31 viii 06
7800 words
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Political Culture and Petroleum Policy: Comparing Canada and Mexico under NAFTA [1]

Chapter for a section on the Culture of Political Economy and the Politics of Economics for a book on "*Political Culture and the Culture of Politics: A Transatlantic Perspective*" to be edited by Juergen Gebhardt and published by the Bayerische Amerika-Akademie, Munich, 2007.

Abstract

This chapter argues that the political economy of Canada – a country rich in resources but poor in economic development and technological capacity -- remains conditioned by its culture in three senses. First, its colonial experience of being protected by its imperial guardian left it ambivalent about its desire for economic autonomy. Its need for foreign markets for its raw materials, capital technology for its development, and immigrants for its growth left it disinclined to conceive and implement policies that would promote its economic self-sufficiency. Second, the decentralization created by the Canadian constitution, which gives provinces sovereign jurisdiction over their natural resources, when combined with the geographically uneven distribution of its resources, has created a sauve-qui-peut culture of individualism that makes the provinces the masters of their own destiny – for richer or for poorer. Third, the integration of major processes of cultural reproduction in those of the United States generates values that favour the inclusion of Canada within the North American hegemony.

The case of petroleum policy shows how, from its first discovery of petroleum, Canada -- in striking contrast with Mexico, which has similarly vast oil resources but a strikingly more nationalist political-economy culture oriented towards autonomy -- integrated itself in the US oil and natural gas economy; rejected Pierre Trudeau's flirtation with an energy policy promoting national autonomy; and accepted disciplines under the Canada-United States Trade Agreement which forfeited national control over the use of these resources.

Mexico's stubborn defence of its energy autonomy makes a striking contrast with its northern counterpart, although it remains under continuing pressure to conform to the deregulatory trend.

Globalization may be homogenizing many aspects of national politics but energy policies vary varies widely from country to country, as this chapter will illustrate in the case of the United States of America's two continental partners, Canada and Mexico.

Ever since January 1, 1994 when the North American Free Trade Agreement (NAFTA, 1994) formally brought Mexico into the political definition of "North America," political culture has become an essential concept for understanding the profound differences between the behaviour of the United States' two neighbours towards their continental hegemon. Understood as the historically constituted values of a society, political culture will be presented in this chapter as the

[1] Preliminary research for this article was done by Kate Fischer whose work in Washington DC during April 2004 was made possible by funds generously provided by the University of Toronto's Dean of the Faculty of Arts and Science. Funds from the Social Sciences and Humanities Research Council of Canada also made possible further research in Mexico City by the author in the winter of 2006.

independent variable that most powerfully explains the different contexts within which North America's two petroleum-rich peripheral states have developed their oil and natural gas industries. Whereas Canada will occupy pride of place in Part I, which outlines the historical determinants of its political culture, Mexico will enter the analysis after Part II has explained the continental integration of Canada's petroleum economy. NAFTA's energy provisions confirmed that, thanks to its more nationalist political culture, the weaker and poorer US neighbour had a stronger will and a more autonomous sense of national purpose for the use of its energy resources (Part III). A final section will show that the new American security state has changed little in the continent's dual bilateralism in the energy sector.

Part I The Political Culture of Canada's Economy

No better solution can be found to the puzzle why Canada is first-world in its standard of living but third-world in its economic structure -- exporting unprocessed raw materials while importing technology and finished products -- than in the brilliant perceptions of Harold Innis' staple theory.[2] Paraphrasing Canada's premier social scientist whose pioneering work dates from the 1930s, we need to distinguish the external determinants of Canada's economic dynamic from its internal features in order to understand how the processes of Canadian cultural reproduction favour its continuing integration within a larger hegemony.

1. The external determinants of Canada's economic dynamic

The globally determined features of Canada's political economy can be summed up under three categories, military, economic, and political.

A. Military. Canada has always been protected by its major customer. First it was the French navy and garrison which assured security for the *habitant* settlers of *la Nouvelle France*. Following General James Wolfe's defeat of his French counterpart Louis Joseph de Montcalm on the Plains of Abraham outside Quebec's ramparts, the British colonies of North America were protected from the expansionist United States by the *pax Britannica*. And ever since 1938, when Franklin Delano Roosevelt declared in Kingston, Ontario that an attack on Canada would be considered an attack on the United States, Canada has come under the protection of Uncle Sam.

The psychic effect of being protected is a high sense of security offset by a low need for autonomy. Consequently, Canada never equated state sovereignty with its capacity militarily to guarantee its own security or economically to achieve national self-sufficiency in the production of armaments.

B. Economy. Although the space now called "Canada" had harboured self-sufficient aboriginal societies for many centuries, its ability to host capitalist economic activity was from the 16th century a function of its being an extension of other economies. The development of the French, later British colonies of North America was generated by a syndrome of interconnected exogenous factors.

Foreign market. Canada has for ever been a land rich in resources, but its abundant supplies could not enter the capitalist economy without a prerequisite demand from abroad, whether this was a hungry Europe's appetite for fish, a fashion-conscious Paris' desire for fur, England's need for wheat, or US industry's voracious consumption of raw materials. There was a dark side to this

[2] Daniel Drache, "Introduction," in Daniel Drache, ed., *Harold A. Innis, Staples, Markets, and Cultural Change* (Montreal: McGill-Queen's, 1995).

relationship: should beaver hats fall out of fashion or should London abandon its Corn Laws, as it did in 1846, then the colonial fur trade or wheat economy would collapse.

Technology. Without the development of navigational techniques, European fishermen would not have been able to sail west to the Grand Banks to scoop up their teeming shoals of cod, dry and salt their catch in makeshift ports on Newfoundland's shores, and steer their cargo back to their European markets.

