



28 May 2001

Aliant Telecom Inc.
Bell Canada
MTS Communications Inc.

Clerk of the Privy Council and
Secretary to the Cabinet
Langevin Block
80 Wellington Street
Ottawa, Ontario
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Bernard A. Courtois
Chief Strategy Officer
Bell Canada

Dear Sir/Madam:

Subject: Canada Gazette - Notice No. DGTP-007-01 (14 April 2001):
Petition to the Governor in Council concerning
Decision CRTC 2000-745: Changes to the contribution regime

These comments are filed on behalf of Aliant Telecom Inc., Bell Canada and MTS (collectively, the Companies) in response to the application (the Application) of Amtelecom Inc., Bruce Municipal Telephone System, Prince Rupert City Telephones and Sogetel (the Petitioners) to the Governor in Council regarding Decision 2000-745 (the Decision).

During the last few years, with regard to the pricing of basic local telephone service, there has been a definite and positive public policy trend to increase reliance on market forces and to decrease reliance on artificial subsidies. This has been accomplished through restructuring residential prices to bring them closer to their underlying costs, while at the same time ensuring that local telephone prices remain affordable for all Canadians through a "contribution" levy on long distance services, paid for by long distance providers.

In the Decision, the Canadian Radio-television and Telecommunications Commission (the Commission) changed the basis upon which money was collected to subsidize local service by spreading the subsidy burden to more telecommunications suppliers and services than just long distance providers and by applying the levy to other specified telecommunications revenues. The pool of revenues that will be collected will form a national subsidy fund from which local service suppliers can draw in order to help pay for service in high-cost serving areas. Telecommunications suppliers include, among others, local and long distance carriers, resellers, satellite and mobile telephone providers.

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This national fund, which is now in effect in most areas of the country, applies to most telecommunications service providers today with some exceptions. In particular, independent telephone companies other than Télébec and TELUS Québec will continue to be subsidized from long distance services during 2001. In other words, no independent telephone company other than Télébec and TELUS Québec will contribute to, nor draw from, the national fund until 1 January 2002. This means that the Petitioners are already in an advantageous position in that they are not required to pay into the fund until next year. Furthermore, when the independent telephone companies, including the Petitioners, begin to contribute to the national fund next year, they will do so at a much lower rate than if they were contributing today. In 2002, the levy is expected to drop from the current 4.5% to approximately 1.5%.

In addition, the Commission, for purely administrative reasons, introduced an exemption for smaller telecommunications suppliers. The Commission established that a \$10 million revenue threshold must be met before these companies would be required to pay into the national fund. This rule is referred to in this submission as the "*de minimis rule*".

Consequently many independent companies, including the Petitioners, may be exempt from the requirement to pay contribution into the national fund by virtue of this rule. However, while they will not have to pay into the fund, they will still be able to collect from the fund.

The Petitioners are asking Cabinet to broaden the *de minimis rule* exemption by:

- changing the revenue threshold for exemption from the requirement to pay contribution to \$10 million of contribution-eligible revenues rather than \$10 million of Canadian Telecommunications Services Revenues (CTSR). This proposal would result in a more generous exemption since CTSR represents gross revenues from Canadian telecommunications services whereas contribution-eligible revenues reflect deductions from CTSR, such as inter-carrier payments and revenues from retail paging, retail Internet services and terminal equipment;
- implementing a basic exemption for those telecommunications service providers with \$10 million or more in contribution-eligible revenues; and
- introducing a graduated levy so that companies with smaller contribution-eligible revenues would pay a smaller percentage than would companies with larger contribution-eligible revenues.

It is the view of the respondent companies that this petition to Cabinet should be rejected in its entirety for the following reasons:

- fairness and equity, i.e., because it would have the effect of lessening - or eliminating - the obligation to support service in high-cost areas for some telecommunications suppliers and their customers and increasing it for others;
- due process – the Petitioners had the opportunity to present their views during the Commission's Review of the Contribution Collection Mechanism proceeding and did not do so;

- CTSR is the appropriate contribution revenue threshold;
- claims of "rate shock" are unfounded; and
- the "Ability to pay" principle is faulty - the Petitioners are apparently attempting to draw an unjustified parallel between income tax and contribution payments.

For the preceding reasons, the Companies respectfully request that the Governor in Council reject all requests made by the Petitioners.

