Legal Issues Relating to the Canadian National Energy Program

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I. INTRODUCTION

Since its unveiling on October 28, 1980, Canada's National Energy Program [1] has been commented upon abundantly in government circles, newpaper articles, trade magazines, and financial industry seminars, drawing both oil industry and foreign reactions. It has received less notice in scholarly publications, however, perhaps because it is a complex and continuously changing program that did not become effective until legislation was enacted.[2]

The purpose of this Article is to sketch a broad picture of the National Energy Program (NEP) while focusing on its Canadianization aspects, the new oil and gas taxation situation, and the Program's various transnational law implications. As of September 1982, most of the National Energy Program has been enacted by federal legislation.[3]

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1. CANADIAN DEPARTMENT OF ENERGY, MINES, AND RESOURCES, THE NATIONAL ENERGY PROGRAM 1980 (Report No. EP80/4E) (1980) [hereinafter cited as NEP].

2. It must be noted that the National Energy Program is not the result of the one document that was tabled in the House of Commons on October 28, 1980, but, rather, of a plethora of documents including government declarations, the 1980 budget papers, implementing legislation, agreements between the federal government and producing provinces such as Alberta, press releases, a subsequent 1981 budget speech, and an NEP UPDATE (Rep. No. EP82/4E) of May 31, 1982 [hereinafter cited as NEP UPDATE].

3. An Act to amend the Petro-Canada Act, ch. 105, 1980-1982 Can. Stat., *reprinted in* III Can. Gaz., vol. 6, no. 16, at 3121 (1982); An Act to amend the Department of Energy, Mines and Resources Act, ch. 106, 1980-1982 Can. Stat., *reprinted in* III Can. Gaz., vol. 6, no. 16, at 3125 (1982); An Act to amend the Petroleum Administration Act and to enact provisions related thereto, ch. 114, 1980-1982 Can. Stat., *reprinted in* III Can. Gaz., vol. 6, no. 16, at 3475 (1982); An Act respecting petroleum incentives and Canadian ownership and control determination and to amend the Foreign Investment Review Act, ch. 107, 1980-1982 Can. Stat., *reprinted in* III Can. Gaz., vol. 6, no. 16, at 3131 (1982) [hereinafter cited as Petroleum Incentives Act]; An Act to amend the Canada Business Corporations Act, ch. 115, 1980-1982 Can. Stat., *reprinted in* III Can. Gaz., vol. 6, no. 16, at 3527 (1982); An Act respecting energy monitoring and to amend the Energy Supplies Emergency Act, 1979 and the Oil Substitution and Conservation Act, ch. 112, 1980-1982 Can. Stat., *reprinted in* III Can. Gaz., vol. 6, no. 16, at 3435 (1982); An Act respecting motor vehicle fuel consumption standards, ch. 113, 1980-1982 Can. Stat., *reprinted in* III Can. Gaz., vol. 6, no. 16, at 3453 (1982); An Act to amend the National Energy Board Act (No. 3) ch. 116, 1980-1982 Can. Stat., *reprinted in* III Can. Gaz., vol. 6, no. 16, at 3537 (1982); Canada Oil and Gas Act, ch. 81, 1980-1982 Can. Stat., *reprinted in* III Can. Gaz., vol. 6, no. 12, at 2655 (1981); An Act to amend the statute law relating to income tax, ch. 48, 1980-1982 Can. Stat., *reprinted in* III Can. Gaz., vol. 6, no. 7, at 1275 (1981); An Act to amend the Excise Tax Act and the Excise Act and to provide for a revenue tax in respect of petroleum and gas, ch. 68, 1980-1982 Can. Stat., *reprinted in* III Can. Gaz., vol. 6, no. 10, at 2457 (1981), *amended by* An Act to amend the statute law relating to certain taxes, ch. 104, 1980-1982 Can. Stat.,

A. Overview of the National Energy Program

The National Energy Program accompanied the federal budget of October 28, 1980. The objectives, or "precepts," were stated as follows:

> It must establish the basis for Canadians to seize control of their own energy future through security of supply and ultimate independence from the world oil market.
> It must offer to Canadians, all Canadians, the real opportunity to participate in the energy industry in general and the petroleum industry in particular, and to share in the benefits of industry expansion.
> It must establish a petroleum pricing and revenue-sharing regime that recognizes the requirement of fairness to all Canadians no matter where they live.[4]

To attain these objectives, the National Energy Program made the following proposals: (1) a "made in Canada" oil price system that is "blended" to account for the different costs of domestic and imported oil, and allows prices to rise to eighty-five percent of the world or United States prices, whichever is lower; (2) the financing of this price system through a "petroleum compensation charge" levied on refiners; (3) a natural gas price system that increases gas prices less than oil prices but adds a new federal tax on natural gas produced; (4) a new petroleum and gas revenue tax (PGRT) of eight percent of production revenues computed without a deduction for royalties and expenses; (5) the phasing-out of depletion allowances to be replaced by a new system of incentive payments for oil and gas exploration and development (PIP grants) although the beneficiaries of the PIP grants would not necessarily be those who see their deductions phased out because the payment scale favors Canadian-owned and controlled companies; (6) additional incentive payments for exploration on "Canada lands," which are lands under federal jurisdiction; (7) a new Canadian ownership levy that will finance the takeover of foreign-owned oil and gas companies by the Canadian Government or its Crown corporations (such as Petro-Canada); and (8) a reserve to the federal government of a twenty-five percent share on all oil and gas plays in the Canada lands.[5]

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reprinted in III Can. Gaz., vol. 6, no. 16, at 3087 (1982).

4. NEP, *supra* note 1, at 2.
5. *Id.; see also* Scarfe, *The Federal Budget and Energy Program, October*

These aims would be achieved principally by the following legislative actions: (1) amendments to the Income Tax Act and to the Income Tax Act Regulations governing resource taxation in general, and depletion allowances in particular, as well as exploration and development expenses;[6] (2) new federal taxes on oil and gas;[7] (3) a new Canada Oil and Gas Act providing new rules for exploration, development, and production of oil and gas on Canada lands;[8] (4) a new Petroleum Incentives Program Act along with a new Determination of Canadian Ownership and Control Act;[9] (5) a new Energy Monitoring Act and amendments to various other acts such as the Petroleum Administration Act, the Petro-Canada Act, and the National Energy Board Act.[10]

Much of the original legislation was to be redrafted in light of various policy changes and the agreement of September 1, 1981, between the federal government and the Government of Alberta.[11]

B. The Main Thrust of the NEP: Canadianization

Canadianization is arguably the principal purpose of the NEP. In this regard, the NEP mentions three goals:[12] at minimum, fifty percent Canadian ownership of oil and gas production by 1990; Canadian control of a significant number of the larger oil and gas firms; and an early increase in the share of the oil and gas sector owned by the Government of Canada.

This apparently inoffensive statement contains rather devastating or spectacular proposals, depending upon one's point of view. Everything in the NEP, from the incentive provisions and the tax changes to the production rules for the Canada lands and the price proposals, has Canadianization in mind. This is especially true for exploration incentives structured to encourage invest-

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28th, 1980: A Review, 7 CAN. PUB. POL'Y 1, 6 (1981) (from which this classification was inspired).

6. NEP, *supra* note 1, at 38-39; DEPARTMENT OF FINANCE (CANADA), BUDGET PAPERS 2 (Oct. 28, 1980) [hereinafter cited as BUDGET PAPERS].

7. NEP, *supra* note 1, at 35-38.

8. *Id.* at 45-48.

9. *Id.* at 39-41.

10. *Id.*

11. Agreement relating to Energy Pricing and Taxation, Sept. 1, 1981, Canada-Alberta [hereinafter cited as Canada-Alberta Agreement], *reprinted in* 1982 CAN. ENERGY PROGRAM REP. (CCH) 75,101.

12. NEP, *supra* note 1, at 102-03.

ment by Canadian corporations and individuals.[13]

This "rally around the flag" idea is misleading. The NEP favors increased exploration on federal lands in northern Canada and in offshore areas as well as increased revenues for the federal government, at the expense of exploration on provincial lands and of the provincial share of resource revenues. It could therefore be argued that Canadianization is but a facade and that the NEP is designed to increase federal revenues.

The NEP's Canadian ownership provisions have met considerable criticism in various quarters, notably within the Reagan Administration in the United States.[14] Though the issue is clouded by the fact that the federal government also wants to wrest oil and gas tax revenues from the producing provinces, it appears to outsiders that the federal government, speaking for Canada, wants to Canadianize the oil and gas industry by whatever means it can use. Even though the federal government is only one level of Canadian government, this political plan must not be underestimated because the federal government has the legal power to enforce most of the program.

C. The National Energy Program and the Canadian Constitution

Although Canadian constitutional law on the distribution of powers between the federal and provincial levels is far from straightforward, various headings of the British North America Act of 1867[15] (B.N.A. Act) would appear to enable the federal Parliament to enact legislation such as that proposed by the National Energy Program. Indeed, provincial property rights to most oil and gas resources within the boundaries of the provinces and provincial legislative jurisdiction over exploration, development, production, and conservation of these resources are not sufficient to preclude a federal role in energy through the exercise of its

13. *Id.* at 39-41.

14. For a summary of the United States Administration's criticism, see *U.S.-Canadian Economic Relations*, 82 DEP'T ST. BULL. 50, 50-55 (June 1982) (statement of Robert Hormats before the Subcommittee on International Economic Policy of the Senate Foreign Relations Committee, March 10, 1982) [hereinafter cited as Hormats].

15. 30 Vict., 1867, ch. 3 (now renamed the Constitution Act, 1867, by Schedule I of the Constitution Act, 1982, which is Schedule B of the Canada Act, 1982, ch. 11 (U.K.)).

taxation, trade and commerce, expropriation, and declaratory powers. Also, the paramouncy (supremacy) rules usually can be used successfully to ensure that in the case of overlapping valid laws, federal legislation will prevail.[16]

Before the NEP, prices for oil and gas had been established by agreement between the federal government and each producing province. The NEP's unilateral attempt to fix prices caused considerable uproar and was met with a series of production cutbacks by the Alberta government. After lengthy negotiations, the two parties on September 1, 1981, reached an agreement with a structure that differs somewhat from that proposed in the NEP.[17]

This incident shows that the two levels of the Canadian Federation must take part in energy decisions. Although the federal Parliament may regulate crude oil prices through its combined taxing and trade and commerce legislative powers, the B.N.A. Act enables provinces to legislate on the exploration, production, sale, and distribution of their natural resources within the province.[18] This shows that energy is a shared responsibility and that the framers of the NEP considered this situation before tabling their document. It is therefore submitted that the framers intended to wrest power and revenues away from the provinces in the energy field.

Similar comments could be made about the tax aspects of the NEP. The proposed tax on exported natural gas and gas liquids was challenged successfully on constitutional grounds first in the Alberta Court of Appeal and then in the Supreme Court of Canada,[19] though admittedly in a very narrow fact situation: the Alberta government was careful to ensure that section 125 of the B.N.A. Act, which provides that no property belonging to a province would be liable to taxation, applied thoroughly. This plainly indicates that the federal government must respect provincial political interests because of the divided jurisdiction that Canadian federalism creates in the energy field.

This Article will not explore the constitutional aspects of the

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16. *See* P. HOGG, CONSTITUTIONAL LAW OF CANADA 101-14 (1977).

17. Canada-Alberta Agreement, *supra* note 11.

18. For a critical discussion of the situation, see Magnet, *Constitutional Distribution of Taxation Powers in Canada,* 10 OTTAWA L. REV. 473 (1978).

19. Reference Re Questions set out in O.C. 1079/80, Concerning Tax Proposed by Parliament of Canada on Exported Natural Gas [1981] 3 W.W.R. 408 (Alta. C.A.), *confirmed by* the Supreme Court of Canada, June 23, 1982. 1982 N.R. 361 (June 23, 1982).

NEP further because others have examined this question.[20] Suffice it to say that legal and constitutional issues are compounded by political issues stemming from the peculiar nature of Canadian federalism.

II. The Taxation Provisions of the Canadian Energy Program

A. Oil and Gas Taxation in Canada

In Canada, corporate income is taxed by the federal government at the rate of forty-six percent.[21] This rate is reduced by ten percent to take into account the income taxes paid to the provinces.[22] Taxable income is income from all sources less the deductions permitted by the Income Tax Act.[23] Oil and gas firms may deduct exploration expenses, development expenses, the frontier allowance, depletion allowances, a resource allowance, and capital cost allowances. In reality, these deductions are tax incentives.

