

Indemnification and the Building of Canadian Pipelines

By Megan DeVries thesis submitted

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Abstract

The Canadian Federal Government's purchase of the Trans Mountain pipeline in 2018 was seen by many as a singular action to support the pipeline industry. However, this research will contend that this is not the case because this thesis will show that the federal government has indemnified the oil and gas pipeline industry in Canada over the past 60 years. This will be shown by focusing on three large-scale positive examples of Federal Government indemnification, they are the modern Trans Mountain pipeline expansion, the 1970's building of Line 9 and the initial construction of the TransCanada pipeline project in the 1950's. All of these cases relied on direct government fiscal and political support to indemnify the projects so that they could obtain financing and eventually be constructed. By using process tracing this thesis shows how the Canadian federal government has in essence been indemnifying all large-scale pipeline projects throughout a large part of Canada's history. Explanations for why this support has existed are then explored through a lens of industry structure, and the thesis posits that the pipeline industry's structure (using the metric of industry size, firm size, profit rate, market concentration and geographical dispersion) is one explanatory factor as to why this policy of indemnification has existed in Canada for such a long period of time.

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List of Abbreviations

NEB

National Energy Board

MSA

Master Service Agreements

Introduction

In June of 2019, Canadian Prime Minister Justin Trudeau announced that his Liberal government would be purchasing the Trans Mountain pipeline and then would spend billions more to build its proposed expansion. The project was purchased despite the fact that the pipeline had seen significant protests by environmental organizations, Indigenous groups, cities along the pipeline and the premier of the province of British Columbia. The acquisition was framed by the federal government as a short-term purchase agreement that was both financially sound, and essential to ensuring a key energy infrastructure project was built (Ljunggren and Williams 2019). This was stated despite the project proponent and previous owner Kinder Morgan had describing the pipeline as an “unquantifiable risk” when describing the outlook of the project (Kinder Morgan 2018). Additionally, the government has been labelled a ‘reluctant buyer’ of the pipeline by the media and other parties (Sanzillo and Hipple 2018, 3). Within this set of circumstances questions therefore arise about why the federal government would put forward so much money on an asset that does not clearly seem to be a business. This also brings forward the question of what sort of public case would there be for the federal government to take steps to save a pipeline they have stated to be so reluctant to purchase.

This thesis seeks to answer the question of whether the federal government has supported the oil and gas industry through indemnification since the 1950’s. Indemnification being defined as a government entity taking responsibility for the large-scale liabilities faced by an industry sector overtime. It further seeks to not just confirm whether this form of support is taking place but asks whether the industry structure of the pipeline industry could provide an explanation for why this policy has continued over

such a period of time. It is hypothesized that the structure of the oil and gas industry, when looking at the five parameters proposed by Salamon and Siegfried (1977), can help to explain why an interest group such as the pipeline industry has benefited from this type of support from the federal government of Canada. The research question is pertinent given the historical resistance on the part of many parties against supporting pipeline construction projects with public money, as well as the common perception within the oil industry that less government involvement is preferable to create the most efficient, profitable industry. This apparent contradiction, along with analysis of the common justification of governments that indemnification was in the “national interest” will allow for the questioning of motives, risk-calculation by interest groups and what actors (interest groups, government actors etc.) are involved in decision making when it comes to Canada’s national oil and gas pipeline policy.

The federal government’s decision to purchase the Trans Mountain pipeline has been painted as an unprecedented action on the part of the government by many politicians and journalists (Connolly and Ferreras 2019). While it is true that this case is the first time that the federal government has wholesale bought out a pipeline that has been approved by the National Energy Board (NEB), it is not the first time that the federal government has supported pipeline productions and been willing to back them up through large-scale financial means. In fact, this thesis will contend that the Canadian federal government has been financially and through regulatory means supporting all large-scale pipeline projects throughout most of Canada’s history. The federal government’s financial and regulatory support of pipelines is explained using the concept of indemnification, which is defined in this paper as a government entity taking

responsibility for the large-scale liabilities faced by an industry sector as a whole to ensure its continued survival as an industry despite any ongoing financial, regulatory and environmental issues in the sector that may make it seem non-viable within a jurisdiction or country. Indemnification therefore serves as a safety net for the industry sector being supported by having the government provide regulatory, financial and policy related help, regardless of the outcome of specific companies or projects for the benefit of the sector as a whole over time.

While literature in Canada in recent years has increasingly focused on pipeline projects, often research has been restricted to a particular project or government policy. The literature review will show that despite increasing interest by scholars in pipeline projects and infrastructure, research focusing on individual projects or environmental consequences of oil infrastructure does not look at systematic patterns in government policy and why they have continued over time. Instead by focusing on industry supply-side structure rather than just government policy or downstream effects, a better understanding of why and how the oil pipeline sector exists the way it does today can be determined. A small industry size, large firm size, high profit and market concentration by companies within an industry and a project that takes place in a concentrated geographical area can positively correlate to positive lobbying efforts and more government support of a particular industry. By looking at three cases, the Trans-Canada pipeline project of the 1950's, the Sarnia to Montreal pipeline in the 1970's (Line 9) and the Trans Mountain pipeline expansion project in our current day, this thesis will show how Canada's federal government has enacted a long running policy of indemnifying the pipeline industry. Using these three case studies, the paper will conduct an in-depth

analysis of an ongoing public policy that uses process tracing to examine the history of this public policy from the 1950's to present day regardless of changing corporate actors, political actors, differing political parties. As can be seen in Table 1.1, although some parameters do not fit exactly within the ideal, Salamon and Siegfried's explanatory framework for how specific industries gain the benefit and support of government's broadly matches the structure of the pipeline industry in Canada. While the industry sector model does not match up perfectly to all conditions for all of the case-studies the majority of indices matching up to show a higher probability of government support, some more (firm size, market concentration) more than others (industry size). When looked at in this way, an explanation can come forward to show why the government continued to support the pipeline industry over such a long period of time.

This type of government support continued over time despite the typically neoliberal view that corporations benefit from a separation from government policies to ensure that most efficient and profitable industries (Friedman 2013, 11). In doing so, the method of analysis used in this research can allow for greater understanding of how large-scale pipelines continue to be built with support from the federal government despite resistance from environmental groups, members of the public, Indigenous groups and in some case often reluctance on the part of the political parties in power to provide such a significant level of support.

In what follows, the introduction includes a literature explaining previous research on pipelines in Canada, indemnification, and government incentives. Next I will show and explain the theory to be used in the thesis. As well, a justification for why industry structure and economic power explains government support of the pipeline industry in

comparison to other alternative theories. Also included within this chapter is the method in which the research was conducted.

Table 1.1 Salamon and Siegfried’s applied industry structure compared to pipeline case studies

Industry structure indicators	Ideal structure for government support	Trans Canada	Line 9	Trans Mountain
Industry Size (relative to general economy of Canada at that time)	Small	Small	Medium	Medium
Firm Size	Large	Large	Large	Large
Profit Rate	High	Low	High	High
Market Concentration	High	Highly concentrated	Highly concentrated	Highly concentrated
Geographical Dispersion	Concentrated	Wide-ranging (across several provinces)	Concentrated (two provinces)	Concentrated (two provinces)

1.1 Literature Review

With the increase in controversial pipelines within Canada in the last few years, there has been a large increase in the amount of research available on not just the oil industry in Canada but also pipelines specifically. However, most pipeline research in Canada has been focused on the environmental or climate change impacts of pipelines (Gareau 2016; MacNeil and Paterson 2018; Carter 2018). Research has also been focused on mapping patterns of resistance to pipelines (Ilnyckyj 2017; Kilburn 1970). Veltmeyer and Bowles (2014) focus on extractive resistance to the Northern Gateway oil project arguing that the pipeline represents a form of neo-colonialism that sees Canada engaging in ‘extractivist imperialism’ against indigenous people. Research in this vein

concentrating on methods of resistance and impacts of pipelines focusing on indigenous people has been published on several pipelines such as those by Spice (2018) and Bradshaw (2015). Less scholarship can be found however on methods of support for pipeline construction. While studies looking at public support for pipeline development have occurred (Sherren et al 2019; McLean 2018), very little research has been conducted on direct government support for individual pipelines and why it exists. While scholars such as Walter (2019) have looked at if media coverage of oil pipelines affects government response, the focus on both Canadian and US cases does not examine financial policies on the part of the government in support of oil pipelines and instead focuses on the media's influence when it comes to government support of pipelines. The study's examination of pipelines on a case-by-case basis also extends only within the last ten years meaning that support cannot be traced under significantly different political, regulatory and economic conditions.

A historical approach can be helpful when looking at policies to answer the question of why support occurs not just on an individual basis but also over a long period of time. Harold Innis was one of the first to do this when studying natural resources in Canada in his work *The Fur Trade in Canada*, in this work he examined the fur trade overtime from an economic, social, transportation and political manner (1999, 4). A more recent example can be seen in Bernauer's examination on the mining and extractive industry in Nunavut and whether changes in the 1993 Nunavut Agreement facilitated changes overtime to present day to allow for greater Inuit control of natural resources (2019). Pierson and Skocpol note that taking a historical approach to political science questions can allow for the ability to address large substantive questions that are

“inherently of interest to broad publics as well as fellow scholars” (2003, 695). By taking time seriously they note that taking time seriously allows for the researcher to analyze macro contexts and hypothesize about the cumulative effect of processes and effects overtime, rather than just examine one phenomenon or process at one time (Ibid, 696). While this approach can be beneficial, it does create a large amount of data to examine which can generate a variety of explanation to explain the phenomenon being studied. For this reason, it is important to be specific about the type of occurrence and time being studied to ensure that the reasoning behind the conclusions of the researcher is clear.

Work on government support has examined the National Energy Board and government subsidies of the oil and gas industry over various period of time in Canadian history. Analysis has occurred on the assessment process for oil and gas pipelines (Van Hinte et al 2007), which while useful does not speak to government support for the pipeline industry overall, as it is focused mainly on indirect government support through National Energy Board procedures. As this thesis makes the argument that the federal government does not just support the pipeline industry indirectly through regulatory mechanisms, but directly using explicit financial support showcases a gap in the literature.

Investigation on the part of researchers has looked into a variety of methods of government support for the oil and gas industry. Sawyer and Stiebert (2010) looked at government support and subsidies to the oil sector at the time of publishing. They provide a very helpful overview of equity investment on the part of the federal government and how its ownership stake in projects such as the Canada Hibernia Holding Company reduces that risk exposure of oil companies in the event that they do not make a profit

(Sawyer and Stiebert 2010, 107). The authors looked at subsidies on both a federal and provincial level and did not separate out pipeline subsidies from the larger oil industry. Furthermore, since the study is based on a single year, conclusions about the rationale for long-term subsidies are not examined and large subsidy events such as one-time indemnification financial payments to pipeline projects are not discussed. Similarly, work conducted by Charles and Wooders (2011) and Merrill et al (2017) look at subsidies of governments in the oil and gas industry but focus on conventional oil subsidies in comparison with other sustainable energy resources. While these studies are helpful in looking at the overall scope of government support for this industry, analysis of specific instances of government indemnification in a definitive part of the oil and gas industry analysis can lead to study not just of subsidies that exist but the conditions that help precipitate them and would contribute to existing literature that currently exists examining government subsidies to this industry.

Hoberg's (2013) work looking at political risk analysis for governments approving modern pipeline proposals can provide an important primer to influences that can affect government support for pipeline projects. While the paper's focus on how institutional veto points and the geographical distribution of risks and benefits can be helpful when looking at government support, the paper is focused on government approval of pipelines, not direct support of pipelines by government entities. Instead, Hoberg's (2013) paper focuses more on the relative balance of pro- and anti-pipeline groups in different jurisdictions and how a number of criteria can change the political risk involved in approving pipeline projects. The paper also focuses on pipeline projects that at the time of publication were not approved by the National Energy Board or the federal government

and does not talk about examples of government risk when looking at past pipeline projects. For this reason, while it outlines many of the influences that affect government support of pipeline projects, the paper's focus on pipeline approvals leaves a gap regarding direct government support.

In addition, while some research has been conducted on government mechanisms or financial instruments used to support pipeline expansion for individual pipelines, little research has traced this support over an extended period of time. While researchers such as Kilbourne (1970) and Thorburn (1959) have traced the policy case for the Trans Canada Pipeline, these projects did not connect the policy case for one pipeline to another. Similarly, most writing on Prime Minister Pierre Trudeau's oil policies mentioning Line 9 are focused on federal provincial tensions (Hamilton and Kroning 1975), or the National Energy Program as a whole (McDougall 1982; Doern and Toner 2019). As the Trans Mountain pipeline has only recently been approved for purchase little peer-reviewed scholarship exists focusing on this policy decision specifically.

Much research has been conducted on the influence of business groups and industries on government policies. Work describing the manner in which firms influence government decision-making can be found not only within political science literature (Salamon and Siegfried 1977) but also within economics (Becker 1983) and management (Shleifer and Vishny 1994). While empirical studies into the relationship between industry structure and firm influence have yielded mixed results (Potters and Sloof 1996) many have found a positive correlation such as that by Salamon and Siegfried (1977) who found a positive relationship between industry concentration and company influence, and Lenway and Rehbein (1991) who found that larger firms may wield more influence than

small companies. Other such as Macher et al (2011) have looked at the country, industrial and firm characteristics that support the influence that companies have on government policies. While this multi-level approach is helpful, such a broad overview can speak about firms in general but lacks the details that a study on an industry in only one country could bring. For this reason a specified industry specific study into how government support for pipeline projects (and by extension pipeline companies) can be explained overtime would fill a gap in the literature both in regards to fiscal support of Canadian pipeline projects and if industry structure can be an explanatory framework when looking at a company's ability to influence government policy.

1.2 Theory

This thesis will show that the specific economic structure of the oil and gas pipeline industry enabled it to influence political action to the point in which Canada has had a more than 50-year history of indemnifying the industry. It is generally agreed upon that companies have the ability to influence governments in the countries in which they operate. However, tracing the characteristics and conditions for how and in what way influence on government policy occurs can be explained in many different ways. Olson (1965) noted that an increase in the number of firms in an industry might decrease the probability of individual members to secure the outcomes that are in the best interests of the industry. This he contended can lead to an increase in the free rider problem in which actors within an industry are less incentivized to work to influence government policy, leading to less lobbying and less favourable government policies in that industries favour. Furthermore, Olson (1965) and others (Wilson 1980; Harrison 2010) note that government policies that create concentrated benefits for specific industries will have

different political calculations for governments compared to spending programs that spread out costs to taxpayers much more broadly. With this in mind, it is key that a theory be used that provides an explanatory framework that has a reason for why government policies will benefit certain types of industries over others.

The theory of this thesis is based on the article, *Economic Power and Political Influence: The Impact of Industry Structure on Public Policy* by Lester M. Salamon and John J. Siegfried (1977). This article posits that not all corporate sectors and businesses are the same and as such, those with different economic structures will have different reaches in terms of the political influence that they have (Ibid, 1028). Salamon and Siegfried's study seeks to prove its hypothesis that changes in the economic structure affects corporate political power by looking at how these differences could account for differences in federal corporate income tax rates and state excise tax rates in the United States of America within the manufacturing and mining sectors. However, this hypothesis could presumably hold true when looking at explanations for how other types of companies and sectors of the economy can influence government actions in other ways in countries other than just the United States. Similar research can be seen in the work of Macher et al. which found that industries ability to affect government policies depends on industry characteristics such as the number of industry competitors, size and origin of companies (2011, 4).

