

CANADIAN COMPETITION RECORD

REGULATORY AND TRADE DEVELOPMENTS

CANADIAN TELECOMMUNICATIONS REGULATION AND POLICY: 1999 REVIEW

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1. Introduction

This article reviews principal developments in the administration of Canadian telecommunication regulation and policy by the Canadian Radio-television and Telecommunications Commission ("CRTC") during 1999.

1999 has been marked by a continuation in the CRTC's practice of withdrawing from direct rate regulation in newly competitive markets, encouraging the implementation of local services competition primarily through oversight of industry standards-setting bodies coupled with highly focused intervention to remove barriers to entry, and developing more focussed measures to ensure universally available affordable basic telephone services. With the increased narrowing of the CRTC's role, the Canadian telecommunications service sector is increasingly subject to regulation under the *Competition Act*. As well, CRTC remedies are themselves increasingly structured along the lines of antitrust remedies with a clear preference for structural, negotiated, limited duration solutions over the behavioural, supervised, and indefinite duration remedies more typical of direct economic

regulation.

No fundamentally new telecommunication policies were implemented in 1999, the course towards increased competition, deregulation, and relying on investors to select appropriate technologies having been firmly established by the mid 1990's in Canada.

The main industry trends in 1999 were: massive investment in broadband data technology, increasing popularity of wireless telephony, deployment of high speed consumer Internet Access Services ("IASs") by both telephone and cable companies, rapidly declining voice long distance rates (with many experiments in flat rate long distance subscription packages), and increasing industry consolidation through mergers of established carriers with new long distance and local entrants.

2. Internet Services

(a) Regulation

After lengthy hearings in late 1998 on an appropriate regulatory framework (if any) for Internet services, the CRTC advised in May 1999 that it could find no public policy basis for regulating Internet access or content services under either the *Telecommunications Act* or the *Broadcasting Act* (Public Notice CRTC 1999-84, Telecom Public Notice CRTC 99-14). The

CANADIAN COMPETITION RECORD

Commission published on December 17, 1999, an unconditional order exempting such services from broadcasting regulation (Public Notice CRTC 1999-197).

It remains to be seen, however, how permanent the Commission's decision to exempt Internet content services from broadcasting regulation will be, given the emergence of Internet-based programming substitutes to conventional free and pay television services.

(b) Carrier Internet Distribution Facility Access

In mid-1998 the CRTC ruled that cable TV services were acting as telecommunication carriers in the supply of consumer IASs (basically a LAN-based broadband channel to residences offering much higher speed than conventional dial-up modem services), and that, in line with established CRTC policies in other markets, cable TV companies should provide a resellable version of that service to independent Internet Service Providers ("ISPs").

Following lengthy but fruitless negotiations between ISPs and the cable industry relating to service design and pricing, in mid-1999 the CRTC responded to an ISP application for direct relief by ordering larger Canadian cable companies to supply their existing high speed consumer access service to ISPs at a 25% discount over the best available retail rate in a cable company's market (Telecom Decision 99-11). One cable company has appealed this decision. It remains to be seen, however, how significant the CRTC's order will be. Over the last year a very large portion of the 'independent' ISP sector (with the notable exceptions of AOL Canada and PSINet Canada and its affiliates) have been acquired by larger general telecommunication service suppliers.

In late 1998, Bell Canada, Canada's largest full service carrier with a dominant position in the Ontario and Quebec telecommunications services markets, began offering in major cities a new low cost high speed IAS to compete with the cable TV service based on the newly developed Nortel Networks 1 mbps modem which has been designed as a simple add-on component in Nortel central office digital switches. This service offers "always on" capability with downlink speeds comparable to the high-speed cable service. It replaces high speed and higher cost Asymmetric Digital Subscriber Line residential services.

The pricing of this new service (which was designed in part to meet the cable service price) formed the basis of a complaint by independent ISPs to the CRTC and to the Competition Bureau alleging predatory pricing and abuse of dominant position, since no resellable wholesale version of this service was initially available.

However, both complaints were dismissed. The Competition Bureau, in its announcement, went out of its way to emphasize the highly dynamic and competitive nature of the Canadian Internet services sector, and accepted the telephone company's argument that its access service pricing, while below cost, was not predatory but rather was a necessary price matching response to the cable TV service as both suppliers sought to develop a high speed consumer access market (Competition Bureau News Release¹ and Backgrounder published 1999-03-17).

