REGULATORY AND POLICY DEVELOPMENTS

CONSTITUTIONAL PROPOSALS WOULD STRENGTHEN FEDERAL COMMERCE POWER

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The post-Meech Lake constitutional reform proposal of the Government of Canada, tabled on September 24, 1991, contains much that would enhance the federal trade and commerce jurisdiction. The document states that "the federal government should have the necessary authority to manage the economic union." There are two principal proposals in this area: a new head of federal power under section 91 of the *Constitution Act, 1867* to make laws "for the efficient functioning of the economic union," and a new "common market clause" to replace the moribund section 121. There are also other reforms proposed in the broad areas of economic regulation, some of which would not require constitutional amendment.

It is proposed that the following clause be added to section 91 of the *Constitution Act, 1867*:

> 91A. (1) Without altering any other authority of the Parliament of Canada to make laws, the Parliament of Canada may exclusively make laws in relation to any matter that it declares to be for the efficient functioning of the economic union.
> (2) An Act of the Parliament of Canada made under this section shall have no effect unless it is approved by the governments of at least two thirds of the provinces that have, in the aggregate, according to the then latest general census, at least 50 percent of the population of all the provinces.
> (3) The legislative assembly of any province that is not among the provinces that have approved an Act of the Parliament of Canada under subsection (2) may expressly declare by resolution supported by 60 percent of its members that the Act of Parliament does not apply in the province.
> (4) A declaration made under subsection (3) shall cease to have effect three years after it is made or on such earlier date as may be specified in the declaration.

The approval of the provincial governments required in subsection 2 would take place in the new Council of the Federation. The document leaves open whether the declaration in subsection 4 would be renewable.

Section 121 of the *Constitution Act, 1867* now reads as follows:

> 121. All Articles of the Growth, Produce, or Manufacture of any one of the Provinces shall, from and after the Union, be admitted free into each of the other Provinces.

The government's discussion paper said that "this clause does not reflect the realities of today's market place." That is surely an understatement. It might have said that this section has been quite ineffectual in preventing a whole range of non-tariff barriers to interprovincial trade (for example, see page 22 of this issue concerning a *GATT* challenge to the Canadian internal barriers to the trade in beer).

The proposed new section 121 is as follows:

> 121.(1) Canada is an economic union within which persons, goods, services and capital may move freely without barriers or restrictions based on provincial or territorial boundaries.
> (2) Neither the Parliament or Government of Canada nor the legislatures or governments of the provinces shall by law or practice contravene the principle expressed in subsection (1).
> (3) Subsection (2) does not render invalid
> (a) a law of the Parliament of Canada enacted to further the principles of equalization or regional development;
> (b) a law of provincial legislature enacted in relation to the reduction of economic disparities between regions wholly within a province that does not create barriers or restrictions that are more onerous in relation to persons, goods, services or capital from outside the province than it does in relation to persons, goods, services or capital from a region within the province; or

(c) a law of the Parliament of Canada or of the legislature of a province that has been declared by Parliament to be in the national interest.
(4) A declaration referred to in paragraph (3)(c) shall have no effect unless it is approved by the governments of at least two-thirds of the provinces that have, in the aggregate, according to the then latest general census, at least 50 percent of the population of all the provinces.
(5) This section shall come into force on July 1, 1995.

In certain areas of economic regulation, the government pledges to eliminate or clarify the overlap of responsibilities with the provinces. The areas mentioned include aspects of unfair trade practices, the regulation of trust companies and corporate securities regulation. The document does not explain how this would be done, other than to say that it would not necessarily be by constitutional amendment.

In the field of communications, the document allows for greater provincial involvement, generally without constitutional amendment, in culture and broadcasting. However, there is no discussion of any changes to federal jurisdiction over interprovincial undertakings provided in section 92(10)(a) of the *Constitution Act, 1867*. Thus the government has not placed its recently confirmed jurisdiction over telecommunications on the table. The proposals are now being studied by a joint committee of the Senate and House of Commons, which is to report in February 1992.