Some technology was locally developed. Originally, native trappers could not have brought their beaver pelts across vast distances to trade for European guns and whiskey without their tough but lightweight birchbark canoe. But overwhelmingly the new technologies that opened up successive staples for export came from abroad: the steam engine and steel made possible the railroads which brought wheat east to Atlantic ports or transported minerals south to the United States. There was a cost attached, of course, in the form of a continuing drain of licensing fees, patent charges, salaries for imported experts, and the many other ways that intellectual property could be commodified.

Capital. Staple development is capital intensive. The finances for outfitting a ship, building a railroad through the bush, or sinking a mine typically came from the economic Centre, often with explicit political sanction. The Company of Gentleman and Adventurers Trading into Hudson's Bay was an early joint stock company established by a British royal charter granting a monopoly of the fur trade in -- and practically sovereign reign over -- the entire region drained by rivers flowing into Hudson's Bay. Such domestic institutions as the Canadian Imperial Bank of Commerce grew up as financial intermediaries complementing the imperial capital markets' capacity to channel domestic savings into productive activity. As the Bank of Commerce's name implied, it's mandate supported the export of staples (commerce) within the empire rather than the development of domestic enterprise within the nation. Foreign capital was not cost-free either: interest had to be paid on bonds for specific periods, while dividends were paid out on portfolio investments for ever, and directly owned branch-plant operations were levied as many charges as imaginative head offices could invent.

In sum, two points need to be retained. While Canada's experience with capitalism has from the very beginning been as an extension of the global market, this production-generating connection with the outside world has always been mediated through the particular military, economic, political, and cultural power imperium in which Canada played at the time a subordinate part.

C. Polity. In the light of Canada's precarious integration in an imperial political economy, it is small cause for wonder that its economic, political, and media elites have been reluctant to cut their country's umbilical cord. This is not to deny that there have been significant movements towards autonomy, but Canada followed a very slow course towards political independence. The British North America Act of 1867, which is commonly understood as Canada's achievement of independence only granted the federated colonies control of their domestic affairs, a control that was qualified until after World War II by the Privy Council of the House of Lords acting as interpreter of the BNA Act's constitutional norms. Autonomy in its foreign policy was only achieved in the 1930s and final constitutional sovereignty only by 1982.

Economically, there have always been forces pressing to extract higher economic rents and diminish the charges levied by foreigners for their capital or technology. But these pressures have often been resisted. *Habitants* who made their own moulds in order to capture the value-added from turning beaver skins into hats had their moulds destroyed by the French colonial authorities. Generally, nationalist economic policies were developed only when the imperial market was closed. Only when the United States refused to renew its reciprocity agreement with Ottawa did the federal government led by Sir John A. Macdonald adopt a protectionist National Policy in 1879. In the aftermath of Nixonomics, the federal government led by Pierre Elliott Trudeau proposed a nationalist industrial strategy, the so-called -- and ineffectual -- Third Option. On the whole, the first preference of Canadian elites has been to maintain their economic umbilical cords, whether directly through trade or indirectly through staffing branches of imperial enterprises.

In short, integration has been Canada's first choice, autonomy a reluctant second.

2. The internal determinants of Canada's economic dynamic
Canadian political culture cannot be entirely explained by how it relates to its external context. Equally significant, and, in the case of petroleum, even decisively important have been the institutional, geographical, and demographic constituents of Canada's political reality.

<u>A. Institutions.</u> When Westminster sought to strengthen its remaining colonies in North America by federating them into a single political entity, it recognized the great distances that separated the Maritimes from British Colombia and the great cultural differences that separated a francophone, Catholic Quebec from the other Anglophone protestant colonies by granting the new provinces sovereign jurisdiction over certain policy fields, which fatefully included their natural resources. As the value of natural commodities increased, Canada's provinces have looked to their exploitation as the main source of their wealth, so have jealously guarded their exclusive right to promote their development.

<u>B. Geography.</u> With some exceptions such as its forests, the geography of Canada's natural resources is highly uneven. Crucially important for Canada's oil and natural gas policies, some 80 percent of its petroleum resources are located within the boundaries of the country's westernmost prairie province, Alberta.

<u>C. Demography.</u> What makes Alberta stand out further from its counterparts is having been settled at the turn of the 20th century primarily by Americans who were pushing on from the northwest US states in search of a last frontier where they could establish their homesteads. While Alberta also received immigrants from Ontario and the Ukraine,[3] it was the large influx from south of the border that made Alberta's population the most American of all the provinces and imprinted on its political culture its distinctively fundamentalist, anti-centralist, and populist values.

3. The processes of Canadian cultural reproduction
Since economic and political interests are subjectively constructed rather than objectively given, how a country's values are articulated is ultimately determined by how its institutions of cultural reproduction operate. It is not enough to affirm that Canadian values have been largely determined over time by Jesuit missionaries from France, English teachers from Oxford, or American professors trained in Ivy League colleges. To be sure, immigrating professionals bring their conceptual systems with them, but naturalizing forces can turn foreign ways of thinking into national systems of thought, as the theoretically original work of Harold Innis's generation demonstrated.

Although the education system is maintained primarily by the public sector, so that pupils and students are taught by teachers and professors who are mainly formed within the country,

[3] I am indebted to Prof. Barry Cooper for this point.

Canada’s other institutions of cultural reproduction have been historically integrated with those of the dominant partner. Having passed through a phase when governments promoted nationally owned publishing houses, Canadian book publishing and distribution remains a small fraction of this industry. The more elitist and least profitable cultural sectors -- dance, opera, classical music, live theatre -- remain in Canadian hands and survive thanks to public subsidy. But for the more profitable, mass-directed media -- from magazines to movies, from radio to television -- Canada is but a northern extension of the American entertainment market, including its advertising, public relations, and consulting branches. Moderate Canadian content rules for AM and FM radio support Canadian popular musicians, but North American intellectual property rights push Canadian singers to make their recording with international labels. Strict ownership laws keep Canadian newspapers under national proprietorship, but the international news which Canadians read is largely filtered through American wire services.

