Opening Canada's Doors to
Foreign Investment in Telecommunications:
Options for Reform

Submission to Industry Canada

by

Verizon Canada Ltd.

July 30, 2010

I. Introduction

1. This submission is made to the federal Department of Industry ("Industry Canada" or the "Department") by Verizon Canada Ltd. ("Verizon Canada") in response the Department's invitation for submissions regarding its consultation paper issued on June 11, 2010, entitled "Opening Canada's Doors to Foreign Investment in Telecommunications: Options for Reform" (the "Consultation Document").

2. Both Verizon Canada and its parent company, Verizon, Inc. (collectively, "Verizon"), have had a long-standing presence in the Canadian telecommunications market. A predecessor of Verizon, Inc., General Telephone and Electronics ("GTE"), operated in Canada through substantial interests in certain subsidiaries, such as B.C. Tel and Québec-Téléphone, for several years prior to the introduction of restrictions on foreign direct investment ("FDI") in Canada's telecommunications sector. Verizon Canada first entered the Canadian Internet services market as a reseller in 1991 and, since that time, has grown and expanded its operations, and now provides a wide range of voice and data services to Canadian businesses and enterprise customers. Verizon employs approximately 200 people across Canada in offices located in Toronto, Montreal, Calgary and Vancouver. We are proud to bring the global reach of Verizon's services to Canadian customers.

3. In Verizon Canada's view, Canada's foreign ownership restrictions in the telecommunications sector are a poor reflection of Canada's general commitment to opening its markets to increased international trade and investment. These restrictions are anti-competitive and negatively impact Canada's domestic telecommunications industry and the interests of Canadians.

4. The many positive impacts of FDI on economies in general, and in the telecommunications industry in particular, are undisputed. Studies show that, in fact, foreign-controlled companies are more likely to create higher-paying white-collar jobs than their Canadian-controlled competitors. Many other studies and reports of government-mandated bodies, industry stakeholders, and academics have advocated

lifting the restrictions on FDI in the telecommunications sector precisely in order to take advantage of these, and other, benefits.

5. Canada's restrictions on FDI are also inconsistent with the government's stated policy objective of placing increased reliance on market forces in Canada's telecommunications sector.[1]

6. For the reasons set out in this submission, Verizon Canada fully supports Option 3 of the Consultation Document, namely the complete removal of foreign investment telecommunications restrictions and, to this end, it respectfully requests that Industry Canada take immediate steps to:

- Remove the foreign ownership restrictions contained in the *Telecommunications Act* and the *Radiocommunication Regulations;* and
- Rescind the *Canadian Telecommunications Common Carrier Ownership and Control Regulations*.

7. Verizon Canada understands that this consultation pertains specifically to the FDI restrictions that currently apply to Canada's telecommunications industry and that the Department is not considering similar restrictions promulgated under Canada's *Broadcasting Act*. For this reason, Verizon Canada's comments are limited herein to a consideration of the FDI restrictions that apply to Canada's telecommunications sector. While Verizon Canada recognizes that there are some service providers that are subject to FDI restrictions under both the *Telecommunications Act* and *Broadcasting Act*, it would clearly remain open to these service providers to restructure their respective operations if they wished to avail themselves of liberalized foreign ownership rules under the *Telecommunications Act*.[2]

1 SOR/2006-355 (http://canadagazette.gc.ca/partII/2006/20061227/html/sor355-e.html).

2 On July 12, 2010, the FDI restrictions relating to Canadian satellites were lifted. With the removal of these restrictions, it is now theoretically possible for non-Canadians to acquire a controlling interest in one or more operators of Canadian Direct-to-Home ("DTH") satellites without disturbing the ownership structure of the broadcasting distribution undertakings ("BDUs") that make use of these satellites to provide DTH services in Canada (e.g., ExpressVu and StarChoice). This example illustrates how even the operations of BDUs can be

II. Canada's FDI policies are a poor reflection of its international commitments to open its markets to increased international trade and competition

8. The current FDI restrictions are inconsistent with Canada's increased integration into the global economy and competitiveness in the international market.[3] Canada's current FDI restrictions stipulate, among other things, that: (i) at least 80 per cent of the voting equity of a telecommunications common carrier be held by Canadians; (ii) at least 80 per cent of the board of directors of the carrier be Canadian citizens that are ordinarily resident in Canada; (iii) at least 66.67 per cent of the voting equity of any parent corporation of the carrier be held by Canadians; and (iv) that the carrier not otherwise be controlled in fact by non-Canadians.

9. Canada thus limits the aggregate direct and indirect foreign ownership in all telecommunications carriers to a maximum of 46.7 per cent, except those that own Canadian satellites and earth station facilities and/or submarine cable facilities.

10. According to the OECD, "Canada's restrictions … are the most severe in the OECD".[4]

Table I: FDI Restrictions by Country[5]

Country	FDI Restrictions
Australia	No restrictions on industry as a whole; some restrictions on Telstra (government-owned incumbent).
Austria	No foreign ownership restrictions.
Belgium	No foreign ownership restrictions.

treated differently from an FDI perspective than the underlying telecommunications networks over which their channel line-ups and packages are distributed.

3 OECD, *OECD Reviews of Regulatory Reform: Regulatory Reform in Canada from Transition to New Regulation Challenges*, "Regulatory Reforms in the Telecommunications Industry" (Paris: OECD, 2002) (http://www.oecd.org/dataoecd/48/28/1960562.pdf) ["OECD Review"].

4 Dimitri Ypsilanti (Directorate for Science, Industry and Technology, OECD), "Review of Foreign Investment Limitations in Canada" at 3. This paper was submitted in 2010 to the House of Commons Standing Committee on Industry, Science and Technology.

5 Adapted from OECD, *OECD Communications Outlook 2009* at 47-9 (http://akgul.bilkent.edu.tr/oecd/oecd-ictoutlook-2009.pdf) ["OECD Communications Outlook"].

