

**Petition to the Governor in Council to refer
Telecom Decision CRTC 2006-15
*Forbearance from the regulation of
retail local exchange services*
back to the Canadian Radio-television and
Telecommunications Commission for reconsideration**

by:

Aliant Telecom Inc.;
Bell Canada;
Saskatchewan Telecommunications;
and
TELUS Communications Company

12 May 2006

Table of Contents

	<u>Page</u>
1.0 THE NEED FOR CHANGE	1
2.0 CRTC'S FLAWED APPROACH TO REGULATION.....	6
Lack of comprehension of basic economic principles	7
Flawed view of competition	8
Flawed view of the role of regulation	10
Unwillingness or inability to reform regulation	12
Out-of-step internationally	12
3.0 SOME SPECIFIC PROBLEMS WITH DECISION 2006-15	13
3.1 Forbearance Test	14
i) Market share loss	15
ii) Wholesale criteria	16
iii) Rivalrous behaviour	17
3.2 Pre-forbearance Rules.....	18
4.0 RELIEF REQUESTED	19

1.0 THE NEED FOR CHANGE

1. On 6 April 2006, the Canadian Radio-television and Telecommunications Commission (the CRTC or the Commission) issued *Forbearance from the regulation of retail local exchange services*, Telecom Decision CRTC 2006–15 (Decision 2006-15, or the Decision). In the Decision, the Commission purported to establish a detailed framework for implementing local forbearance. Specifically, the Commission made determinations regarding the relevant product and geographic markets for retail local exchange services and determined that it would entertain forbearance applications once an incumbent telephone company had suffered a 25% market share loss in the relevant geographic market for which forbearance is sought.

2. In addition, the Commission imposed numerous conditions on incumbent telephone companies requiring, among other things, that (1) the incumbent telephone companies meet for the preceding 6 months individual standards for 14 competitor quality of service indicators, (2) incumbent telephone companies have in place a number of competitor service tariffs, (3) incumbent telephone companies have implemented competitor access to their operational and support systems where required and (4) the incumbent telephone company has demonstrated to the Commission's satisfaction that rivalrous behaviour exists in the relevant market. As a result, the Commission has created great uncertainty in the industry as to when relying on market forces, as recommended by the Telecommunications Policy Review Panel (the Panel), rather than detailed economic regulation might actually occur.

3. On 22 March 2006, the Panel transmitted its Report to the Minister of Industry laying out a comprehensive plan for reform of Canada's telecommunications policy and regulatory framework. Notably, the overall thrust of the Report's recommendations concerning economic regulation was that competitive market forces can now achieve many of Canada's telecommunications policy objectives without regulatory or government intervention. The Panel continually underscored that there should be a general predisposition in favour of reliance on market forces. In support of that view, and after a comprehensive and exhaustive process, the Panel highlighted the very substantial level of competition that has emerged in Canadian telecommunications markets, including the establishment of at least two competitive local access network infrastructures in the large majority of Canadian markets.

4. Despite the Panel's unequivocal finding that very substantial competition exists in the local access and other telecommunications markets, the Panel found that there was an enduring predisposition in our current regulatory framework in favour of regulatory interference.

The Panel's recommendations highlight the considerable economic costs and inefficiencies that this predisposition continues to impose, but also the fact that Canadian consumers continue to be denied the benefits of competition. Rather than creating a mechanism for achieving forbearance, the Commission codified continuing regulatory obligations unrelated to a reliance on market forces and has thereby created great uncertainty in the market.

5. The Minister of Industry is currently studying the Panel's Report. However, the Report's recommendations have already been employed in evolving Canada's telecommunications framework. On 5 May 2006, the Government of Canada referred, *Regulatory Framework for Voice Communication Services Using Internet Protocol*, Telecom Decision CRTC 2005-28 - the VoIP (Voice over Internet Protocol) decision - back to the Commission for reconsideration. In his news release announcing the decision, the Honourable Maxime Bernier stated: "In order to encourage innovation and productivity, it is imperative that regulatory measures interfere as little as possible with competitive market forces."¹ In addition, Minister Bernier specifically referenced the detailed work done by the Panel and commended the Report to the CRTC in its reconsideration. This is a significant endorsement of the key thrust of the Panel's recommendations and is an important statement by a key stakeholder in Canada's telecommunications industry.

6. With this Petition,² Aliant Telecom Inc., Bell Canada, Saskatchewan Telecommunications and TELUS Communications Company (collectively, the Companies) are asking the Governor in Council to address on an urgent basis the serious situation arising from the Decision. The CRTC's Decision claims to set out the details of a framework for removing economic regulation from the traditional telephone companies' local exchange services (de-regulation).³ It does no such thing. As with the VoIP decision, the CRTC has set out a path not to de-regulation, but to further and more detailed regulation, with no end in sight. If allowed to stand, Decision 2006-15 will ensure that markets for local service will continue to be regulated for years to come, even though competitive market conditions are sufficient to protect the interests of customers. Canadian telecommunications customers whether consumers, small or medium businesses, large enterprises, government or institutions will not reap the full benefits of competition in terms of expanded choice of competitive prices and promotions, innovative

¹ Industry Canada News Release, *Government of Canada Refers CRTC Decision on VoIP Back to the Commission for Reconsideration*, 5 May 2006.