Editor's Note: A full report on the Constitution package will be featured in the December issue.

FEDERAL COURT HARPOONS NEB ENVIRONMENTAL JURISDICTION ON GREAT WHALE PROJECT

By: N.J. Schultz
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In a July 1991 judgment, the Federal Court of Appeal struck down the environmental conditions attached by the National Energy Board to licences issued to Hydro-Québec for the export of electric power to New York and Vermont.

The appeal was initiated by both the Attorney-General of Québec and Hydro-Québec. It arose from the September 1990 decision of the NEB to grant the applied-for electricity licences subject to a number of conditions. These included a requirement that the licence would remain valid to the extent that any new production facility required by Hydro-Québec to supply the exports will have been subjected, prior to construction, to the appropriate environmental assessment and review procedures as well as to the applicable environmental standards and guidelines in accordance with federal government laws and regulations. Other conditions were that Hydro-Québec file with the NEB a summary of all environmental impact assessments, government authorizations received, and a statement of Hydro-Québec's mitigation measures; and that the generation of thermal energy to be exported not contravene relevant federal environmental standards or guidelines.

In issuing licences subject to these environmental conditions, the NEB had regard both to the Environmental Assessment and Review Process (EARP) Guidelines Order and its own powers under the *National Energy Board Act*, on an application for an export licence, to "have regard to all considerations that appear to it to be relevant" and to impose terms and conditions on any licence. The arguments before the Court lasted five days and many alternative arguments were made concerning the NEB's role under the EARP Guidelines Order and the breadth of its authority under the *NEB Act* to consider environmental issues when issuing export licences. A related appeal by the Cree sought to quash the export licences. That appeal was dismissed.

The Court observed that the environmental conditions in question related entirely to the facilities required to produce the electricity, and determined that the key question was whether the NEB's jurisdiction extended to facilities for the production of goods for export. That is, the key question was whether the NEB could make the granting of a licence to export certain goods subject to conditions pertaining to their production. The Court was of the view that a negative answer to this question would make any question about the EARP Guidelines Order

academic. The Court was further of the view that the answer to the question should be negative.

The Court noted that the NEB's jurisdiction was to decide whether or not to grant the authority to export electricity. The factors relevant to considering an export application and the conditions which the Board may place on any export authority granted "clearly cannot relate to anything but the export of electricity."

The Court referred to the definition of "export" which, in the case of electricity, speaks in terms of sending from Canada power produced in Canada. It was clear to the Court that export does not cover production itself. This appeared to the Court to be reasonable in that, while a person wishing to export a good must produce it or arrange for its production, a person may produce a good without exporting it.

The Court did not dispute that, in considering an application to export electricity, the NEB must be concerned about environmental consequences since the public interest is involved. However, it was of the view that the only question concerns the environmental consequences of the export, namely, the consequences for the environment of sending the power produced in Canada from Canada. The Court considered that it might be possible to conceive of a situation in which a production facility was so much a part of export operations that it would be possible to bring the use of the production facility within the Board's jurisdiction, although it expressed strong doubt as to the likelihood of this occurring. The Court was satisfied, however, that this was not the case with Hydro-Québec. It found that the Hydro-Québec construction projects which would produce the electricity for the export—the James Bay Phase II development—formed part of Hydro-Québec's overall operation of its electric generating facilities and transmission network, and that carrying out the construction projects was not in any way connected with the exports.

The Court concluded that the serious environmental questions which were raised by the construction of these projects were the responsibility of other authorities and that those authorities have no need of the NEB's support to carry out their duties. The Court concluded that the NEB exceeded its jurisdiction in imposing the environmental conditions.

This conclusion did not lead to the setting aside of the NEB decision to grant the licences. Rather, the Court took the unusual step of determining that the two conditions were severable and struck down only the environmental conditions, leaving Hydro-Québec with the export authority which it desired.