When the country's international economic position and its domestic structures are placed in the context of these cultural processes, it is not hard to understand how Canadian political culture continues to reproduce integrative values favouring the export of unprocessed raw materials and minimizing concerns about the control of key economic sectors by US transnational corporations.

This is not to deny the recurrence of nationalist surges at moments in Canadian political history when there has sometimes been significant pressure for autonomy within the empire of the day, but the country’s leadership has generally taken integrative positions, whether they were labeled "imperialist" a century ago for those wanting to maintain Canada within the bosom of the British empire or "continentalist" for those preaching an ever-deepening integration of Canada's political economy within that of North America. It is to Canada's petroleum integration in the continent that we will now apply this analysis.

Part II The Politics of the Canadian Petroleum Economy

If a nation state is one which exercises its militarily enforced sovereignty over the society, economy, and culture within the territorial confines of its national frontiers, Canada can hardly be considered ever to have achieved nation-state status before the forces known as globalization introduced it to new forms of transnational interdependence. It spent far more time as a pre-national state, having passed, during the first decades of the 20th century, from dependency under the aegis of the British empire to satellitic membership in the American hegemony. In the particular case of the petroleum industry, the vicissitudes of Canada's energy policy reveal that, after a brief flirtation with a nation-state energy paradigm, it moved easily into the era of post-national policy-making.

1. Petroleum and Canada as a Pre-National State

When large deposits of oil were discovered in Alberta in the 20th century, Canada's historic openness to foreign capital explains how easily the existing Canadian oil companies were taken over by the US oil giants. The location of these companies’ head offices in the US southwest combined with Alberta's American demographics also makes it easy to understand how the province looked to Texas and Oklahoma for a model when confronted with the need to develop a regulatory framework for this new industry.

When further massive reserves were discovered in LeDuc, Alberta in 1947, the Cold War was just getting underway. With the Paley Report informing official Washington in 1952 that Canada was a secure resource base for many of the strategic raw materials needed for its new struggle with the Soviet Union, Congress legislated incentives to encourage US firms' exploration and development activity north of the border.

When for its part the Progressive Conservative government of Prime Minister John Diefenbaker set up a commission to recommend how to frame a national policy on petroleum, it seemed perfectly normal that, under advisement from the US Department of State, American transnational oil corporations should have played a major part in recommending how Ottawa should proceed. Concerned that the Venezuelan government might nationalize the oil reserves then owned by Esso, State wanted Canada to import for its central and eastern market this oil which US protectionism excluded from the American market. In return, Alberta's oil, which could supply Western Canada, would be granted special exemption from US petroleum tariffs so that it could satisfy the oil and natural gas needs of the northwestern states. Accordingly, Diefenbaker's 1961 National Oil Policy divided the Canadian market into two segments, making Ontario, Quebec, and the Atlantic provinces vulnerable to the price and supply conditions of the world market.

Petroleum continentalism worked smoothly through the 1960s, with the Canadian National Energy Board working closely on regulatory issues with the US Federal Power Commission. In 1970, George Shultz updated the Paley Report's advice that the United States move to secure its energy supplies and recognize Canada as a low-risk, reliable, strategically important energy partner. Notwithstanding his personal differences with Prime Minister Pierre Trudeau, President Richard Nixon embraced the Shultz Report and declared that imports of oil and natural gas -- along with hydro-power and water -- from Canada would save the United States from its looming energy crisis.[4] It took massive disruptions of the global oil economy to disturb this intimate relationship and push Canada into a brief stormy period in which the federal government tried to turn petroleum to national, rather than continental ends.

2. Petroleum and Canada as a Nation State

The power structure of this informally institutionalized régime came under strain for a decade once the cartel formed by the Organization of Petroleum Exporting Countries (OPEC) quadrupled world oil prices in 1973. To Washington's dismay, the Trudeau government responded to this first OPEC-induced energy crisis by debating whether it could sustain its export volume of a non-renewable resource whose reserves were diminishing. It also took concrete action by raising the price it charged US customers for its petroleum to that of the world market so that it could finance its imports from offshore. At the same time it maintained domestic prices at a lower level, causing Americans to claim that Canada was using its cheaper oil as an industrial input to compete unfairly with US manufacturers.

After several years of growing concern about its energy security and following OPEC's redoubling world prices in 1979, the re-elected Trudeau government launched the National Energy Program (NEP) in November of 1980 to reduce its energy interdependence. With an ambitious medley of interventionist measures, it promoted the pan-Canadian market at the expense of cross-border trade in order to make eastern Canada's economy less vulnerable to fluctuations of the world price and supply of oil and to assure Canada's autonomy by expanding Canadian ownership of the predominantly US-owned industry.[5]

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4 Paul G. Bradley and G. Campbell Watkins, *Canada and the US: A Seamless Energy Border?* (Toronto: C.D. Howe Institute, 2003), 60.

5 Carman Neustaedter, *The National Energy Program* http://pages.cpsc.ucalgary.ca>; Internet, accessed November 8, 2003.

Within a few months, an outraged American oil and gas industry, which had been major a backer of Ronald Reagan's recently successful campaign to oust Jimmy Carter from the White House, placed mounting pressure on the newly elected president to resist the NEP, which it considered to have violated its fifth amendment rights in Alberta by favouring Canadian petroleum companies. For its part, Congress made clear its dissatisfaction with the spectacle of mid-size American oil and gas companies being taken over by prospering Canadian firms on both sides of the border.[6]

The NEP marked a belated attempt by the Canadian government to act as a nation state by achieving petroleum autonomy through forcing oil and natural gas into a national mould at the cost of a partial withdrawal from its extensive north-south integration. During its eighteen months of existence, Canadian ownership in the industry jumped from 6.7 percent to 34.7 percent.[7] Given that the NEP was crafted with almost no provincial or industry consultation, it also created a political backlash from the energy-exporting provinces and private sector in Canada, particularly in the oil- and gas-rich Alberta.[8] In the end, it was collapsing world oil prices that caused the NEP to unravel, but the mutual interests of the Trudeau and Ontario governments in energy nationalism were no match for the combined power of President Reagan's government in Washington, Premier Peter Lougheed's government in Edmonton, and the incensed petroleum industry on both sides of the Canadian-American border -- all demanding a return to the status quo ante OPEC.