² Filed pursuant to section 12(1) of the *Telecommunications Act*.

services and bundles. Investment opportunities in Canada will be negatively affected. Efforts to increase the productivity of Canada's economy and to improve the well-being of ordinary Canadians will be hampered.

7. In order to encourage innovation and productivity by ensuring that regulatory measures interfere as little as possible with competitive market forces, the Companies request the Governor in Council to refer Decision 2006-15 back to the CRTC to make it conform within 90 days. Further, the Companies request that the Commission be directed to reconsider Decision 2006-15 including its pre-forbearance, forbearance and post-forbearance rules in light of the conclusions and recommendations contained in the Telecommunications Policy Review Panel Report.

8. In most parts of Canada today, telecommunications customers have several choices of local service provider. For business customers, the traditional telephone companies offer service in their former incumbent territories as well as across Canada (for example, Bell Canada, TELUS and MTS Allstream). There are also a variety of well-established, multi-billion dollar global players such as AT&T, British Telecom and BT Infonet, Equant (a subsidiary of France Telecom), Avaya (a spin-off of Lucent), Cisco, IBM and Microsoft. For a number of years, business customers have been telling the CRTC that the time has come to stop economic regulation of the incumbents in order that there can be free choice between telecommunications suppliers. In its submission in the local forbearance proceeding, the Coalition for Competitive Telecommunications (the Coalition),⁴ representing the leading Canadian business trade and service associations for more than 12,000 Canadian companies, asked the Commission to respond to the interests of telecommunications users through greater reliance on market forces:

"The Coalition encourages the Commission to allow negotiated contract arrangements, as freely determined by users and suppliers, to play a leading role in the provision of all telecommunications services, including local services. Where choice is available to a business customer, the ability of the customer to exercise that choice (or the threat by the customer to do so) constitutes a powerful and effective discipline on suppliers. It also constitutes the remedy

³ The Companies and the other traditional telephone companies are often referred to as "incumbent local exchange carriers" (ILECs), or "incumbents", based on their former status as sole providers of wireline local exchange services in their traditional serving areas.

⁴ Including The Association of Canadian Acquirers; The Association of Canadian Travel Agencies; The Canadian Depository for Securities Limited; Canadian Manufacturers & Exporters; Megatrade Communications Services Corp.; The Canadian Newspaper Association; Insurance Bureau of Canada; The Investment Dealers Association of Canada; The Investment Funds Institute of Canada; Retail Council of Canada; and Société de gestion du réseau informatique des commissions scolaires.

which business users apply to all their other suppliers and is far quicker, more efficient, more certain and more effective than any regulatory system".⁵

9. Perrin Beatty, president and CEO of the Canadian Manufacturers and Exporters and federal minister of communications from 1991 to 1993, contrasted the finding of the federal government's Telecommunications Policy Review Panel with the kind of regulatory regime set out in Decision 2006-15, and cited the potential harm to consumers and the economy if Decision 2006-15 is allowed to stand:

"In its [the TPRP's] words, 'Canada has more relatively intrusive, complex and costly regulation of major telecommunications service providers, with more extensive prior regulatory approval requirements and longer regulatory delays.'

This kind of regulatory regime poses significant potential harm to consumers and the economy. As I told the Senate committee reviewing the *Telecommunications Act* in 1992, 'any company wishing to compete today must be able to identify, target and penetrate new markets more quickly than ever before.' The last thing they need is for their path to be strewn with regulatory obstacles."⁶

10. The vast majority of consumers can now choose between at least two local telephone service providers (typically, the traditional telephone company and the incumbent cable provider). In most cases consumers also have several additional choices, for example, local service resellers, Canadian and foreign providers of VoIP services that run over high-speed Internet connections, as well as several choices of wireless service provider. And Canadians have demonstrated that they like this choice by switching among service providers

11. The Decision is emblematic of the fact that the CRTC is out of touch with market realities. This is exemplified by its out-of-date view that Canadians do not use mobile wireless service as a real competitive alternative to traditional wireline telephone service. As a consequence of this view, Decision 2006-15 does not take into account market losses to mobile wireless services in the test for de-regulation.⁷ This is a very short-sighted view, as was graphically demonstrated by a Statistics Canada report issued on 5 April 2006, the day before Decision 2006-15 was issued. Statistics Canada reported that "[t]he proportion of Canadian households relying only on cellphones ...has more than doubled [going from 1.9% to 4.8%] in

⁵ *Comments of the Coalition for Competitive Telecommunications*, Telecom Public Notice CRTC 2005-2, 22 June 2005, paragraph 10.

⁶ Perrin Beatty, *Choose not to regulate: Government must take the reins from the CRTC before Canada falls behind in the fast-paced telecom industry*, Ottawa Citizen, 19 April 2006.

⁷ Decision 2006-15, paragraph 61.

just over two years". In Vancouver, the percentage was 9.6%.⁸ In this regard, it is worth noting that in the cable TV market, the CRTC removed economic regulation for a cable company once it had lost just 5% of its cable customers.⁹ If the same rule was to be applied to telephony, it is likely that, in many markets, loss of households to cellphone service would alone already be sufficient to warrant de-regulation of the Companies' local services.