The case is interesting for a number of reasons. Firstly, the Court does not consider the role of the NEB in applying the EARP Guidelines Order. This is because it considered that the environmental issues related to the production of electricity were not proper for the NEB to consider in granting an export licence. Earlier Federal Court of Appeal decisions concerning disputes over the Rafferty-Alameda Dam project and the Oldman River project have made it clear that the EARP Guidelines Order is a law of general application which must be followed by federal authorities in carrying out their duties. The Hydro-Québec case suggests that the starting point for analysis is to define the scope of the underlying authority which is being exercised. Thus, the Court looked at the jurisdiction of the NEB to grant electricity export licences and, having determined that the authority did not embrace the production of electricity, found it unnecessary to consider the EARP Guidelines Order. This suggests, therefore, that the EARP Guidelines Order must be read as operating within the scope of the underlying jurisdiction of the relevant federal authority and does not expand that jurisdiction.

If this is the right interpretation of the Court's judgment, then the scope of review under the EARP Guidelines Order itself may be significantly narrowed. The EARP Guidelines Order has been drafted with a view to encouraging and facilitating the broadest consideration of the potential environmental and social effects of projects. A full public review is contemplated simply on the basis of public concern about a project even if, in the absence of such concern, those with the necessary technical information would not consider a public review necessary. The Guidelines Order also contemplates that effects external to Canada should be considered. The effect of the Court of Appeal's judgment would appear to be that the scope of environmental review under the EARP Guidelines Order cannot extend beyond the scope of the underlying federal authority. This is at

odds with the philosophy underlying the Guidelines Order, as well as with the expectations of many of those who look to the Guidelines Order as a vehicle for voicing their concerns. The latter point can easily be demonstrated by reference to the scope of EARP public reviews which have been undertaken to date.

The Hydro-Québec judgment also has significant potential to narrow the scope of NEB review, not only of export projects, but also of projects involving the construction of new facilities, including oil and gas pipelines. The NEB authority with respect both to export licences and to construction of new facilities is to consider all matters that appear relevant to it. The NEB has traditionally taken this language to mean that it may cast a wide net in its consideration of both export licence applications and applications to construct new facilities. So, for example, in a 1980 application to construct an oil pipeline linking Canada to a proposed new oil tanker terminal in the State of Washington which would receive shipments of Alaska oil coming down the west coast of Canada, the NEB determined that it was relevant to consider the potential environmental implications of the tanker traffic. The rationale was that some of the potential environmental risks associated with the tanker traffic would not occur if the terminal was not built, and the terminal would not be built without the pipeline. The NEB did not purport to regulate tanker traffic but purported only to regulate the pipeline. The applicant, TransMountain Pipeline Company, was required to introduce evidence to demonstrate that the environmental risks associated with the tanker traffic were acceptable as part of making its case that it should receive authority to construct the pipeline which was an integral part of the overall project. Similarly, the NEB has cast a wide net in considering the social and environmental implications of projects involving bringing natural gas out of the Arctic.

The Hydro-Québec judgment will require a reassessment of how the Board views its jurisdiction to authorize exports as well as the construction of new facilities with a view to determining, firstly, the proper scope of that jurisdiction and, secondly, the proper scope of the environmental review associated with the exercise of that jurisdiction. The EARP Guidelines Order would become relevant only within the proper scope of the NEB's underlying jurisdiction with respect to exports and new facilities construction.

CRTC CONDUCTS FIRST TELEGLOBE CANADA PUBLIC HEARING

By: John F. Blakney
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From August 12 to 28, 1991, the CRTC held a major public hearing into a number of matters related to the regulation of Teleglobe following the four-year transitional period established at the time of Teleglobe's privatization. This transitional period ends on December 31, 1991.

