

**Continental Drift:  
Canada-U.S. Oil and Gas Relations 1958 to 1988**

By

Tammy Nemeth

PhD Candidate  
Department of History  
University of British Columbia  
Vancouver, B.C., Canada  
[tnemeth@allstream.net](mailto:tnemeth@allstream.net)

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Thirty years after the first energy crisis, the world is again faced with a substantial rise in oil prices.<sup>1</sup> With a sense of déjà vu, the United States (U.S.) looks to decrease its dependence upon overseas oil, and consumers in Canada and the U.S. complain about high fuel prices. In the 1950s and 1960s, the situation was reversed and low prices of overseas oil threatened the viability of the Canadian and American oil and gas industries. One effect was that Canada and the U.S. agreed to an informal continental arrangement. But by the late 1960s, this informal relationship began to break down, and, despite numerous discussions, a more formal sectoral agreement failed to emerge. Then in the 1970s, and particularly in the early 1980s, increased oil prices helped politicise energy issues. The U.S. sought to increase its access to secure oil supplies and reduce the impact of OPEC, while Canada embarked upon an economic nationalist course, which meant ending oil exports to the U.S. and partially nationalising the Canadian oil and gas industry. These Canadian policies created conflict in Canada-U.S. relations until a new Canadian government, headed by Brian Mulroney, was elected in 1984. Both Ronald Reagan and Mulroney wanted to constrain future governments on both sides of the border from implementing discriminatory trade policies on certain issues, especially oil and gas, thus they negotiated a comprehensive Free Trade Agreement (FTA) with a chapter governing the trade of energy embedded in the agreement. This is the main difference about the current situation of rising oil prices and that of thirty years ago: The energy chapter of the FTA is a formalised continental energy agreement, which has depoliticised oil and gas issues for Canada-U.S. relations.

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The energy provisions of the 1988 Canada-United States FTA marked a dramatic departure from previous Canadian and American energy policies. Although there were overtures from each country to develop a more formal accord to govern the trade of oil at different times since 1958, it was not until 1988 that a truly continental agreement was reached between Canada and the U.S.<sup>2</sup> Newly uncovered documentary evidence reveals that in the 1958 to 1988 period, personalities played a far larger role in shaping the pendulous course of Canada-U.S. oil relations than has previously been acknowledged.

In order to understand why a continental energy agreement was a dramatic change in policy, and how it came about, the Canada-U.S. oil relationship will be explored in three sections. The first section covers the period of the U.S. Mandatory Oil Import Program (MOIP), when an informal continental relationship prevailed and Canada was exempted from this policy. The second section covers the period of the oil crises, when the U.S. desired a more formal continental agreement but Canada pursued a course of economic nationalism instead. The third section covers the move towards a comprehensive Free Trade Agreement, and the convergence in American and Canadian thinking about continental trade. These events and relationships are situated and analysed in the larger context of continentalism, interdependence, transgovernmental relations, and the increased bureaucratisation of governments in both countries over this period of time.<sup>3</sup>

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<sup>2</sup>The meaning of continental used here is based on economist Leonard Waverman's definition: "Joint planning of energy production and shipment without regard to borders." Leonard Waverman, "Reluctant Bride: Canadian-American Energy Relations," in The Energy Question: An International Failure of Policy Vol. 2 North America, eds. Edward W. Erickson and Leonard Waverman (Toronto: University of Toronto Press, 1974), 217.

<sup>3</sup> This paper is based on my larger dissertation project of the same title. In my dissertation I analyse the 1958 to 1988 period by examining six variables that influenced the decision-making process in each country and affected Canada-U.S. oil and gas relations: economics, ideas (continentalism, economic nationalism/protectionism, market forces, anti-Americanism), interest groups (including industry, provinces/states, and other stakeholders), national security, international forces, and personalities. Due to time and space constraints, this paper focuses mainly upon the personalities as in each phase of the relationship that variable consistently exerted the most influence.

## **I. Informal Continentalism or Continental Emergence: 1958-1973**

The main American objective in its oil policy in the cold war period was to have quick and secure access to oil in an emergency. Post-war American production of oil was in a state of mature development, and the dilemma was whether to maximise American production, which would drain America first but be safe and dependable, or to offset it with cheap foreign imports, which would prolong American reserves but make it more reliant on unstable sources from places like the Middle East. Policy-makers also felt a responsibility towards allies and pro-Western developing countries that needed markets for their commodities. Canada was in a unique situation as it fit into both categories.

In the 1950s, American independent producers lobbied vigorously and successfully for some kind of import restrictions. The Republican Administration of Dwight D. Eisenhower sought to balance the competing interests of national security, domestic producers, allies, and developing countries in its oil import policy.<sup>4</sup> Eisenhower delayed action for as long as possible, but in 1955 an informal voluntary import program was established which was then followed in July of 1957 with a more formal arrangement known as the Voluntary Oil Import Program (VOIP).<sup>5</sup> Canada and Venezuela were exempt from the former, but not from the latter. Canadian officials made strong arguments for an exemption to the VOIP. At that time, however, the U.S. said that an exemption would cause irreparable harm to its relations with Venezuela; nevertheless, Canada persisted in pressing the U.S. Administration for some type of preferential treatment. Although Canada was not granted an exemption when the Mandatory Oil Import Program (MOIP) was first enacted on 10 March 1959, the proclamation was amended on 30

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<sup>4</sup>For a detailed examination of energy policy under the Eisenhower Administration see, William J. Barber, "Eisenhower Energy Policy: Reluctant Intervention," in Energy Policy in Perspective, ed. Craufurd Goodwin (Washington, D.C.: Brookings Institution, 1981), 205-286.

April 1959 to include an exemption for imports entering the U.S. via overland transportation routes. This was an effective, though unnamed, exemption for Canada that happened to have an added benefit for Mexico. The question becomes, why did the U.S. decide to enact the MOIP exemption for Canada? The documentary evidence reveals that the decision to grant Canada an exemption without also permitting preference for Venezuela was based on Eisenhower's relationship with Canadian Progressive Conservative Prime Minister John D. Diefenbaker and the support of key officials.

Several key policy-makers and analysts in the U.S. considered Canada to be a domestic strategic reserve, while others recognised Canada as its best ally in the Cold War that needed to develop its industry with open access to the U.S. market. The traditional American approach to trade with Canada was to be open to closer continental economic integration. However, senior State Department and Administration officials, alert to Canadian sensitivities, operated on the principle that initiation of any type of continental trading arrangement – comprehensive or otherwise – had to originate with the Canadians.<sup>6</sup> In the post-war period, the traditional Canadian approach to trade with the U.S. was a form of informal continentalism. Pragmatism rather than an ideological commitment to continentalism was the spirit behind informal

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<sup>5</sup>The Oil Import Administration (OIA) was created to administer the program and was headed by Captain Matthew V. Carson, Jr.

<sup>6</sup>Eisenhower's Chairman of the Council on Foreign Economic Policy, Clarence B. Randall, was the most vocal proponent of a comprehensive free trade agreement with Canada. He attempted, on several occasions, to have the Administration initiate exploratory talks on the issue, but was repeatedly rebuffed by John Foster Dulles and the State Department. See for example, Dwight D. Eisenhower Library (DDEL), C.B. Randall Journals, 1953-61, Box 4, File *CFEP, 1957, Vol. IV [Apr 3-May 6, 1957]*, April 14, 1957, 2; DDEL, U.S. Council on Foreign Economic Policy (CFEP) Records, 1954-61, Chronological File, Box 4, *Chron File – April 1957 (2)*, Letter to Christian Herter from Clarence B. Randall, 16 April 1957; DDEL, U.S. CFEP Records, 1954-61, Randall Series, Subject Sub-Series, Box 2, File *Canada (5)*, Special Paper No. 72, United States-Canadian Economic Integration, 15 July 1957; DDEL, Dwight D. Eisenhower Papers (DDEP), Papers as President of the United States (PPUS) 1953-61, Ann Whitman File (AWF), Dulles-Herter Series, Box 10, File *Dulles, John Foster May 1958*, Letter to President Eisenhower from John Foster Dulles, 14 May 1958. Dulles concludes, "that any suggestion of free trade between Canada and the United States would produce a violent negative reaction on the part of our Canadian friends."

continentalism.<sup>7</sup> The general strategy involved two stages: First, an exemption was secured from American policies that would normally apply to foreign countries; then when the exemption began to fail, a more formal sectoral or commodity agreement was negotiated, like the Autopact. Canada-U.S. oil policy also followed this pattern -- except that it failed to complete the second stage -- and it began with Canada's push for an exemption to the American MOIP.

Eisenhower was receptive to Canadian overtures and pressure for an exemption because of his personal regard for Prime Minister Diefenbaker. There is ample evidence in the archival/documentary record to substantiate the idea that Eisenhower and Diefenbaker had a very friendly relationship that helped to create an atmosphere of co-operation for Canada and the U.S. This is significant because Eisenhower was President during four years of Diefenbaker's nearly six-year Prime Ministership. They often talked to each other on the phone and sometimes Eisenhower wrote or called Diefenbaker to ask his opinion on international developments.<sup>8</sup> Basil Robinson, Diefenbaker's foreign policy aide, in his book on the Diefenbaker years, reflected on the warm personal relationship between Eisenhower and Diefenbaker. Robinson comments that the usual nature of discussion between the leaders was "a friendly, free-flowing exchange of impressions on the world scene and on the current agenda of bilateral issues."<sup>9</sup> In a further telling observation of the unique rapport shared by Eisenhower and Diefenbaker, Robinson revealed the confidential nature of their last private conversation and opined, "to have the kind of relationship which permitted the blowing off of presidential steam – that was rare."<sup>10</sup> Even

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<sup>7</sup> An excellent scholarly account is Michael Hart, A Trading Nation: Canadian Trade Policy from Colonialism to Globalization, (Vancouver: UBC Press, 2002), 171. For the view of a former senior Canadian official and politician who put such pragmatism into action, see the memoir, Mitchell Sharp, Which Reminds Me... (Toronto: University of Toronto Press, 1994), 183; 185; 180-181.

<sup>8</sup>See for example, DDEL, DDEP, PPUS, 1953-1961, AWF, International Series, Box 6, File *Canada (6)*; and National Archives of Canada (NAC), MG 31 E83, H.B. Robinson Fonds, Vol. 3, File *3-9 June-August 1960*.

<sup>9</sup>H. Basil Robinson, Diefenbaker's World: A Populist in Foreign Affairs (Toronto: University of Toronto Press, 1989), 138.

<sup>10</sup>*Ibid.*, 167.

Eisenhower's secretary commented on the cordial phone conversations.<sup>11</sup> However, part of the difficulty with respect to the good relations between the two leaders, is that many of their conversations were just between the two of them – no advisors or secretaries attended to take notes. Indeed, during Eisenhower's visit to Canada in July 1958 Diefenbaker and Eisenhower went fishing together at Harrington Lake and then for a drive in the country.<sup>12</sup> In a letter to Diefenbaker at the end of 1959, Eisenhower expressed his view of the importance of the personal relationship he had formed with Diefenbaker, "You and I have found from experience that there is no substitute for personal contact in furthering understanding and good will."<sup>13</sup>

How exactly did the "understanding and good will" between Eisenhower and Diefenbaker develop and influence oil relations? Between late 1957 and 1959, the oil import problem came to be considered by Canada as the most crucial bilateral problem between Canada and the U.S. This was made clear by Diefenbaker and others at the NATO meeting in Paris in December 1957, and was stated by Canadian Ministers during the 1958 Presidential visit to Canada, as well as at the Joint Canada-U.S. Committee on Trade and Economic Affairs (JCTEA) meeting held in January 1959.<sup>14</sup> A few months later when the MOIP was announced, U.S. Embassy officials in Ottawa reported to the Secretary of State their conversation with Diefenbaker in which he "said he knew how hard [the] President had tried to find [a] proper

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<sup>11</sup>See for example, DDEL, DDEP, PPUS 1953-61, AWF, International Series, Box 6, File Canada (6), Telephone Calls. For examples of Ann Whitman's comments in this file see the dates 14 July and 4 August 1958. From the Canadian perspective see also NAC, MG 31 E83, H.B. Robinson Fonds, Vol. 3, File 3-9 June-August 1960.

