

Before the House of Commons Standing Committee
Industry, Natural Resources, Science and Technology

February 27, 2007

Deregulation of Telecommunications

Speaking Notes
Michael Janigan
Executive Director and General Counsel
Public Interest Advocacy Centre

February 26, 2007

Thank you for extending this invitation to address the committee on matters of concern to residential consumers and particularly vulnerable consumers associated with the deregulatory actions of the government in relation to the CRTC, in particular, and telecommunications in general.

1. The Public Interest Advocacy Centre (PIAC) is a non-profit organization that provides legal and research services on behalf of consumer interests, and, in particular, vulnerable consumer interests, concerning the provision of important public services. PIAC has made submissions to the Minister in response to the Notice in the Canada Gazette setting his proposed order reversing CRTC Decision 2006-15. We have appended those submissions to these notes as Appendix A.

2. As you have been told, both the reversal and the kind of issue that is sought to be reversed are very unusual. The determination of the conditions that show whether a workably competitive market exists that is sufficient to protect the interests of consumers without regulation is not one which lends itself to resolution by fiat. It is very much an issue where the practical experience of the regulator must be used in conjunction with the various theoretical constructs associated with the presence or absence of market power. CRTC Decision 2006-15 was informed by substantial volumes of expert evidence, such evidence being fully tested in an oral hearing before an independent tribunal. No such process has informed the proposed order of the Minister.

3. We are concerned that the government may be unwittingly playing the role of a sorcerer's apprentice setting loose market forces and

problems in the industry that the previous framework of consumer protection was able to deal with with appropriate controls. The principal question is whether the appropriate mechanisms will be in place to identify problems, much less direct a solution.

4. Its important to note what the government actions to date did not do:
 - (i) They didn't introduce competition into any markets where competition didn't already exist. In fact, most major telecom services have already been forborne from regulation by the CRTC
 - (ii) They didn't free the incumbent local exchange telephone companies (ILECs) from the obligation to maintain local rates at tariff levels. These companies were always able to lower rates across their rate bands.
 - (iii) They did set an unfortunate precedent in allowing telecommunications regulation by politics to trump longstanding administrative procedure. It is a precedent that may prove costly for the winners in the long run. The ILECs are now frequently openly dismissive of regulatory scrutiny in current proceedings before the CRTC, citing the actions of their new champion, the Industry minister as justification.

(iv) They do not accord with the wishes of Canadians. A Pollara survey in September of 2006 found that 80% of Canadians opposed to the ILECs setting their own local rates. Strong majorities were against this prospect even in dense urban areas of cable telephony offerings. In fact, most Canadians, (perhaps given the problems in wireless and broadband industries) don't feel that cable provides enough competition for the ILECs.

5. It would be our submission that it is far better to create the conditions where problems with the proposed new regime may be swiftly identified and remedied rather than endlessly debate the consequences. These conditions would include at a minimum:

(i) Thorough, ongoing, and independent research taken on with stakeholder consultation as to the state of competition in the telecommunications industry including issues of choice, price, penetration, affordability, access and customer penetration identified with appropriate customer demographics.

(ii) Establishment of the independent ombudsman consumer agency as recommended by Recommendation 6-2 of the Telecommunications Review Panel Report to provide remedies for consumers in a

deregulated environment and to provide a window on consumer protection problems as well as potential solutions.

- (iii) The establishment of a process that will swiftly and effectively institute consumer protections where the deregulated market has failed to provide competition sufficient to protect the interests of users.

- 6. Thank you for your indulgence and I would be happy to deal with any questions.

Appendix A

Response of the Public Interest Advocacy Centre to the Proposed Order of
the Governor in Council Varying CRTC Telecom Decision 2006-15
Forbearance from the regulation of retail local exchange services
January 15, 2007

We are writing to provide the representations of the Public Interest Advocacy Centre concerning the proposed Order of the Governor in Council varying the decision of the Canadian Radio-Television and Telecommunications Commission (CRTC). The Order would put in place a revised framework to determine when to deregulate retail telephone prices of the former monopoly companies.

The Public Interest Advocacy Centre (PIAC) participated extensively on behalf of ordinary and vulnerable residential consumers in the proceedings giving rise to CRTC Telecom Decision 2006-15. In addition, PIAC represented these same consumer interests in the proceedings convened by the CRTC as PN 2006-12 to consider amendments to the original decision, a proceeding that had not been completed at the time of the issuance of the proposed Order.

The effect of the government intervention into this important Decision of the CRTC is recognized to have significant consequences, both in terms of the

matters in question and the future regulation of telecommunications. We must assume that these consequences and the issues so determined were carefully considered before the government took such a step. However, we are of the view that the Order, and the assumptions that inform the order, are profoundly in error. We will discuss the reasons for this view under the broad headings of “Incorrect Tests” and “Incorrect Precedent”.