12. The Competition Bureau has also urged the CRTC to rely on market forces instead of regulation, all in the best interests of Canadians:

"The Bureau believes the issues being raised in this proceeding, namely a framework for forbearance from regulation of local telephone service, are critical to the development of competitive local telephone services in Canada. Greater reliance on market forces and competition in place of regulation should provide significant benefits to Canadians in terms of competitive prices, greater choice, innovative services, as well as enhanced service quality."¹⁰

13. As many commentators, including the Panel, point out, the CRTC's main objective appears to have been to promote the financial viability of the traditional telephone companies' competitors, rather than to promote competition itself. This has engendered a high level of regulatory intervention to micro-manage market outcomes and allocate market shares, rather than allowing market forces to determine the success or failure of different service providers. The interests of customers in more choice and competitive pricing have received little attention. Terence Corcoran, writing in the *Financial Post* shortly after the Decision, pulled no punches when he wrote: "[T]he whole exercise is misguided. By preventing the phone companies from competing on price, and imposing other rules on the companies, the CRTC is effectively ignoring market realities and killing dynamic market competition." In Mr. Corcoran's view, the CRTC's measures will ensure that "...more than 75% of phone users will continue to pay higher rates until [the CRTC's] market share targets are met."¹¹

14. Both in form and in substance, the CRTC's Decision is in stark and stunning contrast to the final report of the TPRP. The Panel understands the benefits of competition when it states that "[c]ompetitive market forces can process more information and do so more efficiently than any ...regulator" and that "[c]ompetitive markets provide superior incentives to service providers" because "service providers can prosper only to the extent that they meet the needs

⁸ Statistics Canada, *The Daily*, 5 April 2006, page 5.

⁹ CRTC, *Broadcasting Distribution Regulations*, s. 47(1)(b)(iii)(B)

¹⁰ *Telecom Public Notice CRTC 2005-2, Forbearance from regulation of local exchange services: Argument of the Commissioner of Competition*, 15 September 2005, paragraph 3.

of customers".¹² In the Panel's view the time has come to free telecommunications markets from economic regulation in order to better achieve economic and social benefits for Canadians:

"[T]he time has come to reform Canada's telecommunications policy and regulatory framework. In spite of the fact that Canada has one of the most competitive telecommunications markets in the world, we continue to have one of the most detailed, prescriptive and costly regulatory frameworks. This framework is particularly burdensome for Canada's major telecommunications service providers, who now face stronger competition in a number of market segments from well-established facilities-based rivals as well as from new entrants. The Panel believes the Canadian telecommunications industry has evolved to the point where market forces can largely be relied on to achieve economic and social benefits for Canadians, and where detailed, prescriptive regulation is no longer needed in many areas."¹³

15. The Panel sees what the CRTC seems unwilling or unable to accept, namely that this is not the time to approach competition timidly and in "baby steps". Canada is rapidly falling behind the times and is out of step with other countries around the world. Internationally, governments are putting in place policies for all telecommunications markets which allow market forces to operate free of *ex ante* price controls and marketing restrictions. These governments rely on the authorities responsible for enforcing competition law -- or on sector-specific regulation based on competition law principles -- to deal with cases of abuse of dominance.¹⁴

16. For all of the foregoing reasons, and as is explained in further detail below, the Companies request that the Decision be referred back to the Commission for reconsideration with a direction to render its determination within 90 days.

2.0 CRTC'S FLAWED APPROACH TO REGULATION

17. Decision 2006-15 encapsulates the CRTC's entire approach to regulation: one that is flawed and harmful and one that has been roundly condemned by the Panel in its Report and by an increasing number of public commentators. The Decision reflects a lack of comprehension of basic economic principles, a flawed view of competition and of the role of regulation, an unwillingness -- or inability -- to reform regulation, and an approach that continues to be out-of-step internationally.

¹¹ Terence Corcoran, *Goldilocks and the forbearance mess*, Financial Post, 13 April 2006.

¹² *Final Report*, Telecommunications Policy Review Panel, March 2006 (TPRP Report), page 3-5.

¹³ TPRP Report, page 1-22.

¹⁴ TPRP Report, page 1-22.

Lack of comprehension of basic economic principles

18. Decision 2006-15 demonstrates that the CRTC either lacks comprehension of the basic economic principles which determine when competitive conditions are such that market forces can be relied on to protect the interest of customers – or is unwilling to employ such principles in its determinations. Instead, the CRTC has, at least in recent years, adopted the regulatory principle of "balancing" competing interests. The result is unprincipled and often inconsistent decisions that impose arbitrary conditions and competition-dampening marketing restrictions on the traditional telephone companies.

19. Decision 2006-15 is no exception. As discussed in more detail in section 3, the CRTC's so-called "Forbearance Test" includes a number of criteria which are not necessary and have already, in the case of Aliant in Halifax, resulted in failure to de-regulate when the economic conditions for de-regulation are clearly present.¹⁵ Similarly problematic, is where the Commission establishes the market share threshold of 25% on the basis that it "strikes the right balance between ...competing interests".¹⁶ The Commission in determining the threshold did not assess whether significant market power exists at a 5% market share threshold – as was the case with cable rate de-regulation – let alone an assessment at 25%.