Salamon and Siegfried posit that there are five facets contained within the economic structure that can be predictive of the political influence it has. These facets are the firm size, industry size, market concentration (defined as the proportion of an industry's sales or assets by its largest companies), profit rate and degree of geographical

dispersion. Salamon and Siegfried's article argues that the larger the size of the company the greater incentive they have to participate in politics (Ibid, 1031). This is due to both the larger amount of resources a larger company has, but also what they have to gain through reputation, which can gain them more access to the political system (Ibid). Macher et al (2011) additionally puts forward three reasons why larger firms may be more successful. The first is scale due to the fixed costs involved in procuring government influence, the second posits that larger companies have more to offer governments through votes, income or post-governmental employment and third "if lobbying represents a pure private good with no free rider problems, larger firms are likely to engage in more intense influence-seeking activities because productivity efforts are likely to be higher." (Ibid, 4). Pipelines in particular seem to be a good focus of government resources in that they allow for both direct extraction of resources and the creation of secondary industries such as refineries or manufacturing within a country, which if supported by the government would benefit from this specialized support.

Industry size on the other hand, is found by Salamon and Siegfried to work in the opposite manner to that of company size. Larger industries are often less successful, as the increased number of actors advocating for the industry can lead to less incentive to act (with the hypothesis that someone else will in their stead). Market concentration can be both a predictor of profits with the higher the concentration in an industry typically the higher the profits, but it can also lead to less of a free rider phenomenon. This is because the incentive for companies with larger market concentrations is to be directly involved in influencing political decisions since they have more to lose should decisions not go in specific directions (Salamon and Siegfried 1977, 1032). Profit rate is a factor chosen not

just because highly profitable companies can be benefited or harmed by political decisions to a greater degree, and the ability they have to institute the resources needed to influence the political sphere. The paper does disprove its own hypothesis of companies with beneficial concentrated market structures and profitability being able to influence certain types of political decisions when it comes to attempts to influence tax structures (Ibid, 1040). However, the choices of particular firms to not lobby against certain tax increases could be seen as either a product of their ineffectiveness or a strategic choice on their part in light of larger industry conditions (Ibid, 1042). For this reason, they will still be tested to see if they can be seen as explanatory factors for government support of pipelines.

Geographical dispersion is the final facet that is deemed to be important, with both companies and industries that are more geographically concentrated generally being more successful in influencing political decisions compared to those that are spread out over a wide area. This is primarily due to the way in which industries concentrated in areas have the ability to advocate not just on a federal level but can make large impacts on local representative members and the communities in which they are elected. Geographical dispersion is useful not only as a measure of potential influence companies can have but can also be seen as a metric of potential political risk. Pipelines could be an excellent example of this, as they often have the potential to be supported within geographically concentrated areas and depending on their size can physically impact multiple geographical regions which impacts a wider range of populations who could potentially be against expansion in a certain area, jeopardizing the entire length of the pipeline (Hoberg 2013).

The theory put forward by Salamon and Siegfried has been used extensively to study the relationship between corporate lobbying and tax strategies such as in the case of Richter, Samphantharak and Timmons (2009) and Riedel and Simmler (2018). It has also been used to study the connection between taxation and industry structure in the Canadian manufacturing industry (Blais and Vaillancourt 1988). Blais and Vaillancourt do show that certain determinants are significant when studied in the Canadian context, however their emphasis on tax policy as well as its dated nature make utilizing the theory over a wider time period and within a more specific industry helpful. Using the theory in this way could prove useful in explaining past government policy and as a framework to create policy moving forward.

Salamon and Siegfried's theory has also been used to explain how certain industries such as the chemical industry seek to avoid government regulations and sanctions (King and Lenox 2000) or how the steel industry lobby's for trade protections (Schuler 1996). This theory was used to analyze electricity infrastructure development (Henisz and Zelner 2006) which while similar in that both the electricity and oil and gas pipeline sector involve large scale infrastructure projects, their industry structure can differ significantly. This is notable considering the study looked at 78 countries from 1970-94. While both the scope and method of analysis in this study differs greatly from this thesis, it does show that this theory can be used both to analyze the resource sector as well as industries involved in large scale infrastructure projects that are often considered essential or in the national interest. Expanding the type of industry and time frame of study can help to pinpoint important indices of industry structure in a country context not as often studied using this theory as most analysis focuses on the United States.

The theory has also been used to analyze the oil crisis of the late 1970's to examine the impact of public opinion and media attention can influence government action on regulatory threats towards the oil industry (Erfle, McMillan and Grofman 1990). The study found that large, visible firms restrained increases in oil prices for the most important products when media coverage of the oil industry was extensive, but firms raised prices when the government was busy with other issues or there was external international rational for price increases (Ibid, 60). While Erfle et al's paper focuses more on the role of regulatory threat as opposed to the power of firms, there are parallels that point towards why using the Salamon and Siegfried's theory can be helpful when looking at other aspects of the oil and gas industry. Both pipelines and the price of oil have in some cases led to significant public opinion that in some case has led to different outcomes for more visible companies verses those that were not in the public eye. Using this method of analysis for oil and gas pipelines in Canada can help to explain constant policy actions on part of the government while contributing evidence in support of how industry structure can be predictive of its influence on government actions in another industry and over a significantly larger period of time.

There are a number of reasons that Salamon and Siegfried's theory was chosen in comparison to other alternative theories. The theory recognizes the differing political power that exists not just between political and non-political actors, but also by actors within different sectors. Their conclusion that "larger firm size does indeed seem to yield greater political power" (Salamon and Siegfried 1977, 1033) recognizes the potential power within large concentrated industries and provides an explanation for why the Canadian government would go to such lengths to safeguard one particular industry. This

type of interest group model additionally recognizes that different groups will have differing levels of influence that can lead to policy outcomes favouring one group over the other. The recognition of economic power and how it can influence and be interlinked with state power is particularly important to many scholars (Nigam 1996, 7). The importance of economic powers and market forces has only increased with the continued capitalisation of society (Kujipers 2013, 15). Within this study the intertwining of economic and political power is key to note because despite neoliberal assertions of the need for separation between capital and the state this is not what occurs in practice (McCarthy and Prudham 2004, 276). Instead corporations often see politics as a competition of interests in order to maximize profit to the amount they are able (Kuhner 2007, 2365). Companies seeking indemnification are therefore in sharp contrast to the often-asserted neoliberal pro-market insistence against state interference in favour of deregulation, marketization and privatization (Peck 2001). This theory provides an explanatory framework as to how the oil and gas pipeline industry in particular was able to secure such high level of government support across party lines.

The theory used can be contrasted with other theories that could possibly be used such as the Staples Trap (Innis 1999). While Staples Theory provides a good explanation of Canada's reliance overall on the oil industry in particular is more difficult to fit into just the pipeline sector of oil and gas. This is both due to the fact that some scholars have suggested that Canada has reduced its staples bias in the time since World War II (Stanford 2008, 8) in contrast to the government's steady support of the pipeline sector. Additionally, the more nationalist attempts by the Trudeau government in the 1970's stand in contrast to the emphasis on international export evident put forward to support

the Trans Mountain in the present day, as do the amounts of foreign direct investment present during the time period studied that are so important to staples theorists (Haley 2011, 10). While it may be true that Canada is uniquely dependent on resource extraction and export and staples theory can provide an explanation for Canada's reliance on extractive industries (Fast 2014, 33), it is less helpful in explaining the direct mechanisms that led to such wide-scale indemnification of the pipeline industry. Using an argument based on the difference between industry sectors allows for recognition of the differences between different resource industries and the way in which this then affects the oil and gas pipeline industry.

The use of Salamon and Siegfried's (1977) theory provides a reason for why government policies will benefit certain types of industries over others. The different industry structures of different sectors will impact their ability to gain government support. The five facets outlined by Salamon and Siegfried (firm size, industry size, market concentration, profit rate and degree of geographical dispersion) have been studied in the context of corporate lobbying and tax strategies, manufacturing and how certain industries seek to avoid government regulations and sanctions (King and Lenox, 2000). While it has been used when looking at the influence of government action on regulatory threats toward the oil industry (Erfle, McMilland and Grofman 1990) it has not been used in the context of pipeline research before. The theory was chosen because it has the ability to showcase power between political and non-political actors and actors within different sectors and provides an explanatory theory for government support in a small concentrated industry such as the oil and gas pipeline sector. As can be seen within the three case studies chosen, the Trans Canada, Line 9 and Trans Mountain pipelines

provide an example of how a smaller industry size, large firm size and highly concentrated pipeline industry at the time helped the companies overseeing pipeline construction at each time to secure government support for their projects. Although the geographical dispersion for the Trans Canada was wide-ranging instead of concentrating and their profit rate was low this can be mostly explained by the conditions of the industry in the 1950's in which almost no pipeline industry had a large profit rate. This thesis will in the forthcoming chapters will explore in more detail how a theory such as Salamon and Siegfried's (1977) can explain the Canadian federal government's level of support for the oil and gas pipeline industry in each case study.

1.3 Method

This study uses a qualitative case-based method to test its hypothesis. A combination of cross-case comparisons and within-case analysis was used to first prove that cases both represented instances of indemnification and that causal factors could fit into the wider theory of how the policy continued overtime¹. This was done through process tracing as when studying historical instances, it can be particularly helpful in finding similarities through multiple cases (George et al 2005, 203). In the words of Jack Goldstone,

To identify the process, one must ... figure out which aspects of the initial conditions observed, in conjunction with which simple principles of the many that may be at work, would have combined to generate the observed sequence of events (1991, 50).

¹ Alternatively, this was also where if causal factors within a case study did not fit the larger narrative, analysis was done as to why this may have occurred.

This thesis seeks to do just that and highlight first cases of government direct fiscal support of pipelines as well as what conditions are common for the cases studied. The following section will explain the rationale for taking a case study approach, case study selection, as well as how and with what materials research was conducted.

While Salamon and Siegfried (1977) set out to prove their hypothesis using cross-sectional data and regression techniques, the use of case studies to test this theory in the case of the study of pipelines in Canada was chosen instead for a few reasons. Salamon and Siegfried note that case study material can provide critical insights that can form the bedrock for future hypothesis that can then be tested on a more empirical level (1977, 1028). The use of a case study approach that focuses not just pipelines approved within Canada, but instead is focused on instances in which pipelines in Canada have been fiscally indemnified by the Canadian government. This approach was taken because while the paper argues that the act of indemnification by a government provides cover for oil and gas pipeline companies to develop all pipeline projects whether they experience issues or not, this is hard to quantify from a research perspective.² The amount of pipelines present in Canada is relatively small compared to other countries and therefore the instances of pipelines gaining fiscal government support are also infrequent. Harding et al., note that using quantitative methods when studying rare events can make it difficult to gather data on a sample of events leading to further issues when trying to determine commonalities, differences and causal factors (2002, 176). Instead they state that using a

² This may be an avenue for future research as alternative methods of research such as interviews with government and business officials on pipelines not supported financially. While this may be a current limitation of this study given time and length constraints it was not feasible within the scope of this project.

qualitative case study approach can be helpful for political scientists and political sociologists. Additionally, given that some uncontroversial pipelines were approved in many cases without elected officials or businesses speaking extensively in public on the issue, it provides less publicly available evidence for how indemnification is taking place. Instead, by focusing on controversial pipelines that were nonetheless supported by the government, evidence can be seen of how indemnification of the whole industry works. By using case studies, the case for how and why the federal government indemnifies the Canadian pipeline industry can be made across factors such as government in power, time and surrounding economic circumstances.

While studying all pipelines might provide better evidence to support this thesis, given the scope, length of study and need for detailed analysis of each case study it is not feasible to do the study on this level. Nonetheless, despite not using an empirical approach, this thesis will still seek to test the theories brought forward by Salamon and Siegfried on a case by case basis to determine if they can help explain the indemnification of the oil and gas pipeline industry. By using the five criteria of measurement put forward (firm size, industry size, market concentration, profit rate and degree of geographical dispersion) comparisons can be made based on the individual case studies presented. Additionally, conclusions can be reached about whether these indices are predictors of government indemnification of the oil and gas pipeline industry overtime.

These three case studies were chosen due to a number of factors. An inductive approach was used to find case studies that spanned a period of time, displayed indemnification actions by the federal government and pipelines that experienced some difficulty in their implementation. This could then lead to questions regarding why the

federal government would support pipelines through these challenges. While the first pipeline was built in Canada in the 1860's until nearly a century later in the 1950's only three major pipeline routes were built. These projects were of a much smaller scale than those built after the 1950's and the discovery of oil and natural gas reserves in Alberta. The discovery of oil at the Leduc No. 1 oil field in the late 1940's heralded the modern pipeline industry and the time in which oil became a much larger industry in the Canadian economy. It is this period of time from 1950 to present day that this thesis will focus on as before World War II the oil and gas pipeline industry differed drastically from today's.

The first case studied within this thesis focuses on the building of the Trans Canada pipeline in the 1950's. It represents one of the first large actions on the part of the federal government to build a large segment of pipeline with public funds when the financial ability of the company building it (Trans-Canada Pipelines Ltd) seemed near collapse (Bothwell and Kilbourn 1979, 295). The \$115 million dollars pledged represented a large controversy at the time for the ruling Liberal government, who despite being painted as supporting US oil tycoons over Canadian interests continued to push for government support of the pipeline. The second case chosen looks at the expansion of the Interprovincial Pipe Line from Sarnia to Montreal (also called Line 9) in the mid-1970's. This expansion showcases significant federal government support in the amount of almost \$250 million for the pipeline despite changing international oil markets and differing government objective from those expounded in the 1950's.

While many recent pipeline projects have been proposed in recent years, they were not suitable as a third case study for a variety of reasons. The Mackenzie Gas project was not chosen as the company building the pipeline (Imperial Oil) with drew

plans for the pipeline on the grounds that it was not fiscally feasible given the demand for oil both in the 1970's and throughout the 2010's when the plan was revived. The Keystone XL (TransCanada) was rejected by the Obama administration in 2015 and then subsequently approved by President Trump when he came into office. Similarly, Enbridge's Line 3 Replacement Project has been largely completed in Canada and faced its significant delays in on the US side. As these pipelines faced delays due to issues on the US side on issues outside of the Canadian governments control, they do not provide a good opportunity to study how the Canadian government indemnifies pipelines. In contrast, Northern Gateway (Enbridge) was a solely within Canada pipeline proposal similar to Trans Mountain. Both served as a gateway for land locked oil in Alberta to Canada's west coast through BC in order to access international oil markets. However, given capacity concerns, the controversial nature of Northern Gateway and the Federal Court's overturning of the previous government's approval of the project because Ottawa had not adequately consulted First Nations along the project's route (The Canadian Press 2018). The Energy East pipeline, which sought to bring Alberta oil to the east coast of Canada for export, is an infrastructure project that when abandoned can be argued to put more pressure on the federal government to ensure the industry as a whole had access to international markets leading to the support of the expansion of the Trans Mountain pipeline. For these reasons Trans Mountain was chosen as the third case study as it showcases the way in which the federal government indemnifies the oil and gas pipeline industry (but not necessarily every project proposed). The federal government's decision to purchase the Trans Mountain pipeline for \$4.5 billion represents the largest monetary

amount on the part of the federal government despite significant public protest on the part of some parties.

These case studies were analyzed through the use of government, media and other types of document analysis, historical analysis of the time as well as other secondary sources such as academic articles. This method was chosen to ensure consistency of analysis across the large time span of the three case studies selected. While methods such as interviews were considered given that those involved in the Trans Mountain pipeline may be unable to disclose information on an ongoing project, and those involved in the Trans-Canada pipeline in the 1950's might not be alive.

