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# Inter-American Dialogue

LATIN AMERICA ADVISOR | Energy



## Featured Q&A *with the Energy Board of Advisors*

**Q The Dominican Republic is under pressure from the International Monetary Fund to reform its electricity sector. What chance of reform to the Caribbean nation's electricity sector do you see in the short to medium term? Will there be a return of private investment in the sector?**

**A Guest Comment: Bernardo Vega:** "The cabinet of the Fernandez government is split between those who want to initiate a counter reform and go back to state control of the electricity sector and those who want to continue with the private-sector-oriented reforms started in the first Fernandez administration (1996-2000). The government of Hipolito Mejia (2000-2004) purchased two of the three distributing companies privatized as part of the reform, and the Fernandez administration has not rented them out or sold them to the private sector. The IMF is insisting on cutting the subsidies to the electricity sector, which today exceed expenditures in health and education combined. The main problem is getting the three distributing companies to collect more and reduce fraud. The private sector, which invested substantially in the first Fernandez administration and thus increased generating capacity, is standing idle, waiting to see which of the two sides of the cabinet Fernandez will finally back. The World Bank seems to have given up and is unlikely to disburse funds it previously committed to the sector."

**A Board Comment: Roger Stark:** "The IMF's calls for reform are unlikely to be effective unless they address structural issues in the Dominican political and regulatory system. On the positive side, the Dominican Republic (DR) begins with a sophisticated electric regulatory framework and a cadre of highly proficient and credible electric sector technocrats. On the other hand, this will be either the sec-

*Q&A continued on page 3*

### PHOTO OF THE WEEK


Several foreign oil and gas companies, including Spain's Repsol YPF, signed new contracts with the Bolivian government over the weekend. See coverage on page 2.
*Photo: ABI.*

## Inside This Issue

## ENERGY SECTOR BRIEFS

### Mexico's CFE Awards ABB $50 Million in Network Contracts

Switzerland's **ABB** announced Monday it was awarded $50 million in contracts by Mexico's Federal Electricity Commission, or CFE, to expand the CFE's transmission and distribution network in different parts of the country. In a press release, ABB said it would provide and install equipment in five states in southeastern Mexico, expected to be completed by April 2008, and in the central state of Oaxaca, which should be finished in 13 months. The CFE generates, transmits and distributes electrical power to about 23.7 million industrial and household clients in Mexico, ABB said.

### Venezuelan Soldier Hurt During Protest by Jobless Oil Workers

A Venezuelan National Guard soldier was injured Monday during protests outside a refinery in eastern Anzoategui state by unemployed oil workers demanding jobs, local daily *El Universal* reported. A group of several hundred laid-off oil workers in the state are demanding state-owned oil company PDVSA comply with a labor court ruling ordering the company to restore their jobs and pay them each $19,500.

### Sempra Energy Suspends Operations at Mexico Plant

San Diego-based **Sempra Energy** last weekend suspended operations at an electricity generation plant in Mexico, which mostly supplies the US market, for a week of planned maintenance, Reuters reported on Tuesday. The 600-megawatt natural-gas powered Termoelectrica de Mexicali combined-cycle station is located about 115 miles east of San Diego near Mexicali.

# Oil & Gas News

## Foreign Oil and Gas Firms Sign New Contracts with Bolivian Government

Foreign oil and gas companies over the weekend averted possible expulsion from Bolivia, agreeing to sign new contracts with the government and cede greater control over the South American country's vast hydrocarbons resources to the state, Reuters reported. The companies, including Brazil's state-owned **Petrobras** and Spain's **Repsol YPF**—the two biggest investors in Bolivia's hydrocarbons sector—signed the new contracts with Bolivia's state-owned **YPFB** just before the expiration at midnight Saturday of a government-set deadline for renegotiating new agreements or face being expelled from the country. Bolivian President Evo Morales decreed the "nationalization" of Bolivia's hydrocarbons sector on May 1, giving foreign firms six months to renegotiate new contracts that give the state more control over the sector. Two other big investors in Bolivia, France's **Total** and the US' **Vintage Petroleum,** signed new contracts on Friday, according to Reuters. British-owned **BG Group Plc** and **Amoco**, and Argentine firms **Pluspetrol** and **Matpetrol**, also signed new deals. Under the new contracts, the foreign companies will operate as service providers to YPFB in exchange for between 18 to 50 percent of the revenue. Morales said the new contracts would result in a four-fold increase in Bolivia's energy revenues over the next four years from a current $1 billion, according to Reuters. "What we are doing here is exercising our property rights, as Bolivians, over our natural resources, without evicting anyone, without confiscating," he was quoted as saying. On November 13, Morales will submit the new contracts to Congress for approval, Bloomberg News reported. Bolivia still has to reach a new deal on natural gas prices with neighboring Brazil, which buys about half of Bolivia's gas. Bolivian government officials will meet with their Brazilian counterparts in Rio de Janeiro on

## Foreign Firms Say New Contracts in Bolivia Guarantee Profitability

Foreign oil and gas companies operating in Bolivia said new contracts signed with the Bolivian government over the weekend guarantee profitability.