By 1982, the federal minister of energy, Jean Chrétien, was dismantling the NEP's mistimed measures.

3. Petroleum and Canada as a Post-National State

By the early 1980s, advances in information technology were enabling corporations to transnationalize their production, marketing, and financing. As a result, nation states were losing control over their own market space. In order to re-capture some of their economic control, states were reconstituting themselves in regional groupings with their geographical neighbours.

Despite this little move towards regionalism, when, in his 1980 election campaign for president, Governor Ronald Reagan proposed a "North American accord," he caused consternation among his continental neighbours. But the fat was already in the fire. Reagan's proposal was a manifestation of Washington's current obsession about the United States' hegemonic decline in the face of growing competitive pressures coming from a resurgent European Community, an expansionist Japan, the state-led technological brilliance of the "new dragons" of southeast Asia, and even fundamentalist Iran whose militants had humbled the United States by taking its diplomats hostage.

The United States' globally competitive, knowledge-based industries and service sectors believed they were losing out because their intellectual property was being pirated abroad or they were being denied permission to operate in foreign jurisdictions' state-controlled sectors. For their part, less competitive US industries were demanding that Congress provide them with even greater protection against what they deemed unfair competition from importers benefiting from foreign-government subsidies and other manifestations of what they deemed to be unfair practices.

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[6] Stephen Clarkson, *Canada and the Reagan Challenge* (Toronto: Lorimer, 2nd. ed. , 1985), 57, 75.
[7] Ibid, 82
[8] Monica Gattinger, (2005) "From Government to Governance in the Energy Sector: The States of the Canada-US Energy Relationship," *American Review of Canadian Studies* 35:2, 325.

Normally such issues would provide the stuff of intergovernmental negotiations at the continuing rounds of the General Agreement on Tariffs and Trade. But because the GATT had become known as the General Agreement to Talk and Talk for its interminable efforts to forge a consensus, Washington added a third prong to its traditional, two-level trade-policy strategy. If multilateral talks at the GATT showed little promise in the mid-1980s and if unilateral actions targeting individual trading partners with retaliatory measures proved counterproductive, there was an intermediate position. Bilateral agreements with compliant partners could set precedents that established the norms Washington wanted to universalize, putting on the wall writing which more recalcitrant competitors would ultimately have to read -- and heed.

The United States' desire to transform the domain of international intellectual property rights, to strengthen the guarantees protecting for US transnational corporations operating abroad, and to extend trade-rules to cover services required a counterpart need on behalf of potential negotiating partners.

This condition was met on Washington's two borders when the Canadian business community reversed its position concerning its own competitive dilemmas and when the ruling party in Mexico reversed its position favouring autarchic industrialization.

<u>Canada-United States Free Trade</u>

Ever since the mid-1970s, when Canadian direct investment abroad had begun to exceed foreign direct investment in Canada, business elites had started talking a less protectionist language. A devastating recession in the early 1980s, an increase in the US protectionist measures taken against Canadian exports, and general hostility towards the deemed Keynesian policies of Pierre Trudeau's Liberal government combined to give political credence to the dramatic recommendation to embrace free trade with the United States that was made in 1985 by the report of the Macdonald Royal Commission on the state of the Canadian economy.

In the Macdonald Report's analysis, Canada's future economic prosperity required enhanced and secure access to the US market. “Enhanced” meant trade free of tariffs. "Secure" meant trade unthreatened by antidumping duties, countervailing duties, or the legion other measures that Congress had perfected over the years to protect its uncompetitive industries. With these two objectives as its major goals, the Mulroney government initiated one-on-one palavers with the world's toughest trade negotiators

Given the disparity in power between the two sides, it would not have surprised an outside observer that the US agenda prevailed over the Canadian. While tariffs were lowered (Canada's more than the United States'), Ottawa failed to achieve its prime goal, exemption from US trade protectionism. As a result, CUFTA did not produce the free cross-border trade to which the Mulroney government had aspired. However, this document, which Ronald Reagan called the "economic constitution of North America," did resolve many of Washington's irritants with Canada, its energy concerns *primus inter pares.*

CUFTA locked in the already deregulated nature of trans-border energy flows by establishing norms that would prevent a future Canadian government from affecting the price or supply of its petroleum exports to the US. With the Canadian state’s powers curtailed by this new external constitution, [9] market forces of supply and demand would be free to govern cross-

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[9] For an elaboration of the argument that continental free trade agreements combined with the World Trade Organization comprise an external constitution for its member-states, see Stephen Clarkson, “Canada’s

border energy trade. The willing compliance of the Mulroney government with these pro-market provisions facilitated bilateral relations by privileging US energy-security concerns and the petroleum industry's bottom-line desire for profit maximization over any pan-Canadian interest in energy security and cheaper energy for citizens' needs and domestic industrial inputs.[10]

The US Energy Policy Act of 1992 subsequently served as the fountainhead for the natural gas sector's further liberalization through the Federal Energy Regulatory Commission (FERC) Order 636, which mandated the unbundling of vertically-integrated gas utilities to allow more private-sector participation through wholesale competition, access to pipeline infrastructure, and market-based pricing.[11]

Although CUFTA allowed export restrictions in cases of conservation of exhaustible resources, supply shortages, price stabilization, and national security,[12] the Canadian government has chosen not to invoke these conditions. Instead, it voluntarily relaxed its regulation of energy trade.