2

1. Incorrect Tests

It is important to note that the Order proposes to adopt a line of reasoning that is principally supported by the incumbent local exchange telephone companies (ILECs), to alter the test prescribed by the Commission to ascertain when a local telephone market can be sufficiently competitive to forbear from its regulation. The Commission’s test was, in fact, representative of a fairly liberal approach to deregulation from an ILEC perspective. The incumbent loss of 25% market share to one competitor as a trigger for deregulation is significantly lower and less stringent than the threshold advocated by most consumer or public competition theorists. The CRTC had the advantage, in the proceeding giving rise to CRTC Decision 2006-15, of assessing such views. At that time, Professor Johannes Bauer, former director of the Quello Center for Telecommunications Management and Law at Michigan State University, noted in his evidence the generally-held propositions about competitive markets:

Whether the rivalry between firms already in a market is sufficient to discipline any abuse of market power depends critically on the number and size distribution of the firms in the market. If firms were of relatively equal size, actual competition is generally considered effective if more than five firms are present. This roughly corresponds to the notion of “tight oligopoly” and the threshold used in antitrust analysis to flag high market concentration. If a lower number of fairly equal-sized companies populate a market, competition does not suddenly fail to be workable. However, as the number of actual competitors shrinks, it will tend to become less effective.¹

¹ Evidence of Dr. Johannes Bauer of June 22, 2005 on behalf of Consumer Groups, CRTC PN 2005-2, paragraph 66. Online: <http://www.crtc.gc.ca/public/partvii/2005/8640/piac/050622.zip>

3

Dr. Bauer then addressed the central question associated with the local telecommunications market as follows:

In a market without regulatory and other safeguards, the presence of five effective competitors could be considered sufficient to assure robust competition. However, in a market with forbearance — that is, the possibility that regulation is re-introduced relatively quickly should effective competition not emerge or be robust — and additional safeguards, a lower threshold seems defensible. The Commission could establish a transition regime, granting increased flexibility to the telephone companies should the market share of the incumbent fall below 85-90 percent. As the case for forbearance gets stronger the closer a market is to the robust effective competition frontier, flexibility could be designed to increase as the incumbent market share shrinks. Forbearance is justifiable if the market share falls below 60-70 percent.²

Dr. Bauer rejected the concept of a duopoly providing sufficient competition:

If the number of competitors falls to two, a duopoly prevails. Although duopoly markets occasionally work effectively, they typically exhibit high prices and only ineffective forms of rivalry. One example was the mobile voice industry during the 1980s and early 1990s in the U.S. The U.S. multi-channel market, essentially occupied by cable service providers and satellite television service providers, was initially characterized by relatively weak competition, although this has recently changed with the gradual expansion of the market share of satellite. A similar experience seems to apply to the U.S. broadband access market, which in many locations is evolving toward a duopoly structure between ILECs and cable service providers. Duopoly markets may be characterized by episodes

² Ibid., at para. 82

4

of intense competition followed by episodes of collusion. Thus, in duopolies it is particularly difficult to evaluate the future effectiveness of competition from present observations.³

The Commission imposed a model that was much less stringent than the current evidence of behaviour in competitive markets, noted by Dr. Bauer, would appear to require. The fact that the ILECs chafed at these modest

requirements is not indicative of the fairly unrestrictive approach advanced by the Commission in its Decision but rather the ILECs' desire to be financially enriched by premature deregulation.

Beyond the inappropriateness of ignoring the results which were crafted if not by a consensus, then by compromise, arising from an extensive CRTC consultation process which included an oral hearing, there remains a more important concern with the position advanced by the proposed Order: there is no evidence that the government changes will accomplish their stated goals of establishing facilities-based competition. There is, in fact, a great deal of evidence that they will do nothing of the kind.

In CRTC proceeding Telecom Public Notice 2006-12, Dr. Robert Loube, a U.S.-based expert in telecommunications regulation, reviewed the U.S. experience in the long distance and wireless markets concluding:

That market experience indicates that market share loss threshold of 25 percent may be too low. Price decreases did not occur when there only two carriers. It was necessary for three, four and five or more entrants to become active in a market before a significant price decrease occurred. If the Canadian wireline markets are left with only two major players, the incumbent and the cable provider, a market share threshold of 25 percent would not indicate competition. In those situations, it is necessary to reduce the threshold to at least 30 and probably to 40 percent before effective competition will exist.⁴

³ Ibid., at para 69

⁴ Evidence of Dr. Robert Loube, October 26, 2006, PIAC Comments on CRTC Telecom PN 2006-12, para 28. Online: http://www.crtc.gc.ca/public/partvii/2006/8663/C12_200610924/683917.zip

5

There is no evidence from actual markets that the conditions described as constituting competition sufficient protect the interests of users have produced the results that are touted in the Backgrounder to the Order, namely more choices, improved products and market discipline. The alterations to the Commission framework have the potential to be disastrous for consumers and set back the onset of workable local telephone competition for many years.