20. The Commission has rate de-regulated most, if not all, of the major cable systems in Canada on a simple attestation of 5% market share loss. This has proven successful in allowing competition amongst various video service operators to increase in intensity. It has spurred those competing operators on to make their very best offers to consumers and has led to service innovation and differentiation. However, having done this in the cable industry, the Commission refuses to apply the same economic principles to local telephone services. Instead, the Commission in the Decision has placed inordinate emphasis on market share loss as an indicator of market power and has arbitrarily chosen 25% market share loss as one of many pre-conditions to forbearance. The Companies submit that that is because the Commission remains fixated on balancing interests, micro-managing outcomes and engaging in futile allocative exercises rather than focusing on basic economic principles. In all this, there is no mention of the interest of consumers in obtaining the benefits of free competition. There is

¹⁵ Another example of this "balancing act" is the determination of the relevant market for de-regulation where the decision sets out the correct economic definition of a relevant market, but immediately abandons this definition for a "balancing act" based on a variety of non-economic considerations.

¹⁶ Decision 2006-15, paragraph 248.

also no assessment of the harm and uncertainty that these policies and fiats create in the Canadian telecommunications industry and the Canadian economy generally.

21. Commentators have strongly condemned the lack of a principled approach to deregulation. Economist Neil Quigley stated that "...the CRTC's 25% market share threshold cannot be reconciled with any standard test for the presence or absence of market power":

"First, firms with very high market shares may be constrained from raising prices either by regulation or by competitors' ability to snatch customers if incumbents do raise prices. Even a small loss of market share, such as the 5% threshold the CRTC has applied to the cable television industry, could be sufficient to demonstrate a competitive market if there was evidence market share would fall further if prices were increased.

Second, the incumbent telcos' prices are currently regulated by the CRTC. Hence incumbents' losing 25% of their market share cannot demonstrate either the absence or presence of market power -- all it can do is show whether entrants can gain customers while traditional firms' hands are tied. It cannot establish whether incumbents could keep their customers if they raised prices, or regain lost customers without lowering them.

Moreover, the CRTC defines the market, in which the 25% share must be lost, to exclude mobile wireless services on the grounds the tariff structure is different because fixed wire service does not have usage charge for local calls and relatively few households have adopted mobile wireless service as a substitute for fixed wire service. The fact mobile wireless service is often a complement to wireline service, however, does not mean it is incapable of providing competitive discipline on incumbent wireline providers."¹⁷

Flawed view of competition

22. The CRTC's view of competition is flawed and inconsistent in a number of respects. First, the CRTC does not take into account in its analysis how easy it is for competitors to provide local telephony today, in particular through the use of VoIP technology. This is what economists and competition lawyers refer to as "low entry barriers". As the Competition Bureau stated in the local forbearance proceeding, "Absent the presence of significant entry barriers firms cannot exercise market power, irrespective of the degree of market concentration".¹⁸ When entry barriers are low and falling rapidly, regulation can have harmful effects, even though a former incumbent's share losses are modest at the outset.

¹⁷ Neil Quigley, *Hands are tied: While they are forced to share assets with competitors, traditional telephone companies cannot set prices*, National Post, 13 April 2006.

¹⁸ *Supra* footnote 10, at paragraph 55.

23. The Competition Bureau has frequently emphasized that high market share is not a sufficient condition for a finding of significant market power. The CRTC itself acknowledged this in *Review of Regulatory Framework*, Telecom Decision CRTC 1994-19. There must also be high barriers to entry.¹⁹ Even a small loss of market share, such as the 5% threshold the CRTC applies to the cable TV industry, can be sufficient to demonstrate a competitive market if barriers to entry are low. It is a truism today that barriers to entry into local telecommunications are low, if not non-existent, with all the major cable companies and several smaller ones offering local telephone service, as well as more than 100 other VoIP-based service providers operating across Canada today.²⁰ This number does not include wireless service providers, or the several other competing local service providers who offer local telephone services which are not VoIP-based. As noted earlier, in most local markets in Canada today, customers can choose between two or more local wireline service providers, as well as wireless options.

24. The CRTC is well aware of the low barriers to entry and Decision 2006-15 even refers to evidence of low entry barriers and resulting actual entry. The CRTC states that it is "...cognizant of the dynamic nature of the local exchange services market in which competition is developing rapidly". It also states that it "...has seen the beginnings of a marked increase in competition in the local exchange services market", with competitors making inroads in local business urban markets, as well as "...an accelerated roll-out in the residential local exchange services market of facilities-based local exchange services offered by competitors", with initial results indicating that "...hundreds of thousands of Canadians have chosen to switch their local residential phone service from their local ILEC to a competitive telecommunications service provider".²¹ In establishing its Forbearance Test, however, the CRTC places no weight whatsoever on evidence of low barriers to entry -- such as the number of new entrants and customers' demonstrated willingness to switch and the rapidity of competitor gains -- as criteria for de-regulation. .

25. Further, as noted earlier, the CRTC takes no account of competition from wireless services. Even if the CRTC judges so-called wireless substitution is not a significant

¹⁹ In an abuse of dominance case, *Canada (Commissioner of Competition) v. Canada Pipe Co.*, 40 C. P. R. (4th) 453, at 502, which was decided in 2005, the Tribunal explicitly writes:

"[138] As stated in Laidlaw and Nielsen, a large market share leads to a prima facie conclusion that the firm likely has market power. In order to establish market power, this conclusion must be supported by other findings on issues such as the existence of barriers to entry, the number of other competitors, excess capacity and the state of the market. Where barriers to entry are non-existent, even a very large market share will not support a finding of market power." (emphasis added).