<sup>12</sup>H. Basil Robinson, Diefenbaker's World, 51. Robinson commented that Diefenbaker "insisted on plenty of time alone with Eisenhower."

<sup>13</sup>DDEL, DDEP, PPUS 1953-61, AWF, International Series, Box 6, File Canada (3), Letter to Prime Minister John G. Diefenbaker from President Dwight D. Eisenhower, 1 December 1959. Eisenhower also suggested that if Diefenbaker wanted to provide any suggestions for Eisenhower's upcoming European tour he would "welcome a phone call from you."

<sup>14</sup>DDEL, DDEP, PPUS 1953-61, White House Central Files (WHCF), Confidential File, Subject Series, Box 77, File *State, Department of (Jan-Aug 1959)(3)*, "Joint Canada-United States Committee on Trade and Economic Affairs, U.S. Record of Talks, Meeting January 5-6, 1959, Ottawa", 18. Finance Minister Donald Fleming stated, "nothing on the agenda is more important or urgent than oil, from Canada's standpoint."

equilibrium in oil and how great were [the] pressures upon [the] President in this matter. [But Diefenbaker] repeatedly interjected how deeply he [was] concerned over [the] oil action in terms of overall relations.”<sup>15</sup> Therefore, over a period of a year and a half, it was reinforced to Eisenhower, through the communications between him and Diefenbaker, and various levels of ministers and officials on both sides of the border, that the changes to the oil import policy were important to Canada.

What complicated matters for Eisenhower during the consideration for a MOIP, is that he, and several of his top advisors, wanted to keep Canadian oil exempt from any controls, but the U.S. could not appear to show any particular preference for one country over another.<sup>16</sup> The U.S. had a number of agreements with Middle and Near Eastern countries, as well as Venezuela, which gave them “Most Favoured Nation” status with respect to trade in oil. To single out specific countries could cause irreparable harm in areas of the world that were prone to growing animosity towards the U.S.<sup>17</sup> During numerous and extensive discussions, Canadian officials promoted the idea that if it were not granted an exemption from the MOIP, it would definitely build an oil pipeline to Montréal, which would shut Venezuelan oil out of the Canadian market and the U.S. would be blamed.<sup>18</sup> U.S. officials wrestled with the intricacies of the situation; the State Department was divided, with some favouring Canada and others Venezuela.

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<sup>15</sup>DDEL, White House Office, Office of the Secretary of State, International Series, Box 2, File *Canada (1) [May 1958-Aug 1959]*, Telegram 671 to Secretary of State from Ottawa, 10 March 1959.

<sup>16</sup>DDEL, DDEP, PPUS, AWF, Cabinet Series, Box 13, File *Cabinet Meeting March 6, 1959*, “Minutes of Cabinet Meeting, March 6, 1959”, 5.

<sup>17</sup>United States National Archives (USNA), RG59, General Records of the Department of State, Alpha Numeric Files Relating to Canadian Affairs, 1957 to 1963, Box 3, File *Oil Quotas 1957-61*, “Memorandum to Mr. Phleger from Stanley Meteger, Subject: International Commitments of the United States relevant to exempting Canadian Petroleum Products from a Petroleum Import Quota, 17 June 1958.” This memo reveals that the State Department was requested to not only identify U.S. international commitments, but, more importantly, “what steps could be taken to secure relief from such commitments”, in order to pave the way for a Canadian exemption. (1)

<sup>18</sup>DDEL, C.B. Randall Journals, 1953-61, Box 5, File *CFEP, 1958. Vol. X [Sept. 17-Dec. 23, 1958]* “Tuesday, December 16<sup>th</sup>, Executive Office.” Eisenhower had his Council on Foreign Economic Policy (CFEP), headed by Clarence Randall, determine whether a Western Hemisphere preference or a Canadian exemption would be preferable in the MOIP. Randall made the following observation in his diary, “If Canada does not have an outlet

Although Eisenhower preferred to favour Canada alone, in order to mollify forceful State Department objections, he signed a National Security directive at the end of 1958 that stipulated preference should be given to Canadian and Western Hemisphere sources in any oil import program. Discussions between the U.S., Canada, and Venezuela were held to try to arrive at a tripartite or hemispheric agreement on oil, but the talks collapsed.<sup>19</sup> In early 1959, however, it became clear from meetings with Canadian ministers and a diplomatic blitz from the Canadian embassy, that this was an extremely important issue to Canada and Prime Minister Diefenbaker.<sup>20</sup>

The importance that Canada and Diefenbaker attached to the oil import question was, as mentioned above, emphasised at the JCTEA meeting in January 1959, and reinforced in subsequent meetings during March and April with Canada's new ambassador to the U.S. and other Canadian officials. The Canadian Ministers at the JCTEA meeting impressed upon their American counterparts that nothing else on the agenda was as important as the oil import question.<sup>21</sup>

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for her products to the northwestern part of the United States, which is right by every principle of geography, she will build a pipeline to Montréal to dispose of that product. That will cut off present imports to Canada from Venezuela. We will be blamed. On the other hand, giving preference to the Western Hemisphere will exacerbate our explosive relations in the Middle East and will give offense to the Government of Indonesia, which quite surprisingly of late has been standing up to Russia." (3-4)

<sup>19</sup>Tripartite discussions had also been held in 1958, but in December 1958 a new government was elected in Venezuela and the talks were reopened. Those discussions did not go far as the Venezuelan position was unacceptable to the U.S., and required further negotiations. However, time was running out, and a decision on the situation had to be made quickly.

<sup>20</sup>For example, after the JCTEA meeting Merchant reported, "At last week's meeting in Ottawa . . . the Canadian Ministers reiterated their view that there was no more urgent and important topic on the agenda than that of US import restrictions on Canadian oil. . . . This fresh insistence of Canadian Government leaders upon the importance to Canada of US action to exempt Canadian oil from US import restrictions has persuaded us that no other single action which the United States could take in relation to Canada would have a more bouyant [sic] effect upon our relations with that country." USNA, RG59, General Records of the Department of State, Alpha-Numeric Files Relating to Canadian Affairs, 1957-63, Box 3, File *Oil Quotas 1957-61*, Memorandum to Mr. Mann (E) from Mr. Merchant (EUR), Subject: Restrictions on Oil Imports, 16 January 1959, 1-2. See also an account of Heeney's meeting with Eisenhower, DDEL, WHO, OSS, International Series, Box 2, File Canada (1) [May 1958-Aug 1959], Telegram 671 from Ottawa to Secretary of State, Reference Embassy Telegram 669, 10 March 1959.

<sup>21</sup>NAC, BG32 B39, Gordon Churchill Fonds, Vol. 128, File 13, Record of Discussion, JCTEA 5-6 January 1959, Item 3.B United States Restrictions on the Import of Oil, 21. For the American account of the discussion see,

Reporting on the meeting, Secretary of the Treasury Anderson told the U.S. Cabinet that “certain actions may seem of little moment to us but are taken very seriously in Canada, and we must be on the lookout for these.”<sup>22</sup>

Another example of Canada’s diplomatic blitz, and the significance of Eisenhower’s relationship with Diefenbaker, can be found in the notes of a meeting between the Canadian Ambassador and the President. At the end of February 1959, Arnold Heeney, the new Canadian Ambassador, met with Eisenhower to present his credentials, and reiterated the importance with which the Canadians viewed the oil import situation. Heeney reported back to Ottawa that, in the conversation,

the President mentioned oil . . . making it evident that he was aware of the trading difficulties which from time to time arose between our countries. He said that the USA administration, in such matters, tried to ease CDN difficulties but, as I would know, there were serious problems involved with congress and local USA interests. . . .

Heeney also commented on how “Mr. Eisenhower referred to the pleasant and satisfactory conversations he had had with the Prime Minister.” The Canadians recognised that Eisenhower was taking a personal and active interest in the matter, and Heeney reflected this in his report back to the Prime Minister, who was appreciative of Eisenhower’s efforts.<sup>23</sup>

Within days of the new Canadian Ambassador’s meeting with Eisenhower on 2 March 1959, Eisenhower’s reluctance in supporting a sole Canadian exemption turned to a more explicit favouring of the Canadian position. At the 6 March 1959 Cabinet meeting, Eisenhower “stated his interest in the unity of the American continent, and wished it were possible to act in unity

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DDEL, DDE Records as President, WHCF, Confidential File, 1953-61, Subject Series, Box 77, File State, Department of (Jan-Aug 1959) (3), US Record of Ottawa Talks 21 January 1959, 16-19.

<sup>22</sup>DDEL, DDEP, PPUS 1953-61, Cabinet Series, Box 12, File *Cabinet Meeting January 16, 1959*, Minutes of Cabinet Meeting, 16 January 1959, 2.

with Canada on this particular item.”<sup>24</sup> Three days later, the President reinforced this position by asking Deputy Secretary of Defence Quarles “if there wasn’t something we could do to make this oil move look better to our neighbors to the north.”<sup>25</sup> Even though the President desired to favour Canada, the State Department was split on the issue and a battle ensued between those that supported the President’s directive, like Livingston Merchant, and those, like Thomas Mann, who believed America’s interests would be better served by treating Canada and Venezuela equally.

Of great significance for Canada, the dynamic in the State Department altered with the return of Livingston Merchant as Assistant Under Secretary of State for Political Affairs in October 1958. Merchant, who had just served as U.S. Ambassador to Canada, and who understood how much Canada wanted the exemption, brilliantly outmanoeuvred his rival Thomas Mann.<sup>26</sup> Mann, the Assistant Secretary of State for Economic Affairs, had worked as the petroleum attaché in Caracas after the war, and was the driving force in the State Department for Venezuela’s position. He argued that, based on the President’s own NSC directive, no exemption could be given to Canada unless Venezuela received the same treatment.<sup>27</sup> Merchant countered that though a hemispheric agreement would be preferable, the recent Venezuelan

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<sup>23</sup>DDEL, WHO, OSS, International Series, Box 2, File *Canada (1) [May 1958-Aug 1959]*, Telegram 671 from Ottawa to Secretary of State, Reference Embassy Telegram 669, 10 March 1959.

<sup>24</sup>DDEL, DDEP, PPUS 1953-1961, AWF, Cabinet Series, Box 13, File *Cabinet Meeting March 6, 1959*, Minutes of Cabinet Meeting, 6 March 1959, 5.

<sup>25</sup>DDEL, D.A. Quarles Papers, Box 3, File *Daily Diaries 1/2/59-5/17/59c3*, Diary Donald A. Quarles, Monday, 9 March 1959, 2.

<sup>26</sup>This manoeuvring is covered in detail in my dissertation, “Continental Drift: Canada-U.S. Oil and Gas Relations, 1958 to 1988.”