CUFTA gave it little choice, because Canada had agreed to a "proportionality" clause to assure the United States that it would not face another period like that from 1973 to 1982. The proportionality provision in Article 605, which requires that in any export restrictions justified on the basis of conservation, price stabilization, and supply shortage, "the share of total supply available for export purchase may not fall below the average level in the previous 36 months."[13] In other words, no country may reduce the *proportion* of the energy or petrochemicals it exports to the other party. Should Canada raise production in an effort to offset world energy shortages, it would be forced to increase exports to the United States in order to maintain the export proportion. Likewise, should Canada decide to undertake initiatives to increase energy conservation or be faced with energy shortages, it would be unable to cut exports to the United States by a greater proportion than the reduction of its own domestic usage. However, this proportionality clause refers to actions taken by governments restricting exports, not to market forces that serve to limit exports. This means that the Canadian -- or Chinese -- market could potentially out-bid Americans even for more than their proportional share of Canadian energy.[14]

Further evidence that CUFTA achieved Washington's goals with Canada, thus increasing its dominance can be found in the interesting contradiction between the principle of national treatment (which forbids industrial subsidies) and article 608 (1) -- which mandates them for energy development. By having CUFTA extend the notion of nondiscrimination between domestic and foreign *goods* to apply to *investment*, Washington achieved an important precedent. It had long been trying to prevent foreign governments from pursuing industrial-strategy policies which boosted the competitive capacity of their corporations by offering them public subsidies and incentives unavailable to US companies. By accepting the principle of national treatment for investment, Ottawa gave up its long-treasured capacity to promote Canadian corporations in the face of competition from much bigger foreign transnational corporations.

External Constitution under Global Trade Governance," in Ysolde Gendreau, réd., *Dessiner la société par le droit/Mapping Society Through Law* (Les Éditions Thémis, CRDP, Université de Montréal, 2004), 1-31.

[10] Gattinger, (2005) "From Government to Governance in the Energy Sector," 325.

[11] Natural Gas Supply Association. "The Market under Regulation: Important FERC Regulations and Orders." available at <www.naturalgas.org/regulations/market.asp>

[12] Steven Globerman and Michael Walker, *Assessing NAFTA: A Trinational Analysis* (Vancouver: Fraser Institute, 1993), 207.

[13] Ibid.

[14] Ibid, 208.

In the case of energy, however, Article 608(1) states that nothing in the trade agreement is meant to constrain "future incentives for oil and gas exploration, development and related activities in order to maintain the reserve base for these energy resources." Where subsidies would bolster the Canadian capacity to compete with US corporations, CUFTA prohibited them. Where subsidies would bolster US energy security, CUFTA endorsed them. To maintain their reserve base, 608(2) also commits Canada and the United States to sharing their energy reserves in case of emergency.[15] As the energy provider in this relationship, this apparently reciprocal clause created a future commitment for Canada to pump up its exports in case of Uncle Sam's needs in a crisis.

CUFTA contributed to the full liberalization of Canada's upstream (exploration and production) gas market.[16] Even though the National Energy Board is still meant to allow the export only of gas that is surplus to Canadian needs, in practice, now that it is headquartered in Calgary, it lets exports be governed by market demand and supply with no thought to husbanding Canadian resources for a future date when reserves became exhausted.[17]

Article 609(1), which defines an energy regulatory measure as behaviour by "federal or sub-federal entities that directly affects the transportation, transmission, distribution, purchases, or sales of an energy or basic petrochemical good"[18] ensures that sub-central jurisdictions come under the aegis of the new super constitutionalism,[19] thus compromising provincial and state autonomy over energy resources even in areas beyond federal government jurisdiction. With the Canadian constitution placing resources under provincial jurisdiction and with Alberta as the major energy producing province, taking the lead in promoting deregulation and privatizing the downstream (distribution and pricing) side of the market,[20] this loss of autonomy is moot. Alberta produces 80 percent of Canada's natural gas and issues licenses for all gas that is removed from the province but, true to its continentally conscious political culture, it does not distinguish between gas for export to the United States and gas for inter-provincial trade.[21]

In the natural gas sector, Canada and the United States have demonstrated an impressive capacity to plan and invest cooperatively: witness the massive Alliance Pipeline, a bilateral venture that stretches 2,300 miles from western Canada to Chicago.[22] The regulatory boards in both countries, FERC and the NEB, cooperate so closely that they hold joint hearings on proposed cross-border projects. This bilateral governance functions so cohesively that it is almost as straightforward to seek approval for a trans-border pipeline as it is for a domestic US trans-state pipeline or a Canadian inter-provincial one. Current gas transportation infrastructure reflects this integration, as there now exists an essentially seamless border between the United States and Canada, with pipelines crisscrossing the 49th parallel. As described by FERC Chairman, Pat Wood, "You look at a pipeline map of North America [without Mexico] and it's just no boundaries."[23]

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15 Ibid, 210.
16 International Energy Agency, *Canada 2000 Review*.
17 Bradley and Watkins, *Canada and the US,* 7.
18 NAFTA, 609.1
19 Globerman and Walker, *Assessing NAFTA*, 209.
20 International Energy Agency, *Canada 2000 Review*.
21 Ibid, 11.
22 Pietro S. Nivola, "Energy Independence or Interdependence? Integrating the North American Energy Market." *The Brookings Review*. Washington, Spring 2002, 20, 2.
23 Donald F. Santa, quoting Chariman Wood. "New Challenges in the Integrated North American Energy Market." Speech at the Energy in the North American Market Conference, 12 June, 2003. Available at <www.canadianembassy.org/trade/santa-en.asp>

Bilateral oil and gas flows between Canada and the United States since the 1980s have mostly been southbound from Canada into the United States. As indicated in Table 1, the United States does export energy to Canada, its natural gas exports having increased tremendously between 2000 and 2004. Nevertheless, Canada remains an overall energy exporter to the United States, increasing its exports from 455,000 barrels of petroleum per day in 1980, to 2,072 in 2003, and from 797 billion cubic feet of natural gas in 1980, to 3,490 in 2003. This leaves the United States dependent on Canada for over 27 percent of its net energy imports.[24]

By 2003, Canada exported to the United State about 60 percent of its annual oil production and over half of its natural gas,[25] making Canada the United States' single largest petroleum supplier. In contrast, Canada only provided 15 percent of US natural gas needs, in 2003, but this represented 87 percent of total US natural gas imports.