Country	FDI Restrictions
Canada	**At least 80% of the voting shares of a terrestrial wireline or wireless carrier must be owned by Canadians; at least 80% of the board of directors of the carrier must be Canadian. Also, holding companies of terrestrial wireline and wireless carriers must be Canadian-controlled (66 2/3% of voting shares must be owned by Canadians).**
Czech Republic	No foreign ownership restrictions except as regards land ownership.
Denmark	No foreign ownership restrictions.
Finland	No foreign ownership restrictions.
France	No foreign ownership restrictions.
Germany	No foreign ownership restrictions.
Greece	No foreign ownership restrictions.
Hungary	No foreign ownership restrictions.
Iceland	No foreign ownership restrictions.
Ireland	No foreign ownership restrictions.
Italy	No foreign ownership restrictions.
Japan	No general ownership restrictions; foreign capital participation in NTT Corp. must be less than 1/3; board members of NTT Corp. must have Japanese nationality.
Korea	Previously, facilities-based operators could not be more than 49% foreign-owned. However, in the Korea-US Free Trade Agreement, Korea committed to permit 100% indirect foreign ownership.[6]
Luxembourg	No foreign ownership restrictions.
Mexico	No foreign ownership restrictions on wireless services. Foreign investors may own up to 49% of a telecom enterprise and telecom concessions may only be granted to Mexican nationals or companies.
Netherlands	No foreign ownership restrictions.
New Zealand	No foreign ownership restrictions except for Telecom New Zealand (government-owned incumbent).
Norway	No foreign ownership restrictions except that government must hold 34% of shares in Telenor ASA.

[6] The Korea-U.S. Free Trade Agreement, "Report of the Industry Trade Advisory Committee for Information and Communications Technologies, Services and Electronic Commerce (ITAC 8)" (April 27, 2007) at 9 (http://ustraderep.gov/assets/Trade_Agreements/Bilateral/Republic_of_Korea_FTA/Reports/asset_upload_file66_12790.pdf).

Country	FDI Restrictions
Poland	No foreign ownership restrictions except that a majority of the members of a supervisory board of a telecommunications company must be Polish citizens.
Portugal	No foreign ownership restrictions.
Slovak Republic	No foreign ownership restrictions.
Spain	No foreign ownership restrictions, except for provisions that regulate competition generally (whether national or foreign ownership).
Sweden	No foreign ownership restrictions.
Switzerland	No foreign ownership restrictions except that government must maintain majority shareholding in Swisscom.
Turkey	No foreign ownership restrictions.
United Kingdom	No foreign ownership restrictions.
United States[7]	For wireline common carriers and wireless non-common carriers, 100% foreign ownership is permitted without government approval. For wireless common carriers, 25% indirect and 20% direct foreign ownership is permitted without government approval. Additional indirect foreign ownership up to 100% is permitted with the approval of the FCC based on a finding that the investment is in the public interest.

11. The OECD has singled out Canada's rules as particularly discriminatory in comparison to other countries[8] and has recommended that Canada "reduce barriers by eliminating ownership restrictions in telecommunications … and by allowing a majority of board members to be non-residents in sectors where this is currently not allowed."[9] Canada's FDI restrictions are also inconsistent with its support of a collective request submitted as a part of the Hong Kong WTO Ministerial in 2006. This request reads in, in relevant part, as follows: "we request that your government make commitments on telecommunications services in accordance with the following…No national treatment limitations and no

7 These rules were articulated by the FCC in a ruling, wherein the FCC affirmed that the public interest is served by permitting greater investment by individuals or entities from WTO Member Countries in entities that control common carrier radio licensees. The FCC's test presumes that investments from individuals or entities from these countries raise no competitive concerns. It is therefore very permissive of foreign ownership. See *In the Matter of Stratos Global Corporation*, Memorandum Opinion and Order and Declaratory Ruling (FCC 07-213), paras. 72-75 and 95-100, where 100% indirect equity and voting ownership by foreign investors from WTO Member countries was allowed (http://fjallfoss.fcc.gov/edocs_public/attachmatch/FCC-07-213A1.pdf).

8 OECD Review, *supra* note 3.

9 OECD, *Economic Policy Reforms: "Going for Growth 2007"*, Canada Country Note at 8 (http://www.oecd.org/dataoecd/48/22/38088884.pdf).

substantial market access limitations, specifically … (v) Majority foreign capital participation and effective control to be allowed."[10]

12. Canada's foreign ownership restrictions were also the subject of discussions at the 2007 WTO Trade Policy Review, where several representatives questioned Canada's foreign ownership rules. The representative of the European Community, a growing union currently comprised of 27 member states, expressed specific concerns over Canada's foreign ownership caps in the telecommunications sector.[11] Europe's concerns were also voiced in a recently drafted European Parliament report that lists unjustified foreign ownership caps as one of the "ten trade barriers in the modern global economy."[12]

13. The International Chamber of Commerce has also stated that governments should reduce or eliminate foreign ownership restrictions in the telecommunications sector not only to promote investment and take advantage of the benefits of such investment, but also to promote "full implementation of existing commitments made under the WTO framework."[13]

14. Canada's FDI restrictions result in differential and discriminatory regulatory rules that prevent full participation by foreign-owned telecommunications companies in the market.[14] Such restrictions have little place in the increasingly globalized economy,

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10 http://www.uscsi.org/publications/papers/collective/telecom.pdf.

11 WTO (Trade Policy Review Body), *Trade Policy Review (Canada)*, Minutes of the Meeting (Revision), (29 June 2007) WT/TPR/M/179/Rev.1, (07-2754). (http://www.wto.int/english/tratop_e/tpr_e/tp280_e.htm).

12 http://www.europarl.europa.eu/oeil/FindByProcnum.do?lang=2&procnum=INI/2007/2185.

13 International Chamber of Commerce, *Telecoms Liberalization: An international business guide for policymakers, 2nd edition*. ICC Tools for e-Business (Paris: International Chamber of Commerce, 2007) (http://www.iccwbo.org/uploadedFiles/ICC/policy/e-business/Statements/TELECOMS%20LIBER-edition%20Final.pdf).

