Waiting for the Dream: The Consumer Case for Telecom Reform and Results-Based Regulation

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Executive Summary

This report traces the governance and regulation of the retail consumer services of telecommunications industry in Canada, from the inception of the regulation of telephone service by the federal government in the nineteenth century, to current conditions prevailing in telecommunication services markets where competition is supposed to provide the necessary market discipline. As a result of the experience with the various forms of regulation and governance to date, the report notes difficulties that have been experienced in making the chosen regulatory framework work for consumers. Finally, the report makes recommendations for regulatory reforms that are designed to help improve the position of retail residential customers, and level the playing field with existing suppliers and their high volume customers.

Industry governance since the development of telephone networks has been profoundly influenced by the strategic action of stakeholders, in particular the major incumbent local exchange companies, (ILECs), the largest of which was the Bell Telephone Company of Canada, or later, Bell Canada. This action included lobbying with politicians and successful persuasion of the regulator concerning the recovery of revenues from customers and the exclusion of competitors from essential facilities.

For most of the last century, local service telephony was delivered by monopoly carriers who were regulated by the federal or provincial regulators in cost of service regulation. The regulated companies were able to recover all the costs of prudently incurred expenditures, and a reasonable rate of return on their used and useful capital investments. Bell Canada and other ILECs were able to prevent meaningful competition from independent telephone companies (telcos) through limiting access to long distance facilities, strategic changes to the cost structure of telephony services, and a predisposition on the part of the regulator to favour their operations as natural monopolies requiring end-to-end system integrity. The scrutiny of the regulator, initially the Board of Railway Commissioners, and later the Canadian Transport Committee, was largely accepting of the applications of Bell Canada and BCTel for approval of capital and operating expenditures as prudent and the design of rates as a result. A comparison of rate increases between federally-regulated Bell Canada and BC Tel on the one hand and the western telcos, MTS, SaskTel and AGT owned by provincial governments during the time period 1950 to 1977 shows patterns of rate increases for the provincial telcos ranging from 25% to 65% of the federally-regulated telcos.

The Canadian Radio-Television and Telecommunications Commission (CRTC), which became the regulator of telecommunications services in 1976, provided more scrutiny of the costs of ILEC operations, and began to classify and rationalize their expenses in accordance with cost causality rather than business plans. The resultant exercise attributed access costs to local service resulting in the appearance of a large subsidy flowing from long distance to local service. This

paper subsidy would fuel demands for rate reform by high volume users of long distance service by corporate users.

At the same time, economic theorists were attacking the basis for monopoly regulation of utilities and arguing that competition could provide a more efficient result. These theories found resonance both with conservative political leaders and with large business telecommunications customers in developed countries who wished to lower the cost of services, such as long distance, through the enabling of competition, and the lowering of the contribution required from such services to maintain affordability and accessibility of local service.

At the same time, the CRTC's jurisdiction over provincially incorporated or owned telecommunications companies was established by the Supreme Court of Canada. This enabled a unified plan of industry restructuring to take place directed by the CRTC in accordance with the *Telecommunications Act.*

After a series of unsuccessful applications in the 1980s to start long distance competition, and the successful establishment of competition in terminal equipment and private lines, upon application of Unitel and BCRL, the CRTC finally acceded in its Decision 92-12. Competition would be allowed, and the principle of interconnection and equal access to local networks by new entrant competitors was established.

Subsequent decisions, and the *Telecommunications Act* passed in 1993, established a basis for the separation of ILEC operations and facilities into competitive and utility segments, rebalancing local rates to lower contribution to local service made by ILEC and new entrant toll service, and the setting of ILEC rates in a price cap regime. These decisions meant that local rates increased from the rebalancing efforts necessitated by the introduction of competition, increased depreciation expenses and compensation for stranded assets and the costs of facilitating local interconnection including measures such as local number portability. As well, the market was slow to accommodate low volume long distance users into a regime of toll discounts. The new *Act* also required deregulation of a service when competition was sufficient to protect the interests of users.

Some ten years after the onset of competition in long distance, most residential consumers were paying higher rates for local service that were not offset by discounts to their toll service use. And while the rate of increase for telephone services as a whole was less than the increase to the Statistics Canada index for consumer prices for the period, the results seemed unimpressive given that the industry had experienced an increase in productivity arising primarily from digitization of the networks that was some five times the national average.

By the early years of this century, local service competition had not developed in any significant fashion particularly in the residential market. The CRTC tried measures to provide incentives to new entrant competition that including refusing to make mandated price cap discounts to local rates, and increasing the price floors for ILEC competitive services. This galvanized the ILECs to political action: first securing a government-appointed panel to review the telecommunications regulatory framework, and later using the results to force changes in CRTC regulatory practices. The panel, the Telecommunications Policy Review Panel, in its 2006 Report (TPR Report) recommended a limitation on the CRTC achievement of social objectives by economic means and an increased emphasis on market forces so that all regulation had to be thoroughly justified as the only viable choice to achieve telecommunications objectives.

The major ILECs, Bell Canada and TELUS, continued to press for change, prodding then Industry Minister Maxime Bernier to issue a Policy Direction to the CRTC in December of 2006 incorporating many of the regulatory principles put forward in the TPR Panel report. The Policy Direction instructed the CRTC to use market forces to the maximum extent possible and to implement regulation that was minimally intrusive. Minister Bernier also overturned the CRTC Decision to regulate ILEC VoIP services and lowered the bar set by the CRTC Decision for deregulation of local service exchanges. In the result, most urban local exchanges are now deregulated - this includes 77% of residential telephone lines and 68% of business lines as of June 2010.

However, the consumer benefits promised by the major ILEC and the government concurrent with the making of the Policy Direction and its implementation in decisions intervening in local service deregulation have not arrived. The CRTC had already been using questionably low thresholds for competition in exercising forbearance. The government-imposed forbearance rules did little to improve the results. Local telephone exchange rates have not been reduced, and local exchange bundles do not seem to show any impact from the competition that was supposed to come about. Deregulation of basic service in broadcast distribution undertakings (cable and satellite) allowed by the CRTC upon the appearance of very minimal competition has encouraged almost a doubling of those rates and backstopped the Broadcast Distribution Undertaking broadcasting distribution undertaking or BDU-owned channel offerings. International comparisons of broadband and wireless offerings show at best mediocre performance by Canadian providers to the price and choice detriment of Canadian customers.

This report concludes that the failure of the regulatory reform of the last two decades to deliver the goods for ordinary residential consumers is not one that has its roots in theory, but in practice. Here, the interests of powerful stakeholders have affected the service landscape. In the same way that incumbent players used their political and economic influence and regulatory capture to get their way in the monopoly era of regulation, the winners have used the market-based system to their advantage. Neither regulation nor deregulation will engineer a thriving

telecommunications industry producing innovative and efficient products and services with resultant economic growth for Canada if the decision-making processes for each are skewed by conditions and assumptions that favour some stakeholders over others.

Most importantly, the governance and regulation of the telecommunications industry in Canada must respond to results. For the most part, the restructuring of telecommunications has been guided by untested economic theories, largely provided by experts engaged by the largest stakeholders. The relatively poor performance of telecommunications service for ordinary consumers should have long ago engendered a review of the regulatory framework and market structure that is producing the same. In the last five years, the only acknowledged measure of success has been how fast telecommunications services have been deregulated with predictable market results.

The solution is not a return to old regulation but new models. First of all, there are a variety of consumer issues associated with basic rights for information, quality of service, security of service, disconnections, and privacy for example that should be met by all carriers whether they are incumbent or not. Basic service, obligations to serve, complaints resolution, and burdens of service in uneconomic areas have to be in place for all across the board. The best way to ensure that this occurs is via mandatory licensing for all carriers, with appropriate codes of conduct and enforcement with meaningful force in the form of administrative monetary penalties. The *Telecommunications Act* should be amended to reflect these improvements.

Interconnection with essential telecommunications facilities should be available for competitors at rates that are fair to users and suppliers. We cannot let abstruse theories supposing innovation and duplication in the absence of access to govern this important issue.

The CRTC has never examined whether the interests of users remain protected by competition in forborne markets where the evidence indicates otherwise (see for example BDUs and Internet). While incumbent providers are continually advocating for change where the results are not favourable to their interests, consumers have had no such opportunity.

The Policy Direction is an impediment to achieving fair, balanced, results-based regulation and should be rescinded. The sections of the TPR Report recommending the primacy of market forces are, at least in practice, problematic for fixing real market consumer problems. As well, there should be no winnowing down of the objectives in the *Telecommunications Act*, rather a clarification of their importance in relation to the specific powers of the CRTC.

Public participation in telecommunications policy making requires more structural support by the regulator and the government. In broadcasting, there is a critical need to level the playing field

for non-commercial public and consumer interests by resourcing representation at broadcasting hearings in a similar way to the practice in telecommunications.

While the report is in favour of efforts at liberalization of foreign ownership telecommunications rules for new entrants or small market players, it also warns that it is no solution to all consumer problems, particularly those associated with quality of service. As well, current merger rules should be tightened to prevent any competitive benefits from flowing away from Canadian consumers.

Finally, this report endorses the TPR Report recommendations for improving the research and professionalism of the CRTC. It also notes the importance of the adjudicative function of the CRTC and recommends the use of traditional procedural rules such as cross-examination where the facts and issues at stake warrant.

Summary of Recommendations

Recommendation One

The regulator and policy makers must formally review and use the results of their decisions to maintain, improve or eliminate those provisions that have not worked. Real market results are to preferred to untested theory.

Recommendation Two

The Policy Direction of December 2006 should be rescinded.

Recommendation Three

Forbearance decisions should be reviewed where market results indicate market power. Those same results should inform any review process.

Recommendation Four

All providers of telecommunications services should be required to be licensed by the CRTC. The CRTC should develop rules and codes of conduct particularly in relation to consumer protection and anti-competitive issues. The CRTC should be invested with powers to assess Administrative Monetary Penalties in line with those available under the *Competition Act*.

Recommendation Five

The obligation to serve should be extended to all classes of local service providers. Basic services should be extended to include broadband provided in accordance with comparable standards.

Recommendation Six

The Commissioner for Complaints for Telecommunications Services (CCTS) must be renewed and expanded to include membership by all telephone service providers (TSPs) and be given expanded powers to deal with telecom and broadcasting services that are currently excluded . CCTS reporting on systemic problems should not be subject to voting thresholds that allocate industry members of the CCTS Board a veto.

Recommendation Seven

Relief from current telecommunications ownership provisions should be considered only for new entrants and small existing carriers. The Merger Efficiency Defense must be clarified so that a consumer surplus standard should be applicable in mergers. The ability of the merging

parties to offset shareholder gains against consumer price increases arising from a substantial lessening of competition should not be permitted.

Recommendation Eight

Where the issues and circumstances warrant, oral proceedings under the *Telecommunications Act* should be conducted by the CRTC with traditional procedural safeguards for participants.

Recommendation Nine

There is a need for funding research by public interest non-commercial stakeholders in broadcasting and telecommunications, and participation in broadcasting proceedings by such stakeholders. The Government should act immediately to ensure that consumers have the resources to have an informed and respected voice in the governance of these industries.

Introduction

The past two decades have seen vast changes, not only in the way Canadian and worldwide telecommunications are regulated, but in also in the methods of delivery of traditional telecommunications products and services as well as those associated with modern information technology. The central objective of the regulatory trends in this time period has been to introduce market forces, wherever possible, to challenge or eliminate the delivery of telecommunications in a monopoly regime, whether the provider is privately or state-owned.

Yet, strangely, the seeming targets of and potential losers from regulatory reform in Canada are the monopoly incumbents delivering telecommunications services in the 1980s (or their direct descendants in corporate lineage) who seem to be largely flourishing in the new environment. On the other hand, notwithstanding the fervor that deregulation has been pursued as a policy objective, the markets for retail services provided to customers have displayed, for the most part, what could be described as rather uneven levels of competitive behaviour associated with price, quality, delivery and billing. Internationally, Canadians appear to be accessing retail telecommunications services that, on the whole, fail to be world leaders in the most important categories of consumer importance. The exception is, of course, the wireline telephony service, whose regulation as a monopoly service was the source of the zeal for reform decades ago. Here, we still appear to be world leaders in price[1] and service, despite having tinkered with local telephone service for the better part of the last two decades to cater to the reduction of contribution towards local networks from high volume users of other telecommunications services.

It is unsettling that the indifferent results of restructuring have produced even more calls for a laissez faire approach to this industry now generating over $41 billion dollars in revenue annually,[2] and hailed as a touchstone for future economic growth and social cohesion. Incumbent industry stakeholders have secured not only an escape from most regulatory scrutiny, but a government policy directive to the regulator to, in effect, try everything short of regulating. As a consequence, incumbent industry stakeholders have become aggressive and reactive in protecting market share while trying to shed public obligations. This includes preventing access to their advanced networks in the same way that access was obtained by new long distance entrants to telephone networks near the start of the restructuring process. Modest efforts to deal with consumer dissatisfaction with retail service, such as the establishment of a complaints

[1] Wall Communications Inc., "Price Comparisons of Wireline, Wireless and Internet Services in Canada and with Foreign Jurisdictions" April 16, 2010, prepared for the Canadian Radio-Television and Telecommunications Commission, p. 9.

[2] CRTC Communications Monitoring Report 2010 at <http://www.crtc.gc.ca/eng/publications/reports/PolicyMonitoring/2010/cmr.htm>.

resolution commissioner have been attacked as unnecessary by some industry players intent on insulating their customer service practices from independent appraisal outside their norms of their business plan. The public perception, particularly in the key wireless segment of the industry, is that there is now a dearth of both real competition and consumer protection.

The Telecommunications Policy Review Panel Report (TPR Report), of nearly five years vintage, and the Cabinet Policy Direction of December 2006 derived from its recommendations have been the principal foundation for much discussion of potential legislative reform. The TPR Report is a valuable resource as a holistic examination of telecommunications issues across the board, dealing with economic, technical, and social considerations. However, its key policy fixes to achieve shared public goals miss the mark by the near exclusive adoption of a simplistic faith-based approach that tends to favour the interests of incumbent players. It is an important report, but it cannot be a basis for reform that both responds to market reality, and reflects a reasonable balance between suppliers and users.

This study reviews the key consumer concerns in the current telecommunications environment and attempts to address the perceived failings of the regulatory regime and the retail telecommunications markets. However, to do so without an understanding of how we got to where we are now would fail to provide an important perspective on the drivers of various developments in the regulation and deregulation of the telecom industry.

A Brief History of Telecom Regulation

One of the persistent themes associated with the restructuring of the telephone and telecommunications industry in general, has been the desire to escape historical patterns of regulation that have been castigated by many industry stakeholders as inefficient, unnecessary and failing to provide sufficient incentive for innovation and technological developments. The deregulation of most of the retail telecommunications services and the reliance upon market forces for their operation in the public interest that commenced in the last two decades of the twentieth century are cited as key game changing developments that transformed the industry, and ushered in an era where the "customer is king". But while the changes in regulation look transformative, they should be viewed in the context of symmetry with historical patterns of telecommunications governance in Canada and the actions of the principal players. The way things changed had everything to do with what went on before the blossoming of deregulatory fervor.

In fact, from a winners and losers standpoint, the history of the restructured telecommunications industry to date is being written in much the same way that the one hundred or so years previous to the restructuring unfolded. The key incumbent industry stakeholders appear to once again have become the principal beneficiaries and consumers are receiving a more subdued set of benefits along with some additional burdens. Accordingly, a brief review of the establishment of the telephone industry in Canada, and the accompanying development of telecommunications regulation in the public interest may be instructive.

The Bell Telephone Company received its charter by a special act of Parliament in 1880. The charter authorized the company to conduct telephone operations in all regions of Canada. By 1882, the Bell Telephone Company, now in the hands of American ownership,[3] had been successful in squeezing out, or taking over, its major real or potential competitors in the core areas of its operations. However, the growing importance of telephony in Canadian life and the increasing dissatisfaction of consumers with levels of service, particularly in semi-urban and rural areas, gave rise to an interest in both the independent and public provision of telephony. These popular views led to the formation of independent telephone companies, some backed by municipal and provincial governments.

Bell corporate actions were reactive to these developments, as well as policy emanating from the Canadian federal government. Following the disallowance by the Patents Commissioner of

[3] Company capitalization practices detailed later increased Canadian ownership, particularly after WW II. By 1956, when AT&T and the Bell System divested its shares pursuant to a consent decree in an anti-trust action, AT&T had 39% ownership stake.

several key Bell patents in the 1880s, Bell embarked upon a strategy to consolidate its monopoly in Central Canada. In Nova Scotia, Prince Edward Island, and New Brunswick, Bell Canada sold off its facilities (keeping an equity stake in the New Brunswick operating company). In 1911, the Maritime Telegraph and Telephone Company purchased the Nova Scotia Telephone Company that had purchased the provincial Bell assets in the previous century.

However, the early devolution of Bell's interests in the Atlantic Provinces did not foreclose involvement in the twentieth century. In 1962, Bell acquired shares of the Avalon Telephone Company of Newfoundland, later changing its name to the Newfoundland Telephone Company (NewTel) in 1970.[4] In 1999, Aliant Inc., was formed from the merger of Maritime Telephone and Telegraph Company (MT&T), Island Telecom, Bruncor (parent of NBTel), and NewTel Enterprises (parent of NewTel Communications), then the four main incumbent telephone companies in Nova Scotia, Prince Edward Island, New Brunswick and Newfoundland and Labrador respectively. Following the merger, Bell Canada owned 53% of the Aliant Inc. shares. In 2006, a new income trust structure was created: Bell Aliant Regional Communications (Bell Aliant). Bell Aliant received most of Bell Canada's landlines outside of urban centres while Bell Canada absorbed Aliant's high growth wireless and retail business while retaining a 45% share in the new income trust structure that had been created. In June 2010, the income trust was converted to a traditional corporate structure.

Similarly in British Columbia, Bell relinquished its operations to a local company in 1889. Unlike its reemergence in Atlantic Canada, Bell did not attempt to return to the provision of local telephone service in British Columbia. However, Bell's actions elsewhere showed a determination to protect its monopoly and to wipe out its competitors.

In Quebec, in the period of 1885 to 1913, Bell swallowed four rivals after diminishing their viability through a variety of means including drastic margin squeezing and denial of access to rivals for long distance connections. These tactics proved successful for Bell in the same period against other independent companies in Ontario, even to the point of providing free telephones with a view to wiping out competition. Municipalities were offered lucrative franchise fees in return for a local monopoly. In Winnipeg, Bell Canada started a fighting brand in 1885 to compete against itself and its real rival. After the rival disappeared, so did the fighting brand and the cut-rate prices. Bell made agreements with the Canadian Pacific Railway Company to prevent access by rivals to CPR premises and rights of way by promising free service to all offices and stations of the CPR.

The first attempt to regulate the operations of a major telephone company in Canada occurred in 1892. An amendment to the charter of the Bell Telephone Company of Canada, approved by

[4] Wilson, Kevin G., *Deregulating Telecommunications: U.S. and Canadian Telecommunications 1840-1997*, Rowan and Littlefield Publishers Inc., Lanham Maryland, p. 33.

Parliament, provided that rates were not to increase without the consent of the Governor in Council. However, the Minister of Justice in 1897 decided that the amendment only applied to contracts existing before the passage of the Act. This meant that new contracts or changes in equipment rental were not subject to the rate control.[5]

Partly as a result of these tactics, as well as the increasing perception that telephony had to be developed in the national interest by a public authority, the concept of nationalization of the telephone system enjoyed much political support at the beginning of the twentieth century. Notwithstanding the same, the government of Prime Minister Wilfrid Laurier decided instead to place regulatory supervision over the telephone companies under federal jurisdiction with the Board of Railway Commissioners of Canada in 1906. This decision took place amid intense lobbying by Bell officials and rather brazen ignorance of elementary conflict of interest principles. Bell counsel, Allen Aylesworth, was appointed Postmaster General and became responsible for the implementation of measures within the amendments to the *Railway Act*. Other key Parliamentarians were, at the time, receiving annual retainers from Bell, including the Speaker of the House of Commons.[6] As one commentator noted:

> The federal government's choice of regulatory instrument preserved private power over telephone business and did little to disturb the prevailing pattern of industrial organization in that sector. The outcome can be attributed to Bell's lobbying, the company's great strength among the Quebec ministers on both sides of the House, the ideological bias of the Laurier ministry, and the weakness of the independent telephone movement in Ottawa.[7]

The first major regulatory fight in the Board of Railway Commissioners (" the Board") would be over the ability of Bell to refuse interconnection with its long distance lines. Bell Canada had cooperative arrangements with some independents that served areas that were not competitive with the Company's own business. These non-competitive independents had connecting agreements with Bell's long distance lines. Bell's management eventually realized that not all independents posed a threat and they freed the company from the necessity to serve marginal or unprofitable markets.[8]

Other independents that were directly competitive with Bell could only obtain interconnection by order of the Board. Pursuant to the 1906 amendments,[9] the Board had to review and approve all telephone rates, as well as order railway companies to allow connection with their stations (usually prohibited by Bell by agreement) without having to pay compensation. The Board also

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[5] Babe, Robert E., *Telecommunications in Canada*, University of Toronto Press, 1990, p. 91.
[6] Armstrong C., and Nelles V., *Monopoly's Moment*, University of Toronto Press, 1986, p. 170.
[7] *Ibid*., p. 174.
[8] *Ibid*., p. 290.
[9] *Railway Act*, 1906 6 Edw. VII, c. 42.

provided that the Board could hear applications for interconnection and approve them subject to suitable compensation that met standards of technical efficiency and did not entail "undue or unreasonable injury to or interference with the telephone business of such a company."

In 1911, however, when the Board was faced with a request for interconnection from the Ingersoll Telephone Company, it determined that it had a duty to protect the primacy of Bell and its historic place. It found that its long distance exclusion was the "sheet anchor" of its business. In order to interconnect, Ingersoll would have indemnified Bell for business losses arising from any fall-off in subscribers, not just pay the costs of interconnection. When the Port Hope Telephone Company tried to get the Board to declare it non-competing, thus removing an objection to interconnection, it was refused. Similarly, discrimination in treatment of the smaller independents was sanctioned ostensibly because the Board only governed federally regulated companies, not the provincially chartered independents. An appeal to the Supreme Court of Canada was unsuccessful[10] and attempts by the political allies of the independents to remove the requirement from the section of the *Railway Act* dealing with compensation for interconnection were ultimately rejected by a successful Bell lobby in the Senate in 1919. Competing telephone companies were then effectively doomed, and the last competing telephone company disappeared in 1925.

Next, Bell moved to change the terms of the connecting agreements with the remaining cooperative independents, such terms being ultimately incorporated into a Board order in 1923. This change was the commission and pro-rate system. Previously, Bell had priced long distance service at a loss, and maintained high local rates. As set out above, competitors were barred from interconnection with toll lines. This strategy prevented entry into the long distance market and put local service competitors that lacked long distance at a disadvantage. This enabled Bell's pricing strategy of high local rates.

Now, with direct local service competition eliminated, Bell no longer wished to subsidize its long distance service. This was because Bell was also effectively subsidizing the remaining interconnecting independents in reduced long distance rates. Bell decided to rebalance rates so that long distance toll collected from its own and independent subscribers subsidized its local service. This effectively squeezed the local independents that possessed no long distance lines and could not share in the distribution of high toll revenue. In turn, Bell's subsidized local rates were relatively low, and thus set the standard for the independents who found that they couldn't recover their costs when charging the same rates as Bell. The Board of Railway Commissioners subsequently approved this structure and refused to intervene to save the independents, continuing the traditional approach of non-intervention on behalf of provincial independent telco consumers. As well, the normal elements that might drive political or regulatory pressure to

[10] *Independent Telephone Co. v. Bell Telephone Co.*, 513 S.C.R. 503 (1916).

impose fairness across the system were lacking, as Bell itself applied for no general rate increases between 1928 and 1941.

In the result, most of these companies were eventually purchased by Bell. Between 1915 and 1985, independent telephone companies in Ontario declined from a market share of approximately 32% of telephones to 4% in 1985.[11] By then, the old regulatory policies that prescribed indifference by the regulator to the predicament of the independents had been abandoned, but most of their facilities were already in the hands of the Bell monopoly.

The principal justification, apart from regulatory capture, behind the successful continuation of a monopoly by Bell Canada, and that of subsequent monopoly providers in the Trans-Canada Telephone System, was the fact that the industry appeared to be a natural monopoly to the Board and its successors. The anti-competitive aspects of Bell's operations and the shuffling of lower and higher rates of local service and toll were tolerated because of the apprehension that the benefits of competition to individual subscribers would likely be temporary and that competition would jeopardize the system integrity and universal connectivity of the system.

In Western Canada, provincial governments, with the exception of British Columbia, moved to respond to Bell's failure to serve all regions and to the federal government's perceived failure to act decisively to advance telephone access by all citizens. In Manitoba, the government intervened in 1906 to build long distance lines interconnecting local exchanges, some of which were built and managed by the government. By 1908, Bell Telephone Co. had sold its facilities in Manitoba. After a period of direct government control of the provincial telephone network, Manitoba moved in 1912 to regulate the Manitoba Telephone System (MTS) through its Public Utilities Board while the operations, subject to PUB scrutiny, were regulated under a semi-autonomous telephone commissioner.

Saskatchewan followed suit in 1909, purchasing Bell's facilities in Saskatchewan and subsequently operated its government owned telephone company, SaskTel, under little independent scrutiny.[12] The Saskatchewan telephone system remains under public ownership today. SaskTel, however, frequently sides with its fellow privately owned incumbent local exchange companies (ILECs), Bell and TELUS, in their approach to regulatory affairs.[13]

In Alberta, the provincial government financed the takeover of Bell operations in 1908 with a $2 million dollar 30-year bond. This followed actions by the new provincial government to

[11] Babe, Robert E., p. 116.
[12] In 1982, the Saskatchewan Public Utilties Board was created to set rates for the provinces largest publicly owned corporations. Following a dispute with the government over directives, the Board was abolished in 1987.
[13] Interestingly for a publicly owned stakeholder, SaskTel has becomes aggressive in fending off consumer protection such as the Commissioner for Complaints for Telecommunications Services (CCTS), denouncing its practices as creeping regulation in Telecom Notice of Consultation CRTC 2010-247, *Review of the Commissioner for Complaints for Telecommunications Services*.

construct long distance lines in areas not being served, and take over a number of local exchanges. The takeover also followed the rejection of a rather cynical offer by Bell to divide the province into urban regions served by Bell and rural regions served by the government.

Under provincial ownership, there was a rapid expansion of plant facilities and customers in the initial period from 1908 to 1914. Alberta Government Telephones (AGT) was the crown corporation created by the province to operate the telephone system. AGT, like the other prairie systems, had a "no depreciation" policy that drove management to invest in expansion. Gradually, AGT, MTS and SaskTel adopted the same accounting procedures and approach to operations as Bell:

> By the 1930s, all telephone systems were valuing their assets in roughly the same way, sharing the revenues they collected through the Trans Canada Telephone System (TCTS), and approaching technical and service problems from the same point of view.[14]

In 1915, AGT was made subject to the *Alberta Public Utilities Act* to attempt to separate its operations from political decision-making. In 1990, AGT was privatized and in 1995, it acquired Edmonton Telephones (Ed Tel) from the City of Edmonton making it the only provider of local service in Alberta. In 1996, AGT and Ed Tel rebranded as TELUS and in 1999 the corporation merged with BC Tel continuing the merged entity under the TELUS name.

BC Tel had commenced its existence as the provincially chartered Vernon and Nelson Telephone Company in 1903 and later took over the assets of several other municipal telephone companies to become the British Columbia Telephone Company Limited. (Bell had voluntarily ceased operations in British Columbia in the 1880s.) It continued under private ownership, passing into American hands, in the 1920s, as BC Tel. In 1955, the General Telephone and Electronics Corporation (GTE) of Connecticut became the majority owner.

BC Tel also pursued a similar pattern of acquisition of independent telephone companies in the province. GTE sold its ownership interest to TELUS in the above noted 1999 merger. At the time of the merger, BC Tel provided all local service except in Prince Rupert and some remote regions serviced by Northwestel.

Northwestel, which is now owned by Bell Canada Enterprises (since 1988), had its origins in a number of small independent telephone companies with operations commencing as early as the Klondike Gold Rush. Canadian National Telecommunications acquired these companies in the 1950s and 1960s, spinning off all of their northern operations into Northwestel in 1979.

[14] Nelles, V. at p. 292.

Provincial regulation of provincial telephone companies was put in jeopardy by the Supreme Court of Canada decision in *AGT v. Canada (CRTC).*[15] CNCP Telecommunications had requested that the CRTC order AGT to allow CNCP to interconnect its private line telecommunications network with AGT's local telephone exchanges in Alberta. AGT had historically been regulated by the Alberta Public Utilities Board and the application to the Canadian Radio-Television Telecommunications Commission (CRTC) was under the provisions of the federal *Railway Act*. Following an application by AGT to Federal Court to prohibit the CRTC from hearing the application, the issue was eventually decided on appeal to the Supreme Court of Canada.

AGT contended that it was a local work or undertaking within the meaning of s. 92(10)(a) of the *Constitution Act* and within provincial jurisdiction. AGT also claimed immunity from CRTC jurisdiction as an agent of the Crown in right of a province not bound by federal legislation. However, the Supreme Court of Canada found that although AGT's works were located entirely within the province of Alberta, its involvement in the transmission and reception of signals across its border showed that it was an interprovincial undertaking. In coming to its characterization of AGT as an as a component of a national telecommunications system, the court also noted AGT's participation in various commercial arrangements with other carriers, and a degree of functional integration with federally regulated carriers.[16]

The position of independents then remaining at the time of the *AGT* decision that had no cross-border connections was settled by the Supreme Court of Canada in 1994 in a case involving the Quebec-based Telephone Guevremont Company. Adopting the reasons set out in the Quebec Court of Appeal, the Supreme Court of Canada found that the company was an interprovincial undertaking, as it provided a service by which its subscribers send and receive interprovincial and international communications.[17] As such, Telephone Guevremont was subject to the legislative jurisdiction of the Parliament of Canada.

As a result of the *AGT* and *Guevremont* decisions, the CRTC had jurisdiction over all telecommunications carriers in Canada. Newfoundland Tel, NB Tel, MT&T, and Island Tel subsequently filed tariffs for their services with the CRTC. In the 1993 *Telecommunications Act*, the provincially-owned SaskTel was given a transitional suspension of the operation of the *Act* until June 30, 2000.

The carriers that fell under CRTC jurisdiction for the first time became subject to the prevailing regime of regulation that had governed Bell and BC Tel. It was a regime that had evolved from

[15] [1989] 2 S.C.R. 225.
[16] *Ibid*. at p. 262. While the Supreme Court of Canada also acceded to the argument that AGT was an agent of the Crown and couldn't be bound by the *Railway Act*, AGT's privatization in 1990 eliminated that exception. The 1993 *Telecommunications Act* was made expressly binding on the Crown in s. 3.
[17] [1994] S.C.R. 878.

the first consideration of a general rate increase put before the Board of Railway Commissioners in 1919. At that time, the Board circumvented any inquiry into the reasonableness of Bell's existing rates by automatically proclaiming them just and reasonable as they had already been established, and were, by definition, just and reasonable. The Board would then consider the need for an increase.

A pattern of relatively compliant behaviour by the regulator set by this decision was continued in large part in the succeeding years of regulation by the Board of Railway Commissioners and the Canadian Transport Commission under the provisions of the *Railway Act*.[18] The form of regulatory supervision of Bell and BC Tel (the principal telecom companies federally regulated until the 1990s) was that of cost of service regulation, where the regulated company was allowed to recover all prudently incurred costs, and received a fair rate of return on its capital investment on used and useful assets in rate base. The standard for fair rate of return was set in the judgment of Mr. Justice Lamont in the Northwestern Utilities case:

> The duty of the Board was to fix fair and reasonable rates; rates which, under the circumstances, would be fair to the consumer on the one hand, and which, on the other hand, would secure to the company a fair return for the capital invested. By a fair return is meant that the company will be allowed as large a return on the capital invested in its enterprise (which will be net to the company) as it would receive if it were investing the same amount in other securities possessing an attractiveness, stability and certainty equal to that of the company's enterprise.[19]

During most of the period of regulation prior to the inception of the CRTC, the regulator took the position that its job was regulation and not management, such that it declined to investigate questions of efficiency in the operations. There was a presumption in the absence of conclusive proof that the company was carrying on operations in an efficient manner and in the public interest.[20] The requirement for prudency seems to have been set at a relatively low bar. Even when the regulator had questions about the need for certain expenditures recovered in rates, they were brushed aside as outside of the regulatory mandate. In 1927, the Board of Railway Commissioners reviewed Bell's capital expansion program. One of the Commissioners observed that:

> It is difficult to observe the useful purpose of such large additions to or changes in the present plant and equipment…That, however, is not a concern of the Board.[21]

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[18] *Railway Act*, S.C., c. 29, 1888.
[19] *Northwestern Utilities Ltd. v. City of Edmonton*, [1929] 2 S.C.R. 186, at p. 192.
[20] Board of Transport Commissioners for Canada, Application of Bell Telephone Company for an Order under Section 375, case no. 955-170 Judgment Ottawa, 1950.
[21] Board of Railway Commissioners for Canada, Application of the Bell Telephone Company for Local Exchange Services, C.R.C. No. 6057, Annual Report 1927, p. 55.

The successors to the Board of Railway Commissioners, including the Canadian Transport Commission, were ineffective in policing both the need for expenditures and service quality. The regulated companies had little difficulty in securing the results they required. Bell was able to organize its corporate operations in a way that maximized shareholder revenue while circumventing regulatory control. In 1919, the Board adjudicated Bell's rate of return on a per share basis, awarding it a $2.00 per share dividend and an additional amount of surplus (retained earnings) per share. Bell, not surprisingly, watered its stock by selling it to shareholders at very low prices, passing on monopoly profits to shareholders and justifying rate increases for subscribers to earn the rate of return plus surplus per share. These practices ceased when rate of return began to be calculated on rate base starting in 1966.[22]

The relative laxity of regulation coupled with the filips provided to regulated companies by watering stock and similar revenue-augmenting schemes appeared to produce lower levels of service and higher rates for the major two investor owned companies when compared to their publicly owned counterparts. A chart comparing the rate increases of Bell Canada and BC Tel to those of MTS, AGT and SaskTel between the years 1950 to 1977 is reproduced below from Robert Babe's book *Telecommunications in Canada*.

Figure A. Percentage rate increases introduced by five Canadian telephone companies, 1950-67 and 1950-77

	1950-67 Intraterritory		1950-77 Intraterritory	
Company	Local Rates	Toll Rates	Local Rates	Toll Rates
Bell Canada	49.0	22.0	101.0	65.0
BC Tel	87.0	47.0	197.0	112.0
Manitoba Tel	17.6	18.0	45.0	46.0
Saskatchewan Tel	29.0	9.0	67.0	37.0
Alberta Gov't Tel	20.0	n.a.	62.0	n.a.

[Source: Robert E. Babe, 'Vertical Integration and Productivity: Canadian Telecommunications,' 10; based on Restrictive Trade Practices Commission Exhibit T-487c, table A-3, Telecommunications Equipment Inquiry (compiled by the author).]

[22] Babe, Robert E., p. 170.

The CRTC took over regulation of telecommunications in 1976, and considerably expanded the ambit of the regulator's inquiry and approval of a regulated company's operations. In the result, the line between "regulation" and "management" was significantly diminished, allowing for greater scrutiny of the decisions, particularly in the area of capital expansion. Regulated companies were ordered to report on service quality, noting that rates were not reasonable unless accompanied by adequate quality of service and availability.[23]

However, some endemic problems in regulating remained with the CRTC. A 1994 PIAC report noted:

> What is evident from construction program reviews is that the regulator is very reluctant to disallow expenditures made in a capital program of a telco or to question the wisdom of the same. As well, there seems to be little fit between the promised efficiencies of programs and projects engaged in by the telcos in their construction program and their overall level of operating expenses. In any case, there appears to be little effort to follow up or to monitor results.[24]

This became more significant after the CRTC determination to allow toll competition as local rates might be devoted to the construction of facilities that would assist in delivering services where competition existed.