The main tax incentive is the deduction for Canadian exploration expenses. Oil and gas companies, and others who search for oil and gas, can deduct from their income from all sources 100 percent of their Canadian exploration expenses. These expenses include expenditures for geophysical and geological surveys, geochemical work, and test wells drilled to determine the existence, extent, and location of petroleum or natural gas. Naturally, this includes expenses incurred in drilling an oil or gas well or building a temporary access road.[24]

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20. *See, e.g.*, R. Harrison, The Constitutional Context of Canada's National Energy Program (April 8, 1981) (paper presented at the International Energy Development Conference-Canada/U.S., Salt Lake City); A. Lucas, The October 28, 1980 Federal Budget and National Energy Program - Constitutional and Regulatory Issues (Nov. 26, 1980) (paper presented at the Canadian Tax Foundation Conference, Montréal). Another point of contention, well beyond the scope of this Article, is the question of jurisdiction over the Canadian offshore areas. For elaboration of the point, see Harrison, *Jurisdiction over the Canadian Offshore: A Sea of Confusion,* 17 Osgoode Hall L.J. 469 (1979).

21. Income Tax Act, ch. 63, 1970-1972, Can. Stat. § 123.

22. Provinces may also provide rebates. For instance, Alberta legislation provides rebates against provincial income taxes equivalent to the payment of royalties to Alberta. Alberta Income Tax Act, Alta. Rev. Stat., ch. A-31, §§ 11-12 (1980); Alberta Corporate Income Tax Act, Alta. Rev. Stat., ch. A-17, § 26 (1980).

23. Ch. 63, 1970-1972, Can. Stat. § 3 (as amended).

24. *See id.; see also* Income Tax Act, ch. 63, 1970-1972 Can. Stat. § 66.1(2),

To qualify for an exploration expense, the well must be the first well in a field not previously known to exist. This condition, however, is absolutely meaningless because a well drilled in a known field that was not reasonably expected to come into production within twelve months of completion is considered an exploratory well. In light of the continuing natural gas surplus, nearly all natural gas wells qualify for the 100 percent deduction. Also, expenses incurred in Canada that result in a dry hole qualify for the 100 percent deduction. If the deduction is not needed, individuals and corporations other than principal-business corporations may carry it forward and deduct it in subsequent years.[25]

Canadian development expenses provide a second incentive.[26] These development expenses include expenditures for drilling oil and gas wells that do not qualify for the exploration expense deduction and, until December 11, 1979, the cost of resource properties.[27] These expenses may be deducted from income from any source at the rate of thirty percent on a declining basis. This means that almost all development expenses eventually would be deducted. Again, development expenses incurred by individuals and nonprincipal-business corporations may be carried forward and deducted in subsequent taxation years.

A third incentive, the so-called super depletion or frontier allowance, was in effect from April 1, 1977, to March 31, 1980.[28] A considerable amount of money was committed to arctic drilling partly because of the frontier allowance.[29] If the cost of a well exceeded five million dollars Canadian, then the excess cost would generate a frontier exploration allowance of sixty-six and two-thirds percent of excess costs deductible from income from any source. Needless to say, this was in addition to the other deduc-

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(3), (6)(a).

25. *See generally* Watkins, *Taxation of the Oil & Gas Industry*, in CANADIAN TAXATION 823 (1981).

26. Income Tax Act § 66.2.

27. At that time a Canadian oil and gas property expense, deductible on a 10% declining rate, came into effect. *See id.* § 66.4(5)(a); *see also* Roche & Beil, *Federal Income Taxation of the Resource Industries—The 1980-1981 Amendments*, 29 CAN. TAX. J. 287, 289 (1981).

28. *See* Income Tax Regulations, Amendment, P.C. 1977-2471 (Aug. 31, 1977), *reprinted in* II Can. Gaz., vol. 111, no. 18, at 4215.

29. For instance, $58 million was raised from the public in 1978 by Beaufort Exploration Limited under a tax shelter drilling fund featuring the frontier allowance deduction. Financial Post (Toronto), Aug. 8, 1981, at 1, col. 2.

tions just mentioned. By adding the 100 percent exploration expenses deductions, the frontier exploration allowance permitted a taxpayer to deduct 166⅔ percent of the investment. In some cases, therefore, the investment costs nothing. A high tax bracket individual could make money on any investment—even a dry hole.

A fourth incentive is the depletion allowance. This incentive is interesting because it may be used in combination with other incentives. Each dollar incurred in Canadian exploration expense and Canadian development expense enables the oil company or individual taxpayer to earn a depletion base of thirty-three and one-third percent of these expenses. A taxpayer with resource profits may deduct the earned depletion base at the end of the year or twenty-five percent of resource profits, whichever is less.[30] This deduction may be carried forward and used in subsequent years.

The resource allowance provides a fifth incentive. After 1976, oil companies no longer could deduct from their federal tax liability royalties paid to the producing provinces. The federal Parliament then enacted a resource allowance[31] to restore part of the deduction for provincial royalties. Thus, in computing their income, oil companies deduct a resource allowance of twenty-five percent of their resource profits.

Capital cost allowances constitute a sixth incentive. For instance, there is a thirty percent declining balance allowance for machinery and equipment acquired for the purpose of exploring for and producing oil and gas.[32] An investment tax credit of seven to twenty percent of eligible costs creates a seventh incentive.[33]

Other incentives exist at the provincial level. The British Columbia, Saskatchewan, and Alberta provincial tax rebates, the Alberta royalty tax credit—which is called a small explorer's credit—and the Alberta drilling incentives credit deserve note.[34] Another interesting incentive permits an investor to borrow

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30. Income Tax Regulations §§ 1201-1205.

31. Income Tax Act, ch. 63, 1970-1972 Can. Stat. § 20(1)(v.1); Income Tax Regulations § 1210(1).

32. Income Tax Regulations, sched. II, class 10. Other classes provide for allowances relating to certain pipelines, storage tanks, gas processing plants, refineries, and offshore drilling vessels.

33. Income Tax Act § 127(5), (9), (10).

34. *See generally* E. HOLLAND, G. SCHULLI, & R. KEMP, CANADIAN TAXATION OF OIL AND GAS INCOME 339-61 (1979).

money and invest it in exploration programs, take all of the energy-related deductions, and deduct the interest expenses incurred to borrow the money.[35]

These various tax incentives actually have stimulated exploratory drilling in Canada considerably. In fact, the number of exploratory wells rose from 1600 in 1975 to 3200 in 1978. The number of development wells rose in the same period from 2500 to 4000. Despite the huge losses for the federal and provincial treasuries, retention of these incentives in the 1980s was justified by Canada's goal of energy self-sufficiency. Perhaps some adjustments should have been made, but this was a political question. The pre-NEP incentives appeared to be sufficient to encourage the pursuit of oil and gas, especially in light of increasing oil prices. The NEP brought about a major change in the rules.

B. Changes Made by the NEP

1. *The Structural Change*

The National Energy Program proposed a major departure from the previous system of federal incentives for oil and gas exploration and development provided through the income tax system. As mentioned in a 1981 document, the federal government endeavors "to move away from this tax-based incentives system, which was only of benefit to firms in a taxable position, to one which delivers grants to firms directly."[36]

An earlier document puts the case more bluntly by saying that "[t]he new incentive system . . . will facilitate the gradual Canadianization of the oil and gas industry. This Program also introduces a new element of fairness into the incentives system, as the payments are not related to the tax status . . . ."[37]

Exploration and development expenses will now qualify for incentive payments instead of being treated solely by the income tax system. Such incentive payments, however, will be available only to firms with specific Canadian ownership and control. Payments will increase in proportion to the degree of Canadian own-

35. Income Tax Act § 20(1)(c).

36. Canadian Department of Energy, Mines and Resources, The Petroleum Incentives Program at vii (Rep. No. M 27-27/1981E) (1981).

37. Canadian Department of Energy, Mines and Resources, Petroleum Incentives Program: The Basic Rules—A Framework 1 (1980).

ership and control.[38]

After a phasing out period, exploration and development expenses will no longer qualify for earned depletion, with the exception of expenses incurred for the exploration of federal lands by corporations. Of course, the incentive payments reduce the exploration and development expenses that may be deducted under the Income Tax Act.[39]

In sum, the NEP replaces the indirect incentives provided through tax deductions with direct grants that discriminate against non-Canadian firms. Nevertheless, the tax system remains crucial and must continue to be examined in light of the NEP.

2. *Changes to the Existing Tax System*

a. Canadian exploration expenses

The NEP initially proposed a change in the definition of "Canadian exploration expense" to restrict considerably its scope after 1980.[40] This would have changed many exploration expenses, which were deductible at a 100 percent rate, into Canadian development expenses, which are deductible at a much less favorable 30 percent declining rate.[41]

Reaction to this proposal was swift.[42] In response to this reaction, the bill that was introduced to enact this proposal postponed the change for one year and restored exploration expense status to all costs incurred in dry holes and most frontier oil and gas wells.[43] The budget of November 12, 1981, proposed that the amendments would not go into effect until 1983.[44]

Still, the exploration expense tax write-offs will be tightened because costs for capped gas wells drilled in nonfrontier lands will

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38. *See* NEP, *supra* note 1, at 39-41. This policy was implemented in Petroleum Incentives Act, *supra* note 3, sec. 10.

39. *See* An Act to amend the statute law relating to income tax, sec. 34(13) (amending § 66.1(6)(b) of the Income Tax Act).

40. *See* BUDGET PAPERS, *supra* note 6, at 90-91.

41. Income Tax Act § 66.2(2).

42. Because of this and other NEP measures, shares of Canadian oil and gas firms listed on United States and Canadian stock exchanges plummeted, drilling rigs started moving out of the country, and the industry set up a strong lobby.

43. *See* An Act to amend the statute law relating to income tax, sec. 34(10).

44. *See* DEPARTMENT OF FINANCE (CANADA), BUDGET PAPERS 44-45 (Nov. 12, 1981) (this postponement has not yet been enacted). It is included, however, in a comprehensive *Notice of Ways and Means Motion, tabled in* HOUSE OF COMMONS, sec. 34 (June 28, 1982).

be treated as development expenses.[45] Also, any grant received under the Petroleum Incentives Program (PIP)[46] will reduce the amount of exploration expenses deductible. Exploration expenses, therefore, will become a less important factor in investment decisions. Nevertheless, "non-COR companies" may decide not to Canadianize, thereby forfeiting a good part of the potential PIP grants. In such cases, the 100 percent tax write-off of the exploration expenses, although more restricted in scope than before, will remain a very important factor.[47]

b. Canadian development expenses

The National Energy Program expands the scope of development expenses to compensate for the new restrictions on exploration expenses. Bill C-54, which gives the new definition of exploration expenses,[48] amends the definition of development expenses slightly[49] but preserves the provision granting development expense status to expenses incurred for drilling or completing wells that do not qualify as exploration expenses.[50]

Of course, any PIP grants received under the NEP will reduce development expense deductions proportionately.[51] Thus, the development expense deduction becomes a less significant consideration in investment decisions unless the taxpayer fails to qualify for PIP grants.

c. Depletion allowances

Changes in the Income Tax Act Regulations relating to depletion allowances support the NEP policy of replacing tax incen-

45. *See* PRICE, WATERHOUSE & CO., THE NATIONAL ENERGY PROGRAM 18-19 (2d ed. 1981). This has been enacted in An Act to amend the statute law relating to income tax, sec. 34(10).

46. Income Tax Act § 66.1(6)(b) *amended by* An Act to amend the statute law relating to income tax, sec. 34(13).

47. For a comprehensive study of the amendments to the Income Tax Act relating to Canadian Exploration Expenses, see Watkins, *Recent Developments in Petroleum Taxation*, in 1981 PRAIRIE TAX CONFERENCE 74-79 (1981) (Canadian Tax Foundation); Watkins & McKee, *Recent Developments in Petroleum Taxation and the Canadian Ownership Rules under the National Energy Program*, 20 ALTA. L. REV. 46 (1982).

48. *See* An Act to amend the statute law relating to income tax, sec. 34(9).

49. *Id.* sec. 35(5).

50. *See* Income Tax Act § 66.2(5)(a)(i)(B).

51. *See* An Act to amend the statute law relating to income tax, sec. 35(11).

tives with direct incentive payments.[52] For individuals, the depletion allowance is eliminated completely as of January 1, 1981. The thirty-three and one-third percent depletion allowances for qualifying exploration expenses incurred in 1981 and 1982, net of any incentive payments, is maintained for corporations. Development expenses no longer will be eligible for the depletion allowance. After 1982, the thirty-three and one-third percent depletion allowance on the Canada lands remains for corporations only. For other taxpayers, the rate will drop to twenty percent in 1983 and to ten percent in 1984; it will be phased out completely by 1985.[53]

A problem arises, not because the earned depletion is being phased out, but because the depletion is phased out for all entities and replaced by direct incentive payments available only to those qualifying under the Canadian ownership rate (COR) rules.[54] Although this clearly is a discriminatory measure, it remains to be seen whether this discrimination is legal under Canada's international obligation.

3. *New Federal Taxes and Charges*

a. Royalties from Canada lands

The new Canada Oil and Gas Act,[55] enacted as part of the NEP, assesses a ten percent royalty on all production from the Yukon and Northwest Territories, the Arctic Ocean (including the Beaufort Sea), and the federal offshore areas.[56] An additional progressive incremental royalty equal to forty percent of the net profits of an oil and gas field must be paid by producers whose

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52. NEP, *supra* note 1, at 38-39. Amendments to §§ 1205-1206 of the Income Tax Regulations, ch. 945, Consol. Regs. Can. (1978) (as amended), implement this aspect of the NEP. *See* 1981 P.C. 3329 (Nov. 26, 1981), *reprinted in* Can. Gaz., pt. II, at 3739 (Dec. 9, 1981).