14 Telecommunications Policy Review Panel, *Final Report 2006* at 11-17 ["TPRP Report"] (http://www.telecomreview.ca/epic/site/tprp-gecrt.nsf/vwapj/report_e.pdf/$FILE/report_e.pdf). See, in particular, the Afterward of the TPRP's Report as well as the discussion at 3-43 to 3-45 which examines certain rules that have been established by the CRTC in the market for local telephony services which effectively prevent resellers (many of which have non-Canadian owners) from availing themselves of certain rights that have been accorded exclusively to Canadian owned and controlled carriers in this market. In a submission to the Telecom Policy Review Panel, Verizon Canada's predecessor, MCI Canada, submitted a legal opinion which demonstrated that these rules are discriminatory and contravene Canada's commitments under the GATS (see http://www.telecomreview.ca/eic/site/tprp-gecrt.nsf/vwapj/MCI_Canada_-_Submission_(Legal_Opinion).pdf/$FILE/MCI_Canada_-_Submission_(Legal_Opinion).pdf). The Panel responded to this concern by recommending that "[R]esellers in the local telecommunications services market

especially if Canada intends to participate fully in that economy and to apply the principles of fair competition and non-discrimination.[15]

III. The Negative Effect of Current FDI Restrictions in the Telecommunications Sector

15. Statistics Canada has found that, in the last forty years, changes in foreign multinational involvement in the Canadian telecommunications sector have coincided with changes in the regulatory regime governing FDI.[16] The impact of regulation on FDI is apparent even after accounting for other factors such as labour and capital costs, industry conditions, and relative returns on investment.[17] Indeed, according to the Department of Foreign Affairs and International Trade, FDI in the information and communications sector has been steadily declining over the last eight years, from comprising 11.68 per cent of money invested in all Canadian industry sectors in 2000 to nearly halving in 2001 and since then *declining steadily* to 3.93 per cent of FDI in 2009.[18]

16. This corroborates the finding of the April 2003 Report of the Standing Committee on Industry, Science and Technology, *Opening Canadian Communications to the World*,[19] that more restrictive foreign ownership rules are correlated with decreased investment in the Canadian telecommunications sector.[20] Indeed, evidence filed with the 2003 Standing

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who choose to undertake all the obligations of a competitive local exchange carrier should have all the regulatory rights and obligations applicable to competitive local exchange carriers."

15 OECD Review, *supra* note 3.

16 John R. Baldwin and Guy Gellatly, *Global Links: Multinationals in Canada: An Overview of Research at Statistics Canada*. The Canadian Economy in Transition Series, 11-622-MIE – No. 014 (Ottawa: Minister of Industry, 2007) (http://www.statcan.ca/english/research/11-622-MIE/11-622-MIE2007014.pdf) at 16 ["StatsCan Report"].

17 John R. Baldwin and Guy Gellatly, *Global Links: Long-Term Trends in Foreign Investment and Foreign Control in Canada, 1960 to 2000*, The Canadian Economy in Transition Series, 11-622-MIE – No. 008. (Ottawa: Statistics Canada, 2005) (http://www.statcan.ca/english/research/11-622-MIE/11-622-MIE2005008.pdf).

18 Foreign Affairs and International Trade Canada, "Foreign Direct Investment Stocks in Canada", CANSIM Table 376-0052 (http://www.international.gc.ca/economist-economiste/assets/pdfs/FDI-Inward-Stocks-by-NAICS-Industry-ENG.pdf).

19 Report of the Standing Committee on Industry, Science and Technology, *Opening Canadian Communications to the World* (April 2003) ["2003 Standing Committee Report"] (http://cmte.parl.gc.ca/Content/HOC/committee/372/inst/reports/rp1032302/instrp03/instrp03-e.pdf).

20 2003 Standing Committee Report, *ibid*.

Committee indicates that FDI restrictions raise the cost of capital and create a disincentive to investment.[21]

17. These findings were confirmed by the Telecom Policy Review Panel, which observed in its 2006 Report that "[a] number of telecommunications companies, *particularly those in emerging market segments in the wireless telecommunications field*, have argued that the existing foreign investment rules are a disincentive for foreign investors …" Restrictions on the purchase and sale of voting shares certainly discourages investment by strategic investors."[22] More specifically, foreign ownership restrictions increase the cost of capital by at least $1.06 per month per subscriber for an incumbent telephone company.[23]

18. Yet again, in 2008, the Competition Policy Review Panel highlighted the disadvantages of the current FDI-restricting regime: "[t]here is considerable evidence that liberalizing foreign investment restrictions brings demonstrable economic benefit through increasing competitive pressure on all participants in the market … Foreign investment restrictions reduce competitive intensity in a number of ways that are well known. In relation to telecommunications markets, they include placing potential new entrants (to the extent they can enter markets in the first place) at a cost disadvantage relative to incumbents, limiting the sources of finance available to existing incumbents, [and] distorting optimal financing structures".[24]

19. Finally, the June 2010 Report of the Standing Committee on Industry, Science and Technology, *Canada's Foreign Ownership Rules and Regulations in the Telecommunications Sector*, noted that "foreign ownership restrictions disproportionately penalize new entrants and smaller players through their effect on the cost of capital … because of the limit they impose on the potential sources of capital"; concluding: "the economic case in favour of removal of foreign ownership restrictions is clear".[25] Against

21 2003 Standing Committee Report, *ibid* at 15 and 19.
22 TPRP Report, supra note 14 at 11-17.
23 TPRP Report, *ibid*.
24 Competition Policy Review Panel, *Final Report – June 2008* at 47 ["CPRP Report"] (http://www.ic.gc.ca/eic/site/cprp-gepmc.nsf/eng/00060.html).
25 Report of the Standing Committee on Industry, Science and Technology, *Canada's Foreign Ownership Rules and Regulations in the Telecommunications Sector* (June 2010) at 41 and 25 ["2010 Standing Committee

the arguments advanced by some stakeholders that the restrictions only applied to some forms of capital, the Committee cited observations that the *de facto* test "makes foreign capital typically reluctant to push its ownership of debt and non-voting shares above a certain threshold", and that potential future restructuring events would be constrained by the foreign ownership restrictions, thereby providing a further disincentive for foreign investment.[26]

20. There can no longer be any doubt that restrictions on FDI have the effect of limiting investment in telecommunications, overall.[27] This effect is unsurprising given our very global economy, and it is quite opposite to the goal of promoting Canada as a destination for foreign investors. Indeed, one need only look to India's growing telecommunications sector as an example. Investment in India's telecom sector has shown a marked change that is the direct result of trade liberalization. With the second-highest growth rate in the world, much of India's success in its telecommunications sector has been attributed to regulatory reforms opening telecom to domestic and foreign competition.[28] When India lifted FDI restrictions from 49 per cent to 74 per cent for certain types of services, Verizon applied for and received licenses for those services and consequently is increasing its investment and business in India – as are many other global telecommunications companies – with attendant benefits for the Indian economy.[29] Telecommunications liberalization in India has met with remarkable success, leading to lower rates, higher "teledensity", and more reliable service.[30] India's success can, in part, be attributed to the investment in India's newly opened market.