²⁰ Peter Wilson, *VoIP in Overdrive*, Ottawa Citizen, 10 November 2005.

²¹ Decision 2006-15, paragraph 6.

phenomenon at this time (which is not the case, as noted earlier), that is no reason to fail to take account of it at all.

26. Even when faced with actual evidence of market share loss that is far in excess of its own proposed threshold, the CRTC has refused to grant forbearance.²² This creates significant uncertainty. The Commission's mechanism is not a bright line test. Consumers in certain areas of the Atlantic Provinces and elsewhere in Canada are being denied the full benefits of competition because the Commission continues to refuse to forbear even in the face of significant entry by competitors. In Halifax, where the CRTC concedes that Aliant has already lost 33% of the relevant market, and there is already rivalrous behaviour between Aliant and its competitor EastLink,²³ the Commission refuses to grant forbearance. Instead, it imposes further conditions concerning availability and quality of certain competitor services which are clearly not relevant to competitive conditions in the Halifax market, where one competitor has managed to garner a 33% share.

Flawed view of the role of regulation

27. The Panel Report recommends that the regulatory framework for Canada's telecommunications sector should rely on competition and market forces rather than on economic regulation, to the maximum extent feasible.²⁴ It strongly criticizes the CRTC's practice in recent years of "balancing" decisions in favour of the traditional telephone companies' competitors without regard to the ultimate interests of consumers:

"The Commission's goal appears to have been to promote the financial viability of competitors to the ILECs, in order to ultimately provide consumers with the benefits of increased competition. Application of the doctrine has resulted in a new, high level of regulatory intervention aimed at shaping the structure of markets, rather than allowing market forces to determine the success or failure of different service providers. The relative degree of intervention by the CRTC on behalf of new entrants has been very substantial and has led to the imposition of extensive constraints by the CRTC on the activities of the major suppliers of many telecommunications services, the ILECs."²⁵

28. In the Panel's view, it should no longer be possible or desirable for regulators to "micro-manage" the industry to achieve a planned industry structure or to pre-determine most types of

²² Decision 2006-15, paragraph 510.

²³ Bragg Communications Inc., carrying on business as EastLink.

²⁴ TPRP Report, page 3-8.

²⁵ TPRP Report, Recommendation 3-1.

economic arrangements among industry players.²⁶ It should raise a red flag when Ken Engelhart, Vice-President Regulatory with Rogers Communications Inc., in a letter to the National Post on 6 May 2006, can brazenly suggest that the cable companies may need the CRTC's protection in perpetuity. Speaking of EastLink's success, Mr Engelhart stated that this success had been earned while operating in an environment with the CRTC's protection, and that it is not known what this success would have been without such protection. Mr Engelhart concluded: "We do not wish Rogers to be test case in answering such a question". Clearly, it is time to say "enough is enough" and to let the market decide. Protection of competitors from market forces is a never-ending, self-perpetuating and futile process. Once protected from competitive forces, firms remain inefficient and less able to compete because the incentives to become efficient and competitive are constrained, thereby requiring continued regulation while failing to achieve the lowest prices and greatest variety and quality of services for customers.

29. The National Post's Mark Evans and Paul Viera summarized analysts' views on Decision 2006-15, characterizing it as "...more evidence that the regulator does not grasp the industry's competitive dynamics" and that, even after the CRTC's market share of 25% loss of lines is reached, it could take up to 2 years (in some cases more) for economic regulation to be lifted. They go on to note the view of analyst Iain Grant, managing director of SeaBoard Group that the decision demonstrates the CRTC's "penchant for insidious meddling has overcome any feeling for industry dynamics or any respect for the power of consumers to make their own decisions".²⁷

30. In the Financial Post on 5 May 2006, under the heading "free the local phone", industry analyst, Mark Evans, referred to the CRTC's process as unreasonable, bureaucratic, and unduly long and cumbersome. He stated:

"The loss of 25% market share appears unreasonable, and the process to deregulate is far too long and cumbersome. Instead of creating a fast and efficient system, the CRTC has adopted a traditional bureaucratic approach that seems to ignore the fact there have been tremendous technological changes in the past decade.

When you boil it down, the CRTC has to get out of the micro-management business, a staple of its existence. It has already left markets such as wireless

²⁶ TPRP Report, page 3-3.

²⁷ Mark Evans and Paul Viera, *CRTC revamp draws flak*, National Post, 7 April 2006.

and long-distance, so the pressure will only build to adopt the same approach with local phone service."²⁸

31. As the Competition Bureau has pointed out, "The Commission should have a very high threshold of proof to continue regulation that constrains competition since the costs of doing so are substantial".²⁹ In stark contrast, the Commission's forbearance Decision maintains a very high threshold for reducing regulation.

Unwillingness or inability to reform regulation

32. Decision 2006-15 is another example of the CRTC's apparent inability or unwillingness to reform regulation.

33. Industry expert Iain Grant is skeptical of the CRTC's ability to fix itself, given that reform threatens its traditional role. He calls on the federal government to ensure that Decision 2006-15 is "the last gasp of the heavy hand of governmental market manipulation, because "maintaining *status quo* regulation of telecom is bad for the country".³⁰

"For starters, maintaining status quo regulation of telecom is bad for the country. Canadians can now choose from a number of service providers for their phone service. Yet, the CRTC still applies rules that were created when no choice existed. Like the CRTC's recent decision, such outdated rules inevitably favour some competitors over others, a result that is clearly not something government policy should do.

