

**IN THE MATTER OF CANADA GAZETTE,  
Part 1, December 16, 2006**

**ORDER VARYING TELECOM DECISION CRTC 2006-15,  
*FORBEARANCE FROM THE REGULATION OF RETAIL  
LOCAL EXCHANGE SERVICES***

**REPRESENTATIONS OF  
COGECO CABLE INC., BRAGG COMMUNICATIONS INC. AND  
ROGERS COMMUNICATIONS INC.**

**Filed: January 15, 2007**

## COMMENTS ON PROPOSED FORBEARANCE ORDER

### INTRODUCTION

1. These comments are submitted jointly by Cogeco Cable Inc., Bragg Communications Inc. carrying on business as EastLink and Rogers Communications Inc. in respect of the proposed Order of the Governor in Council to vary Telecom Decision CRTC 2006-15, *Forbearance from the regulation of retail local exchange services* (the "Decision"), which was published in the Canada Gazette on December 16, 2006 (the "Proposed Order").
2. As discussed in the body of this submission, the Proposed Order is the most interventionist order ever contemplated in the Canadian telecommunications sector. It steps over the dividing line between policy-making and regulatory implementation and it severely blurs the distinction between Government and regulatory functions. It thereby threatens the CRTC's status as an independent regulatory agency and is very likely to be viewed in an adverse light by the OECD and Canada's major trading partners.
3. Of particular concern is the proposal to eliminate all winback restrictions in advance of any forbearance order. This marketing safeguard was established in direct response to the ILECs' anti-competitive marketing strategies in a market in which they are dominant. To remove these restrictions in advance of a determination that the ILECs have lost their dominance, invites a return to anti-competitive conduct and the possible thwarting of competitive entry. The degree of competition that is present in local markets varies significantly across Canada. To remove this safeguard without regard to this fact is extremely prejudicial to new entrants and could severely retard the expansion of competition in many areas. Removal of the marketing safeguards should not be done until six months after forbearance is granted in a given local market. If none of the other changes proposed below are made to the Proposed Order, this one change is essential. It

should be noted in this regard that winback rules still apply against cable companies in the broadcasting distribution market fully six years after these markets were rate deregulated. An asymmetry that is to cable companies' disadvantage would still exist but the extension of the winback rules in the local telephone market for 6 months after forbearance would lessen the asymmetry.

4. The Proposed Order essentially changes every major determination made by the Commission in its Decision, and rules on other issues in advance of the CRTC even releasing its decision in follow-up proceedings involving the substitutability of wireline and wireless services and the appropriate time to remove restrictions on winbacks. The Proposed Order does not even pay the CRTC or industry participants in those proceedings the courtesy of waiting for the Commission to issue a determination in those proceedings which are now completed.

5. The Government's proposal to rewrite the Commission's determinations on highly technical issues such as the relevant geographic and product markets, the substitutability of services and appropriate interconnection standards, strays into an area of detail that has little to do with policy and much to do with expertise of the regulator.

6. Another key concern respects the lack of an effective adjudicator of competition disputes in a post-forbearance environment. The Telecommunications Policy Review Panel (TPRP) was clear that the *Competition Act* does not provide a suitable framework for the telecommunications sector. It devoted a whole chapter of its report to this issue and recommended reforms to correct this situation. It clearly tied its recommendations for less economic regulation to the need to have adequate remedies in the new environment. The Proposed Order does not even mention this problem or the TPRP's recommendations in this regard.

7. This problem cannot be addressed by simply conferring a civil fining power on the Competition Tribunal. As the TPRP pointed out, the two-stage process embodied in the *Competition Act*, the huge delays in obtaining relief, the lack of expertise of the Bureau and the Tribunal in the telecommunications sector and the inadequacies of the existing *Competition Act* provisions all make this regime an inappropriate one for ongoing dispute resolution in the telecommunications sector. The recent Draft Bulletin issued by the Competition Bureau on abuse of dominance in the telecommunications sector simply serves to underscore these problems.

8. What is needed to address these issues is legislative reform – not piecemeal *ad hoc* interventions by the Governor in Council. The Proposed Order creates a potentially dangerous situation in which regulation and regulatory safeguards are removed prematurely without an effective body to respond to the inevitable fall-out.

9. For these reasons, we respectfully request that the Proposed Order not be issued and that the Government consider more substantive legislative-based reforms to implement both parts of the TPRP's recommendations – less economic regulation and the creation of an effective adjudicator of competition disputes. Unless these issues are addressed in tandem, the ILECs will be able to exploit their market power to the detriment of consumers and the Government's longer term policy objectives.

10. Alternatively, the Proposed Order should be referred to a Parliamentary Committee for further study.

11. In any event, regardless of what tests are used to establish the presence or absence of market power, the Governor in Council ought not to remove the winback restrictions until six months after a determination that the ILEC has in

fact lost its market power and forbearance is therefore justified in the relevant local market.

**THE PROPOSED ORDER VARIES ALL OF THE COMMISSION'S KEY DETERMINATIONS AND ESSENTIALLY REWRITES THE DECISION**

12. In the public proceeding which led to the Decision, the Commission identified a number of key issues for determination. Principal among these issues were identification of the relevant geographic and product markets for forbearance of local exchange services, the appropriate criteria to identify loss of significant market power in a relevant market, and transitional measures that might be taken to relax regulation in local markets where forbearance was not yet justified.

