that agreement).⁴⁷

The CEER intends to act as "a focal point" for contacts between regulators and the European Commission staff. It has organized with regulatory authorities and industry participants in the EU candidate countries to assist in preparing for their entry into the EU in 2004. In addition, the CEER has developed contacts with the NARUC and sponsored three conferences with the NARUC members. During 2002 and 2003, the CEER expects to focus largely on the closer integration of EU electricity and gas markets by addressing cross-border trade and infrastructure development issues.

The CEER has become an active participant in the Madrid and Florence Forums discussed above, and has begun to be tasked by the European Commission to assist in solving the complex implementation issues resulting from the fundamentally political decision to liberalize these energy markets. Hence, at the Florence Forum in May 2001, the Commission tasked the CEER to develop a long-term cross-border trade regime in electricity conjunction with the European Transmission Systems Operators (ETSO) discussed below. This new trading regime is expected to be based, among other principles, on the use of economically efficient locational pricing (charging the costs of network infrastructure primarily on loads, not suppliers). Other aspects of the ongoing CEER agenda include such topics as congestion management, tariff harmonization, and various benchmarking projects.

The development of the CEER and its evolving relationship with the NARUC has potentially significant implications for the U.S. energy law practitioner. Regulators on both sides of the Atlantic are now communicating about topics of common concern. For example, European regulators are

^{46.} MEMORANDUM OF UNDERSTANDING FOR THE ESTABLISHMENT OF THE COUNCIL OF EUROPEAN ENERGY REGULATORS (2000), *available at* http://www.e-control.at/pls/econtrol/docs/FOLDER/CEER/MEMO RANDUM US.PDF (last visited Sept. 12, 2003).

^{47.} There is no likelihood of the heads of state of the Member States immediately condemning an EU restructuring Directive (as was the case when fifteen U.S. governors issued a statement condemning the FERC's proposal for Standard Market Design), because they would have voted on the policy before it ever became a Directive.

expanding their understanding of the causes and consequences of the California energy market collapse through direct communications with U.S. state regulatory commissioners, while U.S. regulators may learn how various EU Member States are adapting the open-access models in their own countries. This linkage is likely to encourage the development of global best regulatory practices. Approaches proven to work, or fail, on one continent may be adapted, or avoided, on another.

3. Creation of Transmission System Operators (TSOs), the ETSO, the GTE and EASEE-gas

The implementation of the Electricity and Gas Directives requires the creation of grid managers for each nation's electricity or gas transmission grid. With regard to electricity grids, these grid managers assume some but not necessarily all of the functions of a U.S. Regional Transmission Organization (RTO). The various designated TSOs have now formed an association for European Transmission System Operators (ETSO) to develop common principles regarding the harmonization and establishment of rules. These rules are designed to enhance network operation and maintain transmission system security, to facilitate the internal European market for electricity, and to accomplish related objectives.⁴⁸

Similarly, an analogous organization has also been formed for the operators of the European gas systems. Known as "Gas Transmission Europe" (GTE), the group was founded in 2000 and represents the transmission function of the European gas industry.⁴⁹ In addition, during 2002, a group focused on achieving common business practices for the gas business in Europe organized under the name of the European Association for Streamlining of Energy Exchange-gas (EASEE-gas).⁵⁰ The group was overtly modeled on the U.S. Gas Industry Standards Board. It is now working with Member State regulators and EU officials through the Madrid Forum described above. The agenda for the group includes the harmonization of measurement units and gas specifications, the creation of Operational Balancing Agreements (OBAs) (planned to be implemented by the end of 2003), standardization of the nomination cycle (to be implemented by mid-2004), and related matters.⁵¹

4. Creation of Power Exchanges

The other set of new entities that should be mentioned are the power exchanges for the trading of electricity. There are now a number of power exchanges in Europe offering a variety of services including physical trades, futures contracts, and even third-party clearing services for over-the-counter

^{48.} The ETSO homepage is found at http://www.etso-net.org (last visited Sept. 13, 2003).

^{49.} The GTE homepage is found at http://www.gte.be (last visited Sept. 13, 2003).

^{50.} For more information see the EASEE-gas homepage at http://www.easee-gas.org (last visited Sept. 13, 2003).

^{51.} Peter Taff, Notes of an EASEE-gas Workshop on 4th December 2002 (2002), available at http://www.easee-gas.org/msword/Workshop_December2002.doc (last visited Sept. 13, 2003).

trades.⁵² In terms of their ownership and services, size, and experience, the existing exchanges cover considerable ground. Some of the exchanges, or their direct predecessors, have been in operation for over a decade. Others have been launched only in the last year or two. Some of the exchanges are entirely privately owned, while others have some government backing. There has already been some consolidation within this new industry sector as two of the German exchanges merged during 2002.

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^{52.} An unofficial, but useful, inventory of electricity trading exchanges may be found at the Germanbased, English language site: http://www.electricitytrading.org/markets/exchanges.shtml (last visited Sept. 13, 2003).