The CRTC's original public notice providing for this hearing indicated that the Commission was interested in examining five areas:

1. matters arising from the transitional period (principally what to do with any revenue excess or shortfall arising during the transitional period, valuation of Teleglobe's rate base at the end of the transitional period, and whether an appropriate capital structure should be fixed for regulatory purposes at the end of the transitional period);
2. the extent to which Teleglobe exercises market power in its major business segments;
3. the form of regulation to be applied to Teleglobe after the transitional period;
4. what service conditions should be put into place to ensure high quality telephone service from Teleglobe; and
5. whether the rules governing the resale and sharing of Teleglobe services should be further liberalized.

In addition to these questions, the CRTC also added to the proceeding its review of Teleglobe's 1991-1995 capital plan (construction program review), Teleglobe's application for amendments to its interconnection agreement with Telecom Canada, and certain follow-up issues arising from the Commission's decision on the regulatory treatment of Teleglobe's cash advances to its parent Memotec Data Inc. arising from Telecom Decision CRTC 1991-5.

Teleglobe's regulatory framework is unique among federally regulated telephone companies in that the *Teleglobe Act* itself provides the CRTC with power to cease regulating Teleglobe activities where it finds that the activity is subject to sufficient competition to ensure that Teleglobe

will charge just and reasonable and non-discriminatory rates. In this proceeding, Teleglobe applied to the Commission for regulatory forebearance for all its services other than international telephone services. The type of forebearance it requested involved both a removal of the prior tariff approval requirements and elimination of the statutory requirements for just and reasonable and non-discriminatory tariffs. To protect the interests of international telephone service users, Teleglobe proposed the implementation of a broad service category costing system, the results of which (starting in 1992) would be used to insulate international telephone service users from revenue shortfalls that might occur in the non-telephone service categories. In 1992, conventional rate-base/rate-of-return regulation would still apply to Teleglobe's telephone service rates and corporate profitability. However, Teleglobe's rate of return would be averaged over a rolling four-year period for the purpose of determining the need to adjust telephone service rates. Teleglobe also indicated that before the end of 1993 it intended to make an application to the Commission for approval of an alternative form of regulation to conventional rate-base/rate-of-return regulation. This alternative would likely focus more on creating stronger incentives to improve productivity and service performance than are inherent in conventional rate-base regulation, and on price as a measure of corporate performance rather than cost containment and profitability. Finally, Teleglobe indicated that the circumstances which would support complete deregulation of all its telecommunication services would likely arise before the end of the decade.

For example, with respect to liberalization of resale and sharing to provide, for interconnection of Teleglobe private line services by resellers to domestic or foreign telephone companies' switches (to provide interconnected voice services that would be a substitute to international telephone service), Teleglobe foresaw that liberalized resale competition, subject to certain conditions, would likely have benefits both to customers and to the company itself. The conditions that Teleglobe has sought to permit such liberalized resale are a prohibition against facilities-based carriers or their affiliates becoming overseas service resellers, an international agreement structure, and CRTC prohibitions against resellers "hubbing" their services in foreign jurisdictions. "Hubbing" means the use of a foreign carrier or foreign switch to redirect Canadian-originated traffic into a third country or to assemble traffic from third countries for transmission to Canada.

In April 1991, Teleglobe Canada reached an agreement with Telecom Canada to revise significantly their system interconnection and operating agreement. This interconnection agreement and the settlement paid to Telecom Canada had not changed materially since 1975. Under the proposed amendment, Telecom Canada would receive significantly lower settlements in 1991 for the assembly and distribution of overseas traffic. The parties have also agreed to further Telecom Canada settlement reductions over the next several years. Teleglobe will now receive a fixed per-minute remittance for all outgoing telephone calls. The retail price to Canadian users of overseas telephone service will continue to be established by Teleglobe. The proposed amendments, however, would permit Telecom Canada to establish discounts (from the basic retail price established by Teleglobe) pursuant to optional calling plans such as Advantage Canada.