53. *See* Watkins, *supra* note 47, at 86-91. Originally, the depletion allowance on conventional lands was to be phased out in 1984. *See* NEP, *supra* note 1, at 39, and amendments to the Income Tax Regulations, ch. 945 Consol. Regs. Can. (1978). The Canada-Alberta Agreement of September 1, 1981, however, extends the phasing out process by one year, thus requiring further amendments to the Income Tax Regulations. At the time of this Article's completion, those amendments had not been passed.

54. *See infra* notes 97-113 and accompanying text.

55. Ch. 81, 1980-1982, Can. Stat., *reprinted in* III Can. Gaz., vol. 6, no. 12, at 2655 (1981).

56. *Id.* § 40(1).

rate of return is over twenty-five percent.[57] Net profits will be computed after deducting investment and capital allowances.[58] These royalties are justified because they represent the price paid to the owner of the resource for the privilege or right to explore and extract it. Their equivalent may be found in provincial legislation[59] and in contracts involving freehold land.

b. The Petroleum and Gas Revenue Tax

As originally proposed in the NEP, a new Petroleum and Gas Revenue Tax (PGRT) of eight percent of Canadian oil and gas production revenue was to be levied beginning January 1, 1981. The tax also applied to royalty payments based on oil and gas production. The purpose of the tax was to increase the federal government's share of the revenue from Canadian oil and gas production.[60] Industry strongly opposed this new tax for two reasons.[61] First, industry felt that the tax was structured to resemble a royalty payable to the owner of the resource because it was not deductible as an expense for income tax purposes. Second, industry argued that the PGRT was equivalent to a tax of approximately twelve percent.[62] Nonetheless, the PGRT proposal was confirmed and expanded by the Canada-Alberta Agreement of September 1, 1981,[63] that provided for a sixteen percent PGRT with a possible twenty-five percent resource allowance deduction.[64] This tax can be criticized on the grounds that it disregards

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57. *Id.* § 41(1).

58. *Id.* § 41(5). For a comprehensive study, see Wickerson, *Canada Oil and Gas Act*, in TAX TREATMENT OF THE PETROLEUM INDUSTRY UNDER THE NATIONAL ENERGY PROGRAM—A TECHNICAL ANALYSIS 129 (1982) (Canadian Tax Foundation).

59. *See, e.g.*, Mines and Minerals Act, ALTA. REV. STAT., ch. M-15 §§ 13(3), 28, 113 (1980); Alta. Reg. 23/74, Alta. Gaz. pt. II, at 223 (Apr. 15, 1974), *amended by* Alta. Regs. 251/74, 243/76, 9/77, 249/79, 268/79, & 162/80.

60. *See* NEP, *supra* note 1, at 37-38. For details on the PGRT, see PRICE, WATERHOUSE & CO., *supra* note 45, at 14-15; Watkins, *supra* note 47, at 112-17.

61. *See, e.g.*, McCallum, *Mobil Canada cites NEP as it cuts spending plans*, The Globe & Mail (Toronto), Jan. 22, 1981, at B2; *see also* McCallum, *Independent Oilmen's President calls NEP a National disaster*, The Globe & Mail (Toronto), Mar. 11, 1981, at B7; Transcript of direct evidence by witness of Amoco Canada Petroleum Co. before the National Energy Board at 4 (Jan. 1981).

62. For effects on profits, see W. DOBSON, CANADA'S ENERGY POLICY DEBATE 24 n.32 (C.D. Howe Institute 1981).

63. *See* Canada-Alberta Agreement, *supra* note 11, at 10.

64. *Id.* As far as the resource allowance is concerned, amendments to the

the company's ability to pay and that only infinitesimal deductions are allowed in computing the production revenue.

The Petroleum and Gas Revenue Tax Act[65] enacted the PGRT. Amendments were needed, however, because the Agreement of September 1, 1981, between the federal government and the Government of Alberta on energy pricing and taxation imposed a new rate.[66] Also, the *NEP Update* of 1982 announced a reduction of the PGRT rate from sixteen percent to fourteen and two-thirds percent for a one year period beginning June 1, 1982,[67] along with a small producer's PGRT exemption of $250,000.[68]

c. The Natural Gas and Gas Liquids Tax

As originally planned under the NEP, all natural gas sales would have been subjected to a new Natural Gas and Gas Liquids Tax (NGGLT).[69] As often happens in Canada, this unilateral tax measure, which was imposed by one level of government for its own benefit, was partially rescinded after much legal and political debate.[70] The NEP had proposed that all domestic and export natural gas sales be subject to a levy under a new Natural Gas and Gas Liquids Tax that was later enacted by amending the Excise Tax Act.[71] The rate was set initially at $0.30 per million cubic feet and was to increase gradually to $0.75 per million cubic feet by 1983.[72] Provincial reaction was swift and immediate. Saskatchewan and British Columbia witheld payment of the tax.[73] Alberta

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Income Tax Regulations, CONSOL. REGS. CAN., ch. 945, § 1210(1) (1978), must be passed.

65. An Act to amend the Excise Tax Act and the Excise Act and to provide for a revenue tax in respect of petroleum and gas, ch. 68, 1980-1982 Can. Stat., secs. 78-117, *reprinted in* III Can. Gaz. vol. 6, no. 10, at 2457 (1981).

66. *See* An Act to amend the statute law relating to certain taxes, ch. 104, 1980-1982 Can. Stat. § 20, *reprinted in* III Can. Gaz., vol. 6, no. 16, at 3087 (1982) (amending the Petroleum and Gas Revenue Tax Act § 84).

67. NEP UPDATE, *supra* note 2, at 73. At the time of completion of this Article, September 1982, no implementing legislation had been tabled.

68. *Id.* at 74. Again, implementing legislation is not yet tabled.

69. NEP, *supra* note 1, at 35-36.

70. Canada-Alberta Agreement, *supra* note 11, at 9.

71. Ch. 68, 1980-1982 Can. Stat. § 43, *reprinted in* III Can. Gaz., vol. 6, no. 10, at 2457 (1981).

72. *Id.* (adding to the Excise Tax Act § 25.13).

73. These provinces finally came to terms with the federal government in agreements similar to the Canada-Alberta Agreement, *supra* note 11. The Canada-British Columbia Agreement, *reprinted in* 1982 CAN. ENERGY PROGRAM REP.

challenged the constitutional validity of the new tax in court and won, although the victory was limited in scope because the fact situation was very narrow.[74]

In the Canada-Alberta Agreement on Energy Pricing and Taxation of September 1, 1981, the federal government agreed "to reduce the NGGLT to a zero rate on exports of natural gas originating in an agreeing province."[75] The Agreement adds, however, that "[t]his decision is without prejudice to the Government of Canada's position that it has the right to levy such a tax."[76] The zero rate will remain in effect until December 31, 1986. The levy will remain for domestic gas sales.

d. Other changes

(i) Petroleum Compensation Charge.—The NEP proposes a new Petroleum Compensation Charge, to be borne by the consumer, that will compensate for the difference between the cost of domestic and federally-subsidized imported oil.[77] This charge was implemented by amendments to the Petroleum Administration Act.[78]

(ii) Federal Export Tax.—The NEP, as originally proposed in 1980, recites that "an export tax is levied on oil equal to the difference between the domestic price and the export price."[79] The tax, levied under the Petroleum Administration Act,[80] will remain, but the revenues are to be shared with the producing provinces, on a fifty percent basis.

(iii) Canadian Ownership Tax.—As mentioned above, Canadianization is the object of the NEP. To help finance this goal, the NEP proposed a levy on Canadian oil and gas consump-

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(CCH) 75,501, was signed on September 24, 1981, and the Canada-Saskatchewan Agreement, *reprinted in id.* at 76,101, was signed on October 26, 1981.

74. *See supra* notes 19-20 and accompanying text.

75. *See* Canada-Alberta Agreement, *supra* note 11, at 9.

76. *Id.*

77. NEP, *supra* note 1, at 30.

78. *See* Petroleum Administration Act, ch. 47, 1974-1976 Can. Stat., *amended by* ch. 28, 1976-1977 Can. Stat.; ch. 24, 1977-1978 Can. Stat.; ch. 114, 1980-1982 Can. Stat., secs. 29-38 (new pt. III.1 entitled Petroleum Compensation Charge).

79. NEP, *supra* note 1, at 36.

80. Ch. 47, 1974-1976 Can. Stat. § 7, *amended by* ch. 114, 1980-1982 Can. Stat., sec. 4.

tion.[81] The rate of the levy, to be determined by regulations promulgated under the Petroleum Administration Act,[82] is unspecified because it depends upon the progress toward Canadianization made through state acquisitions. For instance, after the Petrofina acquisition of 1981, a Canadian Ownership Tax of $1.15 per barrel of oil and $0.15 per million cubic feet of natural gas was levied.[83] The cost of this tax, also called the Canadianization Tax, is to be borne by the consumer. Future acquisitions obviously will increase this tax.

(iv) Incremental Oil Revenue Tax.—The Canada-Alberta Agreement of September 1, 1981, had the effect of imposing yet another levy, the Incremental Oil Revenue Tax (IORT) that was introduced in the federal budget of November 12, 1981, and became effective January 1, 1982.[84] The tax "will be 50 percent of the additional revenues the industry receives as a result of prices on old oil being higher than prices set out in the 1980 National Energy Program."[85] On the other hand, this incremental old oil revenue will not be subject to income taxation.[86] The *NEP Update* of May 31, 1982, announced that the tax would be suspended from June 1, 1982 to May 31, 1983,[87] in order to alleviate present cash flow problems in the oil industry.

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81. NEP, *supra* note 1, at 51.

82. An Act to amend the Petroleum Administration Act and to enact provisions related thereto, ch. 114, 1980-1982 Can. Stat., sec. 39 (adding pt. III.2 entitled Canadian Ownership Provisions).

83. *See* PRICE, WATERHOUSE & CO., *supra* note 45, at 20.

84. *See* Canada-Alberta Agreement, *supra* note 11, at 10. The IORT has been implemented in An Act to amend the statute law relating to certain taxes, secs. 19-20 (adding § 83.1 and amending § 84 of the Petroleum and Gas Revenue Tax Act).

85. THE BUDGET IN MORE DETAIL, Nov. 12, 1981, at 57.

86. *See* PRICE, WATERHOUSE & CO., *supra* note 45, at 17; *see also* Canada-Alberta Agreement, *supra* note 11, at S17 ("incremental revenue will be excluded from income for the purposes of income taxation"). This has been enacted by An Act to Amend the statute law relating to certain taxes, sec. 31(1) (amending the Income Tax Act § 81(1)).

87. *See* NEP UPDATE, *supra* note 2, at 74 (the one year elimination is to be implemented through the regulatory process).

III. Specific Canadianization Provisions of the Canadian Energy Program

A. Canadian Ownership and Control and the Petroleum Incentives Program

Bill C-104, assented to in June 1982,[88] includes a Canadian Ownership and Control Determination Act along with a Petroleum Incentives Program Act whereby incentives available under the latter are based upon eligibility criteria provided by the former.

1. *The Canadian Ownership and Control Determination Act*

This Act established a legislative framework for the administrative certification of the Canadian ownership rate (COR) and status of Canadian control of persons, including corporations. These criteria will be used to implement some of the Canadianization objectives of the NEP such as Petroleum Incentives Program Payment applications, or production license applications in the Canada lands.

This type of legally enacted economic nationalism is not new to Canada. The Foreign Investment Review Act of 1974 (FIRA)[89] serves both as a background to the NEP and as a model for the COR concept. The main purpose of FIRA was to ensure that new direct foreign investment would be authorized only if it was beneficial to Canada. Section 2 of the FIRA contains a lengthy description of this aim.[90] The Act provides five criteria for use in

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88. An Act Respecting Petroleum Incentives and Canadian Ownership and Control Determination and to amend the Foreign Investment Review Act, ch. 107, 1980-1982 Can. Stat., *reprinted in* III Can. Gaz., vol. 6, no. 16, at 3131 (1982).

89. Ch. 46, 1973-1974 Can. Stat.

90. *Id.* § 2(1). Section 2(1) provides:

This Act is enacted by the Parliament of Canada in recognition by Parliament that the extent to which control of Canadian industry, trade and commerce has become acquired by persons other than Canadians and the effect thereof on the ability of Canadians to maintain effective control over their economic environment is a matter of national concern, and that it is therefore expedient to establish a means by which measures may be taken under the authority of Parliament to ensure that, in so far as is practicable after the enactment of this Act, control of Canada business enterprises may be acquired by persons other than Canadians, and new businesses may be established in Canada by persons, other than Canadians, who are not already carrying on business in Canada or whose new businesses in determining whether a proposed investment is beneficial to Canada.[91] The FIRA applies to two types of foreign investments: first, the acquisition of control of a Canadian business enterprise by foreign individuals, corporations, governments, or groups containing foreign members through the acquisition of assets or shares; and second, the establishment of a new business in Canada by foreign persons who do not already have an existing business in Canada, or by foreign persons who have an existing business in Canada if the new business is unrelated to the existing business.[92] There are, of course, thresholds to the review procedure.[93]

Canada would be unrelated to the businesses already being carried on by them in Canada, only if it has been assessed that the acquisition of control of those enterprises or the establishment of those new businesses, as the case may be, by those persons is or is likely to be of significant benefit to Canada, having regard to all of the factors to be taken into account under this act for that purpose.