The CRTC also took an interest in the costs of the regulated companies commencing with proceedings in 1977, not only from the standpoint of prudence, but also to determine the relationships between the various services provided. Its continued inquiry into costing matters raised the hackles of the provincial telephone companies as it also involved the settlement procedures associated with revenues accruing in the Trans Canada Telephone System (TCTS - later Telecom Canada) that these companies were part of while they were provincially-regulated.

The CRTC's various costing proceedings commenced in the 1970s and concluded with the implementation of Phase III costing methodology in the 1980s. This methodology was used to associate actual company revenues and costs with a set of broad categories of existing services. Thereafter, the conceptual framework was married to the actual telco operations, with the results converted to cost manuals and applied in the tariff approval process. The significance of Phase III costing became greater in the restructuring period as the chief Phase III architect noted that:

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[23] Babe, Robert E., p. 168.

[24] Janigan, M. and Lawson, P., "The Dash for Cash: Post Competition Rate Maneuvering by Local Telephone Companies in Canada," PIAC, March 1994.

> The results played a vital role in setting contribution charges for the new entrants as well as providing a framework for the revised regulatory split rate base approach (described later in this report).[25]

This can be clearly seen in the costing results produced by the CRTC during the process of arriving at the approved costing methodology:

Figure B. Revenues, costs and profits by service category, Bell Canada, 1983 ($ millions)

Service category	Revenues	Costs	Difference
Local	1389	868	521
Access	0	1762	-1762
Toll	1988	626	1362
Competitive network	386	317	69
Competitive terminal	878	834	44
Common	99	333	-234

[Source: CRTC, 'Interexchange Competition and Related Issues, 'Telecom Decision CRTC 85-19, 29 August 1985, 53.]

The treatment of access costs and their attribution to the local category is a significant determinant of assumptions about the rate recovery in each class of costs.

The problem was that the CRTC's elaborate costing framework and manuals were not looked upon as simply a way to rationalize the system in a way that effectively allocated costs. Contribution was not necessarily a subsidy, nor was it reasonable to exclude the contribution concept from the design of rates for services that require the facilities associated with access costs. For example, a trucking company that does local and intercity business would not likely set its intercity rates as simply the costs directly associated with intercity travel. The result would likely be exorbitant local rates recovering all the expenses of acquiring, administering and maintaining the fleet.

One trial balloon, launched in an attempt to resolve the problem of collection of the large portion of telephony costs attributed to access, was the idea of local measured service which had been used in a number of other international jurisdictions. Essentially, access charges would not be fully recovered by a flat charge but would be defrayed by additional charges depending upon use

[25] Bigham, Fred, "Telecom Costing in Canada: The Story and the Lessons," in *Telecom Reform: Principles Policies and Regulatory Practices*, Melody, W.H. (ed.) Technical University of Denmark, 1997.

of local service. The Competition Bureau recommended separating rates into local and access components, with the former subject to measured rates. The CRTC, with an eye to the likely public response, was not supportive:

> The Commission continues to take the view expressed in Decision 85-19 that access costs are not usage sensitive and are caused by subscribers obtaining access to network facilities. The Commission also agrees with parties who argue that local service does not cause access costs to be incurred. However, the Commission is of the view that the mere separation of existing local rates into flat-rate components for access and usage would serve little purpose. Such an unbundling would not alter the prices or incentives facing subscribers, provide them with any more flexibility than they currently have, or have the effect of making rates more closely reflect the usage sensitivity of costs.[26]

In the result, as access costs were lumped into local service, the contribution paid by toll to access the network was spotlighted by deregulation proponents as an uneconomic subsidy. In much the same way that the deregulation debate migrated to rather extreme positions, the contribution provided by long distance service, based on the costing methodology, was deemed a "toll tax". Noting that 25% of Bell's customers accounted for 90% of its message toll business, one analyst was of the view that the then $2.8 billion dollars paid in contribution from toll rates constituted:

> (A) tax…not on the millions of individual Canadian telephone customers but on a very small number of corporate users. Just as with any taxpayer "hit" with a hefty tax increase or burden these taxpayers will inevitably seek ways and means to avoid or evade this burden.

While it is true that the achievement of efficiencies in local service provision could be compromised by simply increasing the contribution from long distance toll rates, the insistence that contribution was a subsidy derived from overburdened toll users was a powerful message. This was particularly the case when those users' ranks were disproportionately represented by corporate Canada. When that message was married to economic theories and criticism of traditional regulation that had commenced in some academic circles in the 1960s and subsequently popularized by conservative politicians in the western provinces, it became an irresistible force.

[26] CRTC Telecom Decision 88-4, *Bell Canada - 1988 Revenue Requirement, Rate Rebalancing and Revenue Settlement Issues and British Columbia Telephone Company - To TransCanada Rate Schedule Revenue Settlement Issues*. It might be noted that the Canadian preference for all-you-can-eat service continues to be reflected in relation to customer demands for broadband service.

Economic Theory and Deregulation

In the 1980s, a perfect storm of anti-regulatory animus began to shape up. Such animus was fueled by both a history of utility industry-favourable regulation and technological developments that drove business to demand changes in the method of regulation. In turn, political and economic thought, particularly in conservative circles was critical of regulated industries. At that time, economic analyses were being produced that suggested that competition would be more efficient than regulation. This work informed much of the movement for competition and the structural changes in the industry that occurred.[27]

The economic justification for the treatment of the local service telephone companies as a common carrier delivering a public utility service in a monopoly fashion had to be challenged for reform to take place. In particular, the assumption that the monopolist could deliver the product more efficiently than a number of competitors had to be toppled. The economies of scale that are present in a natural monopoly would cause the average cost of production to go down as the output of the commodity rises. Competition would, of course, mean an increase in overall industry costs by way of new entrant investment. Notwithstanding this well understood concept, the principal proponents of change had to somehow show an aggregate gain in economic efficiency associated with that change.

The first line of attack on traditional regulation cited the problems associated with the economic incentives. Companies regulated by the rate of return or rate of profit model had little incentive to economize or introduce efficiencies to reduce the need for revenue from rates to satisfy the required profit. Instead, wasteful expenditures, such as high management salaries and benefits, could be pursued. Asymmetries of information arising between the regulated utility and the regulator could inhibit the regulator's ability to control operations and maintenance expenses, and understand and allocate revenues and costs correctly. Perhaps most importantly, due to the fact that the utility earns a profit on all capital investments built or made and put in service, there is an incentive to overbuild or "gold plate" the rate base. This drives up the costs of monopoly service. In the result, critics expressed skepticism that optimum levels of capital and operational spending could ever be determined by the regulator. System-wide averaging of pricing (rates) was also questioned as a basis for universal service and criticized as an inefficient subsidy between classes of users.[28]

Other proponents of change to the monopoly regulatory structure focused on the phenomenon of "regulatory capture" where the regulator believes that the interests of the regulated industry are

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[27] Wilson, Kevin G., *Deregulating Telecommunications: U.S. and Canadian Telecommunications 1840-1997*, Rowan and Littlefield Publishers Inc., Lanham Maryland, p. 82.

[28] Richard Posner's 1969 essay "Natural Monopoly and Its Regulation" in the Stanford Law Review (1969) is viewed as a seminal work for proponents of change, cited at Wilson, Kevin G., *ibid.* at p. 91.

the same as the public interest the regulator is responsible for protecting. The informational dependency of the regulator upon the regulated company provided one explanation for regulatory capture. Other theories included lack of attention to the quality of decision-making by politicians, regulator appointments made to encourage support by the affected industry, and the prospect of work with the regulated utility after completing service as a regulator.[29]

An economist, George Stigler, argued that regulation was a product and, as such, subject to supply and demand forces like any commodity. The problem was that the demand was from the stakeholders that were the most enriched by the regulatory process. The group with the greatest self-interest, in this case the monopoly telcos, create the demand that will be satisfied by the supply because the size of the telcos' economic interest is greater than the more numerous but less engaged ratepayers. Stigler's theory undermined the basis for public interest regulation, while other deregulatory proponents questioned the ability of monopolists to set supernormal monopoly prices as long as the monopolist was operating in "contestable markets".

This latter theory was a substantial pillar in the arguments advanced at the inception of competition and relied upon significantly by the incumbents, especially as issues of forbearance later arose, to justify deregulation as being congruent with the interests of users move. It was an all purpose jiu-jitsu competition argument to overcome hard facts about incumbent market share, inertia or the number of competitors that would be necessary for an entrant to compete. Basically, the theory is that if competitors face no inherent disadvantage, then a market is contestable. There must be no legal barriers to entry, no costs for the new entrant that are not also borne by the incumbent, no government subsidy of the incumbent, and entry must be reversible (no sunk costs).[30] Thus, telecommunications policy-makers and regulators need not be concerned with the traditional economic theory that a product market requires four or five competitors of more or less equal size to be considered workably competitive. Regulatory protection for consumers could then be abjured, and incumbents free to set their own prices.

These theories, mostly popularized by the neoclassical economists of the Chicago School of Economics, provided the intellectual heft for parties seeking to open up the telephone system to competition and to square such competition with the regulator's responsibility to act in the public interest. Similar to the deregulatory actions taken by the United States in relation to airlines, this contingent of pro-competition economists was credited with "making the bullets fifteen years before politicians found them to be usable in the battles they wished to fight."[31]

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[29] Wilson, Kevin G., p. 93.
[30] Wilson, Kevin G. summarizing *Contestable Markets and the Theory of Industry Structure* by William Baumol, John Panzar and Robert Willig, Harcourt, New York, 1982.
[31] Derthick, Martha, and Quirk, Paul, *The Politics of Deregulation*, The Brookings Institute, Washington, D.C. 1985, p. 56.

At the same time, corporate interest groups jumped at the chance to contend for lesser government involvement in the American economy. The American Enterprise Institute, the Cato Institute, the Hoover Institute, and the Business Roundtable, among others, were heavily funded by corporate contributions interested in developing economic models, study projects and conferences designed to promote industrial activity free from government intervention.[32]

These theorists, in turn, found common cause with the high volume business users who were convinced that the regulated telecommunications industry was not providing the terms and costs for the new technological digital equipment and services they demanded. They were determined to usher in change to favour their use using the theories of deregulation and competition previously described to do so.

Proponents of change were also surfing a wave of political upheaval that had put deregulation and dismantling of government as principal objectives. The election of Margaret Thatcher as Prime Minister in Great Britain in 1979, followed by Ronald Reagan's presidential victory in the United States in 1980, gave theorists the opportunity to put their ideas into action now backed by political clout. Wilson noted:

> What began as a critique of economic regulation in the 1960s, had taken on the attributes of a political crusade, orchestrated by some of America's largest corporations with strong ideological overtones.[33]

As well, in Canada, the unsuccessful rearguard actions that the incumbent telcos had fought against namely the competitive incursion into traditional monopoly businesses of private lines and terminal equipment, had dented some of their ordinary regulatory armor. Bell's argument for the necessity of maintenaning system integrity by end-to-end control that it had advanced against the proposal for allowing the hook up of customer or competitors' equipment, was not accepted. The rejection paved the way for more unbundling of network services and competitive entry.[34] In 1987, the CRTC allowed resale of leased private lines to single customers and eventually removed restrictions against the joint use of leased circuits by resellers creating small business access to discounted competitive service in private lines.

A constellation of players was also coalescing in Canada to bring about change. The Fraser Institute and the Institute for Research on Public Policy commissioned studies that concluded that the pace of technological change, the salutary effects of U.S. deregulation, and the threat of bypass would mandate a similar Canadian response. Corporations would be the big winners and residential users would be the primary losers. However, the higher price that residential users would have to pay to ensure Canadian competitiveness would ultimately increase customer

[32] Wilson, Kevin G., p. 88.
[33] Wilson, Kevin G., p. 102.
[34] CRTC Telecom Decision 82-14, *Attachment of Subscriber-Provided Terminal Equipment.*

welfare in the aggregate. This would occur by way of increased innovation and greater responsiveness to the needs of consumers on the part of all carriers.[35]

Groups including the Business Council of National Issues, the Information Technology Association of Canada (ITAC), the Canadian Business Telecommunications Alliance (CBTA) and the Communications Competition Coalition (a select group of 20 corporate users organized by the Royal Bank of Canada in 1989) among other groups aggressively pushed the agenda of liberalization. They were vocal proponents of the application put forward by Unitel, a corporate entity, owned by Canadian Pacific and Rogers Communications, to provide long distance toll service in competition with the ILECs. Unitel's application, together with an accompanying application made by BC Rail Telecommunications and Lightel Inc. (BCRL) sought connection of the applicants' telecommunications network to the public switched telephone networks (PSTN) of the respondent ILECs for the purpose of providing public switched and dedicated voice and data telephone service, message toll service (MTS) and wide area telephone service (WATS).

[35] Wilson, Kevin G., p. 207.

CRTC Telecom Decision 92-12

The Unitel application, heard by the CRTC in 1991, put into play both the desirability of competition in long distance toll with the resultant decrease of long distance rates, and the prospect of increased industry productivity arising from possible competition. In June of 1992, the CRTC released Telecom Decision 92-12 which set the ground rules for the commencement of the major aspects of the restructuring of Canadian telecommunications.

As noted above, CRTC Telecom Decision 92-12 followed a period of intense lobbying and public relations on behalf of the competitor groups and business supporters, with particular emphasis on the effect of high toll (long distance rates) on the Canadian economy. This was reinforced by comparison to lower toll rates in the United States at the time of the hearing.

It is interesting to contrast CRTC's Telecom Decision 92-12 with that of CRTC Telecom Decision 85-19 some seven years earlier that also dealt with the issue of proposed long distance competition. In CRTC Telecom Decision 95-19, while the CRTC declined to find that long distance service was a natural monopoly, it turned down the idea of a discount to competitors for lower contribution to local access costs. It found that such a discount would be "uneconomic entry" in that the competitors would have lower costs than the ILECs. The CRTC noted that this would accord benefits to the customers of such competitors "at the expense of existing telephone subscribers in the form of higher local rates."[36]

The increase in local rates to lower contribution from long distance or "rate rebalancing" as it came to be known was a significant factor in the CRTC's 1985 decision to turn down competitive entry. On the one hand, the CRTC said, "rate rebalancing could yield important economic benefits at the macro level," but that on the other hand, universal accessibility (through affordable local rates) was "of fundamental importance."[37]

However, the CRTC itself had been slowly moving to rationalize costs within the incumbents' systems, and with its decisions of terminal equipment and private lines, began to quarantine those aspects of the telephone system that had to be delivered in a monopoly fashion. The CRTC's Phase III costing framework provided the raw material fueling business arguments for cutting toll rates and reducing the subsidy. Effectively, network access costs including all subscriber loops connecting terminal equipment to local exchanges, drop and block wires and protective devices at the subscriber's premises, and the termination of the subscribers' loop at the

[36] CRTC Telecom Decision 85-19, *Interexchange Competition and Related Issues*, p. 48.
[37] *Ibid*., p. 61 & 64.

main distribution frame at the central office, were assigned to local service.[38] This amounted to some 50% of ILEC plant and equipment and produced the need for a contribution from LD revenues which became the local subsidy.

While there is little doubt that the policy initiated in the 1920s of high long distance toll rates sustaining low local rates promoted system access to basic telephony, deregulatory proponents conflated such contribution as an inefficient tax designed to subsidize local users. The central fact remained that both services had to make use of common plant and equipment. As we have noted earlier, the contribution towards that exercise by toll service was deemed a cross-subsidy largely arising out of one conceptual version of the system largely derived for the purpose of understanding monopoly ILEC costs. However, the presentation of the costs in that conceptual framework was essential, together with the economic theories predicting an increase to the aggregate good through competition, to the initial key decisions made in the eventual restructuring of the industry and the crystallization of the mind set of many of the stakeholders and policymakers.

In the proceedings giving rise to Decision 92-12, Bell Canada put forward its own reference plan, largely designed to stave off competitive entry by offering average reductions of up to 55 per cent in toll rates by 2002. These reductions were, however, contingent on local service rate increases. BCTel also presented a reference plan much like Bell's to the CRTC.[39]

In Decision 92-12, the CRTC rejected the ILEC reference plans and opted for a more competitive environment in which:

> Competition would not only provide a strong incentive for the respondents to continue to minimize costs but would offer users a level of choice and supplier responsiveness that cannot be based in a facilities based monopoly environment.[40]

In addition, the CRTC approved the construction of competitive transmission facilities along the rights of way of the Canadian National Railways, and indicated that other facilities' providers could apply for approval if they were prepared to follow similar rules.

The Decision was crafted in a way to emphasize the potentially transformational aspects of the introduction of competition and to minimize the perceived decrements. Kevin Wilson notes what was certainly apparent to insiders:

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[38] Babe, Robert E., p. 156.
[39] Wilson, p. 207.
[40] CRTC Telecom Decision 92-12, *Competition in the provision of public long distance voice telephone services and related resale and sharing issues*, p. 36.

> Of course, the emphasis on choice and innovation was largely a rhetorical smoke screen. What were really at stake were lower costs to Canada's corporate users. The mantra of choice for all users, corporate and residential, had more to do with actual priorities of the Commission with regard to the class of residential users.[41]

In fact, the CRTC rather coyly suggested that local rates need not be raised to accommodate long distance competition:

> The Commission considers that, with contribution charges set at an adequate level, the impact of competition on local rates will be minimized sufficiently that there will be no need to address targeted subsidies.[42]

In addition, the CRTC found that competition would not fundamentally alter the ILECs' obligation to provide basic local exchange service, acknowledging that competitive pressures would likely cause some shifting of ILEC resources into competitive services.[43] The CRTC also promised quick consideration of ILEC long distance rate reductions not predicated on local rate increases.[44]

The extent of its opponents' victory rattled Bell Canada, in that in addition to ordering interconnection and allowing competition, CRTC Telecom Decision 92-12 required Bell Canada to pay some $160 million to prepare their networks for interconnection and allowed Unitel a discount on a declining basis on contribution for the first five years. As a result, Bell launched an appeal to Federal Court alleging an illegal confiscation of Bell's property rights, followed by an announcement that it would further reduce its long distance rates. The Bell response did little to win support and eventually, it withdrew its opposition after securing a promise that the CRTC would hold proceedings to restructure regulation and the government would be introducing new telecommunications legislation that responded to the new competitive regulatory ethos.

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[41] *Ibid.*
[42] *Ibid.*, p. 13.
[43] *Ibid.*, p. 62.
[44] *Ibid.*, p. 15.

Industry Restructuring 1992-2006

The period following the release of the CRTC's Telecom Decision 92-2 saw an energetic response from the incumbents to maintain hegemony and market share, while the regulator scrambled to realize the intent of its Decision and provide a way for market forces to become ascendant in the operation of the industry and the discipline of incumbents.

If competition and interconnection were to occur, the CRTC needed to establish some method of determining the appropriate pricing for long distance service provided by ILECs, together with expected contribution from that service and that of competitors. Rates set for the integrated operations of the ILECs had to be devised for competitive and non–competitive (utility) components. This also meant allocating assets and operational expenditures associated with each component of the rate base to utility and competitive segments. Those rate base assets for expenditures that were prudently incurred but no longer used nor useful had to be dealt with in a fashion that was fair to shareholders and ratepayers. And the individual ILECs had to establish base rates going into restructuring, particularly if they were to be subject to some form of performance based regulation in preparation for competition, where price regulation would be substituted for cost of service regulation.

With the passage of the *Telecommunications Act* (the "*Act*") of 1993 (given Royal Assent in June 1993), the fostering of reliance on market forces[45] became embedded as an objective in s. 7 of the *Act* together with the goal of enhancing the efficiency and competitiveness at the national and international levels of Canadian telecommunications.[46] Some critics noted that competition was really a means to meet an objective rather than an end result. The Telecommunications Review Panel Final Report described later in this paper, noted:

> Section 7 fails to distinguish between policy objectives, such as promoting affordability and effiociency of telecommunications markets, and the means for achieving those objectives, such as regulation or reliance on market forces.[47]

The new *Act* also provided flexibility for the CRTC in the way it could determine to determine just and reasonable rates:

> **27(5)** In determining whether a rate is just and reasonable, the Commission may adopt any method or technique that it considers

[45] *Telecommunications Act*, 1993, c.38, s. 7(f).
[46] *Ibid*., s. 7(b).
[47] The Telecommunications Review Panel Final Report, 2006, p. 2-5.

> appropriate, whether based on a carrier's return on its rate base or otherwise.

The new *Act* also provided that the CRTC shall refrain from regulating key concerns such as pricing and terms of service when it found that a service was subject to competition sufficient to protect the interests of users.[48]

The governing legislation was not the only thing that changed after CRTC Telecom Decision 92-12. The Stentor alliance of telephone ILECs, (formerly Telecom Canada) along with the individual companies began to clamour for an end to regulation as soon as possible. Throughout much of the restructuring process following CRTC Telecom Decision 92-12, they were adamant that the restrictions put on ILECs in terms of pricing and terms of service created an unfair advantage in favour of the new entrant competitors. These companies argued that competition, in its fairly embryonic stage, was sufficient to protect the interests of users.

To a casual observer of industry dynamic, this embrace of market forces instead of regulation by the ILECs might seem rather puzzling. The Canadian regulated utility sector, including the monopoly telephone companies, had done very well in Canada with traditional rate of return regulation over the previous decade. Studies had shown that between 1983 and 1992, gas and electricity distributors and telcos in Canada were given rates of return by regulators that were, on average, 560 basis points above the mean for all Canadian industries.[49]

In fact, the operating dynamics of the industry during this time period favoured what looked to be a counter-intuitive move. The 1980s and early 1990s saw massive ratepayer-funded investment in the digitization of the telephone networks of the incumbent telephone companies in Canada. In the result, over the next several years, almost all Stentor-based companies would become digitized. Telco documents indicated that there were massive productivity benefits upon the horizon that would result from these investments. As a result of such technologies, the marginal costs of providing telephone services were continuing to fall dramatically.

The playbook for the ILEC competition response had been first elaborated in the United States and the response to deregulation brought about as a result of the 1984 anti-trust case in the Federal court brought against AT&T and the subsequent ruling of Judge Harold Greene.[50] There, as a consequence, some regulated telcos had pursued massive acceleration of other capital investments

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[48] *Telecommunications Act*, s. 34(2).

[49] Evidence of Drs. Booth and Berkowitz, Maritime Telephone and Telegraph Rates Hearing that resulted in CRTC 1994-9, filed on behalf of the National Anti-Poverty Organization. This period encompassed a severe recessionary period and a downward economic turn occasioned by the adjustment to free trade.

[50] The consent decree in *United States v. AT&T*, at 552 F. Supp. 131 (DDC 1982), required the divestiture of the Bell Operating Companies by AT&T.

or attempted to divert revenue into non-regulated subsidiaries[51] to avoid cuts to rates for local basic service.

In addition, for the ILECs, the time to pick a fight was sooner rather than later. The Stentor companies were at least 20 times larger than their nearest competitor, with a considerable edge inherent from their position as the local monopoly telephone provider. An all-out war in a deregulated world for the monopoly telephone companies was a singularly attractive proposition.

Others have noted that the response of the Stentor ILECs corresponded to a predictable pattern of behaviour of monopolists forced to deal with the onset of competition and new entrants in response:

> In the third phase, having unsuccessfully defended their monopoly position, incumbents invariably "get religion" and demand to be relieved from regulation and "freed to compete." This is frequently met with resistance from new entrants who ask for some form of asymmetrical regulatory protection from the incumbents. Or they will argue: Now that we're in, close the door because the market can't support any more players. Also, these new entrants often allege predatory pricing and other anti-competitive activity on the part of the former monopolists.[52]

The ILECs' competitive response also included targeted rate reductions to long distance rates, particularly high volume long distance users.[53] The ILECs then attempted to recover the lost revenue from these toll reductions by a variety of proposed rate increases including directory assistance charges, maintenance of the touch tone premium, relief from inside wiring responsibilities as well as increases to basic rates. In the case of extra charges such as the touch tone premium, a pattern of CRTC decision-making was established that gave pre-eminence to the shortfall in revenue between local service rates and costs, obtained by applying the CRTC's cost allocation model. As a result of the same, local service customers would face continued attempts to whittle away basic service by extracting additional fees justified by the shortfall shown by the costing model. While the CRTC did not accede to all the ILEC requests as presented, the net effect of the Stentor companies' strategy, particularly in relation to additional charges, collected more revenues from their local service customers who were unlikely to be winners at this juncture from WATS and toll reductions.[54]

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[51] NYNEX Restructuring case, FCC decision 89-1807 December 29, 1989.

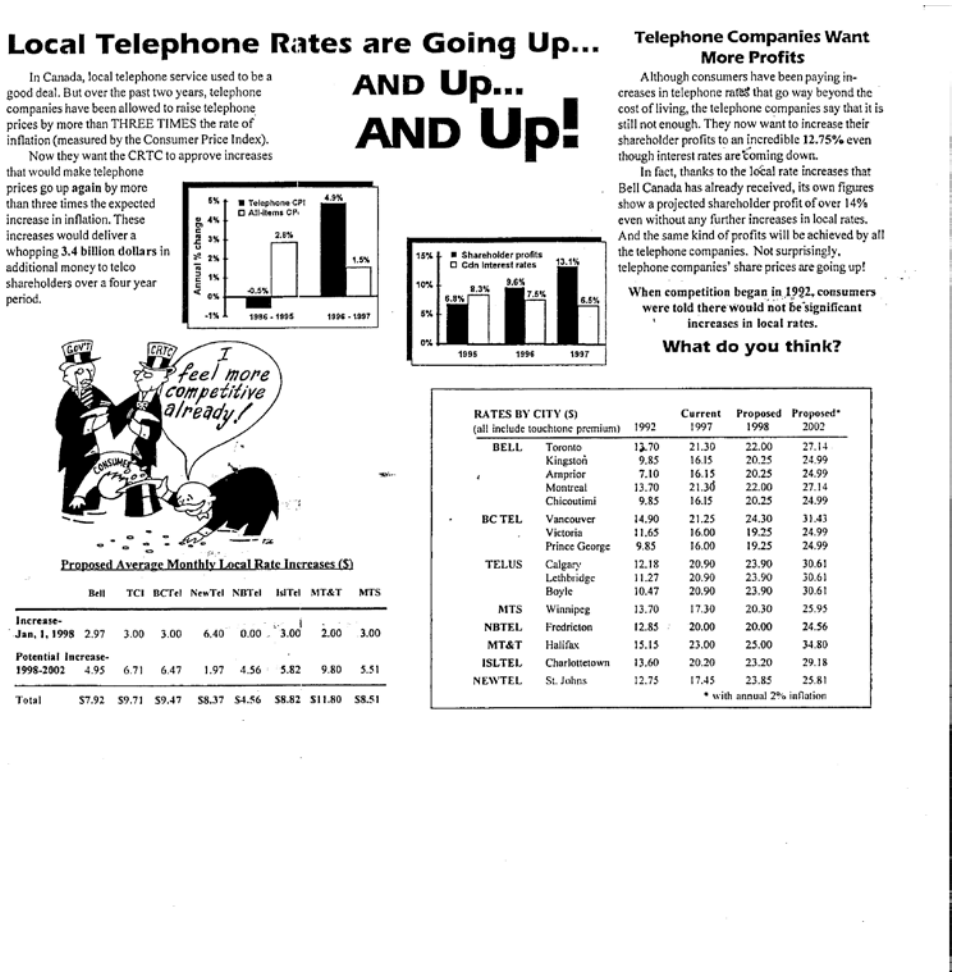
[52] Lancop, Robert G., Chief, Civil Matters, Competition Bureau of Canada,"Taking the Wraps Off Competition" 1996 Carrier Services Group Annual Conference and Workshop, Toronto, Ontario, May 1996 found at <http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/00947.html>.

[53] The rate cuts initiated by Bell Canada in March 1992 were approximately $192 million. See Janigan, M. and Lawson, P. *supra* note 24 at p. 13.

[54] Unitel estimated in 1994 that Bell's revenue enhancing efforts from local service obtained some $218 million which more than offset its $165 million in long distance reductions, Janigan, M. and Lawson, P., *supra* note 24 at p. 15.

The process of transitioning to a new regime where both competitive and utility services are offered by an ILEC was hardly seamless, or cost-free for the local service customer. The first casualty was the hope held out in Telecom Decision 92-12 that the introduction of toll competition need not mean an increase in local rates. In Telecom Decision 94-19, the CRTC stated that price regulation would not produce anticipated benefits, such as reduced regulation and increased incentives to reduce costs, until rates were closer to costs. In Telecom Decision 95-21, the CRTC commenced its rate rebalancing initiative. The process entailed three annual increases in rates for local service, with corresponding decreases in rates for toll contribution. The CRTC ordered a monthly rate increase of $2 for basic residential local services in 1996 and 1997.[55]

Figure C. PIAC Brochure in 1997 prior to CRTC Telecom Decision 97-9



Local Telephone Rates are Going Up... AND Up... AND Up!

In Canada, local telephone service used to be a good deal. But over the past two years, telephone companies have been allowed to raise telephone prices by more than THREE TIMES the rate of inflation (measured by the Consumer Price Index).

Now they want the CRTC to approve increases that would make telephone prices go up **again** by more than three times the expected increase in inflation. These increases would deliver a whopping **3.4 billion dollars** in additional money to telco shareholders over a four year period.

Telephone Companies Want More Profits

Although consumers have been paying increases in telephone rates that go way beyond the cost of living, the telephone companies say that it is still not enough. They now want to increase their shareholder profits to an incredible **12.75%** even though interest rates are coming down.

In fact, thanks to the local rate increases that Bell Canada has already received, its own figures show a projected shareholder profit of over 14% even without any further increases in local rates. And the same kind of profits will be achieved by all the telephone companies. Not surprisingly, telephone companies' share prices are going up!

When competition began in 1992, consumers were told there would not be significant increases in local rates.

What do you think?

Proposed Average Monthly Local Rate Increases ($)

	Bell	TCI	BCTel	NewTel	NBTel	IslTel	MT&T	MTS
Increase-Jan, 1, 1998	2.97	3.00	3.00	6.40	0.00	3.00	2.00	3.00
Potential Increase-1998-2002	4.95	6.71	6.47	1.97	4.56	5.82	9.80	5.51
Total	$7.92	$9.71	$9.47	$8.37	$4.56	$8.82	$11.80	$8.51

RATES BY CITY ($) (all include touchtone premium)		1992	Current 1997	Proposed 1998	Proposed* 2002
BELL	Toronto	13.70	21.30	22.00	27.14
	Kingston	9.85	16.15	20.25	24.99
	Arnprior	7.10	16.15	20.25	24.99
	Montreal	13.70	21.30	22.00	27.14
	Chicoutimi	9.85	16.15	20.25	24.99
BC TEL	Vancouver	14.90	21.25	24.30	31.43
	Victoria	11.65	16.00	19.25	24.99
	Prince George	9.85	16.00	19.25	24.99
TELUS	Calgary	12.18	20.90	23.90	30.61
	Lethbridge	11.27	20.90	23.90	30.61
	Boyle	10.47	20.90	23.90	30.61
MTS	Winnipeg	13.70	17.30	20.30	25.95
NBTEL	Fredricton	12.85	20.00	20.00	24.56
MT&T	Halifax	15.15	23.00	25.00	34.80
ISLTEL	Charlottetown	13.60	20.20	23.20	29.18
NEWTEL	St. Johns	12.75	17.45	23.85	25.81

* with annual 2% inflation

[55] The accompanying requirement for ILECs to reduce basic toll rates was eventually overturned by Cabinet appeal.

The CRTC would consider the magnitude of the third round of rate rebalancing in its proceeding to set the parameters of the price cap on local services. The CRTC allowed up to a $3 monthly rate increase that was to be used to reduce contribution from toll to local service. The CRTC also refused to order mandated reduction in long distance rates for lower-end customers despite the fact that such rates had been impervious to meaningful competitive reductions up that juncture. The CRTC's adopted language in its Decision suggested that contribution towards access expense amounted to a "tax on information intensive enterprises". Coupled with its priority of reduction of the same necessitating rate rebalancing, the regulator appeared fully converted to the principles of the deregulation/competition ideology:

> Improper pricing policies or other barriers to entry can result in the misallocation of resources, a reduction in choice of supply in certain markets and the suppression of demand in others, resulting in, among other things, increased costs to information-intensive enterprises and barriers to communications among Canadians.

Price caps had been chosen as the preferred method of regulation of local service in Telecom Decision 94-19. The CRTC concluded that price caps would allow for more efficient and effective regulation in a number of ways:

> First, price caps reduce incentives and opportunities for companies to over-invest or misallocate costs. Once caps are established, prices cannot exceed them (apart from the operation of a limited number of exogenous variables), even if the investment base is increased. Second, price caps reduce opportunities to cross-subsidize or engage in anti-competitive pricing, because price changes in one basket cannot be offset by changes in other baskets. Third, price caps provide incentives for telephone companies to be more efficient and innovative, since shareholders assume more of the risks and rewards of business decisions and retain the benefits of higher levels of productivity. Fourth, price caps can eliminate the need for regulatory assessment of investment, expenses and earnings between price cap performance reviews.[56]

The price caps for the ILECs were set at the outset of the price cap period for the years beyond the first to equal the first year cap growing at the measure of the inflation rate minus a forecast of the annual decrease in real cost (or productivity factor) over the period. (This forecast is labeled as "X"; hence price cap regulation is sometimes referred to as "I –X regulation".)

The productivity factor for the first price cap period of four years (1998-2002) was set at 4.5%, meaning that rates before inflation would have to show a reduction of that percentage prior to any upward adjustment for inflation. It was expected that this process would prepare ILECs for full competition on all retail services.

[56] CRTC Telecom Decision 94-19, *Review of regulatory framework*.

However, the transition to price capped local service hardly meant an end to the efforts of ILECs to increase rates by attributing greater costs to the utility segment of its operations for depreciation, or stranded assets, or rate base investments in broadband that were not connected to local rates. The ILECs hastened to deploy new networks that would serve their future needs to compete rather than the requirements of basic service and accelerated the pace of their capital recovery through the application of higher depreciation rates.[57]

Similarly, the CRTC imposed the costs of the ILECs in providing local number portability for competitive entrants on local service ratepayers. This measure enabled ratepayers to switch local service providers but at a cost of over $360 million dollars to ratepayers, primarily in forgone rate discounts under the first price cap.[58] With rebalancing, additional depreciation, compensation for stranded assets and local number portability all folded into local rates, consumers were anxious to see the benefits having experienced the burdens.

[57] Gabel, David, "Allocation of Depreciation Expense," FNACQ Position Paper #2, CRTC PN 94-16, p. 2.
[58] CRTC Telecom Order 2000-143, *Local competition start-up and LNP costs established*.

The Test for Forbearance

At the same time, the ILECs were incessant in their pleas to be relieved of regulatory oversight as well as the elimination of the CRTC-established framework that provided contribution discounts to competitors. A 1995 Stentor publication, "A Canadian Success Story at Risk," warned of dire consequences if they had to "bear the burden of the heavy federal regulation designed for the monopoly era." Stentor ILECs could not build the infrastructure necessary for Canada to maintain its telecommunications leadership because of competitor subsidization. As a result, Canadians would have to face a future that included loss of jobs, diminished opportunities for all, a lower standard of living, weakened social programs and a diminished quality of life.[59]

It was with this backdrop that the CRTC considered the key first step for the ILECs that involved the deregulation of the long distance toll market. However, some clear market concerns presented themselves as impediments to forbearance. Notwithstanding aggressive advertising and solicitation by the new entrant long distance competitors, by 1996, most of the market was still resolutely in the hands of the incumbents. Over 70% of minutes were still being handled by Stentor Companies. Over 90% of minutes were being handled by Stentor Companies, AT&T, or Sprint Canada networks. And Bell Canada's own statistics showed that over 65% of their customers spent approximately $11 per month on long distance and thus did not qualify for a discount plan.[60]

In Telecom Decision 94-19, the CRTC set out the analysis upon which it would determine applications for forbearance pursuant to section 34 of the *Act.* The key determination was to be based on the concept of market power. Market power was defined as "the ability of a firm to impose unilaterally and profitably a significant, non-transitory price increase within the relevant market".[61] In the absence of market power, the market was to be considered workably competitive.