13. Following a public process that lasted for approximately five months and involved extensive expert evidence and the participation of all major industry participants and public interest groups in the Canadian telecommunications market including the Commissioner of Competition, and following a further six months of deliberations, the Commission unanimously rendered its determinations on these issues. It put in place a framework for forbearance of local exchange markets that is consistent with competition law principles and with international practice among Canada's major trading partners.

14. The Proposed Order results from a number of petitions to the Governor in Council filed by parties who do not like the Commission's determinations. Numerous other parties filed comments with the Governor in Council supporting the Commission's determinations. It is important for the Government of Canada to understand the extent to which the Proposed Order would alter the Commission's Decision. The Proposed Order would alter the Commission's determinations in all material respects, thereby making it the most interventionist

Order ever issued by the Governor in Council in respect of a CRTC telecommunications decision.

15. Issuance of the Proposed Order in its current form would totally undermine the public proceedings before the Commission and bring into question the credibility of the CRTC as an independent administrative agency in Canada. Parties who spent hundreds of thousands of dollars participating in the CRTC's proceedings will be left wondering why they bothered to do so. Trade monitoring institutions like the OECD are likely to be critical of this extensive Government involvement in supposedly transparent regulatory proceedings in Canada.

#### Geographic Market

16. The CRTC devoted some 86 paragraphs of its Decision and 24 pages of an appendix to identify the appropriate geographic market for purposes of forbearance of local exchange markets. This was a central issue in the proceeding. In its Decision, the Commission carefully canvassed all of the evidence and all of the options before it and settled on use of Statistics Canada's Census Metropolitan Areas (CMA), supplemented by Statistics Canada's Economic Regions (ER) in regions outside the larger metropolitan area. The Commission rejected both the local exchange and the local interconnection region (LIR) as appropriate geographic markets for the extensive reasons provided in its Decision.

17. The Proposed Order rewrites this determination in paragraph 1, allowing ILECs to choose either a local exchange or an LIR, as the relevant geographic market, at its option.

18. No party to the proceeding, including the Commissioner of Competition, had suggested giving the ILECs this option. Indeed, no competition authority in the world would allow an ILEC to choose a relevant market from a menu of

options. This is equivalent to letting the foxes into the chicken coupe.

### Evidence of Loss of Significant Market Power

19. In its decision, the Commission settled on a 25% market share loss as evidence of loss of significant market power in a relevant geographic market. This was generous to the ILECs since retention of a 75% market share usually gives rise to a presumption of market power in competition law. This is the case in Canada where the *Merger Enforcement Guidelines* and the *Abuse of Dominance Guidelines* use a 65% market loss threshold as an indication that market power may exist, and the Canadian Competition Tribunal has held that an 80% market share gives rise to a presumption of dominance.

20. The CRTC's determination is also consistent with market share levels that have justified forbearance from regulation in other jurisdictions including the European Community and the United States.<sup>1</sup>

21. Paragraph 2 of the Proposed Order totally eliminates the market share loss threshold established by the CRTC in favour of a competitive presence test. This new test simply requires the presence of two other facilities-based carriers in a local exchange or an LIR, and requires no evidence that they have been successful in capturing a single customer.

22. Contrary to what is stated in the Proposed Order, this is not consistent with the test advanced by the Commissioner of Competition in the local forbearance proceedings before the CRTC. That test required evidence that

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<sup>1</sup> See for example, the reports entitled *International Approaches to Determining Significant Market Power in Telecommunications Markets and the Role of Market Share* by Giganomics Consulting Inc. filed October 26, 2006 on behalf of the Competitors in the proceeding initiated by Telecom Public Notice 2006-12 (Proceeding to reassess certain aspects of the local forbearance framework established in Decision 2006-15) and *A Comparison of VoIP Regulations between Canada and Other Countries* by Lemay-Yates Associates Inc. filed June 5, 2006 on behalf of the Competitors in the proceeding initiated by Telecom Public Notice 2006-6 (Reconsideration of Regulatory framework for voice communication services using Internet Protocol) .

competitors had (i) a lower cost base than the ILECs (ii) that they were attracting customers in significant numbers and (iii) that they were retaining them. Absent these criteria, there can be no confidence that the ILEC has lost its market power.

### Product Market

23. In its Decision, the CRTC determined that the evidence filed had failed to convince it that a significant number of Canadians were treating wireless service as a substitute for wireline local exchange service. The CRTC therefore did not include cellular service in the relevant product market.

24. On June 16, 2006, the CRTC reopened this issue and asked interested parties to comment on more recent Statistics Canada data that showed an increase in substitutability in some larger centres.<sup>2</sup> Many parties agreed that those wireless customers who actually discontinue their wireline service in favour of wireless service should be included in the relevant product market. A decision on this issue is pending.

25. The Proposed Order negates this proceeding by resolving the issue before the CRTC even issues its decision. The Proposed Order has done so by including the presence of a wireless carrier in a local exchange or LIR as evidence of competitive substitutes for wireline service.

26. Again, it should be noted that the Commission of Competition did not recommend this outcome in the local forbearance proceeding. The Commissioner said that there was not enough evidence on the record to reach a conclusion on the issue. Substitution depends on price, service quality and evidence of customers switching from wireline to wireless service. Nonetheless, the Proposed Order has treated the issue as settled – even before the CRTC

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<sup>2</sup> Telecom Public Notice CRTC 2006-9.

rules on the additional evidence before it in the follow-up proceeding.