Report"]
(http://www2.parl.gc.ca/HousePublications/Publication.aspx?DocId=4618793&Language=E&Mode=1&Parl=40&Ses=3)

26 *Ibid*., at 26

27 OECD Review, *supra* note 3.

28 Canadian Services Coalition, (2007) "Canada and India: Trade and Investment Opportunities in the Services Sector" (www.canadianservicescoalition.com).

29 Department of Industrial Policy & Promotion, "Opportunities in Infrastructure in India: Background Paper", OECD India Investment Roundtable, 19 October 2004, New Delhi (http://dipp.nic.in/oecd_backpaper/infra_index.htm).

30 Coalition of Service Industries, *Making the Most of the Doha Opportunity: Benefits from Service Liberalization* (Coalition of Service Industries Research and Education Foundation, 2006) (http://www.uscsi.org/services_study/full_study.pdf).

21. New entrants play a major role in introducing innovative telecommunications services to the Canadian telecommunications market and their presence in the market has led to more choice for customers, higher quality of services, and a range of new services.[31] Yet existing FDI restrictions jeopardize new entrants' positions in the telecommunications sector. New entrants require access to capital at a reasonable cost for large capital investments to build and upgrade networks, to ensure attractive product and service offerings, and to off-set the usual start-up losses. However, as noted by the TPRP, "[i]n limiting a company's ability to raise equity outside Canada, the foreign investment rules provide an incentive for greater reliance on debt than equity capital and for raising a larger share of equity capital in Canada than firms otherwise might do."[32] In effect, this means that competitors end up with "very high debt levels typically 70% or more of financing which is far higher than the ILECs."[33] Because of the capital intensive nature of the telecom industry it is essential for new entrants to continue to seek sources of financing but as capital is more difficult and costly to obtain for new entrants there is a distinct competitive disadvantage such that it is difficult to fund on-going growth. In one example, it was calculated that GT Group Telecom, a new wireline entrant that was unable to remain solvent, would pay $140,000,000 more *per year* than BCE to secure $1 billion of financing.[34] (It is of note that GT Group Telecom filed for bankruptcy in 2002). Current FDI restrictions are both barriers to entry for potential new entrants and obstacles to those diminishing numbers of new entrants that manage to enter the Canadian market.

22. The practical effect of FDI restrictions on Verizon's operations in Canada is that Verizon Canada is prevented from owning and operating its own transmission facilities. Instead, it must lease facilities from other carriers, making it more difficult for Verizon to control its underlying costs. Verizon is also unnecessarily dependent on other service providers for critical network components and services and it is effectively precluded from making

[31] OECD Review *supra* note 3 at 41-2.
[32] TPRP Report, *supra* note 14 at 11-17.
[33] Submission of Robert Yates of Lemay-Yates Associates Inc. to the Standing Committee on Industry, Science and Technology, cited in the 2003 Standing Committee Report, *supra* note 19 at 21.
[34] See generally Dean Proctor and Simon-Pierre Olivier, (2002) "Capital Flows and the Cost of Capital: The Importance of Liberalized Investment Rules for a Competitive Telecommunications Sector". Prepared for the conference, Switching to High Growth: Issues in Policy and Regulation in the India Telecom Sector, New Delhi, 18-19 October 2002 (http://www.darvoza.uz/downloads/ICT/ICT2287.pdf).

direct network investments. These restrictions also limit the ability of Verizon to provide innovative new products and services to its customers, including some of the more integrated or “seamless” international services that are offered by Verizon to customers in several locations around the world.

23. FDI restrictions limit investment and increase the cost of capital thereby slowing Canada’s competitive development[35] at a cost estimated at $675 million per year.[36] By placing the telecommunications industry in a straightjacket, FDI restrictions have thus failed to serve the goal of the Canadian government of fostering a competitive marketplace[37] and placing increased reliance on market forces in the telecommunications sector.

IV. Dispelling Myths About FDI

24. One of the arguments that is often raised in opposition to greater FDI is that foreign owned or controlled companies are systematically biased in favour of their “home” country and against “host” countries, leading to a “hollowing-out” of the industry in the “host” country. This argument is without foundation and flatly contradicted by the facts. In this era of globalization and multinational enterprises, what is becoming increasingly clear is that many multinationals have no obvious “home” country.[38] Rather, multinational enterprises act to take advantage of opportunities that present themselves in “host” countries, according to the means and qualities of particular “host” countries.

25. For example, a Statistics Canada report, which is based on several studies[39] shows that FDI has a positive effect on domestic competitiveness and productivity.[40] Foreign-owned firms, particularly multinational firms, create more and higher quality job opportunities

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35 OECD Review, *supra* note 3.
36 2003 Standing Committee Report, *supra* note 19.
37 See generally Donald G. McFetridge, “Evaluation of Current Policy Towards Inbound FDI” (revised December 2004), CTPL Trade and Investment Conference (Ottawa, November19, 2004) (http://www.carleton.ca/ctpl/conferences/documents/EvaluationofCurrentPolicyTowardsInwardFDI-McFetridge.pdf).
38 *Ibid.* at 5.
39 See generally StatsCan Report, *supra* note 16.
40 *Supra* note 21 at 4.

for Canadians. Typically, foreign-controlled plants have higher productivity,[41] are more capital intensive, pay higher wages, *and* hire more white-collar workers than those that are Canadian-controlled.[42] Foreign-controlled firms also create just as many – if not more – head office-level jobs as Canadian-controlled companies: the national head offices of foreign-controlled firms accounted for six out of ten new head-office-level jobs created from 1999-2005. In fact, foreign-controlled firms are *more likely* to have a full Canadian head office-level function than a Canadian-controlled company.