Data was collected using both primary and secondary sources. Particular interest was focused on newspaper articles, NEB reports, press releases and communications materials of oil and gas pipeline companies and government documents. Newspaper articles were gathered using the aggregate news databases Factiva, the Toronto Star historical archive and modern Canadian internet newspaper sites. Documents were gathered from the Glenbow Archives, Library and Archives Canada and internet archives. Additionally, non-governmental organizations and think tank reports were consulted as well as academic articles.

1.4 Conclusion

Barry Ritholz in his book *Bailout Nation* writes “any system that allows profits to be kept by a select few but expects the loss to be borne by the public is neither capitalism nor socialism: It is the worst of both worlds.” (2009, 4) This thesis will seek to argue that Canada's system of indemnifying oil and gas pipeline companies represents the worst of both worlds. The Canadian government (and by extension its citizens) hold all of the risk

of losses while oil and gas corporations only stand to gain the profits. By looking at these three case studies spanning from the 1950's to present day, the federal government's long-term policy of indemnifying the oil and gas pipeline industry can be seen. Analyzing these cases through an explanatory framework of industry structure can seek to provide causal explanations for why an indemnification project has persisted in Canada. It can also question if this is a policy that should continue in the future or if alternatives should be considered in its place.

Following the introductory chapter, a chapter on indemnification follows. This chapter outlines the definition of indemnification, indemnification in a business and government context, as well as how the term is used within this research. The next three chapters individually examine each case study chosen. They provide historical analysis for how government actors overtly acted to indemnify specific pipeline projects as well as examine the industry structure and actors of the oil and gas pipeline industry to show how this created the continued conditions for a policy of indemnification by the federal government. This is followed by a conclusion that questions the current state of indemnification of the oil and gas industry by the federal government and discusses the long-term costs of this policy beyond the initial money offered by the government.

Indemnification

Indemnification clauses are used by businesses, organizations, and governments to protect against losses should the specifications within contracts fail to come to pass. They can serve as a sort of stopgap, preventing specific parties from being held liable for their own actions in the event of mistakes or contract issues (Johnston 1978, 1993).

Traditionally indemnification clauses are discussed within business circles to describe specific prescribed formal proceedings overseen by signed contracts and lawyers. While this thesis is not arguing that the Canadian federal government has signed formal agreements agreeing to indemnify the oil and gas pipeline projects and companies, it is arguing that the government's actions regarding pipeline projects in Canada have essentially functioned as if they were the indemnitor for the industry. Governments have supported a variety of industries either directly or indirectly throughout Canadian history (Klein and Le Roy 2010, 237). Because government policies supporting the pipeline industry has occurred systematically over a long period of time, business and industry professionals can use their knowledge of the federal government's willingness to indemnify the industry as a type of risk management calculation that can be counted on in the event that their project encounters significant problems. In this way, although indemnification is traditionally thought of as a clear and equal apolitical partnership between two parties, when looking at indemnification as a concept and examining the oil and gas pipeline industry, the Canadian government seems to have agreed to support the industry without thought to the costs in the future. This then leads to power imbalances when issues with pipelines arise, often leading to the federal government drafting policies that cater not just to the industry but to specific pipeline projects.

Before going into greater detail regarding this however, it is important to define the difference between what would be termed as government support (or subsidy) and what this paper is calling government indemnification of an industry. Without this distinction it would be easy to say that the government indemnifies all industries, thus making the term overly broad. Indemnification in this thesis will be defined as the government taking responsibility for the large-scale liabilities faced by the industry to ensure its continued survival despite the fact that it has encountered significant ongoing issues. Action by the government is therefore taken not just to support a part of a project or company within a sector (often known as a subsidy), but the whole sector itself. Indemnification under this definition is also different from so-called government bailouts. Bailouts can be defined as financial help to an entity that would otherwise be on the edge of failure or bankruptcy most likely as a result of immediate emergency measures (Block 2010, 160). While indemnification of an industry can lead to bailouts of specific projects or sectors, it also serves as a guarantee regardless of the outcome of the project, thus differentiating the two. Additionally, while sectors can lobby for government bailouts, they usually occur infrequently and are lobbied for without the expectation of continued ongoing support of the sector. In using this definition, the chapter will also argue that the indemnification relationship between government and industry is not one of equals, but instead one in which the oil industry holds significantly more power. This will be examined by first discussing what indemnification is, indemnification in the oil and gas industry, the manner in which the Canadian government acts as an indemnitor in a variety of sectors. The chapter will then discuss how this thesis will define indemnification to be

used in relation to the three case studies chosen relating to the Canadian oil and gas pipeline industry.

2.1 Broad Definition

An indemnity is defined by David Newsome Jr as an action that takes place when a party agrees to cover another party's losses to a third party (2012, 42). A simpler way to state this is that indemnification clauses are "the primary place in the contract where the parties hash out who will bear the risk if something goes wrong" or the promise by one entity to take on the other entity's risk in the event of future damages (Izzo 2013,76). In this way, a common indemnification agreement places the responsibility of loss or damage on the party who controls the work (Newsome 2012, 42). Indemnification is therefore a technique or tool used to minimize the risks of a project by making another organization responsible for those calculated risks within the project that they are in charge of or contracted to complete (Voigtmann and Clifford 2018, 10). A common example of the use of an indemnification clause is within the construction industry and can help visualize what indemnification means in a non-abstract manner. Say for example that a contractor signs a contract with a homeowner to redo their house. It is a large project and so to ensure people with specialized knowledge, the contractor gets a different company to build the roof of the house, making a roof building company a subcontractor within the project. An indemnification clause signed between the contractor and subcontractor would ensure for example that a subcontractor working on a homeowner's property would not hold the owner or contractor responsible for damages that may result because of the subcontractor's inability to complete the tasks outlined within the contracts signed by all parties involved in construction. In plainer language, if a subcontractor is

contracted to replace a roof and as a result of the poor work of the subcontractor the roof leaks, theoretically the homeowner and the original contracted company would not be responsible for the cost of fixing the roof and any damages caused to the home due to the leaking roof because they have the protection of an indemnification agreement. Instead, the costs associated with the failure to complete the contract as stated would fall to the subcontractor. By signing agreements such as this, the risk that the contracting company would have to pay the homeowner if mistakes are made decreases significantly and for this reason they are used frequently for many types of business and construction type agreements. This is a simple example of an indemnification agreement, but these types of agreements can become much more complex depending on a number of factors that will be discussed in the following paragraphs.

Table 2.1 Types of Indemnification agreements and United States (US) and Canadian government regulations surrounding these types of agreements

Type of Indemnification Agreement	Fault-based Agreements			Knock-for Knock
	Limited	Intermediate	Broad	
Damage covered	Only covers damage caused directly by indemnitor	Indemnitor responsible for own negligence and the partial negligence of other parties	Indemnitor assumes entire risk for issues, damages or loss on a project	Both parties agree to take complete responsibility for injury or damage claims on projects
Government regulations on agreements	Most agreements valid in Canada and US	Most agreements valid in Canada and US	Not prohibited under Canadian regulations but not valid by most states in US	Barred in certain US states (Louisiana) but have been upheld in Canadian courts
Industries indemnification type found in	Employee use cases, rental car companies	Rental property companies, construction, manufacturing	Infrastructure and construction projects	Oil and gas

Critically, it is key to note that just because one party is responsible for negligence, it does not guarantee that they will not be held financially responsible under indemnification agreements (Kangles et al. 2011, 341). Who is held responsible will depend on the type of indemnification agreement parties have agreed to. While there are many different types of indemnification agreements, they generally fall into three broad categories. These categories are limited, intermediate and broad and can be seen in Table 2.1. A limited indemnity clause only covers damages for the indemnitee that are directly the fault of the indemnitor (Newsome 2012, 43). On the other hand, intermediate indemnity makes the indemnitor answerable for their own negligence as well as the partial negligence of the indemnitee (creating more protection for this party) (Ibid). Broad

indemnification goes to a more extreme level of coverage for the indemnitee. In this type of indemnity, the indemnitor assumes the entire risk of issues/damages/loss surrounding the project (Ibid). This means that the indemnitor must cover losses including those that are singularly caused by the fault of the indemnitee. Despite these different types of indemnification, it is key to note that governments in specific states and provinces do regulate the type of indemnification clauses that can be implemented between parties (Ibid, 44). These regulations are often put in place to ensure that larger companies that subcontract work cannot simply push all risk for projects onto subcontractors despite their own neglect (Ibid, 45). Regulations such as these are particularly prevalent within the United States, where in most states broad indemnification agreements are not seen as valid by most courts (Ibid). In Canada however, broad-type indemnification clauses are not prohibited by any type of legislation, leading to greater risk for certain parties that enter into this type of contract (Rylands 2015, 10).

It is notable that indemnification is largely about risk management on the part of one party within the contract when examined within business and legal scholarship circles. By identifying, analyzing and through clauses minimizing risks (commonly through transfer of risk to make other parties responsible for said risk) any company that uses these clauses stands to gain from the success of a venture while also minimizing their potential liabilities (Newsome 2012, 43). It has been argued by those who write about indemnification in legal scholarship that indemnification agreements can create mutually beneficial conditions in which the purchase redundant insurance coverage can be avoided and there is a decreased litigation that occurs as a result of both parties understanding their respective risk exposure (Kangles et al. 2011, 347). Under optimal

conditions, the type of indemnification clause chosen in an agreement is described as having the ability to create a fair allocation of risks between both entities. This is done so risks are held by the party best able to alleviate or prevent the risks from occurring (Izzo, 2013, 76). For example, a subcontractor for the roof would be responsible for liabilities related to the roof but would bear no responsibility for issues related to other areas of a home such as the foundation. While this type of indemnification may represent the ideal, it is however not always the reality. In fact, it is more likely that allocation of risks present in indemnification agreements often reflect the relative bargaining power of the entities within the agreement rather than an impartial designation of risks due to the roles of the parties within a project (Ibid). This is often simply because the party with more leveraging power (often the bigger entity or general contractor for a project) has the ability to seek new parties in the event that the weaker party does not agree to conditions they have set out (Newsome 2012, 45). If the weaker party refuses the conditions set out, they risk losing out on a job and then have no role in the project going forward. While this is acknowledged as something that can occur within legal literature, the underlying policy, regulatory and political consequences of this type of system is rarely discussed within literature discussing indemnification agreements.

Within the business world, indemnification clauses are often dealt with by the indemnitor by taking out insurance policies, as the assumed risk of potentially paying for catastrophic issues related to the project could cripple them (Ibid, 44). In fact, regardless of the type of indemnity clause included in the contract, all parties involved with the project (in the case of our example the contractor, subcontractor and homeowner) would all take out insurance to ensure that should any issues occur on a project would be

covered as much as possible despite the indemnification clause and might be required within any contract to do so by government regulations (Izzo 2013, 77). This ensures that the parties assuming liability in the project have the ability to cover that liability in the event of a needed payout. Without these assurances, companies could agree to take on large amounts of risk and then fail to pay in the event of their need to be activated. When looking at indemnification as a concept between the pipeline industry and the government however, the federal government often acts not just as the indemnifying party but also as its own insurance company. This can cause the government to pay out of its own consolidated revenue fund or take on debt to support specific pipeline projects. Therefore while both insurance and indemnification clauses serve as a way of allocating risk associated with a project for the parties involved, the amount of risk each party takes on and the consequences of those risks can have larger consequences from a political perspective for governments than companies (Mercier, Kane, and Nammour 2015, 266). This action calls into question whether “risk management” on the part of parties are not simply dry mathematical calculations as they are often portrayed but instead are actions of power made between often unequal parties. This is exactly what a political economy approach to indemnification literature can bring to scholarship in contrast to business and legal scholarship which many times focuses on working within the existing structures rather than examining or questioning the structures themselves. The ways that these indemnification clauses are constructed and used can vary from industry to industry, and consequently given the topic of this essay it is useful to understand how the oil and gas industry has generally utilized indemnification clauses to show how what we are calling indemnification differs from what is standard in the industry. This will enable further

comparison between their formal use and the informal manner they are currently being used within the oil and gas pipeline industry.

2.2 Indemnification in the Oil and Gas Industry

Indemnification agreements/clauses have been used within the oil and gas industry for quite some time. They are most often present within the specific contracting of a project between two entities, be it for the building a single oil well, or within the context of a large project financed LNG or pipeline venture (Rylands 2015, 10). Most often indemnification agreements in this sector occur between those that explore and produce oil and gas (known as the Operators) and companies that provide services to support and facilitate exploration and development activities (known as the Contactors) (Mercier, Kane, and Nammour 2015, 246).

The oil and gas sector is generally characterized as an expensive, risky, initially capital-intensive industry, often indemnification agreements are used to reduce risk and litigation costs in the event damages are incurred (Evans and Butler 2010, 226). In this way, indemnification agreements have been proposed as a tool to encourage compromise and alliance between parties involved within a project and as a tool to ensure that all parties acquire adequate insurance coverage for oil and gas projects (Talbit and Piziak 2013, 6). Additionally, in the event of claims that occur outside of those involved in the project, an indemnification clause provides a way forward for parties involved to defend themselves against those potential future claims (Ibid, 8).

This can particularly be seen in the popularity of reciprocal indemnification agreements within the industry. These so called ‘knock for knock’ agreements, as seen in Table 2.1, ensure that because both parties agree to take complete responsibility for all

injury and damage claims made by its employees no matter which party was at fault the relationship between parties working together can focus on the overall safety of employees rather than the liability in the event of injury (Evans and Butler 2010, 227). These agreements also reduce litigation costs, as there is less incentive for either party to go to court and have the potential to create intangible benefits for companies such as better cooperation and the ability to present a united front in the event of issues that develop with parties outside of the reciprocal indemnification agreement (Ibid, 229). Knock for knocks are however not a guarantee of decided liability, and have been struck down as in the case of the Louisiana Oilfield Anti-Indemnity Act, which while allowing for reciprocal indemnity agreements to do with property damage, makes illegal agreements involving the death or bodily injury of persons (Ibid, 230). In many cases within the United States indemnification for an indemnitee's own negligence is barred under legislation such as the Louisiana example previously discussed (Kangles, Rogers and Harris 2011, 342). Litigation regarding knock for knock indemnification can also be seen in the Canadian context, but with opposing results. In one particular example the Alberta Courts in *Precision Drilling Canada Limited Partnership v Yangarra Resources*, 2015 ABQB 433 upheld a knock-for-knock agreement leading to millions of dollars for the operator despite them not being directly at fault (Rylands 2015, 9). The wording of this agreement had that required the cost of repairing or redrilling a lost or damaged well regardless of the fault of contractor's negligence or fault. This then led to one party bearing the cost of the negligence despite the fact that it was the fault of the other party (Ibid). Thus the wording of these contracts can be of great importance in the event of liability issues, as initially small mistakes in oil and gas development can result in

significant cost burdens regardless of the use of knock for knock agreements to prevent such occurrences.

While knock for knock agreements are present within the industry, most of the oil and gas industry internationally and within Canada is governed by standard form contracts that include a variety indemnification options for parties to agree to (Mercier, Kane and Nammour 2014, 247). In Canada the most common types of indemnification agreements are knock for knock, fault-based regimes and hybrids of these two types of agreements for different components of a single project (Ibid, 251). Fault-based regimes simply agree that under specific terms one party will indemnify the other party based on who is in error and have been described above and can be seen in Table 2.1. Companies also at times use pre-written standard agreements are often called master services agreements or MSAs when drafting indemnification contracts of all types. These standard contracts are most often used to save parties time and transaction costs. They also theoretically ensure that all parties are familiar with the language of the contract (Rylands 2015, 9).