### Interconnection Services

27. In its Decision the CRTC tied satisfaction of certain quality of service indicators for interconnection services offered to competing local telephone carriers to a decision to grant forbearance. These are services on which the ILECs' competitors depend for the provision of high quality service to their own customers.

28. In this case, the Proposed Order has lowered the standards that have to be achieved. The test has gone from one that ensures high quality service to one that demonstrates that the ILEC "did not provide consistently substandard services" to its competitors.

29. This is a significant derogation from the existing standard, and one that jeopardizes the ability of some competitors to compete effectively with the ILECs. Gone is the ILECs' incentive to provide high quality interconnection services in order to obtain forbearance.

### Competitive Safeguards

30. In its Decision, the CRTC decided to retain certain competitive safeguards that were designed to protect competitors from abuse of the ILECs' dominance until such time as the ILECs' significant market power has been eroded. These regulatory safeguards included local winback restrictions and rules respecting promotions.

31. As discussed in greater detail below, these rules were designed to prevent the ILECs from targeting their marketing activities only at those customers they lost to competitors by offering them a special deal to come back to the ILEC as

soon as the customer tried a competitor's service. The ILECs were in a position to engage in this type of activity on the day that the customer decided to switch suppliers since they were starting out with 100% of the customer base and knew exactly when a customer was switching carriers. By targeting price reductions to only those who were leaving, and by maintaining higher prices elsewhere, the ILECs could counter competition whenever it emerged and make up its losses in more inert markets.

32. In its Decision, the Commission decided to reduce the no winback period from 12 to 3 months and to eliminate the restrictions altogether where the ILECs have lost 20% of their customer base in a relevant local market and have satisfied the quality of service guidelines. This would occur prior to forbearance – but only after there was evidence of substantial competitive activity in a given local market.

33. On September 1, 2006, the Commission reopened this issue in a public proceeding in which it asked whether the rules should be modified.<sup>3</sup> This public process is now concluded and a decision is pending.

34. If implemented, the Proposed Order would eliminate these marketing restrictions immediately, regardless of whether a local market is being forborne from regulation and regardless whether the market in question is experiencing any competition at all. Moreover, the Proposed Order would do so before the CRTC has even had a chance to release its decision in the recently concluded proceeding on this issue.

35. If implemented, the Proposed Order could seriously impede the ability of competitors to retain customers during the start-up phase of their market entry when the ILECs still retain significant market power. It could dissuade competitors from entering new local markets and could freeze their ability to

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<sup>3</sup> Telecom Public Notice CRTC 2006-12.

expand their market share in markets where they already have a presence.

36. In our view, this is the single most important issue to address in assessing the changes that should be made to the Proposed Order. For this reason, we have addressed this issue in greater detail below.

### **WHY WINBACK RESTRICTIONS ARE NECESSARY**

37. The reason why the CRTC established restrictions on the ILECs' customer winback activities was to counteract the ILECs' abuse of their dominant position. This was not a response to a theoretical problem. The restrictions were only imposed after the ILECs started engaging in a practice of calling a customer as soon as a decision to switch suppliers was made and targeting that customer with a special offer that would only be available to that customer if it reversed its decision to change suppliers.

38. In some instances this winback activity was initiated as soon as the competitor initiated the process of ordering facilities from the ILEC or otherwise processing the service order, which necessarily involves interaction with the ILEC. Absent regulatory safeguards, the ILEC could use this information to reverse the customer's decision to change suppliers. This information was derived by the ILEC solely because of its position as the gatekeeper of the public switched telephone network – a bottleneck facility with which all other local competitors need to connect and interact.

39. The CRTC found that this targeted response to the loss of a customer was unfairly thwarting the development of a competitive market.

40. Detractors of these safeguards argue that the ILECs' response is a normal competitive response and that it hurts consumers. In fact this is not the case. In a normal competitive market new entrants do not have to advise their principal

competitors when they are about to acquire one of their customers and they do not have to arrange with their principal competitor for facilities and services to effect this transition. It is the ILECs' position as the bottleneck derived from its dominant position in the market that renders this type of winback activity anti-competitive.

41. There are a number of factors which make the local telephone market different from many other markets and which render the ILECs' winback activities anti-competitive.

42. First, virtually all residential households require telephone service so, generally speaking, there is no buy – or no buy decision to be made.

43. Secondly, the ILECs started out with 100% of the market and have almost perfect information about the customers' telephone needs and usage patterns. This gives the ILECs unique knowledge of each customer's decision to change suppliers, as well as customer-specific information concerning the type of special deal that might be attractive to them.

44. Third, unlike many other products and services, local telephone service remains in place until a customer decides to change suppliers. It is not a consumable product that periodically needs to be replaced. There is not generally the same process of competitive shopping at venues where multiple competitive products are available. In this environment, competitors must market directly to consumers to entice them away from the ILEC, and ILECs need only respond at an individual customer level, when they lose, or are about to lose a customer.

45. The ILECs' incumbency, and their knowledge of the precise moment a customer leaves, gives them an opportunity to target their marketing to an individual customer, and their special knowledge of that customer's telephone

usage, gives them an opportunity to target a special offer to that individual customer.