Yours truly,

A handwritten signature in black ink, appearing to read "Bernard A. Courtois". The signature is fluid and cursive, with a prominent initial 'B' and 'C'.

Bernard A. Courtois
Chief Strategy Officer
Bell Canada

Attachment

c.c.: The Honourable Brian Tobin, Ministry of Industry
Ms. Ursula Menke, Secretary General, CRTC
Mr. Michael Helm, Director General,
Telecommunications Policy Branch, Industry Canada
CRTC Regional Offices
The Companies

Canada Gazette Notice No. DGTP-007-01

The Petition to Her Excellency
The Governor in Council

Concerning

Decision CRTC 2000-745

Changes to the Contribution Regime

Comments of

Aliant Telecom Inc,
Bell Canada
and
MTS

28 May 2001

Introduction

1. Trends in public policy have been to reduce subsidies in the telecommunications industry. It has been generally recognized that subsidies have distorted pricing, have been generally harmful, and have been more than required to maintain the overall societal objective of making affordable basic telecommunications service available to all Canadians. The move to subsidy reduction has been accomplished through restructuring residential prices to bring them closer to their underlying costs.

2. Prior to the Decision, contribution was recovered from long distance services. Through the Decision, the Commission spread the subsidy burden to more telecommunications services and suppliers, thus reducing the burden on long distance. The Commission has rejected requests, in the Decision and in subsequent appeals, to treat some services or providers, e.g., wireless, more favourably than others.

3. The arguments presented by the Petitioners are contrary to all of these policies, which were instituted in the public interest to provide economic and competitive benefit/equality. It is unfair to other service providers and their customers, running counter to the Decision's principle that all service providers across Canada should equally support service in high-cost areas.

4. The Decision established a national fund to provide subsidies to defray the costs of primary exchange residential service in high-cost serving areas. The national fund is financed through a levy based on a percentage of eligible revenues of telecommunications service providers (TSPs). While the fund is operational in much of Canada in 2001, independent telephone companies - other than Télébec and TELUS Québec - will neither contribute to, nor draw from, the fund until 1 January 2002, at which time the percentage charge is estimated by the Commission to drop to approximately 1.5% from the current 4.5%.

5. For purely administrative reasons, the Decision introduced an exemption to this general principle in exempting TSPs below a \$10 million threshold in CTSR from the requirement to pay into the national fund. This rule is referred to in this submission as the "*de minimis rule*". Unless exempted by the *de minimis rule*, all TSPs are required to pay the same percent of revenue. Using CTSR as the threshold measure results in the administrative burden associated

with the mechanism being borne by larger service providers. Many independent companies will be exempt from the requirement to pay contribution into the national fund by virtue of this rule. However, and equally as important, this will not affect the ability of an independent company to draw from the national fund.

6. The Petitioners propose major changes to the application of the contribution levy on percent of revenue. These changes would have the effect of significantly broadening the exemption allowed for in the Decision. Specifically, the petitioners propose that the exemption be broadened by:

- i) changing the revenue threshold for exemption from the requirement to pay contribution to \$10 million of contribution-eligible revenues rather than \$10 million of CTSR;
- ii) implementing a basic exemption for those TSPs with \$10 million or more in contribution-eligible revenues; and
- iii) introducing a graduated levy so that TSPs with smaller contribution-eligible revenues would pay a smaller revenue percentage than would TSPs with larger contribution-eligible revenues.

7. The Application would refer back to the Commission the matter of the amount of the basic exemption referred to in ii) and the structure of the graduated contribution charge referred to in iii), including the number of revenue brackets to which the graduated charge would apply.

A Question of Fairness

8. It is the Companies' respectful submission that the Petitioners' request to broaden the exemption should be denied because it would be fundamentally unfair, undermining the intent of the Decision, by lessening, or eliminating, the obligation to support service in high-cost areas for some service providers and their customers, while increasing it for others.

