Resources

No. 21 Winter 1988

The Newsletter of the Canadian Institute of Resources Law

The Free Trade Agreement and Canada's Natural Resources

"...Whether the issue is specialty steel, shakes and shingles, softwood lumber or fish, the resource industries have borne the brunt of U.S. protectionist pressures..."

by J. Owen Saunders

The Free Trade Agreement (FTA)[1] concluded between Canada and the United States holds important – if somewhat ambiguous – implications for Canada's natural resource industries. The agreement is of special interest to, and has been received warmly by, the resource sector if only because it is this sector which has been the primary Canadian target of American protectionist forces in recent years. Whether the issue is specialty steel, shakes and shingles, softwood lumber or fish, the resource industries have borne the brunt of U.S. protectionist pressures.

While one can hardly expect the resource sector to enjoy the attention paid to it by the United States, there is at least one silver lining to this protectionist cloud: it illustrates vividly Canada's competitive capabilities. At least in the world of international trade, protectionism is the sincerest form of flattery. The Canadian resource industries thus approach the FTA with somewhat different focus than many other sectors – that is, the effectiveness of the Agreement in combatting **American** protectionist barriers, rather than, say, the adjustment costs that will follow on the removal of **Canadian** protectionism.

Of the two general types of barriers confronting exporters, tariffs and non-tariff measures (NTMs), it is probably the FTA's provisions with respect to the latter that hold the most significance for the Canadian resource sector. American tariffs on Canadian raw materials are by and large relatively modest. In the energy sector, for example, no tarrifs are imposed on electricity, uranium, natural gas, and natural gas liquids, with the exception of the customer user fee which applies to exports generally.[2] There is a U.S. tariff on crude oil and petroleum products ranging from 5.25 to 52.5 cents (U.S.) per barrel, but the removal of such duties would have a very small effect on the Canadian economy: the federal government estimates the impact as only $16 million annually for crude oil and $10 million for refined products, on the basis of 1987 exports.[3]

The relatively minor effect of tariff provisions on energy products reflects the movement towards deregulation in recent years by both the United States and Canada. However, while the formalization of this "market" approach to energy pricing may be in accordance with present policy initiatives in Canada, it does of course impose constraints on the ability of future governments to pursue policies that have been deemed appropriate in the past. The heart of such constraints lies in Article 903:

> Neither Party shall maintain or introduce any tax, duty, or charge on the export of any energy good to the other Party, unless such tax, duty, or charge is also maintained or introduced on such energy good when destined for domestic consumption.

(This mirrors Article 409, which applies this prohibition to goods generally.)

It might, of course, be pointed out that the prohibition in Article 903 refers to

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a "tax, duty or charge" but does not prohibit discrimination **per se.** Suppose, for example, Alberta were to offer rebates on gas consumed within the province, whether generally or to specific industries. Arguably, this might be prohibited under the Agreement, whether as a colourable attempt to evade the obligations of Article 903, or for that matter as a nullification or impairment of "reasonably expected" benefits under the Agreement, pursuant to Article 2011. If this is so, does the Agreement bind the province?[4] (In any case, the action might well be construed as an invalid subsidy and thus, quite independently of the FTA, subject to countervailable duties, as discussed below.)

And what of **national** policies aimed at setting artificial energy prices? While it is still theoretically possible for a Canadian government to regulate prices so that consumers pay more (as in the 1960s when the Ottawa Valley line rule subsidized western Canadian production) or less (as under the National Energy Program) than the prevailing world price, in practice this would be nearly inconceivable. In the former case, Canadian consumers could not be denied access to (presumably) cheaper U.S. energy, while in the latter it seems politically unimaginable to have Canadian producers in effect subsidizing American consumers, who would necessarily have access to Canadian petroleum resources on the same terms as Canadians.

As noted earlier, the more controversial disputes in Canada-U.S. resources trade in recent years have centred not on tariff barriers or export levies, but on NTMs. Indeed, much of the impetus for, and subsequent criticism of, the Agreement as a whole is rooted in the treatment of such measures. Given the attention paid to the issue of non-tariff resource protectionism in recent years the FTA has remarkably little to say on the matter. This, of course, is because of the decision taken to largely defer the negotiation of new trade rules until after the passage of the Agreement.