Now faced with the application for long distance forbearance, the CRTC set out the criteria for assessing market power in Telecom Decision 97-19:

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[59] "A Canadian Success Story at Risk," 1995 at pp. 7-8. Announcements of this kind of strident character were not uncommon in the post 92-12 period. In 1994, Stentor announced what it called the "Beacon Initiative" essentially a $10-12 billion project to deliver broadband to the home and supplant the cable companies in the development of the Information Highway. It lacked any real way to pay for it through commercial applications and became known in some circles as the "Bacon Initiative".

[60] CRTC Telcom Public Notice 96-26, *Forbearance from regulation of toll services provided by dominant carriers*, Table 2 of Interrogatory Response SRCI(FNACQ/NAPO)7Apr95-1 RRF.

[61] CRTC Telecom Decision 97-19, *Forbearance - regulation of toll services provided by incumbent telephone companies*, para. 13.

> In assessing whether carriers possess market power, the Commission considers a number of factors: (i) market shares of the dominant and competing firms; (ii) demand conditions; (iii) supply conditions; (iv) likelihood of entry into the market; (v) barriers to entry; and (vi) evidence of rivalrous behaviour.[62]

The evidence of prominent industrial economist, William Shepherd, presented on behalf of the Consumer Groups, set out in stark terms the high bar that would have to be overcome to allow consumers to have the benefit of a workably competitive market:

> The bedrock need is for competitive parity among enough reasonably comparable rivals to prevent collusion, with free entry to reinforce the pressure.[63]

In Shepherd's view, informed by the observed results across the U.S. industrial experience, this meant at a minimum:

> (1) at least 5 reasonably-comparable competitors;
> (2) an absence of single-firm dominance. That prevents strong unilateral market control over much or most of the market, which could exploit and/or create imperfections in the market; and,
> (3) reasonably free entry into and among all segments of the market, so that numerous new firms can enter, survive, and acquire significant market shares.

Shepherd also cautioned that oligopoly is not competition:

> If dominance fades, tight oligopoly is the next stage: it exists when 4 firms hold over some 60 percent of the market.[64] Coordination and collusion are likely to occur for significant periods. In both situations, there may be intervals of sharp competition; but joint market control and poor performance are likely to occur much or most of the time.[65]

Shepherd was decidedly less sanguine about the prospects for competition to provide the appropriate market discipline for the benefit of consumers:

> The clear lesson: the popular hopes that monopoly and dominance will quickly disappear are contrary to industrial experience. In addition, the

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[62] CRTC Telecom Decision 97-19, *Forbearance - regulation of toll services provided by incumbent telephone companies*, para. 26.

[63] Evidence of William Shepherd on behalf of the Consumer Groups in CRTC Public Notice 1996-26, p. 5. See the classic analysis in William J. Fellner, *Competition Among the Few*, and New York: Knopf, 1949, ch. 1; Kaysen and Turner, *Antitrust Policy*, ch. 3, Scherer and Ross, *Industrial Market Structure*, chs. 1 and 6-8; Shepherd, *The Economics of Industrial Organization*, chs. 1, 3 and 13; and for recent pure theory, Jean Tirole, *The Theory of Industrial Organization*, Cambridge: MIT Press, 1988, chs. 5-7.

[64] Or when the Hirschman-Herfindahl Index (HHI) is over 2,000 to 2,500. See Scherer and Ross, *Industrial Market Structure*, and Shepherd, *Industrial Organization*, 1990.

[65] Evidence of William Shepherd, p. 6.

> old utility firms have about a century of experience in influencing and resisting policy officials, as well as in averting competition.[66]

Faced with profound market segmentation in the toll market, the CRTC still decided to forbear from regulating the long distance market, but instituted a number of safeguards to try and protect low volume consumers and embryonic competition. The CRTC continued an upward pricing restraint on basic toll market that had shown little evidence of competitive penetration.[67] It also maintained price imputation rules (preventing predatory or Ramsey pricing by ILECs) and the restriction on bundling long distance service with regulated services for the ILECs.

The long distance forbearance decision was very much a harbinger of the CRTC's future approach to assessing the state of competition in telecommunications. On the one hand, the CRTC was inclined to be satisfied with the appearance of rivals offering real price discounts accessible to some consumers for forbearance purposes. On the other hand, the CRTC looked to fix the problems associated with accepting the market conditions as workably competitive through devices like the upward pricing constraint on basic toll and the maintenance of the imputation test.

The role of the Competition Bureau in the proceedings giving rise to Telecom Decision 97-19 conformed with the approach advanced in relation to issues of ILEC regulation throughout the restructuring process of several decades. The Bureau was a stalwart proponent of deregulation, in this case dismissing alleged entry barriers, predicting dynamic competition and, in keeping with its skepticism about predatory pricing by dominant market players, arguing against the continuation of the imputation test.

The Bureau's advice was usually inclined towards non-interventionism despite the consumer interest at risk. As one of its witnesses remarked in the CRTC Public Notice 2006-14 Essential Services proceeding, "[i]mperfect competition is better than imperfect regulation." The Bureau was also relatively content with a duopoly as substitute for regulation rather than mandated access:

> I guess our view would be to say, as in the Osborne Report that he points to competition between the broadband as being in a situation where it looks like the duopoly outcome is acceptable compared to alternatives.[68]

Together with the strident complaints of the incumbents and cries for relief from one-sided regulation, the Bureau was usually remarkably prepared to tolerate market failure as an

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[66] Evidence of William Shepherd, p. 7.
[67] CRTC Telecom Decision 97-19, *Forbearance - regulation of toll services provided by incumbent telephone companies*, para. 69.
[68] CRTC Telecom Proceeding 2006-14, *Review of regulatory framework for wholesale services and definition of essential service*, Transcript Vol. 2, Line 12545.

acceptable risk to obtain competitive markets or at least to line up deregulation with theoretical constructs. As we shall see, these goals have been rather imperfectly achieved.

Early Returns on Competition

Notwithstanding the optimism radiating from competition proponents following Telecom Decision 92-12, and the subsequent restructuring CRTC decisions, the long distance market for low and medium volume residential consumers did not produce the kind of discounts to the Canadian telephone bills that were anticipated. A PIAC report in February 1999 noted:

> …the overall savings for residential consumers are far less than for business consumers, though overall actual price reductions enjoyed by residential consumers are difficult to quantify. Price reductions were available over the study period, and enjoyed by some customers (most of who stayed with a Stentor company and received 15% discounts, while a smaller portion switched to competitors and received higher discounts). But a surprisingly large number of customers, more than half of Canadian households, did not appear to enjoy any price reductions at all, and were still charged the high "DDD" rates. Not only are these high prices unfair to the consumers being charged them, but they also dampen competition by allowing the dominant firm to exploit a market flaw.[69]

In effect, the incumbents saw no need to reduce the basic toll DDD rates for low volume customers who were still overwhelmingly their customers. In the result, through the second generation of price caps, the CRTC maintained the ceiling on basic toll rates for the ILECs

> The Commission notes that the ILECs obtain substantial revenues from calls charged at basic toll rates. For example, such calls account for nearly 30% of Bell Canada's toll revenue. The percentages for other ILECs range from about 10% to 20%. As parties noted, some of these calls are made by customers who use discount toll plans that apply basic toll rates at certain times of the day.
>
> The Commission agrees with ARC et al. and BCOAPO et al. that toll market conditions have not changed significantly since 1997. Accordingly, the Commission considers it appropriate to maintain the conditions on the basic toll schedule established in Decision 97-19. Further, in view of these considerations, the Commission is of the view that the proposed changes in respect of credit card surcharges would not be appropriate. Accordingly, the Commission determines that credit card surcharges should continue to be included in the calculations of the average basic toll schedule price.[70]

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[69] Barrados, Angie, *Still a Long Distance to Go, Residential Consumers and the Transition to Competition in the Long Distance Market*, PIAC, Ottawa, (February , 1999), p. 3.
[70] CRTC Telecom Decision 2002-34, *Regualtory framework for second price cap period*, pp. 518 and 519.

Contrary to what was anticipated in Telecom Decision 92-12 and the subsequent CRTC decisions that enabled industry restructuring, the overall phone bills for most Canadians increased during the 1990s largely because of increases in local rates. Most light users of long distance services, which tended to be disproportionately populated by the low-income segment of customers, had significantly increased phone bills.[71] There was no evidence that the overall benefits to the economy stemming from long distance competition had helped low-income consumers afford these increased prices for telephone service.[72]

An evaluation completed some ten years after the commencement of long distance competition found that most Canadian customers of telephone services still had not benefitted from industry restructuring.[73] Its findings undercut the premise that competition had brought universal benefits to the telecommunications market. Yet when the study appeared, there was still a prevailing industry spin that the move to competitive entry had been an across the board winner. It became increasingly apparent that the restructuring was a cost shifting exercise that financed discounts in toll rates leaving the rewards of digitization to be reaped by telco shareholders.

The PIAC 2003 study referenced Statistics Canada tracking of consumer price, changes in the telephone services sector using a representative basket of services. Over the period of January 1992 to June 2002, the Statistics Canada price index for telephone services rose 17.4%. This increase was slightly less than the rate of inflation. However, during the period in question the telephone companies experienced significant productivity growth. Improvements in productivity came about primarily as a result of the installation of computer-based technology, such as digital switches, that greatly reduced telephone company costs. For example, Bell Canada's productivity growth rate over the period of 1988 to 2002 was five times the long run economy-wide total factor productivity growth. It is therefore likely that telephone service prices would have been much lower during this period had the prices tracked actual costs.[74]

Other assumptions about the effect of competition were effectively disproved during the early years of competitive entry. It had been assumed that the incumbent telephone companies would be sufficiently motivated by the desire to maintain brand loyalty such that significant decrements in service quality would not likely occur. In setting service quality standards after the first price

[71] Barrados, Angie, "Still A Long Distance To Go", PIAC, Ottawa, February 1999, p. 55.
[72] Barrados, Angie, p. 4.
[73] Lawson, P. and Briggs, A., "A Comparative Analysis of Residential Telephone Service 1992-2002", PIAC, September 2003. Heavy usage consumers were the biggest winners, showing reduced telephony costs of between 15-30%. On the other hand, light users of telephone services, (some 25% of ILEC customers) received substantial increases in telephone bills over the ten-year period increases of between 35%-65%. The median, or medium use, customer was also generally subject to increased telephone costs, ranging from –4% to +33%, depending on location.
[74] *Ibid*., p. 2.

caps decision, the CRTC accordingly declined to order financial penalties for depreciation service quality.[75]

The report also notes the deterioration in customer service that appears to have accompanied the development of competition over this ten-year period. Telephone companies seemed to be more focused on capturing customers than on servicing them once captured.

As well, while competition had greatly expanded customer choice, new problems arose. The frequent changes in plans and options made it difficult for customers to compare services and prices to ensure the best deal. Unwanted and misleading marketing was a persistent problem. Customers were far too frequently given inaccurate information about charges and costs associated with service plans. While no longer as great a problem as it previously was, switching of service providers without the consumer's permission ("slamming") remained a marketplace problem.

PIAC's 2003 report stated that the availability of basic local service did not suffer over this period. However, competition in the provision of local residential service was very slow to develop. As of 2002, most residential communities in Canada did not have alternatives to ILEC local service. Only a few providers were offering alternative wireline services and only in a few locations. In fact by 2004, the competitors' share of revenue local residential telephony was only 3%.[76]

The report concluded that while competition had brought welcome changes in choice, service innovation, and reductions in the price of long distance service, it had also brought higher overall telephone prices for the typical residential customer, deterioration in service quality, and a number of new marketplace problems for consumers. A segmented market, inequality of benefits and limited attention to low volume users characterized the early competitive response.

However, the consumer discomfort with the new competitive paradigm was not shared by the former monopoly ILEC providers who, despite their vociferous protests to the contrary, were flourishing. As Rogers Communications noted, referring to the evidence filed in the course of the second price caps proceeding:

> The ILECs were left with supra-normal profits under the first price cap regime, typically achieving Utility after-tax equity returns of approximately 15% in 1999 and 2000 [footnote omitted] and forecasting the same or better for 2001[77] compared to the after-tax equity return of

[75] CRTC Telecom Decision 97-16, *Quality of service indicators for use in telephone company regulation.*
[76] "CRTC Telecommunications Monitoring Report," July 2006, p. 6 available at: <http://www.crtc.gc.ca/eng/publications/reports/PolicyMonitoring/2006/tmr2006.pdf>.
[77] Bell and Aliant forecasted 14.3% and 17.4% after-returns on equity for the Utility segment for 2001 respectively. Telus forecasted a 16.2% after-tax return on equity for the Utility segment for 2001.

> 11% the Commission ruled appropriate for setting the "going-in" rates for the initial price cap regime. The ILECS realized these high returns by achieving productivity gains far in excess of the 4.5% productivity offset established for the initial price cap regime and are entitled to these profits under the rules and operation of the first price cap regime. It would not be appropriate to remove the constraints of the price cap system to allow these profits to increase even further.[78]

Consumers' representatives were unable to join in the general expressions of satisfaction emanating from government and industry circles concerning the restructuring process. In 2005, PIAC noted this to Telecommunications Policy Review Panel (TPR Panel) consultation session:

> Now, for the third time in less than ten years, we are told that residential local exchange competition is once again "just around the corner." As far as competition in local service goes, no sacrifice has ever been too great to achieve this supposed utopia provided the residential ratepayers pay it. We endured a decade of rebalancing local rates upwards, only to again be told that these rates based on actual costs were still too low, so we should pay higher rates to enable competition to survive, and one day give us lower rates again. The last time local rates were made in the second price caps proceeding, hundreds of millions of dollars were added to rates (actually just not subtracted from rates according to the price cap formula) and placed in kind of happy birthday fund to pay for things like discounts to competitors for Digital Network Access or other fun things that stakeholders thought residential consumers would be thrilled to pay for. No surge in competition or competitors was ever observed as a result of this forced largesse… For the reality is that the restructuring of the telecommunications industry and the increased reliance upon market forces to deliver services has also created actual or potential gaps in consumer protection. In this market, it apparently makes more business sense to use your money to buy commercials to attract customers than it does to spend the money resolving their service problems. The experience to date in telecommunications, and in other former monopoly based utility industries such as airlines is discouraging for any prediction that market discipline can ensure high quality of service and effective customer redress for supplier problems. These markets frequently show patterns of service deterioration that substantially limit the ability of all consumer segments to share in any restructuring benefits.[79]

[78] Evidence of Rogers Communications Inc. filed in CRTC Public Notice 2001-37. The supra-normal profit levels realized over the 1998-2001 period are embedded in the existing rates and will be enjoyed by the ILECs on a continuing basis forever.

[79] Presentation of Michael Janigan to the October Policy Forum of the Telecommunications Policy Review Panel, October 24, 2005.

The CRTC Ups the Ante

When the late Charles Dalfen was appointed Chairperson of the CRTC in 2002, he made the development of local telephone service competition a priority. At that time, the market share for the former incumbent telephone companies was more than 95% for local residential phone service and slightly less than 90% in the local business market. The introduction of competition to the local telephone service market had brought a rebalancing of local telephone rates by the CRTC a decade earlier. The rebalancing had led to substantial increases in local telephone rates that lowered the contribution to network costs provided by the long distance services of the incumbent telephone companies. This rebalancing was supposed to price local service at a level that would enable competitive entry, and together with price caps on local ILEC rates, these measures were to prepare for the onset of vigorous local service competition that would discipline rates and service. The failure of competitive entry into local service in any significant way stalled the success of the vision for telecommunications commenced by the CRTC's plan to introduce competition and restructure the industry through its decisions a decade earlier.

The ILECs, however, were in no mood to countenance special regulatory means to speed the onset of meaningful competition. They had railed against the discount given to long distance competitors when competition was introduced in Telecom Decision 92-12 and maintained that the threat of entry was sufficient to deter pricing as monopolists in regulated services markets. The ILEC talking points associated with the supposed coddling of competitors at the expense of the former national champions would be currently throughout the entire era of restructuring. The complaint continues to resonate, as seen in recent proceedings to determine issues such as the sharing of essential services and the requirement to match broadband speeds for wholesale customers.

As noted previously, the *Telecommunications Act* and its predecessor, the *Railway Act*, had been set up primarily to regulate the delivery of monopoly services, not to regulate competitors. The CRTC initially struggled with how to control misconduct of competitors in the long distance market, frequently using its regulation of the ILEC to try and effect the desired behaviour from the new entrant. The volume of complaints concerning practices such as unauthorized transfer of long distance service, or non-transparent billing, led the more established long distance competitors to establish an ombudsman to deal with customer complaints associated with new entrant services.

In turn, competitors complained bitterly about the problems associated with arranging interconnection and billing with the ILECs. These arrangements were the subject of a number of CRTC applications that eventually resulted in the formation of a CRTC sponsored committee,

the CRTC Interconnection Steering Committee (CISC). CISC served to sort out technical and administrative issues without the necessity of formal hearings. It was largely successful in implementing the intent of the CRTC decisions enabling both the entry of competitors in markets such as long distance, and the technical and operational compliance when ILECs were required to allow interconnection.

With the expiry of the discounts for access to ILEC networks afforded to competitors in the initial period of long distance competition, the new entrants were wary of attempts by the ILECs to reprice their service offerings to affect lower prices for services where competition existed, financed by increases to their monopoly delivered services. Alternatively, there was concern that vertically integrated ILECs could thwart the spread of competition through pricing strategies. One such strategy would see the ILECs bundle regulated and unregulated products and services into a single offering that would involve discounting services offered where competition exists to below cost with a view to eliminating competition. The regulated services offered in a monopoly market could subsidize the discounts.

The CRTC adopted a number of strategies in an attempt to prevent such anti-competitive behaviour from occurring. Chief among the approaches used to prevent anti-competitive conduct was the separation of the ILEC rate base into competitive and utility components as discussed previously. The costs of an ILEC service offered in a competitive fashion could not be borne by services offered in the utility, and the monopoly segment had to be priced in accordance with a price cap fashioned after a cost of service review. CRTC tariff rules mandated that a regulated service recover its fully allocated cost to prevent predatory pricing. In addition, the rules mandated the offering of a price floor mechanism that was applicable to interexchange voice services.[80] It required that, in general, when proposing a new service or a price reduction for an existing service, an ILEC must demonstrate that the proposed rate for the service would be sufficient to recover the service costs, where those costs were defined as the Phase II costs of the service plus an imputed contribution "cost". In light of this latter cost component, the Telecom Decision 94-13 price floor mechanism was referred to as the "imputation test".

In 2003, the CRTC identified concerns that the price floor mechanisms that had been adopted in a series of decisions commencing with Telecom Decision 94-13 had failed to achieve a reasonable balance between the interests of customers, ILECs and competitors. The price floor mechanisms caused a weakened state of competition and potential unjust discrimination between customers.[81] In addition to considering changes to the imputation test and service bundling rules, the CRTC also identified targeted discounts associated with pricing flexibility exercised by large

[80] CRTC Telecom Decision 1994-13, *Review for regulatory framework - targeted pricing, anti-competitive pricing and imputation test for telephone company toll filings.*
[81] CRTC Public Notice 2003-8, *Review of the regulatory requirements pertaining to the BITS licensing regime, sharing groups, and CLEC/Municipality agreements for the provision of 9-1-1 service in light of Telecom Decision 2007-51.*

ILECs in long term and volume contracts as a potential source of unjust discrimination and anti-competitive effects. The CRTC accordingly proposed a pricing constraint on such contracts.

This regulatory action, largely in response to the relatively puny competition then in existence in the local service market, triggered a firestorm of controversy orchestrated by the ILECs, but was fueled by a sense, even in consumer quarters, that the CRTC tinkering was well-intentioned but not in the public interest. PIAC noted in its comments filed in the proceeding:

> At first blush, it is difficult to determine the nexus between the advancement of the objectives in CRTC telecommunications mandate and the remedies to be applied in fixing the competition malaise. The Consumer Groups submit that it is a difficult fit to leverage a prescription to mandate price increases to incumbent services or bundles into a framework that is supposed to achieve just and reasonable rates. … The Consumer Groups are not aware of any clamor among residential customers to finance this subsidy, (price increases to incumbent services) particularly in the absence of tangible, non-speculative benefits in consumer welfare to this group of customers. The size and protracted nature of this subsidy makes it a particularly difficult sale to a constituency that has largely been disenchanted with the terms of its conscription in the battle for telecommunications competition. In our view, the proposals would once again throw consumers' pocketbooks into a war by the unwilling, to aid the failing, at the behest of the confused.[82]

In fact, the CRTC efforts with respect to pricing constraints mirrored its fateful decision of establishing deferral accounts for excess local telephone rates in the Telecom Decision 2002-34.[83] In that case, the rates were configured in accordance with a price cap that calculated annual changes in rates in the standard fashion of adding increases based on an inflation factor and deducting expected productivity increases. However, in a rather bizarre effort to prevent local service prices from decreasing, and reducing margins for prospective entrants, the CRTC determined that when the inflation factor was less than the productivity factor producing a negative calculation, the difference would not be passed back to customers. However, the difference would be collected with, the forgone discounts separated from ILEC rate revenue and placed in deferral accounts maintained by the individual ILECs.

During the four year period that the price cap formula was in place, $1.6 billion was collected in deferral accounts in this manner, with most of the money being spent on discounts to competitors to access the digital networks of the ILECs to enable their offerings. Issues associated with the disposition of the remaining funds—$650 million in 2006—have only recently been resolved by CRTC Telecom Decision, after considerable haggling among stakeholders about the costs and

[82] Comments of the Public Interest Advocacy Centre on behalf of the Consumer Groups, January 30, 2004 CRTC Telecom PN 2003-10 (amending PN 2003-8).
[83] CRTC Telecom Decision 2002-34 issued May 30, 2002.

technology of capital projects and form of customer rebates.[84] The implications of the deferral accounts case in relation to the statutory powers of the CRTC are discussed later in this report.

The deferral account controversy was brought about, in part, by the mindset that market conditions could be manipulated by the regulator to ensure competitor success. In this case, rate discounts forgone by residential customers were tossed into the mix to sweeten the pot for new entrants. The result did not appreciably affect competitive efforts, and was well-intentioned but wrongheaded in execution. PIAC's expert, Dr. Johannes Bauer, noted in evidence filed in a proceeding convened to consider the disposition of the remaining deferral account funds:

> Any attempt to keep retail prices artificially high (or, similarly, wholesale prices for network elements artificially low) to accelerate market entry sends the wrong signal to competitors. It may attract inefficient firms and thus contribute to a misallocation of resources and a reduction of economic welfare.

Coupled with a Public Notice announcing the CRTC's intention to regulate ILEC Voice over Internet Protocol offerings (VOIP),[85] the major ILECs'[86] dissatisfaction with the CRTC erupted into a revolt. Internet retail services had been forborne from regulation in accordance with the 1999 Decision of the CRTC[87], and the thought that the ILEC advanced IP networks would be subject to some form of price and service regulation was incendiary for the ILECs.

The CRTC, on the one hand, was eager to try to incent competition, in an effort to advance the objective contained in s. 7 of the *Telecommunications Act* to foster increased reliance on market forces. It viewed the market dominance of the incumbents as a significant impediment to new entrants and wished to jump-start competition by providing a more favourable financial environment for their services. The approach, while controversial, was hardly an outlier for regulatory policy makers. As Mark Armstrong, a leading British proponent of regulatory reform, noted:

> Unless the monitoring of anti-competitive behaviour and incumbency advantages is very effective, it may also be desirable to help new entrants

[84] In accordance with CRTC Decision 2010-637, *Follow-up to Telecom Decision 2008-1 - Proposal by Bell Aliant Regional Communications,Limited Partnership and Bell Canada to dispose of the funds remaining in their deferral account* , some $310.8 million was to be rebated to customers by the ILECs, Bell Canada, TELUS and MTS Allstream, while those same companies were authorized to spend $421.9 million of the accounts for the expansion of rural broadband.

[85] CRTC Telecom Public Notice 2004-2, *Regulatory framework for voice communication services using Internet Protocol.*

[86] This term generally refers to Bell Canada and TELUS but not MTS Allstream. SaskTel generally supported the major ILECs.

[87] CRTC Telecom Order 99-592 respecting retail Internet services.

> into network operation while they build their sunk cost networks to develop an effective competitive challenge to a dominant incumbent.[88]

The ILECs, on the other hand, were beginning to feel the heat from inroads made by new entrant providers in the business telecommunications market. Cable companies had also begun to enter the market for local service with the development of new technology that enabled local telephony through their coaxial cable connection to the home. The sense that they were under siege drove the major ILECs to press for an external review of the telecommunications regulatory framework with a view to reducing what was, in their mind, preferential treatment of competitors, as well as the rules that provided barriers to direct competition with their competitors. Fundamentally, the ILECs sought a world where market forces prevailed, and the equality of treatment and non-discrimination rules would not interfere with commercial responses to customer accounts that promised the highest revenue.

While the public pronouncements of the so-called ILEC revolt were always directed to the potential benefits to their customers that were then ostensibly being foreclosed by CRTC regulation that favoured competitors, CRTC regulation did more than simply attempt to level the playing field between industry stakeholders. In addition to maintaining price control regulation where competition was insufficient to protect consumers of utility services such as local telephony, CRTC regulation also provided quality of service standards, rules for billing and disconnection, customer privacy and obligations to serve. As this report will describe, the ILEC cry for a level playing field was largely successful, with the result of consumer protection as a principal casualty.

[88] Armstrong Mark, Cowan, Simon, and Vickers John, *Regulatory Reform Economic Analysis and British Experience*, The MIT Press Cambridge England, 1997 at p. 207.

Telecommunication Policy Review Panel Appointed

In the spring of 2005, then Liberal Government Minister of Industry, David Emerson announced the formation of a three-person panel to review the state of the telecommunications industry. The job of the Telecommunications Policy Review Panel (TPR Panel) was set out in Minister Emerson's media release:

> The government's objective is to ensure that Canada has a strong, internationally competitive telecommunications industry, which delivers world-class affordable services and products for the economic and social benefit of all Canadians in all regions of Canada.
>
> The panel is asked to make recommendations that will help achieve this objective.[89]

The panel was composed of Dr. Gerri Sinclair, an Internet technology consultant, Hank Intven, an experienced telecommunications lawyer, and a partner in the Toronto office of leading Canadian law firm McCarthy Tétrault LLP, and André Tremblay, a long time telecommunications executive. Non-commercial circles criticized the composition of the panel, given its dearth of public interest representation. Industry Canada provided the secretariat for the panel and it began consultations in the summer and fall of 2005.

The subsequent process and the panel report issued in March 2006 proposed solutions to regulatory issues, invented new paradigms that would be revisited throughout the decade, and continues to inform the ongoing political, industry and regulatory debate. It is accordingly helpful to revisit the cards on the table at the time they were reshuffled by the TPR Panel.

Consumer Groups, represented by PIAC, presented evidence stressing the need to protect consumers and to ensure openness and innovation in the development of information communication technology (ICT) and the supporting networks of delivery. The evidence of Dr. Johannes Bauer presented to the Panel noted the important tasks of regulation:

> The overarching role of regulation is to facilitate the pursuit of public interest goals. More specifically, economic regulation should (1) protect consumers from the abuse of market power; (2) safeguard competition in areas where workable competition does not prevail; (3) ascertain the benefits of ubiquitous availability of telecommunications services.[90]

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[89] Industry Canada, News Release and Backgrounder, April 11, 2005.

[90] Bauer, Johannes, "Expert Evidence/Comments of Dr. Johannes Bauer on behalf of the Consumer Groups (Public Interest Advocacy Centre, the Canadian Internet Policy and Public Interest Clinic, the Consumers Association of Canada, and the National Anti-Poverty Organization)" to the TPR Panel, August 15, 2005, p. 3.

Dr. Bauer's comments set out some important ideas that the Panel should consider in examining the restructuring process:

> Rational telecommunications policy has to allow for the possibility that re-regulation might be necessary. If a market segment develops a high degree of concentration and/or substantially increased entry barriers, re-regulation may be appropriate. A decision should be based on an assessment as to the overall costs and benefits of renewed regulation. Competition analysis will play a strong role in such an assessment.[91]

The principal preoccupation with deregulation as the optimum end state shared by the major incumbent telecom players was also challenged in his evidence:

> Economic regulation is often conceptualized as a substitute for market forces in cases where markets fail or do not yield acceptable outcomes. Whereas this view captures important aspects of regulation, it falls short in important respects.
>
> Most importantly it is based on the mistaken notion that "unregulated markets" exist and that they inevitably result in a superior overall outcome… As demonstrated convincingly by this research,[footnote omitted] throughout history working markets emerged where they were enabled by and embedded in formal and informal rules and norms that are conducive to private initiative and market coordination. In this perspective, regulation is one set of rules that, together with other rules such as legal provisions, antitrust oversight, executive orders, and case law, creates the preconditions for the telecommunications industry and markets to evolve in ways compatible with the broader public interest goals of society. This more appropriate view of regulation has important consequences. It first directs attention away from the question of whether there should be regulation at all to the more relevant question of which set of regulatory or other rules is most conducive to achieve the goals stated in the *Act*. Second, in this perspective, markets and competition are recognized not as goals in and of themselves but as means to realize the objectives stated in the *Act*. Third, economic regulation is more clearly seen as a set of public policies that are not only appropriate in cases of market failure but also in cases of "market deficiency", situations in which the working of markets can be improved by regulation (e.g., where forms of private ordering are afflicted with high transaction costs that could be reduced by regulation). Lastly, sector-specific regulation is properly recognized as one instrument in the toolbox available to realize important public interest goals; whether or not regulation is the best approach needs to be assessed in the context of other policy options (including deregulation).[92]

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[91] *Ibid.*, at p. 4.
[92] *Ibid.*, p. 20

Bauer's evidence was prescient in that it anticipated the deficiencies of the approach that emphasized a forbearance as an on-off switch for regulation with little opportunity to fix practical gaps in service. The Consumer Groups also noted that the clamour for deregulation had yet to produce consumer paradise in the internet and wireless industries, and the difficulties customers experienced in getting redress:

> As for seeking direct redress for individual concerns, consumers have little incentive to approach the CRTC. In the first place, many services, such as wireless and Internet service are forborne. Very little in life is as baffling to the average consumer as being told that although there is a regulator, that the regulator has decided not to regulate, at least not to enforce minimum service standards. In the second place, even with regulated local service, for example, the consumer must resort to the cumbersome and formalistic "Part VII application" under the *Telecommunications Rules of Practice*. [footnote omitted] Few if any consumers have the legal knowledge or the funds to pursue such an application in the CRTC. The process is also not fast; most decisions are reached in over one year and often more. As noted, the CRTC cannot fine companies; it can, however, order restitution of improper charges (again, subject to limits in the tariffs).[93]

The principal ILECs, Bell Canada and TELUS, laid out a deregulatory path designed to insulate them from the regulatory purview of the CRTC, particularly on their future networks. Bell Canada's submission urged the following seven guidelines for change:

> The following seven guidelines should form the cornerstone of a modern telecommunications regulatory framework:
> Guideline One: The current "presumption of regulation" should be replaced with a presumption in favour of the reliance on market forces.
> Guideline Two: *Ex post* regulation should be preferred over *ex ante* regulation wherever possible.
> Guideline Three: Retail price distinctions, including between geographic regions or among customers, should not be prohibited, unless found to be anti-competitive using competition law principles.
> Guideline Four: Regulations should only be applied to retail services if wholesale regulation of bottleneck services is not sufficient to address significant market power.
> Guideline Five: Regulatory regimes should not place marketing restrictions on service providers designed to protect competitors.

[93] Comments of the Consumer Groups (Public Interest Advocacy Centre, the Canadian Internet Policy and Public Interest Clinic, the Consumers Association of Canada, and the National Anti-Poverty Organization) to the TPR Panel, August 15, 2005, p. 134.

> Guideline Six: Competitors should be encouraged – and indeed given incentives – to make their own interconnection and wholesale arrangements free from regulatory review.
> Guideline Seven: Regulation should be restricted to basic and essential services; there should be no economic regulation of discretionary services.[94]

TELUS also had a very limited view of the future of regulation by the CRTC of telecommunications, that was largely bereft of controls or rules save those imposed by competition authorities:

> TELUS' proposals for reform address each element of this objective by recommending significant changes to the institutional and regulatory framework. The CRTC will no longer be expected to play a central role in achieving all of the government's objectives for the telecommunications industry. Rather, competition and market forces, and laws of general application such as the *Competition Act* and the *Personal Information Protection and Electronic Documents Act* will play the role in telecommunications that they now play in other Canadian industries. New approaches to addressing affordability, and service extensions and upgrades in rural and remote areas are also proposed. The CRTC's role will be limited to regulating the provision and pricing of telecommunications services where market forces are insufficient and where there is a need for the provision of telecommunications services to address public safety, security and access to telecommunications services for the disabled.[95]

The whole-hearted wish to escape from the industry-specific regulator, the CRTC, and solely rely on the Canadian competition authorities for market supervision was a recurring refrain voiced by the incumbent telecos during their pursuit of the deregulation agenda.[96] The Competition Bureau itself had fostered this desire, in part, by its propensity to overlook potential problems with deregulation to cheerlead for liberalized markets. This was apparent in many of their submissions to the CRTC in the restructuring period and the statements made both inside and outside the hearing room. General competition law was thus eagerly sought by the ILECs as an alternative to industry-specific regulation.

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[94] Bell Canada's Submission to the TPR Panel, Part D, p. 30.
[95] Submission of TELUS Communications Inc. to the TPR Panel, August 15, 2005.
[96] The submission of the Canadian Cable Television Association (CCTA) to the TPR Panel noted that: "In practice, the only country that has experimented with the complete removal of sector-specific telecommunications regulation and reliance on competition laws is New Zealand. The approach proved to be completely unworkable and in 2001 New Zealand introduced new sector-specific regulation. The New Zealand experiment proved that competition laws of general application cannot be relied upon to implement competition in telecommunications markets that are dominated by an incumbent telephone company."

Another overarching theme from the ILECs that would be repeated throughout the subsequent decade in relevant regulatory proceedings was that not only did the conditions for deregulation exist in the retail market, there was also no need to mandate access to ILEC facilities for new entrants in the wholesale market beyond a brief transitional period. Not only was there no need, but to do so would inhibit the development of facilities-based competition and resultant innovation and efficiency in the telecommunications market.[97]

Many submissions contained much hortatory language about the need to fully embrace ICTs and the gap between ICT adoption in the United States and Canada and its potential effect on the national economy and productivity. Many players tried to link reform of telecom regulation with increased productivity and innovation. Rogers Communications acerbically noted with respect to the Bell effort at such linkage:

> Bell Canada's argument is that Canadian labour productivity levels lag behind the United States by 21%, and that 56% of this gap can be explained by differences in our adoption and use of ICT. According to Bell Canada these "facts" require dramatic action to drive adoption and use of ICT. Aside from a recommendation to accelerate capital cost allowance for computers for business and to establish various studies and advisory groups, the focus of Bell Canada's proposals to redress the problem is to deregulate the local telephone market.
>
> However, no evidence is provided by Bell Canada or Professors Fuss and Waverman to establish a causal link between Canada's telecommunications performance, telecommunications regulatory regime, and lower productivity levels in comparison to the United States. To the contrary, the evidence submitted shows that any productivity gap that might exist is not related to the telecommunications service industry and hence cannot be blamed on Canadian telecommunications regulatory policies.[98]

While urging reform, other competitors attacked the assumptions associated with the ILEC view of deregulation as being synonymous with fostering competition. MTS Allstream recommended:

> The government should direct the CRTC to adopt a policy that boldly and pro-actively implements the new objectives, and to take specific steps to accelerate the conditions under which market forces can eventually govern the provision of services. This does not mean deregulation, which is premature where the incumbents continue to exercise their significant market power in retail markets to pre-empt competition through aggressive targeted pricing and controlling competitors' margins. Rather, it means encouraging competition in whatever form it chooses to take, by making two decisive changes to the regulatory framework:

[97] Submission of Bell Canada to the TPR Panel, September 15, 2000, p. 52.
[98] Submission of Rogers to the TPR Panel, September 15, 2010, p. 19.

a. competitors should be provided with wholesale access to all local access and transport facilities of the former monopolies, including their next-generation networks and facilities, not just legacy bottlenecks labeled "essential" or "near-essential." Technology will continue to evolve, and the framework for interconnection must evolve with it by remaining technology-neutral. This will avoid the costly and unnecessary duplication of facilities and maximize the potential of competition to drive innovation and choice for Canadian businesses and individuals.

b. the CRTC should dispense with its Byzantine system of categorization and pricing of competitor services. The CRTC must firmly regulate the pricing of such wholesale services and replace its current concern with keeping the incumbents "whole" with a focus on placing competitors on the same footing as the incumbents' retail businesses. An approach that creates an "equivalency of inputs" would eliminate the discrimination that currently pre-empts competition.[99]

The CRTC itself, in its submissions to the TPR Panel, tried to focus the debate concerning the need for regulation on market reality when it came to competition:

> Not unexpectedly, the ILECs also resisted any market share loss with all of the tools at their disposal, including "win-back" campaigns targeted at individual customers who decided to switch carriers, as well as various promotions and targeted price reductions designed to recapture any lost customers. While new entrants had to penetrate a market already one hundred percent served by the ILECs, the ILECs could target their marketing efforts in respect of individual customers that chose to leave them, thereby often reversing the customer's decision to switch by offering them a new deal. This conduct, which was impeding the development of a competitive market, prompted the Commission to implement a number of regulatory safeguards designed to restrict the ILECs' retaliatory marketing efforts until competitors managed to get a foothold in the market. Floor prices were also established to prevent the ILECs from dropping rates below cost to undermine new entry.[100]

The CRTC also made some dry observations with respect to the ILEC clamour for ex post regulation:

> As regards the use or *ex post* or *ex ante* approaches, three observations may be offered. First, many of the regulatory safeguards that are currently in place have arisen as a result of complaints regarding conduct of a dominant carrier that was found to constitute a breach of subsection 27(2) of the Act. The second point is that under an *ex post* review approach, the damage can be done to the competitive market by the time

[99] Submission of MTS Allstream Inc to the TPR Panel, August 15, 2005, page 7.
[100] Submission of the CRTC to the TPR Panel, August 17, 2005, para. 75.