9. The Companies also submit that the Petitioners' request for preferential treatment through lower contribution payments should be rejected for a number of other reasons:

- First, it would be contrary to the principle that all service providers should support the provision of local residential service in high-cost serving areas on an equal basis.
- Second, the Petitioners' claims that the provisions in the Decision will undermine affordability objectives and will discourage investment in broadband services are unjustified.
- Third, the Petitioners' justification for preferential treatment based on an "ability to pay" is questionable. Even if one were to accept that "ability to pay" is a relevant issue in this regard, which it is not, the Petitioners' requested changes, based as they are solely on revenue, are not capable of incorporating this consideration. In any case, many of the smaller companies are subject to less competition and are protected by rate of return regulation, and will continue to draw subsidies during 2001, without having to pay into the national fund until 1 January 2002.
- Fourth, even if an independent company is not exempt by the *de minimis rule* from paying contribution, it is likely that most independent companies would receive more from the fund than they would be obliged to pay into the fund. Any assessment of the impact of the new contribution regime on independent companies must take into account the net impact, not simply the requirement to pay into the fund. The Application does not discuss implications of the fact that independent companies will draw from the national fund.
- Fifth, the Petitioners present the fact that the independent companies provide local telephone service in rural and remote areas of Canada as justification, in part, for their proposals. The independent companies are not alone in this respect. Bell Canada and other incumbent local exchange carriers (ILECs) provide local telephone service to hundreds of rural and remote exchanges. For example, Bell Canada provides local telephone service to approximately 630 rural and remote exchanges that the Commission

has designated as high-cost areas. Some of these exchanges, as well as some non high-cost exchanges, are adjacent to independent companies and serve customers in similar circumstances as customers of independent companies. Bell Canada, other ILECs, and other TSPs, such as long distance service providers and wireless service providers, must pay contribution on the revenues from their customers in these areas, just as they pay contribution on the revenues from their customers in other areas.

10. The Commission has already approved price increases for capped residence local services for Bell Canada customers to assist in recovering some of the Company's contribution obligations under the new contribution regime. These price increases affect, among others, customer in exchanges that are adjacent to those of independent companies. In other words, Bell Canada customers in locales similar to those of independent companies are already paying additional amounts in support of the new contribution regime.

Petitioners had the opportunity to present their views during the CRTC's Review of the Contribution Collection Mechanism proceeding

11. The proceeding leading to Decision 2000-745 was a major undertaking. The schedule of submissions covered the period from November 1999 through July 2000 and provided several opportunities for parties to present their views, including an initial submission, responses to two rounds of interrogatories, and Final and Reply Comments. The list of interested parties was extensive. All four of the Petitioners participated in the proceeding, either directly, as in the case of CityTel, or indirectly through their independent company associations,¹ as in the case of the other three Petitioners. The Petitioners took an active role in the proceeding. Specifically, all filed responses to the two rounds of interrogatories, CAPTS and SATAT filed Final Comments, and CAPTS, OTA and SATAT filed Reply Comments.

12. In the proceeding, the Petitioners supported the percent of revenue recovery mechanism and the national fund, both of which were adopted in the Commission's Decision.

¹ Ontario Telecommunications Association (OTA), Société d'administration des tarifs d'accès des télécommunications (SATAT) and the Canadian Alliance of Public Telephone Systems (CAPTS).

13. When asked specifically, through Commission interrogatories, whether there should be a minimum reporting level, the Petitioners, represented by their associations, stated that there should be no minimum reporting level, and that all eligible service providers should report. CityTel stated that eligible service providers with revenues in excess of \$1 million should be required to report.² The Decision establishes the *de minimis rule* at a level higher than proposed by the Petitioners. Nonetheless, the Petitioners are now working to broaden the *de minimis rule* even further.

14. In addition, in spite of the many opportunities to do so, the Petitioners did not raise the issue of a basic exemption or the issue of a graduated levy in the course of the proceeding.

15. In view of the foregoing, it is the Companies' submission that the Petitioners are using the appeal process to secure additional and unwarranted benefits by shifting the burden of subsidy and diminishing the effect of the central principle of the Decision, i.e., that all service providers support services in high-cost areas equally. Use of the appeal process for such frivolous purposes should be discouraged through an immediate denial of the Application.