Whether utilizing any of the three systems described above, the Canadian courts have upheld the view that under the Canadian common law system liability has historically and still is currently allocated based on causation and fault. Because of this, most commercial agreements are drafted with these principles in mind (Kangles et al. 2011, 355). Therefore, courts often see indemnification agreements in this light as with the *Precision v Yangarra* case, in which the court noted that both parties were sophisticated commercial entities with equal bargaining power to fully understand a contract based on allocation of risks in the event of fault. In doing so, the court therefore

upheld not just the knock-for knock agreement but stated that such standard type agreements should be allowed to continue and do not present a public policy problem in which negligence is encouraged (Rylands 2015, 10). They did however state that, “the indemnity clause would only be unenforceable in circumstances in which intentional harm was inflicted.” (Ibid 15) Despite the presence of some case law on indemnification agreements in Canada, due to the number of MSAs that exist there are very few cases to point out potential pitfalls or court opinions on these agreements (Mercier, Kane, and Nammour 2015, 278). This is primarily thought to be because of the high cost of court litigation, which presents a deterrent towards bringing disagreements to court. Instead disagreements about the interpretation of indemnification agreements are instead solved through commercial solutions (Ibid).

The use of MSAs often are used as a starting point between parties, with the understanding that modifications will be made to address special circumstances and atypical environmental issues that may occur (Ibid). It is notable that contracts do not have to be standard and can also occur between the parties themselves or also be negotiated by parties such as the Canadian Association of Oilwell Drilling Contractors and the Canadian Association of Petroleum Producers on behalf of groups looking to enter into an agreement (Ibid). While these industry groups have pushed for industry or country standard forms, forms created today are instead commonly used as a type of reference tool for more specific agreements (Mercier, Kane, and Nammour 2015, 247). Additionally, within the standard energy industry it is rare to find contracts that allocate risk based solely on a fault basis (Kangles et al. 2011, 359). This is most likely due to the high risk associated with many oil and gas related projects as determined by the

proponents of these oil and gas projects (Ibid). Instead contracts can utilize a fault-based and no-fault based liability agreements or allow for different liabilities to be faced by different parties to the contract (often called multiple fault regimes) in order to incentivize contracted parties to take on the construction or operation of high-risk projects (Ibid). In this way, oil and gas companies using indemnification agreements as a type of risk management to ensure their ongoing financial viability in the future. These contracts are often very complex, with different liability and indemnification agreements created for each portion of the project and potential liabilities they may face (ex. asset risks, environmental damages, breach of contract etc.). The contracts may also specify the limit of liability that a particular party can be held responsible for (Ibid, 362). Due to these common practices, oil and gas companies that exist today are very familiar with indemnification agreements and how they can be used to ensure that liability is not held solely by the company.

2.3 The Canadian Government and Indemnification

Governments regularly indemnify specific risks present within their countries, including risks related to natural disasters (floods), nuclear power accidents and terrorism coverage. A justification for indemnification of these and other industries is that the risks involved in these areas have the potential for calamitous losses that would cause insurance agents to become insolvent or create conditions in which insurance premiums would be so expensive as to disincentivize those that need it the most (Brennan, Kousky, and Macauley 2010, 119). An example of this type of government program is flood insurance programs in certain areas of the United States. Other justifications for government indemnification include viewing the move to indemnify on the part of

governments as a tacit subsidy to encourage the continued positive externalities propagated by the industry or project (Lakdawalla and Zanjani 2005, 1893). One such example of this is a government's support of space programs, which are highly risky endeavours that could likely not go forward without both a government's guarantees and funding commitments. This type of indemnification by the federal government can be characterized as a type of indemnifier of last resort for the common good. In these cases, the government consciously enters into agreements with industries to indemnify them in the event of catastrophic or unforeseen events. The government's support of the pipeline industry is not classified as this type of agreement because it is not formalized in this manner and not agreed to beforehand that it is in the public good for the government to support a particular industry. Instead, indemnification of pipelines in Canada, while a continuous pattern overtime, is informal in nature and examined on a case by case basis by governments despite the fact that this piecemeal approach when looked at by the industry is seen as a sector-wide guarantee.

In contrast to the government acting as an indemnifying agent of an entire industry, the Canadian government regularly uses indemnification clauses when making agreements with contractors or private companies when entering into specific agreements as the proponent of a particular project. This formal use of indemnification clauses in contracts exist most often when an entity of the government (in this case most likely the 'Operator') enters into an agreement with another party or business for work required by the government (this could be classified as the 'Contractor'). These types of indemnification agreements mirror those found within the business world and easily fall into the fault-based indemnification categories described in Table 2.1. The parameters of

these indemnification clauses vary, but most are heavily regulated depending on the government department and can only be approved by people holding certain government positions to ensure that such agreements are at an industry standard and fall under appropriate risk parameters (Kari 2019). Arm's length government entities can additionally employ indemnification agreements, which while organized between the crown corporation, and another party would have the federal government as the ultimate indemnitor should crown corporations find themselves financially insolvent (Poschmann 2013, 1).

The Canadian courts exist as a separate branch of government from the ruling and administrative arm, however their position on indemnification can be enlightening in how the court interprets indemnification contracts. Canada common law does not provide a right to indemnity (Kangles et al. 2011, 341). This means that any right to indemnification by any party must be created as the result of a contract or through legislative means. However, at this time no legislation in Canada either restricts or bars indemnification and according to some authors it is unlikely that anti-indemnity legislation such as the *Louisiana Oilfield Anti-Indemnity Act* is to be enacted in Canada (Ibid, 343). Canadian courts have historically sought to align with the true construction of a contract to understand the signed parties' intentions and therefore determine each signatory's reasonable expectations in regard to liabilities (Ibid). The principle of *Contra proferentem* (which states that in the event of an unclear or ambiguous section of a contract the understanding will be interpreted against the party that drafted the document) is also often used in Canadian court cases regarding indemnification clauses (Ibid). Courts are also historically likely to apply the *Contra proferentem* for claimants seeking

indemnification due to its own negligence (Ibid, 344). This is in line with the preference noted by many Canadian courts that those taking on the indemnification risks and negligence of others should be outlined in clear standard language to ensure understanding by all parties (Ibid, 345). While the rulings by the court have governed the actions of industry as to how they draft indemnification agreements, given the lack of legislation limiting indemnification agreements it could be argued that the Canadian government does not take a leading role in regulating how indemnification clauses are drafted. Instead rulings follow in the event of conflict between parties, and government indemnification clauses are drafted according to business standards. In this way it is the business community that forms an entity's understanding of what indemnification is whether used in a formal or informal way.

2.4 Indemnification as a Concept

With the overview of what indemnification means generally, in the oil and gas industry and within the context of the Canadian government, this next section will outline the manner in which indemnification will be used within this thesis. As previously stated, while the Canadian government has not signed official indemnification contracts with the oil and gas pipeline industry, it has acted as the de facto indemnifier of the industry should projects experience unexpected difficulties that threaten the viability of the project to go forward. This is key to note because not only does it position Canadian taxpayers as potentially on the hook for infrastructure and industry projects that have no guarantee of repayment, it also creates conditions within the industry in which the Canadian government carries a significant amount of risk while reward is held in the form of profits by private oil and gas companies. This creates a situation of so-called “privatized gains

and socialized losses” that does not mirror the free market type of capitalism both the Canadian government and oil and gas companies say they are a part of (Ritholtz and Task 2009, 3).

The difference between what would be termed as government support (or subsidy) and what this paper is calling government indemnification of an industry is helpful to expressly state. This is because without this distinction between a subsidy, bailout or indemnification it would be easy to say that the government indemnifies all industries, thus making the term overly broad. Indemnification therefore is defined as the government taking responsibility for the large-scale liabilities faced by the industry to sure its continued survival despite the fact that it has or has not encountered significant ongoing issues that could create the collapse of the industry. Action by the government is therefore taken not just to support a part of a project or company within a sector (often known as a subsidy), but the whole sector itself. Indemnification in this case is also different from so-called government bailouts. Bailouts can be defined as financial help to an entity that would otherwise be on the edge of failure or bankruptcy most likely as a result of immediate emergency measures (Block 2010, 160). While indemnification of an industry can lead to bailouts of specific projects or sectors, it also serves as a guarantee regardless of the outcome of the project, thus differentiating the two.

Informal government indemnification does not necessarily speak only to the oil and gas pipeline industry. In fact, it could be argued that the Canadian government acting as an indemnitor has occurred for numerous industries within Canada at various times within its history. Examples of the indemnification of industries can particularly be seen in the Canadian government’s decisions in 2009 to bail out the automotive industry or the

decision in 1993 to buy a significant share in the Hibernia oil project to ensure the continuation of the oil industry in Newfoundland (CBC 2018). Both of these examples represent not just a subsidy or loan guarantees for specific ventures but direct investments in the projects to ensure the continued survival of the industry sector. The government's continual support of the agriculture industry in Canada could also be seen as not just a way to support individual initiatives within the industry but a wide scale underwriting of the industry. Often the government acting as an indemnitor is justified publicly by stating that it is in the national interest to save the industry, the industry is 'too big to fail' or that it is vital to the Canadian economy (Klein and Le Roy 2010, 228). While these justifications may or may not be true, they represent a departure from the capitalist independent free market private sector that most of these industries purport to be a part of.

In the case of pipelines, it is crucial to note that this type of government indemnification is not a one-time occurrence, but a systematic policy that has occurred over a significant period of time. The result of such long-term direct support therefore not just serves to protect pipeline projects in Canada but also can change the behaviour of oil pipeline companies and the decisions they make. Ehrlich and Becker (1972, 640) note in their theory of self-protection that parties that have certain guarantees will act in a different manner than those who have no such certainties in place. They note that a change in the guarantees or insurance will change how actors not just make decisions but also view risk (Ibid, 641). This phenomenon often called "moral hazard" refers to the common circumstance that the presence of market insurance actually can increase the probability of hazardous events occurring (Dembe and Boden 2000, 262). As Lakdawalla and Zanjani state,

since insurance and self-protection are substitutes ... a policy aimed at encouraging the purchase of insurance simultaneously discourages self-protection. Thus government subsidization of insurance can be interpreted, ironically, as a policy geared toward encouraging moral hazard (2005, 1892).

In this way, government actions towards indemnification of industries/projects will affect the externalities generated by said project.

The possibility of government actions affecting industry actions brings forward specific public policy concerns regarding indemnification agreements and their ability to benefit society as a whole. Kangles et al. (2011, 347) write in regard to indemnification that “if liability is allocated to a party incapable of sufficiently compensating losses, or where the allocation of risk is the unconscionable result of asymmetrical negotiating power, the result may pose a risk to the public.” This is particularly relevant given that a government indemnifying a private sector project is not indemnifying a fault-based regime that covers mistakes that could be made under their purview. Instead, such actions seem to mirror broad based indemnification agreements in which one party agrees to cover issues related to the project regardless of who has created the problems inhibiting ideal project conditions. Furthermore, as this is not a formal agreement, the government is not covered by insurance (as is usually required by such agreements) but instead pays out money from its own balance sheet. Such a large difference between the risk bore by both parties may seem like good risk management to oil and gas pipeline companies, but in reality may simply act as a continuing power imbalance between a strengthening private sector and a public sector on the hook for infrastructure projects that encounter issues.

As discussed previously, broad indemnity agreements are particularly vulnerable to power relations compared to limited or intermediate indemnity agreements. If one party is aware due to a history of past financial commitments made by the federal government in support of the industry, it decreases the relative bargaining power of the government to ensure continuation of the industry without direct monetary intervention. Therefore, if an oil and gas company is aware of this history of repeated financial backing by the government for their industry, this can serve as an informal indemnification agreement in which the company is secure in the knowledge that should the project face certain roadblocks, losses or damages the government will step in. In this way, these informal indemnification guarantees merely serve as an additional form of risk management for pipeline companies and can be built into business plans. What would under a free market capitalist system represent regular liabilities and risks associated with business ventures can now be written off under new incentives provided by the government (Ritholtz and Task 2009, 4). While this serves to decrease risk for oil and gas companies, due to the informal ad hoc nature of indemnification for the industry it dramatically increases risks faced by the government. In contrast to the formal indemnification agreements the government signs in its direct business dealings, there is no formal language governing the perimeters of what will or will not be covered by the government that can be defended if necessary, in court. Instead it is up to the digression of politicians to decide the parameters based on what they feel are politically viable and beneficial often under time deadlines to ensure what they feel is needed for the continued viability of the project.

The case studies analyzed in the forthcoming chapters to answer the questions of whether the Canadian oil and gas pipeline industry falls within the parameters of indemnification described above. If this industry does fit within this framework it calls into question not just the perception of the oil and gas industry within Canada but whether the continued policy of indemnification has benefits for the Canadian government and Canadian citizens.

TransCanada – The Great Pipeline Debate

The building of the TransCanada pipeline represents the first large government indemnification of a pipeline and the start of the federal government's policy of indemnification of the pipeline industry that still occurs in the present day. The pipeline is also a significant example of government controversy surrounding of a pipeline. It can be argued that it had the most political consequences for a government to date, as it led to the direct fall of one government (St. Laurent's Liberals) and the election of another party (John Diefenbaker's Conservatives). However, in the end, the pipeline would not have been built without significant negotiating efforts on the part of the government with TransCanada and the personal support of Minister CD Howe to back the building of the pipeline. This period of pipeline construction then started the modern policy of government support of the pipeline industry. This chapter will provide an overview of the way in which the TransCanada pipeline came into creation with a specific focus on government efforts to support and then indemnify the process of building the pipeline. The first indemnify action by the federal government to help provide a \$25 million dollar loan to the company when they could not secure supply contracts, when this proved politically problematic the government of the day tried to indemnify though a second route tried to indemnify the project through the International Development Bank. However this also fell though, leading to a third indemnify act, when the government agreed to build the Ontario shield portion of the pipeline through a crown corporation and lease it back to TransCanada so that they could stay financially viable and gain financing for the other portions of the project. The government further provided financing guarantees to the company when they could not find financing and provided a direct loan

to the company totalling over \$80 million in a fourth indemnifying act of the project. These actions showcase the start of indemnifying behavior that continued in the pipeline industry in the forthcoming years. The chapter will also show how although some conditions of this pipeline match Salamon and Siegfried's theory that explains government support for an industry (a small industry size, large firm size and high degree of market concentration) other facets are not predictive indicators (The TransCanada pipeline had a large geographic dispersion and the company had a low profit rate from when the project was proposed to during its build). Overall however, the TransCanada pipeline represents a significant indemnifying act, and an example of how certain industries can gain government support.

Liberal Prime Minister Louis St. Laurent oversaw the building of the TransCanada pipeline and what is now known as "The Great Pipeline Debate." While the official dates of the Great Pipeline Debate are from May 8 to June 6, 1956 and refer to the parliamentary debates on the pipeline, the beginning of the TransCanada pipeline in actuality spans from its conception in the late 1940's to 1959 when it underwent its first full year of operation (Newman 1993, 7). Following World War II to deal with the increased natural gas needs of populous Ontario and Quebec, and the large amount of natural gas found in Alberta, it was decided by St. Laurent and his Minister of Commerce CD Howe that a Canadian pipeline connecting the two areas would be beneficial (Roberts 1957, 13).

