

International Trade and Investment Law Practicum

INTERNATIONAL TRADE IN LIQUIFIED NATURAL GAS

A STRATEGY FOR GLOBAL AFFAIRS CANADA

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Executive Summary

The global liquefied natural gas (LNG) market is in flux and, despite its position as the world's fourth largest producer of natural gas, Canada is failing to gain a foothold in the market. Although the global LNG market grew thirty percent in 2017, a number of major Canadian LNG projects were cancelled in the same year. In recent years, demand for Canadian natural gas has decreased as production in the United States (US), its main importer, has grown. The US has already begun exporting LNG from its Gulf of Mexico and East Coast facilities. While there are currently no export terminals under construction on the US or Canadian West Coast, the proximity of any future West Coast terminals to Asia would put them at an advantage in the race to meet the rapidly growing demands of world's largest LNG market.

With demand for natural gas increasing at higher rates than predicted among priority markets such as China, South Korea and Japan, LNG shows potential for Canada to achieve some of its trade-based goals if an appropriate balance is struck with its other objectives, such as protecting the environment and retaining a sufficient supply for its own future energy needs. Despite the need for Canada to seek out new trading partners for its excess natural gas production, no LNG export projects are currently in the construction phase. Proposed projects have been effectively halted by the decreasing global price of natural gas. Infrastructure costs have also substantially increased. Imports of materials that are essential to the construction of export terminals have recently been hit by anti-dumping duties of up to 46.8%, substantially increasing project costs.

The Canadian LNG industry also faces several other irritants that affect a variety of projects. Certain East Coast facilities seeking to import natural gas produced in the United States for

liquefaction in Canada and re-export to third markets have unexpected hurdles in the process of obtaining export permits from the US Department of Energy (DOE). The US natural gas export permitting regime affects Canadian projects seeking to liquefy and re-export US-produced natural gas to certain third countries by subjecting those projects to a separate export approval process that frequently involves substantial delays.

Domestically, the Canadian regulatory matrix introduces unnecessary obstacles for potential projects. Many steps of the approval process are duplicated as between different federal and provincial agencies. These inefficiencies stall production and create additional costs for projects. This memorandum makes three recommendations to Global Affairs Canada to directly and indirectly address these irritants and increase the marketability of Canadian LNG exports.

Recommendation 1: Address the US Natural Gas Export Licensing Regime Affecting Canadian LNG Re-Export Projects

Despite decades of efforts to promote free trade and to integrate the North American energy sector, some restrictions remain. One key irritant impacting Canadian re-exports of natural gas involves the approach taken by the Department of Energy in determining which approval process to use for such projects. This approach was first clarified in Order 3639, issued in 2015, in which the DOE granted partial approval to a Canadian re-export project but also determined that a portion of that project's application must be put through a much longer approval process.¹ According to the DOE's findings in this Order, the Department is required to assess the trade status of the country

¹ Office of Fossil Energy of the Department of Energy, "Order Granting Long-Term, Multi-Contract Authorization to Export Natural Gas to Canada and to Other Free Trade Agreement Nations (DOE/FE Order No. 3639)" at page 2, online: <<https://www.energy.gov/sites/prod/files/2015/05/f22/ord3639.pdf>>.

where the natural gas is sent for “end use”, and consequently applications seeking to export US natural gas to Canada for the purpose of liquefaction and re-export to certain third countries must undergo a lengthy assessment process.²

To address this issue, Global Affairs Canada should seek an outcome that ensures that these findings do not apply to any future applications to import US natural gas to Canada. This can be achieved through the addition of a new provision to the NAFTA energy chapter, by challenging or threatening to challenge the regime’s compliance with US obligations under the World Trade Organization (WTO), or through efforts to support domestic initiatives in the United States to reform the export licensing regime.

Recommendation 2: Help Secure a Remission Order from Anti-Dumping Duties on Materials Used in the Production of LNG Export Facilities

Global Affairs Canada should advise the Minister of Finance of the public interest of exporting LNG to assist the industry’s effort to gain a Remission Order exempting them from anti-dumping duties on specific components.

Recommendation 3: Streamline Canada’s Regulatory Matrix by Authorizing a Single Regulatory Body to Perform Duties under Both Federal and Provincial Regulations

Global Affairs Canada should lead the initiative for a consolidated approval authority for LNG projects in Canada, eliminating the regulatory hurdles posed by a multi-agency process.

² *Ibid.*

I. Introduction

Demand for Canadian natural gas in its traditional export market, the US, has declined with the growth of US natural gas production, leaving Canada with the opportunity to export its surplus to new markets.³ To transport natural gas to these markets, it must first be liquefied for transportation and then vaporized to ultimately be consumed in its gaseous state. If Canada wishes to expand its natural gas exports to new markets, it must build and utilize liquefaction facilities.

While the global demand for LNG imports is growing even more rapidly than predicted, Canada's LNG exports are practically non-existent.⁴ A variety of factors are currently hindering the development of the Canadian LNG export sector. This memorandum identifies three key factors that the Canadian government can play a role in mitigating and makes specific recommendations as to how Global Affairs Canada can work to address these issues.

The memorandum is structured as follows. In Part II, we provide an overview of developments and trends in the global LNG market. In Part III we examine how Canada's participation in the LNG trade can advance its interests if balanced with other competing objectives. In Part IV, we highlight the key barriers to Canada's entry into the global LNG market, identify possible avenues to overcome those barriers and assess the viability and effectiveness of these options.

³ Canada's Role in the Global LNG Market – Energy Market Assessment July 2017, (17 July 2017), *National Energy Board*, online: <<https://www.neb.gc.ca/nrg/sttstc/ntrlgs/rprt/2017lngmrkt/index-eng.html>> at 5 [*Canada LNG Report*].

⁴ *Ibid* at 7.

II. The Global LNG Market and Canada's Position

A. The History of LNG and the Shale Revolution

Liquefied natural gas is natural gas that has been cooled to -160°C and condensed into a liquid state that occupies $1/625^{\text{th}}$ of its original volume.⁵ This process was initially used for storage purposes and was first implemented in the early 1900s. Today, liquefying natural gas allows for efficient transportation where pipelines are not available or not feasible. In 1959, the first LNG ship proved the feasibility of transoceanic transportation of natural gas when it transported its cargo from the United States to the United Kingdom.⁶ Ten years later, Japan imported its first shipment of LNG from Alaska, and then went on to heavily expand its LNG imports over the next two decades. The United States first began importing LNG from Algeria in the 1970s, until rising prices and regulatory reforms led to a rapid expansion of the country's domestic natural gas supply.⁷ The resulting "gas bubble" led to a fall in US LNG imports in the late 1980s.⁸ In the 1990s, demand for natural gas grew rapidly in the US, and predictions of supply shortfalls led to a dramatic increase in LNG deliveries.⁹

The development of new hydraulic fracturing and horizontal drilling processes led to major increases in proven reserves of shale gas in the United States over the last decade.¹⁰ These new

⁵ *Canada LNG Report*, *supra* at 2.

⁶ Understanding Natural Gas and LNG Options, (November 2016), *Power Africa – A US Government Led Partnership*, online: <<https://www.energy.gov/sites/prod/files/2016/12/f34/Understanding%20Natural%20Gas%20and%20LNG%20Options.pdf>> at 10.

⁷ Office of Fossil Energy. (2005, August) "Liquefied Natural Gas: Understanding the Basic Facts" online: https://www.energy.gov/sites/prod/files/2013/04/f0/LNG_primerupd.pdf at page 4.

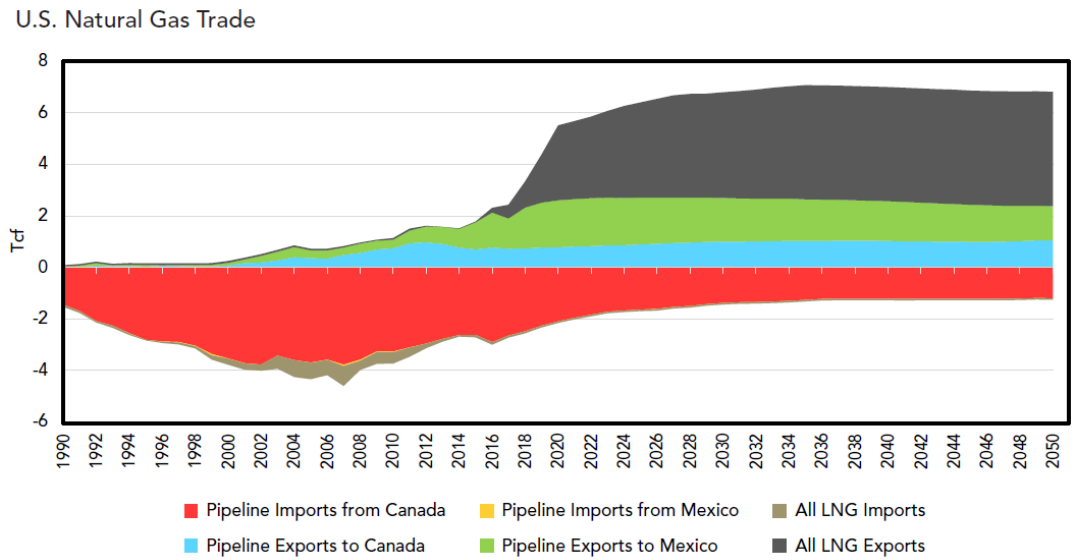
⁸ *Ibid.*

⁹ *Ibid.*

¹⁰ Shale Gas, (13 February 2018), *US Energy Information Administration*, online: <https://www.eia.gov/dnav/ng/ng_enr_shalegas_dcu_NUS_a.htm>.

techniques enabled companies to extract large amounts of oil and gas from shale rock clusters that were previously uneconomic to develop.¹¹ Canada has also seen a dramatic increase in proven reserves of natural gas coming from shale gas formations in Alberta and British Columbia.