<sup>27</sup>For Mann’s position and his supporters in the State Department see for example, USNA, RG59, Alpha-Numeric Files Relating to Canadian Affairs 1957 to 1963, Box 3, File *Oil Quotas 1957-61*, Memorandum of Conversation, Subject: Attitude to be taken regarding Western Hemisphere preference and a Canadian exemption under the oil import program, 26 February 1959; *Ibid.*, Memorandum to the Acting Secretary through Mr. Murphy from W.T.M. Beale, Subject: Canadian Reaction to U.S. Oil Import Program Proposed Tri-partite Oil Talks, 17 March 1959; USNA, RG59, General Records of the Department of State, Subject Files Relating to Venezuela 1958-

election made its possibility remote before an announcement on the MOIP had to be made. In the meantime, Canada could be given an exemption while talks for a larger agreement with Venezuela and Canada continued.<sup>28</sup>

Merchant employed a multifaceted strategy of persuasion and repetition to achieve this aim. He utilised his close personal and working relationships with ailing Secretary of State Dulles and other officials to repeatedly advance the idea of a Canadian exemption.<sup>29</sup> By the end of March, Thomas Mann wrote to a colleague, “We are under heavy pressure to proceed rapidly to settle the Canadian exemption problem.”<sup>30</sup> A week later, immediately after the Secretary of State’s staff meeting where Merchant solidified support from the top officials, Mann received “authorization” from C. Douglas Dillon “to proceed with the work of granting the Canadians a pipeline exemption.”<sup>31</sup> Merchant’s actions ensured that Eisenhower’s more recent personal directive to do something to “act in unity with Canada,” and to “make this oil move look better

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59, Box 1, File 43.2 *Oil Imports Program Jan-March 1959*, Memorandum to the Secretary through Mr. Becker from Thomas Mann, Subject: Restrictions on Oil Imports, 27 February 1959.

<sup>28</sup>An example of Merchant’s position can be found at, USNA, RG59, General Records of the Department of State, Alpha-Numeric Files Relating to Canadian Affairs, 1957-1963, Box 3, File *Oil Quotas 1957-61*, Memorandum to Mr. Mann from Mr. Merchant, Subject: Restrictions on Oil Imports, 16 January 1959. A later example is, *Ibid.*, Memorandum to Mr. Mann from Livingston T. Merchant, Subject: The Oil Import Program and Our Relations with Canada, 20 March 1959.

<sup>29</sup>One journalist described the Merchant-Dulles relationship as follows: “[Merchant] has probably been closer to Secretary Dulles on more subjects than any other man in the department. He went with [Dulles] on most of his trips, was his principal aide in most negotiations, and enjoyed not only a position of great trust but even of close personal friendship with the Secretary of State.” James Reston, “How Good is the Team?”, *New York Times*, 16 February 1959. Reston commented that the four key people involved in political questions were, in order of importance, Christian Herter (Acting Secretary of State), Robert Murphy (Deputy Under Secretary for Political Affairs), Livingston Merchant (Assistant Secretary for European Affairs), and G. Frederick Reinhardt (State Department Counselor). Reston added that Merchant “will undoubtedly be brought into policy matters, beyond the confines of his title, especially in the Near and Middle East.” Thomas Mann was also mentioned as a capable and generally praiseworthy Assistant Secretary (of Economic Affairs). Mann’s boss was C. Douglas Dillon.

<sup>30</sup>DDEL, T.C. Mann Papers, 1950-1961, Box 1, File *Chron File: Jan-Mar 1959 (1)*, Note to Mr. Rubottom from Thomas Mann, 26 March 1959.

<sup>31</sup>USNA, RG59, General Records of the Department of State, Alpha-Numeric Files Relating to Canadian Affairs, 1957 to 63, Box 3, File *Oil Quotas, 1957-61*, Memorandum to Mr. Merchant from Mr. White, 4 April 1959.

to our neighbours to the north,”<sup>32</sup> actually happened. On 30 April 1959, the U.S., despite much opposition from Venezuela, acceded to Canadian pressure for an exemption to the MOIP. In a clever phrasing that applied mostly to Canada, oil transported overland was spared from the import restrictions. However, in granting the exemption to Canada, the U.S. made it clear that if a pipeline to Montréal were built, the exemption would be revoked and Canada would have reduced access to the U.S. market.<sup>33</sup>

The next task for the Canadian government was to develop its own national oil policy.<sup>34</sup> First, acting on the recommendation of the initial Royal Commission on Energy (Borden Commission) report, Diefenbaker created the National Energy Board (NEB), and one of its functions was to help create oil and gas policy.<sup>35</sup> Then, he waited for the second report of the Borden Commission, which was on oil. Of interest, is that Diefenbaker requested Chairman Henry Borden to delay the release of the report until it was known whether Canada had received an exemption to the MOIP. The report recommended that Canada defer committing to the construction of the Montréal pipeline for a few years, in order to give the exemption a chance. If

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<sup>32</sup>“Act in unity” - DDEL, DDEP, PPUS 1953-1961, AWF, Cabinet Series, Box 13, File Cabinet Meeting March 6, 1959, Minutes of Cabinet Meeting, 6 March 1959, 5. “Make oil move look better” - DDEL, D.A. Quarles Papers, Box 3, File Daily Diaries 1/2/59-5/17/59c3, Diary Donald A. Quarles, Monday, 9 March 1959, 2. Fifteen minutes after Quarles’ phone call with Mueller regarding the President’s wishes on the Canadian exemption, Quarles phoned Mr. Loftus Becker from the State Department and arranged an immediate meeting to discuss the matter.

<sup>33</sup>DDEL, DDEP, PPUS 1953-61, AWF, Diary Series, Box 40, File *Staff Notes – April 1959 (1)*, “Memorandum for Mrs. Whitman from Don Paarlberg, April 27, 1959.” Some may ask what active role the oil companies played in this sequence of events, and the answer is very little. The documentary record contains little evidence of correspondence or meetings between government and company officials regarding the decision to exempt Canadian oil from the MOIP.

<sup>34</sup> For a detailed discussion on Canada’s National Oil Policy decision and the poor relationship that developed between John F. Kennedy and Diefenbaker, see, Tammy Nemeth, “Consolidating the Continental Drift: American Influence on Diefenbaker’s National Oil Policy.” *Journal of the Canadian Historical Association*, Vol. 13 (2002): 191-215.

<sup>35</sup> Diefenbaker’s initial election victory in 1957, which resulted in a minority government, was due in some part to an acrimonious debate in the House of Commons over the construction of a natural gas pipeline. Public opinion became polarized, and oil and gas issues politicised. Once elected, as a way to depoliticise energy issues, Diefenbaker appointed a Royal Commission to examine the state of the oil and gas industry in Canada, and provide recommendations for a national policy. Two reports were produced; the first in October 1958 that dealt mainly with natural gas issues, and the second in the summer of 1959 that dealt with oil issues.

Canadian exports did not increase significantly, and more Canadian oil did not displace foreign oil in Ontario, then the Montréal pipeline should be built.<sup>36</sup> This is perhaps one of the reasons why it was another two years before the NOP was announced.

The NOP of 1961 was created around the MOIP exemption, and committed Canada to reliance upon access to the American market for its Western crude, while continuing to import oil from Venezuela and the Middle East. It reinforced the North-South trade pattern that seemed to be more natural for the Western part of the continent. The policy set aside the idea of the Montréal Pipeline for the time being and advocated a substantial increase in exports to the U.S. that would be equivalent to the amount of oil imported into the Montréal area.<sup>37</sup> As mentioned above, Eisenhower himself had pressed his officials to find a way to accommodate Canada's request for an exemption. The significance of this action on Eisenhower's part was not lost on Diefenbaker. As a result, the shape of Canada's National Oil Policy honoured Eisenhower's efforts by establishing the Ottawa valley line and postponing an oil pipeline to Montréal.

From the announcement of the NOP in 1961 until 1968, Canada's main objective was to maintain its exemption to the MOIP, while the U.S. sought to ensure that Canada did not exceed the agreed upon informal export limits. Soon after the Democrat Administration of John F. Kennedy grasped the reigns of government, officials insisted on an informal understanding to

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<sup>36</sup> The Montréal pipeline was a venture backed by the Canadian independent oil producers led by Home Oil. The Multinational companies, led by Imperial Oil, were against the pipeline and told the Canadian government that their refineries would not voluntarily use Canadian oil in Montréal transported by that pipeline. The government could, of course, compel them to use the Canadian oil through legislation and the NEB. Given Diefenbaker's distrust and loathing of "interests" such as the large integrated oil companies, and his reputation as being an ardent Canadian nationalist and sometime anti-American, it is striking that the NOP took the continentalist shape it did. Despite the pressure from Alberta, the industry, and the recommendations of the Borden Report, as I have argued in detail in "Consolidating the Continental Drift," the MOIP exemption and Diefenbaker's relationship with Eisenhower had the greatest influence in the decision for the NOP.

<sup>37</sup>NAC, MG31 E83, H. B. Robinson Fonds, Volume (Vol.) 4, File 4.2, *February 1961*, "Notes on the New Canadian Oil Policy, February 17, 1961." The NOP was created and considered within the Cabinet Committee on Oil and Gas. The Committee was given specific terms of reference in 1960 by the Cabinet to explore the recommendations of the Borden Commission's second report and the newly formed National Energy Board's (NEB)

prevent oil exports from expanding too quickly into the American market. The terms of the understanding were reviewed regularly and adjusted according to changes in the supply and demand structure of the import areas. The most fascinating part of this rather bureaucratic process was the Canadian success at exceeding the limits on a regular basis. This was due mostly to the unique and extensive transgovernmental networks of Canadian and American officials.<sup>38</sup> However, the Canadian-American relationship that had thrived under Eisenhower quickly soured with the poor personal relations that developed between Kennedy and Diefenbaker.

As tensions between Diefenbaker and Kennedy increased, this poor relationship began to take its toll on Canada-U.S. oil relations, as Kennedy's officials sought ways to reflect his disfavour with Ottawa in tangible ways.<sup>39</sup> For example, from July 1961 onward, John M. Kelly, Assistant Secretary of Mineral Resources for the Department of the Interior, sought to circumvent traditional State Department involvement in the talks with Canadian officials. At one meeting, Kelly was characterised by other American officials as being "inflexible" and "blind to Canadian sensibilities in attempting to force on Canada a quantitative quota which he described as 'not negotiable.'"<sup>40</sup> It should be noted that the Canadians at the meeting were also described

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study on the oil pipeline question. The recommendations for the policy were then brought before and debated within the larger Cabinet.

<sup>38</sup> For a recent excellent discussion of the significance and extent of these transgovernmental networks see, Brian J. Bow, "The Missing Link: Transgovernmental Networks, Bargaining Norms, and Issue-Linkage in United-States-Canada Relations" (Ph.D. diss., Cornell University, 2003).

<sup>39</sup> Charles Ritchie, Storm Signals: More Undiplomatic Diaries, 1962-1971 (Toronto: Macmillan of Canada, 1983), 2-3. Ritchie comments, "For an embassy to be in disfavour with the White House at a time when the office of President was at the height of its power and influence was a disconcerting experience. The word had swiftly percolated down into every department of the United States Administration." (2) See also, USNA, RG59 Alpha-Numeric files Relating to Canadian Affairs, 1957-63, Box 3, File *Oil Quotas 1957-1961*, "Memorandum to George Ball from Philip Trezise, Subject: Canadian Oil, 2 November 1961.

<sup>40</sup> USNA, RG59, General Records of the Department of State, Alpha-Numeric files Relating to Canadian Affairs, 1957-63, Box 3, File: *Oil Quotas 1957-1961*, "Memorandum to George Ball from Philip Trezise, Subject: Canadian Oil, 2 November 1961. Though there were a few senior officials who supported Canada's Exemption such as Ball, Trezise, Ed Martin and others, there were some like Thomas Mann and Mr. Alexander who would have

as inflexible with respect to “the sanctity of the overland exemption to the exclusion of reality.” A month later at an interdepartmental meeting of under secretaries on foreign economic policy Kelly declared that the “U.S. consumer is subsidising Canadian producers” because of its exemption to the MOIP. He went on to accuse Canada of jeopardising continental security because it was so reliant upon imported oil in the Montréal/east coast area, and refused to build a pipeline to Montréal. During the discussion, others commented that it was in America’s “national security interest to receive Canadian oil.”<sup>41</sup> This did not deter Kelly as he pressed for the removal of the Canadian exemption while heading the Interior Department’s review of the MOIP. In fact, Kennedy was set to revoke Canada’s exemption to the MOIP to spite Diefenbaker, but after the Liberals were elected, Prime Minister Lester Pearson talked him out of it at the Hyannisport meeting in 1963.<sup>42</sup> This reinforced to many within the Canadian government Canada’s vulnerability to interdependence and American whims.