In the early 1950's with the exception of areas in Alberta, natural gas supplied only a small amount of energy consumed in Canada. Therefore, it was quite a small industry matching the indicator of government support for industry by Salamon and

Siegfried. As a fuel and energy source it didn't surpass wood until 1955, but natural gas experienced exponential growth to the amount that by 1960 it became a greater source of power than hydroelectric (Kilbourn 1970, 3). In 1969 natural gas supplied 20% of Canada's energy second only to crude oil, but this was years away in the 1950's (ibid). It is key to note that despite the much smaller sector of the energy market that oil and gas was a part of, it represented an important component for industrial use (Davis 1957, 133). Natural gas had the advantage that it did not require storing or handling by consumers, could be supplied regardless of weather and could help to solve urban air pollution (Ibid, 134). Additionally, during and after World War II, Ontario experienced fuel shortages due to a lack of new sources of hydropower and US coal that caused rationing of electricity during wartimes (Kilbourn 1970, 14). The discovery of natural gas in Alberta provided a possible Canadian-made solution in which could fill this gap (Stenson 1985, 27). Outside of the Westcoast Transmission pipeline in British Columbia, due to Alberta's moratorium on exporting natural gas, and cautious approach to exporting oil, the industry was not large.

The connecting of western energy with the industrial east when finished would be to date the longest line in the world at 2400 miles covering a significant geographic distance (Clark 1985, 99). In this case all-natural gas to be exported through the Trans Canada pipeline would come from southern Alberta and travel east. It was widely understood at the time that future natural gas consumption requirements would need to be met almost entirely from Alberta reserves (Royal Commission on Energy 1958, 6). It is key to note that the pipeline itself spanned 5 provinces, which could count against charges that a geographical concentration would benefit a company in gaining support from the

federal government. The sheer distance from the oil fields to the bigger markets in the east (Ontario and Quebec) led the pipeline project an air of nation building similar to the railways in the minds of government supporters (Newman 1993, 10) In this way, while the theory related to geographical dispersion leading to less influence does hold merit under some characterizations when looking at financing and oil extraction, it doesn't match what Salamon and Siegfried would state is an ideal for a sector attempting to obtain financial support from a government entity.

While the fastest least expensive route would have crossed into the United States, Laurent favoured a pipeline route that while longer and more expensive, would exist completely on Canadian land and would not require US approvals. Since during this time a large part of the need for a national pipeline route was due to the inability for provinces in Canada's east to reliably be guaranteed oil from the United States, a pipeline that avoided US approvals and lobbying was seen as more expedient by the Canadian government since the oil being transported was only to be targeted for Canadian use (Roberts 1957, 25). Notably, the all-Canadian route would need to cross the Laurentian Shield of Northern Ontario. This area of land is known for its rough terrain, rural landscapes and sparse population and industry. Markedly, there were few customers along this portion of the route, increasing the difficulty of its financial viability (Hooley 1968, 14). This combined with not just large swaths of wilderness, but also a lack of road infrastructure meant that construction of the pipeline would be extremely expensive (Oilweek 2008, 36).

The firm size of the companies involved in bidding to build the TransCanada was quite large for their day and the market was very concentrated. There were only ever a

few firms that could be involved directly in the building of the TransCanada pipeline, and due to the scale of the project it ended up that the amalgamation of two significant oil and gas pipeline companies was needed for the realization of the project. This meant that while most pipeline companies were not huge per se, the fact that they existed and could gain financing for proposed projects automatically meant that they had a large market concentration. This is the case for both Western Pipe Lines Limited and Trans Canada Pipelines the two major companies that expressed interest in building a Canada-wide pipeline and were eventually combined to form the major proposal to build the pipeline. In the early 1950's it was recognized that there would only be enough surplus reserves in southern Alberta for one company to export from the province east to Ontario (Kilbourn 1970, 26). Parallel pipelines were simply not economically feasible and because of this, it meant that not only was their little competition to build the pipeline, but once permits were granted only one firm was seeking government support. These conditions combined with the market concentration, small industry size and few large firms provided ideal conditions for the industry to gain government support.

The two companies initially in contention to build the TransCanada utilized their resources to gain government indemnification for the project, helped out by the structure of their industry. There was no danger of free-rider syndrome; as to do so would not provide any benefit for companies at all. Instead the American backed Trans Canada pipeline company pushed for an all-Canadian pipeline as a way to gain political favour (Roberts 1957, 157). They were very successful in doing so, gaining the support of Ontario Premier Leslie Frost and several western Members of Parliament during the initial proposal stage (Thorburn 1957, 527). Western's approach was much smaller, and

they pushed for a more economical route that would first be built to Winnipeg, allow for export to the United States with possible expansion at a later time. However in the end, Trans Canada spent twice the amount as Western in feasibility studies and their pipeline project did not require approval from of the FPC in the US to allow export by building the pipeline through the US so it was chosen (Newman 1993, 9). The agreement of Premier Manning of Alberta and PM Laurent in November of 1953 that given the financials any pipeline built bringing gas east should be completed by a single company made up of the two competitors again increased the size of the company building the Trans Canada pipeline, and eliminated any competition for a pipeline along this route (Kilbourn 1970, 84). From then on having made inroads to guarantee government support, the industry was restructured to even better leverage government indemnification.

In 1954, with increased government support for an all-Canada pipeline, the project was approved provided that the Western Pipelines Limited and Trans Canada Company come together to form one company (Grey 1970, 186). The deal effectively saw Western Pipelines become a wholly owned subsidiary of the new TransCanada Pipe Lines Company (Royal Commission on Energy 1958, 57). It was hoped that this newly formed company combined with approval for Alberta oil and gas regulatory authorities to allow export of oil outside the province that the pipeline could go ahead as up to that point Alberta had not allowed the export of any of its natural gas reserves. Approval by the province would allow the vision of an all-Canadian west to east line to be realized. It is key to note that once permits were obtained by the newly amalgamated company in 1955, there was significant incentive for construction to continue with that same company despite the issues with financing and approval that are outlined below. In this way larger

firms did not just help company's bid along the pipeline route, but the amalgamation of them into an even larger company helped them to keep the bid when issues with the pipeline arose.

Although the oil and gas pipeline industry in Canada during this time was highly concentrated, Trans Canada Company and Western Pipeline Limited were not the only pipeline companies operating within Canada. During the start of the 1950's very few large-scale pipelines had been built writ-large. Although the Westcoast Transmission pipeline (Trans Mountain pipeline) brought forward by Frank McMahon represented another large player on the pipeline scene, the company headed by McMahon was quite focused on capturing the Pacific Northwest market during the early 1950's (Gray 1970, 152). By the time he proposed an alternative to the Trans Canada later in the decade, entrenched interests meant that the Trans Canada company was the only company with engineering plans and had \$15 million dollars invested in their version of the pipeline, even if the plan they presented was seen as controversial (Kilbourn 1970, 104).

McMahon's proposal was better than the other alternative proposal brought forward by the Toronto investment firm of Gairdner and Company which required the government to invest \$100 million in unsecured junior bonds (an unacceptable risk according to the government) (Kilbourn 1970, 115). However, McMahon's proposal also required much more American support than Trans Canada's, and while he sought no government assistance on the pipeline during its initial proposal he withdrew his proposal before it could be seriously considered by the House of Commons (Montreal Gazette 1956). This meant in practice that TransCanada despite having a few competing proposals to build the pipeline across Canada had cornered the large amount of market backing that they needed

to have the pipeline actually constructed with few alternatives should the government want to encourage more companies to present competing proposals. These were ideal industry structure conditions for a company to gain government support.

3.1 TransCanada Indemnification

The first indemnifying actions related to the TransCanada pipeline occurred in 1954. While obtaining approval from Board of Transport Commissioners in Ottawa, the TransCanada company discovered that potential gas purchasers did not consider the TransCanada project financially feasible (Gray 1970, 193). Instead, they were focused on getting oil sourced from the United States via the Niagara Border which they thought would be cheaper. Additionally, gas suppliers in Alberta did not want to sign supply and sales contracts as they hoped to export instead to the more profitable US market (Gray 1970, 197). The company had difficulty securing supply contracts in Quebec and as it took longer to prove financial feasibility also in Saskatchewan and Manitoba. This difficulty gaining both financial institutional backing and supply contracts led to the TransCanada board to ask the federal government for payments due in the first years on mortgage bonds the company could not meet through depreciation and net earnings (Kilbourn 1970, 60). At this time, the amount was thought to be not more than a \$25 million investment compared to the overall cost of construction that was set at \$350 million (Gray 1970, 195). This loan would then be paid back with interest once a guarantee on the bonds was no longer needed. This represented the first action on the part of the company to seek government backing.

While this loan deal used what was termed an arms-length crown entity, all parties involved understood that the deal effectively led to the federal government underwriting

the pipeline project. When the company presented the idea to CD Howe on January 6, 1955, he was amenable but encountered pushback from his cabinet colleagues. The Minister of Finance, Walter Harris, at the time when writing to Howe stated,

The request for a guarantee raises awkward problems of precedent and past practice. Apart from defence production, there are no recent precedents for direct guarantees on marketable securities to large-scale private industries (Howe 1956, 3664).

The fact that CD Howe who was best known as a war-time minister shows how the pipeline industry had successfully sold themselves to be “essential” to the function of the government, and from this the second indemnifying act can be seen. However, due to the pushback to a direct loan from the federal government, a loan was suggested through the Industrial Development Bank carried out with the Bank of Canada, its parent body (Clarke 1985, 100). On March 13, the bank and Trans Canada agreed to the bank taking \$25 million in equity in convertible debentures with these not to be converted until earnings per share reached \$1.25 and that the bank then pay \$2.50 above the \$10 price of common shares to be offered to the public (Kilbourn 1970, 72). To show the bank’s confidence in the project the bank took \$5 million worth of shares before they went on sale to the public and making the banks. This made the bank’s commitment effectively \$60 million in convertible debentures and \$5 million in common shares. This would leave \$245 million in mortgage bonds to be sold to finance the rest of the project (Clarke 1985, 102). A January 26, 1955 memo to the Prime Minister states that the government is providing capital required for the pipeline project “no matter how cleverly we distinguish

this case.” (Kilbourn 1970, 67) Unfortunately, this deal fell through when the Governor of the Bank of Canada insisted on the bank having voting shares. This created a situation in which suppliers who had policies of not selling to government-controlled entities would not agree to sell to the pipeline, presenting significant financing issues for the pipeline (Gray 1970, 196). This action showcases how even this far back in history oil companies saw themselves as independent and separate from government enterprises despite the fact that certain companies in their sector needed substantial government support to survive. It is interesting however that by oil companies taking this position, instead of preventing government support of the pipeline industry it may have instead just led to an instance in which the government continued to indemnify and support the industry without having the ability to hold voting shares or direct control of the companies building certain pipelines. In this way, the second attempt to indemnify the TransCanada project fell through.

It was decided that, as a result of the failed financing, the pipeline could not be built during the construction season of 1955 and construction would have to wait for successful funding. By the spring of 1955 the outlook of the TransCanada was in doubt with the Globe and Mail hypothesizing that the project was “dead” (1955). While financing had been found for the Toronto Montreal section of the line, the northern Ontario section could not find financing (Kilbourn 1970, 88), effectively crippling the project because this section of the pipeline represented the most expensive and time-consuming section. It would however not be the end of TransCanada seeking government support in order to build the pipeline and a third indemnifying act would occur.

Despite the pipeline being described as dead, solutions continued to be sought within the government so that the pipeline could go forward, leading to the third instance of the government indemnifying the project so that it could continue. A finance official then proposed to build the pipeline through northern Ontario and lease it for operation to a company. The idea was that the government would therefore not guarantee high profits to private stockholders through direct funding for financing but would still be able to push pipeline construction forward (Ibid 89). To accomplish this the government would use a crown corporation (which could run as a private business rather than a part of the civil service) to build the proposed pipeline from the Manitoba border to Kapuskasing, Ontario (Canada 2018). The company would go on to be called the Northern Ontario Pipeline Corporation, and while a neat solution to existing problems in reality was still an entity of the government. This proposal would mean that other parts of the pipeline could be financed privately, and Trans Canada would be able to secure suppliers who had previously denied them due to the government's control under the International Development Bank deal. While the deal was described as "not a subsidy" by Howe (House of Commons 1956, 3664) by effectively indemnifying the most expensive part of the pipeline the government of Canada and Ontario (from whom the corporation received its powers from) was essentially indemnifying not just its construction but the most risky portion of the project. Capitalization for the crown corporation was achieved through direct advances from the Ontario and federal government rather than guaranteed bonds to the public (Thorburn 1957, 522), meaning the government would be on the hook pipeline could produce a return on investment. It was estimated the cost to build this portion of the pipeline would total \$118 million in the fall of 1955 (Glenbow Archives 1955). The deal

included a clause in which Trans-Canada would purchase this section of the line from the crown corporation as soon as it was able (Glenbow Archives 1956). While this agreement represents a significant amount of the indemnification action taken by the government, it was not the only action taken to ensure pipeline construction across the country.

After the signing of the crown corporation agreement, in order to get a guarantee on the amount of steel needed to build the pipeline for the 1956 season, TransCanada was forced when it could not find traditional financing for steel to seek other sources of financing. The steel had to be manufactured in the US, as Canada did not have the capacity, and due to a world steel shortage, money had to be given upfront to guarantee an order would be accepted. In the end a deal was struck with American oil companies the Tennessee Gas Transmission, Continental Oil and Canadian Gulf to cover the \$40 million needed. In exchange they would each receive 17% of the shares of Trans-Canada with a guaranteed 51% controlling interest until a public offering of shares with the opportunity for regaining of Canadian ownership (Royal Commission on Energy 1958, 58). While this turned out to be very controversial politically, it also effectively meant that three of the four largest gas producers in Alberta now had a stake of the project. Thus commenced “The Great Pipeline Debate” and the introduction and debate on legislation for the Northern Ontario Crown Corporation in 1956 after both the deal for the crown corporation had been signed and TransCanada was ‘taken over’ by US interests in the words of critics of the pipeline (Grey 1970, 208).

The creation of this crown corporation however was not the only finance support the federal government provided, and a further fourth indemnifying act occurred after the setting up of the Northern Ontario Crown Corporation. The

pipeline needed further support in light of anti-American sentiment and further delays in financing the western portion of the pipeline. Howe was of the impression that missing the 1956 construction season was untenable but thought that outright ownership of the pipeline was still not in the government's interest (Roberts 1957, 178). Instead on April 11, 1956 he negotiated that the government would give TransCanada a guarantee that if the company failed to find financing for the whole western section of the line, the government would finance it at 90% cost as long as the company found the other 10% by the November 1, 1956 deadline (Glenbow Archives 1956). This guarantee was then going to be used to obtain bank loans in order to finance the project, providing indemnification for investors in this portion of the pipeline by having government guarantees if the company could not find the whole 90%. Unfortunately, banks in New York still saw the project as too risky without guarantees on the export of natural gas to the US from the Winnipeg portion of the pipeline and the company could not close any bank loans (Kilbourn 1970, 97). A loan proposal was then proposed and brought before cabinet on May 7th as the pipeline debate raged in the House of Commons (Blakley 1956). In the end a loan was agreed with the government advancing a portion not exceeding 90% of the cost of the construction of the western portion of the pipeline at an interest rate of 5% for a short period (Glenbow Archives 1956). The government's loan in real numbers was estimated to be an amount of up to \$80 million and the language was included in the bill bringing the Northern Ontario Crown Corporation into existence (Ibid). The loan was described by Howe in the House of Commons as a short term loan with extremely tough conditions made necessary due to the fact that

the pipeline was not financeable in ordinary capital markets since the US regulator the Federal Power Commission (FPC) would not grant approval for the export of gas down to the US (Howe 1956, 3665). In fact, a number of cabinet ministers were explicitly against the idea of loan guarantees for TransCanada as they saw it as being painted as helping big business on the path to profit by opposition parties (Kilborn 1970, 63). Of the pipeline itself it was said right before the Parliamentary debates on the TransCanada pipeline itself in March that “If the [TransCanada pipeline] were to be a sure-fire profit bonanza it would have been already built. The fact is it won’t be. It will be a low interest affair (The Financial Post 1956).” After being pushed through Parliament in an unprecedented manner the bill was pass on June 6th and received Royal Assent on June 7th, just a few hours before the contract between the Trans Canada Company and the federal government was set to expire to finance construction (Thorburn 1957, 525). A week later construction crews started building the western section of the pipeline financed by government money.

