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January 15, 2007

Mr. Leonard St. Aubin,  
Director General,  
Telecommunications Policy Branch,  
Industry Canada,  
300 Slater Street, 16th Floor,  
Ottawa, Ontario  
K1A 0C8

Dear Mr. St. Aubin:

**Re: Order Varying Telecom Decision CRTC 2006-15, *Canada Gazette*, Part I, December 16, 2006**

**I. Introduction**

1. On behalf of MCI Canada and its parent company Verizon Communications Inc., I am pleased to submit the following comments on Industry Canada's recently published Gazette Notice, entitled "Order Varying Telecom Decision CRTC 2006-15" (*Canada Gazette*, Part I, Vol. 140, No. 50, December 16, 2006, hereinafter referred to as the "Proposed Order").
2. MCI Canada has a long-standing presence in the Canadian telecommunications market. It first entered the market in 1991 as an Internet service provider (ISP) which operated under the UUNET Canada brand name. At that time, MCI Canada was the first commercial

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ISP in Canada to offer retail Internet access services to the business/enterprise customer segment. Since then, MCI Canada's operations have grown to include an entire range of Internet services, including high speed Internet access services, private line and frame relay services, web hosting, virtual private networks, and wholesale Internet access services, such as Internet dial port and Internet transport services. MCI Canada was also a leader in Canada in offering a variety of Voice over Internet Protocol ("VoIP") services through its portfolio of business communications products. MCI Canada employs almost 200 people in Canada who are spread out across the country in business offices located in Toronto, Montreal, Calgary and Vancouver. MCI Canada has been rapidly enhancing its suite of voice, MPLS and data products and related managed services as it brings the global reach of Verizon to customers in Canada.

3. MCI Canada has reviewed the Proposed Order to the Canadian Radio-television and Telecommunications Commission ("CRTC") set out in the above-referenced *Canada Gazette* notice, and is pleased to see that Canada's federal government is continuing in its efforts to streamline the regulatory process in Canada. At the same time, however, MCI Canada is concerned that the Proposed Order would be ineffective in achieving the policy objectives set out in section 7 of the *Telecommunications Act* (the "Act"), including the objective of enhancing the efficiency and competitiveness of Canadian telecommunications<sup>1</sup> and the objective of placing "greater reliance on market forces"<sup>2</sup> – two principles which were recently reaffirmed by the Governor in Council in its Policy Direction to the CRTC issued pursuant to section 8 of the Act.<sup>3</sup>
4. As discussed more fully below, the Proposed Order seeks to loosen the regulatory constraints that currently apply to the retail local telephone services offered by incumbent local exchange carriers ("ILECs"). But the Proposed Order misses a critical opportunity to increase the overall level of competition in Canada's local telephone services market because it ignores the restrictions that Canada maintains on foreign direct investment (FDI) in Canadian telecommunications carriers.

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<sup>1</sup> *Telecommunications Act* S.C. 1993, c. 38, subsection 7(c).

<sup>2</sup> *Ibid*, subsection 7(f).

<sup>3</sup> *Order Issuing a Direction to the CRTC on Implementing the Canadian Telecommunications Policy Objectives*, P.C. 2006-1534 / SOR/2006-355, December 14, 2006 [hereinafter, "Policy Direction"].

5. The Proposed Order cannot achieve its stated objective because it attempts to streamline regulation in a market which is not truly open to competitive entry and not fully exposed to the operation of market forces. Instead, Canada's telecommunications services market is characterized by artificial and unnecessary barriers to FDI which limit competition and reduce the dynamic and innovative market behaviour that are the hallmarks of a truly competitive market.

## II. Canada's Restrictions on FDI

6. Under the *Telecommunications Act* and the regulations promulgated thereunder,<sup>4</sup> telecommunications common carriers in Canada must comply with certain restrictions on their ownership which limit the amount that non-Canadians can invest in Canadian carriers. These restrictions stipulate, among other things, that: (i) at least 80 per cent of the voting equity of the carrier be held by Canadians; (ii) at least 80 per cent of the board of directors of the carrier be resident Canadians; (iii) at least 66.67 per cent of the voting equity of any parent corporation of the carrier be held by Canadians; and (iv) the carrier not be otherwise controlled in fact by non-Canadians. Thus, Canada limits the aggregate direct and indirect foreign ownership in facilities-based telecommunications carriers to a maximum of 46.6 per cent for all services, except fixed satellite and submarine cable service.
7. The practical effect of these rules on MCI Canada is that it must restrict its activities in Canada to leasing facilities from other carriers and then selling its own services on top of these facilities. In other words, MCI Canada is prevented from operating its own transmission facilities and building a true facilities-based business in Canada. As a consequence, MCI Canada must effectively operate as a reseller in the Canadian market and remain dependent on Canadian facilities-based operators for critical network components and services. These restrictions limit the ability of MCI Canada as well as other global telecommunications service providers' options for providing high-quality, end-to-end telecommunications services to customers that are not only located in Canada, but around the world. These types of restrictions also run contrary to one of the