Nevertheless, there are a few NTMs of relevance to the energy sector that are addressed explicitly in the Agreement. With respect to uranium, where both Canada and the United States have implemented NTMs (concerning exports and imports respectively) directed towards helping their domestic processing industries, there has been an opening of markets. The United States has undertaken to exempt Canada from its restrictions on enrichment by U.S. facilities of foreign uranium, while Canada similarly exempts the United States from its 1985 Uranium Upgrading Policy.[5]

Additionally, the ability of the National Energy Board to regulate the export of energy goods is constrained somewhat by the removal of one test that might otherwise be applied by the Board,[6] that is, that the export price

> would not result in prices in [the United States] being materially less than the least cost alternative for power and energy at the same location within that country.[7]

In fact, although the reference in the Agreement is to energy goods generally, in practice this only has immediate relevance for electricity, given the NEB's recent movement towards a market-determined price for natural gas. In reply, the United States agrees to modify the Intertie Access Policy of the Bonneville Power Administration to give B.C. Hydro better access to BPA's transmission facilities – facilities which are vital for Hydro's market access to the U.S. southwest.[8]

One other regulatory issue that has been of concern to Canada recently is raised in the Agreement, but is not really resolved. This concerns the relationship between U.S. regulatory authorities (especially the Federal Energy Regulatory Commission – FERC) and Canada's National Energy Board (NEB). Specifically, to what extent can FERC extend its jurisdiction so as to affect Canadian resources policies? This

Agricultural Trade Conference

An international conference on "Decoupling: The Concept and its Future in Canada" was convened by the Canadian Institute of Resources Law in Ottawa on February 11 and 12. More than 150 participants from agricultural associations, industry, government and academia were in attendance at this conference, which featured simultaneous translation at all sessions. Representatives of GATT, the OECD, and a variety of international embassies also attended.

Agricultural trade issues have taken an increasingly high profile on the Canadian public policy agenda in recent years. This has been true both for bilateral trade concerns – as witnessed by the attention paid to agriculture in the Canada-U.S. free trade negotiations – and for multilateral issues, as is clear from the priority accorded agriculture in the current Uruguay Round of multilateral trade negotiations under the GATT.

At the heart of the international trade disputes involving agriculture is the question of subsidization. To what extent should subsidization of agricultural sectors be permitted and what forms of subsidization are most or least acceptable? A key element of this debate is the distortionary effects of subsidies on production, and one of the policy responses in this regard that has been proposed for structuring part of an eventual "solution" to the current ills of agricultural trade is to "decouple" subsidies from production decisions. That is, even assuming the continuation of some support for the agricultural sector, subsidization should be structured in such a way that it will have as little effect as possible on the production decisions – both as to quantity and choice of commodity – of the agricultural community.

Decoupling has gathered both supporters and detractors. The purpose of this symposium, however, was not to advocate the adoption of decoupling as a public policy stance in Canada – and far less to press for the consideration of one particular form of decoupling. It was, rather, to explain the origin, nature and some practical effects of an approach which has attracted serious attention as a possible partial response to existing international trade problems and which may have important implications for the future of agriculture in Canada.

The conference was organized by J. Owen Saunders of the Institute and Peter Finkle of Agriculture Canada. Funding for the conference was provided by Agriculture Canada.

issue was raised recently as the result of FERC Opinion No.256, involving certain natural gas imports from Canada.[9] In the course of its decision, FERC required the Natural Gas Pipeline Company of America to remove from its demand charges certain portions attributable to charges imposed by the Canadian exporters. The reaction of the Canadian government and of the NEB was to protest what was seen essentially as FERC's intrusion into Canadian regulatory practices, an intrusion that was in departure from past practice. In the NEB's view, the decision would prevent Canadian exporters from recovering NEB-approved transportation costs and would also necessitate a "substantial change in Canadian pipeline rate design".[10]

Clearly, any agressive pursuit of this new willingness by FERC to make decisions which effectively infringe on the NEB's jurisdiction could have far-reaching consequences for Canada's ability to regulate exports as it sees fit. Moreover, such an approach could conceivably constitute a powerful barrier to trade if used in the appropriate circumstances. Nevertheless, the only provision in the Agreement that specifically addresses this problem merely requires "consultations" between the two federal energy departments.[11] In the result, the intrusion by U.S. agencies into Canadian energy regulation remains a distinct possibility even after any implementation of the Agreement.

While the possible conflict between Canadian and American regulatory authorities holds some potential significance for the energy sector, clearly the greater concerns of Canadian resource exporters in recent years have concerned more traditional NTM issues: countervailing duties (CVDs) – as with softwood lumber and Atlantic groundfish; antidumping orders – as with Saskatchewan potash; and contingent protection – as with shakes and shingles. Of these three, it is the question of CVDs and the related issue of permissable and impermissable subsidisation that should be of most concern to Canada's resource sector.

As noted, the FTA defers negotiations on a new set of trade rules until after the Agreement is enacted. Pending the eventual negotiation of such rules, the existing rules of each state will be applied – including existing precedent from the relevant trade tribunals of the respective party. This has special significance for Canada's resource sector because of recent and proposed changes in the approach taken by U.S. tribunals and legislators towards subsidisation, and especially towards subsidisation of natural resources.

