



## BACKGROUND

# Trans Mountain Pipeline Expansion Project

Current to September 12, 2018

### Core Issue

On August 30, 2018 the Federal Court of Appeal overturned the Cabinet-level approval of the Trans Mountain Pipeline Expansion Project (TMPEP). In a unanimous decision, the three judges led by Justice Eleanor Dawson concluded in the *Tsleil-Waututh Nation et al. v. Attorney General of Canada* case the National Energy Board (NEB) did not fully consider the impact of increased oil tanker traffic on the southern resident killer whale population off the BC coast and failed to adequately consult with affected indigenous communities.

For these reasons, the Federal Court of Appeal determined the Federal Government's review of the project to be flawed and as a result, all non-essential activity around the pipeline project has been halted indefinitely. On the very same day, Kinder Morgan shareholders voted overwhelmingly to sell the existing pipeline infrastructure to the

Government of Canada for \$4.5 billion. Federal Finance Minister Bill Morneau confirmed the Federal Government would go ahead with the purchase of the pipeline from Kinder Morgan and proceed with the expansion project.

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The decision in *Tsleil-Waututh Nation* is yet another setback in a series of setbacks for the beleaguered project. Private industry throughout Canada responded to the ruling with shock and dismay. The decision around the Trans Mountain expansion adds to the growing list of frustrations

experienced by the business community around Canada's problematic regulatory process for resource development projects.

Canadian Chamber of Commerce President and CEO Perrin Beatty recently echoed this sentiment when he was quoted as saying the court decision "sends a profoundly negative message to investors both here at home and abroad about Canada's regulatory

system and our ability to get things done even after the federal government has declared them to be in the national interest.”<sup>1</sup>

This Backgrounder will offer an overview of the project, the circumstances surrounding the Federal Government’s acquisition of the pipeline infrastructure, a summary of the Federal Court of Appeal ruling, impacts on the province’s energy sector, as well as impacts on select Saskatchewan businesses working on the project. The piece will finish with some concluding thoughts and considerations on potential next steps that will help get Saskatchewan oil to market.

## **Background**

In 1953 the Kinder Morgan Trans Mountain pipeline became operational, with an initial capacity of 150,000 barrels per day.<sup>2</sup> The project initially featured four pump stations and a marine terminal along its 1,147 km route from Edmonton, AB to Burnaby, BC. It is the only west coast link for western Canadian oil. Fast Forward to 2006 – 2008, Kinder Morgan added 160 km of new pipeline through Jasper National Park and Mount Robson Provincial Park between Hinton, AB and Hargreaves, BC. This expansion added 13 new pumping stations and made improvements to the existing pipeline infrastructure. Capacity was increased from 260,000 to 300,000 barrels per day.<sup>3</sup>

In February 2012, Kinder Morgan expressed interest in expanding the Trans Mountain pipeline further after receiving support from oil shippers. The project was proposed in response to requests from oil companies looking to reach new markets by expanding the capacity of North America’s only pipeline with access to the west coast. Expansion of the pipeline would ensure that producers would get full value for their oil. Oil producers would no longer have to sell into the US market at a discounted rate relative to world prices and could receive more for their product. Governments could collect more revenue as a result.

In December 2013, Kinder Morgan submitted a facilities application to the National Energy Board to expand the existing Trans Mountain pipeline. Construction was slated to begin in 2017 with the expectation that oil would flow through the new pipeline infrastructure by the end of 2019.<sup>4</sup> The TMPEP is a \$7.4 billion capital project with about 980 km of new pipeline. It was estimated the expansion project would create approximately 15,000 jobs – with 440 permanent jobs per year during the operational phase. It was also expected to generate a total of \$4.5 billion in federal and provincial government revenues. Mutual benefit agreements between the proponent and participating indigenous groups to assist with capacity-building were valued at \$300 million total.<sup>5</sup>

Eighty-nine percent of the new construction will parallel the existing Edmonton to Burnaby right-of-way and increase capacity from the current 300,000 barrels per day to 890,000 barrels per day.<sup>6</sup> The project will result in 12 new pumping stations, 19 new tanks added to the existing storage terminals and three new berths at the Westridge Marine Terminal (WMT) in Burnaby. The project would allow the WMT to increase the number of tankers it could receive from five to 34 per day.<sup>7</sup>

Following a 29-month consultation process including an environmental assessment, in May 2016 the NEB concluded the project was in the national interest and recommended Cabinet approve the project, subject to 157

conditions.<sup>8</sup> Kinder Morgan stated it would comply with those conditions. In November 2016, Prime Minister Trudeau announced the Federal Government would sanction the Trans Mountain expansion project, along with Enbridge's Line 3 pipeline replacement project.