V. The Positive Impact of FDI

26. The positive impact of FDI has been affirmed world-over. Countries with fully liberalized telecom sectors have faster growth than countries with restrictive sectors.[43] Furthermore, foreign investment liberalization in the telecommunications sector is linked with better economic performance in non-telecommunications sectors of the economy;[44] this may be because foreign firms are more likely to diversify across industries than Canadian-controlled firms such that the benefits brought by increased FDI in the telecommunications sector spill over to other parts of the Canadian market[45] and because domestic firms benefit from vertical linkages with foreign firms.[46]

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41 Wolfgang Keller and Stephen R. Yeaple, "Multinational Enterprises, International Trade, and Productivity Growth: Firm-Level Evidence from the United States" IMF Working Paper, WP/03/248 (International Monetary Fund, 2003) (http://www.imf.org/external/pubs/ft/wp/2003/wp03248.pdf).

42 See also John R. Baldwin and Wulong Gu, *Global Links: Multinationals, Foreign Ownership and Productivity Growth in Canadian Manufacturing*, The Canadian Economy in Transition Series. 11-622-MIE – No. 009. (Ottawa: Statistics Canada, 2005) (http://www.statcan.ca/english/research/11-622-MIE/11-622-MIE2005009.pdf)

43 Coalition of Service Industries, *Making the Most of the Doha Opportunity: Benefits from Service Liberalization* (Coalition of Service Industries Research and Education Foundation, 2006) (http://www.uscsi.org/services_study/full_study.pdf).

44 Scott J. Savage, Alan Schlottman and Bradley S. Wimmer, *Telecommunications Investment, Liberalization and Economic Growth*, AEI-Brookings Joint Center for Regulatory Studies, Publication 03-30 (Washington, DC: 2003), (http://aei-brookings.org/admin/authorpdfs/redirect-safely.php?fname=../pdffiles/phpZd.pdf)

45 StatsCan Report, *supra* note 16 at 23.

46 Alla Lileeva, *Global Links: The Benefits to Domestically-Controlled Plants from Inward Direct Investment–the Role of Vertical Linkages*. The Canadian Economy in Transition Series, 11-622-MIE – no. 010. (Ottawa: Statistics Canada, 2006) (http://www.statcan.ca/english/research/11-622-MIE/11-622-MIE2006010.pdf)

27. Indeed, the fact that FDI has a positive effect on domestic economies is no longer disputed. The only question is "by how much"?[47] The answer is: by a lot. Below are some of the specific ways in which FDI has been shown to improve Canadian markets.

(a) More stability

28. Foreign-controlled companies and multinationals are less susceptible to domestic changes in GDP than purely domestically controlled companies: the international nature of these companies means that the capital costs of the company are derived from the international rather than the domestic market. This broader, global, perspective also means that foreign-controlled companies and multinationals have more stable production levels in the face of fluctuating local demand. As might be expected, these companies also eliminate fewer jobs in response to local downturns when compared to domestic counterparts; labour markets are thus also less volatile. Finally, foreign-controlled companies and multinationals have the ability to react more flexibly to change because of their international "footprint". These factors contribute to the overall stability of foreign-controlled and multinational companies when compared to Canadian-controlled non-multinationals.[48]

(b) Innovation, R&D and Managerial know-how

29. Foreign investment is an important channel for the diffusion of ideas and innovations.[49] Foreign-controlled companies innovate *in all sectors and in almost all size categories* more frequently than Canadian-owned companies, and the innovation rates of foreign-controlled firms are about 10 percentage points higher than domestic counterparts.[50] They are also more likely to produce world-first innovations (as opposed to "improvements" to prior technologies), to apply advanced technologies, and to have R&D divisions.[51]

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47 TPRP Report , *supra* note 14 at 11-16; McFetridge, *supra* note 37 at 4.

48 StatsCan Report, *supra* note 16 at 25.

49 See, *e.g.* Surendra Gera, Wulong Gu and Frank C. Lee, *Foreign Direct Investment and Productivity Growth: The Canadian host-country experience*. Industry Canada Working Paper No. 30 (Ottawa: Industry Canada, 1999) (http://www.ic.gc.ca/epic/site/eas-aes.nsf/vwapj/wp30e.pdf/$FILE/wp30e.pdf).

50 John R. Baldwin and Wulong Gu, *Innovation, Survival and Performance of Canadian Manufacturing Plants*, Economic analysis (EA) research paper series. 11F0027MIE – No. 022. (Ottawa: Statistics Canada, 2004) (http://www.statcan.ca/english/research/11F0027MIE/11F0027MIE2004022.pdf).

51 StatsCan Report *supra* note 16 at 8 and 28.

30. One reason for the high level of innovation from foreign-controlled companies is their access to technology. Foreign-controlled companies are in a position to acquire ideas and inventions through technology transfer via intra-firm networks with parent, sister, and subsidiary companies and can more easily purchase new technology from multinational affiliates. The innovative capacities of foreign-controlled companies are transferred to domestic competitors via adoption of new technologies and the transfer of ideas and expertise through employee movement from foreign-controlled to domestic-controlled companies. Finally, foreign-controlled firms, as customers of domestic suppliers, serve as a source for ideas for innovation.[52]

31. In addition to passive ways in which FDI encourages Canadian innovation, foreign-controlled business are often highly engaged in and make large contributions to innovation in Canada.[53] In fact, Statistics Canada reports that foreign-controlled firms can be more active in local R&D than their Canadian counterparts.[54] They are also just as likely to rely on unrelated local firms and university partnerships as domestic firms.[55] In other words, the R&D activities of foreign-controlled firms do not occur in isolation from host economies; rather, foreign-controlled firms are an important source of vitality for innovation in Canada.

32. FDI also brings financial ideas and influence, strategic marketing techniques, human resource ideas, and other management know-how to Canada; it is "not just about cash".[56]

33. FDI is clearly beneficial for technological innovation, R&D, and transfer of managerial functions and knowledge. Given the restrictions on FDI in the telecommunications sector,

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52 TPRP Report, supra note 14; McFetridge, *supra* note 37 at 3, citing Baldwin and Gu, "Multinational, Foreign Ownership and Productivity Growth", Industry Canada Conference on Industrial Economics and Performance in Canada (Ottawa, September 30-31 2004).