46. In contrast, competitors cannot target special offers at ILEC customers on an individual basis. They do not have the same incumbent knowledge of the customers' usage and they must market their services more broadly to the ILECs' customers.

47. The ILECs often characterize their winback activity as normal competitive behaviour which is the essence of competitive markets. We do not disagree that all companies try to increase their market share by winning back customers. The key distinguishing factor here is that the local telephone market is not an ordinary competitive market. The special incumbent position of the ILECs places them in a position to exploit their dominance in a way that enables them to compete unfairly to preserve their dominance. ILECs can "winback" customers before customers have even tried the competitor's service.

48. In its final argument in the Local Forbearance Proceeding, the Competition Bureau indicated that it had no position on the Commission retaining rules for winbacks as they might be necessary to promote competition until markets are forborne:

The Bureau generally favours a minimalist approach to regulation that tailors the regulatory response to the particular problem and weighs the benefits of regulating against the benefits or detriments of not doing so. Competition is rarely perfect and the Bureau submits that the Commission must guard against trying to micro-manage it. **The Bureau has no position on the Commission retaining rules for winbacks and promotions or the imputation test as they may be necessary to promote competition until markets are forborne.**

(Competition Bureau Reply Argument, para. 133)

49. Later, in its reply argument, the Competition Bureau indicated that, in its view, the marketing restrictions could be removed if the tests for forbearance that

it proposed were adopted by the Commission.

50. Unfortunately, the Proposed Order does not tie removal of the winback restrictions to a decision to forbear from regulation of a local market in the manner suggested by the Competition Bureau. Rather, the Proposed Order would remove the restriction immediately regardless of the state of competition that exists in the local market in question. It will be removed in markets where there is no competition on the same date as it is removed in markets where there is significant competition. This totally ignores the local market conditions. Even if no competitor has yet entered the market, the restrictions on winbacks will disappear. This means that the ILECs will be able to respond to new entry by targeting their marketing to each customer that tries to switch. In this environment, unrestricted winback activity may discourage entry where it has yet to occur, and prevent further inroads being made in markets where entry has occurred – but the ILECs have yet to lose their dominance.

51. A new entrant will often incur costs of \$300 to attract a new customer. If the incumbent wins back 2 out of 3 customers through special targeted offers, the new entrant incurs a \$900 cost per net addition. At this cost, acquiring the customer never pays back and the new entrant eventually stops marketing. The result is that winback marketing can prevent competition from starting in a new market and can freeze competition in its tracks in a market where competition has started.

52. In their petitions, the ILECs characterized the winback restrictions as anti-competitive in the sense that the rules restrict their ability to respond to competition in a “normal” manner. In fact, the rules do no such thing. The ILECs can respond to competition by lowering the price they offer consumers. What they can’t do is target their offer to only those individual customers who have decided to switch carriers. For those few customers, they have to wait for three

months before making a targeted offer.

53. Rather than make a general offer to consumers, as is the usual manner of doing business in a competitive market, the ILECs want to restrict their offer to a small subset of consumers who have made a decision to switch suppliers. Removal of the winback rules enables the ILECs to follow this practice to the detriment of the majority of consumers.

54. The ILECs are being disingenuous and hypocritical when they attack the winback restrictions. The ILECs have in fact supported the imposition of winback restrictions on the cable television companies in the broadcasting distribution market. The ILECs have characterized these rules as necessary to help them enter the multiple unit dwelling market with their own BDU services. They have supported the imposition of these restrictions on the cable industry and have credited the rules with assisting in the development of a competitive BDU market in Canada.

55. Bell Canada's true position on winback restrictions is found in CRTC submissions by Bell ExpressVu supporting their imposition. The following excerpt from the January 28, 2005 issue of Canadian Communications Reports quotes Paul Armstrong, Director of Regulatory Matters at Bell ExpressVu, in his defence of the winback restrictions:

Bell ExpressVu says that the CRTC's proposed changes to winback rules will help it crack the multiple unit dwelling (MUD) market. The proposed changes clarify that not only are cablecos prohibited from contacting for 90 days condo boards, but also from wooing back with special deals individual MUD residents.

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Armstrong tells Canadian Communications Reports that the change is one protective measure that could help Bell ExpressVu get a better hold on the MUD market. "You invest a lot of money in a building to put a facility in there, to market to the building, and so on. When you make that

investment, you have to count on a certain penetration just to break even," he notes. "It really doesn't matter if it's a TV service or anything else. When you're selling to a building, you have to count on a certain penetration level just to break even. If you open a donut store or something in the lobby, you have to assume a certain volume of sales to make your presence worthwhile. And if the donut store next door came along and suddenly said, 'Don't buy donuts from him. I'll give them to you for half price,' you have no opportunity then to make a business."

He continues, "So are you going to go into another building and lose money there too? The cable company can chase you all over town until you run out of money. (The revised winback rule) is another measure that the commission has put in place to give competition an opportunity to get established...It's only a 90-day opportunity to prove to customers that you have the ability to provide the service they want."

Armstrong says that Bell ExpressVu is faring better in the MUD market in Toronto, since the CRTC shot down Rogers' practice of putting buy-back clauses on inside wiring in their agreements with MUD owners (CCR, Nov. 22/04). The modified winback rule should provide another boost in that direction, he points out.