Since it was widely perceived that Canada-U.S. relations had deteriorated significantly during the Diefenbaker years, Pearson and Kennedy decided to have a joint study written on the nature and future of the relationship. Kennedy’s sudden death did not derail the project, which was continued during the Presidency of Lyndon B. Johnson. The result, published on 1 July 1965, was the Merchant-Heeney Report. In order to assist the writing of the report, at the JCTEA meeting of April 1964, Canadian and American representatives agreed to initiate joint

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preferred to see Canada’s exemption retracted and seemed to work to undermine Canada to the Secretary of State and presidential advisors. See for example, *Ibid.*, Box 2, File *Oil Import Program Jan-June 1961*, “Memorandum to Mr. Ball from Mr. Mann, Subject: Canadian Oil Problem, 25 January 1961.”

<sup>41</sup>USDOE, Job number 1013, Box 7, Folder 4 *Petroleum Study Committee Task Force Vol. I: Working Papers 1-45*, “Summary of Minutes of Meeting of Interdepartmental Committee of Under Secretaries on Foreign Economic Policy, 13 December 1961”, 4.

<sup>42</sup> John F. Kennedy Library (JFKL), Papers of President Kennedy (PPK), National Security Files (NSF), Countries, Box 19A, File *Canada – Subjects: Pearson Visit 5/63; 4/22/63-5/5/63*, Memorandum of Conversation, Subject: Canadian Oil Exports, 10 May 1963.

energy studies “to serve in essence as an analytical tool in pursuing the objective of freer movement of energy.”<sup>43</sup> The discussions did not last long, and did not result in an agreement.

Part of the reason for the lack of progress on establishing a firmer co-operative framework for Canada-U.S. oil trade was Johnson’s removal of oil policy from the White House.<sup>44</sup> Responsibility for oil policy came to rest with Secretary of Interior Stewart Udall and Under Secretary of State for Economic Affairs Thomas Mann. Initially, Udall wanted to remove Canadian preference in the MOIP, but came to support the maintenance of the arrangement with firmer control on the levels of Canadian imports. Mann, on the other hand, pushed for equality between Venezuela and Canada, much as he had under Eisenhower.<sup>45</sup> As one scholar points out, “The President’s level of involvement is the critical factor accounting for the difference in decision-making behavior. . . . a President can be an omnipotent player if he so desires.”<sup>46</sup> But since there was no clear direction from the White House on what form policy should take, aside from a general objective of trying to improve relations with Venezuela, the struggle between Udall and Mann resulted in management of the system rather than its overhaul. Thus, for the

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<sup>43</sup> NAC, RG99, NEB, Vol. 72, File 53, JCTEA Meeting of 29-30 April 1963, Item 3A (iv): Energy Relations, Joint Energy Studies. See also, *Ibid.*, Memorandum to Mr. I.N. McKinnon from Grey Hamilton, Subject: Joint Energy Studies, 3 June 1964.

<sup>44</sup> Lyndon Baines Johnson Library (LBJL), White House Central Files (WHCF), Subject Files TA6, Box 19, File *TA6/Oil 1/1/65-5/31/65*, Note to President from Jack Valenti, 29 April 1965. A group of Senators repeatedly tried to cut straight to the President on oil related issues. Frustrated, Johnson wrote on yet another request of the Senators to meet with him, “I must not bring oil into W.H. & tell them not to insist – ask them to see Ellington if they won’t see Udall.”

<sup>45</sup> Venezuela’s government was again unstable in the mid-1960s, and politicians exploited the superficial “unequal” treatment with Canada in the U.S. MOIP for domestic political gain. Mann was convinced that alleviating the *appearance* of discrimination towards Venezuela in the MOIP would remove the U.S. as a target in Venezuelan politics. See for example, LBJL, National Security Files (NSF), Country Files, Box 166, File *Canada – Memos Vol. III 3/65-12/65 [2 of 2]*, Document 141, Memorandum of Conversation, Subject: Canadian Oil Imports and Venezuelan Charges of Discrimination, 2 April 1965; LBJL, WHCF, Subject Files TA6, Box 19, File *TA6/Oil 6/11/65-8/30/65*, Memorandum to the President from Lee C. White, Subject: Proposed Adjustment in Crude Oil Import Program, 4 June 1965. White explained the difference in opinion between Mann and Udall, “Tom Mann has tended to give great weight to the Venezuelan political problem; Udall, on the other hand, has tended to be greatly concerned about Canada and the fact that the Canadian government could fall if the burden on them were too great.” (2)

<sup>46</sup> Jerel A. Rosati, “Developing a Systematic Decision-Making Framework: Bureaucratic Politics in Perspective,” *World Politics*, Vol. 33, No. 2 (January 1981), 245-246.

remainder of the Johnson period, Canada-U.S. oil relations revolved around the continued negotiations about the amount of Canadian oil exports under its MOIP exemption.

By 1967, Canadian oil exports to the U.S. had reached such a large level, above what the U.S. considered reasonable, that an informal agreement was reached in which the National Energy Board would request that exporters “voluntarily” keep the exports to an agreed upon level. The NEB and the U.S. authorities in the Oil Import Administration seemed unable to prevent the Canadian imports from exceeding the agreed upon limits.<sup>47</sup> At this point, Canada was completely unwilling to entertain the idea of imposing export controls on oil. Then, the large Alaskan oil fields discovered around Prudhoe Bay in 1968 threatened Canada’s export position in the American Pacific Northwest. In addition, a new pipeline bringing oil into the Chicago area was nearing completion and would displace Canadian oil in that region as well.

Even with rising American demand, it appeared to many policy-makers that Canadian oil exports would most likely be curtailed, and it would become even more difficult to obtain American understanding (or sympathy) for ensuring Canada’s share of the American market. Those like Mitchell Sharp, former Canadian Deputy Minister of Trade and Commerce and subsequent Cabinet Minister, who subscribed to the informal continentalism approach, realised that the first stage was no longer working; there was too much uncertainty and potential for arbitrary American action, therefore some kind of formal sectoral arrangement would be

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<sup>47</sup>There are several reasons why Canadian exports continued to exceed agreed upon limits. At first it was due to a lack of American supply in the area (the pipelines from Texas and Louisiana were not yet completed). Then, by 1969, it was due to the combined circumstances of a looped pipeline from Canada through Chicago, and a price advantage of Canadian oil because of price increases in the U.S. See USNA, RG 59, E-5200 – Minutes of Economic Staff Meetings, 1960-1969, Box 6, File *E Staff Meetings January-June 1969*, E Staff Minutes 7 February 1969, 2; USNA, Nixon Project, White House Central Files (WHCF), Subject Files, CO 28, Canada [EX], Box 14, File [EX] *CO 28 Canada Begin – 6/30/69 [1 of 2]*, Memorandum to Robert F. Ellsworth from J. Cordell Moore, 25 February 1969; and RG 59, E-1613, Central Foreign Policy Files (CFPF), Subject Numeric – Economic 1967-1969, Box 1349, File *PET 11-2 CAN 1/1/69*, Telegram 052381 from Department of State to Amembassy Ottawa, Subject: Canada-U.S. Oil and Energy Talks April 2, 5 April 1969, 3.

preferable.<sup>48</sup> Elected in 1968, the new Liberal Government led by Pierre Trudeau, at the request of Secretary of State for External Affairs Mitchell Sharp, began discussions in April 1969, which continued into 1973, for a continental energy agreement and then a scaled down continental oil policy between Canada and the U.S.<sup>49</sup>

An important development in this period, which affected how Canada-U.S. oil relations, and a possible continental oil policy, were considered and dealt with, was the similarity between Trudeau and U.S. President Richard Nixon in their approach to governing. Both embraced the efficacy of expansive studies and planning, had an unwavering faith in technocracy, employed a constant rotation of personnel at the executive level, and had an obsession with “tactics” in negotiations. Both Canada and the U.S. initiated studies of their respective oil policies. In Canada, it was an interdepartmental Oil Policy Review, and in the U.S. it was the Cabinet Task Force on Oil Import Control headed by Secretary of Labor George P. Shultz. The Canadian review was not completed until June 1973; by then the circumstances informing the basis of the review had changed rendering it obsolete almost immediately. The American study was released in 1970, but few if any of its recommendations were followed. Prime Minister Trudeau’s interest in oil policy fit into his larger objectives for the Canadian economy, but until his gradual restructuring of the policy-making structure was complete, he preferred to defer real action. In contrast, although Nixon “announced that he was assuming direct responsibility for oil import

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<sup>48</sup>USNA, RG 59, State Department, E-1613, CFPF, Subject-Numeric – Economic 1967-1969, Box 1349, File *PET 11-2 CAN 1/1/69*, Telegram 023543 to Amembassy Ottawa from Department of State [Secretary Rogers], no subject, 13 February 1969. Norm Chappell, the Canadian embassy’s energy counsellor, was reported to have assured Interior and State Department officials that “Canada intended to live up to the 1967 understanding, but he pointed out that it could be modified by joint consultations and GOC was anxious to embark on such talks as soon as certain key positions in State and Interior were filled.”

<sup>49</sup>USNA, RG 59, E-1613, CFPF, Subject-Numeric – Economic 1967-1969, Box 1350, File *PET 17-2 CAN 1/1/67*, Memorandum of Conversation, Subject: Canadian Oil, 25 March 1969, 1-2. See also *idem*, Box 1349, File *PET 11-2 CAN 1/1/69*, Telegram 031468 from State Department to Amembassy Ottawa, Subject: Canadian Oil, 28 February 1969. This was a copy of an Aide Memoire delivered to the State Department by Canadian Ambassador

policy,” his style of leadership inhibited actual change from taking place.<sup>50</sup> Constant reorganisation occurred, competition between senior officials for positions of power and the ear of the leader were encouraged, and there was a lack of consistency and support for policy action. President Nixon may have had a serious *interest* in oil policy, but he provided no clear *direction* for action. Canadian Cabinet discussions in the negotiations for a continental oil policy with the U.S. are filled with talk of tactics – how to delay, and so on.<sup>51</sup> Similarly, Nixon and his advisors often spoke of tactics, one of which was the “harder line,” discussed below, taken to persuade Canada to negotiate seriously for a continental oil agreement.

During the continental oil agreement discussions, it became clear to the American officials that the Canadian government did not want to take any action, or support any policy, that would raise prices in eastern Canada.<sup>52</sup> In addition, since the late Eisenhower period an attitude had been taking root in some U.S. government departments like State and Interior, that the U.S. bore all the costs while Canada reaped all the benefits from the “special relationship.” Policy-makers believed that a continental energy or resources policy with Canada was “inescapable,” but it would have to be more fair or equitable – in the sense that Canada would have to accept some costs in the relationship and not “settle only for the economic benefits.”<sup>53</sup> Thus, the U.S. insisted that as part of any agreement, Canada must exert greater control over its

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A. E. Ritchie, suggesting that oil talks begin. What is interesting is that a comprehensive energy agreement is not specifically mentioned, phrases such as “broad review” of policies were used instead.

<sup>50</sup>Neil De Marchi, “Energy Policy Under Nixon: Mainly Putting out Fires,” in Energy Policy in Perspective, ed. Craufurd Goodwin (Washington, D.C.: Brookings Institution, 1981), 400.

<sup>51</sup>See for example, NAC, RG 2, Privy Council Office (PCO), Vol. 6340, File “23 Sept – 4 Dec 1969”, Cabinet Decisions, 4 Nov 1969, Item 7 “Oil Policy Problems,” 19; NAC, RG 2, PCO, Series A-5-a, Vol. 6395, 20 April 1972, “Canada-United States Oil Considerations Relative to Security of Supply and Access to United States Markets,” 6.