As well, in early 1999 a Bell Canada Internet services affiliate began to offer a wholesale priced 1 mbps modem-based product designed for ISP resale, which a number of independent ISPs have taken up.

CANADIAN COMPETITION RECORD

As a result of these developments, and supported by a hands-off regulatory stance, Canadian consumers can now take advantage of intensive competition in the supply of both low speed (dial-up) and high speed IASs. As well, Canadian Internet content suppliers have the security that there is no current regulatory interest in special regulatory measures, beyond general measures such as copyright and criminal-based constraints being developed for their industry. Barriers to entry in the high speed IAS market segment have been substantially reduced through the introduction of resellable wholesale services by cable companies and Bell Canada.

3. Long Distance Services

In 1999, the long distance sector was marked by continuing rate decreases, greater consolidation of long distance services and mergers with local service suppliers, ongoing selective deregulation, and competitor pressure to revise the local service subsidy mechanism.

(a) Selective Long Distance Deregulation and Competition

In 1998, the CRTC elected to forebear from regulating long distance service rates for the former monopoly integrated local/long distance carriers that had formerly comprised the Stentor group of companies. Still however, under price cap regulation these companies' basic long distance rate schedule cannot be revised upward. Long distance competition has yet to be allowed by the CRTC in the territories of certain carriers that serve primarily remote and northern areas, although the Commission has stated that it will review these policies.

As of the end of 1998, Stentor, the integrated

carriers' co-ordinating body, was terminated by its members. This removed that last institutional barrier to the former Stentor members competing in each other's former "exclusive territory". As a result, 1999 saw efforts by the largest former Stentor members, BCTel/Telus (dominant in British Columbia and Alberta) and Bell Canada (dominant in Ontario and Quebec and which also effectively controls the Atlantic province telephone companies), to sell business (particularly data) services outside their original territories and to establish separate competing national data networks.

In 1999, the CRTC elected to forebear from regulating the two remaining significant long haul services which had continued to be subject to detailed rate and tariff regulations: Teleglobe Canada's Globeaccess Tel services (Telecom Decision 99-14) and Telesat's Fixed Satellite Services (Telecom Decision 99-6).

Globeaccess Tel is Teleglobe's most significant switched overseas telephone service and is sold on a wholesale basis to various Canadian long distance carriers which act as retailers. The CRTC concluded that, with the 1998 removal of routing restrictions on international services which effectively permitted Canadian carriers to acquire wholesale switched overseas services from US or other foreign carriers, Teleglobe's pricing would be effectively constrained by competition. Teleglobe's evidence had identified more than 50 competitors and potential competitors and had described Internet marketplaces through which service providers can obtain transmission capacity or services to virtually all destinations served by Globeaccess Tel.

The Commission has also approved the deregulation

CANADIAN COMPETITION RECORD

of Telesat Canada's Fixed Satellite Services ("FSS") available from March 1, 2000 but subject to a transitional structure involving a price ceiling. FSS are the satellite RF Channels used by broadcasters to distribute signals to broadcast distribution undertakings as well as by Direct to Home ("DTH") service providers. FSS are also used to provide telecommunication services for government and business applications and for telephone service to the far North and to remote areas.

Telesat is no longer required to file tariffs for RF Channel services over FSS provided after March 1, 2000. Under this transitional structure, Anik E satellite rates are fixed to December 31, 2000. There will be a fixed price ceiling for full period, unprotected pre-emptible RF Channel service for lease terms of five years after December 31, 2000 for Anik E service and from the in service date of the yet-to-be-launched Anik F series. In two previous decisions the Commission had denied Telesat forbearance applications but had nevertheless provided the company with greater pricing flexibility by adopting a price ceiling approach.

As a result of the WTO General Agreement on Trade in Services, Canada has agreed to permit competition in the provision of FSS starting March 1, 2000. Telesat's evidence indicated that it had negotiated a substantial number of long term contracts for Anik F series capacity with customers who would otherwise have been able to negotiate with competitive US suppliers (Telesat and US satellite supplier footprints over Canada are very close). This, Telesat contended, provided strong evidence of adequate alternate sources of supply and of the reasonableness of its rates and service terms on a going forward basis. The Commission

concluded that opportunities for RF Channel resale would likely ensure the provision of adequate capacity at reasonable prices to remote areas and to customers not in a position to contract directly for long term capacity.