In the end it could be argued that forming a crown corporation and providing a loan to back the TransCanada was a hugely successful endeavour. It was estimated that it would take five years after the pipeline reached full capacity for TransCanada to pay the government back and for TransCanada to gain full title of the pipeline, instead it took four and was completed in 1962 (TransCanada Pipe Lines Ltd 1962, 6). All of the money loaned plus by the government to build the western portion of the pipeline plus interest was paid back in full after a successful finance offering to the public in 1957 (TransCanada Pipe Lines Ltd 1957, 9).

Until the TransCanada pipeline was built for all intents and purposes the TransCanada Company was simply a paper company and did not have the large profit rates noted by Salamon and Siegfried that help an industry secure government support (Hooley 1968, 45). In fact, many Alberta oil and gas producers opposed exporting gas eastwards as they feared that the risks involved with the profitability of the pipeline could hurt them economically and would affect the sector's profit rates (Kilbourn 1970, 34). Many of the Canadian pipeline companies formed during this time were often newly incorporated and therefore could not boast of great profit rates as they had few guaranteed revenue sources. Although some pipeline companies had secured financing, TransCanada's profit rates were effectively nothing until the 1960's (Ibid, 200-201). The pipeline however never could have been built without the government taking on significant risk and indemnifying the Trans Canada by allowing them to have the capital backing and the security of knowing the federal government was indemnifying their actions.

3.2 Conclusion

Kilbourn writes of the TransCanada company,

in the end the pipeline became for its backers a matter of pride and honour beyond all rational economic sense: a test of their own willingness to survive an ordeal, a symbol of their ability to triumph over doubts and difficulties, an act of faith in progress or Canada or whatever sub-diety lured them on. (Kilbourn 1970, 24)

The same could be said of the federal government's willingness to back and indemnify the project. Not just once, but over and over again the government provided support to the pipeline. TransCanada's success lobbying the government could potentially be explained

by its relatively large firm size, the small size of the natural gas industry and the market concentration of the company. Profit rate however is not a good description of how the company could have gained influence as its financial viability was repeatedly questioned and the company did not make money until well after the pipeline was constructed. Geographical dispersion helps to explain the industry's lobbying power when looking at the concentration of its fiscal backing and the concentration of natural gas extraction. However, the large area covered by the pipeline works against the theory that smaller geographical diffusion leads to stronger lobby efforts. Ultimately the Liberal government's indemnification of the TransCanada pipeline tied the project of the pipeline to the government's fate. CD Howe wrote to a director of the TransCanada on June 22 saying, "I'm afraid the future of our government depends to a considerable extent on the ability of TransCanada to finance the pipeline and pay off the government loan (Kilborne 1970, 140)." The government had indemnified TransCanada by providing financial guarantees, loans through banks, set up crown corporations to help build portions of the line and when they still had financing issues provided direct loans to the company. While TransCanada was able to finance and pay off their government guarantees, the future of Howe's Liberal government did not live to see it and the indemnification of future pipelines was passed onto successive governments.

Line 9

In January of 1974 the federal government under Prime Minister Pierre Elliott Trudeau announced a new government policy on pipelines. This policy sought to create an all-Canadian coast-to-coast pipeline network to ensure Canadian self-reliance on oil (Canada 1976, 152). It was under this policy that the Sarnia to Montreal pipeline extension (also known as Line 9) was formally announced, leading to three significant instances of government indemnification of this pipeline. These acts of indemnification ensured first, a specific amount of oil would be run through the pipeline second, guaranteed the line against losses for a period of 20 years, and third provided the company with a government option to buy the pipeline. In this way, the Canadian federal government's policy of indemnification continued, with the company charged with building Line 9 Interprovincial Pipe Line Company (Interprovincial) gaining significant government support without which the project would not have gone forward. The structure of the oil and gas pipeline industry at this time in some ways mirrored the ideal structure for government support put forward by Salamon and Siegfried, and in other ways differed slightly. The industry at that time was composed of firms of a large size who had a high profit rate in a highly concentrated industry. Line 9 itself was built within a high concentration of geographical dispersion covering only two provinces in contrast to other larger-scale projects. However, the size of the oil and gas pipeline industry had grown significantly since the 1950's and while not huge could more accurately be described as a medium industry relative to the general economy of Canada at that time. While Salamon and Siegfried note that a small industry is ideal for government support, given that the pipeline industry is but a part of the overall oil and gas industry in the

country some of the same factors that encourage government support in small industries can be seen in the larger ones. This will be explored in greater detail in the following chapter which will detail how the pipeline was built, financed and indemnified.

4.1 The Need to Build Line 9

The expansion of the Sarnia to Montreal pipeline project has its roots in the changes to the North American oil and gas market in the early 1970's. Prior to 1971, the United States had a Mandatory Oil Import Program, which greatly influenced the extent to which Canadian companies could export Canadian oil to the US. However, in 1971 in light of increasing demand and cresting oil production in the country, the US revoked the Mandatory Oil Import program to import as much oil and gas as Canada was able to provide (Whyte 2010, 45). This created immediate pressure on the Canadian government from the oil and gas industry to support the construction of oil and gas pipelines from the north across the border to the US in the south rather than focus on supplying oil domestically (Gray 2000, 36). There was also the perception on the part of the industry that Canada possessed a "virtually unlimited" supply of oil and gas in the late 1960's, one that was quite quickly challenged in the early 1970's (Bregha 1979, 24). In December of 1972, the NEB advised the federal government cabinet that Canada would not have enough oil to meet both its domestic needs and the ongoing export levels in the next year (Gray 2000, 50). These issues were then compounded by OPEC's supply embargo, which saw imported oil into Montreal going from an average price in the early 1970's of \$2.45 a barrel to \$13.00 in 1973 (Ibid). At this time Montreal was entirely dependent on imported oil, as no pipeline carrying Canadian oil travelled further east than the Ottawa valley

(Ontario 1978, 1). Because of this, the federal government began looking for solutions that could secure Canada's oil supply and make Canada more energy self-sufficient.

The first indemnifying action of the government of Line 9 occurred in 1973. In response to increasing world prices and decreasing domestic supply, in September of 1973 the government announced its intention of extending the Interprovincial pipeline that existed in Sarnia to Montreal (New York Times 1973). At that time the area east of the Ottawa valley was reliant exclusively on foreign oil as no Canadian oil could run east through pipelines to them (Toronto Star 1976). In December the Prime Minister Pierre Trudeau stood in the House of Commons and announced a new national oil policy for Canada. This proposal encompassed three initiatives meant to shield Canada from the instability of the international market. These measures were the expansion of the pipeline owned by Interprovincial Pipeline Company to Montreal from Sarnia, a temporary freeze on oil prices, and an oil export tax based on the difference between domestic and world oil prices to raise funds and shield Canadian consumers from the steep increases in imported oil (Doern and Toner 1985, 91). It is key to note that focus on the later two policies, combined with the later announcement of a new national oil price and the creation of a new publicly owned national oil company (Petro-Canada) greatly outweighed the media focus on the pipeline expansion project. This had the effect of overshadowing what could have been controversy over support of such a large capital investment on the part of the federal government if announced during another time. This could easily have been a particular media focus by itself as Trudeau had announced his decision to extend the pipeline to Montreal on national television in November and on

December 6 in the House of Commons stated that the extension of the pipeline was “the single most urgent step towards attainment of our national goals (McDougall 1982, 135).”

The Line 9 pipeline showcases the government’s all-in approach to indemnifying the pipeline sector in Canada, so much so that very little opposition was encountered in contrast to when support for the Trans Canada was announced in the 1950’s. The Line 9 pipeline was primarily built to deal with oil scarcity in eastern Canada (caused by increased import prices and western Canadian oil travelling to the US). It is notable that the pipeline was only looked at as a policy solution when the federal government failed to secure an oil swap arrangement with the United States (Whyte 2010, 61). This deal sought to maintain oil exports at a specific level if the Americans did so as well but the US would not agree to such a deal. This meant that despite the Energy Minister stating that the “obvious and first” starting point for the government to come to an agreement with the US that allowed for the stabilized existing market arrangements to ensure a lack of scarcity the government was forced to look to alternative methods and act quickly to ensure oil prices could be levelled (McDougall 1982, 135). It also meant that the approval of the pipeline by the NEB was politicized to a degree as it had already been declared in the public interest by the government when they declared the expansion of Line 9 as the acceptable alternative when negotiating with the US fell through (Whyte 2010, 81).

Indemnification by the federal government for Line 9 was surrounded by much less controversy than TransCanada in the 1950’s. Although the expansion of the Sarnia to Montreal line was technically a matter under the NEB’s jurisdiction, and questions were asked about the federal government’s power to approve pipelines over the head of the NEB this quickly became inconsequential in the urgency of finding a solution to

increasing oil costs (McDougall 1982, 135). However, because both the Conservative and NDP opposition supported the expansion of the pipeline in principle little controversy occurred in the House of Commons on the issue. This could also be due to the fact that a bill didn't have to pass through the House of Commons for the pipeline to be built (Ibid). In fact, some members of the opposition wished the government to go further and supported public ownership of the proposed pipeline or the construction of a new Canadian line to bypass American port access points (Douglas and Dionne 1973, 7216, 7225). In this way, indemnification of Line 9 garnered much more government-wide support than TransCanada, and similar to the past a Canada only solution was eventually settled on using indemnification policies set in place by the federal government.

Interprovincial Pipe Line Limited was a company that displayed many of the industry structure facets helpful to gain government support described by Salamon and Siegfried. Interprovincial Pipe Line Limited owned an existing pipeline that ran from Edmonton, Alberta to the US border near Manitoba, and pipeline that ran from Sarnia, Ontario to Port Credit Ontario as well as other pipelines in the US. Because of the placement of its existing pipeline infrastructure Interprovincial was the logical company to add approximately 520 miles of pipeline needed to connect Sarnia to Montreal. The company was a significantly large player in the Canadian pipeline industry, operating large lines across most of the country. Interprovincial in 1963 became the largest crude oil carrier on a barrel-mile basis and by 1972 the company's average deliveries were above the million barrels per day metric (Enbridge 2019). Due to the large variety of pipeline that Interprovincial owned they oversaw a significant portion of the market concentration. This is also because although there were more pipeline companies in

Canada than in the 1950's, due to the concentrated nature of the oil industry in Canada and the large capital costs of building pipelines, the industry was focused on a few large companies. This combination of large firms and a high market concentrated set up ideal circumstances for the industry to continue to receive government support.

As the project progressed Interprovincial encountered issues numerous issues with the building of the pipeline. While the NEB started hearings on the Line 9 extension in May of 1974, these hearings mostly concerned the proposed pipeline route through Quebec. Concerns regarding financing of the line were not brought to the Board until October 9, 1974 (National Energy Board 1975, 3). At that time Interprovincial stated that they had concerns regarding the continued ability of the company to secure Western oil supplies to send through the line to Montreal and other areas of the Canadian market. Due to this, the company expressed doubts as to their ability to finance the Sarnia to Montreal extension and requested that hearings be adjourned until the matter could be settled (Ibid, 4). This request was granted, and it was understood that the NEB would not meet until hearings were initiated by Interprovincial to clarify its final position on the pipeline.

Interprovincial saw the Sarnia to Montreal extension as problematic financially for a number of reasons. In October of 1974, the NEB released its supply-demand forecast. This report showed a potential for a lack of Canadian oil available to Canadian markets as of 1982, which stood in sharp contrast to the forecasting of endless Canadian oil only a few years before (National Energy Board 1974, 6). This was particularly important because Interprovincial stated that the business risk for the pipeline was much greater than other sections of pipeline they had added to their network. Interprovincial at the time could not get Montreal refiners to enter into any throughput or shipping agreements to

ensure that Line 9 would be used after its construction, leading to uncertain and lower revenue guarantees for the pipeline (National Energy Board 1975, 21). Instead refiners wanted guarantees from the government that using domestic oil would not cost them any more than using imported oil (Toronto Star 1976). For Interprovincial this lack of supply agreements meant that it would take Interprovincial approximately 15 years to recoup its capital investment on the line when it's average for a project of this nature would be 10 with throughput and shipping agreements in place (Ibid, 22). Given these issues and the uncertainty of even getting Canadian oil through their pipeline in the future at a required volume that justified operation of the pipeline (250 Mb/d) the company decided that it "could not proceed with the project without some support" (Ibid). This was the beginning of Interprovincial's attempts to secure government indemnification for the project.

It is key to note that Interprovincial stating they could not proceed with the project without support was just as much an opening position to negotiate with the government as it was a statement of fact on the viability of a pipeline project. Interprovincial was aware of the necessity of the pipeline in the government's view. These type of public statements showcase how indemnification supports the pipeline industry when market conditions for pipelines change to make them less financially profitable. Due to this, financial problems on the line were not simply a reason to shut down the project but instead showcase how the company can use its "risk management" abilities to call in the informal indemnification protect granted to the pipeline industry. Thus, negotiations started with the Federal Government and the first steps toward realization of the indemnification of Line 9 started.

4.2 Line 9 Indemnification

While the federal government had been involved in encouraging the expansion of Line 9, it was not until 1974 that the first clear instances of indemnification occurred. This then progressed to the federal government showcasing the many ways that they were willing to indemnify the project throughout the life of the pipeline. The first action of indemnification on the part of the federal government occurred in the fall of 1974 with a guarantee of oil supply to Line 9 and was brought about by a number of factors. The failure of the Sarnia to Montreal pipeline to go forward had the potential to go against the set policies of the Trudeau Liberal government. In January of 1974 they had announced a policy of establishing an all-Canadian coast-to-coast pipeline network. This policy had its roots in the government's need to establish self-sufficiency for Canada and its cornerstone was the expansion of the Interprovincial pipeline expansion to Montreal (An Energy Strategy for Canada 1976, 152). The area requiring support was therefore quite geographically concentrated leading to a higher likelihood that the government would be willing to provide support. This was because any pipeline expansion needed to be able to directly serve eastern markets and link in with existing pipeline infrastructure, limiting the number of alternative companies that could oversee a project of this scale. The federal government was fully committed to the pipeline and the Minister of Energy, Mines and Resources Donald Macdonald stated to the media that Ottawa was considering building the pipeline itself if Interprovincial backed out of the plan, a sure sign of the level of indemnification that the government had for the sector (Toronto Star 1974).

In light of the government's statements that they would provide support Interprovincial pushed for greater levels of indemnification of Line 9. Interprovincial

requested that the government pay a share of Line 9's fixed operating costs, which at the time would have cost the government \$25 million a year (Toronto Star 1975).

Negotiations were ongoing however and instead a letter was sent on November 19, 1974 from Minister Macdonald providing reassurance that Line 9 would be used to an average 250 Mb/d of the 350 Mb/d total capacity that it could hold. This was realized because the government agreed to take measures to ensure a market for western Canadian crude in the amount of 250,000 barrels per day to eastern Canada (Ibid, Appendix I). Given the uncertainty surrounding the larger amount of oil headed for export to the US at the time this action was taken, and thereby had the federal government stating that they would limit exports of oil if necessary to ensure oil made its way to Montreal markets. A guarantee of this nature indemnified the project because it provided an assured amount of customers.