56. Bell ExpressVu was not alone among ILEC affiliates in supporting the CRTC's winback restrictions in the cable television industry. MTS and Telus also supported it, as recorded in the same Canadian Communications Report:

In a joint submission dated January 13, MTS and TELUS support the CRTC's proposal. "MTS TV and TELUS support the commission's proposed modification to the winback rules and submit that the broadcasting winback rules will only be effective in relation to the termination of a bulk billing agreement if the rules ensure that the incumbent BDU (broadcast distribution undertaking) cannot contact directly, during the established period, any of the residents of the MUD that were previously subject to the bulk billing agreement," states their submission. "...That is, the proposed modification would recognize that it is the end-user MUD resident that makes the final selection in respect of his or her basic cable service and that it is the end-user that is ultimately the target of any winback activities." Both MTS and TELUS are new entrants to the TV distribution business.

57. The winback restrictions referred to in this article are still in place in the cable television industry, ten years after the ubiquitous entry of Bell ExpressVu

and Star Choice into the broadcasting distribution market and respectively six and five years after the first Rogers and Cogeco cable systems were entirely rate deregulated. The restrictions apply only to the incumbent cable television companies – not the ILECs' affiliates and, like the CRTC restrictions in the local telephone market, apply for a three month period. Moreover, as noted above they continue to apply even after the CRTC has forborne from rate regulation in this market.

58. In our respectful submission the Governor in Council ought not to rely on the ILECs' arguments on this issue, as presented in their petitions. The ILECs' position is clearly self-serving. They support the winback rules in a market where they are new entrants and they oppose the rules in a market where they are the incumbents.

59. This is an issue of critical concern to consumers and competitors. Removal of the winback restrictions cannot be allowed to occur at least until such time as a given local market is forborne from rate regulation. The restrictions have been put in place to prevent abuse of dominance. Until such time as that dominance is lost, the abuses witnessed in the period prior to establishment of these safeguards may be expected to reoccur. This will prevent new entry in markets not yet served and stall expansion in markets where entry has occurred – but where the ILECs are still dominant. The restrictions cannot be removed in advance of loss of the ILECs dominance without serious ramifications for the development of competitive markets.

60. Therefore, the Competitors submit that, at a minimum, the winback rules must continue to apply for six months after CRTC approval of a forbearance application for a market. This is a minimal safeguard to address the serious concerns explained in the preceding paragraphs. In addition, it is a modest safeguard in comparison to the situation that exists in the broadcasting distribution market where cable companies remain subject to winback rules in the

MDU market over six years after those markets have been deemed sufficiently competitive to permit the cable companies to be rate deregulated.

### **UNDERMINING THE CRTC'S INDEPENDENCE**

61. The power in section 12 of the *Telecommunications Act* to vary a CRTC decision is an extraordinary one that ought not to be undertaken lightly.

62. As pointed out by the Telecommunications Policy Review Panel (TPRP) in its March, 2006 Report to the Government of Canada, policy-making is the primary preserve of the Government and regulation is the primary preserve of the regulator – in this case the CRTC. “It is the proper role of government to establish policies and that of regulators to implement the policies and to develop more detailed rules necessary to provide certainty as to how the policies will be applied.”<sup>4</sup>

63. In its report, the TPRP noted that the Government of Canada is unique in its ability to both issue policy directives and alter CRTC decisions. It also noted that the OECD has been critical of this blurring of the line between government policy-making and independent regulation:

As noted above, policy is by nature dynamic. Governments have an ongoing role in refining existing policies and developing new policies to anticipate or respond to changing conditions. This policy-making role is most commonly exercised by changing laws governing the telecommunications sector. In addition, the telecommunications legislation in a few OECD countries provides the government with a power to direct — or to communicate with — the regulator on policy matters.<sup>16</sup> In some countries, the legislation permits the government to review decisions taken by the regulator.<sup>17</sup>

Canada appears to be the only OECD country whose telecommunications legislation empowers government to do both; that is, to provide advance directions on policy matters (the "policy direction power")<sup>18</sup> and also to review and vary, rescind or refer a decision back to the regulator on policy

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<sup>4</sup> TPRP Report, p. 9-15.

grounds (the "Cabinet review power").<sup>19</sup> The legislative framework within which the CRTC operates therefore makes it appear to be one of the least independent telecommunications regulatory agencies in any OECD country. The government power to intervene in the regulatory process both before and after decisions have been taken has the potential to be detrimental to the integrity of the regulatory process. The Panel notes that this double-barrelled process has also led to negative comments in OECD reports<sup>20</sup> and other international fora.<sup>5</sup>

64. These observations led to the Panel to recommend in Recommendation 9-5 that the Cabinet powers to review individual CRTC decisions be repealed.

65. If issued in its current form, the Proposed Order will be the most interventionalist Order in Council ever issued in respect of a CRTC decision on a telecommunications matter. It goes far beyond policy-making since it involves rewriting all of key determinations made by the CRTC in its decision – in respect of relevant geographic markets, product substitution, quality of service standards, market share loss thresholds and revocation of marketing restrictions in advance of loss of market power. These are all technical issues in respect of which the CRTC is the expert body. For the Governor in Council to get involved in this level of detail, and to completely rewrite the CRTC's conclusions, seriously undermines the CRTC's independence and credibility.