<sup>52</sup>USNA, RG 434, Oil Import Administration, Box 100, File *Oil Import Administration, Canada (Gen Corres w/Companies See file on Dept of Defense Prod.)*, Resume of Canadian Talks at Ottawa February 10-12, 1970, 3.

<sup>53</sup>USDOE, Job 1009, Box 16, Folder 2 *US/5/412 Task Force on Oil Import Policy, General 1968-May to Oct 1969 Vol. I, Error! Main Document Only*. Broad Approach to Possible Arrangements with Canada [no date].

exports and reduce its reliance on imported oil. But Canada refused to guarantee that it would not curtail exports to the U.S. in an emergency, impose export taxes, or reduce its imports into eastern Canada.

Several meetings were held to try and reach a common position, but the strategy of the Canadian officials, as directed by Cabinet, was to delay and distract for as long as possible. The U.S. persisted with the talks because they believed an agreement would compel Canada to reduce its foreign imports and make it one less place to worry about in case of a crisis; it would also be an assured strategic reserve. Nevertheless, frustrated at the diversions and delays, American officials counselled President Nixon to enact “temporary” formal restraints on Canadian oil imports as a means to motivate the Canadians to take the negotiations for a continental energy policy more seriously.<sup>54</sup> The assumption was that Canada would realise that its best interests lay in a more formal agreement with the U.S. Thus, on 10 March 1970, President Nixon announced that the volume of Canadian oil imported into the U.S. would be formally limited. Nixon’s tactics backfired.

Canada’s immediate response was to suspend negotiations, but within a few months discussions started once more.<sup>55</sup> The U.S. was concerned because it seemed to them that Canada was increasing its oil exports in order to take advantage of the higher prices, while making the Canadian market even more dependent on cheaper but insecure imported oil. In fact, this was the admitted intent as revealed in the Cabinet discussions of the Canadian “Oil Policy Review” of May 1969; the Cabinet understood the Canadian domestic policy to be “of buying in the

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<sup>54</sup>USNA, RG 396, Office of Emergency Preparedness (OEP), Subject Files Oil Policy Committee 1969-1973, Box 46, File *Oil Policy Committee – General 2 of 4*, Memorandum to Peter Flanigan from G.A. Lincoln [Director, OEP], 3 March 1970; USNA, Nixon Project, WHCF, Subject Files TA Tariff-Imports, Box 26, File *[EX] TA4-CM Tariff-Imports [7 of 12 Oil March 1970]*, Memorandum to the President from Peter Flanigan, 9 March 1970.

<sup>55</sup>Editorial “The message is true,” Globe and Mail, 13 May 1970, 6.

cheapest market [Middle East/Venezuelan oil] and selling in the most expensive [U.S. market].”<sup>56</sup> The overall consequences of Canada’s policy was that Canadian oil was exported to the U.S. in record amounts in order to gain the premium American price, while significantly cheaper Venezuelan and Middle Eastern oil flowed into eastern Canada.

Canada was becoming increasingly dependent on imported oil for its domestic needs, and did not seem willing to alter the situation. Then, when pipeline capacity peaked in 1972 and it appeared Ontario refiners would fall short of supplies because sellers received a higher price in the U.S., export controls to limit the amount moving into the U.S. market were implemented in February 1973. When the OPEC-led Arab embargo on the U.S. was announced in October 1973, the Canadians, worried that American oil companies would divert their shipments from Canada to the U.S., and that Canada too might be subjected to the boycott, suddenly “seemed eager to enter into serious discussions about a ‘coordinated’ [sic] oil policy.”<sup>57</sup> American officials replied that they understood from Canadian statements that oil exports to the U.S. would be curbed, which had prompted the U.S. to pursue a policy toward self-sufficiency.<sup>58</sup> A month later, in yet another apparent change of mind, Prime Minister Trudeau alluded in a letter to the President that oil exports were to be phased out.<sup>59</sup> Over the next year, Canadian officials privately served notice on the U.S. that oil exports would indeed be phased out, and an announcement was issued in November 1974.<sup>60</sup> The era of informal continentalism was at an end.

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<sup>56</sup>NAC, RG 2, Vol. 6347, File 512-69, Memorandum to the Cabinet, Oil Policy Review, 15 May 1969.

<sup>57</sup>Lafayette College, William Simon Papers, Series IIIA, Subject Files (Deputy Secretary), Drawer 12 Administration Miscellany – Federal Budget, Folder 12:17 *Canada: 1973-74*, Memorandum for William E. Simon from William A. Johnson, Subject: Discussion with Canadian Energy Officials on October 23, 24 October 1973, 1.

<sup>58</sup>*Ibid.*, 2-3.

<sup>59</sup>USNA, RG 59, E-1613, Subject-Numeric – Economic 1970-1973, Box 1490, File *PET 1 CAN 6/1/70*, Letter to the President from Prime Minister Trudeau, 7 November 1973.

<sup>60</sup>Gerald R. Ford Library (GRFL), WHCF, CO 28, Box 11, File *CO 28 Canada, 12/1/74-12/31/74 (Executive)*, Briefing Memorandum for the President from Henry A. Kissinger, Meeting with Pierre Elliott Trudeau Prime Minister of Canada Wednesday, December 4, 1974, 4.

## **II. Experimental Economic Nationalism or Continentalism Rejected: 1973-1984**

Canada-U.S. oil and gas relations underwent a massive shift in this period, and interdependence in the shape of an informal continental oil and gas agreement was no longer a welcome option. More nationalistic and interventionist policies emerged, especially from Canada, as confrontation and unilateralism were employed in order to assert controversial goals. The separation in Canadian and American views of their oil and gas trade had more to do with internal Canadian dynamics than with American goals, which at this time was to expand imports from non-OPEC countries like Canada. The politicisation of the Canadian bureaucracy and the changes to the policy-making process had a profound effect on Canada's oil and gas policy, which had deleterious consequences for the U.S. The Americans learned from this period that they too were vulnerable to Canadian whims, and experienced the uncertainty of not having some kind of formal agreement to govern oil and gas trade. This section will examine two major developments of the period: Canada's decision to phase out oil exports in 1974, and the introduction of the controversial Canadian National Energy Program.<sup>61</sup>

The Canadian policy reversal, from seeking expanded U.S. markets for Canadian oil to phasing out exports all together in 1974, was heavily influenced by Prime Minister Pierre Trudeau's politicisation of energy issues and the bureaucracy.<sup>62</sup> Energy became politicised during the Trudeau era, not only because prices increased dramatically, but also because energy was at the centre of Trudeau's economic policy. An economically strong and united Canada, with the federal government planning and reshaping the economy to Trudeau's vision, in line

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<sup>61</sup> The focus here is on Canadian policies because there were few American policies in this period that affected Canada, aside from the creation of the International Energy Agency and a few minor bilateral agreements.

<sup>62</sup> Politicisation in this case has a dual meaning. On the one hand, it denotes a high level of attention given a particular issue among key Cabinet Ministers and the Prime Minister (the traditional definition). On the other, it means the appointment of specifically recruited people into key civil service positions, who were either linked with the Leader of the ruling political party or were of a similar ideological persuasion.

with popular left-wing thinking of the time, meant altering the Canadian economy's reliance on staple exports like oil, to secondary manufacturing.<sup>63</sup> In practice that meant encouraging Canadians to take over the foreign investment in the industry so that the revenue generated would accumulate in Canadian hands, which could then be reinvested in expanding manufacturing. If Canadians were unwilling to act, or act quick enough, the federal government itself would take an active interest through the creation of a crown corporation. In addition, once prices began to rise the Trudeau government sensed an opportunity. If Canada could have all of its oil supplied internally at a controlled price, well below the world price, then the competitive advantage gained by Canada's industrial base, which happened to be in the non-oil producing areas of Québec and Ontario, would be incredible.<sup>64</sup> But, in order to carry out these changes, officials had to be trusted to develop the appropriate policies. Trudeau and others in his inner circle suspected that there would be a great deal of resistance to these ideas within the bureaucracy.<sup>65</sup> The solution was to restructure the bureaucracy and the policy-making process; the result was the politicisation of the bureaucracy. Trudeau used the Prime Minister's Office (PMO) and the Privy Council Office (PCO) to recruit, train, and then promote people who preferred nationalist alternatives to continentalism, and would be loyal to the PM above all others.<sup>66</sup>

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<sup>63</sup>Pierre Elliot Trudeau, Memoirs (Toronto: McClelland & Stewart, 1993), 164. Pierre Elliott Trudeau, "The Values of a Just Society," in Towards a Just Society: The Trudeau Years, ed. Thomas S. Axworthy and Pierre Elliott Trudeau (Markham, Ont: Viking, 1990), 361.

<sup>64</sup> In the Canadian federal state, jurisdiction over natural resources lies with the provinces. Most of the conventional oil in Canada, as well as the mammoth-sized Athabasca oil sands, are located in the western province of Alberta. A series of federal-provincial conflicts erupted over resources in this period, particularly pricing and revenue sharing, but since the focus here is on Canada-U.S. relations the intricacies of this confrontation will not be explored.

<sup>65</sup> Members of Trudeau's inner circle included Marc Lalonde, Michael Pitfield, Allan MacEachen, Jean Marchand, Gerard Pelletier, and a few others.

<sup>66</sup> American audiences may not see anything unusual about Trudeau's restructuring, but it represented a tectonic shift in the structure, and perhaps very nature, of the Canadian system. Some might even argue that the process undertaken by Trudeau was the Americanisation of the Canadian bureaucracy and policy process. See for example, Donald J. Savoie, Breaking the Bargain: Public Servants, Ministers, and Parliament (Toronto: University

In order to convince the public and deflect criticisms from Alberta, the other oil producing provinces, and the U.S., there had to be a better reason for phasing out oil exports than industrial advantage in Central and Eastern Canada. The new role of the NEB, envisioned by Jack Austin<sup>67</sup>, the new externally appointed Deputy Minister of Energy, Mines and Resources (EMR), was not to provide policy advice, but rather to support and corroborate policies emanating from EMR. Thus, two NEB reports on supply were written and used as a justification to limit and then phase out exports.<sup>68</sup> In these changing circumstances, the conscientious and independent-minded Chairman of the NEB, Robert Howland, was encouraged to take “early retirement,” and was replaced by another external appointment, the well-connected and political Marshall Crowe.<sup>69</sup> The modification of the policy-making structure of EMR and the NEB, as well as the personnel in those areas, ensured that there would be few difficulties in developing and implementing a more interventionist role for the state in Canadian oil policy. The ultimate objective of those interventionist policies, was to keep oil prices for Canadian consumers at a

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of Toronto Press, 2003). Savoie comments, “Ministers and public servants used to operate under a traditional bargain that gave the public service more opportunity to focus on the long-term interests of the country, however broadly defined, and to challenge the views of ministers in confidence. Civil servants now tend more to anticipate the wishes of the prime minister and of strong ministers and to protect their political interests.” (16) This transformation began with Trudeau’s restructuring of the system.

<sup>67</sup>Austin was a former Liberal Candidate and advocated a state role in the oil and gas industry. He was given the task of consolidating policy-making power in EMR, diverting it from the NEB. Austin led the first wave of restructuring, during which time he quietly replaced officials who disagreed with a more interventionist oil policy.

<sup>68</sup>One scholar, political scientist Dr. John B. Robinson, suggests that throughout the 1970s, the NEB tailored its energy supply and demand forecasts to reflect “the direction of contemporary policy . . . and major project proposals of the time.” John Bridger Robinson, “Pendulum Policy: Natural Gas Forecasts and Canadian Energy Policy, 1969-1981,” *Canadian Journal of Political Science*, XVI:2 (June 1983): 299-301. Although Robinson focuses primarily on the natural gas forecasts, he does explore to some degree the oil forecasts as well.