CTSR is an appropriate measure for the *de minimis* threshold

16. The *de minimis rule* strikes a balance between the principle that all TSPs should pay contribution and administrative considerations. TSPs that are required to pay contribution must report eligible revenues to the Central Funds Administrator (CFA) on a monthly basis. Calculation of monthly eligible revenues must conform to the reporting procedures approved by the Commission and involves the following:

- obtaining total revenues;
- identifying the need for, and, if needed, calculating adjustments to, total revenues in accordance with the established reporting procedures; and
- calculating deductions from total revenues, including:

² Responses to CAPTS(CRTC)14Jan00-301, OTA(CRTC)14Jan00-301, SATAT/CAPTS(CRTC)14Jan00-307, CityTel(CRTC)14Jan00-301. CAPTS, OTA and SATAT proposed that a wide range of service providers would be eligible, including local, long distance, and international service providers, as well as wireless service providers. CityTel proposed that only long distance service providers would be eligible.

- revenues from services provided outside Canada,
- revenues from Canadian non-telecommunications services,
- inter-carrier payments,
- revenues associated with terminals, retail paging services and retail Internet services, and
- revenues associated with ineligible services from bundles that include eligible and ineligible services.

17. TSPs must also transact financial transfers with the CFA on a monthly basis electronically. This often involves a special arrangement with the TSP's financial institution. Both the reporting of eligible revenues and the financial transfers must be carried out according to the CFA's strict schedule.

18. Though not a tremendously onerous task, the Commission decided that it would not be necessary to ask a smaller TSP to follow these steps. Revenue is a reasonable and non-subjective measure of "size" for these purposes. Therefore, establishing the threshold in terms of CTSR reflects the objective of easing the administrative burden on small TSPs.

19. As noted above, the \$10 million threshold level established in the Decision is much higher than the Petitioners suggested in the proceeding leading to the Decision. It is interesting to note that the *de minimis* rule exemption for the FCC's Universal Service Program in the U.S. is \$10,000 in contribution payments per year.³ This is equivalent to a threshold based on contribution-eligible revenues of less than \$0.7 million per year at a levy of 1.5%. The equivalent threshold for the U.S. program, when expressed in terms of contribution-eligible revenue, is therefore more than an order of magnitude less than the \$10 million requested in the application.⁴ It is also interesting to note that the Universal Service Program in the U.S. does not include any other preferential treatment for smaller service providers. For example, it does not include a basic exemption or a graduated levy.

³ Telecommunications Reporting Worksheet, FCC Form 499-A: Instructions for Completing the Worksheet for Filing Contributions to Telecommunications Replay Service, Universal Service, Number Administration and Local Number Portability Support Mechanisms, page 5.

⁴ A threshold of, say, \$1 million in contribution-eligible revenue would mean that a TSP would be required to pay \$15 thousand when reaching the threshold at the 1.5% levy.

20. Moreover, the only way to eliminate the aspects of the transition that the Petitioners dislike, while retaining equal treatment among all TSPs, is to eliminate the threshold altogether.

"Rate Shock" claims are unfounded

21. The Petitioners argue that price increases to customers to recover the levy could significantly alter customers' ability to pay for services and could alter their purchase patterns.⁵ It is worth noting that monthly rates for residence single-line primary exchange service in the territories of independent companies are in the \$20 to \$25 range. Increasing these rates to recover the 1.5% amount implies rate increases of approximately thirty cents per month. Petitioners' claims that having to pay contribution would result in "rate shock"⁶ are, in the Companies' view, totally unjustified. While the Companies understand the principles of the *Telecommunications Act* regarding affordability of service and the sensitivity of the affordability issue, the Companies respectfully submit that price increases of 1.5% would not affect the affordability of services, nor would they alter customers' purchasing patterns of telecom services in general. Further, if this were a valid concern, then it would be a concern nationally, not just in the cases of small independent companies. To give credence to this point is to call into question the percent of revenue mechanism generally, not just the narrow issue of transition on which the petition focuses.

"Ability to pay" principle is faulty

22. The Petitioners' request that a graduated contribution levy be introduced and note that a graduated levy is based on the "ability to pay" principle.⁷ The petitioners are apparently attempting to draw a parallel between the contribution levy and income tax. This analogy is faulty in many respects:

- First, the principle underlying the contribution regime established in the Decision is that all TSPs and their customers should support the provision of primary exchange

⁵ The Application, page 28.

⁶ The Application, page 19.

⁷ The Application, page 32.

residential service in high-cost serving areas. It is, of course, customers who support other customers. The issue of a TSP's "ability to pay" is not germane.