66. The Government's policy is clear. It wants a more competitive local telecom market. It has already issued a policy direction to this effect which is very clear on the subject and its policy goal is clearly shared by the CRTC.

67. However, the CRTC is also bound by the statutory tests for forbearance in section 34 of the *Act*. It is trying to forbear in accordance with these legislative provisions – but the Proposed Order would alter every material determination it has made in respect of this implementation. This lends support to the OECD's criticism of our legislative regime and it undermines the role of the CRTC as an

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<sup>5</sup> TPRP Report, p. 9-15 to 9-16, (footnotes omitted), emphasis added.

independent regulator. It is also inconsistent with the recommendations of the TPRP to limit or eliminate the Government's "back-end" involvement in policy implementation.

68. Both the Government of Canada and the CRTC want a more competitive local exchange market. By altering the CRTC's carefully thought out tests for forbearance, the Proposed Order is risking premature forbearance in advance of loss of significant market power. This would be inconsistent with the requirements of section 34 of the *Telecommunications Act* and could seriously jeopardize the achievement of the legislative policy objectives.

### **FAILURE TO ADDRESS THE TPRP'S RECOMMENDATIONS FOR LEGISLATIVE REFORM IN THE POST-FORBEARANCE ENVIRONMENT**

69. The TPRP was very clear in its Report that less economic regulation must be accompanied by the creation of a new agency, with new powers, capable of addressing competitive disputes in the post-forbearance environment. For this reason it examined Canada's existing legislation and institutions to assess their suitability to effectively address this post-forbearance environment:

As the regulatory framework transitions from an historic approach that seeks to protect consumers from monopoly pricing to one that relies on competitive market forces to discipline pricing, the focus of economic regulation shifts toward ensuring that competition is not thwarted or significantly diminished as a result of anti-competitive conduct by those who might possess significant market power (SMP). In this environment, there is greater reliance on competition law principles, rather than on traditional public utility regulation, to assess whether barriers to entry exist, whether SMP exists and whether there has been abuse of such SMP that has resulted — or is likely to result — in a significant lessening or prevention of competition in the market.

As this shift in regulatory focus occurs, it is important to consider the most appropriate institutional framework to define markets, assess market power, determine whether there has been an abuse of such SMP when it is found to exist, and determine whether such conduct has resulted in a significant lessening or prevention of competition. It is equally important to

ensure that the institution granted this authority has an in-depth understanding of the telecommunications sector as well as the requisite powers and procedures to make determinations in a timely manner, to impose effective remedies when justified and to monitor compliance with its orders. The question that arises is whether the existing sector-specific regulator — the Canadian Radio-television and Telecommunications Commission (CRTC) — the competition law authorities — the Commissioner of Competition, the Competition Tribunal and the courts — or some new institution would be the most appropriate and effective body to assume this role.<sup>6</sup>

70. In its report, the TPRP canvassed the experience of Canada's major trading partners and concluded that none of them had abandoned economic regulation of the telecommunications sector without at least adapting their competition law statutes to embody sector-specific provisions.

71. In the Backgrounder to the Proposed Order, a number of references are made to the TPRP Report and its recommendations concerning greater reliance on competition and less reliance on economic regulation as the best means to achieve the objectives of Canadian telecommunications policy. However, no mention is made in the Backgrounder of the very significant reforms proposed by the TPRP as a corollary to less economic regulation. These reforms involve the creation of a new hybrid agency comprised of both CRTC and Competition Bureau personnel, with wide-ranging new powers to police competition in the highly complex telecommunications sector following regulatory forbearance. They also involved adaptation of existing competition law principles to the realities of the telecommunications market. These reforms are detailed in Chapter 4 of the TPRP Report.

72. In the Backgrounder, reference is made to the Government's propose legislation to amend the *Competition Act* by adding a new fining power. This initiative is cited as part of the Government's plan for addressing competitive disputes following forbearance – but, unfortunately, this measure falls far short of

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<sup>6</sup> TPRP Report, p. 4-3, emphasis added.

what the TPRP recommended.

73. The TPRP expressly rejected the *Competition Act* framework as the appropriate model – both procedurally and substantively:

...while the Competition Bureau has a higher level of expertise in defining markets and assessing market power than does the CRTC, the Panel is not satisfied that the *Competition Act* provides an appropriate framework for the resolution of competitive disputes in the telecommunications sector where SMP still exists or where markets are in transition from SMP. Nor does it provide an appropriate framework in situations where the development, ongoing monitoring and supervision of sector-specific competitive safeguards may be required. As a body with responsibility for administering Canada's competition laws in all sectors of the Canadian economy, the Competition Bureau clearly lacks the degree of sector-specific knowledge possessed by the CRTC.

In addition, the Competition Bureau is constituted as an enforcement agency rather than as a quasi-judicial body. Its process does not allow for the timely resolution of disputes that routinely arise in the dynamic and rapidly changing telecommunications sector. The *Competition Act* has constituted the Competition Bureau as an investigative body that investigates and reviews complaints of anti-competitive conduct. It then decides whether there is sufficient evidence to pursue either civil or criminal proceedings before the Competition Tribunal or the courts. This two-stage process involves significant time lags, sometimes measured in years, between the lodging of complaints and the resolution of issues. This lengthy process is not well suited to an environment in which competitive disputes arise on a fairly frequent basis and require prompt resolution. In addition, the Competition Tribunal does not view itself as a regulator that monitors behavioural remedies on an ongoing basis.