Equally questionable is the eagerness of the government to barge into the determination of the appropriate geographic market for the purpose of any forbearance region. CRTC Telecom Decision 2006-15 defined this task in a consensus fashion:

While parties disagreed over which geographic component the Commission should adopt as part of the relevant market, parties generally agreed that the Commission should adopt a geographic component that reflects a social and economic community of interest, that, for example, has substantially similar local telecommunications market conditions, including common pricing and marketing strategies, local service providers and local service offerings; that is administratively practical and competitively neutral; and that has well-defined, stable boundaries.⁵

In deciding to adopt a definition that relies on telephone company infrastructure rather than real world considerations like the actual social and economic community of interest, the proposed Order subverts the intent of the delineation of the geographic market. This definition is enormously beneficial to one set of stakeholders. The ILECs are desirous of targeting their marketing efforts to customers who are the most densely aggregated, require the highest volume of products and services, and are subject to the emerging presence of competition to the ILECs for providing those products

⁵ Telecom Decision CRTC 2006-15, Forbearance from the regulation of retail local exchange services, para. 83. Online:

<http://www.crtc.gc.ca/archive/ENG/Decisions/2006/dt2006-15.htm>

6

and services. The ability to winnow out those subscribers who don't fit the profile from the target market when offering packages and discounts is a much sought-after ILEC marketing goal – which has been satisfied, in part, by the proposed Order. It opens the door to de facto redlining of customers, resident in the Commission-defined local forbearance regions (LFRs) whose interests will now be excluded from consideration in the new definition of local exchange. It is hoped that Industry Canada will be well equipped with call centres to explain telephone service pricing to angry customers resident in the same metropolitan area who may receive vastly different offers from their ILEC.

2. Incorrect Precedent

PIAC is troubled by the use of the petition to the Governor in Council pursuant to subsection 12(1) of the Telecommunications Act to obtain the result proposed in the Order. PIAC notes that the Telecommunications Policy Review Panel, Final Report 2006 (which this Government has cited as support for its efforts to foster greater reliance on competitive forces) set

out in Recommendation 9-5 that the Cabinet power to review individual CRTC telecommunications decisions should be repealed. In so doing, the TPRP noted:

Although the Cabinet review power has been exercised relatively infrequently since 1993, there have been frequent petitions to use it by parties who were dissatisfied with CRTC decisions. Each time a petition to review a CRTC decision is filed, it imposes significant costs on other stakeholders and the Government of Canada in terms of the resources required to respond to the petition. It also creates an extended period of uncertainty on the industry and other stakeholders, since the government may take up to one year to make its decision on the petition. Finally, consumer groups and other less well-funded parties are at a distinct disadvantage, in comparison to large commercial interests, in their ability to participate in the process. This creates an appearance of unfairness. For all these

7

reasons, the Panel considers that it is not necessary to retain the Cabinet review power.⁶

The Panel's description of the course of events neatly parallels the experience with the Proposed Order. The Order is a the government response to an intense, expensive, multifaceted campaign by the major ILECs to change the CRTC approach to their regulation. It has occurred after they were unsuccessful in an open, transparent process in convincing an independent regulator of the merits of their position.

The approach of the government to the overturning of CRTC Decision 2006-15 conflicts with reasonable standards established domestically and internationally for regulation of important public services such as telecommunications. For example, the International Telecommunications Union's⁷ ICT Regulation Toolkit provides a global overview of how telecom policy is best implemented with practical materials highlighting experience and results. Here the Toolkit discusses the independence of the regulator, based upon precedents found in OECD working party documents :

A regulator must be granted the ability to make decisions, and then must make the decisions that come with the decision-making authority. The credibility of the regulator will be severely limited if other government authorities have the ability to intervene or overrule the regulator. However, this does not

mean that a process should not exist for a regulator's decision to be reviewed if no sound basis exists for a particular determination. Moreover, parties should have the ability to challenge a regulator's decision. However, a regulator's position will be undermined if the participants can lobby other branches of government and thereby overturn a decision that is not favourable to them. Likewise, the necessary protections should be implemented in the law or regulation to ensure that parties

⁶ Telecommunications Policy Review Panel, Final Report 2006, at p.9-18. Online:
[http://www.telecomreview.ca/epic/internet/intprp-gecrt.nsf/vwapj/report_e.pdf/\\$FILE/report_e.pdf](http://www.telecomreview.ca/epic/internet/intprp-gecrt.nsf/vwapj/report_e.pdf/$FILE/report_e.pdf)

⁷ Canada has been a member state of ITU since 1908