> the complaint is made, responded to and ruled upon. Finally, if one looks at the price cap model that currently applies to the ILECs and the tariff streamlining measures recently adopted by the Commission, there are many price changes that can be made by the ILECs without prior notice to the public and without much more than a filing requirement.[101]

The CRTC also expressed caution concerning the eagerness expressed in the TRP consultation paper to design a regulatory structure to fit a view of the telecommunications future:

> The road is littered with technology predictions that have not come to pass and, as the pace of technological change increases, such predictions become more risky to make. It is risky to guess where technology is headed or to influence technological outcomes, and it could be very risky to design regulatory reforms around specific technologies - or to anticipate what the market structure will look like 5 or 10 years out.[102]

[101] *Ibid*., para. 124.
[102] *Ibid*., para. 137.

Telecommunications Policy Review Panel Final Report

The final TPR Panel Report was a far-reaching document that made sweeping recommendations concerning policy and regulation affecting both the composition and methods used by telecommunication regulatory frameworks as well as societal requirements to ensure the proliferation of ICTs. The premise of the TPR Panel Report was that significant changes were needed to Canada's current policy and regulatory approaches that would permit the telecommunications industry to respond more rapidly to new technology and developments.[103]

In large part, the way in which the industry would be enhanced to meet new challenges was by way of solutions that put greater emphasis on market forces. At the same time, the Report sought to marry this concept with the achievement of consumer protection and important social objectives pared down from the laundry list present in s. 7 of the *Telecommunications Act*. Because the Report appeared to accept some key assumptions about the need to quicken the pace of deregulation argued by the ILECs, it is frequently characterized as reflecting a wholly free market approach to telecommunications. A closer reading of the Report reveals its content as a collage, with sections parroting the ILECs' view of the approach to regulation together with more balanced and nuanced visions of the policy and regulatory governance. To some extent, the uneven implementation and policy emphasis of different sections of the Report may have led to harsher criticism than may have otherwise resulted.

For a start, the TPR Panel Report's recommendations on streamlining the objectives in s. 7 of the *Telecommunications Act* caused consternation in public policy circles. The provision in the *Telecommunications Act* reads as follows:

> **7.** It is hereby affirmed that telecommunications performs an essential role in the maintenance of Canada's identity and sovereignty and that the Canadian telecommunications policy has as its objectives
>
> (*a*) to facilitate the orderly development throughout Canada of a telecommunications system that serves to safeguard, enrich and strengthen the social and economic fabric of Canada and its regions;
>
> (*b*) to render reliable and affordable telecommunications services of high quality accessible to Canadians in both urban and rural areas in all regions of Canada;
>
> (*c*) to enhance the efficiency and competitiveness, at the national and international levels, of Canadian telecommunications;
>
> (*d*) to promote the ownership and control of Canadian carriers by Canadians;

[103] Telecommunications Policy Review Panel Final Report 2006, p. 3.

> (*e*) to promote the use of Canadian transmission facilities for telecommunications within Canada and between Canada and points outside Canada;
> (*f*) to foster increased reliance on market forces for the provision of telecommunications services and to ensure that regulation, where required, is efficient and effective;
> (*g*) to stimulate research and development in Canada in the field of telecommunications
> and to encourage innovation in the provision of telecommunications services;
> (*h*) to respond to the economic and social requirements of users of telecommunications
> services; and
> (*i*) to contribute to the protection of the privacy of persons.

The ambit and exercise of the powers of the CRTC was a sore spot that vexed the ILECs in the first place, and while acknowledging the important role of the CRTC in ensuring some social objectives, the TPR Panel Report sought to narrow and constrain the exercise of CRTC powers. Some of this had been done by solutions based on market forces the default choice for setting the terms and conditions of the offering of telecommunications services. As well, the Report recommended the overhaul of the hodge-podge of objectives in s. 7. The TPR Panel Report recommended the following version of the current s. 7:

> *7. It is hereby affirmed that telecommunications performs an essential role in enabling the economic and social welfare of Canada and that Canadian telecommunications policy is based on the following objectives:*
> > *(a) to promote affordable access to advanced telecommunications services in all regions of Canada, including urban, rural and remote areas;*
> > *(b)* to *enhance the efficiency* of *Canadian telecommunications markets and the productivity* of *the Canadian economy; and*
> > *(c)* to *enhance the social well-being* of *Canadians and the inclusiveness* of *Canadian society by:*
> > > *(i) facilitating access* to *telecommunications by persons with disabilities;*
> > > *(ii) maintaining public safety and security;*
> > > *(iii) contributing* to *the protection* of *personal privacy; and*
> > > *(iv) limiting public nuisance through telecommunications.*[104]

There are points of congruity between the current objectives and those proposed above. However, the latter provides a much narrower view of the societal role of telecommunications. One commentator critically noted that the proposed new version:

[104] Telecommunications Policy Review Panel Report, Chap. 2.

> • no longer affirms the role of telecommunications in "the maintenance of Canada's identity and sovereignty," and removes the goals of promoting Canadian ownership and control of telecommunications carriers and stimulating Canadian-based R&D in telecommunications;
>
> • replaces the broadly worded goal-"to safeguard, enrich and strengthen the social and economic fabric of Canada and its regions"-with a much more narrow goal: to enhance the social well-being of Canadians and the inclusiveness of Canadian society," which is further limited to four specific social policy goals (see below);
>
> • replaces "to render ... affordable telecommunications services ... to Canadians" with the weaker "to promote affordable access to advanced telecommunications services ... ";
>
> • removes the policy goal of high-quality, reliable services; and
>
> • limits "social regulation" to four specific social policy goals: access by persons with disabilities, public safety and security (911 service), privacy, and public nuisance (telemarketing).[105]

In fairness to the authors of the Report, the language of the *Telecommunications Act* clearly left the CRTC with far too expansive discretion in determining how to exercise its powers. A large part of the problem came from the broad objectives of the *Telecommunications Act* listed without priority of application in s. 7. One example of the dimensions of this problem came with the CRTC's decision providing and implementing a second generation price cap on local service rates as described earlier. The collection of subscriber monies for local rates that could be spent on an unregulated, and (then at least) operationally unrelated, service that used broadband was a marked departure from the long standing principles of regulation that governed the fashioning of just and reasonable rates, a power that was being exercised by the CRTC pursuant to s. 27 of the *Act*. Customarily, rate setting is an exercise of balancing the interests of the utility with that of the ratepayer by ensuring that the utility recovers prudently incurred costs and a reasonable rate of return.[106] In the decision rendered by Madame Justice Abella in an appeal to the Supreme Court of Canada, the Court found that the language of the *Act* enabled an approach to rate-setting that allowed a more freewheeling approach in exercising rate-making powers:

> This leads inevitably, it seems to me, to the conclusion that the CRTC may set rates that are just and reasonable for the purposes of the *Telecommunications Act* through a diverse range of methods, taking into

[105] Lawson, Philippa,"Gutting the Telecom Act", in *For Sale to the Highest Bidder,* eds. Moll, Marita and Shade, L.S., Canadian Centre for Policy Alternatives, Ottawa 2008, p. 20.

[106] In the case *Puerto Rico Maritime Shipping Authority v. Federal Maritime Commission et al.*, 220 U.S. App. D.C. 13 (1982), the United States Court of Appeals for the District of Columbia noted, quoting Bonbright at p. 20: "Fairness to the ratepayer lies in limiting the rates to that amount which is sufficient but no more than clearly sufficient to cover total cost actually and prudently incurred."

> account a variety of different constituencies and interests referred to in s. 7, not simply those it had previously considered when it was operating under the more restrictive provisions of the *Railway Act*. This observation will also be apposite later in these reasons when the question of "final rates" is discussed in connection with the Bell Canada appeal….
>
> Furthermore, it is required to consider the statutory objectives in the exercise of its authority, in contrast to the permissive, free-floating direction to consider the public interest that existed in *ATCO*. The *Telecommunications Act* displaces many of the traditional restrictions on rate-setting described in *ATCO*, thereby granting the CRTC the ability to balance the interests of carriers, consumers and competitors in the broader context of the Canadian telecommunications industry.[107]

The principle of accountability of the CRTC for monies received from local telephone rates fared little better in relation to the ultimate disposition of the deferral account in light of the *Act*'s provisions:

> In deciding to allocate the deferral account funds to improving accessibility services and broadband expansion in rural and remote areas, the CRTC had in mind its statutorily mandated objectives of facilitating "the orderly development throughout Canada of a telecommunications system that serves to . . . strengthen the social and economic fabric of Canada" under s. 7(*a*); rendering "reliable and affordable telecommunications services . . . to Canadians in both urban and rural areas" under s. 7(*b*); and responding "to the economic and social requirements of users of telecommunications services" pursuant to s. 7(*h*).[108]

The satisfaction that the Court's judgment appeared to side with the CRTC's choices in setting rates, together with the proposed disposition of the funds collides rather forcefully with the reality of what actually occurred. Over $1.6 billion was collected with most of it spent on questionable initiatives to assist the establishment of local competition that did not work, resulting in a broadband program that is still mired in controversy because of Bell Canada and TELUS' plans that appeared to be geared to spending all the funds on their own operations rather than providing an efficient technological fix.

The practical issue that was perhaps occluded by the expansive wording and interpretation of the *Act* was why it was no longer appropriate to provide the balancing exercise between provider and consumer given that the service was still being provided by market dominant ILECs. The analogy made by the court to the subsidization provided by long distance services to local service in the old days of monopoly to justify broadband expenditures was hardly apt: long

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[107] *Bell Canada v. Bell Aliant Regional Communications*, 2009 SCC 40, [2009] 2 S.C.R. 764.
[108] *Ibid.* at para. 75.

distance service used the local network to exist, and this was then a matter of adjusting contribution to reflect that reality, not funding some new unregulated venture.

The judicial deference that has been accorded decisions of statutory tribunals such as the CRTC by Canadian courts can perhaps be criticized, particularly by that stakeholder that have been engaged in tribunal advocacy and have seen what actually transpires or goes into a tribunal decision. However, the examination of this issue in the comprehensive fashion that it deserves would engage more time and resources than can be brought to bear in this report. Suffice to say, it is unlikely that judicial review will be a useful tool in telecommunications to advance public interest complaints where the Supreme Court of Canada is deferential with respect to significant regulatory determinations that are at the core of the tribunal's perceived competence.

The idea of a tribunal such as the CRTC using its powers to determine rates, fees or charges and using the monies in a quasi-governmental fashion to pursue the social objectives of the *Act* thus leaves more than ILECs apprehensive, particularly given the carte blanche interpretation of the *Act* by the Supreme Court of Canada. For consumers, the demise of the well-understood tests associated with the establishment of just and reasonable rates demolishes a bulwark of consumer protection without replacing it with a workable substitute. In *ATCO*, the Supreme Court of Canada determined that ratepayers had no interest in the rate base of the utility. As the majority judgment of Mr. Justice Bastarache noted:

> Thus, can it be said, as alleged by the City, that the customers have a property interest in the utility? Absolutely not: that cannot be so, as it would mean that fundamental principles of corporate law would be distorted. Through the rates, the customers pay an amount for the regulated service that equals the cost of the service and the necessary resources. They do not by their payment implicitly purchase the asset from the utility's investors. The payment does not incorporate acquiring ownership or control of the utility's assets. The ratepayer covers the cost of using the service, not the holding cost of the assets themselves.[109]

We have then the possibility of networks built with customer rates, allowed to charge rates in non-competitive markets to satisfy other national telecommunications demands without reference to the actual costs of service. The extent that the monies derived from customer rates can satisfy such demands is entirely justifiable by reference to the potpourri of objectives in s. 7 of the *Act.* This is not a desirable result.

The question arises as to the appropriate investiture of powers in the CRTC to determine issues that touch upon national objectives. Clearly, the nature of telecommunications is such that the tools provided to the CRTC must be adaptable to a changing environment. On the other hand, the absence of criteria for the exercise of CRTC powers and the low bar true-up required for

[109] *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board)*, [2006] 1 S.C.R. 140, 2006 SCC 4, para. 68.

adherence to statutory objectives makes telecommunications policy somewhat of a high stakes crap shoot.

The TPR Panel Report also attempted to draw a line between economic and social regulation winnowing down the ambit of the societal objectives of "affordable access" and enhancement of "the social well-being of Canadians and the inclusiveness of Canadian society" through measures associates with disabled access, security and safety, nuisance and personal privacy. The Report notes that:

> There should be a clear separation between economic and social regulation with clear identification of the objectives of the regulation and the measures designed to achieve them efficiently rather than using economic regulation to pursue social objectives.[110]

The Report specifically states that economic regulation should only be imposed where it improves efficiency and productivity and only where market forces fail to produce results. It notes three key reasons for the same: (i) significant market power and high prices; (ii) abuse of dominance; and (iii) network externalities. While the latter consideration encompasses the increased value that additional subscribers bring to a network, justifying internal subsidization between customers to maintain universality and affordability, the Report also notes that the additional value of each customer generally decreases as more are added to the network.[111] Part of the deregulation playbook has been the denigration of the value of network externalities that militate for price and quality equivalence throughout the network. Longtime ILEC-retained economic experts, Melvyn Fuss and Leonard Waverman, noted in relation to the issue of subsidy of local service by long distance toll, that hindrance of long distance calling by higher prices might lower the value of network externalities:

> It is insufficient to suggest that theoretically, the existence of call externalities requires a subsidy to access. The issue is empirical since a subsidy is a tax on toll and that tax reduces welfare as well.[112]

On the other hand, the TPR Panel Report also recites the deregulatory mantra of the 1980s that regulation constrains service providers' flexibility, and regulators cannot set prices to maximize benefits from new services or innovations. It warns against restraining the profits of providers that might hinder passing on to customers and warns of the potential problem of providers trying to evade regulatory economic constraints.[113]

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[110] TPR Panel Report Recommendation 3-2.
[111] TPR Panel Report, Chap. 3., footnote 15, p. 3-10.
[112] Fuss, M. and Waverman, L. "Efficiency Principles for Telecommunications Pricing: Fairness for All", in *The Future of Telecommunications Policy in Canada*, ed. By Globerman, Steven, Stanbury, W.T and Wilson, Thomas A., University of British Columbia and University of Toronto, April 1995.
[113] TPR Panel Report Recommendation 3-11.

The TPR Panel Report looked at the presence of significant market power as the fulcrum of economic regulation and the maintenance of constraints on what it terms basic transmission services which is defined as "a service that provides a transmission path between two points along with any functionality required for the path to be used".[114] This definition included local telephone service, long distance and data service. All other retail services were discretionary.[115] Discretionary services were to free of regulatory constraints except those associated with anti-competitive conduct. Basic transmission services were to be forborne from regulation unless there was significant market power.

The TPR Panel Report recommended a framework that looks at an end state where price discrimination between customers, in the absence of significant market power, is not a regulatory concern.[116] The concept of "just and reasonable rate" contained in s. 27 of the *Telecommunications Act* was accordingly to be eased out the door. In effect, when competitive market conditions, not featuring significant market power, produce results that favour one group of customers over others, or fail to achieve other social objectives ("or fairness" as the Report terms it), we should look to other than economic regulation for the solution.

The TPR Panel Report effectively acceded to the view of the major ILECs that telecommunications should be governed by market forces,[117] and only regulated to the extent that was absolutely necessary. It recommended displacing the presumption of regulation contained in the *Act*, with one which placed the burden on the regulator to justify regulation.

In fact, the CRTC's approach to forbearance issues up until that juncture had arguably reflected an approach that had been inclined to lean in favour of finding competitive markets where imperfections in the same existed. The approach was also to refrain from revisiting the same even when there was reason to doubt whether the initial forbearance still applied.[118] For example, the CRTC's decision to forbear from regulating cable basic service (albeit made under the *Broadcasting Act*) reflected a threshold test for competition that pushed the envelope of contestable market theory to an unsubstantiated extreme.[119] The CRTC was similarly incurious about real competition in wireless communications services,[120] and showed no inclination to

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[114] TPR Panel Report Recommendation, 3-13.
[115] The Report recognized that a service may transit from discretionary to basic and vice versa (Recommendation 3-9).
[116] TPR Panel Report Recommendation, 3-12.
[117] TPR Panel Report Recommendation 2-3.
[118] CRTC Telecom Decision 97-19, *Forbearance - regulation of toll services provided by incumben telephone companies*, provided forbearance in a long distance market still clearly dominated by incumbents with a safeguard of continued regulation of basic toll rates.
[119] CRTC Broadcasting Public Notice 1997-25, CRTC Broadcasting Public Notice 1997-25, *New Regulatory Frameworks for Broadcasting Distribution Undertakings* – 5% loss of market share with only 30% competitive coverage.
[120] Deregulated in CRTC Telecom Decision 94-15, *Regulation of wireless services.*

revisit its decision[121] to forbear from regulating the Internet, even though it was clear by this time that, with the decline of dial-up operations, the industry had rapidly become a cosy duopoly shared by the incumbent ILEC and the cable company.

Notwithstanding the ILEC's later claims of over-regulation, the consumer groups had, in fact, been critical of the CRTC tendency to hastily green-light deregulation of a service or regulatory function, and to cease any interest in its performance of the sector following a forbearance decision. There has never been any proceeding, for example, to consider whether the interests of users in a forborne service are still being protected by competition.

The regulatory treatment of the important issue of service quality for customers in forborne regions, set out in the CRTC Telecom Decision 2006-15 illustrated some of the problems caused by a deregulatory emphasis urged by the ILECs and echoed in the TPR Panel Report. Service quality in price-capped and competition-based regimes has traditionally been a matter of intense interest and controversy in the restructuring of utility governance in many jurisdictions.[122] The desire to retain or win new market share may cause management's attention to focus on the cost parameters that will most readily accomplish that goal. As one industry analyst noted:

> Strong pressure to reduce prices or to increase efficiency can have adverse effects on service quality unless specific attention is paid to avoid this.[123]

The approach of the CRTC to this issue, although coming prior to the issuance of the Policy Direction, was also almost exclusively based on competition theory and was perhaps responsive to the prominent ILEC complaints then resonant on the business pages of national newspapers and in the office of the Minister of Industry. In so doing, the CRTC decision ignored previous experience in Canada and elsewhere with service quality.

> The Commission considers that in a competitive market, customers can determine what level of quality is appropriate and will switch providers if the service quality becomes unacceptable. Consequently, the Commission considers that in a forborne environment, it will be in the interest of the ILECs to balance efficiency with service quality in order to offer a product of reasonable quality at a reasonable price. The Commission considers that if an ILEC were to fail to meet its customers'

[121] Telecom Order CRTC 99-592, *Forbearance from retail internet services.*

[122] Levels of service quality may not be easily ascertained by consumers. Incentive-based regimes and competition tend to improve some aspects of service quality (rapid installation of service) while downgrading others (response to trouble calls). See Chunrong Al, "Incentive Regulation and Telecommunications Service Quality," Journal of Regulatory Economics, Vol. 26, issue 3, (2004).

[123] Milne, Claire, "Regulating Quality of Service" in *Telecom Reform, Principles, Policies, and Regulatory Practices* ed. Melody, William Technical University of Denmark, 1997, p. 195.

> expectations for service quality, customers will switch to a provider that offers service of an acceptable quality.[124]

The experience during the first price caps regime showed large scale ILEC non-compliance with quality of service indicators without financial penalty. As the CRTC then noted:

> The ILECs' unsatisfactory quality of service record during the initial price cap regime indicates that measures must be put in place to ensure that customers receive reliable services of high quality. Furthermore, the Commission is not persuaded that competitive pressures in either the retail or competitor services markets will be sufficient to ensure that ILECs will meet approved service quality standards during the next regime.[125]

Nonetheless, the CRTC abolished the enforcement of such standards for local service to customers in forborne areas. In so doing, it accepted the same ILEC arguments that had been refuted in practice during the first price cap period (1998 to 2002) that the threat of competition and the motivation to "protect the brand" would be sufficient to deter poor quality of service:

> The Commission also considers that ILECs generally have an interest in promoting and protecting their brand. The Commission considers, therefore, that the ILECs will be motivated to maintain their retail Q of S in forborne markets.[126]

Whatever the merits of its approach in Decision 2006-15, the CRTC rebuts the ILEC claims of the CRTC's excessive adherence to traditional forms of regulation prior to the issuance of the Policy Direction. One may note that the Decision effectively puts the costs of detection of service quality decrements, remedial requests and potential switching directly onto the backs of individual consumers who may not be as enthusiastic about their potential recourse as the CRTC.[127]

The TPR Panel Report recommendations were clearly driven by the belief that the CRTC had been too slow in its management of the transition of the formerly monopoly industry to a largely competitive one envisioned as the end state. The report also reflected the view that a substantial level of competition had been achieved and that market forces had been successfully providing

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[124] CRTC Telecom Decision 2006-15, *Forbearance from the regulation of retail local exchange services*, para. 443.
[125] CRTC Telecom Decision 2002-34, *Regulatory framework for second price cap period*, para. 74.
[126] *Ibid*.
[127] In a proceeding (CRTC Telecom PN 2008-4) associated with the review of Quality of Service Standards in non-forborne areas, the Consumer Groups introduced evidence of a public survey done by Pollara Inc. in May 2008 across Canada, where 80% of respondents believed that the CRTC needed to enforce quality of service standards for telephone companies. Where there was one provider, 94% agreed that the CRTC should be obliged to maintain reasonable standards. Finally 85% agreed that standards would go down, if the CRTC cannot penalize poor ILEC performance. The CRTC was less than enthused to receive news of the popular disapproval of its decisions and disallowed the cost of the survey in the Consumer Groups' cost award.

what Canadians required. This was presumably unlike those services where "costly and potentially disruptive" government regulatory intervention had been meddling. There was however scant evidence, with the exception of opinion, to back up these beliefs.

A principal difficulty that was inherent in the TPR Panel approach was that there were different levels of risk and costs/benefits to stakeholders associated with the elevation of deregulation or non-regulation to exalted status. The presumption of deregulation that was advocated worked in favour of the best resourced industry stakeholders, and puts the onus on interests in need of regulatory protection to discharge the onus to prove need. There is not only an inbalance of clout, but also of risk associated with that reversal.[128] As Dr. Bauer, on behalf of the Consumer Groups, noted in the CRTC proceedings that examined conditions required for local service forbearance:

> Secondly, the Commission has also heard a lot about the dangers of forbearing too early or too late. This is the so-called Type 1 and Type 2 errors. In our view, the choice between these errors is clear. If the Commission waits longer than is strictly necessary to forbear consumers may be denied some of the benefits of full robust competition. This would be an unfortunate thing, but not disastrous.
>
> On the other hand, if the Commission were to forbear too soon competition could be seriously undermined. Prices could rise and there could be a serious deterioration in quality of service. The timeframe for service initiation or repair could become unacceptably wrong. People could be left without service for days, some people might be even forced to drop their local exchange service if they were in severe financial difficulties. This scenario could easily lead to severe consequences for some Canadians.
>
> In our submission there can be no doubt, if the Commission is to err it should err on the side of caution, it should not forbear too soon.[129]

Even more important was the lack of real evidence that any of the reform measures proposed actually worked. There was little interest in evaluating the success of what had been tried to date, including whether all Canadians had obtained benefits from the liberalization of markets, and whether competition could address existing inequities. As we have seen, there was already considerable evidence of winners and losers from the restructuring design and the recommendations in this area seemed to resemble the deregulatory cant of previous decades.

The TPR Panel Report's shuffling of most social concerns on to the government seemed like a neat way to resolve the problem of prioritizing objectives, on the surface. However, it is far too

[128] In fairness to the TPR Panel Report, the forbearance test of "no significant market power" was more rigorous than any test the CRTC used or had imposed on it by the Cabinet.
[129] Transcript Vol. 3, CRTC Public Notice 2005-2, *Forbearance from regulation of local exchange services*, line 4827.

late in the day, and reminiscent of an industrial age unencumbered by the public interest governance, to pretend that telecom services are simply a commodity whose future production should be directed entirely by concerns associated with efficiency and return on investment. The telecom industry cannot claim a central role in national destiny and at the same time attempt to narrow the importance of the provision of its services by insisting on the unfettered access to customers on terms driven solely by self-interest.

A far wiser course of action might be to ensure that the individual determinations of regulators and policy makers under the governing *Act* are guided by the specific criteria appropriate to that decision, and that in making the decision these objectives or factors predominate in driving the result. For example, in setting rates for a service, traditional considerations of fairness between supplier and customer might well be determinative, while an interconnection decision might bring into play concerns associated with establishment of competition.

It is doubtful that the government completely understands that implementation of this aspect of the TPR Panel Report model means that it will have to backstop more than simply rural and remote customer connection problems in relation to telecommunications services. When a market fails to deliver on the so-called social objectives, policy makers guided by this set of recommendations may find few tools left to attempt to harness network operations with the national interest.

The TPR Panel Report also attempted to tip the scales in favour of the ILEC position with respect to access to incumbent facilities for competitive entry. Prior to the TPR Panel Report, the CRTC had lurched in a number of directions it its rulings on the issue of mandated access to ILEC facilities and networks. Historically, its seminal Telecom Decision 92-12 had allowed interconnection with ILEC facilities to promote competitiveness and lower toll rates.[130] The access went beyond bottleneck facilities:

> The Commission agrees with the view expressed by Unitel that comparable, non-discriminatory access to local exchange facilities and related services and information extends not only to physical interconnection arrangements and dialing plans, but also to ancillary local facilities and services such as billing and collection services, emergency services, directory services, and pay telephones.[131]

However, at the same time that the CRTC was noting that resellers of ILEC facilities had an important role to play in the public interest,[132] it was also stating:

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[130] CRTC Telecom Decision 92-12, *Competition in the provision of public long distance voice telephone services and related resale and sharing issues*, p. 11.
[131] *Ibid.*, at p. 133.
[132] *Ibid*., at p. 126.

> The Commission does not consider that resale and sharing, absent facilities-based entry, would provide a sufficiently sustainable form of competition, given that reseller viability is so dependent on the rate structures of the respondents (ILECs).[133]

Later, the CRTC continued to wish for facilities-based contribution saying:

> …efficient and effective competition will be best achieved through facilities based competition ; otherwise, competition will only develop at the retail level, with the ILECs retaining monopoly control of wholesale level distribution.[134]

In Telecom Decision 97-8, the CRTC acceded to market reality and confirmed that access to essential ILEC facilities was necessary for competition. To be essential, a facility, function, or service must be monopoly controlled, a competitor must require it as an input to provide services, and a competitor cannot duplicate it economically or technically.

The ILECs chafed under the regime provided by Telecom Decision 97-9 claiming that many of the critical inputs supplied to competitors were non-essential. The ILECs claimed this allowed competitors to maximize use of their own facilities leasing only what they additionally required from them and served as a disincentive for investment in their networks, particularly if network innovations must be shared.

The TPR Panel Report largely sided with the ILEC view of the necessity to narrow the mandated access to incumbent facilities, criticizing the approach of allowing access to "near-essential facilities" as critical inputs in the business plans of competitors. It argued that mandated access reduces the need to supply one's own facilities, discourages investment, undermines price levels and undermines facilities-based competition.[135] The Report recommended an end to mandated access of existing non-essential facilities within a five year window.

The Report was obtuse on the possibility of greater entrenchment of the incumbents and the possible development of greater market power and produced scant evidence that there was a market for investments in duplicating the critical inputs otherwise obtained from incumbents. Given the history associated with telecommunications competition in Canada, originating with interconnection and resale, it is somewhat surprising that the Report places so much faith in possible future investments by competitors still existing on the margins.[136]

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[133] *Ibid*., at p. 14.
[134] Telecom Decision 94-19, *Review of regulatory framework*.
[135] TPR Panel Report, pp. 3-32 to 3-37.
[136] The Report does recommend that resellers be given the same status as competitive local exchange carriers with attendant rights of access, interconnection, HCSA subsidies, and telephone number and LNP resources. See TPR Panel Report Recommendation 3-30.

Telecommunications Consumer Agency

The TPR Panel recognized that in the new competitive environment, customer problems may not simply be solved by a switch to a new service provider. As PIAC's 2005 Report on the issue had noted:

> In principle, competitive forces, if sufficiently vigorous, will provide incentives for service providers to be responsive to customers. However, in practice, handling of complaints can be complicated, especially in a large company. Competition, while intense enough to keep prices and terms of service reasonable, may not suffice to take care of individual customer problems. As a result, many industries have set up independent ombudsmen to deal with individual customer complaints.[137]

The TPR Report recognized the increasingly complexity of telecommunications services and recommended a new agency that it termed the Telecommunications Consumer Agency (TCA) be established to protect the interests of Canadian consumers. The TCA should have a structured mandate and resources necessary to do the job without duplicating roles and increasing the regulatory burden.[138] The Report believed that disputes between a customer and the industry should be resolved in a more efficient and consumer friendly manner than the process then in effect before the CRTC.

The TPR Panel Report recommended the establishment of the TCA as a self-funded independent industry agency with its structure and functions determined by the CRTC. The Report advised a governing board with representation from industry, consumer groups and individuals. It also recommended that all TSPs be required to be members of the TCA.

Acting in tandem following the Cabinet's reversal of the CRTC's local forbearance decision, the Commissioner for Complaints for Telecommunications Services (CCTS) was established by CRTC Decision 2007-130 in December 2007 with a permanent Board of Directors for the agency established with representatives from stakeholder groups in June 2008. A permanent Executive Director, Howard Maker, was appointed in 2009 together with approval of its Statement of Mission and Values. In 2010, it commenced a campaign to better acquaint the public with its resolution services. In the year ending in August 2010, CCTS had received over 43,000 public inquiries with 3,747 complaints launched as a result. Its existence and mandate is now under review by the CRTC. This report will make several observations concerning the governance, mandate and future of CCTS below.

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[137] Hariton, George, "Telecommunications Ombudsman for Canada," PIAC, March 2005, Executive Summary.
[138] TPR Panel Report, pp. 6-7.

Institutional Recommendations of the Telecommunications Review Panel Report

The TPR Panel Report reviewed the telecommunications regulatory framework with a view to not only designing a framework for the proper governance, growth, and development of telecommunications and ICTs in Canada but also to ensure that the governing structures have the appropriate tools. Many of these recommendations have been acted on or are in the process of being implemented (i.e. review of the CRTC Rules of Procedure[139]). Others touch upon issues of organization that are not immediate consumer priorities (e.g. registration regimes for licenses for basic international services and certificates of registration among others). The recommendations dealing with new approaches to funding public participation in CRTC proceedings are being considered in part by the CRTC in a recent proceeding[140] and involve issues that have been visited in reports and submissions from Consumer Groups over the last several decades. The gaps in the demand and the ability of the public interest to be adequately represented in telecommunications issues and proceedings are substantial. The bridging of such gaps will likely require a separate study. This report will touch upon this issue again in the recommendations.

There are however important recommendations that have yet to be implemented that deal with the process of appointment of Commissioners, the establishment of an ongoing funded commitment to policy research, CRTC expert assistance, the power of the CRTC to levy administrative monetary penalties, increasing the level of fines under the *Act*, and removal of limitations on rights to sue for damages. The implementation of these measures would help establish the CRTC in a position of greater knowledge, public confidence and an ability to ensure that its decisions are respected. The removal of liability limitations would true up the law with the sea change of the regulatory regime and empower consumers to pursue remedies outside the regulatory process when required.

[139] TPR Panel Report Recommendation 9-28.
[140] CRTC Telecom Notice of Consultation 2009-716, *Call for comments - Review of CRTC costs award practices and procedure.*

Revolt of the ILECs Continued

Bolstered by the TPR Panel report, and the well-known free market sympathies of the new Industry Minister Maxime Bernier, the ILECs conducted a very public campaign against the CRTC and, to some extent, against its chair, Charles Dalfen, over its rulings on Voice over Internet Protocol (VoIP), and the test for forbearance from regulation for local telephone service. In September 2006 in a speech to the Canadian Club, BCE Inc. Chief Executive Michael Sabia accused the federal telecommunications regulator of stifling innovation and limiting consumer choice. Sabia called on the CRTC "to get the message" the federal Conservative government was sending on telecom regulation.[141] In a speech to the Canadian Chamber of Commerce in October 2006, TELUS President Darren Entwhistle called for a "revolution" to overthrow the oversight of TELUS' regulator, the CRTC.[142]

They were rewarded by the actions of the government initiated by the Minister of Industry, Maxime Bernier. First, in June 2006, he proposed a Policy Direction to the CRTC on Implementing the Canadian Telecommunications Policy Objectives and proclaimed the same in December 2006 despite the recommendation of the House of Commons Standing Committee on Industry, Science and Technology to delay implementation pending further study. The Policy Direction incorporated many of the sections of the TPR Panel Report in its provisions, particularly with respect to the mandate to deregulate:

> **Direction**
>
> 1. In exercising its powers and performing its duties under the *Telecommunications Act*, the Canadian Radio-television and Telecommunications Commission (the "Commission") shall implement the Canadian telecommunications policy objectives set out in section 7 of that Act, in accordance with the following:
>
> (*a*) the Commission should
>
> (i) rely on market forces to the maximum extent feasible as the means of achieving the telecommunications policy objectives, and
>
> (ii) when relying on regulation, use measures that are efficient and proportionate to their purpose and that interfere with the operation of competitive market forces

[141] "CRTC behind times: Sabia: Stifling innovation; Bell CEO calls on regulator to bring practices into line with government policy" Montreal Gazette, September 19, 2006 , p. B2.
[142] "TELUS Boss tells CRTC to back off," Ottawa Citizen, October 19, 2006.

to the minimum extent necessary to meet the policy objectives;

(b) the Commission, when relying on regulation, should use measures that satisfy the following criteria, namely, those that

(i) specify the telecommunications policy objective that is advanced by those measures and demonstrate their compliance with this Order,

(ii) if they are of an economic nature, neither deter economically efficient competitive entry into the market nor promote economically inefficient entry,

(iii) if they are not of an economic nature, to the greatest extent possible, are implemented in a symmetrical and competitively neutral manner, and

(iv) if they relate to network interconnection arrangements or regimes for access to networks, buildings, in-building wiring or support structures, ensure the technological and competitive neutrality of those arrangements or regimes, to the greatest extent possible, to enable competition from new technologies and not to artificially favour either Canadian carriers or resellers; and

(c) the Commission, to enable it to act in a more efficient, informed and timely manner, should adopt the following practices, namely,

(i) to use only tariff approval mechanisms that are as minimally intrusive and as minimally onerous as possible,

(ii) with a view to increasing incentives for innovation and investment in and construction of competing telecommunications network facilities, to complete a review of its regulatory framework regarding mandated access to wholesale services, to determine the extent to which mandated access to wholesale services that are not essential services should be phased out and to determine the appropriate pricing of mandated services, which review should take into account the principles of technological and competitive neutrality, the potential for incumbents to exercise market power in the wholesale and retail markets for the service in the absence of mandated access to wholesale services, and the impediments faced by new and existing carriers seeking to develop competing network facilities,

> (iii) to publish and maintain performance standards for its various processes, and
>
> (iv) to continue to explore and implement new approaches for streamlining its processes. [143]

The accompanying notes echoed the essential themes of the TPR Panel Report issued several months previous:

> At present, Canada is facing three key challenges: the telecommunications policy and regulatory frameworks, last modernized in 1993, have not kept up with the rapid pace of technological change; not all Canadians have access to advanced telecommunications networks; and Canadian firms have weak investment in information and communications technologies (ICTs), relative to our global counterparts. The current regulatory framework needs to be modernized if the Government wants to improve the productivity and competitiveness of the Canadian economy and ensure a strong, internationally competitive telecommunications industry.[144]

The pay-off for consumers was somewhat ephemeral and definitely forward-looking:

> At the same time, greater reliance on market forces will allow for greater realization of the benefits of free markets — increased competition and productivity, which in turn has the ability to produce benefits for consumers and businesses alike through greater innovation and investment.[145]

The Policy Direction was one of a number of decisions made at the Cabinet level at the behest of Minister Bernier that altered the regulatory landscape and the approach of the CRTC to the regulation of telecommunications services. In November 2006, in response to a petition to Cabinet, the CRTC decision to regulate VoIP services offered by ILECs over networks that were not their own was reversed allowing them to price and offer such services without tariff approval. In commenting on the decision, Minister Bernier said in a speech to the Economic Club of Toronto:

> We are not here to cause you to waste time with needless regulations and bureaucracy. We are here to help you gain the freedom to seize opportunities, work harder, invest more and prosper ‹ all so that millions

[143] Order Issuing Direction to the CRTC on Implementing the Canadian Telecommunications Policy Objectives, SOR/2006-355, December 14, 2006.
[144] Regulatory Analysis Impact Statement, "Canada's New Government Issues Policy Direction to CRTC that Calls for Greater Reliance on Market Forces," December 18, 2006 at <http://www.ic.gc.ca/eic/site/ic1.nsf/eng/02149.html>.
[145] *Ibid*.