Increased US production has led to a significant decrease in demand for Canadian natural gas. This demand peaked in 2007 when the US imported 3,782,708 MMcf of natural gas from Canada.¹² US imports of Canadian natural gas subsequently fell to 2,959,646 in 2017.¹³ During the same timeframe, US total LNG imports fell from 770,812 MMcf to 78,011 MMcf.¹⁴ Between 2007 and 2017, the total value of annual Canadian natural gas exports to the United States fell \$17 billion as a result of reduced export volumes and lower export prices.¹⁵



Source: Canada’s Role in the Global LNG Market – Energy Market Assessment July 2017, National Energy Board

¹¹ *Canada LNG Report, supra* at 5.

¹² Million cubic feet (MMcf).

¹³ US Natural Gas Imports by Country, (28 February 2018), *US Energy Information Administration*, online: <https://www.eia.gov/dnav/ng/NG_MOVE_IMPC_S1_A.htm>.

¹⁴ *Ibid.*

¹⁵ Commodity Statistics – Historical Summary of Volumes and Prices for Gas, (January 2018), *National Energy Board*, online: <<https://apps.neb-one.gc.ca/CommodityStatistics/Statistics.aspx?language=english>>.

At the same time that a glut of natural gas supply in North America resulted in decreased prices, the price of natural gas in certain non-producing countries increased significantly. Notably, Asian and European gas prices were well above North American levels between 2011 and 2015.¹⁶ This is significant given Asia's position in the global LNG market. Japan is the largest importer of LNG globally with 2016 LNG imports at 83.3 MTPA followed by South Korea (33.7 MTPA), China (26.8 MTPA), and India (19.2 MTPA).^{17,18} Many North American natural gas producers began making significant investments into LNG liquefaction facilities in 2010. At the same time, Asian importing countries started investing heavily into North American gas projects that would supply future liquefaction facilities.¹⁹

B. The Canadian LNG Sector

Following the advent of the shale revolution, the US industry shifted its focus from importing LNG to exporting it. As US natural gas production continues to increase, pipeline exports from Canada to the US have steadily declined. As a result, Canadian natural gas producers have been looking for new exports markets which are only accessible by liquefying the gas. Currently, Canada only uses small-scale liquefaction and regasification facilities to store and transport LNG for domestic use. British Columbia (BC) has become the focus for new LNG projects since the province unveiled its pro-LNG strategy in 2012, resulting in approvals for twenty new liquefaction facilities on the West Coast.²⁰

¹⁶ *Canada LNG Report, supra* at 16.

¹⁷ Million metric tonnes per year (MTPA).

¹⁸ 2017 World IGU Report, (2017), *International Gas Union*, online <<http://www.igu.org/news/igu-releases-2017-world-lng-report>> at 14 [*IGU Report*].

¹⁹ *Canada LNG Report, supra* at 16.

²⁰ "British Columbia's Natural Gas Strategy", (3 February 2012), *BC Ministry of Energy and Mines*, online: <http://www.gov.bc.ca/ener/popt/down/natural_gas_strategy.pdf>.

Currently, 86% of all proposed LNG projects in Canada are on the West Coast, with only 14% on the East Coast.²¹ The liquefaction facilities are focused on the West Coast for two reasons. First, the key gas producing regions are in North Eastern BC and Western Alberta in the Montney, Deep Basin, and Horn River regions.²² The National Energy board estimates that while 30.8 trillion cubic metres of marketable natural gas exists in Canada, the Western Canada Sedimentary Basin (“WCSB”) accounts for nearly 79% of that figure.²³ Proximity to these regions means lower cost of transportation and less investment into pipeline infrastructure. Additionally, many LNG project proponents are gas producers in these regions looking to diversify the market for their products.²⁴

Second, Canada’s West Coast is closer to the dominant Asian market. According to the National Energy Board, West Coast LNG project proposals were largely for the export of LNG from BC to the Asian market.²⁵ Many LNG project proponents also include investors from Japan and Korea, and many have entered into offtake agreements to sell future LNG production.²⁶ This represents a comparative advantage over the East Coast facilities, which must either sail around South America or face the costs of crossing through the Panama Canal to transport LNG to Asia.

However, in recent years, British Columbia has seen four major projects cancelled along its coast.²⁷ Most notably, Petronas canceled its \$36 billion Pacific NorthWest LNG project less than a year

²¹ *Canada LNG Report, supra* at 20-21.

²² *Canada’s Energy Future, supra*.

²³ *Ibid.*

²⁴ *Canada LNG Report, supra* at 9.

²⁵ *Canada LNG Report, supra*, at 8.

²⁶ *Ibid* at 9.

²⁷ “Canadian LNG Projects”, (21 September 2017), *Natural Resources Canada*, online: <<https://www.nrcan.gc.ca/energy/natural-gas/5683>> [*Canadian LNG Projects*].

after the federal government approved the project. Following the path of three other canceled West-Coast projects, Petronas cited dropping natural gas prices in the Pacific Rim and growing global competition as reasons for the decision.²⁸

Six projects on the East Coast have received NEB export permits, four of which have also received NEB import permits to import gas from the US to re-export to Europe, Latin America and India.²⁹ Upon completion, Canadian East Coast projects would be much closer to European import terminals compared to export terminals in the US, Australia, Qatar, and Malaysia.³⁰

While Canada has an abundance of natural gas reserves and only imports small quantities of LNG, there is a single LNG regasification terminal in New Brunswick that imports LNG and helps supply natural gas to Atlantic Canada and the US Northeast.³¹ This facility imports LNG from Trinidad, Norway, Egypt, Qatar, and Peru.³² However, due to the increase of both domestic and US supply, the import facility operates at only 4% of capacity.³³ With the changing landscape of the LNG market, the owners of this facility sought to convert it to an exporting facility. In 2016 the project was put on hold, in part because decreasing prices made it impossible to secure outside investments to fund the project.³⁴

²⁸ Claudia Cattaneo, “Petronas cancels \$36B LNG project as B.C. jacks up demands”, *Financial Post*, (25 July 2017), online: <<http://business.financialpost.com/commodities/energy/a-tragedy-for-canada-petronas-cancels-36b-lng-project-as-b-c-jacks-up-demands>>.

²⁹ *Canada LNG Report*, *supra* at 8, 20-21.

³⁰ *Ibid* at 18.

³¹ In 2016, Canada represented 0.09% of world LNG imports; see 2017 World IGU Report, (2017), *International Gas Union*, online <<http://www.igu.org/news/igu-releases-2017-world-lng-report>> at 14.

³² “Canaport LNG – One Year of Operations”, (December 2010), *Canaport LNG*, online: <https://www.canaportlng.com/pdf/newsletters/IMYKJRuBni_CanaportConnections_v10.pdf> at 1.

³³ “Market Snapshot: Canada’s LNG imports dropped 88% since 2011”, (28 March 2018), *National Energy Board*, online: <<http://www.neb-one.gc.ca/nrg/ntgrtd/mrkt/snpst/2018/03-04cndlngmprts-eng.html>>.

³⁴ *Canada LNG Report*, *supra* at 7.

Two LNG export projects have also been proposed for Nova Scotia.³⁵ The Bear Head facility is located at the Strait of Canso.^{36,37} Goldboro, a project owned by Pieridae Energy that is on schedule to begin construction this spring, is located in Guysborough County.³⁸ Both projects have obtained all ten initial domestic Canadian permit approvals, approval from Canada’s National Energy Board (NEB) for a license to import natural gas from the US and to export LNG to third markets, and approval from the US Department of Energy for a license to export LNG derived from US produced natural gas to all countries with which trade is not prohibited by US policy or law.^{39,40,41} Representatives from the Canadian LNG industry have raised concerns about the impact of the US natural gas export licensing process affecting projects like these, which seek to import US natural gas for the purpose of liquefaction and re-export to third markets. This concern will be addressed in detail in the section on US natural gas export permitting below.

³⁵ Paul Withers, CBC “Nova Scotia and New Brunswick Face End of Domestic Supply of Natural Gas” (8 March 2018) online: <<http://www.cbc.ca/news/canada/nova-scotia/nova-scotia-natural-gas-price-hikes-1.4566069>>.

³⁶ *Ibid.*

³⁷ Liquefied Natural Gas Limited, LNG the Energy Link, “Bear Head LNG Project” (2018) online: <<http://www.lnglimited.com.au/irm/content/bear-head-lng.aspx>>.

³⁸ Ken Summers, *the Nova Scotia Advocate*, “Prospects of Goldboro LNG Plant Improve, Raising Concerns About Nova Scotia’s Emission Reduction Targets” (19 February 2018) online: <<https://nsadvocate.org/2018/02/19/prospects-of-goldboro-lng-plant-improve-raising-concerns-about-nova-scotias-emission-reduction-targets/>>.

³⁹ *Ibid.*

⁴⁰ Office of Fossil Energy of the Department of Energy “Opinion and Order Granting Long-Term, Multi-Contract Authorization to Export U.S.-Sourced Natural Gas by Pipeline to Canada for Liquefaction and Re-Export in the Form of Liquefied Natural Gas to Non-Free Trade Agreement Countries (DOE/FE Order No. 3770)” online: <<https://www.energy.gov/sites/prod/files/2016/02/f29/ord3770.pdf>>.