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<sup>4</sup> See in particular the *Canadian Telecommunications Common Carrier Ownership and Control Regulations*, SOR/94-667 / P.C. 1994-1772.

government's Policy Directions to the CRTC, which appears to be supportive of "incentives for innovation and investment in and construction of competing telecommunications network facilities."<sup>5</sup>

8. To say that Canada's telecom foreign ownership restrictions have had an impact on MCI Canada's business is an understatement. These restrictions severely curtail capital investment and force MCI Canada to pay millions of dollars to other carriers simply because MCI Canada is not permitted to own and operate its own transmission facilities in Canada.
9. This is neither an efficient nor an effective way to build a business, and it is very far removed from what the market would "decide" if market forces were permitted to operate unfettered by Canada's restrictions on FDI in the Canadian telecommunications sector. Until these restrictions are removed, there is no amount of tinkering with "local forbearance" rules that will bring about true competition.
10. It should be noted in this regard that Canada's telecommunications foreign ownership rules have been the subject of extensive study and analysis. In April 2003, the Parliamentary Standing Committee on Industry, Science and Technology (the "Standing Committee") recommended the *complete removal* of the Canadian ownership requirements.<sup>6</sup> According to the Standing Committee, Canada's foreign ownership restrictions deter foreign direct investment and contribute to and, consequently, act as a barrier to entry in Canada's telecommunications markets. The Committee also concluded that these rules contribute to financial instability in the sector, and are "likely stifling Canada's productivity and economic growth performances."<sup>7</sup>
11. By contrast, the Standing Committee observed that an open entry approach would make Canada more attractive to capital, would allow capital markets to determine the most efficient allocation of resources, and potentially encourage the private sector to bring new

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<sup>5</sup> *Supra*, note 3, section 1(c)(ii).

<sup>6</sup> Standing Committee on Industry, Science and Technology, *Opening Canadian Communications to the World*, (April 2003), recommendation 2 at page 37, available at: <http://cmte.parl.gc.ca/Content/HOC/committee/372/inst/reports/rp1032302/instrp03/instrp03-e.pdf> (the "Standing Committee Report").

<sup>7</sup> *Ibid.* at page 55.

services to remote and rural communities as well as attract jobs and research and development work in the telecommunications sector.<sup>8</sup> The Standing Committee concluded that “removing FDI restrictions would stimulate competition and increase innovation in the telecommunications service industry.”<sup>9</sup> As such, the Standing Committee advocated that “reforms to Canada’s foreign ownership regime must be the first step in a multi-step reform of the telecommunications and broadcasting sectors in Canada.”<sup>10</sup>

12. Canada’s foreign ownership rules were revisited, once again, in the 2006 Report of the Telecommunication Policy Review Panel (“TPRP”). Here again, the TPRP recommended the liberalization of current foreign ownership rules. The TPRP concluded that the “removal of the telecommunications restrictions would increase the competitiveness of the telecommunications industry in key market segments, and would improve the productivity of Canadian telecommunications markets”.<sup>11</sup>

### **III. The Benefits of FDI and the Experience in Other Countries**

13. FDI has been one of the main drivers of the long upswing in global economic performance and the positive world economic outlook. Liberalization of FDI environments has produced many benefits: FDI fuels innovation and higher-quality jobs both directly and indirectly; provides an increased pool of capital for investments, generating growth and income, often by an efficient, productive enterprise; generates increased revenues for government; increases the acquisition of technology, knowledge and managerial skills; and generates additional tax revenues. Cooperation with foreign enterprises can also enable companies to respond to the challenge of global competition in product development. Foreign companies can provide new products and services that do not exist in the domestic market and thus create a new market, enhancing competition and increasing benefits to consumers. Overall, consumers see lower prices and better services from increased foreign investment in their market.