While it is arguable that these shortcomings of the *Competition Act* regime could equally apply to other sectors of the economy, other sectors do not share the same attributes as the telecommunications sector. Chapter 3, Economic Regulation, describes some of the specific economic and technical conditions of telecommunications markets. As discussed elsewhere in this report, telecommunications is widely regarded as an enabling technology that is vital to both the social and economic well-being of Canadians. Governments, businesses, individuals, educational institutions, hospitals and emergency services all depend on an efficient and technically advanced telecommunications infrastructure. If the recommendations in this report are adopted, there will be significantly lighter regulation in the Canadian telecommunications sector than there

has been in the past. In this new environment, it will be important to have the capability to address allegations of anti-competitive conduct in a timely and effective manner.

These factors have led the Panel to consider a number of other institutional and procedural approaches adopted in other OECD countries that share Canada's legal and regulatory traditions.<sup>7</sup>

74. These concerns led the TPRP to recommend the creation of a new Telecommunications Competition Tribunal with combined expertise of the CRTC and Competition Bureau, new competition law provisions developed specifically for the telecommunications sector, and broad remedial powers derived from both the *Telecommunications Act* and the *Competition Act*.

75. Amending the *Competition Act* to provide the Competition Tribunal with a fining power does not address the central concern expressed by the TPRP and does not address the Panel's detailed recommendations on the reforms required.

76. By addressing only one half of the equation, namely reducing economic regulation, the Proposed Order fails to address the consequences of ignoring the TPRP's remedial recommendations. In effect, the Proposed Order casts a highly complex and inter-dependent industry, with a long history of abuse of dominance and other competitive disputes, into a legislative framework that is incapable of adequately addressing the issues in a timely manner. Given the importance of the telecommunications industry to our national economy and the social fabric of Canada, this is a very risky proposition. Yet there is no mention of the issue in the Proposed Order or the accompanying Background or Regulatory Impact Analysis Statement. The implication of that material seems to be that the Proposed Order is consistent with the TPRP's Report – but this is clearly not the case.

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<sup>7</sup> TPRP Report, page 4-14, emphasis added.

## **PROPOSED GUIDELINES FOR ABUSE OF DOMINANCE IN THE TELECOMMUNICATIONS SECTOR**

77. On September 26, 2006, the Competition Bureau released a Draft Information Bulletin delineating how it proposes to apply the existing *Competition Act* abuse of dominance provisions to the telecommunications sector after forbearance.

78. The Draft Bulletin confirms the TPRP's findings that the existing legislative framework is ill-suited to this purpose. In particular, the *Competition Act* and its institutional framework is incapable of effectively curbing abuses of dominance in telecommunications markets where significant market power exists or which are in transition from significant market power.

79. The *Competition Act* establishes a framework of general application to all areas of the Canadian economy that is intended to deal with relatively infrequent instances of anti-competitive conduct that can be effectively addressed through structural remedial orders. This underlying premise of the *Act* is inconsistent with the state of affairs that exists in the telecommunications market, where we are still transitioning from a monopoly to a competitive market structure, where there are still barriers to entry that need to be dismantled, and where competitive disputes arise on a frequent basis due to the integrated nature of communications networks and the high degree of reliance by competitors on the former monopoly suppliers' facilities.

80. In addition, the fact that market power, *per se*, is not sanctionable under the *Competition Act* means that the framework established by the *Competition Act* does not contain the tools necessary to dismantle barriers to entry in markets where there exists significant market power. Relief under the *Competition Act* is limited to those situations where a firm with market power engages in a practice of anti-competitive acts that results in a substantial lessening or prevention of

competition (SLC). If competition is not otherwise present in a market due to barriers to entry, no relief is available under the *Act*.

81. It is absolutely essential that lighter regulation of the incumbent telephone companies be accompanied by timely and effective adjudication of and relief for anti-competitive conduct. As the TPRP unequivocally recognized and the Draft Bulletin confirms, the framework established by the *Competition Act* cannot achieve these objectives. The two-step process established by the *Competition Act* for investigation and adjudication of allegations of anti-competitive conduct by two bodies with no resident expertise in the telecommunications industry is cumbersome and results in multi-year delays. While this may be acceptable in relatively static markets involving infrequent disputes, these timelines render the availability of relief largely if not entirely ineffective in dynamic markets, like the telecommunications market, in which competition has only recently been introduced and competitive disputes are likely to be relatively frequent.

82. The remedial powers provided by the *Competition Act* are also insufficient to support the development, ongoing monitoring and supervision of sector-specific competitive safeguards that may be required. The Draft Bulletin expressly confirms that neither the Competition Tribunal nor the Competition Bureau has the legislative mandate to impose behavioural remedies that require ongoing oversight and supervision. The TPRP Report, in contrast, recommended that abuse of dominance be enforced by a single authority vested with all of the enforcement powers under both the *Telecommunications Act* and the *Competition Act*.

83. As pointed out by the TPRP in its report, the Competition Bureau and the Competition Tribunal also lack the industry expertise that is critical to ensuring timely and effective assessment of abuse allegations and application of appropriate safeguards against anti-competitive conduct in telecommunications

markets.