With approval granted, Kinder Morgan made the decision to proceed with the project at an estimated cost of \$7.4 billion.<sup>9</sup> Kinder Morgan asked the NEB in October 2017 to allow construction to commence in response to the City of Burnaby refusing to grant the necessary permits and in December 2017, the NEB allowed Kinder Morgan to bypass Burnaby's municipal bylaws.

In light of increased controversy and uncertainty surrounding the project, in April 2018 Kinder Morgan decided to suspend all non-essential activity on the project and set a May 31, 2018 deadline for the Federal Government to reach an agreement with stakeholders. Soon after, Prime Minister Trudeau instructed Finance Minister Bill Morneau to negotiate an acquisition of Kinder Morgan's pipeline assets to de-risk the project. At the end of May 2018, the Federal Government signaled its intent to purchase the existing pipeline infrastructure from Kinder Morgan for \$4.5 billion and complete the expansion, pending approval from Kinder Morgan shareholders.<sup>10</sup>

In August 2018 two important court rulings around the Trans Mountain project were rendered. The first involved the Supreme Court of Canada deciding the City of Burnaby did not have the right to block Trans Mountain's expansion project.<sup>11</sup> The second was the Federal Court of Appeal's determination that the Federal Government's sanctioning of the project was based on a flawed assessment that it did not sufficiently consider the impact of an expected increase in tanker traffic on the local ecosystem, as well as inadequate consultations with affected Indigenous stakeholders.

## **Federal Government Acquisition of the Trans Mountain Pipeline Assets**

As referenced earlier, the Federal Government agreed to purchase the Trans Mountain pipeline and terminal assets from Kinder Morgan for \$4.5 billion, with the intent of immediately resuming construction on the expansion. The Federal Government's acquisition of Trans Mountain was done through the Trans Mountain Corporation, a newly-formed Federal Crown Corporation that is a subsidiary of the Canadian Development Investment Corporation.<sup>12</sup> The Federal Government's purchase of Trans Mountain will be financed by Export Development Canada, another Federal Crown Corporation.

Minister Morneau has been careful to point out that the Federal Government currently has no intention of being a long-term owner of this project. When appropriate, the Federal Government will divest itself from the project and transfer the related assets to a new owner or owner group. Some investors that have expressed interest in the project and its assets include Indigenous communities, as well as large institutional investors, such as pension plan funds.<sup>13</sup> It is worth mentioning that any private purchaser of the project and its assets would be covered by an indemnity that would protect the buyer against financial losses due to unnecessary delays.<sup>14</sup>

The Government of Alberta has also expressed interest in buying a stake in the

project. It is important to point out that Alberta's contribution would be in the form of an emergency fund and would only come into effect in the event of an unforeseen circumstance. Alberta would receive commensurate value for their financial contribution in the form of equity or profit sharing.<sup>15</sup>

While the Saskatchewan Chamber of Commerce and the Canadian Chamber of Commerce supported the Federal Government's purchase of Trans Mountain as a less-than-ideal measure to ensure the project's completion, the fact that the Federal Government had to nationalize an approved project that already underwent a rigorous evaluation is illustrative of larger deficiencies in Canada's regulatory process.

### ***Overview of Tsleil-Waututh Nation et al. v. Attorney General of Canada et al.***

As mentioned earlier, the Federal Court of Appeal in a unanimous decision overturned the Cabinet-level approval of the Trans Mountain expansion project. Before delving further, it is important to note early on the Federal Court of Appeal did in fact dismiss most claims levelled against the pipeline expansion project and its approval as being without merit.<sup>16</sup> The court also found that the Federal Government "acted in good faith and selected an appropriate consultation framework."<sup>17</sup>

For the Federal Court of Appeal, the approval process surrounding the Trans Mountain pipeline expansion project made two critical errors. The first had to do with inadequate consideration around increased oil tanker traffic off the BC coast and its impact on marine life. At the time, the NEB did not sufficiently consider marine shipping because the NEB believed the issue was outside of their mandate and therefore beyond the scope of their assessment. The Court disagreed with this assertion and determined the NEB shirked its responsibility in taking marine shipping into account.