Sergio Gabrielli, the head of Brazil's state-owned **Petrobras**, the biggest investor in Bolivia's oil and gas sector, said "under this contract there is no loss for us. It guarantees our investment and our return," according to Bloomberg News.

However, Petrobras has denied any commitment to future investment apart from routine maintenance spending for current operations, Reuters reported.

Spain's **Repsol YPF**, which has invested around $1.2 billion in Bolivia since 1996, said in a statement it believed "the new contracts guarantee the return on the investments made to date in Bolivia and those to be developed in the future," adding that "this scenario of legal warranty together with public recognition of the investments made to date by Repsol YPF in Bolivia will permit the development of new investment projects in that country."

Britain's **BG** said the contracts should broadly be as profitable as old contracts, Reuters reported, citing a company spokesperson. However, while the company said it was confident its investment to date in Bolivia would be recovered, it said it had yet to decide whether additional investments would be economically viable under the new terms.

The BG spokesperson hinted that the new contracts may force the company to downgrade its Bolivian reserves, most of which are undeveloped.

November 10, according to Bloomberg News.

### Norway's Statoil Announces Gas Discovery in Venezuela

Norwegian state energy company **Statoil** said Friday it has discovered gas in an exploration well in block 4 of Venezuela's Plataforma Deltana, but company officials told Reuters it was too early to disclose any volume data. The drilling operations are expected to be completed next month, according to Reuters. Earlier last week, Venezuelan Oil Minister Rafael Ramirez said that Statoil had found a reserve of seven trillion cubic feet of gas off eastern Venezuela. Statoil did not mention the Venezuela discovery in its October 30 third-quarter earnings release, which stated that international E&P income was down 15 percent compared to the third quarter of 2005. Overall, Statoil's third-quarter earnings were relatively flat and in line with analyst expectations, falling about one percent.

## Power Sector News

### Venezuelan Supreme Court to Hear Suit Against AES Corp.

Venezuela's Supreme Court said Monday it will hear a suit challenging US-based power company **AES Corp.**'s acquisition six years ago of a controlling stake in **Electricidad de Caracas**, Venezuela's largest private electricity generation and retailing company, Reuters reported. The suit, brought by two lawyers, questions the legality of a foreign company acquiring a utility of "public interest" and calls for the annulment of the deal, arguing it should have been approved by Venezuela's National Assembly. AES acquired 71.3 percent of Electricidad de Caracas in a public offering in 2000. Electricidad de Caracas Executive President Julian Nebreda responded to the lawsuit on Tuesday. "AES' purchase complied with all the norms of the regulatory bodies," Nebreda told reporters, according to Reuters."There is no problem because it complies with all the regulations." Nebreda, and the presidents of AES' local subsidiary and the National Assembly, were all expected to testify by the end of next week, after which the court will decide whether or not to proceed with the suit, according to Reuters. AES currently generates and distributes power in 26 countries.

### Endesa Chile Posts $243 Million Nine-Month Profit

Power generator **Endesa Chile** on Thursday reported profits of 143 billion Chilean pesos ($US 243 million) for the first nine months of 2006, a 75 percent increase over the same period of the previous year. Operating income rose by 24 percent compared to the 2005 period, reflecting the increase in production following favorable hydrology and higher reservoir water levels during the present year, the company said. Endesa Chile's consolidated EBITDA (earnings before interest, taxes, depreciation, and amortization) reached 507 billion Chilean pesos, an increase of 19 percent over the 2005 period. The distribution of EBITDA by country, adjusted for the shareholdings in each subsidiary, shows that Chile contributed 76.3 percent, Colombia 10.3 percent, Argentina 7.8 percent, and Peru 5.6 percent. Endesa Chile reported that its next major project to enter service will be the expansion of its San Isidro plant,

