

State Oversight of GATS and Energy Policy

Remarks by Rep. George Eskridge,
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*before the National Conference of State Legislatures, Committees on
Economic Development, Trade and Cultural Affairs
and Energy and Electric Utilities
December 11, 2003*

Overview

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1. What were Idaho's initial concerns?

Idaho, like many other state legislatures, believes that international trade agreements ~~can promote~~ national economic growth. But we have concerns ~~about~~ how ~~trade~~ agreements may impact state sovereignty, ~~specifically in~~ our case, our state energy policy. Idaho is particularly concerned about conflicts that might arise under the GATS, the General Agreement on Trade in Services, in terms of Idaho's energy policy that protects our low-cost hydro base and promotes the development of renewable energy projects to help meet future needs.

This concern is enhanced by the failure of the trade ambassador to respond to Idaho's letter of April 15, 2003, which expressed our concerns. We have since written a similar letter to our own congressional delegation and have not received responses from the delegation members, causing us to wonder if they are monitoring the trade negotiations as much as they should be.

In the letter, our concerns were in three general areas:

- *Local monopolies* – Will GATS affect Idaho’s ability to regulate or even maintain local monopolies?
- *Domestic regulation* – Will GATS affect domestic regulation generally, including broad powers to regulate water or electricity in the “public interest”?
- *Specific commitments* – Will specific energy commitments by the United States affect our ability to continue developing Idaho’s electricity policy?

a. **Local monopolies.** Although other states have chosen to deregulate electricity services, Idaho has purposely continued to regulate the provision of electric service to retail customers. The questions then become:

- Would existing or future measures adopted by the Idaho Legislature that revise, expand or strengthen our electricity monopoly create a conflict with GATS provisions on grants of monopoly power? Could such action lead to trade sanctions under GATS?
- Would the transfer of a service area from one electric utility to another constitute a “granting” of monopoly under GATS?

b. **Domestic regulation.** The requirement under GATS is that domestic regulation be transparent and objective. There are also negotiations to implement a requirement that domestic regulations be “not more burdensome than necessary to assure the quality of a service.” The Idaho Department of Water Resources (IDWR) limits electric utilities’ use of water for electric generation under broad authority to protect the “public interest.” This authority promotes other public objectives in addition to the quality of electric service, including recreation, local economic development, agriculture, and environmental protection. The Idaho Public Utilities Commission (IPUC) also regulates electric utilities in the “public interest” including the rates charged for service. Under these regulator provisions:

- Is Idaho's broad authority to regulate in the "public interest" sufficiently objective and transparent under GATS to avoid a conflict?
 - Does the authority of IDWR to monitor and govern water use exceed the narrower objective of assuring the quality of a service as proposed in the GATS negotiations?
 - Could the WTO conclude that the IPUC regulatory requirements are more burdensome than necessary?
- c. **Specific commitments.** The United States is negotiating specific commitments in the energy sector. Such commitments might affect Idaho's energy regulation and related policies.
- For example, the National Treatment provision prohibits measures that give an advantage to domestic firms that are not available to ~~foreign~~ firms. Idaho is currently considering tax incentives for renewable energy developers locating their facilities within the state. Would tax incentives made available to private utilities locating facilities in the state conflict with GATS because these tax incentives would only benefit in-state producers?
 - In terms of market access, ~~the GATS rules~~ prohibit quantitative limits on the number of employees, the value of transactions, or the assets or legal structure of a service provider. Idaho has territorial jurisdiction regulations, which prohibit new electric utilities from gaining customers already serviced by the existing utilities located in Idaho. Would these restrictions on competition conflict with GATS?

We are disappointed that we have not yet received a response to these concerns from the Office of the U.S. Trade Representative, and this non-response only elevates our concerns.

It would appear that state sovereignty could be impacted more than we realize, and trade negotiations could interfere with our ability to develop energy policy that meets our economic and environmental needs. For this reason we need to become more aware and involved in the trade negotiations

on GATS and other agreements in order to protect our individual state interests.

I still look forward to a response from Ambassador Zoellick and the Office of U.S. Trade Representative. Since writing our letter last April, we have had an opportunity to expand our thinking about the appropriate state role in oversight of trade agreements. We have expanded our list of oversight questions that we would like to discuss with USTR. In my remaining time, I would like to explain why it is important for other states to join Idaho in this process, define what I mean by state-level oversight, and add just a few more examples of the oversight questions that we would like to discuss with USTR. I will conclude with some suggestions on how to make sure that such engagement with USTR is feasible, both from the perspective of state legislatures as well as the trade negotiators, whose resources are stretched by a demanding schedule.

2. Why is state-level oversight important?

a. **Trade rules** could affect policy making on topics of great concern to states –

- Tax incentives for alternative energy sources
- Regulation of ~~utilities including access~~ to the grid, marketing, and reliability standards

b. **Over 10 current negotiations** in the WTO, regional Free Trade Agreements (FTAs) or bilateral agreements aim to strengthen or expand the coverage of trade rules in each of the following areas that could affect electricity:

- *Trade in services* – GATS, NAFTA and proposed FTAs
- *Trade in goods* – GATT (WTO existing), NAFTA and proposed Free Trade Agreements (FTAs)
- *Procurement* – GPA (the existing WTO agreement on government procurement), a proposed new WTO procurement agreement, proposed procurement provisions in the GATS, and proposed FTAs
- *Subsidies* – SCM (the existing WTO subsidy agreement) and proposed FTAs

- *Foreign investor rights* – NAFTA (existing) and proposed FTAs
- c. **For example** – The GATS negotiations could affect – sooner or later – topics like transmission, reliability standards and “native load” obligations that are currently being negotiated between states and the Federal Energy Regulatory Commission (FERC).