There has been a pronounced movement in the United States in the past few years towards expanding the reach of CVD actions, and more particularly towards broadening the test for what is an actionable subsidy; this movement has been reflected in both tribunal decisions and legislation. It is clear that not all subsidies are impermissable under the relevant multilateral rules as found in the General Agreement on Tariffs and Trade (GATT) and the GATT Subsidies Code. For example, a government-supported health care system would not be regarded as an improper subsidy given that it is generally available, while a government subsidy to insure the health of workers in a specific sector might well be considered as countervailable in that it singles out for preferential treatment a single industry.

"As the Omnibus Trade Bill now stands it is difficult to see how the Free Trade Agreement could survive its passage..."

This concept of specificity[12] has had special relevance for resource exporters into the United States. Until 1984, the U.S. International Trade Administration (ITA) had developed a concept of specificity that would have permitted, for example, a two-tier system of natural gas in Mexico (or Canada) that discriminated between exports and domestic uses. So long as the lower domestic price was generally available in Mexico, there was no preference and thus no specificity. This concept of subsidy, however, was criticized in a 1985 decision by the U.S. Court of International Trade,[13] and was ultimately rejected. In the Court's view the test of general availability as applied by the ITA was incorrect; even a benefit which was generally available might in practice operate so as to bestow a benefit on a particular industry. It was this revision of the concept of subsidy which led to the ITA reversing its original finding in the softwood lumber case. The stumpage programs of Canadian provinces, which had been found unobjectionable by the ITA in 1983 because the benefits were generally available, were found to be impermissable subsidies in 1986 because **in practice** they operated to confer a benefit on certain industries. This precedent would form part of the corpus of law which any joint U.S.-Canadian tribunal would be required to apply in interpreting American obligations under the Free Trade Agreement.

Legislatively also, there have been prepared in the U.S. Congress certain amendments that would go even further in calling into question the policies of foreign exporters of resources into the United States, including provisions that would substantially increase the ability – and duty – of U.S. trade tribunals to apply American pricing practices when considering whether foreign resource input prices constitute subsidies.[14] Of most current concern to Canada, however, is the proposal on subsidies in the Omnibus Trade Bill now before Congress.[15] The Bill would, **inter alia,** destroy legislatively any possible judicial resurrection of the "general availability" test in its provision that:

> the administering authority, in each investigation, shall determine whether the bounty, grant, or subsidy **in law or in fact is provided** to a specific enterprise or industry, or group of enterprises or industries. Nominal general availability, under the terms of the law, regulation, program, or rule establishing a bounty, grant, or subsidy, of the benefits thereunder is not a basis for determining that the bounty, grant, or subsidy is not, or has not been, in fact provided to a specific enterprise or industry, or group thereof.[16]

As the Omnibus Trade Bill now stands it is difficult to see how the FTA could survive its passage. Whether an amended bill would be acceptable to Canada is open to speculation, but clearly the subsidy provisions as now drafted would widen the ambit of CVD actions to a point where they would at a minimum strike against the spirit of the FTA.

Finally, the Free Trade Agreement maintains a silence on some issues of resource management that one might have expected to see addressed. Given, for example, the strong opposition in

this fall's Federal Water Policy[17] to water exports, it is surprising that water is not specifically excluded from application under the Agreement. Certainly there is an argument that any significant water exports would be caught under the exceptions in Article XX of the GATT, which is explicitly incorporated into the FTA.[18] However, it is by no means clear that the relevant exception – relating to protection of "human, animal or plant life or health"[19] – would necessarily apply to at least some smaller water export schemes. The question of water export also raises a more general concern for natural resources management, which cannot be addressed in detail in this brief overview but on which the Agreement is relatively silent: the implications of the FTA for environmental issues.

In sum, while the Free Trade Agreement has generally been received with enthusiasm by Canadian natural resource producers as a means of improving both the terms and security of access to the U.S. market, it is no panacea for the trade disputes that have plagued Canadian resource exporters in recent years. It is quite conceivable that as some types of protection for declining U.S. resource industries are removed, others – particularly CVDs – will be pursued with more enthusiasm, and indeed both Congress and the courts have envinced a willingness to expand such remedies.

Canadians must additionally be concerned by the recent intimations by FERC that it will expand its reach even to the point that the effects of Canadian regulatory decisions may be mitigated or nullified. As noted, the FTA does not prohibit such actions, although they could determine in a very fundamental way how energy trade will be structured in North America. Even those Canadians who accept the desirability of, for example, a North American energy market, have cause for uneasiness in this respect.

Finally, there are a number of important issues relating to natural resources management which will require further exploration, including, for example, the implications of the Agreement for environmental management and provincial jurisdiction over resource management.