Table 1: Canada-United States Oil and Gas Trade, Selected Years, 1980-2003[26]

	Imports to US from Canada				US Exports to Canada			
	1980	1990	2000	2004	1980	1990	2000	2004
Petroleum (thousand barrels per day)	455	934	1,807	2,118	108	91	110	141 (2003)
Natural gas (billion cubic feet)	797	1,448	3,544	3,607	0.1	17	73	395

Source: United States Energy Information Administration, *Annual Energy Review 2003,* Natural Gas Navigator and *Petroleum Supply Annual 2003.*
Notes: Electricity data from 2003 are preliminary.

Part III The Politics of the Mexican Petroleum Economy

The second stage of the United States' regional regrouping allowed it to expand its informal continental hegemony in order formally to include Mexico once that country's ruling Partido Revolucionario Institucional (PRI) joined the counterrevolution.

Long the champion of import substitution industrialization, the PRI had created since World War II a semi-autarchic system based on high tariff walls, pervasive state intervention in the economy through public enterprises, and a corporatist engagement with peasantry and proletariat, which helped in exercise near-total political control. Faced by a devastating financial crisis in the early 1980s, which made it dependent on the International Monetary Fund's mercy, the PRI's leadership changed direction and steadily opened the economy to the world, negotiating its entry into the GATT and the OECD, the price for which was further commitments to liberalize internal economic controls -- with the notable exception of energy.

The importance of energy in Mexican politics can be traced back to the 1917 Constitution,[27] whose Article 27 declared the exploration, exploitation, development, and sale of oil and gas (and the generation, transmission, and distribution of electricity) to be exclusively

[24] North American Energy Working Group. *North America—The Energy Picture.* 2002. Gattinger. "From Government to Governance in the Energy Sector."
[25] Bradley and Watkins, *Canada and the US*, 3.
[26] Gattinger. "From Government to Governance in the Energy Sector."
Bradley and Watkins, Canada and the US, 6.
[27] Globerman and Walker, *Assessing NAFTA*, 206.

under the control of the federal government.[28] Mexico's nationalist approach to its energy sector was further entrenched by what was seen as its second declaration of national control over its economic development,[29] the 1938 nationalization of foreign oil and gas properties and the establishment of a state-owned oil and gas company, Petroleos Mexicanos (Pemex), to manage its petroleum destiny.

Throughout the Cold War, Pemex continued to ship oil northwards to the American market -- in 1991, crude oil was Mexico's second most important export[30] and comprised 14 percent of its total exports to the United States[31] -- but US capital was largely excluded from returning to its pre-revolutionary haunts and reintegrating Mexico's energy market through transnational corporate networks.

Pemex explores for and develops Mexico's petrochemical reserves, including the management of the downstream facilities needed to refine and market them.[32] It is the country's largest corporation, has the largest union in the country,[33] and is a vital source of tax revenue, as it is legally required to transfer up to 30 percent of its earnings to pad the federal government's budget.[34] (Official figures suggest that Pemex supplied 37 percent of government revenues in 2002, but unofficial estimates run as high as 70 percent.[35]) Several ministries share jurisdiction over Pemex and the oil and gas sector, the most important being the *Secretaría de Energía, Minas e Industria Paraestatal* (SEMIP), which oversees the energy sector and is responsible for energy policy.

Until the 1980s, Mexicans' nationalist political culture led successive governments to protect their energy sector from the United States and resist its political dictates and policy trends. Subsequently, as the Mexican economy liberalized and expanded the space open for private investors, PRI governments have attempted to shift their energy policies towards greater private sector governance. In response to these pressures, Pemex reduced its workforce from 210,000 to 100,000, between 1989 and 1995.[36]

Because the Mexican government has siphoned off so much of Pemex's profits to pay for state programs, Mexico has not developed the capacity to refine its petroleum into the derivatives it needs for its own economy. For example, Mexico is a net importer of natural gas from the United States (Table 2) and also imports refined petroleum products such as gasoline because it lacks the financial capacity and/or technical expertise to develop the facilities needed for refining its sour, heavy crude oil. These limitations, coupled with increasing demand projections, create further pressures for more private and foreign investment and greater deregulation.

Table 2: Mexico-US Natural Gas and Petroleum Trade, 1980-2004

[28] North American Energy Working Group, *North America, subsection Mexico, General Outlook.*
[29] Ibid, 7.
[30] Ibid, 32.
[31] Globerman and Walker, *Assessing NAFTA,* 8.
[32] The Canadian Energy Research Institute, *Towards a Continental Natural Gas Market: The Integration of Mexico,* (Calgary: The Canadian Energy Research Institute, 1995), 36.
[33] Ibid.
[34] Nivola, "Energy Independence or Interdependence? Integrating the North American Energy Market"
[35] Interview with Gerardo Bazan, Director del Programa universitario de Energía en la Universidad Nacional Autónoma de México, May 28, 2003.
[36] The Canadian Energy Research Institute, *Towards a Continental Natural Gas Market*, 36.