The second and more important critical error had to do with the Federal Government failing to meet the standards required under the *Crown's Duty to Consult* when engaging with affected Indigenous communities. This critical error took place during Phase III of the project's four phase consultation process. Phase III occurred between February and November 2016.<sup>18</sup>

In her written decision, Justice Dawson provided a more thorough explanation of the Crown's Duty to Consult. To begin, the Duty to Consult is triggered when the "Crown has actual or constructive knowledge of the potential existence of Indigenous rights or title and contemplates conduct that might adversely affect those rights or title. The duty reflects the need to avoid the impairment of asserted or recognized rights caused by the implementation of a specific project."<sup>19</sup>

The depth of consultation with indigenous groups is commensurate with the strength of the Indigenous claim at face value and the seriousness of the potential adverse effects upon the claimed right.<sup>20</sup> To put it another way, if a strong face value claim is established, and the possible infringement of that claim is of great significance, and the risk of non-compensable damage is great, the depth of consultation is to be found at the high end of the spectrum.<sup>21</sup> In addition, the NEB by virtue of its institutional expertise and technical capacity, had available to it the

powers required to implement consultations, as well as the remedial powers to accommodate Indigenous claims, where appropriate.<sup>22</sup>

Further to this, Justice Dawson articulated that the consultation process around the Duty to Consult does not grant or guarantee Indigenous groups a particular outcome or give Indigenous groups a veto over what can be done with land. Justice Dawson also added that consultations carried out in good faith may reveal a duty to accommodate; that good faith is required by both parties throughout the consultation; and that "Indigenous claimants must not frustrate the Crown's reasonable good faith attempts, nor should they take unreasonable positions to thwart the government from making decisions, or acting in cases where, despite meaningful consultation, agreement is not reached."<sup>23</sup>

Ultimately the Federal Court of Appeal determined the Crown did not consult meaningfully with Indigenous stakeholders. Simply stated, listening to and recording complaints was not enough - a more substantive and robust dialogue is required. The lack of meaningful consultation can be attributed to the fact that staff attending the consultation sessions erroneously believed they could not amend or add conditions to the project's approval.

In light of the court ruling, the Federal Government who now owns the pipeline and terminal assets, can remedy this by either redoing the parts of the consultation process that were deemed inadequate to satisfy the court's concerns; appealing the decision to the Supreme Court of Canada; or enacting new legislation. The major advantage of the first option is that no project proponent will be asked to go back to the beginning. With the second option, experts estimate it would probably take 18 months to two years for the Supreme Court to hear the case and even then, no favourable ruling is assured. The legislative option might work in the short-term, but could lead to increased political fighting and more uncertainty. The Federal Government has stated that all options are on the table.

## **Impacts on the Saskatchewan Energy Sector**

Delays in the construction of the Trans Mountain pipeline expansion are expected to create additional challenges for the oil and gas sector both in Saskatchewan and in western Canada more broadly. If completed, the Trans Mountain expansion would have diversified Canada's export market access for oil to US markets in Washington State, California, Hawaii, and Alaska, as well as Asian countries like China, Japan, South Korea, and Taiwan. Doing so would have went a long way in addressing the ongoing bottleneck in Canada's existing pipeline network.<sup>24</sup>

A consequence of insufficient pipeline capacity according to Trevor Tombe, a research fellow at the University Of Calgary School Of Public Policy, is oil that would otherwise be exported by pipeline will have to be shipped by rail instead. Since transporting oil by rail is more expensive, oil producers located in Saskatchewan and elsewhere in Canada earn less on each barrel and therefore pay less to the government in the form of royalties.<sup>25</sup>

Tombe estimates that a \$1 per barrel drop in the price of oil increases the deficit by \$265 million. Ongoing pipeline capacity constraints are adding \$5 to \$10 per barrel to the discounted price fetched by oil producers in Canada. The widening spread between Western Texas Intermediate (WTI) and Western Canadian Select<sub>5</sub>

(WCS) is attributed to the fact that landlocked oil from Alberta and Saskatchewan is unable to reach tidewater and is exported to an already oversupplied US domestic market, resulting in lower prices fetched by Canadian producers.