<sup>69</sup> Crowe had served in the PMO as an economic advisor to the PM, in the PCO in various positions, and had been head of the Canada Development Corporation. There is evidence that the NEB under Crowe, during public hearings on oil exports, deliberately disregarded testimony and data that did not coincide with the Government’s goal to phase out exports. See for example, USDOE, Job 1418, Box 1, Folder 11 *Johnson, Bill Memos and Bass*, Memorandum to William E. Simon, John C. Sawhill, Gerald L. Parsky from William C. Calkins thru William A. Johnson, Subject: Oil Policy Review in Canada – A Trip Report, 12 April 1974. See also, Earle Gray, *Forty Years in the Public Interest: A History of the National Energy Board* (Vancouver: Douglas & McIntyre, 2000), 58.

relatively low level for as long as possible, enhance the state's role in the oil and gas industry, and increase Canadian ownership of the industry. The first step toward that larger vision of self-sufficiency was to phase out oil exports.<sup>70</sup>

This Canadian policy decision had significant consequences for the U.S. Most refineries in the American Mid-West were completely dependent on Canadian oil, as there were no other sources for this land-locked region.<sup>71</sup> The pipelines that had been built to serve that area came from Canada, and new pipelines would have to be built or the refineries would have to close. Given that Canada was supplying approximately ten to fifteen percent of American imports at this time, the phasing out of oil exports also made the U.S. *more* dependent on other sources of oil. Furthermore, despite Canada's participation in the creation of the International Energy Agency in 1974, it seemed to some that Canada was letting America down in its time of need, which sent the wrong message to the rest of the world. Since the Mid-West region was the home of Gerald Ford, Vice President and then President of the U.S., one would think that the response would be fierce. However, although the U.S. actively sought to change aspects of the policy, it was done through quiet diplomacy and with a sense of resignation; America too had been aiming for self-sufficiency, so how could they begrudge their closest neighbour from doing the same?

If politicisation matters, and causes conflict, then why was the American reaction to the phasing out of oil exports in 1974, relatively mild?<sup>72</sup> The most compelling reason for the benign official response was that lengthy advanced consultations and "signals" that these changes would

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<sup>70</sup> For a detailed examination of the decision to phase out oil exports see, Tammy Nemeth, "Continental Rift: The 1973 Energy Crisis and Canada-U.S. Oil Relations," Paper presented at the Association for Canadian Studies in the United States (ACSUS) conference, Portland, Oregon, November 2003.

<sup>71</sup>This is the Northern Tier area. The Pacific region had access to sources from Alaska and overseas so would not be as affected by the Canadian decision.

<sup>72</sup>GRFL, WHCF, CO 28, Box 11, File *CO 28 Canada, 12/1/74-12/31/74 (Executive)*" Briefing Memorandum for the President from Henry A. Kissinger, Meeting with Pierre Elliott Trudeau Prime Minister of Canada Wednesday, December 4, 1974, 4. There is little mention of the phase out in the archival record, around the

be taking place warned the U.S. about pending actions, hence they were not surprised, and the reaction was mild. In the early days of the restructuring of the EMR bureaucracy, interdepartmental discussions still took place with regard to policy development, and the traditional involvement of External Affairs in energy issues still existed. Thus, for example, when it was decided to phase out oil exports to the U.S., American officials were apprised and reminded of the fact for almost a year in advance by Canadian officials from EMR, the NEB, as well as External Affairs.<sup>73</sup> The Prime Minister also forewarned the President in a November 1973 letter that oil exports were to be phased out -- a year before the policy was introduced.<sup>74</sup> In addition, since the U.S. was trying to establish an International Energy Agency to counter OPEC, it did not want to send the wrong message to OPEC or the international community by responding harshly to Canadian policies. Nevertheless, the U.S. did protest Canada's oil export fee and the phasing out of oil exports through quiet diplomacy, and many congressmen and the general public expressed a sense of betrayal, but the Ford Administration seemed resigned to the Canadian policy shift on phasing out exports. A very different reaction from the Reagan

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time of its announcement, except for a brief comment made during Trudeau's visit to Washington in December 1974, when Ford expressed his disappointment but understanding of the policy.

<sup>73</sup>There are numerous documents between 1972 and 1974 that demonstrate the Americans expected some kind of oil export controls, and had been forewarned by March 1973 that oil exports might be phased out completely. See for example, USNA, RG 59, CFPF, Subject-Numeric – Economic 1970-1973, Box 1055, File *FT CAN-US 1/1/70*, Telegram 1110 from Amembassy Ottawa to SecState WashDC, Subject: Policy: U.S. Oil Import Policy and Canada's Role in U.S. Supply, 20 June 1972; USNA, RG 59, Subject-Numeric – Economic, 1970-1973, Box 1494, File *PET 4 CAN-US 1972*, Memorandum of Conversation, Subject: U.S.-Canadian Oil Talks, 27 June 1972 Ottawa. During these talks, the Canadians produced oil export numbers with the notation that the "level [was] not attainable in period for lack of facilities." (p7). USNA, Nixon Project, WHCF, Subject Files, CM29, Box 11, File *[EX] CM29 Petroleum and Coal Products [3 of 47] Jan 1972-March 1973*, Memorandum for Peter Flanigan from Jim Akins, Subject: Further on Canadian Oil Price Increases, 12 January 1973. Signals were being sent from EMR Minister Macdonald that "if United States demand for Canadian oil were to grow to the point where Canada would go short, the National Energy Board had the authority to impose export controls." See also USDOE, Job 1009, Box 10, Folder 8 *US/8/111 Canada – Oil, Gas, etc. Vol. I*, Memorandum to Deputy Secretary Simon from D. R. Ligon, Subject: Canadian Oil Export Controls, 27 February 1973. Simon was told "that we cannot expect to get more crude from Canada in the future until such time as their Arctic reserves are opened up for exploitation."

<sup>74</sup>USNA, RG 59, E-1613, Subject-Numeric – Economic 1970-1973, Box 1490, File *PET 1 CAN 6/1/70*, Letter to the President from Prime Minister Trudeau, 7 November 1973.

Administration confronted the release of the 1980 National Energy Program. But first, a brief comment must be made about the Trudeau-Carter relationship.

The friendly relationship between President James E. Carter and Trudeau had an indirect impact on Canada-U.S. oil relations. Soon after Carter was elected, he selected James Schlesinger to co-ordinate a small group of people to develop a comprehensive energy policy known as the National Energy Plan. Within a few months this small group, working mostly in isolation except for a few token meetings with industry and government agencies, produced Carter's NEP.<sup>75</sup> After announcing the ambitious program, over a year later only about half of the package had made it through Congress. Perhaps coincidentally, Canada followed a similar process for creating its controversial National Energy Program, which happened to share the same acronym as Carter's earlier policy. Minister of Energy, Mines and Resources, Marc Lalonde, was given the direction and authority to create a comprehensive energy policy for Canada. He put together a small, hand-picked, group of loyalists who worked mostly in secrecy with little consultation with industry, the provinces, or the United States. Essentially, the policy they created, which will be discussed in more detail below, sought to reduce foreign (American) investment and ownership of the Canadian oil and gas industry, redirect power and control over oil and gas issues from the producing provinces (who constitutionally control the resources) to the federal government, and ultimately partially nationalise the oil and gas industry. However, due to the differences between the Canadian and U.S. systems of government, the Trudeau government was able to successfully pass the entire NEP with few changes. Given the proximity of the American election to the announcement of the NEP on 28 October 1980, the response from the Carter administration was shock and anger, but had little force behind it.

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<sup>75</sup> James L. Cochrane, "Carter Energy Policy and the Ninety-fifth Congress," in Energy Policy in Perspective, ed. Craufurd Goodwin (Washington, D.C.: Brookings Institution, 1981), 552-555.

However, two years earlier, plans for a comprehensive Canadian energy policy were already being put in place. A major restructuring of EMR was initiated in 1978, at the behest of Marc Lalonde, who anticipated taking over the portfolio after the next election.<sup>76</sup> This time a completely new policy-making division was created under the direction of Mickey Cohen, George Tough, and Ed Clark. They personally selected the new employees and reassigned those who did not meet their standards.<sup>77</sup> When Lalonde became Minister of EMR in 1980, after the brief Progressive Conservative interregnum of 1979, EMR was ready and willing to tackle the creation of a comprehensive program. The prospect and intellectual challenge of “redesigning an entire industry’s dynamics” was exciting, as ideas could be put into action.<sup>78</sup> These people were motivated and buoyed by their unwavering faith in the ability of technocracy and planning to address and solve pressing and troublesome economic issues. With the assistance of core Finance and PCO officials, like Ian Stewart and Michael Pitfield, and without consultation with other departments, the provinces, or the U.S., the NEP was developed in great secrecy as part of the 1980 budget.<sup>79</sup>

The primary goal of the NEP was to achieve energy self-sufficiency in Canada by 1990. Energy security was to be achieved by increasing Canadian ownership and participation in the oil

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<sup>76</sup>Stephen Clarkson and Christina McCall in Trudeau and Our Times, Vol. 1 (Toronto: McClelland & Stewart, 1990) suggest that the 1978 bureaucratic shuffle was motivated by the anticipation of an election in 1978, which was delayed until 1979 (138-39). See also Christina McCall-Newman, Grits: An Intimate Portrait of the Liberal Party (Toronto: Macmillan of Canada, 1982), 318-19. Lalonde’s involvement in the shuffle of EMR and Finance personnel suggests that he had already shifted his focus to a new priority – EMR.

<sup>77</sup> James A. Desveaux, Designing Bureaucracies (Stanford: Stanford University Press, 1995), 78-80.

<sup>78</sup> Clarkson and McCall, Trudeau and Our Times, Vol. 2 (Toronto: McClelland & Stewart, 1994), 199.

<sup>79</sup>Some suggest that Lalonde was compelled to create the NEP in secret because Alberta was unwilling to compromise at the few perfunctory meetings that were held in the spring and summer of 1980. The failure of the Conservative Clark government to negotiate an agreement with Alberta is also pointed to as evidence of Alberta’s intransigence. This argument is rather disingenuous. As far back as January 1974, Lalonde had declared his willingness to act unilaterally with respect to Alberta, on the slightest of pretence, and basically nationalize the industry in the “public interest.” In the Cabinet Discussions of 17 January 1974 Lalonde commented, “If during the course of the energy conference it became apparent that there was no possibility of agreement, the government should preserve its option to force direct confrontation involving, for example, disallowance [of Alberta’s royalties

and gas industry, at the expense of the mostly American owned Multi-National Companies, finding new sources of Canadian oil and gas on federal lands, and increasing the federal share of oil and gas revenues. Numerous new taxes and regulations were introduced and the Canadian Oil and Gas Lands Administration (COGLA) was created to administer exploration and development on Canada Lands (federal lands including the Arctic and offshore areas).<sup>80</sup> Following exploration, any production from the Canada Lands had to be undertaken by a firm that had a minimum of fifty percent Canadian ownership. All companies holding interests on Canada Lands had to renegotiate their exploration agreements with the COGLA and return fifty percent of their lands to the Crown without compensation. In addition, a twenty-five percent interest or “back-in” to be controlled by Petro-Canada or some other crown corporation was required, without compensation, for every development, past or future on the Canada Lands.<sup>81</sup> These measures were met with shock, dismay, and anger from different affected quarters, including the U.S.

The crisis that ensued between the Federal Government and the U.S. was magnified because there had been little forewarning about the nature and level of intervention included within the policy changes.<sup>82</sup> What concerned the U.S. most was that the NEP and the Foreign

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for taxation purposes] and take-over of the control of the oil and gas industry on grounds of public interest.” NAC, RG2, PCO, Cabinet Discussions, 17 January 1974, “Oil and Natural Gas Pricing, Taxing and Revenue Sharing,” 14.