And then there's the undeniable fact that more competition in telecom promises to deliver more benefits to Canadian consumers and businesses, from simple promotional offers and more innovative services all the way to an industry better able to support a truly modern and productive economy.

As with any initiative requiring significant government reform, there are forces that will resist the needed changes. For example, there are established institutions, like the CRTC, which are threatened by the prospect of the new regime."³¹

Out-of-step internationally

²⁸ Mark Evans, *Free the local phone: Competition is heating up as new players enter local phone markets. Why won't the CRTC unshackle traditional carriers?* Financial Post, 5 May 2006.

²⁹ *Telecom Public Notice CRTC 2005-2, Forbearance from regulation of local exchange services: Reply Comments of the Commissioner of Competition*, October 7 2005, paragraph 3.

³⁰ Iain Grant, *Telephone services need less regulation*, Calgary Herald, 9 April 2006.

³¹ Iain Grant, *Telephone services need less regulation*, Calgary Herald, 9 April 2006.

34. Today, there are few countries where detailed rate regulation and tariff approval requirements continue to apply, even for traditional wireline service. Prescriptive *ex ante* regulation has been largely replaced with regulation based on the principles of general competition law. This fundamental shift towards a competition-based approach, in which regulation is not applied unless markets are demonstrated to be noncompetitive, has taken place across both large markets, such as the UK, and small markets, such as Sweden; markets where the incumbent has lost significant market share, such as the UK, and markets where it has not, such as Germany; and in markets all of which have a fraction of Canada's alternative (i.e., cable) infrastructure, ranging from Germany with a tenth of Canada's cable penetration to the UK with half of Canada's.³²

35. Even countries which retain some level of *ex ante* retail regulation - such as the Netherlands - still apply competition thresholds, have reduced the multiple layers of retail regulation and are committed to an expanding scope of ILEC retail pricing flexibility. The US, which is one of the few developed economies to share Canada's approach of presumptively regulating incumbents unless services are specifically forborne, now has significantly less *ex ante* retail regulation than Canada.

36. The Panel Report cites Canada's falling behind other nations as evidence of the need to reform Canada's telecommunications policy and regulatory framework.³³

3.0 SOME SPECIFIC PROBLEMS WITH DECISION 2006-15

37. As indicated above, the CRTC's first major policy Decision released since the issue of the Panel's Report is completely inconsistent with that Report's findings and recommendations. The Decision was a unique opportunity to turn over a new leaf with a regulatory framework which defines the rules for removing economic regulation (forbearance) in a manner consistent with the Panel's recommendations and international best practices, as well as residual rules to apply post-forbearance, and the transitional rules to apply prior to forbearance. The Decision fails on all these counts and that is why the Companies in this Petition are requesting that the Governor in Council urgently intervene to redress this situation.

³² The information in this and the following paragraph is obtained from Peter Waters, Richard Pascoe and Madura Wijewardena, *Global Trends in Regulation of Retail Telecommunications Services Provided by Incumbent Local Exchange Carriers*, Appendix D-7 to Bell Canada's Submission to the TPR Panel, 15 August 2005.

³³ TPRP Report, page I-22.

38. The purpose of the local forbearance decision was, essentially, to provide a framework for the de-regulation of residential and business local exchange services -- including, to the extent needed, a lessening of marketing restrictions on the incumbents prior to de-regulation.³⁴ The CRTC's Decision completely fails in this purpose. The scheme conceived by the Commission is complicated and procedurally cumbersome which simply breeds uncertainty. It will delay de-regulation long after meaningful competition has taken hold in a particular market.

39. First, the Decision's Forbearance Test is not only inconsistent with economic principles but is flawed to the degree that it is most unlikely ever to result in the complete economic de-regulation of any market regardless of the degree of competition in that market. The test will in fact result in further and more detailed regulation – not less regulation.

40. Second, the CRTC fails to provide for a removal or lessening of marketing restrictions on the incumbents prior to de-regulation. Rather than removing or lessening the marketing restrictions, which prohibit the incumbent telephone companies from making their best competitive offers to customers, the Decision extends their operation to some undefined date in the future. This stands in stark contrast to the Panel's Report which was unambiguous in its recommendation that winback campaigns and marketing to competitors' customers should not be restricted by the regulator, as described further below.

41. Third, the Decision establishes a so-called post-forbearance regime where, in addition to approximately 50 regulatory rules that apply to all local exchange carriers and which will continue in a de-regulated environment, the former incumbents, even after de-regulation, will be subject to a further 15 or more regulatory rules which will not apply to their competitors. In particular, pricing restrictions will continue to apply to certain former incumbent services, even though the CRTC has found that there is sufficient competition to protect the interests of customers. This is not a path to de-regulation but to different and residual regulation.

42. These flaws are addressed in more detail in the balance of this section, which also provides details of the Companies' requests for relief.

3.1 Forbearance Test

³⁴ Telecom Public Notice CRTC 2005-2, *Forbearance from regulation of local exchange services*.