- Second, even if one were to accept that "ability to pay" is a relevant issue in this regard, the Petitioners' requested changes, based as they are solely on revenue, are not capable of incorporating this consideration. The Companies note that independent companies differ from other TSPs in that they are not subject to direct competition and are protected from financial loss due to rate of return regulation.

- Third, the percent of revenue contribution mechanism is more like a sales tax than an income tax. The GST and PSTs are applied independent of the magnitude of individual purchases or the purchasing individual's financial status. The revenues associated with the GST and PSTs are used, among other things, to distribute amounts to recipients of social programs. In this way, the percent of revenue contribution mechanism

established in the Decision is similar to the workings of sales taxes: all TSPs pay into the fund on the same basis, and differences in need are reflected in the distributions from the fund.

The incentives and outcomes arising from *de minimis rule*, as illustrated in the Petitioner's hypothetical examples, are misrepresented

23. The Application notes that if a TSP moves from ineligible status to eligible status through an increase in CTSR, the TSP must pay contribution at the prevailing percent of revenue. Accordingly, in such situations a TSP may pay no contribution in one year and then be required to pay contribution the next year. The Petitioners argue that this new cost deters investment in broadband infrastructure and could undermine universal service.

24. The Petitioners' attempt to link affordability and broadband investment to the transitional aspects of the new contribution regime is highly misleading. All TSPs that are required to pay contribution, not just those that make the transition through the *de minimis rule*, must address how to recover the contribution obligation. Making the transition to eligible status simply puts a TSP on the same level as all other eligible TSPs. The only difference between the TSPs discussed in the transition examples cited in the Application and TSPs that are eligible from the outset of the new regime, is that the former make the transition by crossing the eligibility threshold while the latter do so through the establishment of the new mechanism.

25. Issues of affordability and network investment are, therefore, issues that are fundamental to the move to the percent of revenue mechanism, not to the transitional aspects of the *de minimis rule*. Any decision to change the contribution mechanism - due to potential impacts on affordability and broadband investment - could not be restricted solely to independent companies or companies that might be affected by a transition to eligible status through the *de minimis rule*.

26. The incentives arising from the *de minimis rule* are addressed in the Application by means of hypothetical examples based on the prevailing interim levy of 4.5%. The use of the 4.5% figure greatly overstates the results since the percent of revenue contribution regime will not apply to independent companies until 2002, when the contribution percent of revenue is

expected to be approximately two thirds lower, i.e., about 1.5%. In one case, using the 1.5% of revenue actually reverses the Application's conclusions. Specifically, the Application includes an example in which the hypothetical independent company, RemoteTel, decides not to introduce Internet service due to the fact that the additional revenues would result in RemoteTel exceeding the \$10 million CTSR threshold and that the contribution payments would exceed profits associated with the new service in the first year, by an amount of \$24 thousand. When using the contribution rate of 1.5%, RemoteTel is better off in introducing the Internet service in the first year, by \$192 thousand.

27. More generally, the conclusions the Petitioners draw based on the incentives depicted in their hypothetical examples, e.g., RemoteTel, are, at best, far-fetched. For example, business plans for new products and services are not based solely on the financial performance in the first year.

28. Effects, such as those cited in the hypothetical examples, would occur under any administrative threshold, no matter how defined, not only under the use of CTSR. In particular, hypothetical examples illustrating similar results could easily be constructed based on the \$10 million contribution-eligible revenue threshold requested in the Application.

Conclusion

29. In conclusion, based on the preceding, it is the Companies respectful submission that the Petitioners' Application should be denied for a number of reasons:

- First, it would be contrary to the principle that all service providers should support the provision of local residential service in high-cost serving areas on an equal basis.
- Second, the Petitioners' claims that the provisions in the Decision will undermine affordability objectives and will discourage investment in broadband services are vastly overstated and without evidence.

- Third, the Petitioners' justification for preferential treatment based on an "ability to pay" is questionable. Even if one were to accept that "ability to pay" is a relevant issue in this regard, which it is not, the Petitioners' requested changes, based as they are solely on revenue, are not capable of incorporating this consideration. In any case, many of the smaller companies are subject to less competition and protected by rate of return regulation, and will draw revenues from the national fund.

30. Therefore, the Companies respectfully request that the Governor in Council reject all requests made by the Petitioners.

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