At the hearing, Teleglobe also advised that it intended to enter into negotiations with Telecom Canada and other domestic service providers this fall. These will establish a new network access tariff which would replace its interconnection arrangements with domestic carriers. The tariff would be submitted to the CRTC for approval near the end of the first quarter of 1992, to be implemented in mid-1992. Under this arrangement all domestic service providers, whether carriers or resellers or private network operators, would acquire Teleglobe's overseas telephone services at Teleglobe's gateways under non-discriminatory rates in terms of service. Users would then be charged for the overall overseas service by the domestic service supplier.

Teleglobe's application for regulatory forebearance and its proposed interconnection agreement amendments are both based on the view that the international telecommunications market is inherently competitive and that actual levels of competition, particularly in the non-

telephone service segment, are now equivalent to those of a normal non-regulated business. Teleglobe maintained this position even in the face of the bypass restrictions authorized by CRTC Decision 1991-10 in light of the highly developed private network structure in North America, the discretionary nature of Teleglobe's policy protections from competition, and the intense rivalry that currently exists from U.S.-based carriers and resellers.

The Commission's decision is expected before the end of the year.

MARATHON CRTC LONG DISTANCE COMPETITION HEARING CONCLUDES

By: John F. Blakney
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On July 5, 1991, the CRTC concluded its public hearings into the applications of Unitel and BC Rail/Lightel (BCRL) for authorization to interconnect with the switches of federally regulated telephone companies for the purpose of providing public long-distance telephone services in their telephone companies' territories (Ontario, Québec, British Columbia, Newfoundland, New Brunswick, Prince Edward Island and Nova Scotia).

These were the longest public hearings in the CRTC's history, lasting some 53 days and generating over 16,000 pages of written evidence and over 4,500 pages of written argument. A decision of the Commission is expected in the early months of 1992.

The proceeding was activated by applications of particular firms, as opposed to being a general inquiry initiated by the CRTC into the merits and appropriate conditions of long-distance competition. As a result, it focussed largely upon the specific network and service plans of the applicants, the applicants' possible financial performance under various engineering market and service configuration assumptions, the impact on industry efficiency of entry by the applicants and, in particular, the impact of the compensation the applicants proposed to pay to telephone companies for funding low-cost local telephone service (called an "access contribution"). The access contribution impact was tested from several perspectives including the impact on local telephone rates, on the regulatory process, and on industry efficiency.

By far the largest part of the evidence focussed on the reasonableness of the assumptions employed by the applicants in their business plans and supporting draft financial statements, and the sensitivity of alternative assumptions. Both applicants and carrier respondents assumed that no regulator was likely to be persuaded that it should grant entry to a business which would fail. Several other factors served to reinforce this preoccupation with respect to entry through carriers with interconnection to provide public long-distance competition. First, in its earlier 1985 decision which denied a similar application from Unitel's predecessor (CNCP Telecommunications), the Commission's reasons indicated that "uneconomic entry" would not be in the public interest because such an entrant, to stay in the market, would demand that the Commission approve increasingly attractive access contributions for the new entrant. The result of this process would be regulated market shares, possibly higher local rates and reduced industry efficiency. Second, the access contribution, which is in effect a regulatory tax imposed on interexchange carriers and their customers to help suppress the prices of local services and hence the bills of customers that do not use long-distance service of the interexchange carrier, would be a very large amount of money and a very high percentage of an entrant's costs (approximately three-quarters of Unitel's costs under its business plan). Finally, there was the perceived need to avoid the appearance of causing higher local rates through the introduction of telecommunications competition, a concern which subsequently became a cornerstone of Canadian telecommunication policy as articulated by the federal Department of Communications.