To put Canada's pipeline capacity constraints into perspective, Rory Johnson, a commodity economist at Scotiabank estimated that without additional pipelines to tidewater by 2023, rail would be moving 700,000 barrels per day of oil out of Canada. This far exceeds the current outbound rail shipment figure of 200,000 barrels per day, which is currently at an all-time high.<sup>26</sup>

For those that oppose the Trans Mountain project and would like to see the project halted indefinitely based on environmental considerations, the irony is that delaying Trans Mountain may in fact do more harm to the environment in the long-term. While there are challenges to comparing pipelines to rail in a piece by piece comparison, it is generally understood that shipping oil by pipeline is a safer method overall, even taking into consideration that rail spills tend to be smaller than pipeline spills.<sup>27</sup>

## **Impact on Saskatchewan Businesses Working on the Trans Mountain Expansion**

The delays around the Trans Mountain Pipeline Expansion Project are having very real impacts closer to home. EVRAZ North America recently expressed its disappointment over the project's delays. The EVRAZ steel plant in Regina was awarded the contract to build 275,000 tons of steel piping for the project. In fact, roughly 75% of the steel piping required for the project will come from EVRAZ's Regina plant. If these delays continue to persist, there is a possibility that pipe production could be pushed back as a result. EVRAZ employs over 1,000 directly at their Regina site and confirmed publicly in February 2018 that significant layoffs would likely result if work on the project was halted. EVRAZ's challenges are compounded by their now restricted market access into the US due to the Trump Administration's ill-advised steel and aluminum tariffs.

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***Trevor Tombe.***

Smaller Saskatchewan companies are also encountering difficulties. A Saskatoon-based land surveying company awarded the survey work on Spread 2 from Edmonton to Hinton, AB has been directly impacted by the project's uncertainty. Having anticipated to hire at least eight additional people for the project once it got underway, the company is scrambling at the last minute to find work for some of its existing employees. The ongoing uncertainty has prevented the company from engaging in any meaningful staff planning. A Saskatoon-

based manufacturer of commercial structures that was anticipating work on an installation project near Jasper, AB had to forego bidding on other lucrative projects because it did not have the available capacity. These are but a few local examples.

## **Options for Future Action by the SCC**

It is likely the Trans Mountain expansion project will eventually be built, but new pipeline capacity will not go onstream for years. The two key pipeline projects that were cancelled – Northern Gateway and Energy East - could be revisited to add capacity, and expand markets served, as well as provide construction and operation and maintenance-related jobs over the lifecycle of the pipeline. The key is to get the Federal Government to focus on one or both and do all they can to get them built versus what they did do and finding those projects postponed or cancelled outright.

Keen observers following the two proposed pipeline projects would suggest that Northern Gateway would be the quickest to get final approval for. The proponent for Northern Gateway - Enbridge and its partners - would have to signal some kind of willingness to revisit the project. Conversely, a very detailed commitment from the Federal Government would be needed to allow the project to move forward.

While Energy East should be reconsidered and seriously reviewed, it is worth mentioning that the proposed route of this pipeline would have travelled through more populated regions and did not get as far along in the NEB's approval process as did Northern Gateway. However, a group from Moosomin, SK has begun an advocacy effort around Energy East. Energy East would generate positive, long-term benefits to Southeast Saskatchewan, so it is not a project the SCC will lose sight of.

### **Potential Actions:**

- Advocate strongly to the Federal Government to complete Trans Mountain.
- Contact Enbridge to gain insight around their willingness to revisit Northern Gateway.
- Contact TransCanada to assess their willingness to revisit Energy East.
- Communicate to the Federal Government the damage the NEB's problematic approval process has had on Saskatchewan businesses directly, and on the investment climate across Canada, more broadly.
- Seek additional member input on Bill C-69 and the impact it will have on future resource development projects (Bill C-69 is currently before the House of Commons and seeks to replace the NEB with a new agency called the Canadian Energy Regulator. It will also broaden the scope of the Canadian Environmental Assessment Agency and rename it the Impact Assessment Agency of Canada).

## Conclusion

The indefinite suspension of construction activity on the Trans Mountain Pipeline Expansion Project, along the failure of other pipeline projects to go ahead - most notably Northern Gateway and TransCanada's Energy East - is contributing to a growing perception among many investors that Canada is no longer able to develop major resource projects in a timely and predictable manner.

A consequence of Canada's inability to ensure good development projects go ahead is that it undermines our ability to tap into new emerging markets that allow us to realize the full dollar value of our energy exports. It means more oil will need to be shipped by rail, thereby exacerbating already existing capacity challenges, along with the potential for layoffs and foregone revenues by all levels of government. Worst of all, it sends a signal to the international community that Canada is closed for business.

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## Endnotes

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