<sup>80</sup> New taxes included the Petroleum Compensation Charge (PCC), the Oil Import Compensation Program (OICP), the Natural Gas and Gas Liquids Tax (NGGLT), the Petroleum and Gas Revenue Tax (PGRT), and the Canadian Ownership Charge (COC).

<sup>81</sup> Government of Canada, Department of Energy, Mines and Resources, The National Energy Program (Ottawa: Supply and Services, 1980). For a complete description and breakdown of the various taxes and regulations please refer to the NEP document.

<sup>82</sup> The focus here is on Canada-U.S. relations, therefore a detailed outline of the rift with Alberta and the industry will not be included. Suffice it to say that the Alberta government responded vigorously to the NEP. First it reduced oil production and shipments to Eastern Canada, in three stages, by 60,000 barrels per day. It also launched a court challenge to the NEP on the grounds that federal taxation on exports of provincially-owned resources was a violation of the constitution. The result of Alberta’s retaliatory actions was the 1981 Energy Accord, or Canada-Alberta Energy Agreement. In addition, the Alberta government withheld approval of new oil sands and heavy oil projects. For more information see, Bruce G. Pollard, “Canadian Energy Policy in 1985:

Investment Review Agency were “blatantly discriminatory with reference to the operations of American companies in Canada.”<sup>83</sup> If Canada wanted to preserve its resources for itself, the U.S. would be disappointed but not object strenuously, but discrimination against American companies was a whole other matter as it set a dangerous precedent for other countries in the world.

Several accounts of the American reaction to the NEP have claimed that the U.S. was outraged and made heavy-handed demands.<sup>84</sup> This is an exaggeration. Despite the ideological and personal differences between Reagan and Trudeau, Reagan had hopes for greater North American unity. He saw Canada as part of ‘fortress North America’ – economically and politically – at a time of an increase in regional trading blocs and growing cold war tensions. Thus, despite the disagreeable NEP, Reagan was favourably disposed towards Canada and Trudeau. Although elements within the newly elected Reagan Administration advocated retaliatory action, forceful arguments were made with the support of the President, that diplomacy should be employed instead.<sup>85</sup> The U.S. responded by holding a series of discussions with Canadian officials. However, American participants began to sense that the discussions were a delaying tactic to keep the U.S. preoccupied while the NEP legislation made its way through the House of Commons. Once enacted, it would be difficult to convince the Canadians

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Towards a Renewed Federalism?”, Publius, (Vol. 35, Spring, 1991), 166. See also Kenneth Norrie, “Energy, Canadian Federalism, and the West,” Publius (Vol. 14, Winter, 1984), 88.

<sup>83</sup>Ronald Reagan Library (RRL), White House Office of Records Management (WHORM), Subject Files, FG010-02, Box 15, File FG 010-02 (018919CA), National Security Council, Memorandum for Richard V. Allen from Norman A. Bailey, Subject: Cabinet Council on Economic Affairs Meeting of July 29, 1981, 30 July 1981

<sup>84</sup> See for example, Stephen Clarkson, Canada and the Reagan Challenge (Toronto: James Lorimer & Co., 1985), 33-45; Clarkson and McCall, Trudeau and Our Times, Vol. 2, Chapter 6 “Hurricane Ronnie: American Retaliation,” and J.L. Granatstein and Robert Bothwell, Pirouette: Pierre Trudeau and Canadian Foreign Policy (Toronto: University of Toronto Press, 1990), 325-326.

<sup>85</sup>RRL, WHORM, Subject Files, FG010-02, Box 15, File FG 010-02 (018919CA), National Security Council, Memorandum for Richard V. Allen from Norman A. Bailey, Subject: Cabinet Council on Economic Affairs Meeting of July 29, 1981, 30 July 1981. The U.S. Trade Representative remarked at the meeting that he “intend[ed] to take a measured, quiet and non-demagogic approach to the issue.”

to alter the policies. Still, the President insisted that American representatives “attempt to resolve our differences with the Canadians through quiet bilateral consultations.”<sup>86</sup> These discussions bore some fruit and the Canadian government announced, at the end of 1981, two changes to the NEP in Bill C-48, the Canada Oil and Gas Act.

Nevertheless, the NEP had caused a considerable amount of tension not only between Ottawa and the provinces, but also between Ottawa and the United States.<sup>87</sup> The politicisation of energy issues by Trudeau, and the attitude and ideology of officials responsible for developing the NEP, were significant factors in the confrontation that ensued with the U.S. Despite the modifications to the NEP, it remained mostly intact and in effect until 1985 when the newly elected Progressive Conservative government implemented a new energy policy that aimed to dismantle the burdensome regulatory regime of the NEP.

### **III. Formal Continentalism or Continental Convergence: 1984 to 1988**

Canada-U.S. oil and gas relations underwent another immense shift in this period, and continental interdependence was once again a welcome option, this time in the shape of a formal agreement. The energy provisions of the 1988 Canada-U.S. FTA marked a dramatic departure from previous Canadian and American energy policies. For the first time, Canada and the U.S. concluded a formal continental energy policy with respect to the open trade of oil and natural gas, and embedded it in a larger comprehensive agreement.

The NEP had soured the Canadian-American relationship, enraged the producing provinces, and infuriated the oil and gas industry. In addition to the negative view of the NEP from the United States, Western Canadians believed that the Liberal party’s NEP discriminated

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<sup>86</sup>RRL, WHORM, Subject Files, FG010-02, Box 17, File FG010-02 (018975CA) [1 of 2], Memorandum to the President from William E. Brock [U.S. Trade Representative], Subject: Status of U.S.-Canada Bilateral Trade and Investment Issues, 30 October 1981, 2. Brock also conveyed a warning to the President, “We cannot allow these discussions to become a further delaying device, as has happened in the past.” (2)

against them, and the oil and gas industry viewed the NEP as an unnecessary government intrusion into their business: These interests wanted the NEP dismantled.<sup>88</sup> After Brian Mulroney was elected as leader of the opposition in the spring of 1983, he appointed Patricia (Pat) Carney as opposition energy critic. Her task was to develop a Canadian energy policy that would dismantle and replace the NEP.<sup>89</sup> In another coincidence, she did so while in opposition, employing various study groups and task forces of industry representatives, just as Reagan developed his energy policy before elected with the assistance of study groups headed by the Heritage Foundation. A year later, in September 1984, Brian Mulroney and the Progressive Conservative Party were swept to power and Pat Carney was set to dismantle the NEP.

Although the politicised bureaucracy from the Trudeau era attempted to undermine Carney's efforts when she became Minister of EMR, the NEP was dismantled along the lines Carney had developed in opposition. The goal was to allow market forces to prevail, but the federal government retained a *force majeure* clause that would allow the Canadian government to protect consumers in the case of extraordinary fluctuations in world oil prices. The major obstacles for Canadian-American relations, which had been put in place by the NEP, were dismantled; economic nationalism in the oil and gas industry as a policy option was discarded.

However, all of these policy changes did not prevent the possibility of another NEP being implemented by a future government. One option that the Mulroney government could have taken after the NEP was dismantled, was to embrace the traditional informal continentalism approach, and enter into an informal or even a sectoral agreement with the U.S. on the trade of

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<sup>87</sup>Norrie, "Energy, Canadian Federalism, and the West," 81.

<sup>88</sup>Clarkson, *Canada and the Reagan Challenge*, 71-81.

<sup>89</sup> For a detailed examination of how the NEP was dismantled, and the importance of Pat Carney in ensuring its demise see, Tammy Nemeth, "Pat Carney and the Dismantling of the NEP," (M.A. Thesis, University of Alberta, 1997).

oil and gas. But, the world oil and gas market had changed remarkably since the first oil crisis. Conservation, increased fuel efficiency, and recession had decreased consumer demand considerably. In addition, the increase in world prices and the uncertainties of OPEC, had led to an increase in exploration and development in non-OPEC areas. By the mid-1980s, those new supplies began to enter the market. Instead of oil shortages, there were now surpluses; world oil prices began to decline appreciably, and the future of OPEC seemed to be in question. Now that the Canadian policy was not to hoard Canadian resources for Canadian use, a market would be needed, and the Conservatives looked south. But protectionism in the U.S. was on the rise, and many Americans still harboured some resentment and a great deal of mistrust towards Canada because of the policies of the 1970s and early 1980s.

The Reagan Administration disliked much of the protectionism and subscribed instead to the ideology that market forces should direct the economy, not the bureaucracy; less government would allow business to operate more efficiently and profitably. Burned by the previous Canadian actions, U.S. officials in the Reagan Administration wanted something more permanent than an informal understanding, or a sectoral agreement. This was also an opportunity for Reagan to fulfil his goal of a more united North America. The Conservatives also recalled the difficulties Canada had experienced under the informal continentalism of the 1960s, and did not want to be held hostage to potential American arbitrariness, and the caprices of Congress. A sectoral agreement was also ruled out because of the greater chance for either country to disregard it in a crisis: Informal continentalism was rejected by both sides.

Consequently, Canada and the U.S. sought to confirm their commitment to trade liberalisation, market prices, and deregulation of energy resources in the FTA.<sup>90</sup> The Mulroney

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<sup>90</sup>Bruce W. Wilkinson, "Trade Liberalization, the Market Ideology, and Morality: Have We a Sustainable System?" in Ricardo Grinspun and Maxwell A. Cameron eds., Political Economy of North American Free Trade

government, in a dramatic departure from traditional Canadian policy, sought to curtail future Canadian governments from developing any similar discriminatory policies in the future by formalising the deregulation and depoliticisation of energy. The method chosen was a continental energy arrangement embedded in the larger Canada-U.S. FTA. The significance is that this arrangement cannot be undone or dismantled without dissolving the entire agreement. An important factor in bringing the two countries together to even consider a possible comprehensive agreement, was the friendly personal respect and friendship between Mulroney and Reagan, augmented by the fact that Mulroney shared most of Reagan's economic views.<sup>91</sup> The ultimate decision to enter into a FTA was also aided by the re-establishment of transgovernmental networks of senior officials in Canada and the U.S. Ambassador Allan Gotlieb and Derek Burney, who worked tirelessly to improve and expand the lines of communication, headed the process on the Canadian side.<sup>92</sup> After two years of intense negotiations, a deal for the Canada-U.S. FTA, including a chapter on energy, was reached on 4 October 1987, finalised in 1988, and implemented in January 1989.

But how exactly do the FTA energy provisions secure deregulation and depoliticisation of the Canadian and American energy trade? Neither country can impose price controls on oil and natural gas, establish a two-tiered pricing system, or impose import or export charges, without levying the same amount on domestic consumers. [sec. 902/903] Both countries may

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(Montreal: McGill-Queen's University Press, 1993), 27. When referring to the ideology of trade liberalization and market integration in North America, Wilkinson states that the Canada-U.S. FTA "stress[es] the importance of market forces and market objectives in such an ideology."

<sup>91</sup> John Herd Thompson and Stephen J. Randall, Canada and the United States: Ambivalent Allies (Montreal: McGill-Queen's University Press, 1994), 274, 277.

