

Hydro and the Free Trade agreement

by Alex Netherton

The inclusion of a continental energy policy, a *bête noir* to nationalists, within the Free Trade Treaty (here called FTA) has raised some serious and debatable questions. But the major change represented by the Treaty is not the shift toward continentalism, but rather the loss of regulatory and sovereign power by the Canadian government to preserve a "national interest" while cultivating this trade. Furthermore, the terms of the Treaty work more toward establishing the legal claims of US purchasers to Canadian energy than they do to awarding Canadian producers a secure access to their most advantageous US markets. The Treaty ignores the concern that unqualified energy commitments to continental markets may leave Canada without control over natural resources.

Canadian export policy

The contentious issue for electricity exports stems from the level of long-term control a purchaser of energy may gain over the exporter's resources. Unlike other forms of energy, electricity cannot be stored. Therefore a purchaser of dependable energy buys more than a quantity of energy; he also buys the primary rights to the use of the capacity, e.g., generators and turbines. This is what the industry refers to as a "firm" or primary energy contract. Because it secures long-term supply, it can be regarded as a substitute for investing in capacity. Most utilities are interconnected and trade extensively. There is a great deal of "economy" trading where utilities shop around for the least costly energy, something like the trading-on-the-spot market for oil. These transactions, also called "secondary power" sales, can be terminated at any point by buyer or seller. The purpose of the secondary power sales for both parties is to benefit from the savings gained through the most efficient use of resources.

Our concern is primarily with the level of firm energy contracts between Canadian and US utilities. At issue is the danger, through firm power contracts, that Canadians could lose control of the use and benefits of the resource base. This is not an idle question. Historically, Canadian energy policy was torn by these conflicts. In present times the Newfoundland-Quebec contract concerning Churchill Falls raises the same issues. So does the continental energy policy.

Current practice

Since 1963 Canadian export policy has handled the problem in three ways. Firm energy contracts, indeed the investment in hydroelectric megaprojects for export, were encouraged. But the export energy had to be surplus to Canadian needs, it had to be priced fairly, and conducted through a mechanism of licences for specific periods of time. The licences could last up to twenty-five years.

Federal policy was oriented towards allowing US importers the ability to securely use Canadian resources while at the same time allowing these utilities a healthy planning horizon to gain alternative sources of supply should the resources later be needed for the Canadian domestic market. The recapture provision has never been used. This policy underscored all subsequent trade.

The National Energy Board was given the power to regulate electricity exports and international transmission facilities. The NEB regulatory concerns touch two major areas, both of which will be substantively changed by the Treaty. First, exporting utilities have to demonstrate that an exportable surplus exists for the life of the export licence. Second, the NEB has examined the export price according to three price criteria: first, that the price cover all of the costs of production in Canada; second, that the export price be not lower than the equivalent Canadian price for the same energy; and third, that the cost of the power to the purchaser be not materially lower than the nearest low-cost alternative in the export market (a revenue earning measure). The durations of the export licences have run from ten to twenty years. Generally, NEB regulation of this trade has not produced either the inter-governmental or government/industry conflicts witnessed in other energy regulation. It appears to have been able to accommodate the fundamental aspirations of the federal government, provinces and US consumers in continental trade.

Growing demand

Since 1973 Canadian exports of electricity to the United States have grown immensely. There are several political and economic reasons behind the trade. All of them support the relatively strong economic position of hydro-generated electricity on American markets dominated largely by more expensive thermally generated electricity. Water is a renewable energy resource, less costly and less environmentally damaging than either the nuclear, petroleum or coal alternatives. The increase in value and volume of exports has been the product of specific trading relationships between interconnected Canadian and US utilities or pools. The largest hydro-based utilities are in British Columbia, Manitoba and Quebec, and they are in the best position to develop along continental lines. Of the three, Quebec has been the most successful.

The underlying logic of this trade presents a new role for Canadian hydro resources on continental energy markets. Unlike the period from 1963 until the present, this trade assumes Canadian hydro resources will become not an in-

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