53 Baldwin and Hanel (2000) (http://www.statcan.ca/english/research/11F0019MIE/11F0019MIE2000151.pdf)

54 StatsCan Report, *supra* note 16 at 27.

55 StatsCan Report, *supra* note 16 at 27-8.

56 TPRP Report, *supra* note 14 at 11-20; Steven Globerman, "Implications of Foreign Ownership Restrictions for the Canadian Economy – A Sectoral Analysis", Discussion Paper Number 7 (April 1999), Industry Canada Research Publications Program at 4 (http://www.ic.gc.ca/epic/site/eas-aes.nsf/vwapj/dp07e.pdf/$FILE/dp07e.pdf); testimony of Konrad von Finckenstein, QC, Commissioner of Competition, Competition Bureau, to the House of Commons Committee on Industry, Science and Technology, February 24, 2003 (http://cmte.parl.gc.ca/Content/HOC/committee/372/inst/evidence/ev732323/instev23-e.htm#Int-437224).

it is not surprising that Canada is "behind" in the newest markets where multinationals are in the global forefront, namely broadband deployment and mobile wireless services.[57]

(c) Increased competition

34. A report by Forrester Research found that competition in the Canadian telecommunications sector is "worrisome", and urged business telecom customers to support competition by making service arrangements with non-ILEC companies because of the high concentration of ownership in this industry sector.[58] Since the release of the Forrester Research report, there have been several other reports and studies which have observed that Canada's international rankings in both the pricing and penetration of broadband and mobile wireless services are slipping, which is often a symptom of insufficient competition.[59]

35. Clearly, there is a need for more competition in the Canadian telecommunications market – competition that should not only be supported by customers but also by the government. However, current restrictions on foreign investment shut out major potential sources of financing for telecom competitors in Canada. By allowing competitors and new entrants access to funds from foreign investors, competition in telecom will increase.[60] Increasing market competition in the telecommunications sector leads to higher levels of productivity, telecommunications service quality, and lower prices.[61] In fact, even the threat of increased market entry has a strong positive impact on these factors.[62]

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57 TPRP Report, *supra* note 14 at 11-21.

58 Brownlee Thomas, "The Worrisome State of Canadian Business Telecoms Competition" (Forrester Research Inc., 2007) (excerpt at: http://www.forrester.com/Research/Document/Excerpt/0,7211,43609,00.html).

59 See, for example, the Senate Standing Committee on Transport and Communications, *Plan for a Digital Canada*, issued on 16 June 2010 (http://www.planpouruncanadanumerique.com/index.php?lang=en) and the *OECD Communications Outlook 2009*, *supra* note 5.

60 Lemay-Yates Associates Inc., "Access to capital – Impact of foreign investment restrictions on telecom competitors", Report to the Standing Committee on Industry, Science and Technology (February 2003) at 3.

61 Olivier Boylaud and Giuseppe Nicoletti (2000) "Regulation, Market Structure and Performance in Telecommunications", OECD Economics Departments Working Papers No. 237 (http://papers.ssrn.com/sol3/papers.cfm?abstract_id=238203).

62 *Ibid,* at 7.

36. In summary, encouraging FDI brings an infusion of capital to the Canadian market, thereby generating growth and income[63] and encouraging strategic investment in high-risk situations where Canadian investors may not wish to participate.[64]

VI. Canada Should Liberalize its Restrictions on FDI in the Telecom Sector

37. The data overwhelmingly supports the lifting of Canada's telecommunications foreign ownership rules in the telecom sector. As indicated above, the cost of capital is a chief concern for new entrants to the telecommunications market, and FDI restrictions severely affect the availability of capital from otherwise interested investment partners. The current telecommunications foreign ownership rules restrict the amount of voting equity that can be held by a foreign company, forcing them to hold debt or to not invest at all. In other words, the restrictions limit the ability of investors to truly participate in the growth of a firm, thereby creating a "chilling effect" for foreign investors who might otherwise have an interest in investing in the Canadian telecom sector. In particular, the restrictions limit both the number and type of investors who can or would participate in the market if given a open opportunity to do so.

38. As noted above, Canada limits the aggregate direct and indirect foreign ownership in facilities-based telecommunications carriers to a maximum of 46.7 per cent in all Canadian carriers, except owners/operators of Canadian satellites and earth station facilities and international submarine cable facilities. <u>Option 1</u> outlined in the Consultation Document – increasing the direct foreign ownership limit to 49 per cent – is therefore an entirely inadequate policy response. Such a negligible change will be unable to produce the multitude of benefits that nearly a decade of studies, reports, government panels and committees predict will result from the removal of FDI restrictions. Such a change would certainly also do almost nothing to "open Canada's doors further to venture capital … giving Canadian firms access to the funds and expertise they need."[65]

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63 William Dymond and Michael Hart, "Canadian Cultural Policy, Ownership Restrictions, and Evolving International Trade Rules", cited in McFetridge, *supra* note 21 at 2.

64 S*upra* note 37 at 12 cited in TPRP Report, *supra* note 14 at 11-17.

65 Speech from the Throne, March 3, 2010 at 7 (http://www.speech.gc.ca/grfx/docs/sft-ddt-2010_e.pdf).

39. Canadians deserve a policy shift that does more than essentially preserve the status quo. Only Option 3 truly levels the playing field for new entrants and opens the possibility for real competition and innovation in Canada's telecommunications sector.

40. Moreover, it is unrealistic and incongruous for Canada to both encourage foreign investment and globalization while maintaining restrictions on FDI domestically.

41. In 2003, the Standing Committee on Industry, Science and Technology recommended that Canadian ownership requirements applicable to telecommunications common carriers be *entirely removed*, including the prohibition against foreign control.[66] This policy decision was made after careful consideration of the two objectives of stimulating competition and innovation in the telecommunications sector while maintaining Canadian sovereignty and security.

42. The then Deputy Ministry of Industry, Peter Harder, in his oral remarks to the 2003 Standing Committee on Industry, Science and Technology on the issue of the telecommunications sector asked:[67] "[W]e have a competitive sector that is weakening and for which investment has fallen dramatically. It is said this sector is much more reliant on external sources of capital than incumbent providers are, which have significant internal revenue sources. Can the restrictions be said to favour the incumbent providers such that they are impairing competition?" In his submission in the same proceedings, the then Commissioner of Competition, Konrad von Finckenstein, on behalf of the Competition Bureau, testified categorically that: "We do not believe that foreign ownership restrictions are necessary to achieve a healthy and vigorous telecommunications industry."[68]

66 2003 Standing Committee Report, *supra* note 19.