	Imports to US from Mexico				US Exports to Mexico			
	1980	1990	2000	2004	1980	1990	2000	2004
Petroleum (thousand barrels per day)	533	755	1,373	1,642	28	89	358	209
Natural gas (billion cubic feet)	102	0	12	0	4	16	106	398

Source: Adapted from United States Energy Information Association, *Annual Energy Review, 2004*

Although more reluctant than Mulroney had been -- President Salinas de Gortari had hoped to achieve economic salvation through an agreement with the European Union – the Mexican government came to negotiate a trade and investment agreement with the United States following its own belief that its economic development model had reached an impasse. Unless Mexico gained special access to the US market, the ruling party's technocratic elite believed it would not be able to extricate itself from the economic morass created by what it considered was the exhausted import-substitution-industrialization model of the post-World War II era.

Once Brian Mulroney discovered President George H. W. Bush negotiating with Salinas, he desperately lobbied to take part in the trade talks lest Canada lose what advantages he felt had been gained from CUFTA. It was in this way that North America was redefined through the signing of the North American Free Trade Agreement (NAFTA) to include Mexico.

Although NAFTA's Chapter 6 put a veneer of common governance over the continent's petroleum sector, it actually disguised the perpetuation of two separate bilateralisms. Chapter 6 reiterated Canada's CUFTA commitments to a deregulated, integrated, free-market economy.[37] The US Undersecretary of State, Alan Larson, confirmed this reality when describing the integration of the North American energy system, saying that, more important than the geographic proximity of the three nations, "is *the rule of law* and predictable investment conditions created by NAFTA, integrated pipeline networks, close cooperation between our governments and energy companies, and long-term, reliable supply relationships."[38] However, the law that ruled energy matters to the south of the Rio Grande remained Mexican, because, during the negotiations that led to NAFTA, the United States failed in its attempt to loosen Pemex's monopoly hold over the country's oil and gas sectors.[39]

Mexico made fewer energy-policy concessions in NAFTA than had Canada by negotiating significant exemptions from its disciplines. The first article of Chapter 6 stated that, "The Parties confirm their full respect for their Constitutions"[40] (which was code for asserting the continuing imperatives of Mexico's Article 27) and consequently recognized that Mexico retained the right to full national control over the exploration and exploitation of oil and natural gas, along with associated activities such as refining and foreign trade.[41] However, private participation in cross-border trade was accepted by the Mexican government subject to its approval and Pemex's continuing control: "Where end-users and suppliers find cross-border trade may be in their interests, [they] shall be permitted to negotiate supply contracts…[with] the state enterprise."[42]

[37] Ibid.
[38] "Cellucci Urges Continental Energy Market," *Energy Processing Canada.* Author's emphasis.
[39] The Canadian Energy Research Institute, *Towards a Continental Natural Gas Market,* 35.
[40] NAFTA, 601.1.
[41] Globerman and Walker, *Assessing NAFTA,* 3.
[42] Ibid*,* 210.

The national-security exception, which is recognized as an appropriate reason for energy-export restrictions in international economic law, is defined differently in NAFTA for Canadian-American relations than for Mexico's relations with the other two signatories.[43] Canada negotiated a narrow definition of national security to protect itself against the United States invoking its security as a justification for imposing arbitrary import restrictions.[44] Article 605 gives Mexico the right to restrict exports or imports any time it is deemed necessary to protect what is broadly defined as Mexico's "essential security interests."[45]

These differing rules over national security confirm how the energy sector continues to be governed by two separate political cultures. This skewed nature of the two bilateralisms could also be seen in the proportionality provision of the Canadian-American agreement to which Mexico subsequently took an exemption in NAFTA, so that it still only applies to the United States and Canada.

Overall, natural gas is the most deregulated part of the Mexican energy sector. Efforts to privatize Pemex's gas operations began in 1995, when federal legislation opened natural gas storage, transportation, and distribution to private and foreign investment and allowed private companies to export and import this fuel. As a result, the gas pipeline infrastructure between Mexico and the United States has a small number of private pipelines crossing the Mexican-US border. There are currently eight gas pipelines running across the US-Mexico border that connect with both Pemex's supply pipelines (which account for 85 percent of current capacity) and a few privately owned connections into north-west Mexico.[46] Pemex still controls the upstream gas sector, but midstream and downstream activities are fully open to private competition, subject to the limitation that private companies can only be involved in one function.[47]

For economic and environmental reasons, Mexico's current energy policy commits it to increase its use of natural gas over other fuels, putting even more pressure on the government to seek private and foreign investments. However, under the Regulatory Act of Constitution Article 27 on Petroleum, "the exploration, extraction, production activities, and first-hand sales" of natural gas are still considered strategic and thus protected, whereas only "construction, operation, transportation, storage, and distribution" are open to private participation.[48] Under these restrictions, Pemex has made efforts to ally itself with international oil and gas corporations, launching a joint-venture refinery with Royal Dutch/Shell.[49]

The cause of liberalization was boosted by the first ever meeting between FERC and its Mexican counterpart, the *Comisión Reguladora de Energía* (CRE), in February 2003. A further step towards energy liberalization in Mexico can also be seen in the government having reduced the number of 'basic' petrochemicals (which are constitutionally reserved for state control) by reclassifying them as secondary (and therefore opening them to private participation), thus shrinking the number of basic petrochemicals from fifty to eight.[50]

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[43] Ibid, 207.
[44] Ibid, 208.
[45] Ibid, 208.
[46] Joseph M. Dukert, "North American Energy Interdependence—A Critical Survey," U.S. Association for Energy Economics' *Dialogue* (April, 2002), 16. http://www.usaee.org
[47] Fossil Energy International, "An Energy Overview of Mexico," available at <www.fe.doe.gov/international/mexicover.html>.
[48] North American Energy Working Group, *North America, subsection Mexico, General Outlook*.
[49] "Pemex Chief Says Company Needs Boost." *Washington Post*. February 2, 2004. Online Edition, <www.washingtonpost.com/wp-dyn/articles/A6806-2004Feb2.html>
[50] Ibid.