(b) Local Service Subsidies

As part of a plan to maintain subsidy support for local services in high cost areas with the implementation of a price cap form of local carrier monopoly service regulation, the CRTC froze the per minute long distance "contribution" charge component of long distance carrier local network access charges. A number of long distance carriers had sought a lifting of this "frozen" contribution level and a return to periodic revision of contribution charges based upon annual local subsidy and long distance traffic forecasts. They had contended that a dramatic traffic increase starting in 1998 had resulted in a contribution windfall to local exchange carriers. After a detailed review of submissions and traffic data, the CRTC, in late 1999, disagreed that actual traffic levels were dramatically above its expectations and declined to terminate its four year contribution freeze (Telecom Decision 99-20). Instead, the CRTC concluded that any contribution rate adjustments would have to be predicated on a general review of its contribution collection mechanism (discussed next).

A number of long distance service suppliers have also argued that the "per minute" contribution collection mechanism which has been in place since the implementation of "equal access" long distance competition in 1993, and which is based upon circuit-switched technology, unfairly discriminates against message rated services and fails to recognize the increasing significance of data services and Internet communications, which

CANADIAN COMPETITION RECORD

utilize packet-switched technology, and the increasing range of other possible contribution generating services.

Under the present contribution mechanism, long distance carriers pay a per minute contribution charge to the local carriers at both the originating and terminating switches for a call. As well, for some data services a flat monthly contribution charge based upon a percentage of the service's monthly rate is assessed. This data line contribution surcharge has been extended to data services used by ISPs where such lines are used to supply Voice-Over-The-Internet ("VOTI") long distance services where some element of analogue voice to Internet Protocol conversion takes place within the ISPs' network. This policy effectively requires ISPs to establish discrete VOTI-capable and non-VOTI networks to minimize contribution exposure. Moreover, the level of contribution on VOTI-capable circuits is a fixed monthly charge and is assessed regardless of the actual level or price to the customer of VOTI traffic. This CRTC contribution position has undoubtedly discouraged the development in Canada of VOTI services, although some ISPs do offer long distance services as conventional long distance service resellers.

To address these perceived inequities, the CRTC has initiated a general review of the range of services subject to contribution payment and the collection mechanism (Telecom Public Notice 99-6). It is arguable that packet-switching technology and per minute switch-based contribution charges are incompatible. It is also arguable that the CRTC has relied far too long upon conventional long distance services as the principal generator of basic local service subsidies. Long distance has for some time ceased being a premium product and has become a low-priced commodity (for which

contribution now makes up a very large portion of carrier costs and the retail price), while at the same time the range and revenue generation of non-basic local (or vertical) services has grown markedly and there has been a rapid growth in data relative to voice traffic. The simplest and most equitable alternative would seem to be an *ad valorem* surcharge on all premium or non-basic services.

4. Local Competition

Most implementation issues to provide for local landline switched voice service competition (as authorized by the CRTC in 1997) had been settled by 1999. However, competitive entry has been much slower than occurred for long distance services. To date, Competitive Local Exchange Carriers ("CLECs") have targeted only business customers in larger urban centres. This reflects the relatively higher investment required for CLEC entry, the CRTC policy of not setting Incumbent Local Exchange Carrier ("ILEC") access charges at low entry stimulating levels, and the absence of high incumbent profit margins that would facilitate dramatic discounting by new entrants. New entrants must therefore compete more on service quality and attractive bundled prices than on individual service pricing. However, in late 1998, the CRTC did set final rates for unbundled ILEC local services (local network components such as local loops, 911 service, and message relay service, that are made available to local competitors), which were generally lower than interim rates approved in 1997 and which are based upon recovery of incremental costs only plus a 25% mark-up.

In 1999, the CRTC's attention was directed more towards ensuring that landline carrier access to buildings and rights-of-way was not frustrated or made unreasonably costly as a result of action by

CANADIAN COMPETITION RECORD

right-of-way and property owners. As a result, the Commission has prohibited agreements whereby a particular local exchange carrier would be the exclusive landline telephony supplier to multiple dwelling unit buildings. The Commission also determined that the service provider demarcation point for telephone wire and related facilities used by a local telephone company will be located in the main terminal room of each building where the local telephone company obtains the property owner's written acceptance of responsibility for in-building wire and related facilities (Telecom Decision 99-10).