91. *Id.* § 2(2)(a)-(e). That section provides:

(a) [T]he effect of the acquisition or establishment on the level and nature of economic activity in Canada, including, without limiting the generality of the foregoing, the effect on employment, on resource processing, on the utilization of parts, components and services produced in Canada, and on exports from Canada;

(b) the degree and significance of participation by Canadians in the business enterprise or new business and in any industry or industries in Canada of which the business enterprise or new business forms or would form a part;

(c) the effect of the acquisition or establishment on productivity, industrial efficiency, technological development, product innovation and product variety in Canada;

(d) the effect of the acquisition or establishment on competition within any industry or industries in Canada; and

(e) the compatibility of the acquisition or establishment with national industrial and economic policies, taking into consideration industrial and economic policy objectives enunciated by the government or legislature of any province likely to be significantly affected by the acquisition or establishment.

92. *Id.* § 3(1).

93. *See id.* § 5(1)(c), which provides that the Act does not apply to the acquisition of a business enterprise whose gross assets do not exceed $250,000 and whose annual gross revenue does not exceed $3 million. *See also* Foreign Investment Review Regulations, § 6(1), which provide an abbreviated form of notice for small business investment proposals involving the establishment or acquisition of a business with gross assets of less than $2 million and fewer than 100 employees. The last federal budget proposed to raise this threshold to $5 million and 200 employees. 124 H.C. DEBATES, no. 370, at 18,880-81 (June 28, 1982).

Bill C-104 requires individuals, corporations, partnerships, and trusts to have a certificate showing their Canadian ownership rate (COR) and their control status. The bill provides that the following persons are qualified to apply for a certificate:

> (a) an individual other than a non-eligible person;
> (b) a corporation incorporated in Canada;
> (c) a partnership . . . governed by the laws of a province;
> (d) a trustee in respect of a trust, if the trustee and beneficiaries are, with respect to their status as such, governed by the laws of a province;
> (e) an insurance company incorporated in Canada in respect of any of its segregated funds within the meaning of the regulations; and
> (f) any person prescribed as being qualified to apply for a certificate or who falls into a class of persons prescribed as being qualified to apply for a certificate.[94]

The term "non-eligible person" as used by subsection (a) is defined in the FIRA.[95] Persons qualified to apply under subsection (f) are listed in section 6 of the Canadian Ownership and Control Determination (Draft) Regulations which provides that "[a] corporation incorporated outside Canada is qualified to apply for a certificate if (a) it is wholly owned by a corporation incorporated in Canada, (b) it was incorporated prior to October 29, 1980, and (c) its activities have been conducted primarily in Canada at all times after October 28, 1980."[96]

The application must be filed in the form and manner prescribed by the regulations. Similarly, the COR and control status

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94. Ch. 107, 1980-1982 Can. Stat. § 37, *reprinted in* III Can. Gaz., vol. 6, no. 16, at 3131 (1982).

95. *Id.* § 35(2). Section 35(2) provides: "For the purposes of this Part, the expression 'non-eligible person' has the same meaning as it has under section 3 of the Foreign Investment Review Act. . . ." Section 3 of the Foreign Investment Review Act defines a "non-eligible person" as including "an individual who is neither a Canadian citizen or a permanent resident or a corporation incorporated in Canada or elsewhere that is controlled directly or indirectly by such an individual or group of individuals." Foreign Investment Review Act, ch. 46, 1973-1974 Can. Stat. § 3.

96. CANADIAN DEPARTMENT OF ENERGY, MINES AND RESOURCES, CANADIAN OWNERSHIP AND CONTROL DETERMINATION DRAFT REGULATIONS (1982) [hereinafter cited as DRAFT REGULATIONS]. At the time of completion of this writing the final regulations had not yet been passed; however, the Petroleum Incentives Act, *supra* note 3, ch. 107, 1980-1982 Can. Stat. § 62(1), gives temporary status to the draft regulations for a first application made within six months after part II comes into force. *Id.*

are determined in accordance with Part II of the Act and the regulations.[97] Certain persons are presumed to have a 100 percent COR.[98] These persons still must establish the facts that give rise to that presumption in order to obtain their COR certificate.[99] An applicant who asks for a control status certificate also must show that he is under Canadian control because the COR designation does not create control status.[100]

For most applicants, the COR is determined on the basis of formal equity.[101] In the case of corporate applicants, this is done by measuring the percentage of shares held by Canadians.[102] When partnerships or trusts are involved, the relationship between the Canadian participation and the capital or income must be deter-

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97. Petroleum Incentives Act, *supra* note 3, § 38; *see also* DRAFT REGULATIONS, *supra* note 96, at pt. II, §§ 12-25.

98. *See* DRAFT REGULATIONS, *supra* note 96, §§ 7-10.

99. Section 7 of the DRAFT REGULATIONS, *supra* note 96, provides: "[t]he . . . persons . . . are deemed to have a COR of 100% *if they are qualified* to apply for a certificate." *Id.* § 7.

100. Indeed, Canadian control is determined under §§ 35(2) and 38(2) of the Petroleum Incentives Act, *supra* note 3, which refers, with certain exceptions, to the concept of the "non-eligible person" of the Foreign Investment Review Act, ch. 46, 1973-1974 Can. Stat. The control status is, therefore, determined under the latter.

101. *See* DRAFT REGULATIONS, *supra* note 96, § 12.

102. The COR of a person, which has one class of formal equity (as defined hereinafter), shall be the beneficial ownership of that class of formal equity determined in accordance with part two of the DRAFT REGULATIONS, *supra* note 93, and the COR rate of a person which has more than one class of formal equity shall be: "(a) [T]he weighted average of the beneficial ownership of those classes of formal equity which in the opinion of the Minister may be weighted, or (b) the lowest of the beneficial Canadian Ownership of each class of formal equity determined in accordance with this part." *See* DRAFT REGULATIONS, *supra* note 96, §§ 6, 12-13. Formal equity means:

> (a) with respect to a corporation, any share of the corporation, other than a share excluded by the regulations, that is, or is deemed under the regulations to be, issued and outstanding,
>
> (b) with respect to a partnership, any interest or right in the capital or income, or both, of the partnership,
>
> (c) with respect to a trust, any beneficial interest in the property of the trust and
>
> (d) with respect to any other person, such interest or right in respect of that person as is prescribed . . . .

Petroleum Incentives Act, *supra* note 3, ch. 107, 1980-1982 Can. Stat. § 35. For the rules determining the beneficial Canadian ownership of a class of formal equity, see *id.* §§ 19-20.

mined.[103] This Article will not examine at length the detailed COR calculation rules because they have been covered elsewhere.[104] For present purposes, it is sufficient to note that these rules, which are contained in the regulations, provide that, when the applicant is a corporation, partnership, or trust, the COR level of each class of ownership must be measured.[105] A class of ownership may comprise shares in a corporation, debts that are equity investments, or interests in a partnership.[106] To determine the COR of an applicant, the COR of each class of formal equity must be determined in order to calculate a weighted average. If this is not practicable, the COR of the applicant will be the lowest COR of the classes.[107]

An examination of the list of a corporation's shareholders is not sufficient to determine the COR of a class if the list includes corporate shareholders.[108] In such a case, the citizenship and residence of the investors in the shareholding corporations are examined to the extent of the third link of arms-length ownership.[109]

The FIRA and its regulations provide the method used to determine Canadian control.[110] This method is designed to identify the person or group of persons who are in effective control, as opposed to legal control, of the applicant.

COR and control status certificates are to be issued by the Minister of Energy, Mines and Resources.[111] Generally, a certificate becomes effective as of the acknowledged date of receipt of the application and, subject to material variations, it continues to be effective for one year or for such longer period—not to exceed two years—as may be prescribed by regulation.[112] The holder of a certificate must file a new application or amend his original appli-

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103. *See supra* note 102.

104. *See, e.g.*, PETROLEUM MONITORING AGENCY, METHOD FOR MEASUREMENT OF CANADIAN OWNERSHIP AND DETERMINATION OF CONTROL UNDER THE NATIONAL ENERGY PROGRAM, (Rep. No. M27-24/1981 E) (1981). *See generally* Watkins & McKee, *supra* note 47.

105. *See supra* note 102.

106. *Id.*

107. *See* Watkins & McKee, *supra* note 47, at 65-66.

108. *Id.* at 67-70.

109. *Id.* at 71.

110. Ch. 46, 1973-1974 Can. Stat.

111. Ch. 107, 1980-1982 Can. Stat. § 39(3).

112. *Id.* § 42(1).

cation when any one of the following occurs:

> (a) the certificate shows the holder to be Canadian controlled and he has ceased to be Canadian controlled;
> (b) the Canadian ownership rate of the holder has decreased in the circumstances prescribed by more than the prescribed number of percentage points;
> (c) the holder knows or ought to know that the certificate was issued on the basis of an erroneous determination or false or misleading information;
> (d) the holder knows or ought to know that any provision of an agreement, arrangement or undertaking that was submitted with the application for the certificate was breached or was not fully observed; or
> (e) the Minister requires the application or amendment to be made . . . .[113]

An applicant may file in the same way if its Canadian ownership rate has increased or if it has become Canadian controlled.[114]

2. *The Petroleum Incentives Program*

The Petroleum Incentives Program (PIP) was also enacted by Bill C-104.[115] As stated in the NEP, the program has the following two objectives:

> [E]stablish the basis for Canadians to seize control of their own energy future through *Security* of supply and ultimate independence from the world oil market; [and] Offer to Canadians, all Canadians, the real *opportunity* to participate in the energy industry in general and the petroleum industry in particular, and to share in the benefits of industry expansion.[116]

The primary aim of PIP is to meet these objectives of energy security while encouraging increased Canadian ownership and control of the industry. In fact, however, this program mainly replaces existing earned depletion allowance tax incentives. A 1981 departmental paper noted:

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113. *Id.* § 43(1).
114. *Id.* § 43(3).
115. Petroleum Incentives Act, *supra* note 3, ch. 107, 1980-1982 Can. Stat., pt. I. As a result of the Canada-Alberta Agreement, *supra* note 11, the government of Alberta administers and finances its own PIP program. The two programs are similar.
116. *See* NEP, *supra* note 1, at 2.

To date, the major federal incentives for oil and gas exploration and development have been provided through the income tax system. The PIP represents an attempt to move away from this tax-based incentives system, which was only of benefit to firms in a taxable position, to one which delivers grants to firms directly. It is expected that the program will help maintain and, indeed, accelerate the pace of exploration and development activity in Canada.[117]

As mentioned earlier, the NEP also stated that the federal government was committed to achieving at least fifty percent Canadian ownership of the industry by 1990.[118] The federal government apparently believes that the industry also will meet these objectives through PIP while maintaining an attractive investment environment for foreign-owned firms.[119]

The PIP concept is simple; it calls for cash incentive payments, in addition to the general Crown share incentive of twenty-five percent of exploration expenses in the Canada lands, to applicants that are Canadian-controlled and have a COR of fifty percent or more with respect to certain exploration, development, and asset costs.[120] The incentives increase as the COR increases and represent a determined percentage of the expenditures incurred. The incentives also depend on the type of expenditures, the area involved, and the year in which these expenses were incurred.[121] The extent of PIP grants available is indicated by the

117. CANADIAN DEPARTMENT OF ENERGY, MINES AND RESOURCES, THE PETROLEUM INCENTIVES PROGRAM at vii (1981).

118. *See* NEP, *supra* note 1, at 102-03.

119. In the Canada lands, a Crown share incentive of 25% is available to all companies which are incurring eligible exploration expenditures as defined. Petroleum Incentive Act, *supra* note 3, § 3. This Crown share incentive is supposed to promote exploration while providing a share of such expenditures commensurate with the Government's retained interest in the Canada lands.