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Notes

1. Free Trade Agreement Between Canada and the United States of America, text as initialled on December 10, 1987.
2. And which itself has been the subject of a recent successful GATT action against the United States.
3. Canada, *The Canada-U.S. Free Trade Agreement and Energy, An Assessment* (1988), at 42. The elimination of a customs user fee would confer additional benefits.
4. The effect of the FTA on provincial powers over natural resources raises some important and difficult questions of constitutional law which cannot be addressed in this overview. I have discussed some of these issues in a paper for a conference on the Agreement, convened by the Centre for Research on Public law and Public Policy, Osgoode Hall Law School (March 17 to 19, 1988).
5. Free Trade Agreement, Annex 902.5.
6. Free Trade Agreement, Annex 905.2.
7. National Energy Board Part VI Regulations, C.R.C. 1978, c.1026 as am., s.6(2)(z)(iii).
8. Free Trade Agreement, Annex 905.2(2).
9. *Natural Gas Pipeline Company of America*, 37 F.E.R.C. 61,215 (1986). For a discussion of this case, and more general impacts of U.S. deregulation on Canada, see Madigan, "The Impact of U.S. Regulatory Policy on the Export of Canadian Natural Gas to the United States", in Saunders (ed), *Trading Canada's Natural Resources* (Calgary: Carswell, 1987), 295-308.
10. Madigan, *id.*, at 307.
11. Art. 905.
12. For a more detailed treatment of the issues addressed in the following brief summary, see Yoder, "United States Countervailing Duty Law and Canadian Natural Resources: The Evolution of Resources Protectionism in the United States" and Coffield, "United States-Canada Natural Resources Trade: Sources of Conflict/Prospects for Agreement", both in Saunders, *supra*, note 9, 81-99 and 121-153 respectively
13. *Cabot Corporation* v. *United States*, 620 F.Supp. 722 (1985), expanding on earlier criticism the Court had directed towards the ITA in *Bethlehem Steel Corp.* v. *United States*, 590 F.Supp. 1237 (1984). For a discussion of both cases see Yoder, *id.*
14. See Yoder, *supra*, note 12, at 94, 98.
15. There are actually 2 similar bills before Congress, one emanating out of the House of Representatives, the other out of the Senate: Trade and International Economic Policy Reform Act of 1987, HR 3, 100th Congress, 1st Session (passed April 30, 1987) and Omnibus Trade and Competitiveness Act of 1987, S. 1420, 100th Congress, 1st Session (passed July 21, 1987). The references below are to the Senate bill, which is regarded as less extreme than the House proposals with respect to subsidies. The House proposals on subsidies are opposed by the U.S. Administration whereas the Senate position would appear acceptable to it.
16. S.1420, *id.*, s.33. Emphasis added.
17. Environment Canada, *Federal Water Policy* (1987).
18. By Art. 1201.
19. General Agreement on Tariffs and Trade, T.I.A.S. No.1700, 55 U.N.T.S. 194, Art. XX(b). Quaere whether water would fall under Art. XX(g), "relating to the conservation of *exhaustible* natural resources" (emphasis added.)

Trade Book Now Available

Trading Canada's Natural Resources, Essays from the Third Banff Conference on Natural Resources Law, convened by the Canadian Institute of Resources Law in Banff, Alberta, May 6-9, 1987. Edited by J. Owen Saunders. Published by Carswell Legal Publications, December, 1987. 374 pages hardcover. $75.00.

This book presents a series of papers examining the trade opportunities and problems facing Canada's resource sector. Contributors drawn from industry, government, private practice, and the academic community apply their expertise to trade law issues associated with natural resources, examining the problems and opportunities presented by a free trade agreement with the United States and the options and remedies available through the GATT. The focus of the book is primarily legal, but papers from other disciplines are included, providing an economic, business and political context for the discussion of legal issues and resource trade policy. The book discusses:

- economic and political factors and non-economic values that influence trade policy
- current trade issues in the forestry, mineral, energy, agriculture, and fisheries industries
- forms and effects of government protectionism and how protectionist measures may be countered
- impact of government regulatory schemes, nationally and internationally, and the effects of deregulation of the gas industry
- ways in which resource industries can adapt to the new trade environment and develop and maintain international trade contracts and agreements

This book may be ordered from: Carswell Legal Publications, 2330 Midland Avenue, Agincourt, Ontario M1S 1P7 or call toll free 1-300-387-5164 (Toronto business hours only).

Righteous Indignation, The Public Interest and Deregulation of Natural Gas

"...The circumstances which gave rise to the application are deeply disturbing. The Board's Reasons for Decision, while perhaps not wrong in law and thus not reversible, are equally so..."

by Janet Keeping

Introduction

On September 25, the National Energy Board decided that it would not issue an order compelling TransCanada PipeLines Ltd. (TCPL) to transport gas for the Manitoba Oil and Gas Corporation (MOGC). MOGC had arranged for direct purchases of gas to meet the needs of all Manitoba gas consumers (except those that chose to secure their own supply). MOGC acknowledged that the gas it sought to have transported would subsitute for volumes currently purchased by Manitobans from distributors in the province. The circumstances which gave rise to the application are deeply disturbing. The Board's Reasons for Decision,[1] while perhaps not wrong in law and thus not reversible, are equally so.