> of Canadian consumers can benefit in quality at the end of the day, and benefit in price at the end of the month.[146]

Next up was the CRTC's decision on the criteria for forbearance from regulation of local telephone service. In April 2006, the CRTC set a requirement for a loss of market share of 25%, together with evidence of rivalrous behaviour and a demonstrated compliance with competitor access rules for forbearance to take place. It had also mandated a basic service price ceiling at the last price capped rate for any forborne local service.

The ILECs were disturbed at the possible long term continuation of local service regulation, disputing the significance of market share. In the proceeding, one of their experts, Neil Quigley, put a new spin on the contestable market theory by challenging whether competition in the product or service market itself was actually necessary for the incumbents to be challenged by the forces of competition possibly unleashed by new technology. This in turn supported the ILEC opposition to mandated access to essential ILEC facilities:

> Where technological change provides a credible threat to the incumbent network, competition from potential providers of local access will force incumbents to invest to preserve their market position, thus providing consumers with greater benefits than competition between actual providers using the same technology.[147]

Bernier responded to the ILECs' petition and public revolt by bringing about a Cabinet Decision allowing forbearance when wireline competition appeared in a local calling area, which was now tailored to permit greater forbearance, and where a wireless competitor not affiliated with the incumbent or competitor wireline operator was also in operation.[148] Rules preventing incumbents from contacting a customer upon learning of their defection to a competitor were also eliminated.

The accompanying Regulatory Impact Analysis Statement to the Decision noted that the ILECs still had a 95% share of the residential phone market. But if this seemed a strange juncture to be exiting price and service regulation, the Statement countered with happy talk and speculation, largely parroting ILEC claims on the subject of local service competition:

> Analyses show that if the revised criteria result in deregulation of retail prices for 60 percent of the population and 55 percent of businesses, for every potential 1 percent change in price, the impact on incumbents' retail customers in aggregate over an entire year could potentially be 29

[146] Speech by the Honourable Maxime Bernier, Minister of Industry to the Economic Club of Toronto, November 15, 2006 at <http://www.ic.gc.ca/eic/site/ic1.nsf/eng/01557.html>.
[147] Quigley, Neil, "Dynamic Competition in Telecommunications", Commentary, C.D. Howe Institute, February 2004 at <http://www.cdhowe.org/pdf/commentary_194.pdf>.
[148] Order Varying Telecom Decision CRTC 2006-15 P.C. 2007- 0532.

> million for incumbents' residential customers and 16 million per year for incumbents' business customers. If competitors were to respond with comparable price changes, the impact on residential and business customers would be even greater. In addition, the elimination of restrictions on "winbacks" and other promotions should enable more innovative pricing and enhance rivalry among competitor companies, thereby potentially reducing overall costs for consumers. While it is possible that over time only a small number of competitors may offer service, this does not mean that consumers' interests will not be well-served. Innovation will be encouraged resulting in more intense competition between traditional telephone companies and competitors such as wireless, cable and voice over Internet Protocol (VoIP) providers. Facilities-based competition is a durable form of competition that will deliver the greatest benefits to consumers, disciplines the market and strengthens investment in telecommunications infrastructure. Specific impacts on individual companies are difficult to predict.[149]

The blue sky approach of Bernier and his Ministry was echoed in large part by the business media, many members of which seemed confused by what was actually at stake in the government's capitulation or embrace of the ILEC revolt. Many simply repeated the victors' talking points:

> This is a very big step for consumers, because you will have much more vigorous price competition," said Mark Goldberg of Mark Goldberg & Associates Telecommunications Consulting. "The big telephone companies can now start to truly compete for your business.[150]
>
> So, a show of hands please: Who is going to miss the Canadian Radio-television and Telecommunications Commission now that is has effectively been told to stop regulating the local phone business? Wait, before you answer that, consider this: Your local phone bill is likely to go down. And the market for your business is about to get a lot more competitive. Anyone?[151]

Others predicted the CRTC's demise:

> And absolutely no one has risen to the agency's defence. Not a word of protest from the Opposition parties, barely a peep even from those whose interests were affected by the decision. The CRTC has no defenders left, no constituency -- and, increasingly, no role. Leaderless, purposeless,

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[149] Media Release, "Canada's New Government Proposes to Accelerate Deregulation of Local Telephone Service in the Interests of Canadian Consumers" December 11, 2006, online: <http://www.ic.gc.ca/eic/site/ic1.nsf/eng/02151.html>.

[150] Tony Wong, "New look to phone landscape Bell, Telus hail move to let them set local phone rates," Toronto Star, December 12, 2006.

[151] Sean Silcoff, "Bernier makes the right call Minister takes 'sensible' action based on markets" Financial Post,Tuesday, December 12, 2006.

> made redundant by the advance of technology and neutered by a determined Industry minister, it's curtains for the commission.[152]

The victors themselves promised a better deal for consumers, scoffing at claims by consumer representatives that Bernier's actions were harmful to ordinary consumers:

> Bernier's decision was necessary and is something Canadians have been asking for, so it doesn't make sense for consumer groups to raise the alarm over the regulatory changes, echoed Shawn Hall, Telus spokesman.
>
> Consumer advocates seem to have missed the point that this is good for consumers and that consumers want it," he said.[153]

No one asked if the market, as the ILECs claimed, was so competitive why they hadn't reduced prices for local service. The ILECs could have done so without Bernier's intervention within rate bands as long as such prices were not predatory. Many members of the media did not realize that price reductions had been in fact possible:

> It's hard to believe that, before yesterday, rules governing the local telephone business meant that Bell, Telus and their peers could not set their own prices in any market until competitors had stolen one-quarter of their business…[154]

The idea that the CRTC had been mandating higher telephone rates and that Minister Bernier was allowing them to be reduced by competition was a message that was successfully spun by the ILECs.[155] While PIAC and other consumer groups decried the changes, the CRTC fell in line with the new regulatory paradigm, and commenced the use of the Policy Direction as a document of Talmudic significance in governing its approach to its responsibilities under the *Act*.[156] In turn, as this report will discuss, the Policy Direction and the other initiatives of Minister Bernier in the late 2006 and early 2007 pushed the debate over telecommunications policy and regulation into a continuing struggle between the extremist proponents of deregulatory ideology and those

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[152] Coyne, Andrew, "CRTC at the Crossroads" National Post, December 13, 2006.

[153] Weeks, Carly, "Consumer groups fight Tory plan to deregulate phone service" CanWest News Service, January 15, 2007.

[154] Silcoff, *supra* note 155. The fact that such reductions would include areas of low or no competition kept ILECs from doing so. The new forbearance conditions would allow the ILECs to target the customers they were interested in retaining.

[155] It still puzzles the media. For example, the editorial "Hold the phone: The trouble with telecom competition," Vancouver Sun, September 16, 2010 reflects the view that the ILECs could not lower rates.

[156] An opinion piece by the author in the December 21, 2006 Wire Report, noted: "It is important to understand what the ersatz telco revolution is really about. The big telephone companies want to charge for their local services on the basis of demand rather than cost, and to have complaints about service resolved chiefly by telling consumers to find another supplier. The companies can then provide discounts in highly lucrative markets while maintaining high prices in smaller, less attractive markets without the annoyance of the public interest."

attempting to salvage meaningful consumer protection and workable competition from a seemingly diminishing horizon of interest in consumer issues.

Effects of the Policy Direction

The Policy Direction admonitions to prioritize deregulation and justify regulation have skewed the regulatory process in ways that are contrary to the objectives of the Telecommunications Act.

The Policy Direction advises reliance on market forces to the maximum extent possible and measures that interfere with market forces to the minimum extent possible to achieve the policy objectives. It also prescribes a series of criteria that should be used to analyze economic (efficient entry), non-economic (symmetrical and competitively neutral) regulation and the necessary circumstances for interconnection. It also mandates a review of mandated access to wholesale services and facilities as well as ongoing streamlining and performance reviews of processes.

At first blush, the language of the Policy Direction sounds like common sense advice much to the effect of "if it ain't broke, don't fix it." In practice, the application of the Policy Direction has been to abjure from fixing, even when the effects of not doing so have a disproportionately negative effect on consumers or ILEC competitors. The Policy Direction has provided the impetus for dismantling the framework of consumer protection in telephony services, carefully built up over years of CRTC decisions without acceptable replacements, in order to comply with the Policy Direction's provisions associated with symmetry and minimal intrusion.

The CRTC set to work on truing up the Policy Direction with the matrix of social and consumer protection regulation issuing Telecom Decision 2008-34 that put these provisions in the cross-hairs of the new instrument:

> In addition, the Commission considers that social and other non-economic regulatory measures that are broadly applied affect a large number of stakeholders and, therefore, should generally be given a higher priority than more narrowly focused regulations. As a result, the breadth of a regulatory measure was another factor the Commission considered in determining the priority for review.[157]

The fate of consumer protections such as the privacy restrictions on ILECs is illustrative of the problems of securing consumer priorities in an environment intent on reducing the regulatory profile. In CRTC Telecom Regulatory Policy 2009-723, the CRTC considered whether to remove the restriction associated with customer confidentiality provisions, set out in Telecom

[157] CRTC Telecom Decision 2008-34, *Action plan for reviewing social and other non-economic regulatory measures in light of Order in Council P.C. 2006-1534*, para. 7.

Decision 2007-13, that prohibited telecommunications service providers (TSPs) from disclosing confidential customer information (CCI) without the express consent of the customer, except in certain specified circumstances. While the CRTC was of the view that the measure furthered the policy objective set out in s. 7(i) of the *Act* by preventing unwarranted disclosure of CCI, it nonetheless allowed TSPs to share CCI with affiliates for the purpose of providing a customer with telecommunications and broadcasting services. The rationale was that because integrated TSPs can do that within their own operations, the Policy Direction requires symmetrical regulatory treatment and thus should allow sharing among the various service entities comprising a TSP bundle without compliance with the necessity of customer consent. The Policy Direction, in effect, trumped the achievement of a statutory objective.

In one case, adherence to the Policy Direction meant that information governed under the unsolicited telecommunications rules or the National Do Not Call List ordinarily published in the telephone directory must be examined to determine if the publication of the same is too onerous.[158] Customer Disconnection and Deposit policies, otherwise in furtherance of the accessibility and affordability objectives in the *Act*, was farmed out to the Commissioner for Complaints for Telecommunications Services (CCTS) so they could be streamlined to comply with the minimal interference with competitive forces required under the Policy Direction. Non-sufficient funds (NSF) and late payment charges, historically the source of customer affordability problems with staying on the network, were forborne under the condition that these rates shall not exceed the lowest rate charged in association with any of its non-tariffed services. It is difficult to say how any of this is in the consumer interest.

While the approach of the CRTC to the apparent necessity of straining the some common sense customer provisions through the Policy Direction colander has not been unreasonable, it is far from apparent why this exercise should occur or continue to occur.

The Policy Direction is hampering successful competitive entry.

Regardless of its merits, CRTC Telecom Decision 92-12 was a bold effort to enable competition by both permitting it to occur, and facilitating its occurrence. By contrast, the CRTC's approach to the task of enabling wholesale access to essential facilities and to net neutrality[159] has been inconsistent and reactive, motivated in large part by the necessity to appear minimally intrusive.

[158] CRTC Telecom Regulatory Policy 2009-156, *Revised regulatory requirements to provide information to customers.*

[159] The TRP Report recommendation confirming "the right of Canadian consumers to access publicly available Internet applications and content of their choice by means of all public telecommunications networks providing access to the Internet." This recommendation is seldom cited by incumbent broadband providers dealing with net neutrality issues.

While the Policy Direction provided potential support for an approach that focused on the end result of greater competition, rather than negating the means of mandated access, the CRTC has evolved positions that seem designed for safe harbour from attack from the political wing of telecom governance, rather than effectiveness. On the one hand, its 2008 Essential Services Decision seemed to provide a practical basis for mandating access requiring that such a facility meet the following conditions:

> 36. (i) The facility is required as an input by competitors to provide telecommunications services in a relevant downstream market;
>
> (ii) The facility is controlled by a firm that possesses upstream market power such that withdrawing mandated access to the facility would likely result in a substantial lessening or prevention of competition in the relevant downstream market; and
>
> (iii) It is not practical or feasible for competitors to duplicate the functionality of the facility.
>
> 37. With regard to future applications to consider the essentiality of a non-mandated service, the definition will read as follows:
>
> To be essential, a facility, function, or service must satisfy all of the following conditions:
>
> (i) The facility is required as an input by competitors to provide telecommunications services in a relevant downstream market;
>
> (ii) The facility is controlled by a firm[6] that possesses upstream market power such that *denying* access to the facility would likely result in a substantial lessening or prevention of competition in the relevant downstream market; and
>
> (iii) It is not practical or feasible for competitors to duplicate the functionality of the facility.[160]

However, the CRTC approach to broadband access and net neutrality, on the whole, has been timid: the customers of independent ISPs have parity with the customers of the facilities-based provider but the CRTC is unwilling to provide competitors with access to technical arrangements called CO-based ADSL access service. The advantage of such an arrangement, if it were brought into being, would be to allow an independent ISP to get connected before the traffic management measures are imposed by the incumbent carrier and thus offer services that would be different from the facilities based ISP.[161] The CRTC had originally ordered new wholesale access being

[160] CRTC Telecom Decision 2008-17, *Revised regulatory framework for wholesale services and definition of essential services*, paras. 36 and 37.
[161] CRTC Telecom Regulatory Policy Decision 2010-632, *Wholesale high-speed access services proceeding.*

CO-based ADSL access service[162] only to accede to a review and vary application from Bell Canada et al. to withdraw the classification as conditional essential. Notably, its most recent speed-matching decision came after the Minister had requested reconsideration of its initial decision based on considerations such as competitive disadvantage, incentives for investment that are featured in the Policy Direction.

There is good reason for believing that the Policy Direction hinders the development of services on advanced network and drives the inevitability of the incumbent model of facilities-based competition, a made-in-Hollywood scenario for a duopoly.[163] The Policy Direction is drawing collateral support in its obstruction from the theoretical economic constructs associated with the predicted behaviour of competitors denied access to incumbent networks. There is no reason that the essential facilities criteria that was set out in the CRTC's 2008 Decision requires the additional gloss provided by the Policy Direction to make competitive advanced network services a reality.

The Policy Direction has encouraged irresponsible industry conduct and an approach that is reactive to interference with business plans.

The requirement that the CRTC rely on market forces to the maximum extent possible and use measures that interfere with competitive market forces to the minimum extent has emboldened industry stakeholders to advance positions inside and outside the hearing room that disclose an aggressively combative attitude towards regulatory measures including the process itself. Since the Policy Direction, it is not a rare occurrence for interrogatories directed to ILECs to be answered with responses that indicate that the answers are not required because of the Policy Direction. Applications to review and vary CRTC Decisions under Part VII of the Act proliferate with the frequent assertion that the Policy Direction demands adherence and a reversal of the impugned decision. Appeals to Cabinet from CRTC decisions on similar grounds under s. 12 of the *Act* have also increased. Together with the precedents of the previously described political intervention earlier in the decade, the net effect has created uncertainty and weakened the authority of the regulator.

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[162] CRTC Telecom Decision 2008-17, *Revised regulatory framework for wholesale services and definition of essential services*.

[163] Eli Noam in a April 25, 2007 article for the Financial Times "Public Telecoms 2.0: The Return of the State" noted: "The result (of deregulation) has been an industry structure dominated by big incumbents, surrounded by a number of energetic but small rivals whose survival is largely based on protection by the regulator, and who are mostly using the infrastructure of the incumbent and reconfiguring it. One could attribute this dominance to some globally pervasive conspiracy among incumbents and captured regulators. Or, more credibly one could attribute it to some fundamental workings of network industries, in which economies of scale and network effects combine to give advantages to the largest firms."

Backed up by the non-interventionist credo of the Policy Direction, stakeholders feel increasingly free to blatantly pursue self-interest in regulatory matters in opposition to *Act* objectives. In recent proceedings dealing with universal service obligations and the provision of basic service, Bell Aliant rather aggressively indicated that it could not maintain its current service obligations in its franchise territory, distributing photographs of its smashed towers and other disabled facilities. Its representatives noted that they also had no plans to supply broadband service to certain non-urban areas of their territory in the future despite rather pointed questions from the hearing panel.[164]

The Policy Direction has no provision for review of its effect.

There has been no review of the effects of the Policy Direction towards the achievement of its objectives nor is one planned, except for recitals associated with the withdrawal of regulation. How do we know whether consumers are better off, whether efficiencies have been achieved, whether innovation has been promoted and whether competitive markets have been achieved? The CRTC produces it annual "Communications Monitoring Report," but it does not provide the basis for subsequent action to examine its decisions in response to the same. The 2007 *Cabinet Directive on Streamlining Regulation* provides:

> Departments and agencies are to regularly assess the results of performance measurement and evaluation to identify regulatory frameworks in need of renewal. Once identified, departments and agencies are to examine the regulation with a focus on:
>
> • the effectiveness of the current regulation in meeting the policy objective;
> • the current instrument selection, level of intervention, and degree of prescriptiveness;
> • clarity and accessibility of the regulation to users; and
> • the overall impact on competitiveness, including trade, investment, and innovation.[165]

Contrary to current understanding in some quarters, the Policy Direction reflects the way in which objectives are to be met, not the final objectives themselves. It is necessary to go through the exercise contemplated by the *Cabinet Directive on Streamlining Regulation* to make sure that the Policy Direction got it right. This has never been done. There are some real market indications, however, that consumers are still not getting the promised or optimum results from the regime of competition and diminished regulation since restructuring began.

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[164] CRTC Telecom Notice of Consultation 2010-43, *Proceeding to review access to basic telecommunications services and other matters.*
[165] *Cabinet Directive on Streamlining Regulations*, 2007, pp.10-11.

Consumer Update on Telecom Services

As we have noted above, similar to most decisions along the path of industry restructuring, there has been little examination of the consequences of the Policy Direction and the reversals of CRTC decisions that took place three years ago. Because of the general expectation of consumer benefits arising from the government imposition of terms for local service forbearance, it might be useful to start here.

From 2007, the new imposed terms for forbearance were used to deregulate local telephone exchanges in Canada. As of June 2010, local service forborne from regulation included 77% of residential telephone lines and 68% of the business lines.[166] This includes Canada's 30 largest cities. It is also known that 71% of local and access revenues come from forborne areas. Nationally, ILECs have hung onto approximately 63% of the wireline revenue from retail business and residential services. If the predictions of consumer savings and deals were correct, they should be showing up in urban areas. This does not seem to be the case. Using 2007 data from the CRTC and information obtained from ILEC representatives themselves in August and September of this year, the chart below was made to illustrate that consumer savings have not been achieved. It reflects both local basic rates in the Bands shown as well as the price for the two most requested local options, voice mail and call display.

[166] Katz, Leonard, Vice-Chairman, Telecommunications Canadian Radio-television and Telecommunications Commission to the Canadian Telecom Summit panel on "Building Digital Canada" Toronto, Ontario, June 8, 2010.

Figure D. Comparison of Rates for Residential Primary Exchange Service – 2007 and 2010

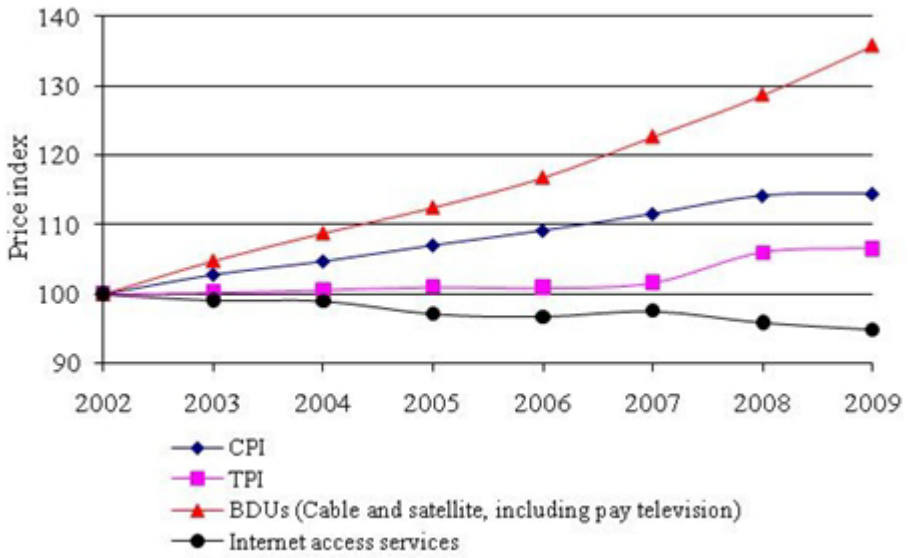
CITY	BAND	YEAR	RATE for RESIDENTIAL PES	VOICE MAIL	CALL DISPLAY
Montreal (Bell)	B2/A2	**2007**	**$22.00**	$7.00	$6.00
		2010	**$25.33**	$8.95	$8.95
Ottawa (Bell)	B1/A1	**2007**	**$21.20**	$7.00	$6.00
		2010	**$27.93**	$8.95	$8.95
Toronto (Bell)	B2/A2	**2007**	**$22.00**	$7.00	$6.00
		2010	**$27.93**	$8.95	$8.95
Winnipeg (MTS)	Core A / Suburban B	**2007**	**$23.85**	$5.50 Basic $6.70 Plus	$6.10
		2010	**$24.49**	$3.50 - $10.95	$7.50
Vancouver (Telus)	A1 / B4	**2007**	A1 **$25.04** B4 **$26.90**	$2.95* Basic $4.95* Enhanced + $.10/ use charge.	$7.95
		2010	**$27.18**	$6.95	$7.95
Edmonton (Telus)	A/B	**2007**	**$23.23**	$4.95* Basic $6.95* Enhanced + $.10/ use charge.	$7.95
		2010	**$23.95**	$6.95	$7.95
Halifax (Bell)	A1/A2	**2007**	**$25.00**	$8.00	$8.00
		2010	**$25.82**	$6.95	$8.95

[Source: Collected by PIAC][167]

The data collection exercise shown above appears to line up well with data in the CRTC 2010 Communications Monitoring Report:

[167] Collection of data was done by telephone interview with ILEC representatives and retrieval of tarriff information from the CRTC .

Figure E. Price Indices [TPI[1], BDU[2] (cable and satellite, including pay television), Internet access services, and CPI]



Notes: 1.The TPI reflects the price changes experienced by a household for a basket of telephone services. The basket of telephone services reflects a weighted-average of consumer expenditures on basic local service, other local services (such as options and features), and long distance, installation, and repair services. However, TPI does not include wireless or Internet service expenditures.

2. The BDU price index reflects the price changes experienced by a household for a basket of cable television service. The basket includes both 'Basic' and 'Extended' cable services. Basic cable service is the minimum service to which all customers must subscribe. Extended service is the most popular package of additional channels. The index does not account for 'bundling discounts'.

[Source: Figure 5.1.10 of the CRTC 2010 Communications Monitoring Report]

The TPI line in the graph reflects that there was no outbreak of consumer savings arising from deals on local service and local service options that should have emerged from the local service forbearance that was much sought after and that was expected by Minister Bernier. Given that the CRTC imposed ceiling on stand- alone basic service, the price performance is particularly dismal given the expectations. These results may also reflect the implications of the consumer complaint that the ILEC provider considers the basic service price ceiling to be inapplicable if telephone service is purchased in a bundle with Internet, wireless or TV services.

A recent CRTC report acknowledged the illusory nature of the benefits promised by swift local service and BDU deregulation urged so fervently by the industry incumbents:

> Although it requires further study, it appears that bundling strategies are having the effect of enabling service providers to maintain price levels. The following figure demonstrates that, with the exception of Internet pricing (which has fallen slightly), telephone and BDU pricing has been on an upward trajectory in comparison with the overall consumer price index.[168]

It is not altogether speculative to deduce that the remaining efforts at price control in the form of the price ceiling on basic stand alone local service and the administration of the price cap in non-forborne areas have coaxed the best overall performance for wireline services measured against world standards particularly in the low use end than any deregulated service.[169] It would appear that this had nothing to do with Minister Bernier's reversal of the CRTC local forbearance rules.

Retail internet services were forborne from regulation in 1997 by the CRTC at a time when numerous internet service providers (ISPs) furnishing dial-up Internet services existed. The advent of the broadband standard for internet service and its overwhelming provision by cable companies and ILECs has only created a largely unregulated duopoly with attendant results for customer price and choice. The decision to forbear has never been reviewed in light of the market change. A 2004 Pollara survey showed that almost two-thirds of Canadian consumers thought that the government should develop and enforce consumer protection rules for Internet services. Then, as it is now, the biggest concern of those desiring consumer protection rules was service quality.[170] Going forward, the issue likely to predominate the consumer concerns associated with Internet services is the maintenance of "network neutrality,"—the operation of the network in a manner that does not impede, block or slow the flow of content, services or applications or impair the functioning of devices connected to the network.

Not unexpectedly, however, Canadian broadband offerings show, at best, mediocre value in relation to international standards.[171] A recent controversy is illustrative of the lack of effective competition in the broadband market. Rogers Communications reduced its customers' internet download limits in order to squeeze Netflix, an internet streaming subscription service, that is a potential competitor for the delivery of video services with other Rogers' services such as cable, pay-per-view, and video rental services. The reduction of service, which is effectively a price

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[168] CRTC, "Navigating Convergence: Charting Canadian Communications Change and Regulatory Implications", February 2010, para. 125.
[169] Wall Report, p. 9.
[170] PIAC, "Consumer Issues with Internet Service: Is Self Regulation Working", August 2004, p. 62.
[171] See the report of Berkman Center for Internet and Society at Harvard University, *Next Generation Connectivity: A review of broadband Internet transitions and policy from around the world* (February 2010), online at <http://cyber.law.harvard.edu/sites/cyber.law.harvard.edu/files/Berkman_Center_Broadband_Final_Report_15Feb2010.pdf>. See also the Organization for Economic Co-operation and Development (OECD), *OECD Communications Outlook 2009*, online at <http://www.oecd.org/document/44/0,3343,en_2649_34225_43435308_1_1_1_1,00.html>.

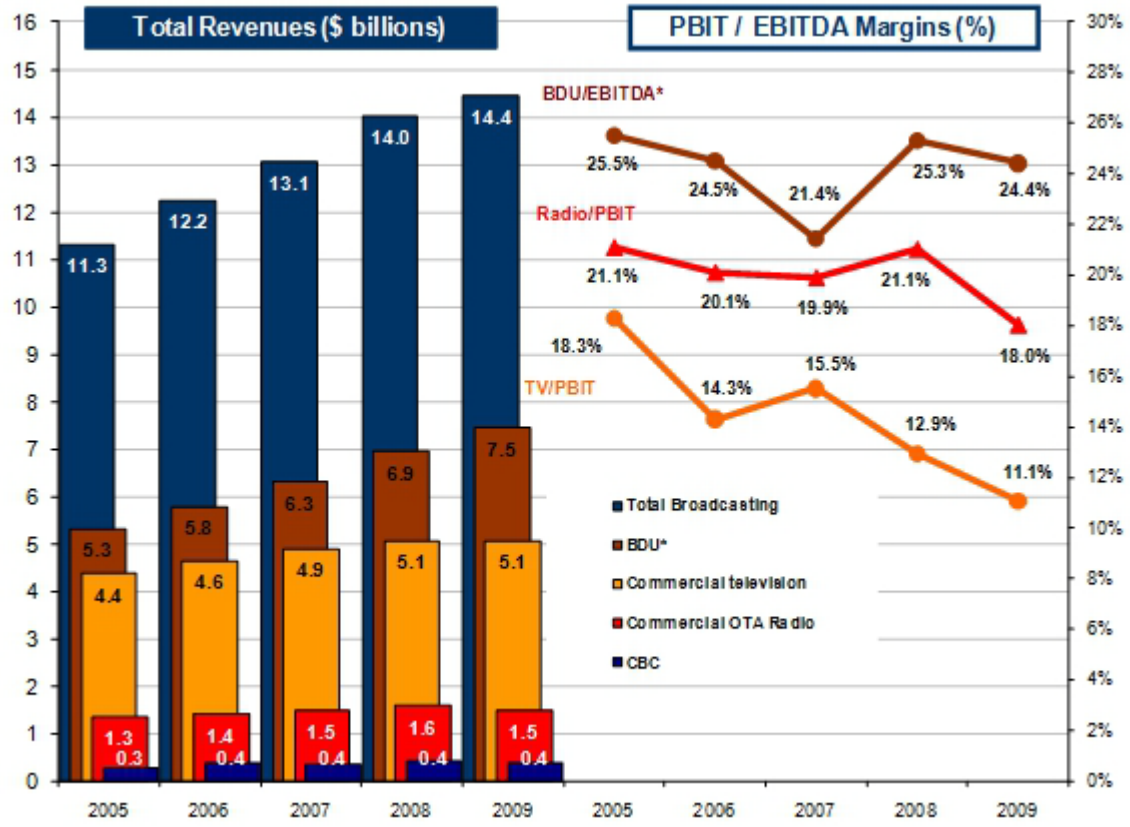
increase, was made ostensibly without concern for loss of market share, a prime indicator of dominance by a vertically integrated player in a market that is supposed to be competitive.[172]

Cable broadcast distribution undertakings (BDUs) have been a particularly egregious example of premature deregulation leading to the exploitation of a dominant position. In 1997, the CRTC allowed basic cable service to be deregulated if a competitor obtained 5% of the BDU franchise market and provided a service that was available to 30% of the market.[173] The incredibly low threshold for effective competition prompted an eventual avalanche of BDU basic service forbearance applications. However, unlike the normal economic expectation of price decreases in competitive markets, cable basic service skyrocketed in price, in some cases doubling within a decade of the CRTC's deregulation decision. BDUs crammed additional offerings (that were often owned by the BDU) into the basic service package, and passed on price escalations to boot. In the result, cable and satellite BDUs experienced customer revenue increases and profitability levels that were beyond reasonably expected levels in a competitive market. The 2010 CRTC Communications Monitoring Report illustrates the effect of the escalating prices for BDU services shown in Figure E above. The BDU deregulation picture clearly shows the dangers of faith- based economics based on untested theories of contested markets, as well as the overall failure to review and learn from mistakes when consumers are the stakeholders most affected by the mistakes. Despite the handsome returns currently and historically exhibited by BDUs, when the CRTC imposed an additional contribution on the BDUs to the Local Programming Fund to assist local broadcasting in 2008, there was little hesitation on the part of the BDUs in passing on the fee to their subscribers.

[172] Hui, Joyce, "Rogers' anti-competition plans to cap bandwidth limit," Open Media, July 27, 2010 at <http://openmedia.ca/node/1516>.

[173] CRTC Broadcasting Public Notice 1997-25, *New Regulatory Frameworks for Broadcasting Distribution Undertakings.* This rather bizarre foray into competition law principles unfortunately became a precedent for a low threshold for forbearance of services in telecom given the rivalry between cable and ILECS and the demand for equal treatment.

Figure F. Total broadcasting revenues and PBIT/EBITDA margins



[Source for Chart: Figure 4.1.4 from 2009 CRTC Communications Report]

We have included as an Appendix to this report an edited version of the Public Interest Advocacy Centre's brief presented to the Senate Standing Committee on Transport and Communications on October 7, 2009. Generally, independent studies have generally confirmed the very poor to ordinary performance of Canada's wireless carriers in delivering value. For example, a recent study done by the New America Foundation showed Canada at or near the top in prices for low-tier packages for phone, data and text services delivered in a wireless mode.[174] The following charts are taken from that study.

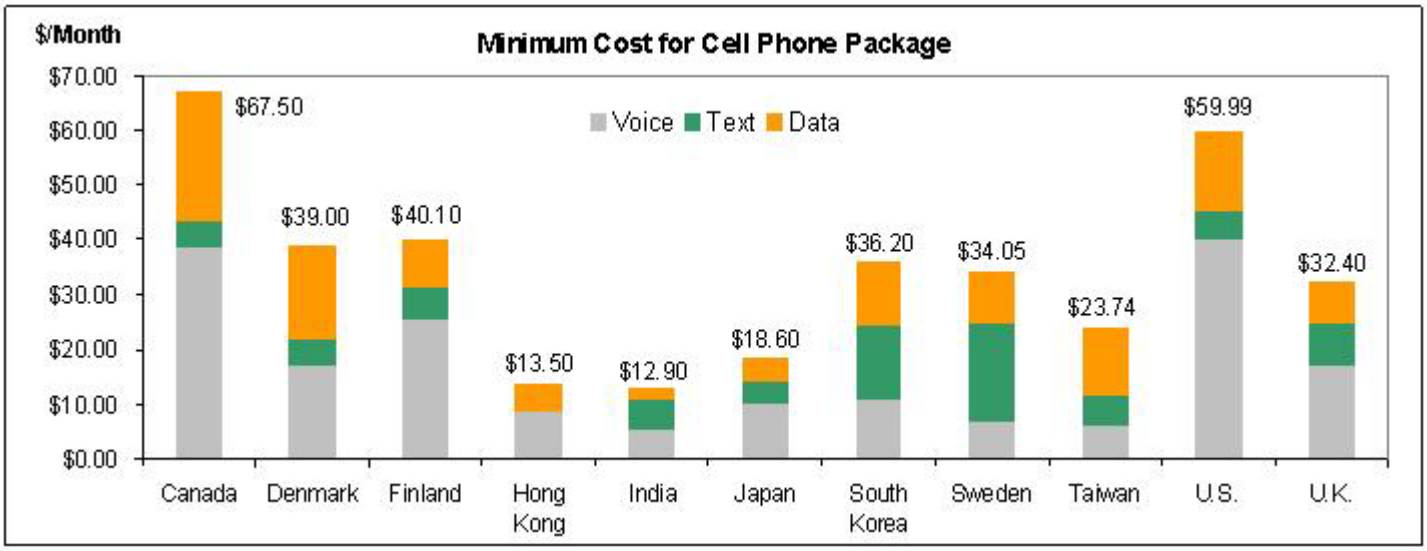
[174] Chiehyu Li, Bincy Ninan, "An International Comparison of Cell Phone Plans and Prices," New American Foundation, October 14, 2010 at <http://oti.newamerica.net/publications/policy/an_international_comparison_of_cell_phone_plans_and_prices>.