Not surprisingly, then, the principal assumption tested by respondents in this proceeding was the access contribution

mechanism and the level of this charge proposed by the applicants. Unitel contended that existing telephone company costing systems overestimate telephone company requirements for access cross-subsidization, and that in calculating future access contribution charges, new entrants should essentially have to pay for the access contribution foregone by the telephone companies as a result of traffic taken away from them by new entrants, but not for new traffic generated by competition. Unitel also contended that new entrants should have an access contribution discount for a start-up period to reflect the less-than-perfect network access the new entrant would obtain. The carriers replied that their costing systems were accurate, that Unitel had underestimated the inherent rate of growth of a monopoly market (and thus underestimated the access contribution foregone as a result of competition), and that the contribution charge scheme proposed by Unitel and BCRL would be circumvented by them, in any event, by connecting major customers with direct access lines that were not subject to the per-interconnection trunk access contribution mechanism proposed by these entrants. Again, as in 1984-85, they contended that a contribution discount would encourage "uneconomic entry" and that the CRTC would, without tough proactive contribution rules, be inevitably drawn into balancing market shares through access contribution adjustments.

Not surprisingly, Unitel and BCRL contended that, as a result of the public long-distance competition they were proposing, industry and incumbent firm productivity would improve more quickly in terms of product innovation, price differentiation and cost-revenue relationships. This has generally been the case when competition has been introduced into previous monopoly markets.

More surprising, however, was the extent to which new respondent telephone companies contended that the interexchange and local exchange portions of their business constituted a natural monopoly. That is, the telephone company respondents led by Bell Canada asserted that not only would entry by Unitel or BCRL on the terms proposed result in less industry efficiency, but also that *any* form of facilities-based interexchange competition would also be inefficient.

The telephone companies used two principal arguments to support this proposition. Firstly, they argued that incumbent carriers' marginal costs of interexchange switching and transmission capacity would always necessarily be lower than the marginal costs of such facilities investments made by a new start-up firm having no interexchange plant base of significance to build upon. Secondly, they maintained that there are great future efficiencies to be gained from vertically integrated local and long-distance network components. Thus, permitting interconnection of competitors at a particular switching facility in particular markets under this model would be viewed as necessarily disrupting the ability of the carrier to generate efficiencies through single network planning.

Perhaps the most surprising aspect of this natural monopoly position is that it was advanced at the same time as both Unitel/BCRL *and* the telephone company respondents were all emphasizing the increasing rate of technological obsolescence and technological change in their industry, the importance of service and labour force innovation to increase network productivity, and the declining importance of plant costs in the overall cost structure of the firm. To the extent that these latter considerations are given weight, the importance of a static comparison of marginal plant costs between an incumbent and a new entrant at a given structure of new and current technology and a given network configuration becomes a less compelling argument in favour of the *status quo*.

As additional support for the natural monopoly position, the respondent telephone companies presented a rate plan for the next ten years which they maintained would produce rate levels equivalent to those which under the most optimistic assumptions could flow from facilities-based entry as proposed by the applicants. The respondent telephone companies contended that these rate revisions would keep Canadian long-distance rates at a level comparable to expected U.S. long-distance rates over that period of time. Upon closer inspection, these plans incorporated slightly more optimistic long-distance market and productivity growth rates than had occurred in the 1980s and concentrated the benefits thereby derived on larger businesses through lower rates

for services directed at these customers. Little service innovation was assumed.

The final arguments of the interveners represented the full range of interests from pro-*status quo* to pro-competition. The bulk of the submissions supported increased domestic long-distance competition through facilities-based supplier interconnection. The initial start-up costs of facilitating such interconnection were not viewed as a serious impediment, nor was the capacity of the CRTC to calculate and enforce a reasonable competitor access contribution seriously doubted. Some parties which, in 1985, saw long-distance competition as necessarily resulting in socially unacceptable local rate increases have modified their views. There appears to be general reconciliation to the inevitability of some rate rebalancing (local services covering a higher share of fixed access costs), with or without long-distance competition. Recent U.S. experience is also undeniable: subscriber drop-off and local rate increase issues have been managed over the last five years and are no longer policy concerns. There is also increasing concern that the Canadian telecommunication service sector will, in the future, underperform the telecommunication sectors of its major international competitors most of which have opted for long-distance competition, or soon will.