Background to the Application

In March 1985 the oil and gas producing provinces (British Columbia, Alberta and Saskatchewan) signed the Western Accord, an agreement concerning oil and gas pricing and taxation, with the federal government. One of the almost immediate effects of the Accord was the deregulation of oil pricing, but the agreement had import for natural gas as well. Part II of the Accord dealt with domestic natural gas pricing and provided in part that:

> IT IS AGREED that a more flexible and market-oriented pricing mechanism is required for the domestic pricing of natural gas. It is recognized that a new domestic pricing regime that is equitable to the producing, transporting and distributing components of the industry, and is acceptable to producing and consuming provinces, requires extensive consultation with the interested parties. To facilitate this consultation and develop a new market-sensitive pricing system it is agreed that:
>
> 2. A task force of senior officials from the federal government and the producing provinces will work with all interested parties, including consuming provinces and industry, to develop a more flexible market-sensitive pricing mechanism on or before November 1, 1985.

Negotiations leading to the November 1st deadline were difficult. Deregulation was generally thought desirable, the disagreements were over how it should be accomplished. In the end, a deal was struck but – as with the Western Accord – only among the producing provinces and the federal government: the consuming provinces (Manitoba, Ontario and Quebec) were not party to the October 31, 1985 Agreement on Natural Gas Markets and Prices.

Under the system of natural gas pricing and marketing in place prior to deregulation, natural gas was purchased by TCPL from western (largely Alberta) producers and resold to distributors in central Canada under long term contracts. Gas was priced in both transactions with reference to an Alberta border price which was fixed through agreement between Alberta and the federal government. The October 1985 Agreement did away with the Alberta border price, leaving gas prices to be negotiated, and provided that TCPL would no longer enjoy a monopoly in central Canadian gas markets. With the Agreement in place, it became possible for end users to purchase gas directly from producers and use TCPL only for transportation service.

Many important questions were left unanswered by the Agreement. Perhaps the most significant of these concerned the long-term contracts between TCPL and the gas distributors in the consuming provinces. Were these to run their term, or could they be abandoned allowing the distributors and their customers to negotiate new and presumably better deals directly with gas producers? It fell to the National Energy Board to decide the matter: it said that the long-term agreements were, in essence, sacrosanct – they had to be honoured.[2]

The decision created two classes of central Canadian gas consumers – large volume industrial users, found mainly in Ontario, who were freed to hunt for bargains and the rest whose needs taken individually were too small to allow for direct purchases and who were thus of necessity wedded to their

CELS Expands into Quebec

A section on the Quebec Electricity and Gas Board, available in both French and English, was recently added to the Canada Energy Law Service. The looseleaf Service, a comprehensive guide to the energy tribunals of the western provinces, Ontario, Canada, and now Quebec, is published by the Institute in conjunction with Richard De Boo Limited. For each tribunal there is a commentary, a collection of legislation, and a digest of board decisions and applicable judicial cases. With the addition of the Quebec section and other recent updates the Service has been expanded from three to five volumes. The information on the Quebec Electricity and Gas Board was compiled for the Institute by Quebec lawyer Louise Martin, of the firm Clarkson, Tétrault. Updates will be issued as required.

The Canada Energy Law Service is available from: Richard De Boo Limited, 81 Curlew Drive, Don Mills, Ontario, M3A 3P7. For more information you can call toll-free 1-800-387-0142 (Ontario and Quebec) or 1-800-268-7625 (other provinces, including area code 807).

distributor's long-term contracts with TCPL.

The consuming provinces were not pleased. The Manitoba government was especially outspoken:[3] most of its consumers were paying about $1.00/Mcf more than industrial users under direct sales. It decided to have the Manitoba Oil and Gas Corporation contract anew for Manitobans' gas supply. The plan was that the Corporation would resell to distributors in the province, but TCPL refused to ship the Corporation's gas forcing an application by MOGC under section 59(2) of the *National Energy Board Act.*[4]

It is hardly surprising that the fight was bitter. Manitoba was angry: not only was it left out of the ultimate decision-making process regarding deregulation of natural gas, its consumers were – it felt – unfairly treated under the October 31, 1985 Agreement. Alberta, on the other hand, was somewhat desperate: gas prices had fallen dramatically since (although by no means entirely due to) deregulation and the province was afraid of the impact on its producers should the relatively high prices under long-term contracts be lost.