120. These terms are defined in the Petroleum Incentives Programs Regulations, 116 Can. Gaz. §§ 9-11, at 2439 (1982). Hence, the eligible exploration and development expenses are "Canadian exploration expense" and "Canadian development expense," subject to prescribed modifications, under the Income Tax Act §§ 66.1(6)(a), 66.2(5)(a), and the eligible asset costs are prescribed by the regulations to be the capital cost of new tertiary recovery equipment and the cost of converting previously used equipment into tertiary recovery equipment. *Id.*

121. The ranges of COR are described at § 10 of the Petroleum Incentives Act, *supra* note 3, and the levels of incentives are described in §§ 7-9 of the same Act.

following table:[122]

PIP PAYMENTS AS A PERCENTAGE OF EXPENDITURES

COR level of applicant*	Provincial Lands		Canada Lands	
	Exploration expenses	Development expenses & asset costs	Exploration expenses**	Development expenses & asset costs
Level 1 (1981-1986)	-	-	25	-
Level 2 (1981)	-	-	35	-
(1982-1983)	10	10	45	10
(1984-1986)	15	10	50	10
Level 3 (1981-1986)	25	15	65	15
Level 4 (1981-1986)	35	20	80	20

*Canadian individuals are deemed to have a COR level of 4. Corporation COR levels are as follows:

Level 1: less than 50% COR.
Level 2: 50% COR plus.
Level 3: 60% COR in 1981, increasing 1% per year to 65% by 1986.
Level 4: 65% COR in 1981, increasing 2% per year to 75% by 1986.

**Percentages include the 25% Crown Share Incentive (section 3 of Petroleum Incentives Program Act).

Note that PIP grants are available only to participants who own a working interest in property or who are acquiring a working interest as a result of those expenditures for which they are seeking PIP grants.[123] There are also "anti-leakage" rules that prevent PIP payments to entities with insufficient COR levels.[124] The rules provide for lowering eligible expenses; this usually will occur when entities with different COR levels have an interest in the same oil or gas play.

B. Canadianization Measures Under the Canada Oil and Gas Act

As previously mentioned, the NEP includes a Canada Oil and Gas Act[125] that makes considerable changes in the regulation of

122. *See* PETROLEUM INCENTIVES ADMINISTRATION, APPLICANT'S GUIDE app. 3, at 58 (1982) (Minister of Supply and Services).

123. Petroleum Incentives Act, *supra* note 3, pt. I, § 4(b); Petroleum Incentives Program Regulations, 116 Can. Gaz. § 8, at 2439 (1982).

124. *See* Petroleum Incentives Program Regulations, 116 Can. Gaz., pt. II, at 2439 (1982).

125. Ch. 81, 1980-1982 Can. Stat. Actually, the title is deceiving. A Federal Lands Oil and Gas Act would not have been such a misnomer. Indeed, most of

oil and gas in the Canada lands.[126] The new act will govern exploration, development, and production activities on these lands because the previously existing system of licenses and permits under the old Canada Oil and Gas Lands Regulations[127] is now being phased out. The former system will be replaced by detailed exploration agreements during a corresponding phase-in period.[128]

Canadian oil and gas legislation applies to lands under Provincial jurisdiction. The title must thus be understood in the political context of Canadian Federalism.

126. *Id.* § 2(1). "Canada Lands" refers to those areas of Canada not within Provincial boundaries. It has the meaning of:

> . . . lands that belong to Her Majesty in right of Canada, or in respect of which Her Majesty in right of Canada has the right to dispose of or exploit the natural resources and that are situated in
>
> (a) the Yukon Territory or the Northwest Territories, or Sable Island, or
>
> (b) those submarine areas, not within a province, adjacent to the coast of Canada and extending throughout the natural prolongation of the land territory of Canada to the outer edge of the continental margin or to a distance of two hundred miles from the baselines from which the breadth of the territorial sea of Canada is measured, whichever is the greater.

Id.

As far as the application of the Act to Canada's East Coast is concerned, an agreement between the Government of Canada and the Government of Nova Scotia was reached on March 2, 1982, *reprinted in* 1982 CAN. ENERGY PROGRAM REP. (CCH) 76,501, relating to oil and gas resource management and revenue sharing in Nova Scotia's offshore area without prejudice to their respective legal positions. The agreement provides for a joint Board of five members, three of which represent the Canadian Government and two of which represent the Nova Scotian Government, chaired by the Administrator of the Canada Oil and Gas Lands Administration. An agency, which reports to the Board, administers oil and gas activities under the Canada Oil and Gas Act, ch. 81, 1980-1982 Can. Stat. The agreement also provides for mechanisms regarding respective participation to the Crown share and the sharing of revenues such as royalties under the Canada Oil and Gas Act or the petroleum and gas revenue tax. No agreement between the Government of Canada and the Government of Newfoundland had been reached at the time of completion of this writing. For a discussion regarding the jurisdictional question, see R. HARRISON, *supra* note 20.

127. The former regulations, Canada Oil and Gas Regulation, CONSOL. REGS. CAN., ch. 1518 (1978), remain in force to the extent that they are consistent with the new Act until they are revoked or replaced by new regulations. All interests provided by the former regulations that were in force when the new Act was enacted continue in force subject to §§ 63-73 of the new Act. The interests provided for under the Canada Oil and Gas Act, ch. 81, 1980-1982 Can. Stat., replace all oil or gas rights or prospects acquired or vested in relation to Canada lands prior to the enactment of the new Act. *Id.* §§ 61(1), 62(1)-(2).

128. *Id.*

An exploration agreement for Canada lands confers "the right to explore for and the exclusive right to drill for oil or gas, the exclusive right to develop those Canada lands in order to produce oil or gas and the exclusive right, subject to compliance with the other provisions of this Act, to obtain a production licence."[129]

The provisions of the exploration agreements are quite comprehensive,[130] and some specifics with transnational implications will be dealt with below. First, an exploration agreement requires that participants submit a plan to the Minister of Energy, Mines and Resources for approval prior to the commencement of any work program. The plan must contain provisions for the employment of Canadians and for providing Canadian manufacturers, consultants, contractor and service companies with a full and fair opportunity to participate on a competitive basis in the supply of goods and services.[131] Second, the exploration agreement may require equity participation by the Government of Canada and Canadians, including any aboriginal peoples of Canada that may be affected by the exploration agreement.[132]

A point of contention is the Crown share mentioned in section 27 of the Act. Section 27 reads as follows:

> (1) "Crown share" means the share reserved to Her Majesty in right of Canada under subsections (2) and (3).
> (2) Subject to subsection 62(5), there is hereby reserved to Her Majesty in right of Canada, and the Minister of Energy, Mines and Resources on Her behalf shall hold, a twenty-five percent share
>
> > (a) in an interest provided under this Act in respect of Canada lands that were Crown reserve lands immediately prior to the interest; and
> > (b) in the first interest provided in respect of the relevant Canada lands under any of sections 63, 64 and 66.
>
> (3) Subject to being disposed of pursuant to section 32, the share of Her Majesty in right of Canada under subsection (2) is reserved out of any interest that succeeds the interest, out of which it was previously reserved.[133]

An exception alleviates the effect of this drastic provision. The

129. *Id.* § 9.
130. *Id.* §§ 9-16.
131. *Id.* § 10(2)-(3).
132. *Id.* § 10(2)(d).
133. *Id.* § 27. Paragraph 27(2)(b) refers to transitional provisions. *Id.*

twenty-five percent interest is exacted whether or not the lands already are subject to a supposedly exclusive license or permit *unless* production commenced before 1981.[134]

Section 61(2) of the Canada Oil and Gas Act also relates to the Crown share and reads as follows:

> No party shall have any right to claim or receive any compensation, damages, indemnity or other form of relief from Her Majesty in right of Canada or from any servant or agent thereof for any acquired, vested or future right or entitlement or any prospect thereof that is replaced or otherwise affected by this Act, or for any duty of liability imposed on that party by this Act.[135]

Moreover, after December 31, 1982, an exploration agreement must provide that, as periodically required by the Minister, each interest holder shall obtain and provide the Minister with evidence that the interest holder's COR is in a form satisfactory to the Minister.[136]

Once the exploration phase has ended, the production stage begins. A production license is required to confer the exclusive right to produce oil and gas and pass title to the oil or gas produced,[137] subject to the payment to the Crown of any applicable royalty.[138] The Minister will not grant or renew a production license unless satisfied that the beneficial owner of the license has a COR of at least fifty percent. The Act thus provides that the licensee:

> (a) if an individual, would be a Canadian citizen ordinarily resident in Canada or a permanent resident within the meaning of the Immigration Act, 1976, other than one who has been ordinarily resident in Canada for more than one year after the time at which he first became eligible to apply for Canadian citizenship;
> (b) if a corporation, would be incorporated in Canada and have a Canadian ownership rate of not less than fifty percent; or
> (c) if two or more individuals or corporations or individuals and corporations would be comprised of individuals referred to in paragraph (a) or corporations incorporated in Canada or both and would have a Canadian ownership rate of not less than fifty

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134. *Id.* § 28.

135. *Id.* § 61(2). Limited cases exist where compensation is paid for expenses incurred before 1981, but this compensation only will be payable out of future profits. *See id.* § 29.

136. *Id.* § 10(5).

137. *Id.* § 17.

138. *Id.* §§ 40-41.

percent.[139]

The Act also covers applicants whose COR is below fifty percent or falls below fifty percent during the term of the license.[140] In such cases, the Crown will own a share in the production license equal to the difference between fifty percent and the actual COR of the interest owner, as determined by the Minister. This Crown share will be disposed of at the earliest opportunity by a public tender open only to those parties with a seventy-five percent COR, and to individuals as previously defined.[141]

It readily can be seen that this Act changes the law considerably. Although somewhat outside the scope of this Article, it should be mentioned that some criticism has been aimed at other provisions of the Act, such as those involving transfer and assignment, cancellation of rights and production orders, the new royalty regime, and the broad discretionary powers.[142]

C. The Act to Amend the Canada Business Corporations Act

To properly implement the NEP's Canadian ownership and control provisions, corporations had to be given adequate legal means to operate under the new rules. Because federal company law was ill-equipped for this purpose, the Canada Business Corporations Act had to be amended.[143] The Act made the following two changes: (1) a corporation henceforth will have the power to hold shares in itself to assist it or any of its affiliates or associates to qualify for licenses, permits, grants, payments, or other benefits;[144] and (2) a corporation henceforth will have the power to restrict the issue and ownership of new classes of shares.[145] These

139. *Id.* § 19(1).

140. *Id.* § 23(1)-(2).

141. *Id.* §§ 19(1), 23(6).

142. *See, e.g., Submission to the Standing Committee on National Resources and Public Works on Bill C-48* (statement by the Canadian Bar Association), *reprinted in House of Commons, Minutes of Proceedings and Evidence of the Standing Committee on National Resources and Public Works,* Issue No. 421, app. "RESS-35," at 42A:132 (1981); *see also Brief* (submitted by Dome Petroleum Limited), *reprinted in id.,* Issue No. 43, app. "RESS-36," at 43A:1 (1981).

143. Canada Business Corporations Act, ch. 33, 1974-1976 Can. Stat. (as amended).

144. An Act to amend the Canada Business Corporations Act, ch. 115, 1980-1982 Can. Stat. cl. 2 (enacting § 31.1).

145. *Id.* cls. 1, 8 (enacting §§ 6(1)(d), 168).

amendments will enable a corporation to attain or maintain a specified level of Canadian ownership or control. The Act also provides for coercive machinery to enforce these provisions.[146] Thus, a corporation will be able to sell constrained shares held by a shareholder in violation of these provisions. Such constraints must be noted conspicuously on the share certificates; moreover, the corporation will not have the power to sell the shares unless it has given notice and has followed the conditions prescribed by federal regulations.[147] The proceeds of the sale form a trust fund for the benefit of the divested owner.[148]

These amendments, though technical in nature, constitute a departure from the usual standard of free ownership and transfer of shares of public corporations because foreign investors are precluded from acquiring them.[149] Within the context of the general design of Canadianization, however, these changes are logical.

D. Other Canadianization Provisions

The NEP originally announced the establishment of a new Crown corporation that would have operated as a "national gas bank" to purchase gas that could not be sold to Canadian-controlled firms.[150] No legislation to implement this provision was introduced and, in *National Energy Program Update* of May 31, 1982,[151] the federal government announced that it had "decided not to proceed with the Gas Bank."[152] The NEP also mentioned that the National Energy Board would be asked to give preference to Canadian-owned and Canadian-controlled firms when considering export applications.[153] No implementing legislation has been introduced.

The Canadian ownership tax[154] is another major component of

146. *Id.* cl. 4 (adding pt. V.1 entitled Sale of constrained shares to the CBCA §§ 43.1-.2).

147. *Id.* cl. 5 (enacting § 45(8.2)); cl. 4 (enacting § 43.1).

148. *Id.* § 43.2.

149. The United States administration has expressed its concern over the measures stating that they "could depress prices of stock in foreign hands since non-Canadians could be excluded as potential shareholders." *See* Hormats, *supra* note 14, at 54.

150. *See* NEP, *supra* note 1, at 42.

151. *See* NEP UPDATE, *supra* note 2.

152. *Id.* at 63.

153. *See* NEP, *supra* note 1, at 50.

154. *See supra* notes 81-83 and accompanying text.

Canadianization because it provides for a fund enabling the federal government to acquire the Canadian assets of multinational oil companies.[155] Finally, it must be mentioned that the NEP seems to instruct the Foreign Investment Review Agency to review carefully transactions by foreigners that involve a change of control or the establishment of a new business in the Canadian oil and gas industry.[156] Mounting criticism of this approach in the United States and in Canada,[157] however, eventually could elicit a less demanding attitude from the Agency.