⁴¹ Office of Fossil Energy of the Department of Energy, “Order Granting Long-Term, Multi-Contract Authorization to Export Natural Gas to Canada and to Other Free Trade Agreement Nations (DOE/FE Order No. 3639)” at page 2, online: <<https://www.energy.gov/sites/prod/files/2015/05/f22/ord3639.pdf>>.

III. Canada's Interests with Respect to LNG

Canada has been working internationally to promote a global trading system that is more inclusive and progressive.⁴² The Federal Government made strengthening and diversifying trade a priority in the 2018 Federal Budget Plan, noting that the success of the nation depends on strong trade relations.⁴³

Canada has identified several Asian Pacific economies as part of its Global Markets Action Plan, among them are the three largest LNG importers, South Korea, Japan and China.⁴⁴ They are listed as significant target markets for Canada's oil and gas sector, the sector itself is also identified as a priority for growth within the Plan.⁴⁵ China is Canada's second-largest single-nation trading partner.⁴⁶ The Government proposed providing up to \$75 million over five years to Global Affairs Canada to enhance Canada's presence in China through diplomatic and trade support.⁴⁷ Both countries share a goal of doubling bilateral trade by 2025.⁴⁸ Targeting China is part of a larger plan to increase Canada's export to Asia.⁴⁹ The hope is that by expanding trade with China, more Canadian jobs will be created in the economy.⁵⁰

⁴² International Trade Minister to Champion Canada's Progressive Trade Agenda at 11th WTO Ministerial Conference in Argentina online: Government of Canada <https://www.canada.ca/en/global-affairs/news/2017/12/international_tradeministertochampioncanadasprogressivetradeagen.html>. [*Progressive Trade Agenda at the WTO*].

⁴³ Department of Finance Canada, (2018) Budget 2018: Equality and Growth for a Strong Middle Class. At <<https://www.budget.gc.ca/2018/docs/nrc/2018-02-27-en.pdf>> at 64 [*Budget 2018*].

⁴⁴ Global Affairs Canada, (2016) *Global Markets Action Plan*. online: <<http://international.gc.ca/global-markets-marches-mondiaux/plan.aspx?lang=eng#1a>>. at Priority Markets.

⁴⁵ *Ibid* at Priority Sectors.

⁴⁶ *Budget 2018, supra* at page 66.

⁴⁷ *Ibid* at 67.

⁴⁸ *Ibid* at 66.

⁴⁹ *Budget 2018, supra* at 66.

⁵⁰ *Ibid* at 67.

LNG represents a major opportunity for Canada to expand trade with China and other Asian markets. The appetite for LNG in this market is still growing, and some forecasters have even noted that there may be a shortage considering this trend and the low investments into the supply side of the industry.⁵¹ While LNG currently only accounts for 6% of China’s energy use, it has a goal of expanding that figure to 10% by 2020 and 15% by 2030.⁵²

The construction of the infrastructure necessary to export Canadian LNG into these regions would also create jobs as predicted by the Government. The BC government has supported the industry’s claim that 100,000 jobs would be created with only four or five projects going ahead, while other commentators have far less optimistic outlooks.⁵³ In one Kitimat project proposed by LNG Canada, the figures provided in their environmental assessment filing were a workforce of 7,500 for construction, and up to 800 workers for the operation of the facilities.⁵⁴ This would indicate that the 100,000 figure is generous but the numbers filed do not include the jobs that the industry would indirectly create in the economy.

The environment is also a priority for Canada and must be balanced with its other interests. The National Energy Board notes that there is concern over the local impacts of hydraulic fracturing,

⁵¹ Tom DiChristopher, “Shell Warns of Liquefied Natural Gas Shortage as LNG Demand Blows Past Expectations” *CNBC* (26 February 2018), online: *CNBC* <<https://www.cnbc.com/2018/02/26/shell-warns-of-lng-shortage-as-demand-for-liquefied-natural-gas-booms.html>>.

⁵² Nathan Vanderklippe, “China Renews Commitment to Less Coal, More Natural Gas”, *The Globe and Mail* (10 July 2017), online: *The Globe and Mail* <<https://www.theglobeandmail.com/report-on-business/industry-news/energy-and-resources/china-renews-commitment-to-less-coal-more-natural-gas/article35627780/>>.

⁵³ Marc Lee (July 2015). LNG and Employment in BC. *Canadian Centre for Policy Alternatives* at <<https://www.cleanenergybc.org/wp-content/uploads/2015/10/CCPABCLNGEmploymentReport.pdf>>.

⁵⁴ LNG Canada (March 2013). Project Description, Application to BC Environmental Assessment Office. At: <<https://projects.eao.gov.bc.ca/api/document/58869075e036fb0105768b54/fetch>> at page 133.

as well as about pipeline routing and the use of land and marine resources.⁵⁵ Exporting LNG will result in the continuation of hydraulic fracturing within Canada which will impact the environment.

Internationally, Canada's commitment to the 2030 Agenda for Sustainable Development demonstrates that Canada has an interest in having affordable and clean energy available for a more prosperous world.⁵⁶ Canada's efforts to advance a progressive trade agenda have also included advocating for environmental sustainability.⁵⁷ The Government recognizes that the fight against climate change cannot be an individual effort and that Canada should work to promote clean energy abroad.

Gender equality and the empowerment of women and girls are also part of Canada's international goals.⁵⁸ "Environment and climate action" is one of the six action areas set out in the Government's Feminist International Assistance Policy.⁵⁹ Canada has advocated internationally for a gender-based approach to climate change, stating that in especially poor and vulnerable communities "women and girls are often the primary producers of food and providers of water, heating and cooking fuel for their households" and they bear the burden when climate change affects the availability of these resources.⁶⁰

⁵⁵ *Canada LNG Report, supra* at 18.

⁵⁶ *Budget 2018, supra* at 163.

⁵⁷ *Progressive Trade Agenda at the WTO, supra*.

⁵⁸ *Budget 2018, supra* at 156.

⁵⁹ *Ibid* at 156.

⁶⁰ *Ibid* at 160.

LNG can be part of Canada’s strategy to achieve some of its environmental goals. While natural gas is a fossil fuel, it has been argued that it will play a key role in the transition to low carbon energy sources. Natural gas creates half the emissions of coal to create the same energy output.⁶¹ It can replace coal and serve as a backup while renewable energy forms are still being implemented.⁶² In light of the intersection of the environment and climate action with gender, LNG may also have spillover effects in assisting gender initiatives.

Natural Resource Canada is seeking to improve Canadian quality of life by creating a sustainable resource advantage.⁶³ Given the growing global trade in natural gas and Canada’s abundant natural gas supply, a strategic LNG policy should play a major role in shaping Canada’s energy future. Formulating an LNG policy that reflects Canada’s interests and the priorities of Global Affairs Canada is a crucial first step towards achieving several of the Department’s objectives and eliminating major irritants impacting Canadian LNG competitiveness.

Because of the US’s enhanced production of natural gas, if Canada wishes to continue finding secure markets for its natural gas exports, the industry must look beyond the traditional trade-by-pipeline approach. As noted above, companies have been looking at building LNG export facilities in Canada to give Canadian natural gas access to additional markets.⁶⁴

⁶¹ *Canada LNG Report, supra* at 5.

⁶² James Taylor, “Closing Coal Power Plants, Replacing With Natural Gas, Makes Economic Sense”. *Forbes* (26 February 2018) online: <<https://www.forbes.com/sites/jamestaylor/2018/02/26/closing-coal-power-plants-replacing-with-natural-gas-makes-economic-sense/2/#>>.

⁶³ Natural Resource Canada, (2017) “About Us” online: <<https://www.nrcan.gc.ca/department>>.

⁶⁴ *Canada LNG Report, supra* at 8-9.

While it is not a listed priority for the Canadian government, there is potential for existing Canadian natural gas exporters to benefit from LNG as well. Diversifying Canada's energy trade to include LNG would alleviate the pressure that US buyers are able to exert on domestic suppliers as Canada's only natural gas export market. It would create a more robust Canadian energy trade globally as well.

IV. Issues and Recommendations: Addressing Factors Affecting Canada's Prospects as an LNG Exporter

Canada has much to gain from participation in the global LNG trade, but numerous project delays and cancellations have prevented Canada from advancing its objectives. The biggest challenge facing the industry is the persistent decline of natural gas prices in the global market, resulting in the cancellations of projects referred to earlier. LNG projects come with high development costs to construct the infrastructure necessary for exportation. In order to justify those expenditures, investors need to be confident that prices will remain high enough that their ventures will be profitable.

Since commodity pricing is determined by global market forces, Canada cannot meaningfully address them in a way that would be beneficial. On the other hand, the current regulatory and policy landscape that investors face in Canada contributes to Canada's lack of results in the sector. Canada has the option to make changes to the regulatory framework that could increase the projected profitability of LNG projects, restoring investors' confidence and efficiently advancing Canada's objectives.

Investors have become weary of Canada's future as an LNG exporter. The decisions of administrative bodies including the US Department of Energy and the Canadian International Trade Tribunal (CITT) have complicated the industry's ability to develop the infrastructure as planned. Canada's expansive regulatory matrix has also resulted in the delay of project approvals. The effects of these irritants have compounded other market uncertainties and jeopardized Canada's opportunity to convert its surplus natural gas into LNG for export to new markets.