<sup>92</sup> Allan Gotlieb, I'll Be With You in a Minute, Mr. Ambassador: The Education of a Canadian Diplomat in Washington (Toronto: University of Toronto Press, 1991). For information on Burney see, Jeffrey Simpson, Faultlines: Struggling for a Canadian Vision (Toronto: Harper-Collins, 1993), Chapter 1. For a detailed examination of the FTA negotiations see, Michael Hart, with Bill Dymond, and Colin Robertson, Decision at Midnight: Inside the Canada-U.S. Free-Trade Negotiations, (Vancouver: UBC Press, 1995).

continue to provide government incentives for oil and gas exploration and development, but investors must be treated fairly in both countries. [ch 16 sec 1602/1605,sec. 906] Investors are not to be constrained by such things as ownership requirements or having to purchase local goods and services while operating in the other country, which were required under the NEP. Furthermore, as a direct result of the NEP's twenty-five percent "back-in" with no compensation, articles 1602 and 1605 were created to ensure that American companies would be treated the same as Canadian companies, and would receive fair remuneration based on market value for any expropriated assets.<sup>93</sup> Both countries must discuss regulatory changes affecting the other country before being implemented. This is meant to discourage discriminatory regulations. A formal dispute settlement or grievance board was established in Article 905 to help alleviate complaints if one country feels that the other is violating the articles of the agreement. Canada gains access to Alaskan oil, which is forbidden from export to any other country. [Annex 902.5] Both countries limit the regulatory actions available to them through the proportional sharing arrangement so that neither country can arbitrarily cut off exports to the other country in a time of crisis or conservation. The reduction must maintain the same proportion of export to supply as averaged over the previous thirty-six months. Since Canada exports more oil and natural gas than it imports from the U.S., this provision is often considered to be more favourable for the U.S. than for Canada. [sec. 904]<sup>94</sup>

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<sup>93</sup>Government of Canada, Department of Foreign Affairs and International Trade, The Canada-U.S. Free Trade Agreement (Ottawa: Supply and Services, 1988), 233-237.

<sup>94</sup>Ibid., Chapter 9 Energy and Chapter 16 Trade and Investment. The energy chapter also recognizes other energy agreements or arrangements such as the IEA [sec.908], provides a clearer definition of national security [sec. 907], and establishes a formal dispute settlement or grievance board [sec.905]. Five years later when the North American Free Trade Agreement (NAFTA) was negotiated, the energy chapter of the FTA, as it applies to Canada and the U.S., was transplanted in toto to NAFTA under Chapter Six "Energy and Basic Petrochemicals." The text may be found at a number of different websites as well as in the library. For example, the Canadian Department of Foreign Affairs and International Trade has the full agreement on its website: [http://www.dfait-maeci.gc.ca/nafta\\_alena/agree\\_e.asp](http://www.dfait-maeci.gc.ca/nafta_alena/agree_e.asp) [last accessed 23 April 2004].

Debate surrounding the energy provisions in the FTA is usually centred upon the proportional sharing clause and the import and export pricing restrictions because they do limit Canada's policy options and sovereignty to some degree. Why would Canada agree to measures that compromised her independence? Energy crises are uncommon, whereas more general fluctuations in the market are more common. Policy-makers believed it was more prudent for Canada at this time to secure guaranteed access to the large American market even if it meant the remote possibility that Canada's sovereignty would be constrained in a time of crisis. Through their membership in the IEA, Canada and the United States are committed to share resources in a time of crisis. The inclusion of the proportional sharing clause confirms this obligation and further limits the potential regulatory actions available to both countries in a crisis. Canada's agreement to the energy provisions within the FTA can be interpreted as trying to guarantee the long-term economic stability of oil and natural gas exports to the large American market, while both sides would be constrained from imposing protectionist discriminatory taxes and regulations as they had often done in the past.

By 1984, both Canada and the U.S. believed that market rather than protectionist forces should prevail, and sought a comprehensive bilateral agreement to ensure that the deregulation of the oil and gas industry would be difficult to reverse. Even though both Canada and the U.S., by the time the FTA was being negotiated, had undertaken initiatives to deregulate their respective oil and gas policies, the energy chapter within the FTA served to ensure that discriminatory taxes and regulations could not be implemented by future governments, nor could energy be used as a bargaining lever for other trade disputes, without renegotiating or terminating the agreement.

Some might argue that the reason energy became depoliticised, and Canada-U.S. oil and gas relations improved, was because oil prices plummeted, therefore it was no longer an issue.

The test for this hypothesis is in the recent increases in oil and gas prices, and the attempt to link energy issues with difficulties in the lumber trade. The public has expressed concerns that maybe prices should be controlled, but there has been no talk from politicians about price controls or limiting oil imports at the expense of exports to the U.S., because those types of initiatives cannot be implemented. A few years ago there were calls in Canada to reduce oil exports to the U.S. if Americans restricted softwood lumber imports, this, however, was an idle threat tailored for an uninformed public that played well to anti-American sentiment.<sup>95</sup> The continental energy agreement enshrined in the FTA/NAFTA depoliticised bilateral energy issues by formalising the market imperative, and therefore their trade. Price controls and issue linkages can only be applied if the FTA/NAFTA is abrogated.

### **Conclusion**

Throughout the 1950s and into the early 1970s, America's priority was to ensure ready access to secure supplies of oil in case of an emergency, like a war. Canada's priority was to secure guaranteed access to the U.S. market for increased oil production that was surplus to Canadian use. The informal continentalism approach worked well at this time because there was a surplus of oil in the world market, and barriers to the U.S. market. Canada, through the personal relationship between Prime Minister Diefenbaker and President Eisenhower, and with the support of key officials like Livingston Merchant, secured an exemption to the restrictive American MOIP despite considerable opposition from officials within the State Department, and at the risk of jeopardising America's relationship with Venezuela. Then, in 1961, after much discussion and debate within Cabinet, Canada implemented its NOP that was designed around the MOIP exemption, and increased Canada-U.S. interdependence. Concerned about its

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<sup>95</sup>See for example, Peter O'Neil, "Energy and the Lumber Trade War," Vancouver Sun, 10 March 2001 and Edward Greenspon, "Chretien Serves Bush Medley of Hot Potatoes," Globe and Mail, 23 April 2001.

relationship with other oil exporting countries, however, the U.S. under President John F. Kennedy insisted on an informal understanding with Canada to prevent oil exports from becoming “unreasonable.” The agreed upon levels were negotiated on a fairly regular basis, and Canada was quite successful at exceeding the limits that American officials determined were reasonable. But, the poor personal relationship between Kennedy and Diefenbaker took its toll, and by early 1963 Kennedy was set to revoke Canada’s MOIP exemption just to spite Diefenbaker. This action was prevented by the election of Lester Pearson in the spring of 1963. Pearson and Kennedy had great respect for each other and enjoyed a very friendly rapport, thus Kennedy decided to maintain Canada’s exemption. After Kennedy died the relationship between Johnson and Pearson was mixed. LBJ removed oil from the White House and delegated responsibility to Secretary of the Interior Stewart Udall and Under-Secretary of State for Economic Affairs Thomas Mann. These two had different objectives with respect to Canada, with Udall supporting maintenance of the exemption, and Mann working to either remove it or get equal treatment for Venezuela. Udall succeeded in the end, but secured more formal restraints on Canadian imports. In 1964, anticipating the Merchant-Heeney report, Prime Minister Pearson and President Lyndon B. Johnson initiated technical level talks on a more formal continental energy agreement. Interest waned rather quickly, and was not rekindled until 1969.

Between 1963 and 1968, the tremendous efforts and strong personal links or networks between Canadian and American officials prevented the oil and gas difficulties from becoming major irritants. But in 1968, the large Alaskan oil field was discovered at Prudhoe Bay and was seen as a threat to Canada’s tenuous and continually contested access to the U.S. market. Therefore, overtures were made for consultations almost as soon as the Nixon cabinet had been

confirmed. Of interest is the fact that Canada, not the U.S., introduced the idea to begin discussions on a continental energy agreement during Prime Minister Trudeau's visit to Washington in March 1969. The two new administrations initially approached the idea of increased continental interdependence with great vigour, but almost as quickly the goal of a sectoral continental agreement in oil was beyond reach. The failure rested on Canada's refusal to meet American requests to make its East Coast more secure by building an oil pipeline to Montréal to utilise Canadian oil. At this point, imported oil was still cheaper than Canadian, though that began to change in 1972, and Trudeau would not permit a policy that unnecessarily increased prices to Québec and Ontario consumers.

Various Canadian and American governments had occasionally considered the idea of a continental energy policy, but it had never gained widespread acceptance within policy circles. This was particularly the case when the Trudeau Liberals were in power. The NEP was designed to curtail provincial and American control over the oil and gas industry and reduce reliance upon the American market by keeping Canada's oil and gas for Canada. The changes that took place in the Canada-U.S. oil and gas relationship between 1974 and 1984 were an attempt by Canada to extricate itself from the interdependence in the trade of oil and gas, and the informal continentalism that had been the mainstay of Canadian policy since the 1950s.

In the Trudeau era, energy was politicised not only because prices had skyrocketed, but also because it was at the centre of Trudeau's economic strategy. Trudeau wanted to *reduce* not increase Canadian oil and gas exports to the U.S., so that secondary manufacturing could be expanded. Concerned that the bureaucracy, mired in the certitude of informal continentalism, would impede his plans, Trudeau restructured the bureaucracy and the policy-making process. He used the PMO and the PCO to recruit people for government service and promote those who

were more in line with his way of thinking.<sup>96</sup> The cumulative effect of these personnel changes was that the ideological complexion of the federal government was gradually altered in order to reduce resistance to Trudeau's self-declared "leftist" policies.<sup>97</sup> These policies included the phasing out of oil exports, and the NEP. Both had profound effects on Canada-U.S. relations as they were intended not only to decouple Canada from the world oil market, by setting prices internally and being self-sufficient in oil, but also to decouple Canada from its interdependence with the U.S. in the oil and gas trade. Although the Ford administration's reaction to the phase-out of oil exports was relatively benign, the Reagan administration protested more strongly, yet quietly, the interventionist Canadian NEP.

Concurrent with Trudeau's bureaucratic restructuring, Nixon restructured the American bureaucracy, particularly the State Department. In both countries, the power and influence for foreign policy was shifted to the PMO and President's Executive office, and removed it from External Affairs and the State Department. The effect of these actions was that the informal transgovernmental networks that had worked so well in the 1950s and 1960s were eroded, which contributed to the increase in poor relations between the countries in the early 1980s.

When the Mulroney Conservatives took over the government in 1984 they decided to embark upon a path of improved federal-provincial relations and closer ties with the U.S. in the matter of energy policy. The Conservatives rejected economic nationalism, and subscribed instead to the view that market forces should be allowed to prevail with little government

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<sup>96</sup>An excellent discussion of the consolidation of power in the PMO/PCO during Trudeau's time in office can be found in Donald J. Savoie, Governing from the Centre (Toronto: University of Toronto Press, 1999) and <sup>96</sup>Colin Campbell and George Szablowski, The Superbureaucrats: Structure and Behaviour in Central Agencies (Toronto: Macmillan of Canada, 1979). In reflecting on the Trudeau years, one cabinet Minister thought that the "combined power of PMO and PCO had grown far beyond anything reasonable in a parliamentary democracy." (318) See also McCall-Newman, Grits, Parts 2, 3 and 5; and Clarkson and McCall, Trudeau and Our Times, Vol.2.

<sup>97</sup>Desveaux, Designing Bureaucracies, 67-73. Desveaux observes, "Austin, as deputy minister, was able to effect more change in both organizational [sic] structure and decision-making than his predecessor, Claude Isbister, because he had the ear of the prime minister."

intervention. Therefore, the NEP was dismantled. This, however, did not eliminate the possibility of future NEPs or discriminatory action. Representatives from both countries had bitter memories of the uncertainty and potential for caprice that had governed the relationship in the past. Rather than return to informal continentalism and the negotiation of either an understanding or a sectoral agreement on oil and gas trade, or adopt an economic nationalist approach, the Conservatives decided to take an even greater policy leap by including the energy chapter in the FTA.<sup>98</sup> The Reagan Administration welcomed the possibility of improving Canada-U.S. relations, and was open to the idea of a comprehensive free trade agreement. Reagan's personal relationship with Prime Minister Mulroney, and the improvement of transgovernmental networks guided by Allan Gotlieb and Derek Burney, helped to put free trade on the agenda and facilitate negotiations. Ultimately, in oil and gas issues, the personal relationships between Presidents and Prime Ministers, and the networks between key officials across the border, had the most profound effect on which approach was chosen when and why.

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<sup>98</sup>The energy provisions of the North American Free Trade Agreement are in Chapter 6.