IV. International Commercial Law Aspects of the Canadian Energy Program

A. Discrimination and the NEP: An Overview

The NEP clearly discriminates against foreign-owned or controlled interests. Whether this discrimination is legal remains an open question. It is appropriate at this juncture to present facts, reactions, statements of the law, and opinions that may be useful if a party such as the United States seeks legal recourse.

1. *Discriminatory Measures in the NEP*

The National Energy Program is discriminatory in the sense that foreign-owned firms are treated less favorably than Canadian-owned firms when applying for production licenses, exploration incentive grants, and national treatment generally. The main discriminatory element of the NEP is the replacement of the depletion allowance, which was available to all entities, with PIP grants, which are available only to firms that have a high level of Canadian ownership. The procurement provisions are just as discriminatory and may hurt foreign-owned original licensees even more if economic factors are taken into account. Furthermore, over and above the twenty-five percent "back-in," an oil or gas play needs another twenty-five percent Canadian interest to be eligible for a production license under the new Canada Oil and

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155. As a result, Petro-Canada, a Federal Government Corporation, was able to bring about the takeover of Petrofina Canada in February 1981. *See* NEP UPDATE, *supra* note 2, at 47.

156. *See* NEP, *supra* note 1, at 50.

157. *See, e.g.*, CANADIAN BAR ASSOCIATION, BRIEF TO THE HON. HERB GRAY, MINISTER OF INDUSTRY, TRADE AND COMMERCE ON THE FOREIGN INVESTMENT REVIEW ACT, (Sept. 24, 1981); *see also* Hormats, *supra* note 14, at 52.

Gas Act.[158]

The phasing-out of depletion allowances is no small matter. The federal government's intentions are clear; in its supplementary information on the budget of October 28, 1980, the Department of Finance stated that "[d]epletion and other incentive deductions have reduced the effective federal tax rate in the oil and gas sector. . . . These incentives have primarily benefited large established corporations which are generally foreign-owned or controlled."[159] The Department added that these tax incentives were of little use to the smaller Canadian-owned corporations that did not have sufficient income to benefit from them.[160] Thus, the NEP provides for "a new incentive in the form of direct incentive payments for exploration and development [under which] [t]he rate of incentive payment will be higher for Canadian-owned firms."[161] As a result, the need for the tax-based incentives is reduced and depletion allowances, which were available to all, are to be phased out. The maximum benefits derived from the PIP grants that replace them are available only to Canadian-owned and controlled firms.[162]

The procurement provisions of the NEP originally were heavy-handed. The NEP announced new legislation restructuring the legal framework governing oil and gas activity on the Canada lands. One of the objectives mentioned was to "[e]nsure that a high level of Canadian goods and services is employed in oil and gas activities carried out on Canada Lands."[163]

Section 10(3) of Bill C-48,[164] the implementing legislation, initially proposed that "[a]n exploration agreement shall require the holder . . . to submit a plan satisfactory to the minister . . . for the use of Canadian goods and services in carrying out [any] work program."[165] A later version of the bill, reprinted June 29, 1981, responded to international criticism that Canada was contravening the General Agreement on Tariffs and Trade (GATT) by altering the procurement provision so that the plan now provided "Canadian manufacturers, consultants, contractors and service

158. Ch. 81, 1980-1982 Can. Stat. § 27.
159. *See* BUDGET PAPERS, *supra* note 6, at 87.
160. *Id.*
161. *Id.*
162. *See supra* notes 120-24 and accompanying text.
163. *See* NEP, *supra* note 1, at 47.
164. Canada Oil and Gas Act, ch. 81, 1980-1982 Can. Stat.
165. *Id.* § 10(3).

companies with a full and fair opportunity to participate on a competitive basis in the supply of goods and services used in that work program."[166]

Another objective of the NEP was to require fifty percent Canadian ownership for any oil or gas production from Canada lands. Again, this objective is contained in Bill C-48.[167] This situation also may be considered highly discriminatory because an initial licensee that is foreign-owned will be forced to enter a consortium to make the play at least fifty percent Canadian-owned.[168]

A final discriminatory aspect of the NEP is the preference given to Canadian-owned firms in the allocation of gas export permits.[169] This discriminatory provision was to be implemented by including the following paragraph in section 83 of the National Energy Board Act: "On an application for a license [to export oil and gas], . . . the Board shall . . . (c) have regard to the extent to which Canadians participate or will participate in the production of the gas to be exported."[170] To date, no implementing legislation has been introduced.

2. *The United States and International Response*

Shortly after the National Energy Program was announced, the United States reacted to the NEP's allegedly discriminatory provisions in various ways.[171] For instance, as early as November 7, 1980, Assistant Secretary of State Dean R. Hinton travelled to Ottawa to present United States concerns about the NEP. On

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166. *Id.* (reprinted as amended and reported June 29, 1981, by the Standing Committee on National Resources and Public Works). This provision was enacted as such in the Canada Oil and Gas Act.

167. *Id.* § 19.

168. *See infra* notes 231-60 and accompanying text.

169. *See* NEP, *supra* note 1, at 50. "The National Energy Board will be asked to take Canadian ownership levels into account, from now on, in considering export applications. The Government of Canada would prefer that in granting such licences, the Board would give preference to Canadian-owned and Canadian-controlled firms." *Id.*

170. *See* Discussion Draft of the Energy Security Act, pt. III (1981) (released by the Minister of Energy, Mines and Resources on June 6, 1981, proposing amendments to the National Energy Board Act, CAN. REV. STAT., ch. N-6, cl. 69) [hereinafter cited as Discussion Draft].

171. Some of the material referred to was made available by Mr. Peter Lande, Energy Attaché to the United States Embassy in Ottawa to whom the author is indebted. *See infra* notes 172-76.

March 11, 1981, United States Trade Representative William E. Brock sent a letter to Canadian Industry Minister Herb Gray that outlined United States concerns about the NEP.[172] The concerns relating to discrimination fall into two categories: trade policy and investment policy.

The letter of March 11, 1981, stated the United States position that both the NEP and Bill C-48 (first reading) require "the use of Canadian goods and services by oil and gas companies which seek approval of operations on the 'Canada Lands' or in major non-conventional oil projects"[173] and that these "Buy Canada provisions . . . conflict with the provisions of GATT Article III."[174] The letter adds that the United States "intends to request formal consultations with the Government of Canada under the provisions of GATT Article XXII:I."[175]

The letter of March 11, 1981, also stated that the Canadianization objectives of the NEP create discriminatory measures that are a cause for concern "in the [l]ight of the [p]rinciple of national treatment . . . established as a goal by the 1976 OECD [Organization for Economic Cooperation and Development] Declaration and a related Decision which reaffirmed the principle in 1979."[176] The United States Trade Representative probably was alluding to the tax and incentive provision of the NEP in which discriminatory PIP grants were to replace the nondiscriminatory depletion allowances.

On March 13, 1981, at a meeting of the OECD Committee on Investment and Multinational Enterprises, the United States and other OECD members expressed their concerns about Canada's alleged violations of the national treatment provisions.[177] These

172. Letter from William E. Brock (United States Trade Representative) to Herb Gray (Canadian Industry Minister) (Mar. 11, 1981) [hereinafter cited as Brock Letter].

173. *Id.*

174. *Id.*

175. *Id.*

176. *Id.*

177. Apparently, six states have registered complaints concerning Canada's National Energy Policy with the OECD. The Globe & Mail (Toronto), Oct. 20, 1981, at B9. As far as the March 1981 meeting is concerned, it appears that "seven OECD countries criticized the discriminatory aspects of the NEP and voiced serious concern about its massive departure from the concept of national treatment." Statement of the Office of the United States Trade Representative (July 9, 1981) (before the Subcommittee on Oversight and Investigation of the House of Representatives Committee on Energy and Commerce) [hereinafter

reactions and others triggered a series of events that eventually led to changes in the NEP. For instance, the procurement of goods and services provisions of Bill C-48[178] were changed. Although this measure brought expressions of satisfaction from the United States Trade Representative,[179] he continued to express United States concerns about the fifty percent Canadian ownership requirement for production leases in Canada lands and the replacement of depletion allowances with petroleum incentive payments based upon levels of Canadian ownership.[180]

A statement of the Office of the United States Trade Representative of July 9, 1981, explicitly set forth the United States position:[181] "In a national treatment sense, current Canadian investment policies, as reflected in . . . the National Energy Program (NEP), are discriminatory in that U.S. and other foreign-owned firms are treated less favorably than Canadian firms." The Deputy United States Trade Representative added that "the NEP [is a] very serious derogation from the OECD's 1976 Declaration on National Treatment, even taking into account the interpretative statement made by the Canadians at the time of their initial adoption of this Declaration."[182] This position was reiterated on September 22, 1981, by United States Under-Secretary of State Rashish who stated: "Canadian Investment policies unjustly discriminate against U.S. and other foreign investors. These policies clearly represent a major departure from the principle of 'National Treatment'. . . ."[183]

B. International Commercial Law Principles and the NEP

1. *The General Agreement on Tariffs and Trade*

The General Agreement on Tariffs and Trade (GATT) was signed originally in 1947 by twenty-three countries, including

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cited as Trade Representative Statement].

178. Canada Oil and Gas Act, ch. 81, 1980-1982 Can. Stat. § 10(3).

179. Letter from William E. Brock (United States Trade Representative) to Peter M. Towe (Canadian Ambassador to the United States) in Washington, D.C. (June 1, 1981).

180. *Id.* at 2.

181. *See* Trade Representative Statement, *supra* note 177.

182. *See id.* (opening statement of David R. McDonald).

183. Speech delivered to the Center for Inter-American Relations, New York (Sept. 22, 1981).

Canada,[184] in order to eliminate, among other things, "discriminatory treatment in international commerce."[185] GATT article III is entitled "National Treatment on Internal Taxation and Regulation." Paragraph 4 states: "The products of the territory of any contracting party imported . . . shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal . . . purchase . . . or use."[186] This paragraph is incompatible with the procurement provisions initially envisioned in the NEP and contained in the first reading of Bill C-48.[187] These provisions were amended, however, as a result of United States and international reaction; now, Canadians must have "a full and fair opportunity to participate on a competitive basis in the supply of goods and services."[188] It therefore could be argued that the procurement provisions of Bill C-48 no longer conflict with GATT. Nevertheless, to the extent that they are subject to ministerial discretion, the provisions may contravene GATT.

Another country may require "consultation" with Canada under article XXII of GATT if it believes conflict exists; this is the first step in any international legal proceeding.[189] The next step would be an action under article XXIII of GATT whereby written representations are made to Canada. If the matter is not resolved, it would be referred to the contracting parties.[190] While the decision of the latter appears to be binding, it is unenforceable.

2. *The OECD Declaration on National Treatment*

The OECD was established by a convention signed in Paris on December 14, 1960. The signatories agreed "to contribute to the expansion of world trade on a multilateral, non-discriminatory basis in accordance with international obligations."[191] Canada is a

184. General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. 3, T.I.A.S. No. 1700, 55 U.N.T.S. 187 [hereinafter cited as GATT].

185. *Id.* 61 Stat. 12, T.I.A.S. No. 1700, 55 U.N.T.S. at 196.

186. *Id.* art. III, 61 Stat. 18, T.I.A.S. No. 1700, 55 U.N.T.S. at 204.

187. Canada Oil and Gas Act, ch. 81, 1981-1982 Can. Stat. § 10(3) (first reading, Dec. 9, 1980).

188. *Id.* (rev. June 29, 1981).

189. *See* GATT, *supra* note 184, art. XXII, 61 Stat., T.I.A.S. No. 1700, 55 U.N.T.S. at 266.

190. *Id.* art. XXIII, 61 Stat., T.I.A.S. No. 1700, 55 U.N.T.S. 266.

191. Convention on the Organisation for Economic Co-operation and Devel-

member of the OECD.

On June 21, 1976, the Committee on Foreign Investment and Multinational Corporations of the OECD adopted a Declaration on International Investment and Multinational Enterprises[192] accompanied by an annex entitled "Guidelines for Multinational Enterprises" that favors "national treatment." The Declaration provides that "Member countries should . . . accord to enterprises . . . owned or controlled . . . by nationals of another Member country . . . treatment under their laws, regulations and administrative practices, consistent with international law and no less favorable than accorded in like situations to domestic enterprises . . . ."[193] Although this Declaration does not bind member countries, a binding decision on national treatment was issued on the same date by an OECD Council[194] which required that "[m]easures taken by a Member country constituting exceptions to 'National Treatment' . . . shall be notified to the Organisation. . . ."[195]

Under this notification procedure, member countries advise the OECD about their respective exceptions to the national treatment rules. The resulting study of national treatment, published in 1978, is very interesting.[196] This study contains a list of derogations from the principle of national treatment by member countries. For instance, a relatively long list of United States derogations from this principle appears in the report.[197] Together with most other member countries, the United States and Canada discriminate against foreign companies in a number of ways. For example, "[f]oreign-controlled enterprises operating in the United States may not: (1) hold in aggregate more than 20 percent of the

opment, Dec. 14, 1960, art. 1(c), 12 U.S.T. 1728, T.I.A.S. No. 4891, 888 U.N.T.S. 179.