Figure G. International Comparison of Low Tier Wireless Bundled Packages

$/Month	Voice	Text	Data	Total
Canada	$38.70	$4.80	$24.00	$67.50
Denmark	$17.00	$5.00	$17.00	$39.00
Finland	$25.50	$5.70	$8.90	$40.10
Hong Kong	$8.50	N/A	$5.00	$13.50
India	$5.40	$5.40	$2.10	$12.90
Japan	$10.10	$3.80	$4.70	$18.60
South Korea	$10.80	$13.40	$12.00	$36.20
Sweden	$6.75	$17.80	$9.50	$34.05
Taiwan	$5.94	$5.80	$12.00	$23.74
U.S.	$39.99	$5.00	$15.00	$59.99
U.K.	$17.00	$7.70	$7.70	$32.40

[Source: New American Foundation Study 2010]

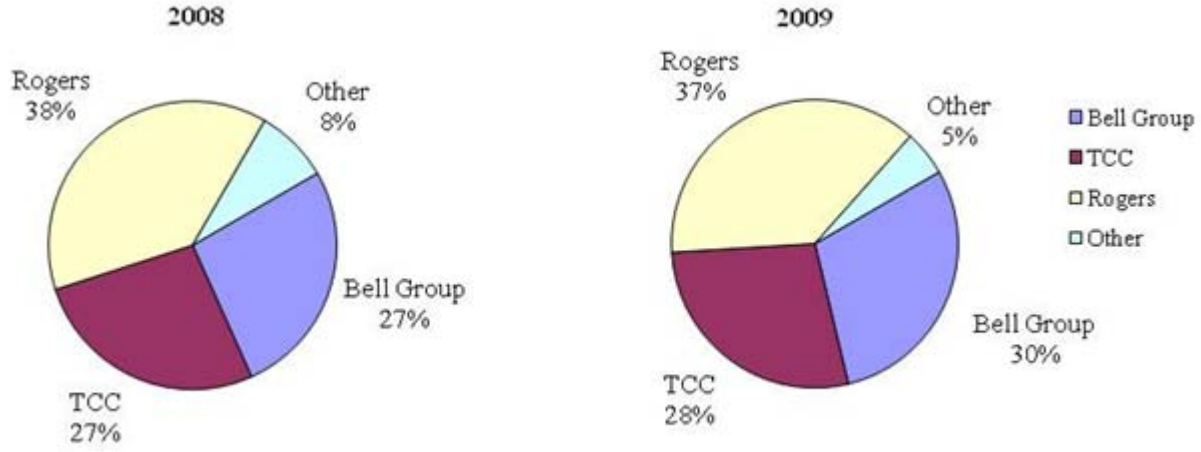
Figure H. International Comparison of Minimum Cost for Cell Phone Package



[Source: New America Foundation 2010 Study]

The wireless industry picture in terms of competitiveness has not been ideal. The market concentration that prompted the decision of the federal government in 2008 to set aside spectrum remained a significant feature of Canadian wireless markets in 2009. The figure below taken from the 2010 CRTC Communications Monitoring Report details the 2008 and 2009 market shares in the wireless industry.[175]

Figure I. Wireless TSPs' subscriber market share



[Source: Figure 5.5.7 from 2010 CRTC Communications Monitoring Report]

Wireless service itself does not seem to be compensating for non-competitive rates. Wireless complaints now make up 51% of the complaints handled by CCTS and increasing consumer unhappiness about one-sided wireless contract terms have spurred the adoption of legislation in Quebec that provides for relief against termination fees. Bill 60 that came into effect in June 2010 provides that termination fees on sequential wireless contracts will be based only on the subsidy that carriers provide to clients. The subsidy amount is the difference between the cost of the device paid for by the service provider and the price the consumer paid for the device when entering into a long-term contract.[176]

In Ontario, a private members bill, Bill 133, proposed to go further in requiring that wireless services:

[175] Note that a study by the Communications, Energy and Paperworkers Union of Canada (CEP), "Foreign Ownership in Canadian Telecommunications" uses Canadian average monthly minutes and several other in-country adjustments to perform a usage basket comparison that improves Canada's wireless performance to fifth among the OECD. The study suggests that wireless is a natural monopoly and foreign investment will likely lead to consolidation, not new competition.

[176] Bill 60, *An Act to amend the Consumer Protection Act and other legislative provisions*, 2009, ch. 51, 39th Leg., 1st Sess., new sections 214.1 to 214.11. The Bill also prohibits unilateral amendments to contracts governed by the *Consumer Protection Act*.

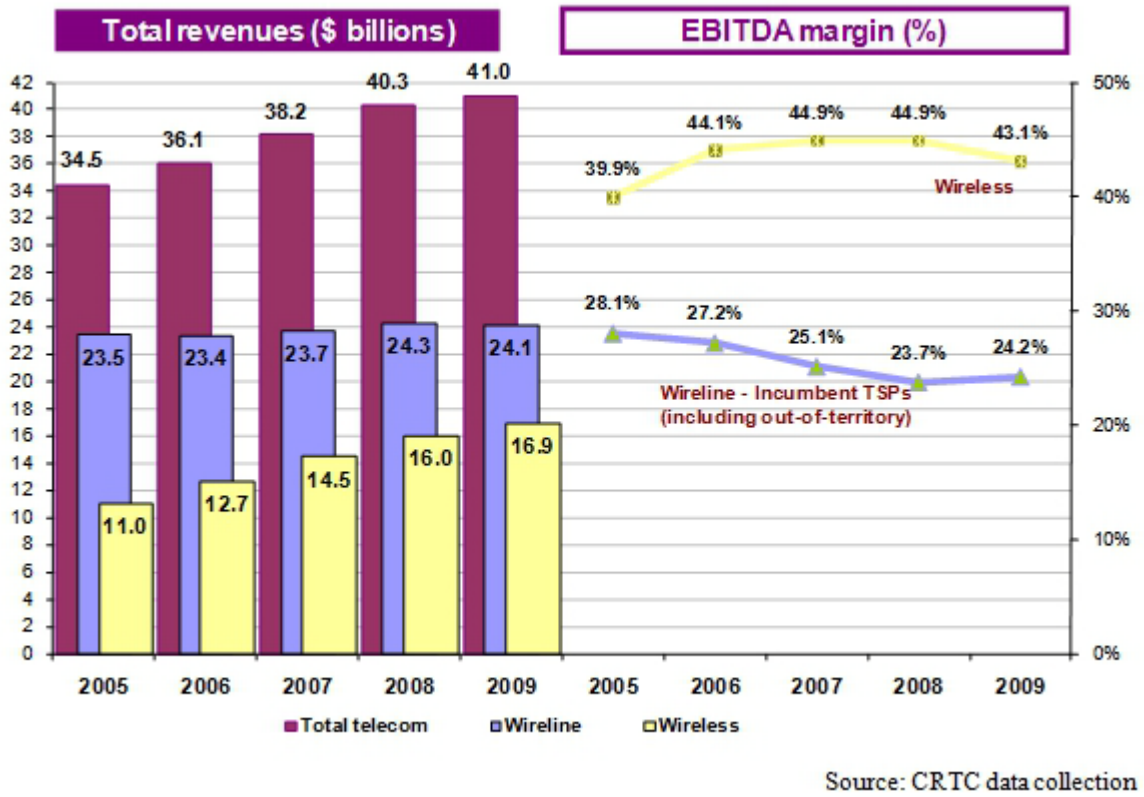
- Clearly disclose the cost of all optional and mandatory services included in an agreement
- Provide service agreements in plain language, making them more understandable to consumers
- Reduce the cancellation fee charged to consumers
- Improve transparency regarding automatic renewal
- Notify the consumer when they may incur additional charges as a result of exceeding usage limits
- Eliminate activation dates and expiry dates on pre-paid cards for wireless service
- Make costs more transparent when advertising the price of wireless services
- Unlock any device that has been paid for in full or is no longer bound by a service agreement.[177]

While the demand for action may be partly the result of the rise in importance of wireless services in Canadian life, it is interesting to note that earlier in the decade, the wireless industry was frequently cited as the poster child for an appropriately competition-disciplined telecommunications service. Today, the success is mainly reflected in the whopping industry profits. As the figure from the 2010 CRTC Communications Monitoring Report shows below, wireless providers are faring very well indeed, whatever the market treatment of their customers. While their industry association, the Canadian Wireless Telecommunications Association, has scrambled to head off consumer protection legislation with its voluntary 2009 Wireless Code of Conduct, it is clear that customers expect clear inroads into the chronic problems of non-transparent billing and excessive extra charges such as roaming charges and made-up additional charges such as the "government regulatory charge."[178]

Incumbent wireless operators have countered new entrant providers who acquired spectrum in the 2008 Industry Canada wireless auction by introducing discount fighting brands to attempt to capture a share of the discount market and squeeze new entrants.

[177] Bill 133, *Wireless Phone, Smart Phone and Data Service Transparency Act*, 2010, Ontario.
[178] This fee replaced the "system access fee" for Rogers Wireless Service.

Figure J. Telecommunications revenues and EBITDA margins



[Source: Figure 5.1.7 of the 2010 CRTC Communications Monitoring Report]

This strategy has attracted the ire of the new entrants as anti-competitive margin squeezing. Mobilicity has filed a complaint to the Competition Bureau concerning Rogers Chatr service.[179] The Chatr service faces a $10 million fine proposed by the Competition Commissioner to the Competition Tribunal for misleading advertising concerning quality of service.[180]

The irony of the era of restructuring and rule by market forces is that there is greater concentration than ever in the telecommunications and broadcasting environments. The 2010 CRTC Commmunicatinos Monitoring Report shows that a small number of companies account for 94% of the telecommunications revenues.[181]

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[179] "Mobilicity files complaint against Rogers' Chatr" CTV News, September 8, 2010 at <http://www.ctv.ca/CTVNews/SciTech/20100908/mobilicity-rogers-chatr-100908/>.
[180] "Rogers faces $10M fine over dropped-call ads", CBC News, November 19, 2010 at <http://www.cbc.ca/consumer/story/2010/11/19/consumer-chatr-rogers-competition-bureau.html>.
[181] CRTC Telecommunications Monitoring Report 2010, Part 5.10.

Figure K. Telecommunications Service Industry at a Glance

	2008	**2009**	***Growth***
Telecommunications revenues ($ billions)	40.3	41.0	1.8%
Percent of total telecommunications revenues			
Top 5 ILECs	66%	66%	
Top 5 cable companies	26%	28%	
Top 5 resellers	2%	2%	
Capital expenditures ($ billions)			
Wireline	5.9	5.7	-2.9%
Wireless	6.1	2.2	-63.0%
Earnings before interest, taxes, depreciation, and amortization margin (%)			
Wireline	24%	24%	
Wireless	45%	43%	
Average retail revenues per line per month1			
Wireless	$59	$58	-1.7%

Note: 1. Total retail revenues divided by total retail lines divided by 12.

[Source: CRTC data collection – 2010 CRTC Communications Monitoring Report]

Four major broadcasting networks are owned by a telecommunications company, and the BDUs are heavily entrenched in the practice of owning their own channels that are promoted as basic or additional service. Internet content producers squabble with broadband providers about internet throttling and packet prioritization. It is hard to remember the accepted wisdom of 15 years ago from the Final Report of the Information Highway Advisory Council:

> **Recommendation 7.7.** The principle of carriage/content separation should be maintained, at a minimum, through the requirement of structural separation between programming and distribution undertakings and other reasonable safeguards.[182]

If objective measures of consumer success in the retail telecommunications market are reviewed, a reasonable conclusion is that the current methods of regulation and competitive delivery of

[182] "The Challenge of the Information Highway", Final Report of the Information Highway Advisory Council, 1995.

telecommunications services are not working very well.While the government, the regulator, and the industry winners are brimming with enthusiasm about the progress of deregulation,[183] for ordinary residential consumers, it seems obvious that the benefits of restructuring to date have primarily devolved to other stakeholders in the market. To compound the inequities, the regulator and policy makers are handcuffed by a Policy Direction that is both an impediment to competition and a hindrance to effective consumer protection.

If regulation was a business whose success or failure was dependent on delivering results for ordinary Canadian consumers, it would currently be in receivership. The challenge for consumers is to restore balance to the regulatory ecosystem so that the telecommunications objectives can be respected in preference to potential regulatory burden.

[183] Competition proponent and McGill Professor Richard Schultz swooned over the courage of Minister Bernier outmuscling bureaucrats and regulators in his forbearance decision although Minister Bernier had no knowledge of telecommunications before becoming Minister. His article discloses how the Minister worked in tandem with the major ILECs to get his way. Shultz, Richard, "Maxime Bernier, the Yes Minister," National Post, May 29, 2008.

The Way Ahead

Twenty years ago, in his book, *Telecommunications in Canada*, Professor Robert Babe examined the history of telecommunications in Canada with a view to demythologizing the technology. Babe argued that the technology of communications does not necessarily have imperatives, or determine outcomes so much as their human agents who have deployed the same as part of a struggle for wealth and power. Before restructuring, technological concepts like economies of scale, system integrity and service universality were used by incumbent telephony to justify the maintenance of market hegemony. Babe foresaw that the efforts to secure hegemony in the digital economy would also be anchored in a similar strategy of technological determinism:

> Unfortunately, much of the literature on the information revolution addresses what is happening and projects what will happen in an idealized world, far removed from the nitty-gritty of actual institutions, rivalries, corporate and governmental powerplays, greed, propaganda, and public relations. In the idealized world of the policy-maker and futurologist, engineered devices are mythologized as 'technology' and human agents become transformed into mere spectators, moulded by an ineluctably evolving technical environment. Re-establishing technology as industrial art, purposively deployed, is especially important today when persistent claims are made that Canada is being drawn inexorably into an information society and that Canadians must adapt meekly to the ensuing changes.[184]

Four years later, Lawrence Surtees, described the struggles to establish competition and interconnection that gave rise to CRTC Telecom Decision 92-12 and recognized the dichotomy between the rhetoric of what was being sought and the reality in the marketplace:

> Long-distance competition is not just about cheap telephone calls or the right to choose an alternate carrier; it is about a struggle for supremacy over the electronic highways to our homes, offices and cars.[185]

Telecommunications restructuring has mostly been described in the context of principles of economics or technological developments like advanced networks. But in precisely the way that Professor Babe describes, they were the tools that were used and shaped to suit the players in the actual world of commerce.

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[184] Babe, Robert E., p. 250.

[185] Surtees, Lawrence, *Wire Wars, The Canadian Fight for Competition in Telecommunications,* Prentice Hall Canada Inc. Scarborough, Ontario, 1994, p. xix.

The establishment, maintenance and regulation of digital wireless and wireline voice and data networks at the start of the restructuring process coincided with and helped nurture a movement for regulatory reform that encompassed high-end business users, classical economic theorists eager to test market forces, industry-engaged economic and technical experts churning out anti-regulatory screed, governments eager to reduce the financial burden of regulation in deficit weary times and industry stakeholders aggressively lobbying the regulator and policy makers for an opening or advantage. The deregulation of telecommunications also carried with the whiff of excitement in escaping rule by the CRTC that had a commissar-like image, largely because of its restrictive broadcasting decisions on cable content and pricing. In an address at an industry conference in 1996, the author of this report noted the "law of the jungle" vision of regulation that was in vogue in some circles:

> This usually finds expression in statements like: "If the CRTC would stop trying to tie us up with useless regulations, we could compete effectively in Canada and in the global marketplace". These kinds of statements would have more resonance if they were not generally uttered by executives of corporations who are about to put their hand in our pockets and don't want to be stopped from so doing. They also are usually accompanied by extravagantly priapic rants extolling the manly rigours of competition and the woe that betides unborn generations of Canadians if we see fit to meddle with their corporate bottom line. Another nice touch is some collateral support provided by an economics professor who is fairly salivating at the prospect of a business environment, red in tooth and claw, outside his comfortable publicly-funded university office.[186]

However, there were also other forces shaping the deregulatory exercise. Worldwide, there were efforts to liberalize communications markets and to encourage the globalization of the provision of telecommunications services. International commerce was increasingly dissatisfied with monopoly systems of telephony, particularly those that were government-owned. The United States had moved through a historic anti-trust case to break up AT&T and move to competitive entrants such as MCI into long distance market. The need for greater investments into telecommunications and advanced networks to provide the information highway of the future upon which the national economy would be based made governments nervous about finding the resources to build without relaxing regulatory controls on its industry.

The concatenation of industry technological developments, global regulatory trends and prevailing patterns of political power and influence profoundly affected the restructuring process. The Cold War had ended and governments were loathe to be associated with regulation that smacked of command and control. Consumer representation and advocacy for market issues was at its weakest ebb as government funding waned and other public interests such as the environment and national social programs sucked up the public policy oxygen. Fresh from the

[186] Janigan, Michael, "CRTC - Don't Print the Obituary," Insight Conference, Toronto, 1996.

recession of the early 1990s, governments were uncertain about the recovery and solicitous of industries that might provide future employment magnifying the already significant clout of incumbent telecom industry players.

Canada's Competition Bureau, an agency that might have provided a clear eyed view of market developments, chose to adopt positions at critical junctures that placed much faith in the potential dynamics of competition based on the nature of the industry services and technology, rather than the actual market shares of the players and the conditions on the ground. The Bureau's own decisions on issues, such as allowing mergers in the new Personal Communications Services (PCS) markets with incumbent wireline players, or finding no cartel behaviour by Stentor, were prima facie problematic for competitive development, and insufficiently transparent to allow public scrutiny.

However, it is a mistake to suppose that we have migrated from a regulatory telecom paradise to the current world where the consumer is at the bottom of the food chain in terms of benefits. The experience throughout the world has shown the inefficiencies associated with monopoly regulation and an ability to manage operations more effectively, where there are appropriate incentives to do so. The experience in Canada with the financial results of the ILECs under price cap regulation is, in large part, due to the rationalization of their operation from an economic efficiency standpoint. Competition also brought an end to silliness like monopoly control of handsets and refusals to interconnect to maintain hegemony.

But restructuring also brought trends that were not helpful for consumers not necessarily from theoretical economic models or technology, but from the way they were used by the heavy hitters. Principally, it increased the stakes involved in political lobbying, economic influence, and media spin. The result ransformed not only the regulator's decisions, but also, with the Policy Direction, the way that decisions were supposed to be made. It caused the CRTC to take ownership of restructuring in a way that made it defensive of its failings and too eager to pass on the costs of encouraging competition on to consumers. It made deregulation itself the measure of success, creating logrolling for early forbearance decisions that had more to do with industry politics than competition economics. It hobbled the CRTC's ability to deal effectively with services like payphones, where hesitation over their importance, and adherence to deregulatory precedent, contributed to their escalating rates and the ultimate marginalization of the service.

However, the key factor that has caused the interests of ordinary consumers to be reduced in importance in the restructuring process, is the failure to review the results of deregulatory or competition-based initiatives where consumer protection or other forms of public interest controls were previously in place with a view to determining whether the objectives of the *Telecommunications Act* were being achieved. No forbearance decision has ever been reviewed to determine whether users continue to be protected, although in many cases market conditions

(e.g. the market) are very different than when the decision was made. Key decisions affecting consumer interests must be trued up with results. This is a asic governance principle for any regulator. With the exception of the publication of a CRTC Monitoring Report, this is not happening.

Recommendation One
The regulator and policy makers must formally review and use the results of their decisions to maintain, improve or eliminate those provisions that have not worked. Real market results are to be preferred to untested theory.

A principal impediment to results-based telecommunications governance can be found in the Policy Direction. The Policy Direction is based on a mindset that equates the presence of rules with the negation of competitive markets and is one-sided in its application. As noted elsewhere in this report, the Policy Direction is harmful to both consumer protection and competition and represents a rather rudimentary approach to a complicated industry. Eli Noam of Columbia University, one of the initial proponents and gurus of the emergence of telecom competition has noted:

> Telecom visions for the future of the market used to be very simple. When we thought about the future in telecom, we thought there would be competition and then more competition and regulation would eventually become unnecessary and then fade away. I would argue none of this has happened or will happen, and if anything regulation will become more important than ever.[187]

As we have seen, inattention to the markets established after forbearance has seldom achieved good results for consumers.

Recommendation Two
The Policy Direction of December 2006 should be rescinded.

[187] Quoted by McClelland, Stephen, "Return of the R Word," Telecommunications Magazine, Monday, January 14, 2008, p. 1 at <http://www.ptc.org/emailer/pdf/Telecom_Regulation_ptc08.pdf>.

Forbearance, exercised as a result of the presence of competition sufficient to protect users, is a test based on market power. The CRTC has defined market power as, "the ability of a firm to impose unilaterally and profitably a significant, non-transitory price increase within the relevant market." The pricing results for services in many forborne telecommunications services markets seems to show that forbearance was premature, or that the market has become uncompetitive. Forbearance decisions should be reviewed on the basis of results that show the presence of market power. Real market results, where available, should be the basis for forbearance decisions by the CRTC rather than a formula such as that provided by the Cabinet reversal of the CRTC's local forbearance decision in 2007.

While the conclusion that the market is not competitive may not cause a return to the status quo before forbearance, it will force consideration of changes to assist the interests of users.

Recommendation Three
Forbearance decisions should be reviewed where market results indicate market power. Those same results should inform any review process.

The current *Telecommunications Act* is principally concerned with regulation and deregulation of monopoly carriers. As we have seen, when deregulation of former monopoly or market dominant carriers occur, the conditions governing consumer protection or conditions of service may also be affected. A new strategy for ensuring efficient and consumer friendly conduct in the marketplace must be evolved.

An approach that would mandate the licensing of all telecommunications carriers to provide a level playing field for all service providers and ensure that across-the-board standards for consumer protection exists. Accompanying the licensing regime would be the development of rules and codes of conduct for operation that might include rules concerning the marketing, operation, billing and reporting of telecommunication services operations. Licensees would be bound by those rules and required to participate in funding and respecting the processes of the regulator and the CCTS.

The Ontario Energy Board (OEB) follows a similar model of licensing of various industry players including marketers, transmitters, generators and distributors. Rules and codes respecting consumer contracts, disconnection, and late payment penalties have been implemented to attempt to police misrepresentation and other marketplace misconduct. The OEB holds hearings to inquire into and punish transgressions by licensees either by fine or loss or suspension of license.

The CRTC should be granted the power to assess substantial Administrative Monetary Penalties for failure to adhere to Rules and non-monetary penalties to ensure compliance.

Recommendation Four
All providers of telecommunications services should be required to be licensed by the CRTC. The CRTC should develop rules and codes of conduct particularly in relation to consumer protection and anti-competitive issues. The CRTC should be invested with powers to assess Administrative Monetary Penalties in line with those available under the *Competition Act*.

Broadband services have become an important network for the delivery of a wide range of services including telephony. The concept of universal service has become more important than ever with next generation networks and there now exists much public policy support for a universal service obligation that includes broadband. The Broadband Task Force in 2001 recommended an action plan that would have seen access to broadband in all Canadian communities by 2004. The Telecommunications Policy Review Panel Report of 2006 urged the creation of a national strategy for adoption of ICTs, noting the effect of improved broadband connectivity as "a prime means of spreading the social and economic objectives of information technology."[188] It also recommended that the government "immediately commence a program to ensure that affordable and reliable broadband services are available in all regions of Canada, including urban, rural and remote areas, by 2010 at the latest."[189] The June 2010 Senate Standing Committee on Transport and Communications recommended that the government in its digital strategy should define "universal" as 100% of its citizens.

In relation to the issue of basic service, all classes of local exchange service providers when operating in a non-High Cost Serving Area (HCSA) should have an obligation to serve in their serving territory. A transition to a rules-based licensing regime might facilitate this development.

Market forces are sometimes inadequate to render reliable and affordable high quality telecommunications services to Canadians in all areas of Canada, even where there is competition, and thus the obligation to serve must be preserved. The obligation to serve exists independently of statute and contract and arises from a broader common law duty to serve and should not be removed. The existence of competition does not change or remove the common law obligation to serve.

[188] TPR Panel Report, p. 7-43.
[189] *Ibid*., 8-1.

The present basic service objective (BSO) has been a success, ensuring basic service that is accessible, affordable and functional. The CRTC must maintain all elements of the BSO with regard to voice service or providers will either seek to eliminate them or charge customers a separate fee for them.

The basic service objective needs to be modernized to include broadband access. Broadband is available to and used by a majority of consumers but the lack of availability to a minority of consumers can result in social exclusion and public intervention is warranted. For wireless broadband to satisfy the BSO, there must be no functional difference between the wireless and wired broadband, the price within 15% more (or is less), and an acceptable quality of service achieved under all conditions of normal use.

Recommendation Five
The obligation to serve should be extended to all classes of local service providers. Basic service should be extended to include broadband provided in accordance with comparable standards.

The Commission for Complaints for Telecommunications Services (CCTS) is under review by the CRTC as of the date of this study. As we have noted, CCTS has been backed with an advertising strategy, only this year, leading to an increase in complaints as detailed herein. CCTS should be continued and expanded as the issues that were fundamental to its establishment associated with the inability of competitive markets to resolve customer complaints remain present and require the services provided by CCTS.

The service should be expanded to meet the expectations of Canadian telecommunications users. The current exclusion of complaints from
"non-price-forborne" areas was based on the theory that in these "regulated" areas,
there are methods for vindicating one's rights before the CRTC. This ignores the reality of lack of resources and capacity to do so at the CRTC.

CCTS should also be able to take complaints about cable television and
satellite TV service. Consumers do not understand why these services, which are frequently bundled with telecom services that are covered, cannot be subject to CCTS complaint resolution.

CCTS should also study systemic customer service problems in the industry and make recommendations on how to fix the same. The ability of CCTS to embark upon systemic

investigations should not be subject to the voting threshold rules that allocate too much control to the three industry members on the Board.

All TSPs should be members of the CCTS. The Consumer Group support removing the $10 million telecommunications services revenue threshold for membership. The CRTC's initial concerns that fees would be too high and administrative processes too burdensome for smaller ISPs are now unjustified.

Recommendation Six

The Commissioner for Complaints for Telecommunications Services (CCTS) must be renewed and expanded to include membership by all telephone service providers (TSPs) and be given expanded powers to deal with telecom and broadcasting services that are currently excluded. CCTS reporting on systemic problems should not be subject to voting thresholds that allocate industry members of the CCTS Board a veto.

There is some merit to the criticism that increasing the number of foreign competitors is increasingly cited as a cure-all for Canadian market failure. One such analyst has noted:

> A centrepiece of Canada's industrial policy is attracting foreign investment. This seems to me a lack of imagination on the part of our elites; rather than develop genuine industrial strategies, so much the better to just let foreign capital come and create the jobs for us.[190]

In relation to perceived market failure or dismal performance, PIAC does not submit that foreign competition will remedy all customer welfare problems arising from the operation of the current networks. There is the requirement for implementation and enforcement of standards of service and codes of conduct applicable to all service providers as previously described. There is a continuing need for a complaints ombudsman to mediate customer disputes. Effective competition may lessen the necessity of action to enforce such rules or mediate complaints, but more competition itself cannot replace the need for their establishment.

On the other hand, Canadian ownership requirements have frequently been an inadequate substitute for positive expectations or obligations for private interests to act in the public

[190] Lee, Marc, "Foreign Ownership in the Resource Sector," Progressive Economics Forum, at <http://www.progressive-economics.ca/2007/07/19/foreign-ownership-in-the-resource-sector/>.

interest.[191] From the consumer standpoint, there is little that commends a strategy that provides for the protection of the interests of users of telecommunications networks and services simply by foreign ownership controls.

Pursuant to s. 91 of the *Competition Act*, a merger involves the acquisition of control whether by purchase, lease of shares or assets, amalgamation or a combination of control over a significant interest in a business of a competitor, supplier, buyer or other person. Mergers may prevent or substantially lessen competition in a market. Section 92 of the *Competition Act* gives the Competition Tribunal the power to take appropriate steps to prevent this harm.

However, the *Act* recognizes that mergers may also lead to efficiency gains. Section 96(1) provides that a merger will be allowed if it is likely to bring about gains in efficiency that will be greater than, and will offset, the effects of any prevention or substantial lessening of competition that is likely to result. A substantial lessening of competition is normally accompanied by a significant non-transitory price increase: indeed, this is the measure used by the Competition Bureau and other competition authorities. This redistributes income from consumers of the merged firm's products to the firm itself.[192]

From PIAC's perspective, the exercise of encouraging new entrant competition in telecommunications markets can be easily negated by a pattern of mergers that would effectively re-concentrate the market. The federal government's strategy of a decade ago of providing a head start for PCS providers Microcell and Clearnet was nullified by subsequent mergers with Rogers and TELUS approved by the Competition Bureau. It is thus vital that the efficiency gains accruing to shareholders in a proposed merger involving new foreign-owned competitors are not allowed to be set off against the losses accruing to consumers arising from a substantial lessening of competition. This is particularly the case when the gains accrue to foreign shareholders and can be less expected to ultimately benefit Canadian consumers.

The recommended approach would require that, for the efficiencies defense to succeed, customers should not lose because of the merger. In particular, prices should not substantially increase, relative to what they would be, absent the merger.[193] Equivalently, consumer surplus should not decrease.[194]

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[191] The issue of foreign ownership controls has been more easily accepted by the business community than issues associated with concentration of ownership. The Davey Committee report of 1970 and the Kent Commission of the 1980s illustrate this observation.

[192] In turn, the increased revenues will be passed on, in part to employees through higher salaries and benefits, and in part to shareholders through an increase in earnings that is translated into increased share prices. The magnitude of the final incidence is an empirical matter. To simplify the discussion, we refer to shareholder effects and do not discuss employee effects. This has no impact on the arguments advanced.

[193] The reader is reminded that here "price" is intended to include non-price attributes, such as quality.

[194] The Federal Court of Appeals has rejected this approach in *Commissioner of Competition* v. *Superior Propane Inc*., [2003] F.C.A. 53. Thus, a legislative amendment may be required to implement it.

This consumer surplus standard is used in four other jurisdictions: the United States, European Union, United Kingdom, and Australia.[195] Adoption of a consumer surplus standard by Canada would be a step toward harmonization with these countries. This approach is also relatively simple to implement. The focus, from the customer end, is on the level of prices. For ease of administration, a price index for the firm could be constructed, as a weighted average for all the products sold by the pre-merger firms. For the efficiencies defense to be successful, a requirement might be whether it is likely that the price index will increase for a given period of time post-merger.[196]

A failure to correctly establish a standard for the merger efficiency defense that is in accord with the objective of enhancing consumer welfare will subvert the intent of the liberalized rules and may simply lead to the continuation of non-competitive markets, albeit in different hands.

The state of competition in most telecommunications markets and the resultant effect on price, choice, innovation and quality of service in those markets compels the consideration of lessening of foreign ownership controls to promote new entry. The incomplete market discipline provided by the current state of competition to be the most important policy driver for change, and a solution that directly links foreign investment with start-up telecommunications companies and existing small industry players, is likely to achieve the best results.

Recommendation Seven

Relief from current telecommunications ownership provisions should be considered only for new entrants and small existing carriers. The Merger Efficiency Defense must be clarified so that a consumer surplus standard should be applicable in mergers. The ability of the merging parties to offset shareholder gains against consumer price increases arising from a substantial lessening of competition should not be permitted.

[195] According to Massimo Motta, *Competition Policy: Theory and Practice* (New York: Cambridge University Press, 2004) at p. 274: "So far, the EC [European Commission] in its decisions has not explicitly ruled out the possibility of using an efficiency defense, but it has not showed much sympathy for this argument either. Whenever cost reductions have been claimed by the merging parties, the EC has dismissed those claims on various grounds."

[196] The details of constructing such a price index have been explored in depth in a number of industries in Canada, such as telecommunications and energy that are subject to price cap regulation. Simplifying greatly, an average price index is calculated each year for firms that have market power. The firms must obey the constraint that this index cannot exceed a cap determined by the rate of inflation and by the productivity gains that can reasonably be expected in that industry.

The restructuring of the telecommunications industry necessitated certain revisions in the way the CRTC handled applications. Many more of the applications have involved interpretations of existing policy, rather than lengthy determinations of the factual and regulatory veracity of telco evidence, or that of the briefs opposing their position. There became less necessity for oral hearings, and in turn, the reduced need fostered more latitude in the submission of untested evidence, comments, and approach to compliance. The large rate applications of the past had been instrumental in providing a key window on telecommunications service and the regulated companies. Price caps moved this scrutiny into different parameters, and currently, CRTC telecommunications proceedings are attempting to fine tune the agenda prodded by the Policy Direction. Oral hearings are increasingly uncommon in proceedings conducted under the *Telecommunications Act*, and, when conducted, resemble those that take place pursuant to the exercise of CRTC powers under the *Broadcasting Act*.[197] Under the broadcasting proceedings rules, no cross-examination of applicants or interested parties by other parties takes place. The hearing is composed of speeches from the applicants and interested parties and questions to the speechmakers and their frequently numerous supporting retinues by CRTC panel members.

It is important to note that the CRTC is not intended to be a passive adjudicator of the issues placed before it and indifferent to the evidentiary record in relation to the exercise of its statutory authority. As one commentator noted:

> Courts and commissions do have commonalities. Both make decisions that bind parties. Both base decisions on evidentiary records created through adversarial truth-testing. Both exercise powers bounded by legislative line-drawing. But courts do not seek problems to solve; they wait for parties' complaints. In contrast, a commission's public interest mandate means it literally looks for trouble. Courts are confined to violations of law, but commissions are compelled to advance the public welfare.[198]

However, regardless of the changing focus of the regulatory purview, the necessity of the presence of a truth-seeking process in administrative tribunals has not been transformed by an emphasis on a deregulatory mindset. As PIAC noted in a recent telecom proceeding considering the CRTC Rules of Procedure:

> But light-handed regulation should not be light-headed regulation; in a deregulatory environment, there is likely an increased necessity to ensure protections such as mechanisms for discovery and cross-examination at an oral hearing where there are serious differences on the state of the facts in key issues. Stakeholders did not morph into fully candid and

[197] The last telecommunications proceeding that allowed cross-examination took place in October 2007 in the CRTC Telecom PN 2006-14 Essential Services proceeding.

[198] Hempling, Scott, "Commissions are not Courts; Regulators are not Judges," National Regulatory Institute, at <http://nrri2.org/index.php?option=com_content&task=blogcategory&id=16&Itemid=38>.

> transparent entities with the onset of regulatory forbearance. As well, traditional oral hearings did not become impossible to convene and hold as a result of the same.[199]

The CRTC itself has recognized that there may be a necessity to have different kinds of frameworks for determinations of issues of differing complexity and importance.[200] The procedural rules should provide for specific components of the adjudicative process to be adopted depending on the complexity and importance of an issue to the *Telecommunications Act* objectives. CRTC Telecom Decision 2009-428 noted the continuum between efficiency and sufficient thoroughness in relation to the choice of procedures. Considerations such as complexity and the precedential value of the ultimate decision are cited therein as reasons to ramp up the procedural protections provided.

It is reasonable to apply the same analysis to other issues determined by the CRTC. The CRTC should be required to give consideration to the full range of procedural protections as the default option when key aspects of the public interest associated with the objectives of the *Telecommunications Act* are engaged in a proceeding. The complexity of the issues, differences in material facts, and the precedential value of the proceeding should also factor into such a decision. If it is necessary to abbreviate, condense or amend the traditional comprehensive approach, justification should be provided in the notice initiating the hearing.