**Featured Q&A**

*Continued from page 1*

ond or third time in recent memory that the DR has reformed its electric regulatory system. Prior attempts have failed due to issues of faulty execution and perceptions of non-transparency and political risk. Almost everyone representing private investors or multilateral institutions in the DR has been exposed to sensational anecdotes regarding allegedly corrupt practices—in a relatively small business community, rumors travel fast. While most of these anecdotes are either exaggerated or flatly untrue, the fact remains that the DR is perceived as a market in which business deals can be won, lost, or 're-traded' on the basis of behind-the-scenes dealings (a perception that is reinforced by recent banking and energy sector scandals). To break away from this stereotype, the DR will have to implement regulatory 'best practices' that demand transparency in regulatory matters, and provide suitable and reliable mediation and arbitration procedures to quickly and fairly identify, resolve, and/or litigate electric sector disputes as they arise. Failure to address these issues will lead to yet another round of regulatory reform."

> "... This will be either the second or third time in recent memory that the DR has reformed its electric regulatory system."
>
> *- Roger Stark*

**A** **Guest Comment: Lucas Aristizabal:** "New low-cost sources of energy generation, renegotiation of power agreements, and likely tougher laws to prevent energy theft and non-payment of service are all possible changes in the medium term for the Dominican Republic electricity sector. The current administration has recognized the importance of solving the challenges facing the power sector and has stated its strategy for this sector to reach financial sustainability. This strategy was included in the country's agreement with the International Monetary Fund. Key initiatives to support the sector include improving the cash recovery of distribution companies by reducing energy losses and increasing collections, raising the average revenue of distribution companies through tariff adjustments, and improving the regulatory framework. The country faces the challenge of, as the World Bank describes it, 'balancing the needs to respect proper-

*Q&A continued on page 6*

which will require an estimated investment of $200 million and start commercial operations in open cycle with an estimated capacity of 220 MW in April 2007, using diesel oil. The cycle will be closed the following year, raising capacity to approximately 300 MW. At the end of 2008, once liquefied natural gas (LNG) is available in Chile, it will achieve its full capacity of 377 MW, the company said.

### AES' Chilean Unit to Invest $1 Billion in Thermoelectric Plant

The Chilean unit of US power company **AES Corp.** said Tuesday it plans to invest about $1 billion to build a thermoelectric complex in northern Chile, Reuters reported. **AES Gener** said the Angamos complex, to be built in the city of Mejillones, will include four carbon-fueled generating plants and will provide electricity for Chile's northern SING grid. AES Gener did not indicate when construction would get underway, but said it had presented environmental impact studies for the project to the Chilean government. In September, Chilean President Michelle Bachelet promised to facilitate the process of granting environmental permits to foreign investors in the energy sector, but said that investors would still be held to rigorous standards. Chile has been stepping up efforts to attract investment in its energy sector amid cuts in natural gas supplies from neighboring Argentina, which in the past has provided almost all of Chile's natural gas needs and powered about one third of Chile's electricity sector. The cuts are forcing Chile to turn to more expensive, substitute fuels, such as diesel and coal, to fuel plants. Chilean Energy and Mines Minister Karen Poniachik said in September that Chile needs to add 340 megawatts a year to its power grid between now and 2009 and double its electricity generation by 2020 to meet energy demand.

## Lula Re-elected President of Brazil in Landslide Victory

***Pledges to Make Helping the Priority During Second Term***

Brazilian President Luiz Inacio Lula da Silva was re-elected Sunday in a landslide victory, easily fending off a challenge from former Sao Paulo state Governor Geraldo Alckmin.

Lula won about 61 percent of the ballots versus 39 percent for Alckmin, who ahead of an October 3 first-round vote was able to capitalize on a late-breaking scandal involving Lula's re-election campaign to force Sunday's run-off.

Lula gave the thumbs up sign after being re-elected on Sunday.

*Photo: Agencia Brasil.*

In his victory speech, Lula pledged to make helping the poor a priority during his second four-year term. "The poor will have preference in our government, Lula said, according to state news service Agencia Brasil. "The foundations are built. We have no more time to lose."

However, Lula also promised a "tough fiscal policy" aimed at keeping a lid on debt. Lula said he would reach out to his political opponents and said he would work closely with Brazil's Congress, where he will need to build a coalition to pursue his political and economic programs.

Opposition figures affirmed they would work with the Lula government, but said they would not give Lula a break from investigations into corruption scandals, which have dogged Lula's first term in office. Lula's election victory on Sunday "does not authorize impunity," said Roberto Freire, a deputy in Brazil's Congress and president of the PPS party, according to local daily *Folha de Sao Paulo*.

