

Energy Report: Blackouts Shape EU Agenda --- Focus Is Likely to Shift to Balancing Competition, Reliability

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WHEN A DOUBLE failure on Swiss power-transmission lines knocked out electricity to most of Italy in late September, grid managers were preoccupied at first with trading blame.

But the Italian blackout and other outages across the Continent this summer have created reverberations that will help shape the liberalization agenda in the European Union, where power markets are to be opened fully by 2007.

The result, industry and government officials said, is likely to be a change of emphasis at both the national and EU levels. The focus is likely to move away from a focus on lower consumer prices and toward a strategy that balances competition targets with measures that safeguard the reliability of electricity networks and output.

"Today's emphasis is on security of supply, security of price and environment," said Scott Foster, senior director of power at Cambridge Energy Resource Associates in Paris. "The agenda is less on liberalization and more on security. We will get a liberalization framework and market control to make sure that lights stay on, but [regulators] are likely to tolerate much more market power."

Policy makers will face a challenge in reconciling the competing economic, environmental and security interests of a network that transported some 269 terawatt hours of electricity across European borders in 2002, according to the Union for the Coordination of Transmission of Electricity, the association of European high-voltage-network operators.

A terawatt hour measures electricity consumed in an hour at a constant rate of one terawatt, or a trillion watts.

Electricity consumption in the electricity-transmission union's member and associate-member countries -- including those in Central and Eastern Europe -- totaled 2,163 terawatt hours in 2002.

Regulators and cross-border transmission organizations, such as the electricity-transmission union, are likely to have a stronger role, observers said. But the recent problems in Italy -- which were blamed in part on the country's high volume of imported power -- have thrown a spotlight on the generation sector as well.

Growing competition and wholesale-price volatility in the U.K. and Nordic power markets, the EU's most liberal, already have highlighted the risks for generators in those markets. European

power officials have taken particular note of the U.K. market -- where some power stations have been mothballed owing to weak wholesale prices -- amid fears that cross-border competition could put more pressure on the Continent's electricity system.

Eurelectric, a trade group representing European generators and distributors, estimates some 300 gigawatts, or 300 billion watts, of new capacity will be needed by 2020, requiring investment of some 250 billion euros.

"The question then is whether electricity companies will have sufficient incentive to respond to the signals and invest money in these areas," said Chris Boothby, a spokesman for Eurelectric.

European efforts to make power networks more dependable could lead EU countries to re-evaluate nuclear energy, though many governments have turned away from it in recent years. Proponents have long argued that nuclear energy, which doesn't emit greenhouse gases, would help the EU fulfill strict environmental mandates.

But some analysts said the emphasis on more reliable forms of power could lead countries that have turned against nuclear power to reconsider it. "A number of players are thinking about nuclear again," CERA's Mr. Foster said. "It remains to be seen if the public has come along for the ride."

Still, prescriptions from governments and regulators for improving the reliability of Europe's energy networks are unlikely for some months, as agencies are still examining the reasons for the Swiss power failure and the Italian chain reaction.

The Swiss government, implicated in the cross-border transmission failure, called for high-level consultations with government officials in Italy and France. Switzerland shares a connection with the two countries.

The Italian outage, which left some 56 million people without power for as long as 24 hours, came just weeks after a blackout hit southern Sweden and Denmark and just a month after a freak outage closed London's Underground at the peak of rush hour.

With political sensitivities high ahead of the 2007 deadline for opening EU markets, national regulators have been cautious about publicly discussing potential measures to improve the reliability of cross-border power transmission.

But other pan-European groups are taking a broader look at the system. The Union for the Coordination of Transmission of Electricity plans to deliver an interim report on the Italian blackout on Oct. 20. It declined to comment on implications before then.

Two industry lobby groups -- European Transmission System Operators and Eurelectric, the generators' and distributors' group -- are trying to influence the EU policy debate.

Eurelectric's Mr. Boothby said his organization continues to demand an "investment-friendly regulatory framework and greater consistency between different regulatory models across Europe, plus effective coordination and cooperation between national regulatory bodies."

The danger remains that regulators will overreach, said Stewart Gray, an analyst at consulting firm Wood MacKenzie in Edinburgh, which has provided price forecasts to utility companies but doesn't advise companies or governments. "If people really want 100% security of [energy] supply, they will have to pay a lot more for it," he said. "You'll have massively overengineered systems."

Instead, industry officials said, grid operators must improve coordination of cross-border power flows, as high-voltage transmission is separated from power generation and distribution as part of European cross-border liberalization.

"By 2004, transmission will have to be unbundled. By 2007, it will be distribution," said an official with a large European power company. "How do we deal with those issues? The grid in the Continent is a big bathtub. The water level has to always remain constant."

One solution, CERA's Mr. Foster said on the association's Web site, is a system of regional transmission organizations that would coordinate management of European grids. Such a system, he said, would set the stage "for a power market whose boundaries are electrical instead of political."

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