67 Testimony of Peter Harder, Deputy Minister of Industry, to the House of Commons Committee on Industry, Science and Technology, January 28, 2003 (http://cmte.parl.gc.ca/Content/HOC/committee/372/inst/evidence/ev657402/instev12-e.htm#Int-388320).

68 Testimony of Konrad von Finckenstein, QC, Commissioner of Competition, Competition Bureau, to the House of Commons Committee on Industry, Science and Technology, February 24, 2003. (http://cmte.parl.gc.ca/Content/HOC/committee/372/inst/evidence/ev732323/instev23-e.htm#Int-437224).

43. Even the incumbent telecommunications common carriers (Bell Canada and TELUS) were in favour of removing the foreign ownership restrictions, affirming that removal of those restrictions would not adversely affect them.[69]

44. In 2006, the Telecommunications Policy Review Panel stated its belief that "Canada should rely primarily on market forces to achieve its telecommunications policy objectives."[70] It suggested replacing the current restrictions with a more "flexible" regime.[71] Several submissions to the Telecommunications Policy Review Panel also advocated elimination of the foreign ownership restrictions, most notably TELUS,[72] the Montreal Economics Institute,[73] the Information Technology Association of Canada,[74] the Canadian Cable Television Association,[75] and the Commissioner of Competition.[76]

45. The 2008 Competition Policy Review Panel entirely supported the findings and recommendations of the 2006 Telecommunications Policy Review Panel.

46. The OECD has also recommended that "Canada should change the foreign ownership and control restrictions as soon as possible in order to rapidly increase productivity, investment, and jobs". The OECD found that the FDI restrictions slow the development of the Canadian telecommunications market.[77]

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69 2003 Standing Committee Report, *supra* note 19 at 17.

70 TPRP Report, *supra* note 14 at 11-13. See also TPRP Report, Recommendation 3-1.

71 TPRP Report *ibid.* at 11-24 ("replace them with a more flexible regime that permits such investment where it benefits Canada and restricts investments that would not benefit Canada").

72 Submission of TELUS Communications Inc. (15 August 2005) (http://www.telecomreview.ca/epic/site/tprp-gecrt.nsf/vwapj/TELUS-Submission.doc/$FILE/TELUS-Submission.doc).

73 English submission of Montreal Economic Institute (August 2005) (http://www.telecomreview.ca/epic/site/tprp-gecrt.nsf/vwapj/Institut_économique_de_Montréal_e.pdf/$FILE/Institut_économique_de_Montréal_e.pdf).

74 Submission of Information Technology Association of Canada (ITAC) (August 2005) (http://www.telecomreview.ca/epic/site/tprp-gecrt.nsf/vwapj/ITAC.pdf/$FILE/ITAC.pdf), referencing "The Impact of Foreign Investment Restrictions" (February 2003) for the ITAC position on foreign investment rules (http://itac.ca/Archive/InformationInfrastructure/ITAC-ImpactofForeignInvestmentRestrictions.htm).

75 Submission of the Canadian Cable Telecommunications Association (CCTA) (15 August 2005) (http://www.telecomreview.ca/epic/site/tprp-gecrt.nsf/vwapj/CCTA.doc/$FILE/CCTA.doc).

76 Submission of the Commissioner of Competition (Sheridan Scott) (15 August 2005) (http://www.telecomreview.ca/epic/site/tprp-gecrt.nsf/vwapj/Competition_Bureau_-_Submission.pdf/$FILE/Competition_Bureau_-_Submission.pdf).

77 OECD Review, *supra* note 3.

47. Some of the foremost Canadian authorities on law and economics argue that foreign ownership restrictions in the telecommunications sector should be eliminated, stating that the restrictions are "fundamentally at odds" with efficiency and low prices.[78] Canadian economic research institutes, think tanks, and former political leaders have also consistently concluded that restriction of foreign business activities impeded Canada's economic development.[79]

48. Since 1995 the Office of the Competition Commissioner has actively supported the lifting of foreign ownership restrictions.[80] During Industry Canada's consultation on a proposed *Framework to Auction Spectrum in the 2 GHz Range including Advanced Wireless Services*, the Competition Commissioner submitted on behalf of the Competition Bureau

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78 E. Iacobucci, M. Trebilcock and R. Winter, "Economic Deregulation of Network Industries: Managing the Transition to Sustainable Competition" (2004) (https://ospace.scholarsportal.info/bitstream/1873/3497/1/244187.pdf).

79 See, *e.g.* Fraser Institute (November 2007), *FraserAlert*, "The Benefits of Foreign Business Activity in Canada" (http://www.fraserinstitute.org/commerce.web/product_files/benefitsforeignbus.pdf); Mike Harris and Preston Manning, "International Leadership by a Canada Strong and Free" (The Fraser Institute and the Institute économique de Montréal, 2007) (http://www.iedm.org/uploaded/pdf/070507_en.pdf); Jack M. Mintz and Andrey Tarasov, "Canada Is Missing Out On Global Capital Market Integration", C.D. Howe Institute E-Brief (21 August 2007) (http://www.cdhowe.org/pdf/ebrief_48.pdf); Neil Quigley and Margaret Sanderson, "Going Mobile — Slowly: How Wireline Telephone Regulation Slows Cellular Network Development" (2005) *C.D. Howe Institute: Commentary* 222 (http://www.cdhowe.org/pdf/commentary_222.pdf); .D. Howe Institute, *Communiqué*, "Pace of technological change in telecommunications a challenge for regulators, says C.D. Howe Institute study" (9 February 1999) (http://www.cdhowe.org/pdf/orr.pdf); the Conference Board of Canada, "4th Annual Innovation Report: Canada needs to attract foreign investment to spur innovation" (Winter 2002-2003) 7(1) Inside Edge 6 (online: http://www.conferenceboard.ca/insidedge/pdf/ie_q1_03.pdf).