On Monday, Lula da Silva promised economic growth in his second term and steps to reduce the gap between rich and poor, the Associated Press reported. Lula said his second term will be marked "by economic development, better income distribution and quality education."

Brazilians are "fed up with being an emerging power" with boom-and-bust economic cycles, Lula said, according to the AP. Editor's: see related Q&A in the October 31, 2006 issue of the daily *Latin America Advisor*.]

# Political News

### Mexican Congress Calls on Oaxaca Governor to Resign

Mexico's Congress on Monday asked Oaxaca state Governor Ulises Ruiz to resign and help defuse six months of protests and violence in the state, local daily *El Universal* reported. Despite the opposition of Ruiz's PRI party and the allied PVEM party, the lower Chamber of Deputies approved a resolution calling on Ruiz to "resign his office to re-establish governability, legal order, and peace." A slightly softer Senate resolution, which asked the embattled governor to "reconsider" stepping down, was passed unanimously. The two resolutions were passed after President Vicente Fox over the weekend dispatched more than 4,000 federal riot police to the state capital to take control of the city and restore order. Police were sent in after two protesters and a US journalist were killed Friday by gunmen believed to be local police. One man was killed over the weekend when he was struck in the head by a tear gas canister, and clashes between rock-throwing protesters and federal police using tear gas and water cannons continued this week. About a dozen people have been killed in Oaxaca since May, when striking teachers and other activists launched protests demanding the resignation of Ruiz, who they accuse of electoral fraud and orchestrating a campaign of violence against them. Ruiz said Monday he would not resign, called the congressional resolutions unconstitutional, and blamed the crisis on groups from outside of the state, *El Universal* reported. [Editor's note: see related Q&A in the October 18, 2006 issue of the *Advisor*.]

## Bush Signs US-Mexico Border Fence Bill into Law

US President George W. Bush last Thursday signed into law a bill calling for the construction of hundreds of miles of fencing along the US-Mexico border, but said the law was only one part of a comprehensive immigration reform package. Under the Secure Fence Act, the US will build 700 miles of fencing along the 2,000 mile-long southern US border. The law also authorizes more vehicle barriers, checkpoints, and lighting to help prevent illegal immigration, and authorizes the Department of Homeland Security to increase the use of advanced technology, like cameras, satellites, and unmanned aerial vehicles to monitor the border. "We're modernizing the southern border of the United States so we can assure the American people we're doing our job of securing the border," Bush said. However, the president said the law, passed by Congress in September, was only one part of efforts to reform the US' immigration system. "We have more to do," he said, renewing his call for the creation of a temporary guest-worker program. The president also repeated his opposition to "amnesty" for illegal immigrants in the US, but said "there is a rational middle ground between granting an automatic pass to citizenship for every illegal immigrant and a program of mass deportation." Bush signed the bill 12 days before mid-term congressional elections, in which his Republican party is at risk of losing control of one or both houses of Congress to the Democrats. The act drew swift condemnation from Mexico. Outgoing President Vicente Fox, who since the beginning of his administration in December 2000 has fought a losing battle to strike an immigration accord with the US, called the law "useless and shameful," and compared the fence to the Berlin Wall. "If this was an election-minded decision, well, in the sin there lies the penance," Fox was quoted as saying. President-elect Felipe Calderon, who takes office on December 1, called the law "deplorable" and said it "resolved nothing." US lawmakers are not expected to renew debate on comprehensive immigration reform until after the mid-term elections. A Senate bill proposes boosting border security while also putting some of the estimated 12 million illegal immigrants in the US on the path toward citizenship and creating a guest-worker program. House Republicans, however, reject "amnesty" for illegal immigrants and are calling on a purely pro-law enforcement approach. [Editor's note: see related Q&A in the November 1, 2006 issue of the daily *Latin America Advisor*.]

## US Probing Venezuelan Ties to US Electronic Voting System Company

The US government is investigating whether a software company that controls a major US manufacturer of electronic voting systems is secretly controlled by the government of Venezuelan President Hugo Chavez. News of the probe—first reported by *The Miami Herald* on Saturday—by the Committee on Foreign Investment in the United States (CFIUS), a panel of 12 government agencies overseen by the Treasury Department, came just 10 days before crucial mid-term congressional elections in the United States and amid fears that electronic voting systems could be vulnerable to manipulation. CFIUS, which looks into deals involving foreign investors to determine whether they compromise national security, is looking into possible ties between **Smartmatic**, a South Florida-based company founded by Venezuelans, and the Chavez government, which awarded the company three contracts worth a total $120 million to provide electronic voting machinery in the South American country, *The New York Times* reported. Last year, Smartmatic acquired Oakland, CA-based **Sequoia Voting Systems**, a maker of electronic voting equipment whose machines are used in 17 US states, according to the *Herald*. Smartmatic and the Venezuelan government deny the government has any control over the company. [Editor's note: look for a related Q&A in the November 2, 2006 issue of the daily *Latin America Advisor*.]