This particular battle was not inevitable. (Manitoba could after all have acquiesced to the decisions regarding implementation of the Agreement.) But it would have been astonishing if failure to involve the consuming provinces in natural gas deregulation had not led to serious difficulty. It was widely recognized that the deregulation of natural gas was not going to be easy, but had the differences between the consuming and producing provinces been ironed out before deregulation was launched, the problems could have been minimized. (In this era of increased commercial freedom, it should have been recognized that the marketplace of ideas has something going for it, too.) It was announced in July of 1987 that further discussions regarding deregulation would involve the consuming provinces.

NEB Decision

As noted above, the NEB denied the Manitoba Oil and Gas Corporation's application for an order compelling transportation of its direct purchases of gas. The Board noted that section 59(2) of the Act does not prescribe criteria according to which a decision under it should be made. It then proceeded to set out the factors that in its view should guide such a decision: the primary consideration should be whether the order sought is "in the public interest". The decision should also be consistent, the Board said, with its rulings respecting self-displacement in earlier TCPL decisions. (Self-displacement occurs, the Board had earlier ruled, when a distributor contracts directly for gas that would substitute for, or displace, volumes that are already part of its firm supply from TCPL.) It should also have regard, the Board continued, to its decisions on previous secton 59(2) applications and, finally, "due consideration should be given to the [October 31, 1985] Agreement ... in the context of the Board's responsibilities and mandate under the Act, in particular, Part IV of the Act relating to traffic, tolls and tariffs".[5]

"...the NEB sees itself as a mere handmaiden to the political process..."

In fact, the Board's decisions on previous applications for gas transmission played an insignificant role in its disposition of the MOGC case. The Board said that the Manitoba application was not of the same kind as the section 59(2) applications it had approved. "[T]he Board notes that subsection 59(2) Orders which it has previously issued related to a specific and identifiable end-user whose direct purchase displacement and applied-for access to transportation services did not result in the total displacement of a distributor's market or supply arrangements ..."[6]

The most important criterion was, the Board said, the public interest, and it fleshed that concept out with its previous rulings regarding self-displacement and its interpretation of the October 31, 1985 Agreement. The Board's reasoning was very simple: MOGC's proposal amounted to self-displacement; self-displacement was contrary to the intent of the Agreement and therefore not in the public interest; the transportation order under section 59(2) was denied. The fundamental question – was the October 31, 1985 Agreement in the public interest? – was simply not examined, and it could have been. As the Board noted, the Agreement has only political, not legal, significance; it is not part of the statutory scheme which defines its jurisdiction. The Board emphasized that the relevant public interest was the *overall* public interest[7] and noted that the Agreement was not signed by the consuming provinces, yet the Board took the Agreement as constitutive of the public interest. One is left with the impression that the Board was wilfully blind to the one-sidedness inherent in the implementation of deregulation.

That the blinkers were on is further illustrated by the Board's response to the debate in the hearing over whether self-displacement was, or was not, within the intent of the Agreement. The Board, as already discussed, concluded that self-displacement was not contemplated by the Agreement. It continued, "To decide otherwise would require the Board to conclude that, in its decisions of the past two years, it had misinterpreted the intent of the Agreement." This is understandable enough. The Board struggled with those earlier decisions and was reluctant to acknowledge a mistake. But it went on to reassure itself that its decisions had been correct by observing that "The Board has had no indication from any of the parties to the Agreement that its decisions were not congruent with and complementary to the Agreement". With gas prices having plummeted since deregulation which of the producing provinces would have argued for self-displacement? (And the federal government has had to remain mute in order to make it appear as if the Agreement really was the splendid success it claimed.)

The truth of it is the Board's interpretation of the Agreement has likely been correct. Manitoba is also correct that the Agreement does not explicitly rule out proposals of its kind, nor does it limit direct sales to industrial users. But Alberta's position on the document's interpretation is probably the better one. Had it not been the intention that long-term gas supply contracts be honoured, certain provisions of the Agreement would have been unnecessary. But more convincingly, the background to deregulation of gas shows that it was to lower gas feedstock and industrial fuel costs that direct purchases were first proposed.[8] From that beginning to the October 31, 1985 Agreement it

probably was, as the Alberta Petroleum Marketing Board argued before the NEB, that "only individual consumers such as large industrial end-users were contemplated as direct sale purchasers because, the majority of small consumers would not have the resources, in any practical sense, to go on a direct sale".[9]

The last issue the Board dealt with in its decision was whether denial of the Manitoba application "would result in unjust discrimination in terms of access to the transportation services of the TCPL system". The Board answered that, "the effect of granting this application would be to permit self-displacement, would not be consistent with the orderly transition to market-sensitive pricing as contemplated by the Agreement and would be contrary to the public interest."[10] In other words, discriminatory it may be but, if so, it is discrimination sanctioned by the Agreement.