192. OECD Committee on Foreign Investment and Multinational Corporations, *Declaration on International Investment and Multinational Enterprises*, OECD Press Release A(76)(20) (June 21, 1976), *reprinted in* 15 I.L.M. 967 (1976).

193. *Id.* art. II.1, *reprinted at* 968; *see generally* Plaine, *The OECD Guidelines for Multinational Enterprises*, 11 INT'L LAW. 339 (1977).

194. OECD, *Decision of the Council on National Treatment, reprinted in* 15 I.L.M. 978 (1976).

195. *Id.* at 979.

196. OECD, NATIONAL TREATMENT FOR FOREIGN-CONTROLLED ENTERPRISES ESTABLISHED IN OECD COUNTRIES (1978).

197. *Id.* at 57-59.

shares of stock of the Communications Satellite Corporation; . . . (4) engage in operations involving the utilisation or production of atomic energy; . . . [or] (8) acquire a controlling interest in a telegraph company. . . ."[198] This list is by no means exhaustive and the federal government of Canada most certainly is happy to add to it.[199]

Of course, Canada and other countries had their own lists of derogations. Perhaps a case could be made that a country which derogates from the national treatment principle should refrain from expressing outrage at another country's derogations from the same principle. The question that must be addressed is whether the NEP respects the OECD national treatment principle, notwithstanding the argument that other countries are acting in identical ways.

A cursory look at the NEP readily provides a negative answer. The size of the petroleum incentive payments grants for which an entity is eligible is keyed to the degree of Canadian ownership and control.[200] Production licenses will be granted only to oil plays with a fifty percent Canadian ownership.[201] Natural gas export permits will be granted by the National Energy Board on the basis of the producer's status as a Canadian-owned and Canadian-controlled firm.[202] Presumably, these derogations from the national treatment principle will eventually be notified by Canada to the OECD under the latter's binding 1976 Decision.[203]

The 1976 Declaration and its related 1976 Decision were reviewed in 1979 by the OECD Committee on National Investment and Multinational Enterprises.[204] An OECD Council decision on

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198. *Id.* at 58-59.

199. *See, e.g.*, Notes for a speech by Canadian Ambassador Towe to the American Gas Association, at 12 (Oct. 13, 1981) (New York). The speaker referred to the United States Mining Act of 1872, 17 Stat. 91 (codified in scattered sections of 30 U.S.C.), and to United States laws relating to maritime transport, banking, and broadcasting industries. *Id.*

200. *See supra* note 122 and accompanying text (PIP payments table).

201. Canada Oil and Gas Act, ch. 81, 1980-1982 Can. Stat. § 19.

202. *See* NEP, *supra* note 1, at 50 ("The National Energy Board will be asked to take Canadian ownership levels into account . . . in considering export applications."). *But see* Discussion Draft, *supra* note 170.

203. *See supra* note 195 and accompanying text.

204. OECD, *Report of the Committee on International Investment and Multinational Enterprises on the Review of the 1976 Declaration and Decisions*, OECD Doc. C(79) 102 (Final) (June 5, 1979), *reprinted in* 18 I.L.M. 986 (1979).

national treatment was reached on June 13, 1979,[205] under which member countries were required to notify OECD of new derogations from the national treatment principle within thirty days.[206] Apparently, Canada did not notify the OECD in the month following publication of the NEP. Whether Canada is at fault here is open to question because the measures taken did not become law until enabling legislation was passed; in some cases this occurred as late as September 1982. Nevertheless, the NEP technically breaches Canada's international commitments with the OECD because it discriminates against foreign firms.

A final problem must be examined. In 1976, the Canadian federal government made the following interpretative statement when it assented to the 1976 Declaration: "Canada will continue to retain its right to take measures, affecting foreign investors, which we believe are necessary, given our particular circumstances."[207] The effectiveness of this interpretative statement has been challenged by the United States in the following manner: "Notwithstanding Canada's interpretative statement in the OECD, the United States Government had understood that Canada through its continuing participation in relevant OECD exercises, maintained a fundamental commitment to national treatment and its extension over time."[208] Canada may claim "special circumstances" and the United States justifiably could use the term "violation" to describe the NEP's derogations from the national treatment principle. Both are correct from their own perspectives. Unfortunately, no international legal procedure for resolving such differences exists. The only recourse would be to consultations under the Declaration and its annex, but these are more political than legal in nature.

3. *The International Energy Agency, Oil Prices, and the NEP*

As oil prices have risen in the past decade, so has international concern about them. Various fora have tackled the problem of

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205. OECD, *Revised Decision of the Council on National Treatment* (adopted June 13, 1979), *reprinted in* 18 I.L.M. 1173 (1979).

206. *Id.* art. 3, *reprinted at* 1174.

207. *See* Notes for a statement made by the Secretary of State for External Affairs 2 (June 21, 1976) (OECD Ministerial Meeting) [hereinafter cited as Notes]. A similar interpretative statement was made by Canada in 1979 when the OECD reviewed its Declaration and Decision on National Treatment.

208. *See* Brock Letter, *supra* note 171.

higher oil and gas prices and have adopted or suggested remedies. For its part, Canada was a party to declarations made at the 1979 Tokyo Economic Summit and the 1980 Venice Economic Summit. It also is a member of the International Energy Agency (IEA), which addressed the problem both in 1976 and 1977 and continues to monitor energy prices.

a. The IEA and Canada's commitments

The IEA was established in November of 1974 within the framework of the OECD to implement an international energy program.[209] The Agency was established to promote cooperation among its members, to reduce excessive dependence on oil, and to develop a stable international energy trade through cooperation between oil-producing and oil-consuming countries.[210]

In 1976, the IEA established a program for long-term cooperation on energy.[211] Chapter V of the agreement provides that participating countries shall "refrain from introducing legislation or administrative regulations in the energy field which would prevent them from affording the nationals of other Participating Countries treatment no less favourable than that afforded to their own nationals."[212] In other words, the parties agreed to refrain from introducing legislation that would have the effect of discriminating against foreign firms. This chapter of the agreement, however, does not appear to be binding on Canada because Canada did not commit itself to this nondiscrimination provision.[213]

In October 1977, the IEA adopted its "Principles for Energy Policy,"[214] article 3 of which allows "domestic energy prices to

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209. OECD, *Council Decision Establishing an International Energy Agency of the Organisation*, OECD Doc. C(74) 203 (Final) (Nov. 18, 1974), *reprinted in* 14 I.L.M. 789 (1975).

210. Agreement on an International Energy Program, Nov. 18, 1974, 27 U.S.T. 1685, T.I.A.S. No. 8278, *reprinted in* 14 I.L.M. 1 (1975).

211. Long-Term Co-Operation Programme, Jan. 30, 1976, 27 U.S.T. 231, T.I.A.S. No. 8229, *reprinted in* 15 I.L.M. 249 (1976).

212. *Id.* at ch. V, 27 U.S.T. at 245, T.I.A.S. No. 8229 at 14, *reprinted in* 15 I.L.M. at 262.

213. The Foreign Investment Review Act of 1974, ch. 46, 1973-1974 Can. Stat. prevented Canada from agreeing to chapter V. *See* Notes, *supra* note 207, at 2.

214. International Energy Agency, *Principles for Energy Policy* (1977), *reprinted in* ENERGY POLICIES AND PROGRAMMES OF IEA COUNTRIES, 1980 REVIEW 329 (1981).

reach a level which encourages energy conservation and development of alternative sources of energy."[215] The IEA mentions the pricing proposals of the NEP in its 1980 Annual Review: "The Canadian price path for oil and gas is much lower than would be in accordance with IEA and Summit decisions, which have repeatedly drawn attention to the importance of keeping oil prices at world levels or moving to them as quickly as possible."[216] It adds that Canada should "take steps to increase domestic oil prices to world market levels."[217]

b. Canada's commitments under the economic summits

At the June 1979 economic summit in Tokyo, the participating countries[218] committed themselves to a uniform energy policy.[219] Under the Tokyo Declaration, the participating countries agreed:

> on the importance of keeping domestic oil prices at world market prices or raising them to this level as soon as possible . . . [and sought] to minimize and finally eliminate administrative action that might put upward pressure on oil prices that result from domestic underpricing of oil and to avoid new subsidies which would have the same effect.[220]

The Venice Economic Summit Declaration was more precise.[221] The parties to this summit agreed that "maximum reliance should be placed on the price mechanism and domestic prices for oil should take into account representative world prices."[222] Canada signed this Declaration.

c. The establishment of a blended price in Canada

As of October 28, 1980, the National Energy Program estab-

215. *Id.*
216. ENERGY POLICIES AND PROGRAMMES OF IEA COUNTRIES, 1980 REVIEW 124 (1981).
217. *Id.* at 127.
218. The following countries participated in the summit: Canada, the United States, France, Japan, Italy, the United Kingdom, and the Federal Republic of Germany. *President Carter Attends Economic Summit Meeting in Tokyo,* 79 DEP'T ST. BULL. 1, 8-9 (Declaration of June 29, 1979, is reproduced).
219. *Id.*
220. *Id.* at 8.
221. *President Carter Attends Economic Summit in Venice,* 80 DEP'T ST. BULL. 1, 8-11 (Declaration of June 23, 1980, is reproduced).
222. *Id.* at 9.

lished a new schedule of prices for domestically produced oil along with a new price system intended to "blend the costs of different sources of oil into one weighted-average price to consumers."[223] The federal government refused to link Canadian and world energy prices, but endeavored to establish a so-called "made in Canada" price that would blend higher cost imported oil with lower cost domestic oil. In no case would the blended price exceed eighty-five percent of the international price or the average price of oil in the United States, whichever was lower.[224]

On September 1, 1981, after many months of bickering, the federal government and the Government of Alberta reached an agreement on a new price schedule.[225] The oil prices agreed upon are substantially higher than those proposed in October 1980. Under the agreement, oil prices will go up periodically with a ceiling of seventy-five percent of the world price for old oil[226] and of 100 percent of the world price for new oil.

d. The legal situation

Although the decision to keep domestic prices below world market prices appears to contravene Canada's commitments at the 1979 and 1980 economic summit meetings as well as section 3 of the IEA's 1977 *Principles for Energy Policy,* little or no legal recourse against Canada is available.

The letter of March 11, 1981, from Trade Representative Brock to the Canadian Minister of Industry, Trade and Commerce,[227] referred to the IEA and the Venice Summit and stated that "decisions have been made which emphasize the importance of keeping oil prices at world levels or moving toward prices at world levels as quickly as possible."[228] The letter added that the United States shared "the view expressed at the IEA's recent meeting that the NEP's price path is much lower than that dictated by both IEA and Summit decisions."[229] The letter added that artificial Canadian prices give producers in Canada a com-

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223. *See* NEP, *supra* note 1, at 25.
224. *Id.* at 30.
225. *See* Canada-Alberta Agreement, *supra* note 11, at 1-7.
226. *Id.* at 1.
227. *See* Brock letter, *supra* note 171, at 4. This concern was reiterated in Mr. Brock's letter to Canadian Ambassador Towe on June 1, 1981.
228. *Id.*
229. *Id.*

petitive advantage over their United States counterparts and that Canada is thus "free to allow its producers to export low priced Canadian resources in the form of low priced manufactured goods."[230] But Canada's commitments stem from "soft" international law. A breach of "soft" international law merely decreases the credibility of the country involved.

So far as international trade is concerned, the main drawback of the Canadian position is the ability of Canadian nationals to compete unjustly with foreign competitors because artificially low oil costs reduce the price of Canadian-produced goods. The pricing agreement of September 1, 1981, diminishes the effects of the differential, however, and it appears doubtful that a strong case now could be made against Canada on this matter. Nevertheless, it can be said that the Canadian federal government has not abided by its international commitments regarding oil pricing.

C. "Confiscatory" Provisions in the NEP

1. *The Twenty-five Percent Back-in*

Some of the most bitter reactions to the National Energy Program related to the proposal to "[r]eserve to the Crown a 25 per cent interest in every right on Canada Lands. This interest . . . [is] in the form of a carried interest, convertible to a working interest . . . . It [applies] to all existing interests, however acquired."[231] This proposal brought an immediate outcry from the oil industry, which called it "confiscation" and "expropriation without compensation."[232] The reserve has come to be known as the twenty-five percent back-in and has been defined appropriately by D.G. Crosby at a hearing of the committee of Parliament

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230. *Id.*

231. *See* NEP, *supra* note 1, at 47. The 25% back-in has been enacted in Canada Oil and Gas Act, ch. 81, 1980-1982 Can. Stat. § 27.