The remainder of this section will explain the identified inefficient market conditions which hinder Canada's ability to export LNG, followed by recommendations for Global Affairs Canada to address each issue. The three irritants discussed are the US natural gas export licensing regime, the anti-dumping duties imposed on Chinese steel imports, and the Canadian regulatory matrix.

1. THE US NATURAL GAS EXPORT LICENSING REGIME

The Issue

Representatives from the Canadian LNG industry have identified the natural gas permitting regime employed in the United States as an irritant that will likely increase the timeframe, cost, and security of supply concerns of potential future LNG projects involving US-produced natural gas. As a result, the permitting regime threatens the competitiveness and profitability of such projects and may deter potential investors.

The National Gas Act (NGA) section 3(a), 15 U.S.C. § 717b(a) states that

...no person shall export any natural gas from the United States to a foreign country... without first having secured an order of the Commission authorizing it

to do so. The Commission shall issue such order upon application, unless... it finds that the proposed exportation... will not be consistent with the public interest.⁶⁵

In accordance with section 3(a) of the NGA, US natural gas exporters must obtain approval from the Department of Energy for their proposed exports.⁶⁶ Unless the application qualifies for an exception, the DOE assesses whether the proposal is in the public interest, and grants or denies export approval accordingly.⁶⁷ The criteria for the public interest assessment are not defined in the statute, and the assessment requirement gives the DOE broad power to potentially deny export licenses to any projects it deems not to be in the public interest.⁶⁸

The DOE's assessment can also drastically increase the approval timeframe. This section will include a review of several examples of projects that have been significantly impacted by the public interest assessment. Between the uncertainty and delays that the assessment introduces into the process, this requirement poses a serious threat to the potential competitiveness, profitability, and investment attractiveness of any projects subject to it.

In an effort to reform the process and address some of these concerns, Congress introduced a

⁶⁵ Title 15 COMMERCE AND TRADE, Chapter 15b – Natural Gas Act, § 717b(a), page 1002
<<https://www.energy.gov/sites/prod/files/2013/04/f0/2011usc15.pdf>>.

⁶⁶ Office of Fossil Energy, “How to Obtain Authorization to Import and/or Export Natural Gas and LNG” *Natural Gas Regulation*, online: <<https://www.energy.gov/fe/services/natural-gas-regulation/how-obtain-authorization-import-andor-export-natural-gas-and-lng>>.

⁶⁷ Office of Fossil Energy, “How to Obtain Authorization to Import and/or Export Natural Gas and LNG – Natural Gas Import & Export Regulation - Free Trade Agreement (FTA) Countries and LNG Exports” at para 3, *Natural Gas Regulation*, online: <<https://www.energy.gov/fe/services/natural-gas-regulation/how-obtain-authorization-import-andor-export-natural-gas-and-lng>>.

⁶⁸ Nicolas Loris, the Heritage Foundation, Backgrounder, No. 3232, “Removing Restrictions on Liquid Natural Gas Exports: A Gift to the U.S. and Global Economies” (27 July 2017), online: <<https://www.heritage.org/sites/default/files/2017-07/BG3232.pdf>>.

streamlined approval track for natural gas exports to countries with which the US has a free trade agreement (FTA) that includes national treatment requirements for trade in natural gas. Under this expedited track, applications to export natural gas to qualifying FTA countries are deemed to be in the public interest and are granted automatic approval. Specifically, the National Gas Act section 3(a), 15 U.S.C. § 717b(c) states that

...the exportation of natural gas to a nation with which there is in effect a free trade agreement requiring national treatment for trade in natural gas, shall be deemed to be consistent with the public interest, and applications for such importation or exportation shall be granted without modification or delay.⁶⁹

Canada qualifies as an FTA country under this approach as a result of the national treatment provisions set out in the current NAFTA.⁷⁰

However, an application involving a Canadian natural gas project, submitted after the introduction of the expedited approval process for FTA countries, revealed that not all Canadian projects are guaranteed to fully enjoy the benefits of the expedited process. On October 24th, 2014, Pieridae Energy (USA) Ltd.⁷¹ filed an application with the Department of Energy requesting long-term,

⁶⁹ Title 15 COMMERCE AND TRADE, Chapter 15b – Natural Gas Act, § 717b(c), page 1002
<<https://www.energy.gov/sites/prod/files/2013/04/f0/2011usc15.pdf>>.

⁷⁰ Office of Fossil Energy, “How to Obtain Authorization to Import and/or Export Natural Gas and LNG - Natural Gas Import & Export Regulation - Free Trade Agreement (FTA) Countries and LNG Exports” at para 2, *Natural Gas Regulation*, online: <<https://www.energy.gov/fe/services/natural-gas-regulation/how-obtain-authorization-import-andor-export-natural-gas-and-lng>>.

⁷¹ Pieridae Energy is a Canadian company with offices in Calgary, Halifax, and Quebec City

multi-contract authorization to export natural gas from the United States to Canada and, after liquefaction in Canada, to export the natural gas to third countries.⁷²

On May 22nd, 2015, the DOE issued Order 3639 granting Pieridae authorization to export natural gas to Canada and to other free trade agreement countries.⁷³ However, the Order also stated that the portion of the Application seeking authorization to export US-sourced natural gas to non-FTA countries for “end use” in non-FTA countries would remain on the docket and would be reviewed separately without the benefit of the public interest presumption.⁷⁴ Authorization to export to non-FTA countries was eventually granted on February 5th, 2016, a full eight and a half months later.⁷⁵

As a result of the DOE's findings in Order 3639, Canadian projects seeking to import US natural gas for liquefaction and re-export to non-FTA countries will undergo a full public interest assessment. As was the case with the Pieridae application, this can significantly lengthen the approval timeframe. Extreme examples can be found among the DOE's docket records for LNG export applications, which are subject to the same approval process as natural gas exports via pipeline.⁷⁶

⁷² Office of Fossil Energy of the Department of Energy, “Order Granting Long-Term, Multi-Contract Authorization to Export Natural Gas to Canada and to Other Free Trade Agreement Nations (DOE/FE Order No. 3639)” at page 2, online: <<https://www.energy.gov/sites/prod/files/2015/05/f22/ord3639.pdf>>.

⁷³ *Ibid* at page 3.

⁷⁴ *Ibid* at page 3 to 4.

⁷⁵ Office of Fossil Energy of the Department of Energy “Opinion And Order Granting Long-Term, Multi-Contract Authorization to Export U.S.-Sourced Natural Gas by Pipeline to Canada for Liquefaction and Re-Export in the Form of Liquefied Natural Gas to Non-Free Trade Agreement Countries (DOE/FE Order No. 3768)” online: <<https://www.energy.gov/sites/prod/files/2016/02/f29/ord3768.pdf>>.

⁷⁶ Title 15 COMMERCE AND TRADE, Chapter 15b – Natural Gas Act, § 717b(b), page 1002 <<https://www.energy.gov/sites/prod/files/2013/04/f0/2011usc15.pdf>>

Between September 2010 and March 2018, the DOE received 64 long term applications to export US produced LNG to FTA countries.⁷⁷ Of those applications, nine were vacated, three are pending approval, and 52 were approved.⁷⁸ Over the same period, the Department received 58 applications to export US LNG to non-FTA countries. Of those applications, one was dismissed, seven were withdrawn, 21 are currently under review, and 29 were approved.⁷⁹ In 55 cases, LNG projects submitted applications to export to both FTA and non-FTA countries.⁸⁰ In eight of these cases, both applications were vacated, withdrawn, or dismissed.⁸¹ In 24 cases, both applications were approved.⁸² In one case, both applications are still pending approval.⁸³ In the remaining 20 cases, which represent 36% of the projects that submitted both FTA and non-FTA applications, the application for authorization to export to FTA countries has received approval while the application for authorization to export to non-FTA countries is still undergoing review.

Docket No.	Applicant	Application Filing Date	Date of FTA Export Approval	Status of Non-FTA Export Approval
12-47-LNG 12-101-LNG	Gulf LNG Liquefaction Company, LLC	2 May 2012 31 August 2012	15 June 2012	Under DOE Review
12-123-LNG	CE FLNG, LLC	21 September 2012	21 November 2012	Under DOE Review
12-152-LNG 13-153-LNG	Commonwealth LNG, LLC	12 October 2012	20 December 2012	Under DOE Review

⁷⁷ Office of Fossil Energy “Long Term Applications Received by DOE/FE to Export Domestically Produced LNG from the Lower-48 States (as of March 16, 2018)” online: <<https://www.energy.gov/sites/prod/files/2018/03/f49/Summary%20of%20LNG%20Export%20Applications.pdf>>.