In its decision on the Manitoba application the Board has equated the public interest with the intent of the October 31, 1985 Agreement. There are two problems with this approach. The first is that, in doing so, the Board has failed to give any independent content to the concept of the public interest. It did not examine the concept in any general way; it gives us no idea of what the public interest might require apart from what is needed to implement the Agreement. Some will respond that the "public interest" is a bogus term in any event, that it has no meaning but is only used by decision makers to put conclusions, which are in fact based on whatever considerations they choose to use, on a more elevated plane. But the depth of such cynicism is unfounded. There are regulatory agencies which have examined the concept of public interest in a systematic way and then applied the results of their analysis to applications before them.[11] The words "in the public interest" mean something, but no enlightenment on the subject can be gleaned from the NEB decision on the MOGC application.

Instead of formulating its own concept of public interest, the Board merely applied its interpretation of the Agreement to the facts of the application, and this is a second difficulty with the Board's approach. It would have been the Board's duty to apply the Agreement were it part of the law circumscribing the Board's mandate but it is nothing of the kind, as the Board itself notes in its Reasons. The Board's decision-making probably does not amount to an illegal fettering of its discretion. But what it does amount to is further evidence of the extent to which the NEB sees itself as a mere handmaiden to the political process. When the signatories to the Agreement "requested" the Board review previous decisions regarding TCPL's tolls and tariffs, the Board answered the questions reopened in the desired way, i.e., in the fashion most suitable to implementation of the Agreement, even where its considered opinion, prior to the Agreement, had been decidedly otherwise.[12] It is no wonder then that the MOGC's application failed; it was doomed from the outset.

Interestingly enough, none of the above is to say that the Manitoba proposal was in the public interest. If deregulation is to produce a market in natural gas then there must be many buyers and sellers of the commodity. Manitoba sought to reduce the number of potential Manitoba consumers to one – the MOGC, and that does seem to militate against the transition to a natural gas marketplace. One should be sympathetic with the frustrations of Manitoba, and other central Canadian consumers denied the benefits of deregulation, but if towards a market is the path the country is taking, then the MOGC proposal was wrongheaded. Whether attempts to establish a free market in natural gas are ultimately successful, or in retrospect even seen as wise, the weight of current opinion nationwide is that deregulation is the way to go.

The problem with the National Energy Board decision under scrutiny here is not that the sought after order should have been made, but that the Board's reasoning is disturbingly superficial. The Manitoba proposal did not fail to be in the public interest because it amounted to self-displacement, the prohibition on which looks, as Manitoba argued, suspiciously discriminatory. It was not in the public interest because it militated against establishing a true market in natural gas and that is indisputably what most Canadians with an opinion on the matter think is in the public interest.

Epilogue

Subsequent to the NEB's decision the Manitoba gas utilities and Western Gas Marketing Ltd. (the marketing branch of TCPL) entered into a one-year contract that has Manitobans paying about $2.30/Mcf, down from about $3.00, but still more than the price of gas in direct sales. Notwithstanding this temporary compromise, the MOGC has applied to the Federal Court of Appeal for leave to appeal the Board's dismissal of its application.

Janet Keeping is a Research Associate with the Canadian Institute of Resources Law.

Notes

1. See National Energy Board, Reasons for Decision,Manitoba Oil and Gas Corporation, MH-1-87, September 1987.
2. See National Energy Board, Reasons for Decision, TransCanada Pipelines Ltd., RH-2-85, September 1985, at 34-35.
3. See, for example, a news release issued by Manitoba Energy and Mines Minister Wilson Parasiuk on December 16, 1986: "Parasiuk Critical of Inter-City Gas-TransCanada PipeLines Deal: Deal to Cost Manitoba $60 Million Per Year".
4. *National Energy Board Act,* R.S.C. 1970, c.N-6, as amended.
5. *Supra,* note 1, at 3.
6. *Supra,* note 1, at 6.
7. *Supra,* note 1, at 3.
8. See the report of the Ontario Energy Board concerning Natural Gas Used as a Feedstock in Ontario, E.B.R.L.G. 26, February 10, 1984.
9. *Supra,* note 1, at 4.
10. *Supra,* note 1, at 7.
11. See for example the report of the Ontario Energy Board regarding Expansion of the Natural Gas system, E.B.O. 134, June 1, 1987.
12. Compare *supra,* note 2, with the Board's Reasons for Decision in TransCanada PipeLines Ltd. – Availability of Services, May 1986.

Eugene Kuntz to Give Seminar

Eugene Kuntz, an eminent American oil and gas lawyer, will be presenting a public seminar on the topic of "Classifying Nonoperating Interests in Oil and Gas" at The University of Calgary on April 7. Professor Kuntz is the holder of the Chair of Natural Resources Law at The University of Calgary.