232. *Submissions forwarded by the industry before the House of Commons Standing Committee on National Resources and Public Works in 1981, reprinted in Minutes and Proceedings and Evidence of the Standing Committee on National Resources and Public Works*, No. 39, at 39A:6 (Mar. 19, 1981) (Chevron Canada, Ltd.); *see also id.* No. 40, at 2 (Mar. 26, 1981) (Canadian Petroleum Association); No. 32, at 2 (Mar. 4, 1981) (Mobil Oil Canada, Ltd.). *But see id.* No. 23, at 10 (wherein Professor Rowland J. Harrison states that the 25% back-in is not necessarily confiscatory and that the question is not only legal but also political).

studying Bill C-48, the proposed Canada Oil and Gas Act,[233] as follows: "Back-in is a shorthand way of saying that all of the interest holders have to move over proportionately to make room for the party coming in."[234]

The original Bill C-48 contained the following provisions on this matter:

> Her Majesty . . . is hereby vested with . . . a twenty-five per cent share
> (a) in any interest provided under this Act in respect of lands that were Crown reserve lands immediately prior to the provision of this interest; and
> (b) in the first interest provided in respect of the relevant Canada lands by any of sections 63, 64 or 66 [which relate to former permits and leases].[235]
>
> * * *
>
> No Crown share vests in respect of a former lease under which oil or gas was first produced . . . on or before January 1, 1976. . . .[236]
>
> * * *
>
> The interests and rights provided by this Act replace all oil and gas interests and rights . . . acquired or vested in relation to Canada lands prior to the coming into force of this Act.[237]

These proposals were fair game to the extent they were applied prospectively. The retroactive provisions were not, and both Canadian industry and the United States Government complained vehemently.

Suprisingly, no provision for compensation was contained in the original version of Bill C-48. Although legally defensible,[238] it was politically unwise and the federal government later was

233. Ch. 81, 1980-1982 Can. Stat.

234. *See Debates of the House of Commons, Standing Committee on National Resources and Public Works*, No. 17, at 19 (Jan. 21, 1981).

235. Canada Oil and Gas Act, ch. 81, 1980-1982 Can. Stat. § 27(2) (first reading, Dec. 9, 1980).

236. *Id.* § 28.

237. *Id.* § 61(1).

238. "The prohibition 'Thou shall not steal' has no legal force upon a sovereign body. And there would be no necessity for compensation to be given." Florence Mining Co. v. Cobalt Lake Mining Co., 18 Ont. L. R. 275, 279 (Ct. App. 1908) (Riddell, J.). Regarding compensation, see Manitoba Fisheries, Ltd. v. The Queen, 1979 S.C.R. 101 (Can.) (canvasses Canadian domestic law where compensation for the taking of goodwill was allowed following the closing of a fishery).

obliged to retreat.[239]

2. *United States and Industry Reaction*

The United States Trade Representative's letter of March 11, 1981,[240] mentions that the provisions which "retroactively reserve a 25 per cent interest to the Government of Canada . . . and prohibit the licensing . . . for development without 50 per cent Canadian ownership, raise potentially serious issues concerning Canada's obligations under mutually recognized international law and practice with respect to direct and indirect expropriation and compensation."[241] This reaction brought a change in Bill C-48[242] that authorized so-called *ex-gratia* payments of twenty-five percent of qualified expenditures made before 1981.[243] This measure was considered insufficient by the United States Trade Representative because "the announced approach may not take full account of the true commercial value of the assets involved. . . ."[244] In July 1981, the Trade Representative added that this particular provision of the NEP "retains, in our view, its expropriatory nature."[245]

3. *The Canadian Federal Government Response*

The federal government responded to the United States reaction to the twenty-five percent back-in by saying that there was no expropriation at all. According to the Canadian Ambassador to the United States,[246] the provision creates only a "Crown Inter-

239. *See* Canada Oil and Gas Act, ch. 81, 1980-1982 Can. Stat.
240. *See* Brock Letter, *supra* note 171.
241. *Id.*
242. Canada Oil and Gas Act, ch. 81, 1980-1982 Can. Stat. § 29(2).
243. *Id.; see also Statement before the House of Commons Standing Committee on National Resources and Public Works, reprinted in Minutes of Proceedings and Evidence of the Standing Committee on National Resources and Public Works*, No. 49, at 20 (May 14, 1981) (Federal Energy Minister Marc Lalonde).
244. Letter from William E. Brock (United States Trade Representative) to Peter M. Towe (Canadian Ambassador to the United States) (June 1, 1981).
245. *Impact of Canadian Investment and Energy Policies on United States Commerce: Hearings Before the Subcomm. on Oversights and Investigations and the Subcomm. on Telecommunications, Consumer Protection, and Finance of Comm. on Energy and Commerce*, 97th Cong., 1st Sess. 299 (1981) (statement of the office of the United States Trade Representative).
246. Speech by Peter M. Towe (Canadian Ambassador to the United States)

est" and takes account of several factors: federal government ownership of the lands; the inclusion of incentive payments in the package of which the provision is but one part; the new world energy environment; reform of the previously entrenched land reservation concept; the twenty-five percent Crown incentive payments of exploration costs to all firms exploring in Canada lands; and the absence of discrimination between foreign and Canadian-controlled firms. Moreover, the twenty-five percent carried interest is incurred before production; therefore the Crown in effect pays its share of the subsequent development expenses.[247]

This explains why the amendments to the twenty-five percent retroactive back-in provisions of Bill C-48, which was changed under heavy United States and industry pressure, do not provide for compensation, but rather authorize twenty-five percent *ex-gratia* payments of exploration expenditures incurred before 1981 if significant discoveries are made before 1983.[248] No payments are to be made for dry holes, which supports the argument that no compensation is required for the back-in. Payments will be made from the Crown's share of future production.[249]

4. *International Law Aspects*

Whether or not the NEP and its implementing legislation contain expropriating measures remains a subject of considerable disagreement. A decision that these measures—such as the twenty-five percent back-in—are confiscatory would raise the question whether they are consistent with international law when applied to foreign-owned or controlled firms. In the case of domestic firms, domestic law would prevail. For foreign firms, there is considerable confusion about the state of the law.[250]

According to a 1962 United Nations resolution, "[n]ationalization, expropriation or requisitioning shall be based on grounds of public utility, security or the national interest. . . . In such cases the owner shall be paid appropriate compensa-

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to American Gas Ass'n in New York City, at 7 (Oct. 13, 1981).

247. *Id.* at 7-9.

248. Canada Oil and Gas Act, ch. 81, 1980-1982 Can. Stat. § 29.

249. *Id.* § 29(3).

250. For a comprehensive study of the situation, see Mendes, *The Canadian National Energy Program: An Example of Assertion of Economic Sovereignty or Creeping Expropriation in International Law,* 14 VAND. J. TRANSNAT'L L. 475 (1981).

tion. . . ."[251] The United Nations passed numerous other resolutions on the same subject.[252] Among these, a 1973 resolution mentions that "application of the principle of nationalization . . . implies that each State is entitled to determine the amount of possible compensation."[253] A 1974 resolution also required appropriate compensation for expropriation after "taking into account . . . relevant laws and regulations and all circumstances that the state considers relevant."[254] But these United Nations resolutions are not binding because they are not seen "as a source of international law or as legally binding precedents on the member nations."[255] Moreover, the United States generally has not supported these resolutions. In fact, the twenty-five percent back-in may comply with the language of Resolution 3281[256] because previous tax incentives and exploration grants to foreign firms would be among the "circumstances" to consider.

The United States position is quite different from the stance taken by the United Nations because the United States favors prompt payment of compensation.[257] United States law authorizes retaliatory measures when expropriation occurs against its individual or corporate citizens.[258]

Despite its appearance, the twenty-five percent back-in is not necessarily confiscatory, especially when given the federal government's perception of the situation.[259] Nevertheless, as an oil industry representative once stated: "[I]t does constitute a frustration of those legitimate expectations on which prior investment decisions have been made."[260]

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251. G.A. Res. 1803, 17 U.N. GAOR, Plenary (Agenda Item 62), U.N. Doc. A/5344/Add. 1, A/L. 412/Rev. 2 (1962).

252. *See* Mendes, *supra* note 250, at 487-91.

253. G.A. Res. 3171, 28 U.N. GAOR Supp. (No. 30) at 52, U.N. Doc. A/9030 (1973).

254. The Charter of Economic Rights and Duties of States, G.A. Res. 3281, 29 U.N. GAOR Supp. (No. 31) at 52, U.N. Doc. A/9631 (1974).

255. *See* Mendes, *supra* note 250, at 492.

256. *See supra* note 254.

257. *Id.* at 494-95.

258. *See, e.g.,* Trade Act of 1974, 19 U.S.C. §§ 2101-2487 (1976 & Supp. V 1981).

259. *See Minutes of Proceedings and Evidence of the Standing Committee on National Resources and Public Works,* No. 23, at 36-38 (1981) (statement by Mr. Rowland J. Harrison before the House of Commons Committee that studied Bill C-48).

260. D. MacFarlane, Notes on Energy Resources and International Rela-

Whether the measure is expropriatory in nature or not, there appears to be no recourse under international law for nondiscriminatory expropriation. Rather, it seems that any recourse must be political, and could be accomplished through national governments.

V. Conclusion

It would appear from the foregoing discussion that international legal responses to the various taxation and Canadianization measures of the Canadian National Energy Program are rather limited. Neither the OECD, the IEA, nor the United Nations is an effective forum for airing complaints about the lack of national treatment, the low energy prices, or the inadequate compensation for confiscatory government actions. Pronouncements by these organizations remain "soft" and nonbinding international law. On the other hand, legal recourse could conceivably exist under the GATT rules. Even with the recent changes, the NEP still may contravene GATT. The GATT rules appear to provide the only practical forum for international litigation in this area.[261] Therefore, any international proceeding by the United States would have to be based on a GATT violation. The NEP's most obvious contravention of GATT (the procurement provisions of Bill C-48) has been modified by the federal Parliament and now is not as vulnerable to attack. Finally, the absence of national treatment in internal taxation contravenes the OECD Code rather than GATT and recourse under the former would be based on soft law.

A complaint against the NEP conceivably could be made on the ground that discriminatory subsidies to be paid under the PIP program violate GATT. Whether this type of international legal recourse exists is uncertain. Furthermore, whether the United States or any nation may present a case specifically on behalf of its nationals is also open to question.[262]

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tions, at 30 (Oct. 30, 1981) (paper delivered at the Annual Meeting of the Canadian Council on International Law in Ottawa).

261. The United States Government has already initiated consultations on FIRA under the provisions of GATT article XXII as of February 17, 1982. *See* Hormats, *supra* note 14, at 53. The Government is also envisioning the possibility of initiating a case against the NEP "if it is implemented in ways which are contrary to Canada's GATT obligations." *Id.* at 54.

262. *See* Saunders & Gault, *The National Energy Program and the Pursuit of Claims under International Law*, Resources, May 1982, at 1 (newsletter of

A look at the essential facts of the NEP reveals that the whole scheme should be labelled "Ottawa-ization" instead of Canadianization for two reasons. First, the NEP favors exploration on Canada lands over exploration on provincial lands. Second, the increased federal revenue share from oil and gas production comes at the expense of provincial and oil industry shares. The agreement of September 1, 1981, between the Government of Alberta and the federal government is but another episode in the struggle between Ottawa and the provinces for revenues and for a restatement of Canadian federalism. With the support of Québec, the producing provinces have stressed the sovereignty of federated states over natural resources, and have argued that the Canadian provinces are autonomous in their own fields of jurisdiction. The federal government takes a totally different view of the relationship. It believes that the central government is somewhat superior to the provincial governments which, under this viewpoint, are less important local governments. This perceived "bigfoot" approach in energy matters has offended the federated states by impeding their efforts to profit from their natural resources. Perhaps realizing the inadequacy of its approach, the federal government finally has arrived at agreements with the producing provinces. This has left the oil corporations—especially the international corporations—with little or no advantage and reduced cash flows.

Political will is not necessarily economically attractive, as far as private investment decisions are concerned. Nevertheless, when this political will is translated into legislation, it changes the law of the land which everyone must follow. Foreign nationals may fall victim to injustice, but this is a risk attendant to investing in another country. The NEP may be objectionable; it even may be illegitimate. In the absence of a world legal order, however, it remains legal. In transnational law, neither reason nor cash-flow problems count. Enforceable law counts. Notwithstanding its motives, the bulk of the NEP remains valid Canadian law.

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the Canadian Institute of Resources Law, Calgary). The authors quite appropriately refer to Barcelona Traction, Light and Power Co. (Belg. v. Spain), 1970 I.C.J. 3 (Judgment), when they mention the case of Canadian subsidiaries of United States multinational oil corporations. Because these subsidiaries are incorporated in Canada and presumably have accepted Canadian jurisdiction, an argument could be made that it would be highly inappropriate for them to have a foreign state pursue a case on their behalf. Indeed, a preliminary objection by Canada could then be made.

It is understandable that perceived discriminatory measures are disfavored because non-Canadian owned or controlled companies are inconvenienced and frustrated. Nevertheless, these measures are an expression of Canadian political will. Whether, as others would see it, this philosophy eventually will be replaced by wisdom and reason remains to be seen. The answer will unfold as currents of political activity impact on Canada's energy policy.