While increased competition is favoured, there is somewhat less endorsement of the specific proposals of Unitel and BCRL, particularly Unitel's request for an access contribution discount and its expectation that the benefits of vigorous competition can be realized without significant changes to the current CRTC system of individual tariff justification and approval.

This puts the CRTC in a difficult position. It can disallow the applications, as it did in 1985, on the basis that they were too sweet for the applicants and risk no further future applications. After all, Unitel is presently the only potential national long-distance competitor. It can allow them on their terms and risk being accused of condemning itself to an indefinite period of market management and handicapping in favour of new entrants. Or it can allow the applications on different terms—in particular, a different access contribution structure—and return the ball to the Unitel/BCRL court.

This having been said, the CRTC's situation is in essence no different than that of any regulator faced with specific applications for entry permission into a market which has, to date, been supplied by one firm. The case differs from a trucking industry licensing case in public visibility, the extensiveness and detail of the evidence, and the amount of money at stake, but not with respect to the nature of the arguments pro and con.

NEB DENIAL OF PIPELINE APPLICATION CREATES STORM OF CONTROVERSY

By: Lawson A.W. Hunter
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In July 1991, the National Energy Board denied an application by TransCanada Pipelines for the construction of a short pipeline costing $24 million to connect TCPL's existing Niagara Line to a new export point on the Niagara River at Grand Island for a connection with the proposed Empire State pipeline. The NEB determined that the gas to be transported for Empire could be delivered via TransCanada's existing Niagara Line through the existing export point at Lewiston, and that this alternative would be economically and environmentally superior to construction of a new line.

Taking delivery of the gas at Lewiston would require Empire either to reconfigure its project so that its own line would connect with TCPL at Lewiston or to arrange for transportation on the existing pipeline facilities which connect with TCPL at Lewiston.

The Empire project has indicated that it has no desire to take service from the existing interstate pipelines in the area. Empire has put forward its project as an intrastate pipeline subject to New York authority on the basis that its project will provide additional competition to the existing pipelines which serve New York consumers. A

substantial amount of the gas to be transported by Empire is U.S.-sourced gas which would be transited through Canada on the TCPL system.

The NEB's denial of the proposed pipeline has been construed by some, including U.S. producers and some U.S. Federal Energy Regulatory Commission members, as being contrary to free trade. TCPL, along with the Empire sponsors, have initiated a review application before the NEB to reverse the decision. It has been argued, among other things, that granting approval for the new pipeline would be consistent with free trade as well as the *Transit Pipelines Treaty*. That *Treaty* between Canada and the United States provides for the non-discriminatory treatment of natural gas which transits either country. The *Treaty*, however, preserves the jurisdiction of regulatory agencies in each country with respect to the construction and routing of new pipelines. In addition, the *Free Trade Agreement* is made subject to laws of general application such as the laws governing the construction and routing of new pipelines.

Once again, energy regulatory action is being questioned not primarily on the basis of the actual statutory authority which exists, but rather on the manner in which that statutory authority should be exercised in light of the *spirit* of free trade.

A decision by the NEB on the review application is pending. In a related matter, one of the parties to the hearing, a U.S. interstate pipeline, is challenging the NEB's review process on the grounds of a denial of natural justice and bias associated with a meeting which took place between some NEB members and representatives of some of the parties making the review application. The meeting occurred a few days before the review application was filed and shortly after the NEB released its reasons for decision. This action in the Federal Court of Canada is also pending.

CRTC APPROVES BYPASS RESTRICTIONS

By: John F. Blakney
Fraser & Beatty, Ottawa

In a decision dated June 26, 1991 (Telecom Decision CRTC 1991-10), the CRTC approved the amendment of federally regulated telecommunication carrier tariffs to prohibit the routing by customers of basic service traffic by way of the United States when that traffic originates or terminates in Canada. The carriers have interpreted the term "basic service traffic" as referring to services other than enhanced telecommunication services as defined by past CRTC decisions.