## POLITICAL & ECONOMIC BRIEFS

### Mantega Says Lula to Build on Gains of First Term

Brazilian Finance Minister Guido Mantega on Monday said the government of President Luiz Inacio Lula da Silva, who was re-elected in a landslide on Sunday, will seek in its second term to build on the gains produced during the first. "In the first term, it was necessary to bring the economy into equilibrium. Now that we've done that, we will push on to the next phase of more intense growth and job creation." Lula on Monday dismissed rumors that he would replace Mantega as part of an expected cabinet shuffle.

### Ortega Has Lead in Nicaragua, but Could Face Second Round

Sandinista Daniel Ortega has a strong lead heading into this Sunday's presidential election in Nicaragua, but may fail to get enough votes for a first-round victory, Reuters reported, citing two polls published on Friday. A poll by Costa Rican firm **Borge & Associates**, gave Ortega 34.4 percent support, versus 23 percent for conservative Eduardo Montealegre. The second poll, by Nicaragua's **M&R Consultores**, gave Ortega 33.8 percent versus 25.4 percent for Montealegre. In Nicaragua, candidates must win at least 40 percent, or 35 percent plus a margin of victory of at least 5 percentage points, to win in the first round.

### Cuba Shows Pictures of Castro

Cuban media over the weekend showed photos and a video of Fidel Castro standing and talking, part of an apparent effort to dispel rumors the 80 year-old Cuban leader was on his deathbed, the Associated Press reported. Castro underwent intestinal surgery in late July, ceding power to his brother, Raul Castro.

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ty rights, provide safe and efficient service, and avoid social discontent among the poor.' This 'calls for [an] imaginative public-private solution.' Any sector reform must be carried out at a negotiation table, with all parties involved participating in order to have a successful sector recovery and reach financial sustainability while protecting property rights. The government has taken several steps to achieve these objectives. It announced the introduction of approximately 1,200 MW of coal-fired generation plants expected to come online during the next three to five years; it has invited generation companies to renegotiate power purchase agreements in order to lower electricity prices; it signed two sector agreements pledging public funds to ensure payment to generators; and it has transferred approximately $1.4 billion to the energy sector during the past two and a half years. In addition, government-owned distribution companies have increased efforts to reduce energy losses and increase collections. Return of private investment to the sector is likely to the extent the government can establish a track record of stability and reasonable returns. The capacity expansion announced this year by the government would probably be developed partially with private investment."

**A**

**Guest Comment: Steven Kargman:** "As a general matter, it is rarely a simple or straightforward process to achieve fundamental reforms in the electricity sector of an emerging market country. Often it is not easy to reconcile the competing interests of the broad range of stakeholders in any given emerging market electricity sector, which may include public and private interests, domestic and foreign parties, and a diverse set of electricity sector participants. Moreover, the issues involved can potentially have major social and political implications, and these issues can also be fairly complex from a legal, regulatory, technical, economic, and financial standpoint. Thus, reaching a consensus and comprehensive approach, especially in a short period of time, can pose significant challenges. However, under certain circumstances, a crisis dynamic can provide additional and important impetus to reaching a solution. Whether or not this will be the case in the Dominican Republic, with all of its current problems in the electricity sector, remains to be seen. Nonetheless, even in a crisis environment, given the complexity of the issues involved and the wide range of interests of the stakeholders, it can still take some time to work through all of the relevant issues. Broadly speaking, the prospects for new private investment in the Dominican Republic's electricity sector would seem to be fairly limited in the near term unless and until the overall situation stabilizes and new, sustainable arrangements for the electricity sector are put in place. Private investors, particularly foreign investors, may very well be reluctant to put their capital at risk in a market that appears to be in as much flux as is the case today in the Dominican Republic's electricity sector. But if and when fundamental reforms of the electricity sector are eventually achieved, private investors may then possibly be willing to take another look at this market. Yet any such new potential private investors would most likely want to carefully review whether existing private investors have been treated fairly, including whether their legitimate interests and concerns have been taken into account in fashioning an overall solution."

**Bernardo Vega** *is President of Fundacion Cultural Dominicana and a former Dominican Ambassador to the United States.*

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