The Commission has also been called upon to assert special remedial powers under the *Telecommunications Act* to establish reasonable cable company and telecommunications carrier access rates for municipal power utility support structures (poles and underground conduits) (Telecom Decision 99-13). The Commission has also instituted a proceeding to establish access rates for rights-of-way and other municipal property of the City of Vancouver after having previously found, based on a complaint of a fibre optics transmission system supplier, that intervention was warranted to facilitate local landline facilities competition in that market (Telecom Public Notice 99-25).

These proceedings can be expected to establish general national precedents for establishing landline carrier transmission facility access rates and terms in relation to municipal and public utility rights-of-way and other property.

5. Basic International Service Provider Licensing

As a result of recent amendments to the *Telecommunications Act*, the CRTC implemented,

as of January 1, 1999, a very light-handed regime for the licensing of all Canadian providers of basic international telecommunication services, including resellers which are not otherwise subject to CRTC regulation (Telecom Decision 98-17).

Two classes of licensee are established: Class A: facilities-based and hybrid carriers; and Class B: pure resellers. Applicants are required to supply underlying ownership and service portfolio information and a list of all interconnection or traffic exchange agreements or arrangements with foreign telecommunication service providers. Class A licensees must provide quarterly traffic reports.

The principal substantive license conditions are a prohibition against anti-competitive conduct for both Classes, and, for Class A licensees, a requirement to remit contribution on international contribution-eligible traffic.

The principal objective of this regime, as seen by the CRTC, is to detect and prevent possible exercises of monopoly power over international traffic routing, particularly by foreign carriers.

6. CRTC/Competition Bureau Interface

With the increasing, albeit selective, withdrawal by the CRTC from direct regulation of telecommunication carrier conduct, the provisions of the *Competition Act* have become increasingly applicable to this sector.

The Competition Bureau has traditionally taken the position that the *Competition Act* applies to all business conduct which has not been approved through the direct and lawful exercise of a regulatory power. However, there has been some uncertainty expressed over the applicability of the

CANADIAN COMPETITION RECORD

Competition Act to business activity which is no longer subject to direct regulatory approval by virtue of a CRTC forbearance decision (which the CRTC can vary at any time), especially where forbearance is subject to certain ongoing conditions being met by the carrier. As well, in many cases, the CRTC and not the Bureau possesses the requisite expertise to fashion the best remedy on a timely basis.

In November 1999, the CRTC and the Bureau published a joint statement² on the interface of their respective statutory responsibilities. The statement advises that, where the CRTC has unconditionally exempted from regulation or has forborne unconditionally, the *Competition Act* will apply until that decision is varied or rescinded. The *Competition Act* will also apply to partially or conditionally forborne or exempted activities. However, the *Competition Act* would not be applied where the Commission is managing a transition to competition and prior to a formal forbearance or exemption order. In particular, the Commission's primacy in designing measures such as floor pricing standards to prevent anti-competitive cross-subsidization is recognized.

Two areas of concurrent or parallel jurisdiction are recognized – merger/change of control review, and marketing practices. The Commission's exclusive authority is recognized in relation to interconnection and access issues, having regard to its special expertise and capacity for flexible and timely dispute resolution. Finally, exclusive Competition Bureau authority is recognized in relation to criminally prohibited conduct such as price fixing and other agreements to lessen competition unduly, such as bid rigging and price maintenance.

The policy generally accords with Bureau and CRTC practice (which has to date been highly cooperative while recognizing the need to discharge separate statutory responsibilities and to respect separate statutory confidentiality requirements), as well as the views of practitioners on the appropriate division of responsibilities in the transition to deregulated telecommunication markets.

The principal benefit of the statement should therefore be in discouraging parallel complaints where one is effectively brought for tactical or harassment purposes, particularly six resident complaints which oblige the Bureau to conduct an investigation even where the issue can best be handled by the CRTC. For its part, the CRTC can be expected to make future forbearance decisions as clear as possible on the powers no longer to be exercised by it, and to carefully define the complete portfolio of transitional safeguards at the outset.

Notes

- ¹ The News Release is reproduced at page 12 of this issue of the *Record*. The related Backgrounder can be found on-line at the Competition Bureau's web-site: <http://strategis.ic.gc.ca/SSG/ct01476e.html>.
 - ² The Statement is reproduced at page 28 of this issue of the *Record*. The related Backgrounder can be found on-line at the Competition Bureau's web-site: <http://strategis.ic.gc.ca/SSG/ct01544e.html>.
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