As President Fox discovered when he announced his measures to privatize Pemex, efforts to increase privatization in the energy sector meet fierce public and political hostility.[51] Despite the president's willingness to comply with US demands, it remains questionable how far the Mexican government will be able to go in privatizing what is treasured in Mexican political values as one of its few remaining national industries. Fox lacked the two-thirds support needed to amend the Constitution and introduce the US model of sweeping energy reforms.

Privatization and deregulation have reached their constitutional limit, leaving Mexico's oil and gas sector by far the most nationally-contained and strictly-governed in North America. In the congressional assembly that took place in 2005, PRI deputies even called for the expansion of state-ownership and governance over the energy sector,[52] affirming the need to strengthen Mexico's autonomy in the face of Fox's attempt to introduce private-sector control. The lack of political will to restructure Pemex's output abilities and increase its revenue, means that, unless the government leaves Pemex its revenues for reinvestment, it will not be able to keep up with increasing domestic consumption.[53]

Part IV North America's Dual Bilateralism under Pressure from the Security State

Although NAFTA's notionally trilateral umbrella disguised two completely separate sets of bilateral energy relationships, the United States has been pressing for a harmonization that will give it more access to Mexican petroleum supplies. Using the same logic as the 1952 Paley Report, Vice President Dick Cheney's 2001 National Energy Policy advocated energy integration and a tripartite energy framework "to expand and accelerate cross-border energy investment, oil and gas pipelines, and electricity grid connections."[54]

This pressure emanating from Washington pushed its two neighbours to formalize cross-border integration planning and envisage a clear regulatory framework for making infrastructure investment decisions. Actual North American energy cooperation was advanced in April 2001 when the three heads of government created the trilateral North American Energy Working Group (NAEWG) at the Summit of the Americas in Quebec City. Building on the already established bilateral yearly energy consultations between United States and Canadian representatives, as go in the sure will he was waiting for a the NAEWG was given a mandate to "foster communication and cooperation among the governments and energy sectors of the three countries on energy-related matters of common interest and to enhance the North American energy trade interconnections consistent with the goal of sustainable development, for the benefit of all."[55]

Still in its infancy, the NAEWG has so far only been engaged in sharing energy data. In 2002 in published a continental self-portrait showing with common statistical units where each country stood in its energy resources, production, consumption, infrastructure, and future requirements.[56] In the winter of 2006 it updated that snapshot in a second, trilingual 94-page

[51] "The Americas: Where Energy is Sacred; Reform in Mexico," *The Economist*, 364 (London, July 13, 2002), 48.
[52] Enrique Andrade Gonzalez, "Mexico Still Hopes for Energy Reform," *Mexidata.info,* Monday, March 14, 2005. [http://www.mexidata.info/id420.html]
[53] Sidney Weintraub, "Mexico's Oil, Gas, and Energy Policy Options," *Issues in International Political Economy,* no. 68, August 2005.
[54] National Energy Policy, 14.
[55] North American Energy Working Group, *North America.*
[56] North American Energy Working Group, *North America -- The Energy Picture* (June 2002).

report[57] which showed that progress in cross-border energy cooperation had been incremental in the intervening four years.[58]

When the September 11th terrorist attacks placed national security at the forefront of the US policy agenda, the United States government became even more determined to maximize its domestic energy security and take greater advantage of its periphery's energy supplies.

Further official action was taken in March 2005, when the three heads of government recognized and responded to the blow to North American economic development that had resulted from the post-September 11, 2001 shift by the United States to a security paradigm. In their Security and Prosperity Partnership for North America (SPP) signed in Waco, Texas, the three leaders proclaimed their reaffirmed commitment to the continent's economic integration. In Ottawa three months later, a trilateral ministerial SPP meeting published a slick trilingual "Report to Leaders" of some 300 measures that had been cobbled together by working groups of bureaucrats from the three governments to constitute an agenda for intergovernmental cooperation.

This Report to Leaders' energy chapter contained nine commitments – "expand science and technology collaboration," "increase energy efficiency collaboration," "increase regulatory cooperation," "enhance electricity collaboration," "greater economic production from oil sands," "increase natural gas collaboration," "enhance nuclear collaboration," "enhance cooperation on hydrocarbons," "improve transparency and coordination in energy information, statistics and projections." This very general wish list spoke to the SPP's diplomatic strategy of enhancing continental integration through the three executives sponsoring incremental bureaucratic actions, given that political paralysis in the Mexican legislature prevented a major move towards further energy deregulation or any privatization of Pemex that might divest it of its dominion over the country's petroleum industry.[59]

Meeting in Cancún in March 2006, Presidents Fox and Bush along with the newly elected Conservative prime minister of Canada, Stephen Harper, declared the SPP successful after its first year in operation and announced the creation of a big-business-competitiveness Council to advise the three executives about how to promote further integration. The relentless external pressure caused by unchecked US energy consumption will continue to push Mexico towards further energy deregulation, a force that will be complemented by the internal pressure for enhanced continental integration that will result from Vicente Fox being succeeded by another conservative president.

Whatever happens in the future, the distinctive paths taken by the United States' two peripheries shows how powerfully *the culture of a country's political economy can determine the politics of its economics*. [Please check that this formulation, which comes from the conference program, is still used editorially in the book's table of contents and the editor's introduction.]

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[57] North American Energy Working Group, *North America -- The Energy Picture II* (June 2006).
[58] Joseph M. Dukert, "North American Energy – 2006: Three Governments Offer a New Self-Portrait," *CSIS -- Centre for Strategic and International Studies, Washington, DC* 3 (March, 2006), 1.
[59] *Security and Prosperity Partnership of North America: Report to Leaders.* (June 2005), 28-33.