3. What does state-level oversight entail?

- a. Identify issues of local concern – *e.g.* – assess the potential local impact of trade rules.
- b. Raise questions for discussion with USTR – *e.g.* – *Idaho and NCSL letters on GATS.*
- c. Recommend safeguards for state lawmaking authority.
- d. *Connect with NCSL and* other states to voice these concerns.

4. What are some examples of oversight issues?

The past several months have been a very busy period of trade negotiations. The more we learn, the more questions we have about the potential impact of trade rules on state-level energy policy. The following are examples of concerns we would like to discuss with our colleagues in other states and with the staff of USTR.

a. Tax incentives for alternative energy (wind, solar, hydro)

- **Idaho is developing tax incentives** as opposed to regulatory mandates like renewable portfolio standards (RPS).
- **Canada used the GATT to successfully challenge** tax incentives for in-state production of alcoholic beverages in 1992. This trade dispute is called “*Beer II*,” and its findings have been confirmed by more recent WTO decisions.
 - Could Canada **challenge** alternative energy incentives because they change the conditions of competition so as to favor in-state producers and disfavor imports of Canadian hydropower or other sources?
- **After the Uruguay Round negotiations** in 1994, NCSL and other state associations worked with USTR to safeguard a long list of state-level tax measures including “subfederal tax measures which afford less favourable treatment to a service ... supplier that is outside the sub-federal jurisdiction.” USTR reported to the states that “These reservations were submitted ... on June 29, 1994.” However, WTO minutes show that Canada and other nations blocked acceptance of these reservations.
 - What is the status of these reservations? Were they in fact rejected by the WTO?
 - Did USTR ever notify states of the WTO’s reaction after these reservations were initially submitted?

b. Services incidental to energy distribution – state regulation of electricity

- **Negotiations on energy distribution – scope of coverage of state measures.** In the domestic energy debate, the FERC has proposed unbundling of electricity transmission from electricity production as well as retail distribution. Northwestern states want to maintain some degree of vertical integration and bundling. Both the United States and the WTO Secretariat interpret “*services incidental to energy distribution*” as including “transmission and distribution services on a fee or contract basis of electricity.” The WTO further explains that “this seems to include transport and distribution of electricity ... when these services are operated by an independent services supplier and not by a vertically integrated manufacturer.” On the other hand, the WTO also says that “breaking up of the public monopolies and unbundling of vertically integrated utilities is the first market access issue on the road of multilateral liberalization” of the energy sector. We are concerned not only about the current trade negotiations, but also future rounds that are likely to implement the WTO’s “**unbundling**” objective.

- Let’s assume that currently, GATS rules do not apply to vertically integrated utilities, like Idaho Power. How would the GATS rule on market access affect long-term contracts that Idaho Power uses to purchase electricity on the grid? For example, would GATS rules affect state regulations that require these contracts to be based on cost and not on whatever price the market will bear?
- Do current or proposed U.S. commitments cover issues that states are currently negotiating with the FERC – for example – laws that govern access to the grid, marketing electricity sold on the grid, and reliability standards for transmission? In essence, could GATS rules undermine any compromise that the states negotiate with FERC regarding Regional Transmission Organizations (RTOs)?

- The most recent U.S. offer says that the offer should not “be construed as extending a mode 3 [“commercial presence”] right to acquire or invest in a government monopoly ...” However, the market access rule of GATS explicitly prohibits single service providers or new monopolies. Nor does the U.S. offer speak to state regulations on how a monopoly must behave in the market. How then can USTR safeguard state laws that prohibit market-based competition for Idaho Power’s customers?
- **The most sweeping rule in the GATS**, which is now being negotiated, is called “domestic regulation.” It would require state measures to be “no more burdensome than necessary.” When asked which laws might flunk this test, other countries placed rate-making for utilities high on the list, particularly when sub-federal jurisdictions use a variety of approaches.
 - In the Pacific Northwest, the market participants include Canadian utilities and American utilities that are owned by companies based in the European Union. Could Canada or another country use the “least burdensome” test under one of the FTAs or the GATS to challenge rate-making by state public utility commissions?
 - We have read in WTO minutes that U.S. trade negotiators have themselves raised questions about the unpredictable impacts of implementing the “no more burdensome than necessary” test. We appreciate USTR’s stance in this regard. Will U.S. negotiators oppose implementation of this GATS rule?
 - At one point, the United States suggested a “reference paper”, an attachment to GATS commitments, that would implement the “no more burdensome” rule for a new energy sector specifically, rather than across the board. What is the status of this proposal?
- **The most remarkable feature of the proposed FTAs** is that they include all the GATS rules, but they drop the safeguard of negotiating the coverage of services on a sector-specific basis.

This is sometimes called a “top-down” approach in contrast to the “bottom-up” approach of the GATS. Our concern is that even if electricity transmission is not covered by U.S. commitments under the GATS, it would be covered under the FTAs. There are no electricity reservations in the U.S. annex to the U.S. Chile FTA. There are almost no reservations for future state lawmaking of any kind – the exception being social services.

- Will you include electricity reservations in the next FTA?
- If so, will you reserve state-level regulation of electric utilities?
- Did you consult with state legislatures before you decided to abandon the framework of specific commitments? If so, who *did you talk* to?

c. Procurement specifications – preference for alternative energy

- **Washington plans to use procurement** as a way to creating a “clean energy” industry to create jobs and meet local needs when hydropower falls short.
- **The WTO agreement and the proposed FTAs** limit purchasing to price and not the process by which electricity is produced. Would a preference for wind energy violate the procurement rules of the WTO or proposed FTAs?
- **The proposed FTAs include a safeguard** for measures that “promote conservation of natural resources.” Would this protect a preference for in-state production of alternative energy?