80 See, *e.g.*Speaking Notes for Sheridan Scott Commissioner of Competition, "Myths and Realities: Competition in the Telecom and Generic Drug Industries" (29 October 2007), C.D. Howe Institute Toronto, Ontario (http://www.competitionbureau.gc.ca/epic/site/cb-bc.nsf/en/02511e.html); Speaking Notes for Sheridan Scott Commissioner of Competition, "The 2007 Canadian Telecom Summit, Toronto, Ontario" (13 June 2007) (http://www.competitionbureau.gc.ca/epic/site/cb-bc.nsf/en/02361e.html); Speaking Notes for Sheridan Scott Commissioner of Competition, "55th Antitrust Law Spring Meeting Telecommunications: What's Next? Where Will We Be in Five Years?" (18 April 2007) (http://www.competitionbureau.gc.ca/epic/site/cb-bc.nsf/en/02163e.html); *Annual Report of the Commissioner of Competition For the Year Ending March 31, 2006*, Chapter 6: Advocating for Competition and for International Co-ordination, Section 6.1.4 Telecommunications (http://www.competitionbureau.gc.ca/epic/site/cb-bc.nsf/en/02340e.html); Working Group on the Interaction between Trade and Competition Policy, World Trade Organization, WT/WGTCP/W/146**,** 12 September 2000 (00-3518), Communication from Canada (14 June 2000) (http://www.competitionbureau.gc.ca/epic/site/cb-bc.nsf/en/01266e.html); Speaking Notes for George N. Addy, Director of Investigation and Research, The 4th Annual Industry Canadian Resale Congress (27 February 1996) Toronto, Ontario (http://www.competitionbureau.gc.ca/epic/site/cb-bc.nsf/en/00944e.html); Speaking Notes for George N. Addy, Director of Investigation and Research, An appearance before the Standing Senate Committee on Transport and Communications (1 November 1995) (http://www.competitionbureau.gc.ca/epic/site/cb-bc.nsf/en/01034e.html); *Annual Report 1994/95* (http://www.competitionbureau.gc.ca/epic/site/cb-bc.nsf/en/01378e.html);

that "foreign investment restrictions do limit competition ... the Bureau submits that the appropriate way to compensate for any lack of competition attributable to the foreign investment restrictions is to remove them."[81]

49. Finally, the government has stated that it wishes to place increased reliance on market forces in Canada's telecommunications sector, and in fact has stated that the foreign ownership rules set out in the *Telecommunications Act* "act as restrictions on foreign investment which constitutes a barrier to market entry."[82]

VII. Conclusions: Increasing Competition in Canada's Telecom Sector

50. The *Telecommunications Act* embodies several policy goals for Canada. The current FDI restrictions do not support and often directly conflict with many of these policy goals.. Other regulatory regimes exist that can be used to meet Canadian telecommunications policy goals.

51. Certain issues, such as national security and protection of citizen privacy, are not fully addressed[83] and arguably not properly addressed by foreign investment restrictions. Since the tragic events of September 11, 2001, security concerns have been of increased importance for many countries, including the U.S. and U.K. However, these countries have telecommunications FDI rules that are far more liberal than Canada's.

52. Canadian sovereignty is also better regulated by other means than restricting FDI. Other OECD countries have explicit and implicit safeguards in place to ensure that FDI does not prejudice the national public interest[84] and, in Canada, foreign takeovers are subject to review by the Minister of Industry pursuant to the *Investment Canada Act*.

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81 Comments of the Commissioner of Competition (25 May 2007), on the *Consultation on a Framework to Auction Spectrum in the 2 GHz Range including Advanced Wireless Services* (DGTP-002-07) (online at: http://www.ic.gc.ca/epic/site/smt-gst.nsf/vwapj/dgtp-002-07-Competition-Bureau-comments.pdf/$FILE/dgtp-002-07-Competition-Bureau-comments.pdf) at para. 4-43.

82 Industry Canada (November 2007), "Policy Framework for the Auction for Spectrum Licences for Advanced Wireless Services and other Spectrum in the 2 GHz Range" (http://www.ic.gc.ca/epic/site/smt-gst.nsf/vwapj/awspolicy-e.pdf/$FILE/awspolicy-e.pdf) at 3.

83 TPRP Report, *supra* note 14 at 11-23

84 TPRP Report, *ibid.* at 11-24.

53. Accessibility of services in remote and under-served regions is, understandably, a concern. However, even in the absence of foreign investment restrictions, the CRTC would maintain the regulatory jurisdiction to ensure accessible service in those regions. In addition, various levels of government have had and can continue to have special initiatives or programs such as Industry Canada's "Broadband for Rural and Northern Development Pilot Program", to promote service accessibility and availability in remote and under-served areas.

54. Other goals of Canada's telecommunications policy are: the enhancement, at the national and international levels, of the efficiency and competitiveness of Canadian telecommunications; and the stimulation and encouragement of innovation and R&D in Canada. Compelling evidence indicates that these policy goals can be furthered by removing the foreign ownership restrictions in the telecommunications sector. Furthermore, the available research and the experience of other OECD countries demonstrates that liberalizing FDI leads to a higher quality of services, more consumer choice, better availability, and lower costs to the consumers.[85] Removing the foreign ownership restrictions in the telecommunications sector will also make Canada a more attractive destination for foreign investors.[86]

55. Finally, the *Telecommunications Act* explicitly encourages a reliance on market forces as a means of achieving other policy objectives. The importance of reliance on market forces has been re-emphasized in a Policy Direction to the CRTC issued by the Governor in Council on the recommendation of the Minister of Industry in December 2006.[87] The CRTC is thus mandated to rely as much as possible on market forces to regulate telecommunications in Canada. Current FDI restrictions force the CRTC to regulate heavily in order to produce artificial competition in the market. Removal of FDI restrictions would bring an influx of capital and create the conditions necessary to bring true competition to the market. The CRTC would then be able to place greater reliance on market forces as a means of regulating the telecommunications sector.

85 TPRP Report, *ibid.*
86 2003 Standing Committee Report, *supra* note 19 at 34.
87 SOR/2006-355 (http://canadagazette.gc.ca/partII/2006/20061227/html/sor355-e.html).

56. The right choice for Canada is Option 3. Fully removing FDI restrictions will increase the competitiveness and productivity of the Canadian telecommunications sector. It will encourage capital investment, boost innovation and R&D in Canada, increase the availability and quality of services for consumers, and all without causing a loss of "head office" functions in Canada or infringing on Canadian sovereignty and security.

57. We therefore ask that Industry Canada take immediate steps to remove the foreign ownership restrictions contained in the *Telecommunications Act* and *Radiocommunication Regulations* and rescind, in their entirety, the *Canadian Telecommunications Common Carrier Ownership and Control Regulations*.

All of which is respectfully submitted by Verizon Canada Ltd., this 30th day of July, 2010.