⁷⁸ *Ibid.*

⁷⁹ *Ibid.*

⁸⁰ *Ibid.*

⁸¹ *Ibid.*

⁸² *Ibid.*

⁸³ *Ibid.*

	(Formerly Waller LNG Services, LLC)			
13-26-LNG	MPEH LLC	22 February 2013	24 May 2013	Under DOE Review
13-69-LNG	Venture Global Calcasieu Pass, LLC (Formerly Venture Global LNG, LLC)	13 May 2013	27 September 2013	Under DOE Review
13-115-LNG 13-116-LNG	Eos LNG LLC	23 August 2013	26 November 2013	Under DOE Review
13-117-LNG 13-118-LNG	Barca LNG LLC	23 August 2013	26 November 2013	Under DOE Review
14-56-LNG 15-78-LNG	Strom Inc.	18 April 2014	21 October 2014	Under DOE Review
14-88-LNG	Venture Global Calcasieu Pass, LLC (Formerly Venture Global LNG, LLC)	May 13 2014	10 October 2014	Under DOE Review
14-89-LNG 14-98-LNG	SCT&E LNG, LLC	9 July 2014	15 December 2014	Under DOE Review
15-25-LNG	Venture Global Calcasieu Pass, LLC	9 February 2015	17 June 2015	Under DOE Review
15-44-LNG 15-45-LNG	G2 LNG LLC	19 March 2015	17 July 2015	Under DOE Review
15-53-LNG 15-96-LNG	Port Arthur LNG, LLC	20 March 2015	20 August 2015	Under DOE Review
15-62-LNG	Texas LNG Brownsville LLC	15 April 2015	24 September 2015	Under DOE Review
15-97-LNG	Corpus Christi Liquefaction, LLC	1 June 2015	27 August 2015	Under DOE Review

15-190-LNG	Rio Grande LNG, LLC	23 December 2015	8 August 2016	Under DOE Review
16-15-LNG	Eagle LNG Partners Jacksonville LLC	27 January 2016	21 July 2016	Under DOE Review
16-28-LNG	Venture Global Plaquemines LNG, LLC	1 March 2016	21 July 2016	Under DOE Review
16-144-LNG	Driftwood LNG LLC	28 September 2016	28 February 2017	Under DOE Review
17-105-LNG	Fourchon LNG LLC	17 August 2017	11 March 2018	Under DOE Review

The oldest of these projects received FTA export approval within six weeks of filing, while its authorization to export to non-FTA countries has been pending for over five and half years.⁸⁴ Between the Pieridae case and these examples, the Canadian LNG sector clearly has good cause for their concern.

Relevant Treaty Provisions

Trade between the US and Canada is governed by several treaties. Two treaties are particularly important in relation to the US export licensing issue: the General Agreement on Tariffs and Trade 1994 (GATT 1994) and the North American Free Trade Agreement (NAFTA). The United States and Canada are both members of the WTO and hence subject to the disciplines set out in the GATT 1994. Under Article XI of the GATT 1994, members agree not to maintain quantitative restrictions

⁸⁴ Office of Fossil Energy “Gulf LNG Liquefaction Company, LLC - FE Dkt. No. 12-101-LNG (NFTA)” online: <https://webcache.googleusercontent.com/search?q=cache:mjEYzR8JchEJ:https://fossil.energy.gov/ng_regulation/applications-2012-gulflngliquefactioncompanyllc12-10+&cd=1&hl=en&ct=clnk&gl=ca>.

on exports, including restrictions implemented through export license requirements.⁸⁵ Specifically, Article XI(1) states that

No... restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licences or other measures, shall be instituted or maintained by any contracting party... on the exportation or sale for export of any product destined for the territory of any other contracting party.

This provision does not prohibit export licenses per se, but rather prohibits the imposition of trade restrictions implemented through export license requirements. Thus, the provision applies to measures such as the US natural gas export licensing process, which currently imposes restrictions on exports. US natural gas producers have even cited the country's GATT 1994 obligation to allow the free export of goods in their applications for export approval, and have argued that the "current restrictions on natural gas exports to non-FTA countries are clearly inconsistent with the obligations the US agreed to under the WTO and the...GATT."⁸⁶

If the US licensing regime were found to be in violation of Article XI(1), the regime would not be saved by any of the exceptions enumerated in Article XI(2) or Article XX. That includes Article XX(g), which creates a general exception for measures relating to the conservation of exhaustible

⁸⁵ *The General Agreement on Tariffs and Trade (GATT 1947)*. online World Trade Organization: <https://www.wto.org/english/docs_e/legal_e/gatt47_01_e.htm#articleXI>.

⁸⁶ Brian Scheid, Global Energy Institute, "Could Any Limits on the US Export of LNG Violate the Law?" (5 February 2013) online: <<https://www.globalenergyinstitute.org/could-any-limits-us-export-lng-violate-law>>.

natural resources, because such measures must be made effective in conjunction with restrictions on domestic production or consumption,⁸⁷ which the US export licensing regime does not do.

The *China-Raw Materials* cases offer a favourable precedent for challenging the US export permitting regime along these lines.⁸⁸ In 2009, the United States, along with Mexico and the European Union, initiated dispute settlement proceedings that challenged measures implemented by China which, the US and its co-complainants alleged, imposed restraints on the exports of several raw materials.⁸⁹ The forty identified measures included restrictions imposed through export licensing requirements, as well as restrictions imposed through export duties, export quotas, export quotas management, minimum export price requirements, and the administration and publication of trade regulations.^{90,91} In the 2009 case, the Panel found that China must bring its measures into compliance with its obligations, and that the measures were not saved by the Article XX(g) exception for exhaustible natural resources, and these findings were upheld by the Appellate Body.⁹² The fact that the United States was the complainant in this case offers the added benefit of potentially restricting the US' ability to credibly defend its imposition of restrictions on trade implemented through its own export licensing measures.⁹³

⁸⁷ The World Trade Organization “Analytical Index of the GATT – Article XX General Exceptions” page 562 online: <https://www.wto.org/english/res_e/booksp_e/gatt_ai_e/art20_e.pdf>.

⁸⁸ Brian Scheid, Global Energy Institute, “Could Any Limits on the US Export of LNG Violate the Law?” (5 February 2013) online: <<https://www.globalenergyinstitute.org/could-any-limits-us-export-lng-violate-law>>.

⁸⁹ The World Trade Organization Secretariat “DS394: China — Measures Related to the Exportation of Various Raw Materials” online: <https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds394_e.htm>.

⁹⁰ The World Trade Organization “China-Raw Materials Case - Summary of Key Findings” (2017) online: <https://www.wto.org/english/tratop_e/dispu_e/cases_e/1pagesum_e/ds394sum_e.pdf>.

⁹¹ World Trade Organization, Panel Report “China - Measures Related to the Exportation of Various Raw Materials - Reports of the Panel” (5 July 2011) Doc No. 11-3179, compiling WT/DS394/R, WT/DS395/R, and WT/DS398/R, at para 2.3.

⁹² *Supra* “China-Raw Materials Case - Summary of Key Findings”.

⁹³ *Supra* “Could Any Limits on the US Export of LNG Violate the Law?”.

Chapter Six of the existing NAFTA also includes several relevant provisions. Notably, Article 603(1) of the current Energy Chapter incorporates the language of the GATT.⁹⁴ While Article 603(5) states that the NAFTA parties may administer export licensing systems for energy goods, the provision requires that such systems be consistent with the rest of the NAFTA, including Article 603(1).⁹⁵ Recalling that Article XI does not prohibit export license requirements per se, but rather the imposition of trade restrictions implemented through measures such as export license requirements, Article 603(5) of the NAFTA can be read as allowing export license requirements that do not impose restrictions on trade.

Article 603(3) of the Energy Chapter also states that, where a NAFTA party maintains a restriction on energy exports to a non-NAFTA party, nothing in the NAFTA text prohibits that NAFTA party from requiring, as a condition of export to another NAFTA party, that energy goods from the exporting party be “consumed” within the territory of the importing party.⁹⁶ Consumed is defined for the purposes of the chapter in Article 609 as “transformed so as to qualify under the rules of origin set out in Chapter Four (Rules of Origin), or actually consumed”.⁹⁷ This provision suggests that the US licensing regime may be sanctioned, at least for the purposes of NAFTA. However, even if the current US measures are consistent with NAFTA, they remain inconsistent with the US’s WTO obligations.

⁹⁴ The Foreign Trade Information System of the Organization of American States “North American Free Trade Agreement - Chapter Six: Energy and Basic Petrochemicals” online:
<<http://www.sice.oas.org/Trade/NAFTA/chap-06.asp>>.

⁹⁵ *Ibid.*

⁹⁶ *Ibid.*

⁹⁷ *Ibid.*

Available Actions

Canada has at least three potential avenues it can pursue to address this trade irritant. First, it may negotiate for the addition of new language to the Energy Chapter that redefines “consumed” to include liquefaction and that deems certain export applications from the Parties to be for end use in such a way that those applications would always be put through the FTA country process and granted automatic approval. Second, Canada may challenge, or threaten to challenge, the US natural gas export permitting regime through the WTO dispute settlement process. Third, Canada may support current efforts to reform the US natural gas export licensing regime through Congress and may lobby for language that specifically address the issues affecting Canadian projects as a result of Order 3639.

The first available action involves taking advantage of the opportunity presented by the ongoing NAFTA negotiations to address the issue directly. In the new Energy Chapter, Canada could redefine “consumed” for the purposes of the Chapter to explicitly include liquefaction or to include umbrella terms for processes that would include liquefaction. Canada may also negotiate the addition of a new provision after 603(3), such as

4. Where an application to export an energy or basic petrochemical good from one Party to another for consumption⁹⁸ within the territory of the other Party is submitted to the relevant authority, the application shall be deemed to be an export application for end use of the good in the territory of the other Party for

⁹⁸ Consumption, in this case, now including liquefaction under the new definition for the chapter.

the purposes of determining the appropriate approval process for the application.

This language should be crafted to ensure that all applications seeking to export US natural gas to Canada avoid the country-of-end-use inquiry and benefit from the expedited FTA approval process.