43. At paragraph 242 of Decision 2006-15, the CRTC prescribed five criteria, all of which must be satisfied in order for forbearance to be granted in a specific market:

"The Commission considers that an applicant ILEC can demonstrate to the Commission's satisfaction that it no longer can exercise market power in a particular relevant market when that applicant ILEC can demonstrate that it has met all of the following criteria:

- (a) The ILEC has suffered a 25 percent market share loss in the relevant market for which forbearance is sought (market share loss);
- (b) The ILEC has, for the six months prior to the application, met individual standards for each of the 14 specified competitor Q of S indicators of the rate rebate plan (RRP) for competitors, when the results are averaged across the six-month period (competitor Q of S);
- (c) The ILEC has put in place the necessary Competitor Services tariffs. In the case of an application for forbearance from regulation of residential local exchange services, the ILEC has an approved Competitor Services tariff for bundled ADSL available over loops not used for primary exchange service (dry loops) as well as in conjunction with PES, and in the case of an application for forbearance from regulation of business local exchange services, the ILEC has an approved Competitor Service tariff for bundled ADSL available both over dry loops and in conjunction with PES as well as approved competitor Ethernet access service and transport service tariffs (Competitor Services tariffs);
- (d) Where the Commission has required it, the ILEC has implemented competitor access to its OSS in accordance with Competitive local exchange carrier access to incumbent local exchange carrier operational support systems, Telecom Decision CRTC 2005-14, 16 March 2005 (Decision 2005-14) (Access to OSS); and
- (e) The ILEC has demonstrated to the Commission's satisfaction that rivalrous behaviour exists within the relevant market (rivalrous behaviour)."³⁵

i) Market share loss

44. Criterion (a) requires the ILEC to have lost at least 25% market share in a so-called Local Forbearance Region (LFR). There are a number of major flaws with the 25% share criterion. First, as discussed earlier, the market share loss of 25% is much higher than is appropriate in dynamic and rapidly evolving industries such as the telecommunications industry of today.

³⁵ Decision 2006-15, paragraph 242.

45. The second flaw is in the CRTC's choice of geographic area for the relevant market for de-regulation. The CRTC's "Local Forbearance Regions" (LFRs) are, for the most part, very large, and as discussed above, have been chosen in a manner that ignores economic principles. For example, the Ottawa-Gatineau LFR includes Ottawa-Gatineau and 27 surrounding communities stretching from Clarence Creek (Ontario) in the east to Quyon (Quebec) in the west, north to St-Pierre-de-Wakefield (Quebec) and south to Kemptville (Ontario). A second LFR covers the rest of Eastern Ontario stretching from Hawkesbury in the East to Pakenham in the West and Brockville in the South. Belleville, Trenton, Pembroke and over 40 other widely dispersed Ontario communities are grouped together in another LFR.

46. By way of another example, in Saskatchewan, the Commission has included massive rural areas with urban areas in defining the relevant geographic market. The Commission has concluded that there are only five local forbearance regions in Saskatchewan. SaskTel had proposed that the appropriate geographic market for forbearance would be at the exchange level. As a result of the Commission having chosen an unreasonably large geographic area as the relevant market, the effective estimated market share that must be lost for SaskTel to be able to compete on a level playing field will be far in excess of 25%. The effective market share loss that must be suffered in order to receive forbearance if a competitor enters only the largest urban centre in the region are as follows:

In Regina-Moose Mountain local forbearance region – 36% of consumer lines and 31% of business lines in the Regina exchange
In Saskatoon-Biggar local forbearance region – 32% of consumer lines and 30% of business lines in the Saskatoon exchange
In Swift-Current-Moose Jaw – 67% of consumer lines and 70% of business lines in the Moose Jaw exchange
In Yorkton-Melville – 119% of consumer lines (therefore unachievable) and 85% of business lines in the Yorkton exchange
In the Northern and Prince Albert local forbearance region – 140% of consumer lines and 106% of business lines in the Prince Albert exchange (therefore unachievable).

In other words, in places like Yorkton and Prince Albert where cable entry will occur, it is likely that there will never be local service economic deregulation.

ii) Wholesale criteria

47. Criteria (b), (c) and (d) relate to wholesale services used by some competitors. They require the incumbent to have satisfied 14 competitor quality of service (Q of S) standards for

each competitor in its entire traditional serving area (not simply in the LFR under consideration) for six consecutive months, to have provided access by competitors to its operations support systems (OSS) (for example, its ordering and billing systems), and to have made available to competitors a variety of CRTC-approved wholesale broadband Internet services, and potentially other competitor services in the future.

48. Criterion (b) relates to Q of S standards. In this regard, the CRTC requires that the Q of S conditions apply i) across all geographic markets in which an ILEC competes, ii) for each and every competitor against which that ILEC competes, and iii) across all of the ILEC's product markets. Thus, no local forbearance would be permitted where, by way of example only:

- i) Aliant met all of its Q of S requirements in 100% of the cases in Halifax, but not in Prince Edward Island. Local forbearance would still not be permitted in Halifax;
- ii) Aliant had not met the quality of service standards for Rogers Communications in New Brunswick. Local forbearance in Halifax would still not be permitted despite the vigorous competition by EastLink in Halifax and the fact that Rogers does not even compete in the Halifax market; and
- iii) Aliant had not met the quality of service standards for a competitor in the business market in Moncton. Local forbearance would nonetheless not be granted for residential services (found by the CRTC to be a separate product market), despite the fact that the competitor did not even compete in the residential market in Aliant territory.