84. The list of anti-competitive acts provided in the *Competition Act* is general and not specifically targeted to conduct in the telecommunications industry. If any degree of certainty is to be achieved, an attempt must be made to tailor these provisions to the type of practices that have historically arisen in the telecommunications sector. Again, this was recommended by the TPRP – but has been ignored in the Draft Bulletin.

85. The final element of abuse of dominance – proof of a substantial lessening or prevention of competition – is dealt with only in a cursory fashion in the Draft Guidelines, without any specific reference to specific characteristics of telecommunications markets and their relationship to the “substantiality” of anti-competitive effects. SLC cannot be proven where a market is otherwise foreclosed to competition. Furthermore, in markets where entry has occurred, the Competition Tribunal and the Competition Bureau have effectively required that all entrants have failed before finding a substantial lessening or prevention of competition. The effect of this test is that relief under the *Competition Act* in respect of anti-competitive conduct is largely if not entirely illusory.

86. If sanctions for anti-competitive conduct are to provide anything more than theoretical relief, much more than the delineation of the theoretical tests established by section 79 of the *Competition Act* and identification of evidentiary issues that may arise in applying these tests to the telecommunications industry is required.

87. In accordance with the recommendations of the TPRP, timely and effective adjudication of anti-competitive conduct demands clear definition of telecommunications-specific anti-competitive conduct and enforcement by a single quasi-judicial agency with detailed expertise in the telecommunications industry and each of the elements of abuse. To be effective, such an agency

must be equipped with a wide range of remedial powers, including behavioural remedies and ongoing monitoring and supervisory authority.

88. These measures require legislative changes – not the delineation of the manner in which existing, largely ineffective, provisions of the *Competition Act* are to be applied to the telecommunications market. This was expressly recognized by the TPRP and it has been ignored in the Proposed Order.

## **CONCLUSION**

89. As discussed in the body of this submission, the Proposed Order is the most interventionist order ever contemplated in the Canadian telecommunications sector. It steps over the dividing line between policy-making and regulatory implementation and it severely blurs the distinction between Government and regulatory functions. It thereby threatens the CRTC's status as an independent regulatory agency and is very likely to be viewed in an adverse light by the OECD and Canada's major trading partners.

90. Of particular concern is the proposal to eliminate all winback restrictions in advance of any forbearance order. This marketing safeguard was established in direct response to the ILECs' anti-competitive marketing strategies in a market in which they are dominant. To remove these restrictions in advance of a determination that the ILECs have lost their dominance, invites a return to anti-competitive conduct and the possible thwarting of competitive entry. The degree of competition that is present in local markets varies significantly across Canada. To remove this safeguard without regard to this fact is extremely prejudicial to new entrants and could severely retard the expansion of competition in many areas. Removal of the marketing safeguards should not be done until six months after forbearance is granted in a given local market. If none of the other changes proposed below are made to the Proposed Order, this one change is essential.

91. The Proposed Order essentially re-writes every major determination made by the Commission in its Decision, and rules on other issues in advance of the CRTC even releasing its decision in follow-up proceedings involving the substitutability of wireline and wireless services and the appropriate time to remove restrictions on winbacks. The Proposed Order does not even pay the CRTC or industry participants in those proceedings the courtesy of waiting for the Commission to issue a determination in those proceedings which are now completed.

92. The Government's proposal to rewrite the Commission's determinations on highly technical issues such as the relevant geographic and product markets, the substitutability of services and appropriate interconnection standards, strays into an area of detail that has little to do with policy and much to do with expertise of the regulator.

93. Another key concern respects the lack of an effective adjudicator of competition disputes in a post-forbearance environment. The TPRP was clear that the *Competition Act* does not provide a suitable framework for the telecommunications sector. It devoted a whole chapter of its report to this issue and recommended reforms to correct this situation. It clearly tied its recommendations for less economic regulation to the need to have adequate remedies in the new environment. The Proposed Order does not even mention this problem or the TPRP's recommendations in this regard.

94. This problem cannot be addressed by simply conferring a civil fining power on the Competition Tribunal. As the TPRP pointed out, the two-stage process embodied in the *Competition Act*, the huge delays in obtaining relief, the lack of expertise of the Bureau and the Tribunal in the telecommunications sector and the inadequacies of the existing *Competition Act* provisions all make this regime an inappropriate one for ongoing dispute resolution in the telecommunications sector. The recent Draft Bulletin issued by the Competition

Bureau on abuse of dominance in the telecommunications sector simply serves to underscore these problems.

95. What is needed to address these issues is legislative reform – not piecemeal *ad hoc* interventions by the Governor in Council. The Proposed Order creates a potentially dangerous situation in which regulation and regulatory safeguards are removed prematurely without an effective body to respond to the inevitable fall-out.

96. For these reasons, we respectfully request that the Proposed Order not be issued and that the Government consider more substantive legislative-based reforms to implement both parts of the TPRP's recommendations – less economic regulation and the creation of an effective adjudicator of competition disputes. Unless these issues are addressed in tandem, the ILECs will be able to exploit their market power to the detriment of consumers and the Government's longer term policy objectives.

97. Alternatively, the Proposed Order should be referred to a Parliamentary Committee for further study.

98. In any event, regardless of what tests are used to establish the presence or absence of market power, the Governor in Council ought not to remove the winback restrictions until six months after a determination that the ILEC has in fact lost its market power and forbearance is therefore justified in the relevant local market.