There have also been indications that the limitations on the ability of parties to test the evidence arise out of the assumption that nothing useful is to be gleaned from the cross-examination process. Other mechanisms provide limits on participants attempting to enlarge the record. The larger telecom proceedings currently may feature an oral phase where parties present arguments before the CRTC panel, and may occasionally add comments to the presentation of other stakeholders if called upon to do so. There is also often a specific list of questions and issues prepared by the CRTC that participants are asked to address, that essentially provides the parameters of their submission. The questioning of the panels is generally by CRTC panel members only.[201]

In PIAC's view, the abbreviation of oral hearings into a process that now more resembles a parliamentary hearing than an administrative tribunal has not enhanced the quality of the record for the purpose of making important decisions. As PIAC's submission in the CRTC proceeding considering new CRTC rules noted:

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[199] Submissions of the Public Interest Advocacy Centre, December 17, 2009, CRTC Broadcasting and Telecom Notice of Consultation 2009-602, *Call for comments on new draft regulations concerning CRTC Rules of Practice and Procedure*, para. 6.

[200] CRTC Telecom Regulatory Policy 2009-428, *Canadian ownership and control review policy*.

[201] In the recent hearing of CRTC Telecom Notice of Consultation 2010-43 on the obligation to serve and basic service, some questions were allowed to be asked by interested parties at the rebuttal stage.

> There is a reason that courts and tribunals, for centuries, have relied on tools such as cross-examination to determine the truth of the matters before them. While the Commission may prefer to rely on its own ability and powers to generate information in hearings, its choice of process may have a role in determining the result. Interrogatories and Commission-driven questions cannot replace the need to challenge evidence directly. It is perhaps trite to state that evidence that may be subject to cross examination is usually more carefully prepared than that where cross-examination will occur. While the technical nature of telecommunications means that cross-examination of expert witnesses by some counsel can be un-illuminating, the assumption that the currently used hearing procedure is an acceptable substitute is profoundly mistaken.[202]

However, more than the quality of the record has been affected by the emphasis on expedience in the conduct of proceedings. The CRTC must exercise an extensive adjudicative role in carrying out its duties under the *Telecommunications Act*. Any one of a number of responsibilities, including decisions on forbearance, orders for interconnection and compensation to be paid, or setting of rates when applicable, involves the CRTC as the impartial decision-maker in accordance with the provisions of the *Act*. The rather extensive entry of the CRTC members into the fray to test the evidence, limiting the role of counsel, and circumscribing the potential dimensions of representations on a given issue, go well beyond the traditional view of the role of the adjudicator. While it is clear that members of an administrative board such as the CRTC may express strong views[203] and ask questions in a vigorous fashion, the CRTC's truncated hearing process casts it firmly into the arena as a player/surrogate for the various public and private interests engaged in the hearing. It is difficult to maintain the appearance of fairness when, to a large extent, the adjudicator not only determines the limits to the challenging of evidence, but insists on taking the lead in directing any such challenge.

The downside of this new role is that the CRTC appears to be increasingly viewed by the industry as another player in the game, albeit an important one. The interventions and questions by Commissioners at a hearing are dissected as evidence of close-mindedness, or inability to understand the evidence. Partly as a result of the town council nature of current oral hearings, there is reluctance to petition the Minister for substantive relief.[204] As PIAC noted in its response to CRTC Notice of Consultation 2009-602:

> …the Commission's retreat from the full protections afforded stakeholders in traditional oral hearings has not been helpful in terms of the Commission's stature in the public eye as well as the acceptance of

[202] PIAC submission to Broadcasting and Telecom Notice of Consultation 2009-716, *Call for comments - Review of CRTC cost award practices and procedures*, para. 5.
[203] *Newfoundland Telephone Co. v. Newfoundland (Board of Commissioners of Public Utilities)*, [1992] 1 S.C.R. 623.
[204] One example is the endless wrangling on essential services issues including matching speeds in broadband.

> its decisions. When the important element of "having one's day in court" is removed, disgruntled interveners have re-litigated their positions with vigor in the media and with politicians. PIAC submits that the closer that an administrative process for decision-making comes to the ordinary machinery of policy determination by government bureaucrats, the less likely that the ultimate decision will be accepted. Processes truncated for supposed efficiency may not conserve less time and resources.[205]

In PIAC's view, the new approach of the CRTC to the holding and conduct of hearings extracts too high a price in fairness. More informal hearing procedures and more reliance on CRTC commissioners is a formula that inherently favors the well-resourced industry stakeholders.

Recommendation Eight
Where the issues and circumstances warrant, oral proceedings under the *Telecommunications Act* should be conducted by the CRTC with traditional procedural safeguards for public interest and consumer participants.

While there has been no diminishment of the requirement for consumer representation in CRTC telecommunications proceedings throughout the restructuring period up to the date of this report, the funding available for consumer representation outside the hearing room has largely been limited to project-related funding available from the Contributions Program for Non-profit Consumer and Voluntary Organizations provided by the Office of Consumer Affairs within Industry Canada. This frequently means that the consumer viewpoint is reactive to the agenda of the regulator and other industry stakeholders. With less overall scrutiny available in regulatory proceedings of the operations of telecommunications service providers, this means that the acquisition of knowledge, the interface with industry and government policy makers and submissions outside the hearing process are largely un-resourced. As well, public interest funding for *Broadcasting Act* consumer issues remains unavailable despite over two decades of efforts and the passage of a private members bill tabled in the Senate earlier in the decade.

This problem does not require a change to the CRTC telecom participation rules as recommended by the TPR Panel,[206] but an examination of mechanisms to make the consumer representative work done there and in other policy making venues more meaningful. The relative worsening of the ordinary consumers' position in the restructuring process is testament to the necessity to improve their representation.

[205] Submissions of the Public Interest Advocacy Centre, December 17, 2009, CRTC Telecom NOC 2009-602, para 20.
[206] TPR Panel Report, Recommendation 9-30.

Recommendation Nine

There is a need for funding research by public interest non-commercial stakeholders in broadcasting and telecommunications, and participation in Broadcasting proceedings by such stakeholders. The Government should act immediately to ensure that consumers have the resources to have an informed and respected voice in the governance of these industries.

Appendix A

Mobile Commerce and Wireless Communications: A Canadian Consumer Perspective

Public Interest Advocacy Centre

Edited Version of Brief Prepared for: The Standing Senate Committee on Transport and Communications

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1. Introduction and summary of findings associated with price, bundles and quality in Canada vs. rest of world

Wireless telephones are the fastest growing consumer product in history.[1] Wireless phones are rapidly becoming a ubiquitous tool for Canadian life and are an indispensable tool for business. The Canadian Wireless Telecommunications Association, an industry lobby group, estimates that there are as many as 21.5 million wireless phone subscribers in Canada.[2] Canadian telecommunications providers offer wireless service to more than 98% of Canada's population and two out of every three Canadian households have access to a wireless phone.[3] Half of all telephone connections in Canada are wireless phones and Canadians send 77 million text messages per day and place over 6 million 9-1-1 calls per year.[4]

The Canadian wireless industry is financially healthy and represents a major part of Canada's total telecommunication revenues. The Canadian Radio-television and Telecommunications Commission (CRTC) publishes an annual Monitoring Report where it surveys the telecommunication industry using a variety of different metrics. According to the survey, mobile revenues in Canada represented 40% of total telecommunication revenues in 2008, up from 38% in 2007.[5] Mobile revenues remain the single largest revenue component for Canadian telecommunications providers. Mobile revenues, excluding paging, amounted to $9.3 billion in 2004 and increased to $15.9 billion in 2008, representing an average annual growth rate of 14.3%.[6] Mobile data revenue growth was considerably higher at an annual rate of 35.2% in 2008.[7]

The Monitoring Report explains that mobile wireless growth continues on its path in Canada largely due to pricing plans in certain markets, improved handsets,

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[1] Canadian Wireless Telecommunications Association, *Canada's Wireless Industry: A Global Success Story Continues* (September 2009) <Http://www.cwta.ca/CWTASite/english/index.html>.
[2] *Ibid.*
[3] *Ibid.*
[4] *Ibid.*
[5] Canadian Radio-television and Telecommunications Commission, *Communications Monitoring Report 2009* (August 2009), pp. 235-237 <http://www.crtc.gc.ca/eng/publications/reports/policymonitoring/2009/2009MonitoringReportFinalEn.pdf>.
[6] *Ibid.*
[7] *Ibid.*

the sale of data services, and service bundles. However, the rate of growth in terms of revenues and number of subscribers has been declining since 2005. Revenue growth dropped from 16.5% in 2005 to 10.5% in 2008 and subscriber growth dropped even more dramatically during that time from 13.3% to 9%.[8] Despite this, the average annual revenue per user (ARPU) increased by 3% from $59 per month in 2007 to $60 per month in 2008.[9] In 2004, wireless revenue growth was approximately 1.4 times that of the growth in the number of wireless subscribers. In 2007, this figure increased to 1.8 times which resulted in an increase in the monthly ARPU. However, in 2008, this ratio dropped to 1.2 times which may be an indication that ARPU growth rates are reaching a plateau.

The Canadian wireless market is in transition from a market dominated by more rudimentary phones with simpler operating systems to smart phones. Market analyst IDC Canada has indicated that the sale of traditional mobile phones has fallen 37% in the first quarter of 2009 compared to the same period in 2008.[10] At the same time, smartphone sales are up 38% for the first quarter of 2009, compared to the same period in 2008. Smartphones are still a relatively small segment of the overall market at 27%,[11] but these figures show how impressively their adoption is increasing.

In spite of strong economic indicators, Canada's wireless industry is weak when examined in comparison to other countries. Merrill Lynch, a well known financial and advisory firm, recently ranked Canada's wireless penetration (a measure of cell phone users per capita) at 65%. This figure put Canada just ahead of Indonesia and Iraq but in last place among 22 countries surveyed.[12] The International Telecommunications Union (ITU) has also been tracking Canada's wireless penetration rank over time. According to the ITU, Canada was ranked 35th for wireless penetration in 1998. In 2008, Canada had slipped to 128th.[13]

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[8] *Ibid.*
[9] *Ibid.*
[10] "As Prices Fall, smartphones make consumer gains"(June 9, 2009) CBC, <http://www.cbc.ca/technology/story/2009/06/09/smartphones-apple-iphone-price.html>.
[11] *Ibid.*
[12] Ron Nurwisah, "Wireless Wars: Barriers to new providers" (July 22, 2009) *The National Post,* <http://network.national post.com/np/blogs/fpcomment/archive/2009/07/22/wireless-wars-barriers-to-new-providers.aspx>.
[13] *Ibid.*

Pricing for Canadian mobile phone services and mobile data services is among the highest in the developed world. This fact was highlighted by the recent Communication Outlook report published by the Organization for Economic Co-operation and Development (OECD). This report compares prices for wireless phone services available in the 30 OECD member states. The OECD report compares prices in different states by looking at 3 categories of wireless usage; low usage, medium usage and high usage.[14] Low usage is defined as 360 minutes of voice calls, 396 text messages and 8 multimedia messages per year. Medium usage is defined as 780 minutes of voice calls, 600 text messages and 8 multimedia messages per year. High usage is defined as 1680 minutes of voice calls, 660 text messages and 12 multimedia messages per year.

Canada fared poorly in this comparison, ranking 20th out of 30 states for low usage, 28th out of 30 states for medium use and 18th out of 30 states for high usage.[15] Even more alarming is how Canada ranked in last place for wireless penetration among the 30 states surveyed with only 62 wireless subscribers per 100 people. The OECD average is close to 100% and some states have more than one phone per person.[16] Italy's wireless penetration was 150%. It is interesting to note, however, that the price of wireless telephone services in the United States remain even higher in the United States than in Canada. Detailed graphs of each country analyzed by the OECD report can be found at Appendix 1.

These figures serve as an indicator to Canada's relatively weak position as a world player in mobile commerce.[17]

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[14] Organization for Economic Co-Operation and Development (OECD), *OECD Communications Outlook 2009* (August 2009), <http://www.oecd.org/document/44/0,3343,en_2649_34225_43435308_1_1_1_1,00.html>.
[15] *Ibid.*
[16] *Ibid.*
[17] In October of 2010, the New American Foundation released a study comparing wireless phone rates in 11 countries. It found that Canada ranks as the most expensive for packages that include voices, text, and data. http://oti.newamerica.net/publications/policy/an_international_comparison_of_cell_phone_plans_and_prices

2. Wireless codes in Canada and abroad

In the previous federal election, the Conservative government promised to implement a code to regulate the wireless industry and protect consumers. The initiative read as follows:

A re-elected Conservative Government led by Stephen Harper will prevent telecommunications companies from charging fees to customers for receiving unsolicited commercial text messages. We will amend the Telecommunications Act to strengthen the power of the Commissioner of Complaints for Telecommunications Services, including the creation of a code of conduct for wireless services. We will also create a compliance and deterrent power that allows the Canadian Radio-television and Telecommunications Commission (CRTC) to block these and similar unfair charges in the future.[18]

The wireless industry responded by producing a code of conduct through its industry group, the Canadian Wireless Telecommunications Association (CWTA). In this code, the CWTA members pledged to:[19]

- Provide their customers with complete details on the rates, terms and coverage offered in each of their plans
- Help ensure that wireless customers understand the terms of their contracts
- Communicate with customers in terms that they understand
- Ensure clear advertising
- Protect customer rights when carriers must change contract terms
- Provide read access to customer service
- Safeguard customer's personal information
- Resolve customer complaints efficiently, fairly and courteously

The issue of telecommunications services has proven important enough to Canadian consumers to include it in the ruling party's election platform. There are other data to suggest a significant measure of consumer dissatisfaction in Canada. One such indicator is the type and volume of complaints received by the

[18] Conservative Party Platform, <http://www.nationalpost.com/documents/081007-platform.pdf> or <http://www.conservative.ca/EN/1091/106349>

[19] CWTA's Code of Conduct for Wireless Service Providers (August 2009), <http://www.cwta.ca/CWTASite/english/codeofconduct.html>.

Commissioner for Complaints for Telecommunications Services (CCTS). In its 2007-2008 report, the CCTS outlined the number and type of complaints for that period. The telecommunications sector which drew the most complaints was the wireless sector with 690 complaints or 31% of the total number of complaints received. Complaints regarding local exchange and VOIP services represented 29% of the total, internet access 23% of the total, long distance 16% of the total and 1% were other complaints.[20]

Consumer dissatisfaction may have been one of the reasons that Liberal MP David McGuinty introduced a Bill into Parliament in June of 2008 proposing reforms to wireless services. The Bill's short title was *The Telecommunications Clarity and Fairness Act*. The Bill proposed a number of changes to protect consumers from unfair telecommunications practices. Some of the proposed changes included:

- a prohibition against the levying of any additional fee or charge that is not part of the subscriber's monthly fee or monthly plan rate[21]
- a requirement that telecommunications providers make available to the public, for every contract, a fact sheet that discloses each service being provided and its associated cost as well as any other fee a subscriber will be required to pay[22]
- A government assessment about how telecommunications providers can be compelled to provide clear and accurate descriptions of all costs involved in a telecommunications service plan, provide accurate disclosures about the speed a customer will experience over a network, what sort of traffic management practices in use over a network that could reduce its performance for a customer and an assessment of network management practices that favour, degrade or prioritize any packet transmitted over a broadband network based on source, ownership or destination.[23]

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[20] Commissioner for Complaints for Telecommunications Services (CCTS) *Annual Report 2007-2008* (October 2008), p. 13, <http://www.ccts cprst.ca/en/attach/AnnualReport/CCTS%20Annual%20Report%202007-2008.pdf>.
[21] Bill C-555, *An Act to provide clarity and fairness in the provision of telecommunications services in Canada,* 2nd Sess., 39th Parl., 2008, cl. 2a.
[22] *Ibid.,* cl. 2b.
[23] *Ibid.,* cl. 3a-c.

Unfortunately, this Bill did not pass as Prime Minister Harper dissolved the 39th Session of Parliament and a general election was called.

Other jurisdictions around the world have various wireless codes in effect that protect consumers. One such jurisdiction is the European Union. In 2002, the European Parliament released its Directive 2002/22/EC on universal service and users' rights relating to electronic communication networks and services. Here are the principles the directive establishes, in the words of the European Parliament:

- The concept of universal service should evolve to reflect advances in technology, market developments and changes in user demand

- A fundamental requirement of universal service is to provide users on request with a connection to the public telephone network at a fixed location, at an affordable price.

- There should be no constraints on the technical means by which the connection is provided, allowing for wired or wireless technologies, nor any constraints on which operators provide part or all of universal service obligations. Connections to the public telephone network at a fixed location should be capable of supporting speech and data communications at rates sufficient for access to online services such as those provided via the public Internet. The speed of Internet access experienced by a given user may depend on a number of factors including the provider(s) of Internet connectivity as well as the given application for which a connection is being used.

- More effective competition across all access and service markets will give greater choice for users.

- The connection provided shall be capable of allowing end-users to make and receive local, national and international telephone calls, facsimile communications and data communications, at data rates that are sufficient

> to permit functional Internet access, taking into account prevailing technologies used by the majority of subscribers and technological feasibility.[24]

Wireless codes have also featured prominently in U.S. policy making recently. As long ago as 1996, the United States Congress directed the Federal Communications Commission (FCC) to reform its policies with respect to cellular phones.[25] The Commission sought to promote certain principles within the wireless marketplace. Those principles included: transparency, non-discrimination, competitive neutrality, just and reasonable rates and affordability.[26] The FCC also began regulating certain areas of the wireless market to protect wireless consumers and end some unfair business practices within the market.

One practice of particular importance to mobile commerce is that of SMS advertising. Consumers often receive these unsolicited messages from advertisers and in many cases they are required to pay for the reception of the message. This practice currently falls under the purview of the *Telephone Consumer Protection Act* (TCPA) and the *CAN-SPAM Act*. The TCPA originally protected consumers from unwanted telephone calls and faxes. The TCPA has subsequently been interpreted by the FCC and U.S. Courts to apply to wireless phones and SMS messages under certain circumstances. Violations of the TCPA carry minimum statutory damages of $500.00 per offence. Numerous class action lawsuits have been launched by consumers to enforce TCPA offenses.

The *CAN-SPAM Act* primarily regulates email marketing messages but has also other types of commercial messages as well. The *CAN-SPAM Act* also regulates the transmission of SMS messages in the United States if done using specific technologies, particularly those that send communications en masse.[27] The

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[24] Directive 2002/22/EC of the European Parliament and of the Council of 7 March 2002 on universal service and users' rights relating to electronic communications networks and services (Universal Service Directive), <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:32002L0022:EN:HTML>, (March 2002), *Official Journal L 108 , 24/04/2002 P. 0051 – 0077*.

[25] Federal Communications Commission, *Connecting the Globe: A Regulator's Guide to Building a Global Information Community* (Federal Communications Commission, 1999), <http://www.fcc.gov/connectglobe/sec6.html>.

[26] *Ibid.*

[27] Brian W. Esker and David Rice, "Mobile Commerce: A Legal Landscape" (November 25th, 2008), *Mobile Marketer* November 2008, <http://www.mobilemarketer.com/cms/lib/2585.pdf>.

CAN-SPAM Act specifies that any commercial solicitation be clearly identified as such in the message, that the message bear a clear and accurate return number or path, that the subject line of the message be accurate and not mislead the consumer in any way and that the recipient of the message be allowed to easily opt out of any further messages.[28]

These two pieces of legislation allow for more rigorous enforcement of abuses or unfair practices that consumers may experience on the part of service providers or third party companies in the mobile commerce environment. However, these practices continue in the United States and there is no comprehensive code in place at the national level. The Federal Trade Commission has also been involved in the issue and held a town hall meeting in 2008 to examine consumer protection issues arising in the mobile commerce market place. They published a report as a result of the meetings entitled "Beyond Voice: Mapping the Mobile Marketplace". This report identified unsolicited text messages, malware and spyware as the most important issues facing consumers in the mobile commerce environment.[29] Mobile carriers currently block hundreds of millions of unsolicited text messages per month in the United States.

State governments in the United States are also taking action. Wireless Bills of Rights have been introduced in 22 states including New York, California, Massachusetts and Arizona.[30] The California Telecommunications Consumer Bill of Rights was adopted by the California Public Utilities Commission in 2004. The Bill offers wireless consumers a number of important rights. Some of them include:[31]

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[28] *Ibid.*

[29] Giselle Tsirulnik, "FCC to police wireless space to ensure consumer protection" (April 23rd, 2009), *Mobile Marketer* April 2009 <http://www.mobilemarketer.com/cms/news/legal-privacy/3098.html>.

[30] Spencer E. Ante, "The Call for a Wireless Bill of Rights" (March 20th, 2008) Business Week, April 2008, <http://www.businessweek.com/magazine/content/08_13/b4077080431634.htm?chan=magazine+channel_what%27s+next>.

[31] California Public Utilities Commission, *Revised General Order 168, Market Rules to Empower Telecommunications Consumers and to Prevent Fraud*, (California Public Utilities Commission, 2006), <http://docs.cpuc.ca.gov/published/GENERAL_ORDER/54500.htm>.

- A right for new subscribers to cancel a new service plan within 30 days of activation without any penalty (minus costs for voice minutes and data consumed).
- Full disclosure of all details of a consumer's service agreement on the service provider's website as well as any changes to pricing, tariffs or contractual terms and conditions.
- Marketing practices that are not untrue, deceptive or misleading in any way about rates and services.
- Clear billing, written in a legible sized font and outline all charges clearly. Government mandated charges must be computed separately from charges levied by the provider.
- Carriers must debit payments the day they are received and consumers are permitted a minimum 22 day payment grace period from the date the bill was mailed.
- Late payment penalties may not exceed 1.5 percent per month on the balance overdue.
- Wireless providers must notify consumers at least 25 days in advance of every proposed change to their service agreements that may result in higher rates or charges or more restrictive terms and conditions.

A final example of a national level wireless code is that of Australia. Prior to the implementation of their wireless code, many of Australia's mobile data services were regulated by the *Telecommunications Service Provider (Mobile Premium Services) Determination 2005*. This determination provided the groundwork for an industry self regulation scheme. A self regulation scheme was implemented in 2006.[32]

In 2007, *The Communications Legislation Amendment (Content Services) Act 2007* was passed. This amendment changed the wording of the *Broadcasting Services Act* to create a new schedule (Schedule 7) to regulate content services delivered to Australia via carriage service.[33] This new Schedule took effect in January 2008. Schedule 7 permitted the content industry to implement its own

[32] Please see the Communications Alliance website for details: <http://www.commsalliance.com.au/Activities/mps>.
[33] *Ibid.*

codes of practice. These codes became invalid on July 1 2009 when the industry published a newer, updated code.

3. The importance of wireless devices and mobile commerce protections

The importance of wireless data devices is increasing daily. Wireless data devices are important tools for communication and business but have a growing number of other uses as well. Nearly all of these innovative uses rely upon the data and messaging features of modern mobile phones rather than the core voice calling function.

One novel program has been implemented by the City of New York. Citizens are now able to use the photo and video capabilities of their phones to interact with their municipal government. Callers to New York City's 9-1-1 emergency services can now send photos and videos to the New York Police Department's (NYPD) Real Time Crime Center. If these photos or videos are useful as investigation tools or criminal trial evidence, they are forwarded to officers on scene or crime detective.[34] These photos or evidence may also be circulated to patrolling officers, other law enforcement agencies or the general public as the situation warrants.

New York City residents may also upload videos or photos when calling the City's 3-1-1 service for maintenance and quality of life complaints. Typical complaints involve garbage collection, graffiti and potholes. Uploads via wireless devices allow City maintenance crews to have visual information about a given situation and address problems more efficiently. A similar program has been instituted by the Washington D.C. transit police. That allows the public to send similar reports from their wireless devices about crime or other transit issues.[35]

Another important public safety program that relies upon advanced wireless services is the U.S Department of Homeland Security's Alert Aggregator/Gateway system. This system has not yet been implemented, however, when it is completely operational, it will employ commercial wireless carriers to send important local,

[34] Dan Butcher, "NYPD uses mobile to fight crime" (September 16th, 2008) *Mobile Marketer,* September 2008, <www. Mobilemarketer.com/cms/news/legal-privacy/1721.html>.
[35] *Ibid.*

state and national emergency alerts to consumers. The system is designed to provide three types of alerts.[36] The first kind is a Presidential Alert, where national emergency alerts are delivered to wireless consumers, superseding any other alerts. Next is the Imminent Threat alert, where alerts are sent out regarding emergencies that may pose an immediate risk to citizen's lives or well-being. Finally, there are Child Abduction Emergency/AMBER Alerts. The AMBER Alerts report missing children to the public in an abduction or runaway situation.

These examples help to illustrate how wireless devices are increasingly important to the public. Their ability to send and receive numerous kinds of data makes them an essential tool to consumers. Despite the clear benefits these devices offer, there are a number of important issues that consumers face in the Canadian mobile commerce environment.

The Transatlantic Consumer Dialogue (TACD) is a forum of U.S. and EU consumer organizations that develops joint consumer policy recommendations directed to the U.S. government and European Union to promote the consumer interest in EU and U.S. policy making. The Canadian mobile commerce market bears many similarities with the U.S. market and any examination of the U.S. market could prove very useful in the Canadian context as well. In August 2005 the organization published the "Resolution on M-commerce",[37] expressing concern for the increase in consumer complaints about m-commerce for fraudulent activities as well as for unfair business practices:[38]

- Unauthorized purchases made with a consumer's mobile phone without that person's knowledge or consent. Unless there is a PIN or some other form of authentication required, it is easy to use someone else's mobile phone to purchase something at that person's expense;

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[36] Mickey Alam Khan, "FEMA named aggregator/gateway for national mobile alert system" (June 2nd, 2008) *Mobile Marketer*, June 2008, <http://www.mobilemarketer.com/cms/news/legal-privacy/1081.html>.
[37] Trans Atlantic Consumers Dialogue (TACD), *Resolution on Mobile Commerce*, August 2005, <http://www.tacd.org/docs/?id=283>. *See* also: European Commission, *TACD 2005 Recommendations Report and European Commission Services' Responses*, June 2006, European Commission <http://ec.europa.eu/consumers/cons_issue/tacd-recommendations_2005_en.pdf>.
[38] *Ibid.*

- Marketing to children who are using mobile phones but may not have the capacity or authorization to make purchases. Advertisements for ring tones, games, and other products or services popular with young people can be found in media (television, radio, Internet, and print publications) targeted toward children and adolescents;

- Inadequate disclosures in advertisements about the products and services offered the cost, and the terms and conditions. Often the details of the transaction – for instance, that there will be a recurring monthly charge – are in fine print or are not made clear or easily-readable;

- Spam being sent to mobile phones. Consumers may become deluged with unsolicited offers for mobile commerce;

- Security of financial information given to vendors to make mobile commerce transactions. Information could be intercepted in transmission or obtained surreptitiously by hidden RFID readers;

- The disparity of dispute rights depending on how payment is made. Dispute rights for unauthorized transactions and incorrect charges may differ according to whether the charges were placed on a telephone bill, billed to a credit card, deducted from an "e-wallet," or debited from a consumer's bank account. They also differ from country to country. In addition, consumers may not be protected from their mobile service being terminated for failure to pay disputed charges that were billed to their mobile accounts. They may also find it hard to prove the terms on which they purchased, if the details of transactions are not confirmed (e.g., on itemized phone bills);

- Privacy and discrimination issues related to tracking purchases and the locations of the device users. Mobile commerce vendors may be able to collect information about what goods and services consumers purchase and where they go, and use it for secondary purposes or share it with others. This could lead to more intrusive marketing and other uses of information about consumers' activities and locations that they neither expected nor

desired. This information could also be used to identify the most profitable consumers and offer them the best deals, leaving less profitable consumers increasingly excluded from markets.

All of these issues are equally applicable to Canadian mobile commerce consumers and should be considered carefully by lawmakers.

4. Measures to fix existing mobile commerce problems

Pricing

A major barrier to Canadian wireless consumers is the price they pay for their service. As the OECD report reveals, Canadian wireless services are priced much higher than many other developed states. Furthermore, the state of wireless competition in Canada is such that pricing for wireless service is generally high. Features outside of the basic plan, such as SMS messaging, roaming and long distances are typically billed per message or per minute on most basic plans. Wireless data is particularly expensive and no carrier in Canada offers a plan that provides for unlimited data (at least at the time this report was written).

It is this high pricing that contributes to a stagnating mobile commerce market in Canada. Last year, the World Economic Forum noted that Canada's wireless market was an important reason why it has slipped in its ranking for "network readiness" among many countries in the world. Canada was ranked 6th worldwide in 2005 but now ranks 13th.[39] Our wireless pricing is so high the Research in Motion, the manufacturer of the iconic wireless messaging/mobile commerce device, the Blackberry, has commented that they could sell eight or nine times as many of its devices here, if carriers would simply lower their prices to a rate similar to elsewhere in the world.[40] Furthermore, high wireless data prices have driven Canadians to spend less time on the mobile internet. Google has noted a marked gap between the amount of time Canadians spend using its online applications like webmail or mapping and other places in the world.

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[39] Michael Geist, "Canada's Telecom Crisis: My Appearance Before the Senate Transport and Communications Committee," June 8th, 2009, <http://www.michaelgeist.ca/content/view/4037/125/>.
[40] *Ibid.*

The European Union faced a similar problem that Canada is currently facing. High prices for wireless services prevented consumers using many of their wireless services, particularly while roaming. This phenomenon had wider economic effects and so the European Union decided to regulate wireless fees. The European Parliament enacted new rules for its members that came into force on July 1st, 2009. The effects of the new rules are listed below:

- Limits the price for sending a text message while abroad at €0.11. Receiving an SMS in another EU country will remain free of charge.
- Reduces the cost of surfing the web and downloading movies or video programs with a mobile phone while abroad by introducing a maximum wholesale cap of €1 per megabyte downloaded. This limit will be decreased each year.
- The new rules will also protect consumers from "bill shocks" by introducing a cut-off mechanism once the bill reaches €50, unless they choose another cut-off limit (recently, a German downloading a TV program while roaming in France faced a bill of €46,000). Operators have until March 2010 to put this cut-off limit in place.
- Further reduces prices for mobile roaming calls with a maximum tariff of €0.43 for making a call and €0.19 for receiving one.
- Introduce per second billing after the first 30 seconds for calls made and immediately for calls received.
- Ensure that citizens are kept adequately informed of the charges that apply for data roaming services. [41]

These new rules make wireless billing cheaper and more predictable for consumers in the European Union. This has the effect of promoting mobile commerce among them. Similar provisions in Canada should produce the same effect. Canadian

[41] European Commission, "The new proposal for reducing roaming prices" 2009, <http://ec.europa.eu/information_society/activities/roaming/regulation/index_en.htm#new_rules>.

consumers are more likely to make use of wireless data services if they are cheaper and pricing is predictable.

Spam

The first use of the term "spam" was to refer to articles posted to online message boards, which were of no relevance to the topic in discussion and violated the forum policies. This kind of content was sent to several newsgroups, and quickly became a nuisance to other users. Later, the term was then applied to describe junk e-mail messages, many of them of commercial nature and many other of a dubious nature.[42] Today the term is used as a synonym for unsolicited commercial e-mail.[43] The term SMiShing is relatively new and it is used to refer to spam when its transport mechanisms are SMS and MMS.[44]

In Canada, relevant provisions of PIPEDA, the Competition Act and the Criminal Code may be useful legal tools to counter spamming activities, however there currently exists no law that specifically targets spam. PIPEDA protects the privacy of Canadians and the Privacy Commissioner has found that spam is a violation of privacy in two reported cases.[45] Unfortunately, both of these decisions do not have any binding legal consequences and no penalty was imposed for either of them. Specific legislation dealing specifically with spam is not in place in Canada. The *Competition Act* prohibits misleading advertising and could be used to combat some cases of spam that make misleading commercial claims. The *Criminal Code* provides penalties for fraud and could offer recourse to consumers who have fallen victim to online scams.

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[42] International Telecommunication Union (ITU), *Spam in the Information Society: Building Frameworks for International Cooperation*, 2005, <http://www.itu.int/osg/spu/spam/contributions/Background%20Paper_Building%20frameworks%20for%20Intl%20Cooperation.pdf>.

[43] Both the ITU and the Anti-Spam Action for Canada agree on this definition of spam. See: Canadian Task Force on Spam, *Report of the Task Force on Spam*, and May 2005, <http://www.itu.int/osg/spu/spam/contributions/Background%20Paper_Building%20frameworks%20for%20Intl%20Cooperation.pdf>.

[44] Symantec, *Internet Security Threat Report, Trends for July-December 06*, March 2007, Symantec < http://eval.symantec.com/mktginfo/enterprise/white_papers/ent-whitepaper_internet_security_threat_report_xi_03_2007.en-us.pdf>.

[45] See this site for details <http://www.priv.gc.ca/cf-dc/2005/297_050331_01_e.cfm>.

What is needed in Canada is a statute that addresses spam and SMiShing directly. There are currently two Bills being debated on the issue, one before the House of Commons and one before the Senate.

The House of Commons Bill, C-27, would effectively ban unsolicited electronic messages of a commercial nature to an "electronic address", in most cases.[46] The definition of an "electronic address" in the Bill includes telephones[47] and would most likely cover wireless devices, such as smartphones, which are used to undertake electronic commerce.

The Senate Bill, S-220, provides much of the same protection as Bill C-27. The Bill also outline specific procedures that must be implemented by commercial messagers to clearly identify themselves and the origin of their message, have accurate subject lines and allow consumers to opt-out of receiving further messages easily.[48] Either of these two Bills would provide very valuable protection to consumers in the mobile commerce realm.

Mobile payments

The mobile payments system is very popular in Japan and South Korea, where consumers can use their mobile phone to pay for less expensive items or services. Mobile payments in Japan have been available to consumers since 1999, when the system was based on short messaging system (SMS), but today handsets are equipped with chips, scanners and other technologies that allow users to simply wave their phones over a sensor and transactions are completed on the spot. Similar technologies allow South Koreans to make mobile payments as well. The main difference between the Japanese and South Korean payment systems is who funds the payments. In Japan, mobile payment systems have been driven largely by Japanese wireless providers such as NTT and DoCoMo. In South Korea, mobile payment services are usually offered by both wireless carriers and the banking

[46] Bill S-220, *An Act respecting commercial electronic messages*, 2nd Sess., 40th Parl., 2009, cl.6(1).
[47] *Ibid., cl.* 2(1).
[48] *Ibid., cl.* 5(1) – 7.

industry. In North America, it is more likely that the South Korean model will be adopted.[49]

In the United States, mobile payments are still based on SMS, and allow money transfers through mobiles without storing users' information in the handset.[50] Along with SMS, they rely on confirmation calls to senders and Personal Identification Number (PIN) numbers as layers of security to protect the authenticity of transactions. This seems like a more secure system than the popular Japanese system that relies upon contact-less RFID chips for authentication. A lost or stolen phone with a Radio Frequency Identification (RFID) mobile payment system activated could be used very easily for fraudulent purposes by anyone carrying the phone. A system relying upon a PIN would be far less susceptible to fraud as only the authorized user could allow a payment to take place.

M-Payments in Canada are not yet popular but mobiles are being currently used as an alternative method of payment. It is currently possible to pay for parking time in Vancouver, Toronto, Winnipeg, Edmonton, Calgary and Burnaby. Consumers need to place a call to the number printed in the parking meter to buy the amount of parking time necessary, which charged to their credit or debit cards. In Vancouver alone there are 8,300 of these parking meters m-payment enabled.[51] The three major carriers, Rogers, Bell and Telus, have also announced a wireless payment system through a venture between the three companies. Although the venture was announced in 2005, this partnership has not yet blossomed into a commercial operation. The project would allow prepaid wireless users to buy additional minutes on their existing accounts with their debit or credit cards.[52] In 2008, Citibank MasterCard, Bell Mobility and Nokia ran a trial project where they integrated the functionality of a PayPass MasterCard with a Nokia cellular phone. This trial ran from August 2008 to November 2008 and consumers could use their phones to pay at any merchant that accepted MasterCard's contact-less PayPass

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[49] Roman Friedrich *et al*., *Making Mobile Payment Work for Everyone*, Strategy+Business Resilience Report, online: Strategy+Business <http://www.strategy-business.com/resiliencereport/resilience/rr00023>.
[50] Paypal Mobile is one such service: <https://www.paypal.com/cgi-bin/webscr?cmd=xpt/cps/mobile/MobileOverview-outside>.
[51] Bill Boei, *Top Up Your Parking Meter with a Cell Call*, The Vancouver Sun, 27 June 2006, <http://www.canada.com/vancouversun/news/westcoastnews/story.html?id=3828b870-dfb1-47f8-a81d-c694702a11dd>.
[52] Wireless Payment Services Inc. (WPS), *Press Release* 8 November 2005, <http://www.wpspay.com>.

service.[53] It is not known whether a similar program will emerge from this trial on a permanent basis. However, the trial did demonstrate how such a payment method could work using largely existing technology.