The proceeding that led to this decision was initiated by an April 1990 Teleglobe Canada application requesting that the general tariffs of Bell, BC Tel and Unitel be amended to prohibit resellers from using transborder services to route interconnected voice traffic to and from overseas destinations via interconnection with the facilities of carriers in the United States. Teleglobe's application was based on a statutory obligation to provide public international telecommunication services, various CRTC rulings with respect to traffic that may be routed to the United States under Canada/U.S. Carrier interconnection agreements, and government policy statements favouring the use of Canadian facilities. The respondent carriers generally supported Teleglobe's application but also noted that U.S. bypass was becoming a problem for them as well.

The CRTC broadened the proceeding in September 1990 by issuing a public notice which requested comment on whether Teleglobe's arguments also applied to data, non-interconnected and private line traffic, and whether the concerns raised by Teleglobe with respect to Canada/overseas traffic carried through the United States were equally relevant to Canada/Canada traffic carried over U.S. facilities. The CRTC also wished to examine whether restrictions on the use of Canada/U.S. private lines could be effectively and uniformly enforced, whether the potential for Canada/overseas and Canada/

Canada traffic bypass and revenue loss was significant, and whether there were other approaches to dealing with bypass other than tariff prohibitions.

At the time of Teleglobe's privatization in 1987, the Department of Communications (DOC) stated that one of the government's policy goals was to facilitate the efficient use of Canadian network infrastructures by ensuring the carriage of Canadian telecommunication traffic on Canadian network facilities. With reference to Teleglobe, DOC stated that it was in the national interest that telecommunication services between locations in Canada and from Canada to other locations be provided over Canadian-owned or Canadian-controlled facilities to the greatest extent feasible. DOC indicated that it would rely on existing regulatory mechanisms, and specifically approval of interconnection agreements, to ensure that overseas routing via Teleglobe facilities was maintained. For example, all Canada/U.S. interconnection agreements approved by the CRTC contain a provision that prohibits the transmission of overseas traffic between the interconnecting carriers unless Teleglobe is technically incapable of handling the traffic.

Not surprisingly, the carrier parties supported the extension of bypass controls to non-switched traffic and to Canada/Canada traffic, and user interests opposed the proposed controls. There was a consensus among all parties that the most effective long-term remedy for bypass would be comparable Canadian and American inter-exchange rates. The carriers indicated that identification of bypass activities could be technically difficult and costly and that customer affidavits would be intrusive and likely ineffective. Generally, carriers indicated that bypass had been increasing in significance over the several years. In Teleglobe's case, U.S. carriers had introduced new overseas discount services in 1990 specifically directed at Canadian customers connecting at a U.S. carrier switch near the border through a Canadian/U.S. private line. The Commission agreed that additional bypass restrictions and carrier tariffs were necessary and that they should apply to both Canada/overseas and Canada/Canada traffic with the exception of non-basic or enhanced traffic. However, the decision also emphasizes that lower prices are the only satisfactory long-term solution to bypass prospects.

Following the decision, a number of Canadian resellers announced that they would not route overseas traffic via their Canada/U.S. network structures.

The impact of this decision on overseas and domestic bypass will likely be very difficult to estimate.

It is likely that the decision will have a certain short-run chilling effect on commercial suppliers of switched work services such as resellers, at least with respect to their consumption of additional services from facilities-based carriers after the new tariff restrictions are implemented. Even here, however, the difficulty in monitoring bypass traffic and pressures that may be created by continuing Canada/U.S. domestic and overseas price spreads may mitigate the impact of Decision 1991-10.

Many consider that the main threat of bypass does not come from resellers but rather from multi-national business organizations which have developed North American and global private telecommunications networks. Many such organizations have already built up sophisticated networks which they are unlikely to alter in order to obey the letter of the CRTC's no-bypass decision. It may also be doubted that this decision will have a significant impact on the consumption of incremental services or facilities for these networks, particularly where the network planning and purchasing decisions are made outside Canada or where the core switching or routing functions are outside Canada.