The second action available to Canada involves challenging, or threatening to challenge, the trade restrictions imposed through the US export licensing regime as a violation of Article XI of the GATT 1994. While the *China – Raw Materials* cases offer a strong precedent⁹⁹ and such a case would have a good chance of success, Canada must consider the extent to which its own export licensing requirements may restrict its ability to credibly challenge the US regime.¹⁰⁰

In Canada, the National Energy Board (NEB) considers whether the volume of natural gas in an export proposal is surplus to Canada's domestic requirements.¹⁰¹ The *National Energy Board Act* originally imposed no time restrictions on the licensing process.¹⁰² In 2016, the *Act* was amended to include a new time limit whereby the NEB is now required to decide whether or not to issue an

⁹⁹ While panel and Appellate Body reports are not binding, they are generally highly persuasive.

¹⁰⁰ World Trade Organization “Legal Effect of Panel and Appellate Body Reports and DSB Recommendations and Rulings” (10 August 2004) online: <https://www.wto.org/english/tratop_e/dispu_e/disp_settlement_cbt_e/c7s2p1_e.htm>.

¹⁰¹ *National Energy Board Act*, RSC 1985, c N-7, Article 118 online: <<http://laws-lois.justice.gc.ca/eng/acts/n-7/section-118.html>>.

¹⁰² *National Energy Board Act*, RSC 1985, c N-7, version in force from 12 July 2010 to 5 July 2012, Article 117 (1) online: <<http://laws-lois.justice.gc.ca/eng/acts/n-7/20100712/P1TT3xt3.html>>.

export license within six months of receiving a complete application.^{103,104} Since the new time limit came into force, one import application and three export applications have been submitted. One export application was withdrawn, one export application, submitted in February 2018, is pending approval, the import application was approved within four weeks, and the remaining export application was approved within twenty-three weeks.¹⁰⁵ While the dataset for applications processed under the reformed approach is too limited to draw broad conclusions, these initial cases suggest that Canada's current licensing process does not impose significant restrictions on the trade of natural gas.

However, pursuing dispute settlement would also involve significant use of resources, both in terms of time and money. In the first fifteen years of the WTO's dispute settlement system, the average duration of WTO panel proceedings, excluding the time spent composing the panel and translating reports, was ten months.¹⁰⁶ In recent years, the average timeframe for proceedings, from the establishment of a panel to the adoption of a report, is sixteen months in cases that are

¹⁰³ Penny Becklumb & Mohamed Zakzouk, Economics, Resources and International Affairs Division, Library of Parliament "Legislative Summary of Bill C-46: An Act to amend the National Energy Board Act and the Canada Oil and Gas Operations Act" (21 May 2015) at para 2.8 online: <https://lop.parl.ca/About/Parliament/LegislativeSummaries/bills_ls.asp?Language=E&ls=c46&Parl=41&Ses=2&source=library_prb>.

¹⁰⁴ *National Energy Board Act*, RSC 1985, c N-7, Article 118.1(1) online: <<http://laws-lois.justice.gc.ca/eng/acts/n-7/page-27.html#h-89>>.

¹⁰⁵ National Energy Board, "Application Schedule – Export and Import Licence Applications" (1 March 2018) online: <<https://www.neb-one.gc.ca/pplctnflng/mjrpp/lngxprtlcnc/index-eng.html>>.

¹⁰⁶ Y. F. Agah (March 2011) "WTO Dispute Settlement Body Developments in 2010" online: <https://www.wto.org/english/tratop_e/dispu_e/speech_agah_4mar10_e.htm>.

not appealed and 21 months in cases that include an appeal.¹⁰⁷ Approximately two thirds of WTO cases are appealed.¹⁰⁸

While this process is much faster than some international dispute settlement processes, it still may not represent a worthwhile use of Canada's resources unless the impact of the trade irritant grows to merit greater action or Canada secures support from other countries impacted by the export licensing regime. Countries such as Japan and EU member states such as Germany, the intended end use country in the *Pieridae* case, may be interested in supporting such efforts.¹⁰⁹ Otherwise, the threat of action may simply offer a useful means of strengthening Canada's negotiating position.

The third option available to Canada is to bolster domestic US support for reforms, and to lobby for legislation that specifically addresses Canada's concerns. There is support amongst US natural gas producers, anti-regulation and pro-business organizations, and the current administration for reforms to address the negative impacts of the export licensing regime.¹¹⁰ Current proposals include a rule that will expedite the approval of small-scale natural gas exports and a new decision

¹⁰⁷ Iain Sandford, Jan Yves Remy & Colette Van Der Ven, "TPP Dispute Resolution: Settlement Mechanism Vs. WTO" (1 February 2016) online: <<https://webcache.googleusercontent.com/search?q=cache:JG2W-qlFgcEJ:https://www.law360.com/articles/752781/tpp-dispute-resolution-settlement-mechanism-vs-wto+&cd=20&hl=en&ct=clnk&gl=ca>>.

¹⁰⁸ *Ibid.*

¹⁰⁹ In the event that an individual EU member state, such as Germany, were interested in supporting Canada's case, it would have to persuade the EU Commission to pursue the case.

¹¹⁰ Nicolas Loris, the Heritage Foundation, Backgrounder, No. 3232, "Removing Restrictions on Liquid Natural Gas Exports: A Gift to the U.S. and Global Economies" (27 July 2017), online: <<https://www.heritage.org/sites/default/files/2017-07/BG3232.pdf>>.

deadline of 45 days for authorization to site, construct, expand, or operate LNG facilities.^{111,112} Canada's recent lobbying efforts to mobilize support for the preservation of NAFTA at all levels of the US government could turn, in part, towards supporting and steering similar domestic efforts.¹¹³

2. INFRASTRUCTURE AND STEEL TARIFFS

Canada has been struggling to give its liquefaction projects the momentum necessary to start construction. As previously mentioned, the decreasing prices for natural gas globally have jeopardized the future of Canadian LNG. The National Energy Board's outlook, as shown in its reference case for Canada's Energy Future 2016, assumes Canada's net natural gas exports all but halt in a low commodity cost scenario.¹¹⁴ In order for Canada to export LNG, prices must remain high enough to justify the high investments in infrastructure.

The infrastructure necessary to export LNG has also become costlier in light of the decision to subject some components to anti-dumping duties. In May 2017, the Canadian International Trade Tribunal ("CITT") found that certain fabricated industrial steel components were being dumped into Canada.¹¹⁵ This finding would allow for anti-dumping duties of up to 45.8% on components

¹¹¹ Secretary of Energy Rick Perry, "US Department of Energy Proposes Expedited Approval for Small-Scale Natural Gas Exports" (2017, September) <<https://www.energy.gov/articles/us-department-energy-proposes-expedited-approval-small-scale-natural-gas-exports>>.

¹¹² *TITLE II — INFRASTRUCTURE, Subtitle C—Trade, SEC. 2201*. online: <https://www.energy.senate.gov/public/index.cfm/files/serve?File_id=eb454e3b-7f32-479e-b1a6-e84f9019941d>.

¹¹³ David Ljunggren, "Canada Doubles Lobbying Efforts in Congress in Case Trump Pulls Out of NAFTA" (2017, November) online: <<https://globalnews.ca/news/3862053/canada-lobbying-trump-nafta/>>.

¹¹⁴ *Canada's Energy Future*, Supra.

¹¹⁵ *Certain Fabricated Industrial Steel Components* (June 9 2017), NQ-2016-004 (CITT) at para 1.

essential to the construction of export terminals. For one project, this represents an estimated cost increase of \$1 billion on the original \$40 billion project price tag.¹¹⁶

Certain LNG proponents submitted a request to the CITT asking that these components be excluded from this dumping determination. The tribunal denied this request alongside its finding of dumping. The reasons given for this denial was that the tribunal did not have a firm indication of what it was being asked to exclude, stating that the requests were highly speculative and overly general.¹¹⁷ This suggests that the industry still has work to do before a Remission Order, or other relief would be appropriate. Requisite steps may include providing final plans, and more evidence to demonstrate that the required components are unavailable from other suppliers.

Given the decreasing commodity costs, and the growing infrastructure costs the market for LNG export facilities is not as inviting to investors. The prospect of a lack of profitability has scared some stakeholders. There is speculation that Chevron is looking to sell their stake in one of its joint projects in Kitimat.¹¹⁸

The CITT has the authority to grant exclusions from its findings in the preliminary injury assessment, with the guiding principle that imports of particular products have not caused injury.¹¹⁹

¹¹⁶ Ben Nelms, “Federal Government to Rule on Spat Between Steel Fabricators, LNG Canada”, *The Globe and Mail* (23 January 2018), online: <<https://www.theglobeandmail.com/report-on-business/industry-news/energy-and-resources/federal-government-to-rule-on-spat-between-steel-fabricators-lng-canada/article37712245/>>.

¹¹⁷ *Certain Fabricated Industrial Steel Components*, *Supra* 34 at para 161.

¹¹⁸ John Tilak, “Exclusive: Chevron in Talks to Sell Stake in Canada LNG Project – Sources”, *Reuters*, (5 March 2018), online: <<https://www.reuters.com/article/us-chevron-canada-exclusive/exclusive-chevron-in-talks-to-sell-stake-in-canada-lng-project-sources-idUSKBN1GH2XJ>>.

¹¹⁹ *Supra Certain Fabricated Industrial Steel Components*, at para 151.