The seminar will take place from 1:30 p.m. to 4:30 p.m. on Thursday, April 7 in the Moot Court on the fifth floor of the Bio Sciences Building at The University of Calgary. A reception will follow. There is no registration fee but participants are asked to register at 220-3220 before April 7.

Bypass Pipelines:

Developments Since the Last Issue of *Resources*

by Janet Keeping

Introduction

Since last issue's article on bypass pipelines was written, there have been developments on two fronts.

Jurisdiction: As noted in that article both the Ontario Energy Board (in December 1986) and the National Energy Board (shortly afterward) claimed jurisdiction over bypass pipelines in Ontario. The Ontario board's assertion of jurisdiction was upheld by the Ontario Supreme Court in a decision dated March 26, 1987. As a result, the orders made by the National Energy Board allowing Cyanamid Canada Pipeline Inc. (CCPI) to construct a bypass pipeline in Ontario were rendered largely useless.

To clarify its position: CCPI applied to the National Energy Board for review of those orders. In connection with that review the NEB directed a reference to the Federal Court of Appeal regarding jursidiction over intraprovincial bypass pipelines. On November 27 the Court issued its decision in favour of exclusive **provincial** jurisdiction.

The Court decided the issue on the basis of ss. 91(29) and 92(10)(a) **Constitution Act, 1867,** the combined effect of which is to put interprovincial works and undertakings within the exclusive jurisdiction of Parliament. The Court held that, since CCPI's proposed pipeline would exist entirely in Ontario and "mere physical connection to the admittedly interprovincial TransCanada Pipeline (TCPL) work is not sufficient to found federal jurisdiction", if the bypass line was to come within s. 92(10)(a) "it must be as an undertaking rather than as a work alone" (at 25).

As to whether the pipeline would be an interprovincial undertaking, the Court held that it was TCPL and not CCPI that would be carrying on a commercial interprovincial undertaking. It added that, even if this was wrong, CCPI's commercial arrangements (buying gas in Alberta to be transported across Canada for sale in Ontario) would not constitute an interprovincial transportation or communications undertaking and thus not be within s. 92(10)(a).

The Court went on to hold that in determining whether the pipeline would be an integral part of the TCPI undertaking, the NEB had been wrong in failing to apply the "necessary nexus test". The Court concluded that the proposed pipeline was not within federal jurisdiction because there is "no such necessary connection. Far from being vital, essential, integral or necessary to TCPL, the proposed bypass is unnecessary and redundant" (at 28).

Litigation on the Ontario side of the issue has also developed further. The matter of provincial jurisdiction over bypass pipelines within the province was referred to the Ontario Court of Appeal in April, 1987. On February 15, 1988, the Court read its decision: it agreed with the Federal Court of Appeal that the CCPI proposal is within the exclusive jurisdiction of the province and adopted the Reasons for Decisions of that court.

The story is not yet complete for CCPI is seeking leave to appeal the Federal Court of Appeal's decision. The application for leave is expected to be heard by the Supreme Court of Canada on April 25.

Bypass in British Columbia: The article on bypass pipelines in the last issue also noted that applications for two bypass pipelines had been made in British Columbia. One of those was subsequently dropped, but the other was heard by the B.C. Utilities Commission, pursuant to a reference from the Ministers of Energy and Environment. In a report to Cabinet dated October 1987 the Commission recommended that approval to proceed with a bypass pipeline not be granted, provided that Inland Natural Gas Company (the local distribution company in question) offer the applicant "appropriate" rates on a transportation service contract.

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Resources No. 21

Resources is the newsletter of the Canadian institute of Resources Law. Published quarterly, the newletter's purpose is to provide timely comments on current resources law issues and to give information about Institute publications and programs. The opinions presented are those of the authors and do not necessarily reflect the views of the Institute. Resources is mailed free of charge to more than 6,000 subscribers throughout the world. (International Standard Serial Number 0714-5918) *Editor:* Theresa Goulet

Canadian Institute of Resources Law

The Canadian Institute of Resources Law was established in 1979 to undertake research, education, and publication on the law relating to Canada's renewable and non-renewable resources. Funding for the Institute is provided by the Government of Alberta, the Government of Canada, the Alberta Law Foundation, the Donner Canadian Foundation, and the private sector. Donations to the Resources Law Endowment Fund are gratefully accepted.

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Bill C-74

Alastair R. Lucas, Acting Executive Director of the Canadian Institute of Resources Law, recently testified before the House of Commons Legislative Committee on Bill C-74, The Canadian Environmental Protection Act. (See the article by Alastair R. Lucas in **Resources** 20, "The Canadian Environmental Protection Act", for more information about the proposed legislation.)