Marketing to Children

The practices of companies that market products directly to children or adolescents are not explicitly regulated in Canada at the national level. The *Food and Drugs Act* states No person shall label, package, treat, process, sell or advertise any food in a manner that is false, misleading or deceptive or is likely to create an erroneous impression regarding its character, value, quantity, composition, merit or safety."[54] *The Competition Act* provides that "no person shall,…knowingly or recklessly make a representation to the public that is false or misleading"[55] These laws apply equally to children and adults, however, there are no national laws that account for children, who are a particularly vulnerable class of consumers. Children and young people are also an increasingly large segment of wireless users.

This lack of federal oversight is a relatively recent phenomenon, since screening of several types of advertising was performed by Consumer and Corporate Affairs Canada until the early 1990's.[56] The federal oversight responsibility was transferred to Advertising Standards Canada (ASC) in 1992, which is Canada's national advertising self regulatory body. The ASC maintains the *Canadian Code of Advertising Standards* (CCAS) which seeks to set standards for marketers and they are maintain a separate code for children entitled the

Broadcast Code for Advertising to Children.

The CCAS contains two clauses about marketing to young people:

[53] For details, please see: http://www.mastercard.com/ca/paypass/mobile/about/contactless_payments.html
[54] *The Food and Drug Act*, R.S.C. 2009, c. F-27, s.5(1).
[55] *The Competition Act*, R.S.C., 1985, c.C-34, s.52(1).
[56] Cook, Brian, "Marketing to Children in Canada: Summary of Key Issues. For the Public Health Agency of Canada" April, 2007, < http://www.cdpac.ca/media.php?mid=426>.

Clause 12 – Advertising to Children
"Advertising that is directed to children must not exploit their credulity, lack of experience or their sense of loyalty, and must not present information or illustrations that might result in their physical, emotional or moral harm."

Clause 13 – Advertising to Minors
"Products prohibited from sale to minors must not be advertised in such a way as to appeal particularly to persons under legal age, and people featured in advertisements for such products must be, and clearly seen to be, adults under the law."[57]

Furthermore, the *Broadcast Code for Advertising to Children* a number of clauses which relate to advertising to children such as: comparison claims, factual presentation, safety, avoiding undue pressure and social values. In practice, however, this code applies only to television broadcasts, as radio ads targeting children are extremely rare.[58] This means that marketing directed towards children or youth over wireless networks or the internet is not covered by this code. This leaves children and young people potentially vulnerable to unfair business practices in the mobile commerce environment.

This situation is remarkably different in Quebec. Quebec has enacted a complete ban on all forms of advertising directed towards children. The province's *Consumer Protection Act* forbids any type of marketing to children 13 years old or younger, with some minor exceptions.[59] The ban only applies to advertising which originates in Quebec. This law provides a clear benefit to impressionable children; however, its restricted application means other children around the country are not protected. What is needed is a set of laws that will protect children all over the country, since mobile commerce occurs largely at the national and international levels, not the provincial level. Increasing adoption and use of wireless data devices by young people makes this protection more imperative by the day.

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[57] Advertising Standards Canada, "Canadian Code of Advertising Standards" <http://www.adstandards.com/en/Standards/canCodeOfAdStandards.aspx>.
[58] *Supra* note 52.
[59] *Consumer Protection Act*, R.S.Q. 2009, P-40.1, s. 248.

Ad Disclosures

Complaints regarding the disclosure of the terms of a wireless phone or data device contract are very common among Canadian consumers. Often, advertised prices for service plans do not disclose the true monthly cost of a device, omitting fees such as initiation or activation fees, system access fees and 9-1-1 access fees. Furthermore, consumers may not be completely aware of other fees on their wireless plans that they may incur such as overage charges, long distance fees or roaming fees.

False or misleading advertising is a crime in Canada. Section 52 of the *Competition Act* prohibits marketers from making representations that are false or misleading in any material respect.[60] Furthermore, the *Competition Act* also provides for civil penalties as high as ten million dollars for corporations who mislead the public on a first offence and fifteen million for subsequent offences.[61] Both the civil and criminal provisions of the law do not have a requirement to demonstrate that a person was misled. While the Competition Bureau is charged with investigating complaints about false or misleading advertising, it may be preferable to grant the CRTC or the CCTS investigatory powers in this respect. Both organizations possess specialized knowledge and expertise of the Canadian telecommunications market.

Wireless services are the type of service that receives the most complaints according to the 2007-2008 CCTS annual report.[62] In fact, billing complaints comprise the largest portion of all complaints received by the CCTS at 33% of all complaints received by the CCTS.[63] It is clear that many Canadian consumers are dissatisfied with the wireless services they consume and ad disclosures may constitute a significant part of this dissatisfaction. More action is needed to ensure that all marketing messages concerning wireless services are clear and do not mislead consumers.

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[60] *Supra.*, note 54.
[61] *Supra.*, note 54., paragraph 74.01(1)*(a).*
[62] *Supra*., note 19 at p.13.
[63] *Supra*., note 19 at p. 12.

Security of financial information

A key consideration to any mobile transaction is the security of the information being exchanged. If consumers cannot be confident that their private financial and identity information is secure, they will avoid mobile commerce for more secure, traditional forms. A particular fear is identity theft, which is a highly disruptive and rapidly growing form of crime.

On January 2007, Canadians learned about major incidents of data theft and hacking into the systems of an investment firm owned by one of Canada's largest banks and two major retail outlets that resulted in substantial data losses, including clients' financial information.[64] In the case of the investment firm, a computer hard drive containing vital personal financial information of at least half a million clients went missing. With respect to the retail outlets, client's credit card information was accessed to and removed from the stores' servers and later used to attempt access into the systems of a U.S.-based discount chain company.[65] To this date, it is uncertain how all that information was used and to what end. What is known so far is that the data theft from the stores in Canada is part of the biggest card heist recorded in history.[66]

Egregious cases such as these reported in the media contribute to the uncertainty felt by a large number of consumers concerning electronic financial records. Unfortunately, identity theft is not limited to a small number of large heists in Canada. In fact, in a recent survey regarding identity theft one in ten Canadians who shop online claim to have been victims of identity theft.[67] Over eight thousand cases of identity theft with more than seven million dollars in losses were reported to the RCMP in 2008.[68]

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[64] CanWest News Service, *Security Breaches Hang Over Millions of Mutual Fund, Credit Card Holders*, Ottawa Citizen, 19 January 2007, <http://www.canada.com/ottawacitizen/news/story.html?id=0bfad5c4-60a7-4864-85c9-3b131207e48e&k=95359>.
[65] *Ibid*.
[66] Ellen Messmer, *TJX Data Theft Called Largest Ever: 45.7M Credit Card Numbers*, (29 March 2007) Network World, <http://www.networkworld.com/news/2007/032907-tjx-data-theft-largest.html>.
[67] "1 in 10 Canadians hit by Web ID theft" (October 22nd, 2008) UPI.com <http://www.upi.com/Top_News/2008/10/22/1-in-10-Canadians-hit-by-Web-ID-theft/UPI-37041224679643/>
[68] *Ibid.*

Legislators have recently sought to address the problem by tabling Bills to combat identity theft. Senate Bill S-4 seeks to make important amendments to the *Criminal Code* to criminalize certain behaviour relating to identity theft, such as possessing or trafficking credit card account information.[69] Other provisions seek to protect the integrity of the postal system by criminalizing the malicious redirection of mail, possession of mail receptacles or bags and also possession or re-creation of keys used to access mail containers or devices.[70] The Bill did not outline any specific clauses to protect wireless consumers from abuse. However, a similar clause prohibiting the possession or distribution of tools to circumvent safeguards and encryption on mobile commerce networks, similar to the postal key prohibition, would be a useful protection for Canadian consumers. Furthermore, an automatic and rigorous fraud prevention system, similar to those employed by credit card issuers, could help automatically detect and stop fraudulent transactions from taking place over a wireless network.

Payment Dispute Rights

The issue of payment dispute rights is a potentially serious one for consumers who may have unauthorized charges on their account. The simplest and likely most effective solution for difficult legal situations arising between consumers, wireless providers and merchants is to have a separate payment provider from the wireless provider. The simplest option would be to have credit card issuer process payments, as they already employ robust anti-fraud measures and a long standing and reasonably effective dispute resolution mechanism for consumers.

Mobile payments are linked to outside financial institutions in South Korea, a leader in mobile commerce. Furthermore, the test project that took place in 2008 in Canada used the MasterCard payment system. This proves that such a marriage of players is possible. This option would likely be the most practical and expedient one for wireless consumers in Canada.

Privacy issues

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[69] Bill S-4, *An Act to amend the Criminal Code (identity theft and related misconduct)*, 2nd Ses., 40th Parl., 2009, cl. 4(1)-5.
[70] *Ibid.*, cl. 6(1).

It is often the case that organizations' laxity in establishing controls to guarantee the privacy of personal information handled in the course of business, or in enforcing existing policies, translates in actual harm to consumers. Harm can arise from system's vulnerability to data leakages and unauthorized parties' intrusion or lack of staff's awareness of the organization's policies and duties with respect to consumers. Following, two examples cited by the Privacy Commissioner's Office in its *PIPEDA Report to Parliament* in 2005:[71]

○ An individual complained that his former employer was able to access his account with a rewards program and make changes to it. In her letter of finding, the Assistant Commissioner recommended to the organization now responsible for the rewards program that it implement password controls on the account holder information that can be accessed through its automated system. Our follow-up confirmed that the organization had introduced voice print technology and password protection for access to account holder information.

○ An individual complained that her Internet service provider failed to protect her personal information adequately, did not provide her with a satisfactory explanation when she tried to resolve her concerns, and did not give her access to the personal information she had requested. The investigation did not support the allegations about failure to protect her personal information, and the access complaint was resolved during investigation. On the accountability issue, the Assistant Commissioner recommended that the company implement a procedure for outstanding privacy concerns to be brought to the attention of the company's privacy officer. The organization already had such a procedure, but acknowledged that its staff required greater awareness of and sensitivity to privacy. It undertook to provide the necessary training.

[71] Privacy Commissioner of Canada, *Privacy Commissioner's Report on the Personal Information Protection and Electronic Documents Act Annual Report to Parliament 2005,* (2005), <http://www.privcom.gc.ca/information/ar/200506/2005_pipeda_e.pdf>.

The development of increasingly complex systems seems to be advancing at a faster pace than the mechanisms designed to protect consumers' privacy and information. Experience shows that consumers are insufficiently equipped to deal with the rising number of interactions occurred in the digital space. While it may be relatively simple to identify machines and servers, it is not as easy to identify a person involved in a particular online transaction. In the case of unauthorized use of a mobile phone or similar device, risks for fraud are multiplied by the number of technologies embedded in each device, be it a RFID or other chip, NFC, a web browser, SMS, etc. They are all different avenues that open opportunities to fraudsters for illegitimate use.

What is needed is a set of effective laws that are rigorous enough to protect consumers' privacy but also flexible enough to adapt to new technologies and mobile commerce situations. Legislation specifically written for mobile commerce would be ideal and would avoid some of the delay and uncertainty of relying upon PIPEDA.

Extra Wireless Charges

All the major wireless carriers in Canada charge what is referred to as a "system access fee". This fee, according to many observers, is misrepresented as a kind of government imposed fee. The appearance of a government mandated fee does not seem to be an unintentional mistake. When a CBC television news reporter walked into various cell phone stores posing as a customer to inquire what the fee was for, a Fido sales representative called it "a government fee," a TELUS sales representative called it "a tax," a Bell Canada sales representative termed it "a licensing fee," while a Rogers Wireless representative said that it was a fee "for maintenance for towers and stuff like that [to provide customers with] better services." The pattern of behaviour by the major wireless operators in marketing their products with the same invented charge in the same amount does not bode well for a competitive solution to the reduction or elimination of the system access fee. [72] In fact one provider Bell Mobility has increased its system access fee to

[72] In 2008 TELUS launched a Koodoo wireless service that featured no system access charge while keeping the charge for TELUS customers. Paul Jay , "Do Koodoo ads cross the Line" , CBC, News, <http://www.cbc.ca/technology/technology-blog/2008/11/do_koodo_adds_cross_line.html:>.

$8.95 per month. It also seems apparent that the practice seems geared to generating a lower advertised price.

This deceptive practice has not gone unnoticed. A class-action lawsuit against Canadian cell phone carriers – naming Bell Mobility Inc., TELUS Corp., Rogers Wireless Inc., and various subsidiaries and smaller regional providers – for unjust enrichment has been certified by a Saskatchewan court. At issue is whether Canada's cell phone providers have misled monthly subscribers by implying that so-called 'system access' or 'licensing' fee are somehow required by federal regulators – such as the CRTC. Furthermore, the practice has given rise to action in Parliament to deal with the issue. Liberal MP David McGuinty introduced Bill C-555, the *Telecommunications Clarity and Fairness Act*, on Monday, June 2, 2008. The bill proposes that the conditions of holding cellphone spectrum licenses be changed to "include a prohibition against the levying of any additional fee or charge that is not part of the subscriber's monthly fee or monthly plan rate" and to require cell phone providers to make available with each service contract a fact sheet that discloses every service being provided and any associated costs.[73]

Clearly the issue of extra wireless charges needs to be addressed. The CRTC should consider banning the practice. Wireless plan prices quoted and advertised to consumers should incorporate all the costs of service, to avoid misleading consumers.

5. Measures to Improve Wireless Competition

A major issue affecting the Canadian wireless market is a lack of competition among wireless providers. Wireless providers continue to enjoy high profits, but consumers pay very high prices for their wireless services. More competition within the marketplace is needed.

The Industry Canada attempted to address this issue in the summer of 2008 when it held a spectrum auction for wireless carriers. It set aside spectrum for new

[73] Sympatico MSN, "Liberal bill seeks to abolish cellphone surcharges," (3 June 2008) <http://technology.sympatico.msn.cbc.ca/Bell.Sympatico.CMS/Print.aspx?type=feed&lang=en&channel=technology.sympatico.msn.cbc.ca&feedname=cbc-tech-science-v3&newsitemid=tech-mcguinty>.

entrants to the market in a bid to increase competition. This was a positive move for consumers; however, it should be seen as a start to a policy of promoting greater competition, not an end to the issue. Indeed, more spectrum auctions would allow more entrants into Canada's wireless market and this would benefit consumers and the economy.

The 700 MHz spectrum is of particular interest in the context of mobile commerce because its lower frequency makes it very attractive for wireless broadband deployment. Because lower frequency waves are able to propagate farther and penetrate more obstacles like building walls, this spectrum would allow for capital and equipment costs to be dramatically lower than existing infrastructure.[74] This fact means that there would likely be lower barriers to market entry for new wireless providers and this would stimulate competition in the marketplace. The federal government should do its utmost to encourage new entrants to acquire this spectrum when they eventually auction it off. This spectrum is ideal for wireless high speed internet and presents excellent opportunities for the mobile commerce marketplace. The next spectrum auction process should also have set-asides for new entrants to ensure that competition is firmly established.

Another, simpler measure that could be implemented would be a "wireless calculator" or a web application that could compare wireless plan features and prices for consumers. This idea was adopted and very nearly implemented by Industry Canada for the benefit of consumers before the program was cancelled. The aborted calculator cost the federal government $1.4 million[75] and 3 years to create. The calculator's cancellation was very unfortunate as it would have been a neutral, third party application that would have been a useful tool for consumers. It would have also fostered additional competition within the market place since it would have forced wireless providers to try and offer the most competitive rate possible for consumers. The federal government should strongly reconsider its decision to eliminate the wireless calculator in order to promote greater

[74] "USA and Canada 700 MHz Regulatory and Market Analysis" <http://www.wimax.com/commerce/catalog/700mhz>.
[75] "Aborted cellphone rate calculator cost Ottawa $1.4M" (September 10th, 2009), CBC.ca, <http://www.cbc.ca/technology/story/2009/09/10/cellphone-calculator-government-scrapped.html>.

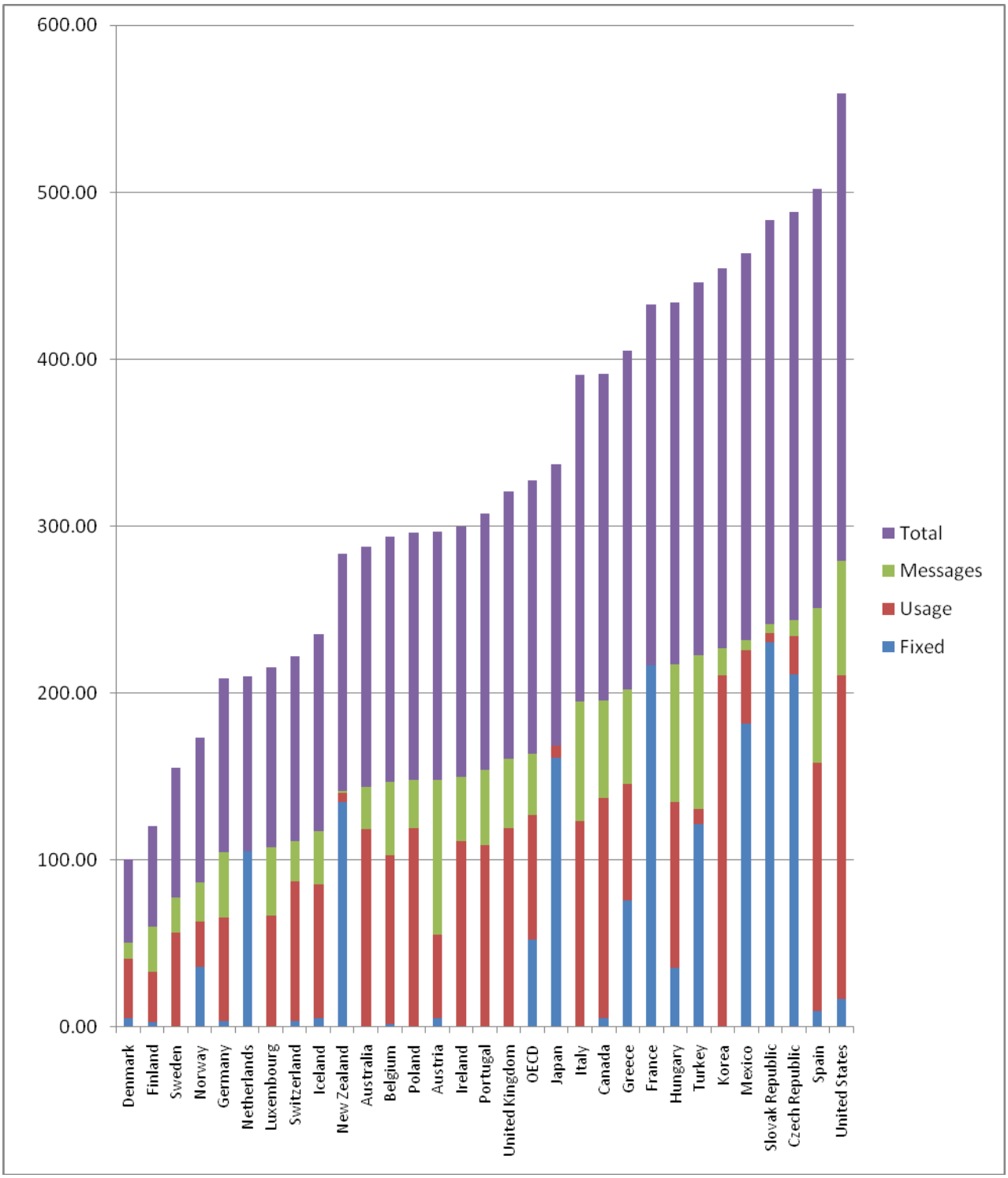
competition within the wireless market and help consumers choose the best plan for their needs.

6. Policy Recommendations

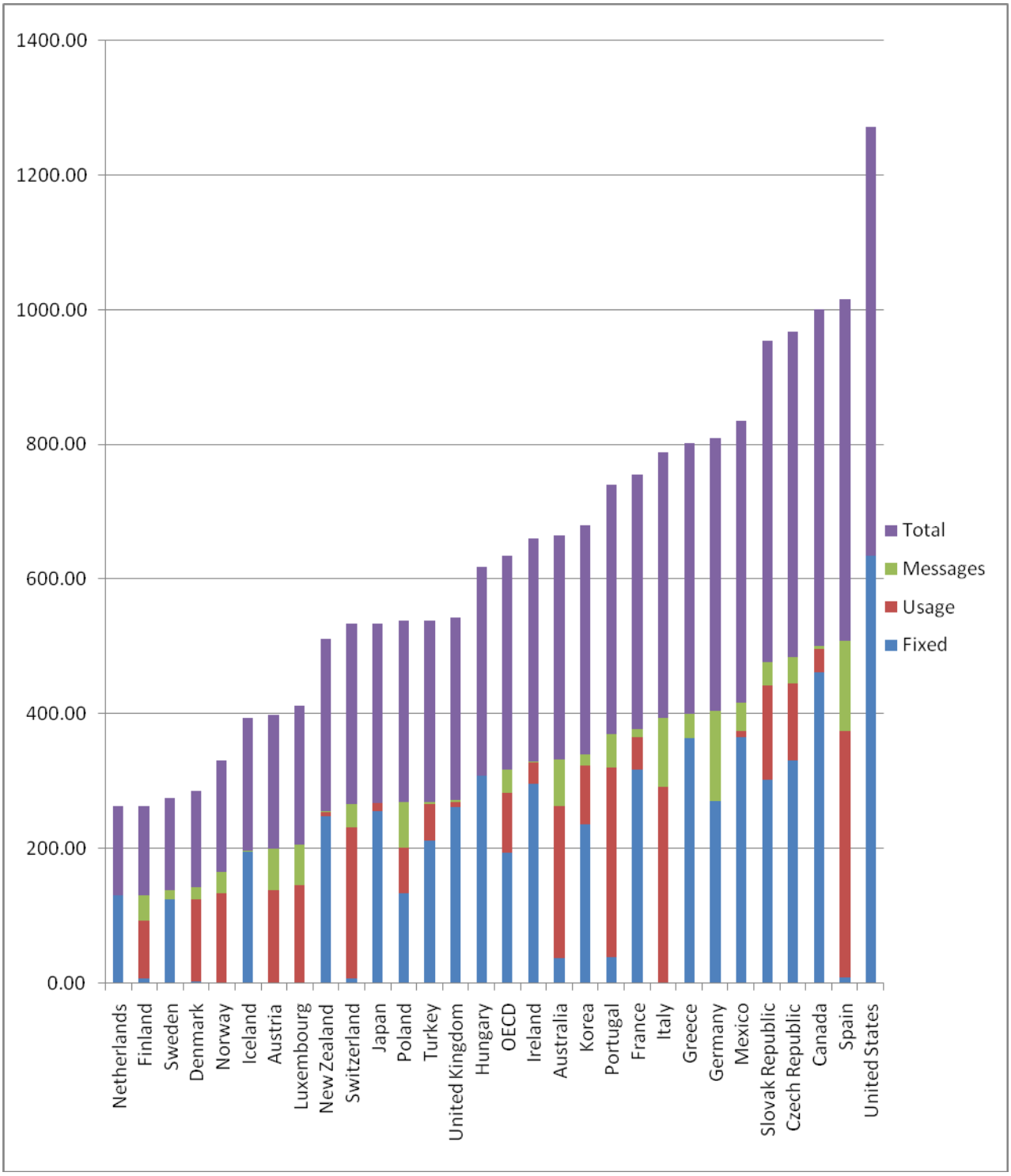
- Pricing: Consider placing a cap on the rates that wireless carriers may charge for their services. This makes pricing simpler and more predictable for consumers and will encourage growth in the consumption of wireless services.
- Spam: Enact legislation prohibiting spam to protect consumers from fraud, abusive marketing practices and violations of their privacy.
- Mobile payments: Encourage the creation of a mobile payments system with common standards to facilitate mobile payments. Partnerships between carriers and credit card issuers could provide the convenience and security necessary for consumers to create a viable mobile payments system in Canada.
- Marketing to children: Children are a very vulnerable group of consumers that deserve protection. Legislation banning most forms of advertising to children under 13 years of age, such as Quebec's *Consumer Protection Act* would protect these at-risk consumers from abuse.
- Ad disclosures: More work needs to be done to ensure that advertising for telecommunication services discloses the true cost and nature of the services being offered. A body with the specialized knowledge of the wireless industry such as the CRTC or the CCTS should be charged with ensuring the accuracy of advertising for wireless service.
- Security of financial information: Identity theft is a very rapidly growing type of crime and wireless networks present a new avenue for identity thieves to ply their trade. *Criminal Code* amendments that prohibit the possession and trade of financial information and technology facilitating identity theft should be enacted.
- Payment dispute rights: Canada should follow the South Korean model and make existing financial institutions be intermediaries in mobile commerce transactions. The dispute resolution mechanism for credit card issues is well established and protects consumers' rights.

- Privacy issues: Wireless networks pose new risks for the protection of their users' privacy. Carriers should ensure they comply strictly with the provisions of PIPEDA to ensure the privacy and security of their customers.
- Extra wireless charges: Wireless carriers need to provide prices to their clients that accurately reflect the price consumers will pay for these services. The practice of charging additional "system access fees" and other such fees must end immediately.

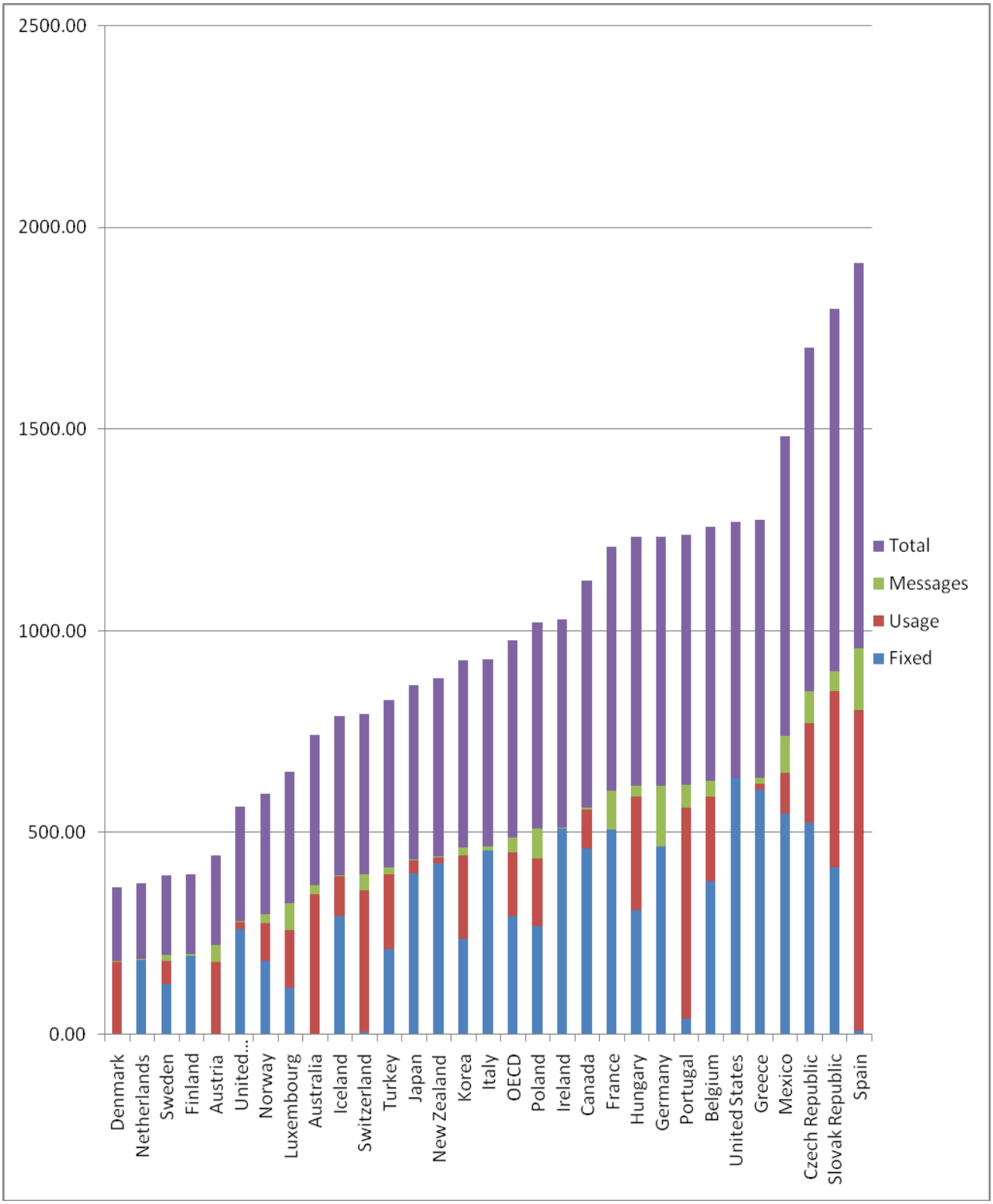
Appendix A



OECD mobile low-usage basket, August 2008, tax included ($USD)



OECD mobile medium-usage basket, August 2008, tax included ($USD)



OECD mobile high-usage basket, August 2008, tax included ($USD)

Appendix B

2010 Questionnaire on the reform of the *Telecommunications Act*

Introduction:

In order to provide a window on stakeholder views, PIAC circulated a questionnaire to approximately ninety companies, organizations and individuals in the categories shown, using a recent CRTC proceedings list. This list was augmented in the case of categories four and five, with additions in these categories so that these would receive at least twenty-five percent of the questionnaires sent out. PIAC's legal counsel completed one questionnaire. The results are tabulated below. The survey was not designed as an empirical instrument, but rather as a more of a weathervane as to current attitudes concerning issues raised by this report or likely in play in relation to telecom reform. In that light, it was felt that the raw data rather than percentages should be reported.

Key:

1. Representative of an industry provider of telecommunications and/or broadcasting distribution services for over 25 years
2. Representative of an industry provider of telecommunications and/or broadcasting distribution services for less than 25 years
3. Telecommunications or broadcasting consultant, expert, or former regulator
4. Academic
5. Representative of a non-profit consumer or public interest organization with an interest in the delivery of telecommunications and broadcasting products and services
6. Representative of a union whose members are employed in the telecommunications industry
7. Representative of an industry association
8. Other (Did not identify themselves on questionnaire)

Question # 1. **The *Telecommunications Act* should be reformed as a matter of high priority.**					
	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.		1	1		
2.		2	2	2	
3.	1	1	1	2	
4.					
5.	6	2	2	1	
6.					
7.		2	1		
8.			2		

Question #2 . **The *Telecommunications Act* and the *Broadcasting Act* should be combined into one statute.**					
	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.				2	
2.	1			2	3
3.			2	3	
4.					
5.	5	2	2	1	1
6.					
7.			2	1	
8.				2	

Question # 3. **The Telecom Review Panel Report of 2006 remains the blueprint that should direct future statutory and policy reform.**					
	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.		1		1	
2.		2	3		1
3.	1	3		1	1
4.					
5.		4	2	3	2
6.					
7.		1	2		
8.	1				1

Question #4. **The policy and regulatory framework under the current *Telecommunications Act,* the actions of the CRTC and the federal government and produced or allowed to develop healthy competitive markets for:**

	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1. Local Telephony					
1.		1		1	
2.	2	1		2	1
3.	2	2		2	
4.					
5.		2	1	5	3
6.					
7.	1			1	1
8.	1				1
2. Long Distance					
	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.		2			
2.	4	2			
3.	4	1	1		
4.					
5.	2	4		3	2
6.					
7.	1	1			1
8.	1			1	
3. Mobile Wireless					
		1	1		
2.	3		2	1	
3.	1	2	1	1	1
4.					
5.		2	3	2	4
6.					
7.	1			1	1
8.	1			1	

4. Retail Broadband internet					
1.		1	1		
2.	2	2		1	1
3.	1	1	1	2	1
4.					
5.		1	1	5	4
6.					
7.	1			1	1
8.	1				1

Question # 5. **The test of market power has been correctly applied to the telecommunications and broadcasting services that the CRTC regulates to determine the issue of forbearance.**					
	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.		1		1	
2.	1			4	1
3.	1	1	2	2	
4.					
5.		1	2	3	4
6.					
7.	1		1	1	
8.	1			1	

Question # 6. **The powers of the CRTC should be more clearly defined and not be based on implementation of general telecommunication objectives. (vague wording)**					
	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.		2			
2.		3		2	
3.	1		3	2	
4.					
5.	2	3	4	1	1
6.					
7.		2			
8.			1		

Question # 7. **The role of the CRTC in telecommunications under a new Act(s) should be primarily to make and enforce necessary industry-wide rules, rather than regulate market dominant carriers.**

	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.				2	
2.	1	2		2	
3.			1	4	1
4.					
5.	2	2	2	4	1
6.					
7.	1			1	
8.	1			1	

Question # 8. **CRTC Commissioners' appointments have been made in keeping with an open professional recruitment process that has ensured the best qualified have been appointed.**

	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.				2	
2.		1	1	3	
3.			2	2	2
4.					
5.			2	5	4
6.					
7.				2	
8.				2	

Question # 9. **The CRTC has maintained a qualified and experienced staff that meets the professional requirements associated with telecommunications and broadcasting regulation.**

	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.			1	1	
2.	1	1	1	2	
3.		2	2	1	
4.					
5.		4	3	3	1
6.					
7.		1		1	
8.			1	1	

Question # 10. **The changes in the process of conducting CRTC proceedings, including the limitation on oral hearings, cross-examination, and interrogatories, has improved the hearing process.**

	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.			1	1	
2.		1	1	2	1
3.		2		3	1
4.					
5.		1	2	4	4
6.					
7.		1	1		
8.		1		1	

Question # 11. **The Commissioner for Complaints for Telecommunications Services (CCTS) plays a necessary role in the resolution of consumer problems and consumer protection.**

	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.		1	1		
2.		1	2	1	
3.	1	3	1		1
4.					
5.	2	4	3	1	
6.					
7.			2		
8.			1	1	

Question # 12. **CCTS should be responsible for consumer complaints in the delivery of all telecommunications and broadcasting services.**

	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.			1	1	
2.	1		1	2	1
3.	2	1	2	1	
4.					
5.	4	1	3	3	
6.					
7.		1	1		
8.			1		1

Question # 13. **CCTS should be established with its own legislative jurisdiction and not be subject to CRTC supervision and determination.**					
	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.			1	1	
2.	1		1	1	2
3.	2		1	2	1
4.					
5.	5	1	2	2	1
6.					
7.		1	1		
8.			1		1

Question # 14. **The CRTC has an important role in monitoring and reporting on the state of the telecommunications and broadcasting industries.**					
	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.		2			
2.	2	1			2
3.	4	2			
4.					
5.	7	4			
6.					
7.	2				
8.		2			

Question # 15. **The burden to ensure universal access to basic telecommunications and broadcasting services should be borne by all stakeholders in the network.**					
	Strongly Agree	Agree	Neither Agree nor Disagree	Disagree	Strongly Disagree
1.		1			1
2.	2	2			1
3.		2	3		1
4.					
5.	6	4			
6.					
7.	1	1			
8.	1		1		

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Mr. Janigan has been the Executive Director of the Centre since 1992. Prior to assuming his current position, Mr. Janigan was a city and regional councillor representing a downtown ward in the City of Ottawa. He was elected to that position in the community where he carried on a busy litigation practice. Mr. Janigan was born in Ottawa and attended the University of Western Ontario in London, Ontario where he obtained both his undergraduate degree in science and his LL.B. degree. He has also completed an LL.M. in Competition Law at the University of London. He has been called to the Bar of the Law Society of Upper Canada and is also a member of the State Bar of California. Mr. Janigan was formerly "of counsel" to the Washington, D.C. law firm, Scott Hempling and Associates**,** which provided legal advice to regulatory commissions across the United States.

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