The Tribunal considers factors such as whether the domestic industry produces, actively supplies or is capable of producing like goods compared to the subject goods.¹²⁰

The Tribunal's decision to reject the request for an exemption noted that no engineering procurement and construction (EPC) firm was chosen for the proposed Kitimat plant.¹²¹ These engineering firms typically consult with fabricated industrial steel component (FISC) purchasers before sourcing materials and constructing the components.¹²² The Tribunal ultimately decided that they did not have a firm enough understanding of what they were being asked to exclude from their determination and denied the request on that basis.¹²³

In light of the Tribunal's finding, Global Affairs Canada has an opportunity to assist the industry in securing a Remission Order. The *Financial Administration Act*, s. 23(2) allows for the Governor in Council to issue a Remission Order on the recommendation of the Finance Minister if it would not be in the public interest to enforce these anti-dumping duties. Under s. 45 (1) of the *Special Measures Import Act (SIMA)* the CITT must initiate a public interest inquiry if the Tribunal believes there are reasonable grounds to consider that the imposition of an anti-dumping duty might not be in the public interest.¹²⁴ The section further provides that a report shall be provided to the Minister of Finance and made publicly available if the Tribunal opines that the imposition of the duty in the full amount is contrary to the public interest.¹²⁵

¹²⁰ *Ibid* at para 152.

¹²¹ *Ibid* at para 161.

¹²² *Ibid* at para 12.

¹²³ *Ibid* at para 161.

¹²⁴ *Special Import Measures Act* (R.S.C., 1985, c. S-15).

¹²⁵ *Supra Special Import Measures Act*, at s. 45(4), s. 45(5).

It has become characteristic in these inquiries for the Tribunal to note that there is no provided definition of the public interest, nor has the Tribunal gone to the length of providing a definition itself. In fact, s. 45(3) of *SIMA* gives the board broad discretion to consider any factors that it considers relevant to its inquiry.¹²⁶

In the leading decision of the Tribunal in *Refined Sugar*, the tribunal seemed to be strictly interested in balancing the competing commercial interests of consumers and domestic producers and downstream domestic purchasers, including consumers.¹²⁷ In that instance the Tribunal did not find that the public interest warranted a reduction or elimination of the anti-dumping duties imposed and did not report to the Minister of Finance per s. 45 of *SIMA*. The Tribunal noted that refining margins (which were the subject of the dispute rather than just prices) were not likely to increase significantly, so they did not find a significant adverse effect on the interested parties.¹²⁸

In contrast the Tribunal did find public interest grounds to reduce anti-dumping duties in *Prepared Baby Foods*.¹²⁹ Here, in addition to the commercial interests of producers and suppliers, the Tribunal considered evidence regarding the welfare of low-income homes and the health of infants.¹³⁰ The Tribunal also considered the competitiveness of the domestic producer, and the viability of an upstream supplying farm, and specifically how its closure would impact the surrounding community.¹³¹ The recommendations were made so that competition could be restored to the industry, with the view of balancing these competing interests.¹³²

¹²⁶ *Ibid.*

¹²⁷ *Refined Sugar* (August 28, 1996), PB-95-002 (CITT).

¹²⁸ *Ibid* at Conclusion para 3.

¹²⁹ *Certain Prepared Baby Foods* (November 30, 1998) PB-98-001, (CITT) Report to the Minister of Finance.

¹³⁰ *Ibid* at page 11 para 2.

¹³¹ *Ibid* at page 11 para 2.

¹³² *Ibid* at page 54 at para 7.

Recommendation: Help Secure a Remission Order by Emphasizing That Canada's Trade Based Interest Will be Advanced by LNG Exports

Global Affairs Canada can assist the industry to ensure the issuance of a Remission Order by using its expertise to advise the Minister of Finance of the public interest in pursuing a Canadian role in the global LNG trade. Just as the Tribunal considered aspects of child nutrition in *Prepared Baby Foods*, the Minister may consider public welfare beyond the immediate financial implications of competing foreign and domestic suppliers. Global Affairs would be able to inform the Minister with insight as to how Canada's international interests would be advanced, and why they are worth advancing over the alternative of leaving the anti-dumping duties as they are. Specifically, Global Affairs Canada can provide the Minister with insight into the importance of Canada's energy trade, its need to diversify its exports to include LNG, and the potential gains from such diversification.

The most obvious benefit that Global Affairs Canada will be able to speak to is the economic boost Canada would experience if it were able to export LNG. Global Affairs Canada has the resources to provide more independent estimates on the number of jobs that would be created, and of materials that would be sourced domestically. In a letter sent from the Canadian Association of Petroleum Producers to the Finance Minister, the industry claimed that domestic steel producers stood to benefit from a Remission Order as well.¹³³ The unpublished letter claimed that thousands of tonnes of domestically-sourced reinforced steel would be needed to complete the project.

¹³³ Brent Jang, "Shell Maps Out LNG Plan for Northeast B.C.," *The Globe And Mail* (April 1, 2018) online: The Globe And Mail <<https://www.theglobeandmail.com/business/article-shell-maps-out-lng-plan-for-northeast-bc/>>.

In *Prepared Baby Foods*, the Tribunal made considerable mention of the importance of a farm to the economic welfare in the local community. Hence a similar argument that the facility would be of central importance to the welfare of the community may be persuasive. In Kitimat the unemployment rate reported in the latest census was 12.5%. This is almost twice the 6.7% average for British Columbia as a whole.¹³⁴ With a labour force of only 4,230 for that same period, employment in Kitimat would surely benefit if liquefaction facilities were able to break ground on project construction. This argument would not remain uncontested, as domestic steel proponents would argue that other communities would suffer for these gains. However, given the economic struggle of Kitimat and the limited nature of the Remission Order sought by the applicants, this argument may not persuade the Minister.

The Canadian public interest would also be advanced by developing an LNG trade because of the implications it would have for trade in China. Global Affairs Canada has listed developing a comprehensive whole-of-government engagement strategy with China as one of its priorities.¹³⁵ As stated earlier, the focus of Canada's LNG market would be serving the increasing Asian demand for LNG. China is already a major importer and recently overtook South Korea as the world's second largest LNG importer globally. With its growing appetite for cleaner energy, LNG could be a significant part of a broader conversation to align Canadian and Chinese interests. Ensuring Chinese dependence on Canadian energy would assist Canada in facilitating this strategy.

¹³⁴ Statistics Canada accessed at <<http://www12.statcan.gc.ca/census-recensement/2016/dp-pd/prof/details/page.cfm?Lang=E&Geo1=PR&Code1=59&Geo2=CSD&Code2=5949005&Data=Count&SearchText=kitimat&SearchType=Begins&SearchPR=01&B1=All&TABID=1>>.

¹³⁵ Global Affairs Canada (2017), "Priorities" online: <<http://www.international.gc.ca/gac-amc/priorities-priorites.aspx?lang=eng>>.

Another consideration is that a Remission Order can be worked into the ongoing conversation between Canada and China regarding trade. Some have opined that the Canadian industry is doomed without the Canada's government creating policy to secure Chinese investments and greater access to the market.¹³⁶ A Remission Order may advance this possibility.

Despite delivering their recommendations to the Minister directly, Global Affairs Canada can still play a role in ensuring that a public interest hearing is held, perhaps even on an advanced timeline. In 2017 a Remission Order was granted on gypsum board products.¹³⁷ The Finance Minister took unprecedented action to move the Tribunal's review process along by asking them to consider the public interest immediately instead of after the Tribunal's initial ruling. In this instance a request was made in October to have the report ready for the following January.¹³⁸ This decision was motivated by the extraordinary circumstances and mounting public pressure caused by the Fort McMurray wildfires, as communities were desperate to rebuild from the disaster.

It is unlikely that the Finance Minister will extend these same sympathies to LNG proponents and fast track the investigation. The initial finding of injury has already been reached, and the stakes are not the same. The need to develop infrastructure to transport fossil fuels to other continents makes for a less persuasive case than tragedy-stricken families importing raw materials to move

¹³⁶ Nathan Vanderklippe, "China Renews Commitment to Less Coal, More Natural Gas" *The Globe and Mail* (July 10, 2017). online: <<https://www.theglobeandmail.com/report-on-business/industry-news/energy-and-resources/china-renews-commitment-to-less-coal-more-natural-gas/article35627780/>>. See also Rober Jonston and Weran Jian, "Now is the Time for a Strong Canada-China Energy Partnership" *The Globe and Mail* (December 4, 2017). online: *The Globe and Mail* <<https://www.theglobeandmail.com/opinion/now-is-the-time-for-a-strong-canada-china-energy-partnership/article37174324/>>.

¹³⁷ *Gypsum Board Products Anti-Dumping Duty Remission Order, 2017*. Canada Gazette Vol. 151, No. 5 (8 March 2017).

¹³⁸ Karina Roman, "Ottawa Orders Review of Drywall Tariffs in Western Canada" *CBC News* (17 October 2016). online: CBC <<http://www.cbc.ca/news/politics/drywall-tariffs-alberta-construction-1.3808633>>.

on from their losses. Nonetheless, this case demonstrates that it is possible to hasten the process for receiving a Remission Order. We propose that Global Affairs Canada makes a recommendation to the Finance Minister to order a public interest hearing.

3. CANADA'S ARDUOUS REGULATORY MATRIX

The Issue

The Canadian regulatory matrix for natural gas products puts prospective LNG projects through a complex and costly procedure.¹³⁹ Project proponents need a legal team with specialists in environmental law, energy, taxation, regulatory, commercial, financial, Aboriginal, labour, international trade, intellectual property, and other areas of law. Each facility requires access to gas reserves via pipelines, with each step of the facility development process requiring approvals and permits.¹⁴⁰

Given that the regulations and required permits for gas production and facilities, pipelines, and LNG facilities are similar, the focus of this section will be on parallel federal and provincial regulations on the construction and operation of LNG facilities. Additionally, due to recent high-profile LNG project cancelations on the West Coast and significantly greater commercial interest in the area, the focus of this section will be on BC.