49. As to criterion (c), the requirement to "put in place the necessary Competitor Services tariffs", this is completely open-ended and subject to mischievous demands from competitors because the CRTC has not defined what these services may be in the future. In any event, many of these competitor services, such as wholesale broadband Internet services specifically referred to in criterion (c) (bundled ADSL) are not required by facilities-based cable competitors who already have their own broadband networks in place.

iii) Rivalrous behaviour

50. Criterion (e) requires the ILEC to demonstrate the existence of rivalrous behaviour in the market.

51. In theory, this criterion is appropriate. In practice, however, as discussed below, the traditional telephone companies are prevented by CRTC regulation from engaging in many types of rivalrous behaviour that are the essence of competitive markets. In particular, winbacks, certain types of promotions, targeted marketing and price differentiation are all prohibited by the CRTC for incumbents.

3.2 Pre-forbearance Rules

52. Prior to forbearance, the incumbents must seek and obtain before-the-fact CRTC approval for the prices, terms and conditions under which they provide service.³⁶ Each so-called tariff filing must include a detailed cost study developed according to complex and arcane imputation and costing rules.³⁷ Over and above this requirement, the CRTC imposes various marketing restrictions and prohibitions on the incumbents, including the following:

- The CRTC does not permit incumbents to adjust prices in specific markets based on competitive conditions in those markets.³⁸
- When incumbents want to offer discounted pricing for bundles of regulated and non-regulated services, they are required by the CRTC to follow the same costing, filing and tariffing process as is used for regulated services.³⁹
- The CRTC has placed significant restrictions on the flexibility to offer promotions to customers.⁴⁰
- The CRTC prohibits the incumbents from directly contacting customers for a period of three months from the time a former local customer takes service from a competitor (the "winback rule").⁴¹

³⁶ Telecom Decision CRTC 2005-27, *Review of price floor safeguards for retail tariffed services and related issues*, sections III, VI, VII and VIII.

³⁷ The documentation of these rules runs to approximately 1,000 pages. See, for example, *Bell Canada Phase II Costing Manual*, 28 January 2005.

³⁸ Telecom Decision CRTC 2005-25, *Promotions of local wireline services*, paragraph 72, and Decision 2005-27, paragraph 302.

³⁹ Decision 2005-27, sections IV, VI, and VII.

⁴⁰ Decision 2005-25, paragraph 72.

⁴¹ For example, see CRTC Letter Decision dated 16 April 1998, *Commission Decision Regarding CISC Dispute on Competitive Winback Guidelines*, page 2, Telecom Decision CRTC 2004-4, *Call-Net Part VII Application – Promotion of local residential competition*, paragraph 117, and Decision 2006-15, paragraph 486.

53. None of the above restrictions has its foundation in economic principles, but Decision 2006-15 did not eliminate any of these rules. The only modification it made was to reduce the time period for the winback restriction for residential services from 12 months to 90 days.⁴²

54. In stark contrast the TPRP Report found that *ex post* reviews of anti-competitive conduct based on competition law principles is sufficient to protect the public interest. It dismissed the need for each of the above restrictions finding that:

- adjusting prices in specific markets based on competitive conditions in those markets, or price differentiation, is a normal business practice;⁴³
- incumbents should not be required to seek prior tariff approval for prices for bundles containing both regulated and deregulated services, provided the regulated services in the bundles are available on a stand-alone basis;⁴⁴
- winback campaigns that benefit consumers should not be restricted by the regulator;⁴⁵ and
- promotions should not require prior CRTC approval.⁴⁶

55. Not only did Decision 2006-15 fail to remove these restrictions, only in the case of winbacks is there the potential to remove the restriction under somewhat less onerous conditions. An incumbent can apply for relief from the winback rule in a particular market when it can demonstrate that :

"...it has lost 20 percent of its market share in that relevant market and that, for the three months prior to the application it has met individual standards for each of the 14 specified competitor Q of S indicators of the RRP for competitors, when the results are averaged across the three-month period".⁴⁷

56. Of course, this test suffers from the same problems as criterion (b) of the Forbearance Test, discussed above. Yet again, an unwillingness to de-regulate on the basis of the existence of competitive conditions and more regulation, not less.

4.0 RELIEF REQUESTED

⁴² Decision 2006-15, paragraph 486.

⁴³ TPRP Report, page 3-29.

⁴⁴ TPRP Report, page 3-20.

⁴⁵ TPRP Report, page 3-23.

⁴⁶ TPRP Report, page 3-27.

57. In light of the above, the Companies request that the Minister of Industry recommend to Her Excellency the Governor in Council, pursuant to subsections 12 (1) and (5) of the *Telecommunications Act*, that Decision 2006-15 be referred back to the Commission for reconsideration with a direction to render its determination within 90 days. Further, the Companies request that the Commission be directed to reconsider Decision 2006-15 including its pre-forbearance, forbearance and post-forbearance rules in light of the conclusions and recommendations contained in the Telecommunications Policy Review Panel Report.

⁴⁷ Decision 2006-15, paragraph 488.