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<sup>8</sup> *Ibid* at pages 34-5 and 37.

<sup>9</sup> *Ibid* at page 42.

<sup>10</sup> *Ibid* at page 56, emphasis added.

<sup>11</sup> Telecommunications Policy Review Panel Report (March 2006) at page 11-25, available at: <http://www.telecomreview.ca/epic/internet/intprp-gecrt.nsf/en/Home> (“TPRP Report”).

14. Greater access to foreign investment will enhance competition in the Canadian telecommunications markets. It is often difficult for new entrants and smaller established companies to obtain financing, and this challenge is exacerbated where restrictions on foreign direct investment effectively serve to shut out a major potential source of financing for telecom competitors in Canada.
15. Canada's ability to drive technology choice is limited as long as the market is constrained from achieving its potential, both in terms of size and full participation by companies from countries where technology advances are pre-eminent. Indeed, technology choices are often driven by close integration and collaboration with its major trading partners in the United States and the European Union.
16. Limiting FDI is not an effective way to balance policy objectives or to address security and sovereignty concerns. Over-protectiveness hinders Canada's access to a larger capital pool for investment in new and improved telecommunications infrastructure. Indeed, as noted above, Canada's restrictions on FDI run counter to various governmental policies relating to the development of broadband infrastructure and other innovative services. Foreign investment historically has been a large part of the Canadian telecom industry and has played a key role in the development of its infrastructure.<sup>12</sup> Major investments are required for next generation services, capital is increasingly mobile across markets, and it will be imperative for the Canadian market to be as attractive as possible for the capital needed to expand the sector.
17. Taking into account Canada's FDI limitations and other aspects of the environment for foreign investment, a December 2006 OECD Report ranks Canada among the OECD countries as having the one of the most restrictive environments for foreign investment in telecommunications. In fact, only Korea and Mexico impose similarly restrictive FDI limitations in the telecommunications sector.<sup>13</sup> Thus, the Telecom Policy Review Panel appropriately acknowledged that Canada retains one of the most restrictive and inflexible

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<sup>12</sup> Both Bell Canada and BC Tel built their local telephone networks at a time when non-Canadians held sizeable investments and, indeed, controlling interests in these companies.

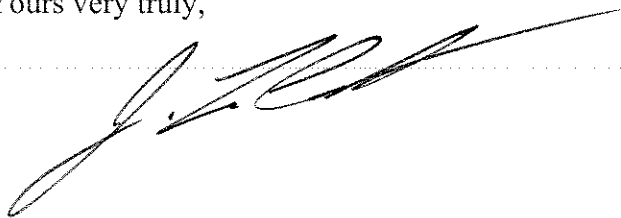
<sup>13</sup> OECD, FDI Regulatory Restrictiveness Index: Revision and Extension to More Economies, December 2006, Working Papers on International Investment, Number 2006/4, p. 6. Other countries in this category include Iceland, Mexico, Australia, and Austria.

set of rules limiting foreign investment in the telecom sector among *all* OECD member countries and pointed out the drawbacks of this policy.<sup>14</sup>

#### IV. Conclusions

18. Canada's restrictions on FDI prevent it from placing greater reliance on market forces in the telecommunications services sector – one of the single most important policy objectives identified by the government of Canada in its recent Policy Direction to the CRTC.<sup>15</sup> By restricting the ability of non-Canadians to build businesses in Canada and invest in Canadian telecommunications infrastructure, these rules limit the benefits of efficiency and innovation that Canadians would reap from a market that is truly competitive.
19. Canadians deserve a truly competitive telecommunications market. Both the Telecommunications Policy Review Panel and the House of Commons Standing Committee on Industry, Science and Technology have recommended that Canada's restrictions on FDI in the telecommunications sector be removed because they discourage competition and investment in the sector. The competitive objectives of the Proposed Order will never be realized if Canada does not also take steps to remove its restrictions on FDI.

Yours very truly,

A handwritten signature in black ink, appearing to be 'J. J. ...', written over a horizontal dotted line.

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<sup>14</sup> TPRP Report, *supra*, note 11, at 11-24.

<sup>15</sup> *Ibid.* Section 1(a)(i) of the Policy Direction instructs the CRTC to “rely on market forces to the maximum extent feasible as the means of achieving the telecommunications policy objectives.”