This was however not enough guarantee for the company and further indemnifying actions were sought by the company leading to the second instance of indemnification. Negotiations continued until the federal government ultimately agreed that given issues with financing the company was facing, they would reimburse Interprovincial for any revenue amounts that fell short of covering the fixed and variable costs of the pipeline extension (Toronto Star 1975). This was agreed to in January of 1975 and then passed through Cabinet in the subsequent months. It was agreed formally on April 8, 1975 and outlined that for a period of 20 years from the date in which the company was granted approval from the NEB the government would cover the revenue losses of Interprovincial (National Energy Board 2014, 8). The agreement notably did not

guarantee the company any profits but did effectively indemnify the company against any losses from this section of the pipeline (Ibid, 23).

These measures of government support are highlighted by actions taken by the company to secure financing that could only have been realized by both short and long term guarantees to indemnify the project. Following the formal agreement in April of 1975, Interprovincial decided that given this agreement and the letter assuring use of the pipeline it would proceed. This decision to proceed was not without qualifications however as the company stated that it was only going forward with the project “in the interests of national security, but it would not have done so otherwise because of the questionable prospects of realizing a reasonable profit for the shareholders on the undertaking.” (Ibid, 23) The company following agreement with its underwriters that the project was financeable proposed to raise the entire capital cost (at that time estimated at \$185 million) through debentures in Canada. This was proposed to be split into one serial debenture totally \$45 million covering one to five years and an additional \$140 million of 20 year sinking fund debentures. In between securing this money, \$60 million dollars of bridge financing was arranged with bankers to cover construction of the project (Ibid). It is key to note that this financing was finalized after the government agreed to indemnify the project in the short term through guaranteed supply side, but also in the long term by guaranteeing no losses for the company on this project for 20 years. Without both indemnifying acts the company would have had significant financing issues and would probably not have proceeded with the project.

One further adjustment was agreed upon given the new oil uncertainty in Canada. Given the long-term uncertainty regarding the availability of Canadian oil it was decided

that the pipeline should be built so that oil could flow in either direction (National Energy Board 1975, 10). This meant that if oil was discovered on the east coast of Canada it could flow west, but practically also meant that imported especially overseas oil could potentially flow into Ontario via another non-US route. Building the pipeline in this manner created a potentially more profitable and therefore more financeable product in a world where oil supply was uncertain.

The size of Interprovincial helped it to secure the terms that they wanted when building Line 9. Given these indemnifying agreements with the federal government, Interprovincial requested hearings at the NEB regarding the Sarnia to Montreal expansion on February 21, 1975. A meeting was held explicitly on the financibility of the project on April 11, 1975. At this time Interprovincial presented their agreement with the Federal government to the NEB board and the NEB approved them in May of 1975 (National Energy Board 1975, 4). The NEB proceedings are another instance in which Interprovincial's firm size and influence can be a predictor of positive government decisions. Farm landowners angry about the proposed route of Line 9 vocalized frustration. One farmer stated that there was a significant disadvantage for smaller interveners in the Sarnia-Montreal pipeline NEB hearings in terms of time, money and legal experience compared to the Interprovincial Pipe Line Company (Lucas and Bell 1977, 84-87). However, given the power of the company, government backing and importance put on the pipeline during the oil crisis of the 1970's these protests did not have the ability to significantly derail the project.

By the mid-1970's the government's policy of indemnification led to millions of dollars in costs for the federal entity. Line 9 was built for \$250 million in 1975 and

became fully operational on June 4, 1976 with a throughput capacity of 315,000 barrels per day (Enbridge 2019). The significantly larger capital costs for the pipeline was due to bad weather during construction, increased construction costs and issues with pressure testing that required the line to be examined and repaired after its initial operation (Interprovincial Pipe Line Limited 1976, 4). These increased capital costs through further debenture financing in 1976 and 1977 (Toronto Star 1976). The requirement by the NEB that Interprovincial sell oil at the same rates to Montreal as Toronto was also put into effect in 1976 (Slocum 1979). This required the federal government making up the difference between the actual cost of operating the pipeline and the revenue they were allowed to charge which in 1976 totalled \$20.2 million (Ibid, 3). This represented a significant cost to the federal government as a result of the indemnifying guarantees that they had provided Interprovincial regarding the pipeline.

There was however a third indemnification act agreed to by the federal government for Interprovincial. On February 25, 1977 the federal government and Interprovincial signed an additional agreement that provided the federal government the option to purchase Line 9 (National Energy Board 2014, 8). This further indemnified the pipeline, as there was a clause in the contract, which allowed the Federal government to purchase the Montreal extension from Interprovincial during the course of their 20-year agreement. It also provided further assurance to the company and any financiers/shareholders that in the event of year after year losses the federal government would step in and take over the entire liability for the pipeline. This was particularly important as given the \$29 million-dollar gap in revenue owed by the federal government to Interprovincial, the pipeline was not a money-making enterprise. Instead, the pipeline

was operating at a significant loss, only made viable by the indemnifying agreements put forward to the company by the federal government.

This agreement came on the heels of a 1976 NEB ruling that the company should be regulated using a rate base concept used by utilities effectively buffering Interprovincial from regulations by indemnifying the company against set rates (Globe and Mail 1978). This stood in contrast to the previous system in which Interprovincial filed its proposed tariffs with the NEB and revenues were dependent on the amount of oil running through the pipeline (Slocum 1979). Interprovincial had attempted to convince the NEB that an additive fee of 61.5 cents needed to be added to oil travelling through Sarnia, however the NEB only agreed to a 20 cent tariff, effectively guaranteeing in the words of the company “another substantial deficiency payment on the part of the federal government in respect of 1977” (Interprovincial 1976, 3). The agreement with the federal government to provide an option to buy Line 9 came on the heels of a year (1977) in which Interprovincial posted earnings of \$1.71 per share which were the second highest in the company’s history (Interprovincial 1977, 3). However, the NEB in 1977 also allowed no rate of return for the Sarnia to Montreal line on the premise that the line was financed by debt (Ibid). This created a situation in which continued government indemnification was needed to support the pipeline year after year.

In this way, profit based on individual pipelines is not a good indicator of a company’s ability to influence the government, but the overall profitability of pipeline companies can indicate their ability to gain government support. This is because pipeline companies will often have lines that vary on profitability over time depending on the price of oil, source of that oil, types of government regulations and a whole host of other

possibilities that can occur. It can be argued however that the company making larger profits did allow it to have the resources to lobby the government for the significant support that they were able to obtain for the line, showcasing how profitability can benefit large companies looking to gain government support. While high company profits cannot always be perfectly correlated with increased government support, the option to buy, while never actualized did provide reassurance to Interprovincial, their backers and shareholders. In a climate in which high tariffs were no longer guaranteed and it was unclear that the pipeline would be profitable, an option to buy represented assurance in the face of an unknown future. The government may not have been publicly supportive of the growing profits of Interprovincial, but they were however willing to indemnify the company against losses down the line giving the company significant support in a sector known for its cyclical nature. This form of support could only benefit a company, encouraging it to become dependent on government indemnification in the future.

Twenty years after the government helped to build Line 9, it divested its interests in the pipeline. An agreement was announced by the federal government that Interprovincial would continue to both own and operate Line 9 and that Canada was released from any “rights and obligations” from the previously signed agreements (National Energy Board 2014, 8). Interprovincial purchased the government’s option to acquire Line 9 for \$10.3 million dollars. Although the federal government sought other offers for the pipeline with a reservation price of \$20 million no other party submitted a bid (National Energy Board 1997, 60). The government’s indemnification of Line 9 had led to not just years of million-dollar payments, but also the sale of the line below market value. This sort of support could only be explained by viewing the government’s actions

as indemnification of the large-scale liabilities that the pipeline industry took on.

Indemnification of this project ensured that the company had a guarantor who could smooth any issues that the project encountered and ensure its viability when faced with changing conditions.

In the next year a request to the NEB was made to reverse the flow of oil through the pipeline. Additionally, annual reports by Interprovincial show that payments were made throughout the 1980's in the high single digit millions and into the 1990's where continued payments of around \$10 million were made (Interprovincial 1982, 10; Interprovincial 1991, 50). In 1999, the NEB granted approval and the direction of the flow of oil in Line 9 was reversed to allow for the westward travel of up to 240,000 barrels per day of offshore crude (Enbridge 2019). The government provided Interprovincial with hundreds of millions of dollars over 20 years to keep the pipeline open, guaranteed oil flows through the pipeline and provided them with an option to buy agreement. It was a momentous amount of indemnification without which the pipeline would not have been built or overseen in this manner.

Trans Mountain

In May 2018 Prime Minister Justin Trudeau announced that the Government of Canada was purchasing the Trans Mountain pipeline and would continue to advocate for the expansion proposal attached to the line. This purchase represents the largest single indemnification action on the part of the federal government of the pipeline industry. However, the steps required to get to this act of nationalisation are many and show a pattern of government support even before the outright purchase of the pipeline. This was however not the first indemnifying action related to the pipeline project. First Kinder Morgan requested direct indemnification for the project should it continue to encounter regulatory hurdles, second, they requested monetary investment to help indemnify the project, before finally agreeing to take on the complete liability of the pipeline by purchasing it fully representing the third and largest indemnification act. Additionally, it is key to note that the oil and gas pipeline industry structure at this time exhibited many of the characteristics that made it a good candidate for gaining government support. Kinder Morgan (the company proposing to expand Trans Mountain) was a large company with a high profit rate in a highly concentrated industry. The pipeline proposed was concentrated to two provinces along an existing route, taking up comparatively little geographic space. While the oil and gas industry could be described as medium in size relative to the general economic of Canada, pipeline projects made up a smaller portion of them. All of these facets helped Kinder Morgan gain federal government support and indemnification that continues to the present day. This will be discussed in further detail in the ensuing paragraphs.

5.1 The Need to Expand Trans Mountain

There were a number of reasons put forward initially for the expansion of the Trans Mountain pipeline. The decision to propose the pipeline was made in an environment of concern regarding the relatively low cost for Alberta oil that could be found in the United States compared to higher prices and diversification that could be found by shipping oil internationally from Canada's west coast (Harrison 2019, 61). An additional factor brought forward at this time noted how Canada's investment climate would suffer when looked at by international companies in light of numerous issues on the part of pipeline companies to get their proposed projects (Trans Mountain or otherwise) approved and built (Angevine and Green 2016). Particularly notable about this was that the oil and gas industry, while not the biggest industry in Canada made up in 2013 \$133 billion in nominal Gross Domestic Product (GDP) (Natural Resources Canada 2014, 4). This equaled the equivalent of 7.5 percent of total GDP making the industry a significant medium size industry to the economy (Ibid). This way of thinking emphasizes that the oil sands are a stranded asset of Canada's which cannot be realized without the building of pipelines from the oil sands outward (Ibid). Additional pipelines that can connect the oil sands to British Columbia's coast would therefore provide a mechanism to export oil internationally benefiting both Canada and the oil companies operating within Canada. These were the primary narratives brought forward by Kinder Morgan when they proposed the Trans Mountain expansion project in 2013.

The proposed expansion of the pipeline was put forward by a large firm and with the benefit of new construction requiring very little additional geography from the original pipeline itself. Kinder Morgan, a Texas based pipeline company which is the

largest energy infrastructure firm in the S&P500, who owned the 1953 pipeline, put the expansion project forward. In addition to this line, they operate 84,000 miles of pipelines and 157 terminals (Kinder Morgan 2017, 3). The Trans Mountain pipeline had been in use since 1953 and is one of Canada's oldest intra-provincial pipelines that was constructed to ensure oil could be sent to the Pacific Northwest market ahead of oil from the Texas region (Ibid). The expansion project proposed a second pipeline built parallel to the existing pipeline route allowing for a tripling of the amount of oil sent westward. This would increase pipeline capacity from 300,000 to 890,000 barrels per day and would escalate the amount of diluted bitumen flowing from Edmonton, Alberta to Burnaby, British Columbia. Given that the pipeline was pre-existing it would also decrease the amount of environmental disruption along the pipeline route compared to alternative pipeline proposals contemplated. The need for such a large increase in oil capacity was justified as a way for Canada to export more oil to other international particularly Asian buyers and bring up \$73.5 billion in economic benefits to Canada over the next 20 years (Earnest 2015, 7). In this way a large firm proposed a pipeline project that was confined to a very specific geographical area.

However, the increased capacity of this pipeline created extensive opposition from a number of groups including First Nations, environmental groups and certain municipalities in BC. In particular, concerns about the increased tanker traffic along the coast and the environmental threat they posed as well as concerns about climate change and how the increase of this pipeline could justify further oil sands expansion (Cruichshank 2019).

Kinder Morgan once approved took significant action to decrease the risk faced by such a large-scale pipeline project. Despite the concerns voiced by opposition groups, on May 19, 2016 the NEB released its final report on the Trans Mountain Expansion Project stating that “the project is not likely to cause significant adverse environmental effect,” was in the public interest and recommended approval by federal cabinet (National Energy Board 2016, 2-3). The board imposed 157 conditions that would have to be fulfilled in the event the pipeline went forward, however many groups did not feel key issues such as tanker traffic had been addressed by the report (Bakx 2016). On May 29, 2016 the expansion was passed by the Trudeau cabinet. Regardless of continued protests along the pipeline, on May 30, 2017 Kinder Morgan Canada Ltd debut on the TSX with a \$1.75B Initial Public Offering (IPO), the fourth-largest IPO in Toronto Stock Exchange history (Ashworth 2017). Kinder Morgan by doing this spun off its Canadian holdings into its own separate company. This was done in order to fund the money needed in order to expand the Trans Mountain, and was also widely seen as a way to buttress against the political climate and uncertainty surrounding pipeline approvals (Ibid). While the stock was initially priced between \$19 and \$21 it dropped to the \$16 range later in the year given the uncertainty of the pipeline project and the price of oil going forward. Kinder Morgan had been approved, and the company in seeking financing showed that it was willing to take significant action to prevent risks and bolster profits.

Though the profit rate for Kinder Morgan was high, the company encountered numerous continued issues regarding the project. Despite a successful third-quarter in 2017 of \$42.4 million up from \$20.3 million the previous year, continued political and regulatory issues with the pipeline caused Kinder Morgan on December 4, 2017 to

announce what they called a primarily permitting strategy when it came to construction on the Trans Mountain (United States Securities and Exchange Commission 2018). This strategy meant that the company was focused on the permitting process rather than full construction and spending until further assurance could be ensured on permits, approvals and judicial reviews that were still in flux (ibid). This strategy allowed Kinder Morgan to begin work on the expansion on December 27, 2017 and the NEB granted the company the ability to ignore Burnaby city bylaws full construction was delayed (Kinder Morgan 2017, 16). This was however not the end of Trans Mountain's construction issues.

The beginning of construction was complicated by numerous protests and announcements. On January 30, 2018 the BC government announced that it would seek to implement additional environmental regulations regarding pipeline safety, spill response and restrictions on the amount of diluted bitumen transported through BC (Zussman 2018). These regulations were aimed to come into effect in 2019 and greatly affected Trans Mountain by further delaying an already delayed project. Additional opposition occurred when BC Premier John Horgan said that they would pursue the formation of a reference case in the provincial Court of Appeal to enquire if a provincial government could legally control the shipment of oil through the province on environmental grounds (The Canadian Press 2019). This challenge also had the potential to prevent expansion projects like Trans Mountain seeking to increase the amount of oil running through BC territory. The Trans Mountain project became increasingly contentious and politically factious as the province of Alberta (who were in favour of the pipeline) and the province of BC came to head about the constitutional ability of provinces to restrict the amount of oil being transported through the province (Hoberg 2018, 10). Direct protests additionally

continued to occur along the Burnaby route of the pipeline from numerous groups intent on preventing construction crews from working to expand the project (The Canadian Press 2019). In sum, contentious actions continued to accrue as the months went by leading to uncertainties surrounding the project.