LNG projects face various levels of federal, provincial and municipal regulations. For example, in BC, proponents need permits pertaining to the British Columbia Utilities Commission,

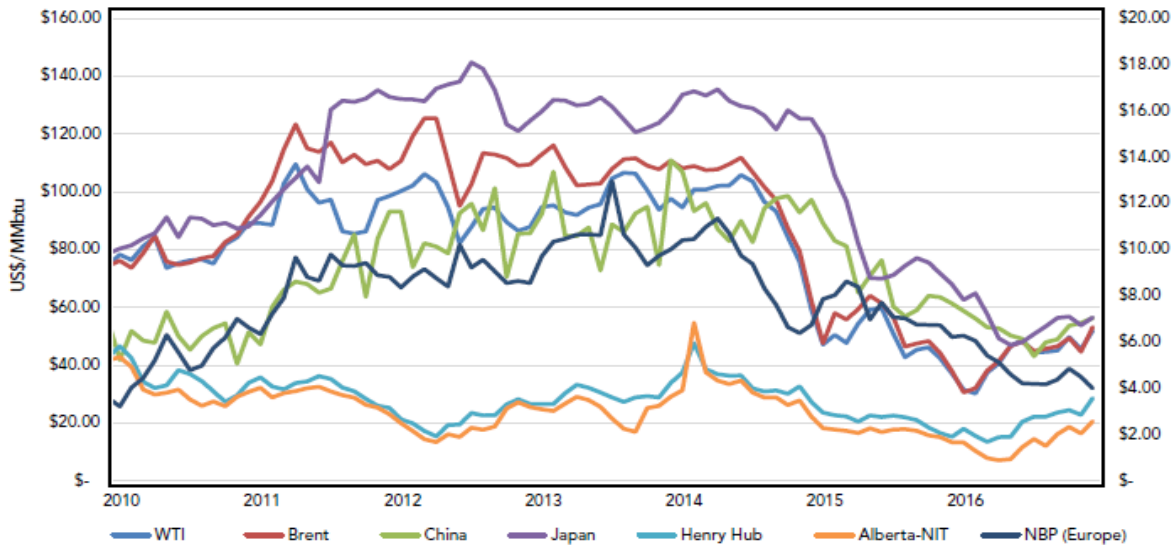
¹³⁹ "Liquefied Natural Gas (LNG) Regulation in British Columbia", *McCarthy Tetrault*, (February 2017), online: <http://www.mccarthy.ca/pubs/LNG_Regulation_in_BC_February_2017.pdf> at 7 [*BC LNG*].

¹⁴⁰ *Ibid* at 7-8.

Environmental Assessments, water use, contaminated site usage and water discharges on top of the general permits required by the *Oil and Gas Activities Act*.¹⁴¹ In addition to these provincial permits, proponents might also have to get approval from a federal environmental assessment, an NEB export license, *Investment Canada Act* permits, while following other federally regulated procedures.¹⁴² Project proponents must follow these industry specific regulatory regimes in addition to getting general municipal building and zoning approvals from the city.¹⁴³

Following the recent Petronas LNG project cancelation in BC, insiders have claimed that market factors, in addition to the five-year regulatory approval process, added excess risk and uncertainty to the project, resulting in its cancelation.¹⁴⁴ Analysts speculate that if the project had received approval earlier, Petronas would likely have committed to building the project.¹⁴⁵

Global Historical LNG Prices and the WTI Oil Price



Source: Canada’s Role in the Global LNG Market – Energy Market Assessment July 2017, National Energy Board

¹⁴¹ *Ibid* at 25-33.

¹⁴² *Ibid* at 33-36.

¹⁴³ *Ibid* at 36-37.

¹⁴⁴ Andrew Leach, “Why Petronas Cancelled its Plans for an LNG Project on BC’s Coast”, *Maclean’s*, (29 July 2017), online: <<http://www.macleans.ca/economy/economicanalysis/why-petronas-cancelled-its-plans-for-an-lng-project-on-b-c-s-coast/>> [*Petronas Article*].

¹⁴⁵ *Ibid*.

Natural gas price spreads between Alberta and Japan were the highest between 2011 and 2015, but since then, global prices have come into closer balance, with Japanese gas spot prices decreasing but remaining higher than BC and Alberta gas prices. With these lower global prices, project proponents have recalculated their options, and some have determined that going forward is not feasible in this climate.¹⁴⁶ Petronas submitted their project for approval in 2012, and after five years of waiting for regulatory licenses, the window of opportunity closed.¹⁴⁷ The existing lengthy and complex regulatory process arguably played a key role in the cancellation of this project and the Douglas Channel, Prince Rupert and Aurora LNG projects.¹⁴⁸

Excess delay has been a major driver of project cancellations because project proponents are essentially gambling on what the price of natural gas in another country will be three to five years down the line, while incurring significant costs now. The higher uncertainty and delay there is in a process, the higher the risk of moving forward with the project. Petronas' five-year regulatory delay caused them to miss the then available window of profitability. There is a clear need for reform to cut approval times and increase transparency and predictability to prevent the cancellation of future projects.

Recommendation: Streamline Canada's Regulatory Matrix by Authorizing a Single Regulatory Body to Perform Duties under Both Federal and Provincial Regulations

Global Affairs Canada can address Canada's complex regulatory structure by advocating for a single LNG regulatory body within the federal government and by working with other agencies to

¹⁴⁶ *Canada LNG Report, supra.*

¹⁴⁷ *Petronas Article, supra.*

¹⁴⁸ *Canadian LNG Projects, supra.*

assist with consolidating the approval authority for LNG projects in Canada. An example of what such a body could look like already exists in BC. Under the *Oil and Gas Activities Act*, the Oil and Gas Commission (OGC) is the principal regulator of oil and gas activities in BC, and they have broad authority to regulate oil and gas exploitation in the region.¹⁴⁹ Specifically, the OGC administers permits for heritage conservation, water use, water discharge, and regulates the construction, design, risk assessment, safety and emergency planning of LNG facilities.¹⁵⁰

The federal government can streamline the lengthy LNG regulatory process by authorizing the OGC or similar provincial bodies to perform front-end duties under federal regulations. The federal government would still retain its constitutional authority to regulate federal areas, but could then delegate the front-end, administrative duties to another agency in partnership with a province. While this task does not fall squarely within the ambit of Global Affairs Canada, the Department can play a key role in advocating for this change within the federal government. Areas such as the NEB export license, *Investment Canada Act* requirements, and environmental assessments could become further streamlined by continuing with the “single window” policy approach. East Coast provinces with proposed LNG export facilities like Quebec, New Brunswick, and Nova Scotia, could also adopt a similar regime. The federal government would only be delegating administrative authority to these consolidated regulators, while still maintaining its authority to regulate.

With respect to feasibility, BC and the federal government already have a similar initiative within the *Federal Port Development Act* (FPDA). This act authorizes a provincial body to exercise a

¹⁴⁹ *BC LNG, supra* at 11.

¹⁵⁰ *Ibid.*

power or perform a duty under a federal regulation in relation to federal port lands. Pursuant to the FPDA, the OGC can regulate the construction and operation of LNG facilities on federal port lands, a duty normally reserved for federal regulators.¹⁵¹ This was part of BC's strategy to provide regulatory certainty to LNG project proponents so that investors can move forward knowing the rules that apply and that provincial officials can ensure projects are safe and sustainable.¹⁵²

Canada recently unveiled a plan to introduce a new energy regulator to provide greater efficiency and consistency by offering a single agency that works closely with regulatory bodies.¹⁵³ While full details of this new regulator have not yet been made public, the available details show that the new agency will have greater coordination with provinces and territories to reduce bureaucracy and redundancy in provincial and federal regulatory regimes.¹⁵⁴ Any Canadian strategy for LNG should continue this trend of streamlining and consolidating regulatory regimes. Working alongside provinces, these consolidated regulators will then have broad authority to deal with all aspects of the LNG industry, from dealing with gas supply, pipeline infrastructure, to the approval and construction of LNG facilities. Pursuing a goal of consolidating overlapping regulatory regimes will provide predictability to project proponents and reduce the delays that create market uncertainty.

¹⁵¹ *Ibid* at 32.

¹⁵² "Act positions BC to regulate liquefied natural gas (LNG) in federal ports", (16 February 2015), *BC Gov News*, online: <<https://news.gov.bc.ca/stories/act-positions-bc-to-regulate-liquefied-natural-gas-lng-in-federal-ports>>.

¹⁵³ "Better rules to protect Canada's environment and grow the economy", *Projects and Environmental Assessments*, online: <<https://www.canada.ca/en/services/environment/conservation/assessments/environmental-reviews.html#pb>>.

¹⁵⁴ *Ibid*.

V. Conclusion

While global natural gas prices have fallen, and the window of opportunity is shrinking, Canada still has the potential to successfully enter the global LNG market as an exporter. Through the implementation of a multi-faceted LNG strategy, the Canadian government can address the issues impacting the industry's competitiveness and seize this opportunity to grow and diversify Canadian energy exports. This strategy should include amending or eliminating the US export licensing regime, approving targeted steel tariff exemptions for LNG projects, and consolidating approval authority for LNG projects. Global Affairs Canada can play a key role in both the export licensing negotiations and negotiations aimed at optimizing the benefits from access to efficiently priced components and access to US produced gas. Overall, the successful pursuit of a unified LNG strategy would allow the Department to promote free trade, enhance the competitiveness of the North American energy industry, diversify Canadian energy exports to include greener transition commodities and advance Canadian business interests.