5.2 Indemnification of Trans Mountain

It was at this time then that Kinder Morgan first asked the federal government to indemnify the pipeline project. On March 6, 2018 after months of delays and challenges on the Trans Mountain project, Kinder Morgan representatives met with James Carr, the Minister of Natural Resources and his chief of staff in Houston, Texas (United States Securities and Exchange Commission 2018). The meeting focused on the ongoing challenges facing the Trans Mountain expansion project. The increased and ongoing protests had caused the company to voice that it was “become increasingly concerned that without active intervention from the Government of Canada, the Company’s continued pursuit of [Trans Mountain expansion] could endanger the Company’s ability to pay dividends to its equity holds and maintain its credit ratings.” (Ibid) They stated that without government intervention the company would need to take on billions of dollars of debt to fund construction of a pipeline whose future, and therefore the company’s ability to service this debt remained uncertain (Ibid). Requests were also put forward for the federal government to provide clarity and certainty on federal approvals that would show the supremacy of federal regulations over provincial initiatives in this area given the resistance of the BC government to the project. Finally, the company requested “a financial backstop that would keep Shareholders whole in the event of a stoppage or

suspension of the [Trans Mountain Expansion Project].” (Ibid) This was the first attempt by the company to seek government support and indemnification from the government.

The details of this indemnification were well constructed by the company and quite explicit in their request. Minister Carr agreed at this time that the federal government would work with the company in advance of Kinder Morgan’s April 2018 board meeting on the issues of concern brought forward. Meetings were therefore scheduled in person between representative of both parties to discuss potential legislative and judicial responses throughout the month of March. This escalated when during meetings on March 21st and 24th attended by Kinder Morgan, the Ministry of Finance and members of the Prime Minister’s office, Kinder Morgan presented a series of specific potential arrangements which included the government taking specific legislative and executive actions. This agreement included a proposal that the government provide what was termed as a backstop in which the federal government would agree to indemnify Kinder Morgan for all Trans Mountain expansion costs incurred in pursuit of expansion if the expansion project was abandoned by the company according to its own discretion (Ibid). This amounted to a direct request for indemnification of the company on the part of the Canadian federal government. While government representatives didn’t immediately agree to this proposal, the request on the part of Kinder Morgan is a significant recognition of the role that the federal government continues to play today in indemnifying the Canadian pipeline industry.

The explicit and detailed nature of this request shows how the industry structure facets outlined by Siegfried and Salamon can aid certain companies in securing government support. Their requests show recognition on the part of Kinder Morgan of

their own large firm size and market concentration of the pipeline industry in Canada enabling them to request something that would not be pursued by smaller companies in more crowded industries. Kinder Morgan as a large energy infrastructure company held significant lobbying ability. This combined with past government actions, a small geographic dispersion of the Trans Mountain pipeline compared to other pipeline proposals such as Energy East, and few other alternative options contributed to Kinder Morgan's ability to successfully negotiate with the government.

Kinder Morgan's requests then escalated and they requested indemnification through direct monetary investment in the project. Further meetings between Kinder Morgan and federal government officials on March 26 and 27 discussed the ability of the federal government to provide guarantees to the company. At this time the potential for Canada to become an equity investor in Trans Mountain Pipeline LP was brought forward (Ibid). While discussions were preliminary in nature, government officials stated a willingness to provide some form of indemnification, with conditions, that would compensate Kinder Morgan for pipeline expansion costs and potentially see the government takeover ownership of Trans Mountain to oversee expansion construction (Ibid). Kinder Morgan at this time further increased pressure on the government when on April 8, 2018 they announced that the Board had suspended all non-essential spending on expansion construction and that in light of BC's continued actions the company would not commit additional resources to the project. The company stated that they could not put Kinder Morgan shareholders at risk on the remaining amount the company would need to spend to continue moving forward with the project (Kinder Morgan 2018, 91). Following this, the Premier of Alberta Rachel Notley promised, "Alberta is prepared to

do whatever it takes to get this pipeline built – including taking a public position in the pipeline. Alberta is prepared to be an investor in the pipeline (Government of Alberta 2018).” Indemnification through direct monetary investment was very much on the table between Kinder Morgan, the federal government and the Alberta provincial government.

This then led to the final and most extensive indemnification act, in which the federal government purchased the Trans Mountain pipeline from Kinder Morgan. Clearly at this time negotiations were not going well between the two parties, and the federal government once again demonstrated their willingness to act as an indemnifier for the pipeline industry. Pressure to come to a deal increased between the federal government and Kinder Morgan, and although the government of Canada pushed for a backstop option on April 30 Kinder Morgan proposed that the government purchase the pipeline for \$6.5 billion. Canada instead proposed that the offer of a backstop could be made available to a private sector buyer of the pipeline and if none came forward then the Federal government would purchase the assets of the pipeline for \$2.3 billion plus a percentage of Kinder Morgan’s sunk costs (United States Securities and Exchange Commission 2018). Kinder Morgan’s board however rejected this proposal and despite negotiations having been publicly ongoing between the federal finance Minister Bill Morneau and Kinder Morgan for a month no deal had been reached. On May 16, 2018 Morneau stated publicly that the federal government would be willing to offer Kinder Morgan or any other future owner of the Trans Mountain project indemnity for any financial losses resulting from political opposition by the BC government who were putting up extensive protest and opposition to the project (Alini 2018). While further offers were made by the government to protect themselves from the full liability of

complete ownership none were accepted by Kinder Morgan until on May 23 Canada agreed to purchase the pipeline from Kinder Morgan outright. The Canadian federal government had fully indemnified the Trans Mountain pipeline project.

This decision to completely indemnify the pipeline did not get rid of the numerous issues facing its construction. On May 24, 2018, a group of municipalities, First Nations, environmental groups and the province of BC challenged NEB approval at the Federal Court of Appeal (National Energy Board 2019). Then only a few days later on May 29 Morneau made the announcement that Canada was purchasing the Trans Mountain pipeline for \$4.5 billion with Alberta contributing up to \$2 billion to cover costs resulting from any unforeseen circumstances that might occur (Canada 2018). Financing for the project was managed by the Canadian Development Investment Corporation, a holding company that owns and manages several crown corporations for the federal government). Notably Parliament was not required to review the federal government's decision because the purchase of the pipeline was paid for by the loan from one Crown corporation to another on request of the Minister of Finance (Parliamentary Budget Office 2019, 15). The pipeline despite having secured financing from the federal government continued to face numerous court and regulatory related hurdles that continue as of Spring 2020.

The Canadian government's decision to purchase Trans Mountain is key in light of what has happened to Kinder Morgan Canada, the Canadian subsidiary of Kinder Morgan, since its sale. Much can be learned that supports how an industry and company structure can help it secure government support for better or worse. Kinder Morgan Canada was spun off from its American parent in the mid-2017 to raise money to expand Trans Mountain (The Canadian Press 2019). However, after its sale Kinder Morgan

Canada announced the following May that it had decided to remain a stand-alone public company after a strategic review within the company which looked at whether the sale of part or all of the corporation should move forward. It was then announced in November of 2019 that Pembina Pipeline, a Calgary-based company was cleared by the Competition Bureau of Canada to buy Kinder Morgan Canada for \$4.3B (Ibid). This is key because at the time of its initial expansion proposal and the years thereafter the pipeline was backed by one of the largest energy infrastructure companies in North America (Otterbourg 2014). The company was not just large in size, but also one of the few that had the resources to put forward proposals of this scope. Other competing companies around 2013 had put forward their own proposals with Enbridge putting forward their Northern Gateway project crossing from Alberta to northern British Columbia and TransCanada putting forward the Energy East Pipeline which would go from Alberta east to New Brunswick (Hoberg 2013, 377). At the time of negotiation Kinder Morgan had a significant amount of sway on a government that felt the need to support the pipeline industry (Hoberg 2018, 4). These industry structure factors helped Kinder Morgan secure government indemnification.

Kinder Morgan used the proceeds from the sale of Trans Mountain to pay down existing debt and on January 3, 2019 the company distributed the net proceeds from the sale to its shareholders as a return of capital totalling approximately \$1.2 million Canadian (Kinder Morgan 2018, 91). The Canadian government as of early 2020 continues to own the Trans Mountain pipeline and has committed to spending billions expanding the pipeline despite continued cost overruns. On January 2020, the federal government stated that they will avoid selling the pipeline as long as political and legal

risks remain and until construction is completed (Rabson 2020), effectively continuing to indemnify the pipeline and with it the pipeline industry going forward.

Conclusion

CD Howe writing to the Minister of Finance during the 1950's stated, for all pipelines into new markets, a deficiency guarantee has always been required ... Unfortunately in Canada, no sponsorship other than the Canadian government exists which can assume responsibility for so large a project.

(Kilbourn 1970, 62)

Howe was speaking of the TransCanada pipeline, but the sentiment has continued since that time when it comes to pipeline construction in Canada. A federal government policy of indemnification for the pipeline sector has continued since TransCanada, leading to greater financial stability for the Canadian pipeline industry in Canada, but more risk and little reward for the Canadian taxpayer.

This thesis has shown that the federal government has supported the oil and gas industry through indemnification since the 1950's. It has done so by using process tracing to examine three test cases, the building of the TransCanada pipeline in the 1950's, the Line 9 pipeline from Sarnia to Montreal in the 1970's and the expansion of the Trans Mountain pipeline in the 2010's. In all cases the federal government worked with pipeline companies to provide not just monetary support, but help securing financing, clearing regulations and dealing with those who were against or expressed reluctance regarding the pipeline. This amounted to \$115 million in support to the TransCanada, almost \$250 million to support to Line 9 and just \$4.5 billion to outright purchase the Trans Mountain line to ensure the project moved forward. In today's dollars this amounts to the government supporting TransCanada in the amount of approximately \$1.102 billion and support for Line 9 equalling \$1.103 billion. The federal government tried to help both

TransCanada and Interprovincial to secure financing to build their pipelines, and the federal government used its own crown corporations to support both the TransCanada and Trans Mountain pipelines. Loans and guarantees against losses were discussed in the case of all three pipelines.

Indemnification in this thesis was defined as the government taking responsibility for the large-scale liabilities faced by the industry to guarantee its continued survival despite the fact that the sector has encountered significant ongoing issues. In all three cases looked at within this thesis the federal government acted as an indemnitor for the sector and the companies within it by protecting the risky projects pursued by companies. Oil and gas pipeline companies could build in the support of the federal government when taking risks because they had done it before for the industry. By examining these cases through the lens of indemnification what is typically used as a business and legal term becomes political and can be used to examine large-scale long-term government policy.

Throughout its chapters, this thesis has also shown how industry structure can provide an explanation for why the federal government's policy of indemnification of the pipeline industry has continued for the past 70 plus years. When looking at the five parameters brought forward by Salamon and Siegfried (1977), the TransCanada pipeline showed that a small industry size, large firm size and high market concentration encouraged the federal government to support the building of the pipeline. In TransCanada's case the lack of competitors to build the pipeline meant that the federal government was locked in to supporting one particular company despite financing issues and cost-overruns. However not all of the theories parameters hold to the ideal, in practice TransCanada was a paper company when it was first formed to build the pipeline, years

later it would post significant profits, but while it was lobbying the government it had very little money to its name. By the same token, the TransCanada pipeline had huge geographical span that covered over 2400 miles (Clark 1985, 99), but was successful gaining the support of CD Howe and the government it can be argued because of and not in spite of its size. The Line 9 pipeline showed that a large firm size, high profit rate and market concentration helped them maintain indemnification by the federal government. Additionally, the concentration of the pipeline helped to limit complications for the pipeline while still connecting a major population (Montreal) and industry sectors (Sarnia) in Canada. However, while the pipeline industry as a whole in Canada cannot be described as large, the growing of the Alberta extractive industry combined with the increased manufacturing and commercial uses for oil and gas as compared to the 1950's showcases how the industry size of the industry increased overtime. This does not seem to have significantly affected Interprovincial's ability to maintain government indemnification but does stray from what might have been a larger factor in another industry.

In the same way, for Trans Mountain the pipeline was supported in an environment in which Kinder Morgan was a large company in a concentrated industry with high profit rates trying to build a pipeline in a relatively concentrated geographical space. The ongoing medium size of the industry may however be explained by the perception of a growing need to transport oil and now and in the future. The fear of future oil shocks in the 1970's and the international oil markets that could be captured through pipeline expansion west may have superseded the growth of the industry. In these ways while the theory put forward generally provides an explanation for federal

indemnification of the pipeline industry, there are a few indices that do not fit exactly into the model.

There are a number of other possible explanations for government indemnification and support of pipeline projects overtime. First amongst them is the idea of pipeline projects as nation-building infrastructure projects and that government support of them is simply a way of Canada asserting its own nationalism by supporting this industry. This explanation fit best perhaps with the building of the TransCanada pipeline, as CD Howe the Canadian politician pushing the most for the pipeline often compared the building of the pipeline to the building of the railroad (Gray 1970, 56). This is however a harder sell for the Line 9 and Trans Mountain pipelines, and while talk of government support being “in the national interest” occurred it is difficult to determine if the pipeline was supported due to national interest or if national interest was used as an explanatory factor once indemnifying actions had already been decided upon (Harrison 2019). Another possible explanation is the influence of American economic influence on government support for pipeline construction within the country overtime. Many of the acts on the part of the United States in regard to pricing, capital, regulation and government policy precipitated indemnifying actions by the federal government of Canadian pipelines. This thesis did not look at any pipelines that crossed international boundaries, as it would have widened the scope of the project to an unmanageable size. However, examining this line of inquiry could lead to greater understanding of how and in what way government policies of indemnification take place. These explanations as well as examinations of factors that influenced government support beyond industry structure such as staples theory,

institutionalist explanations or a further examination of how international finance shapes large scale infrastructure and resource projects could prove fruitful.

The work in this project focused mainly on laying the foundation of providing support for the idea of indemnification as a concept to explain government support for private industry and showcasing how it has occurred in the context of the Canadian pipeline industry. Further work can and should be done to not only look at the role indemnification played in numerous other pipeline cases throughout Canadian history, but also the justifications and explanations for why that indemnification took place overtime. By examining examples of Canadian pipelines that either were not built or were built without government support a greater understanding and case for how a policy of indemnification shapes the industry can be drawn. As described earlier in this thesis while much work has been done examining the resistance to pipelines (Garneau 2016; MacNeil and Paterson 2018; Carter 2018) and the National Energy Board (Priddle 1999; Doern and Toner 2019) but in contrast little has been done to look at government support of pipeline projects in Canada from their inception and how this changes overtime. Examining all stages of the lifecycle of a pipeline can help to challenge common portrayals of the relationship between the pipeline sector and the Canadian federal government. By bringing business terms and concepts such as indemnification from business and law literature (Voigtmann and Clifford 2018; Rylands 2015), into the political realm non-political terms such as indemnification, risk-management and mitigation can be examined to paint a clearer picture of a government industry relationship.

When CD Howe wrote to say that all pipelines built into new markets had to be supported by the federal government, he could not have foreseen how long this policy would stay in place. The federal government's purchase of the Trans Mountain pipeline is not a once in a century event but a result of the long-term indemnification of the pipeline industry. To deny this reality is to fail to bring forward facts that are needed when critically examining the way that the pipeline industry works in Canada. This is true whether you are on the left trying to advocate for more public ownership of the means of production or on the right pushing for a free market approach to the economy. It is only when examining government indemnification policy over a long period of time that an accurate picture of how intertwined these entities truly are becomes clear.

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