

Appendix A - Comments on Telecommunications Regulatory Guidelines Proposed by Bell Canada

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A. *Analysis of Bell Canada's regulatory model*

1. Please see Bell Canada's August 15, 2005 submission to the Telecom Policy Review Panel, *Canadian Connection*, specifically Appendix A-2, beginning at paragraph 13 et seq. and entitled "Guidelines for Next Generation Telecommunications Regulation". I offer the following analysis of Bell's in-depth description of its proposed 'guidelines'.

"Guideline One—The current "presumption of regulation" should be replaced with a presumption in favour of the reliance on market forces" [*Canadian Connection, Appendix A-2, paragraph 16*]

2. The market analysis approach suggested by Bell Canada¹ has several merits. For example, it is desirable to make economic regulation contingent upon the status of competition in a market and to replace the presumption of regulation with a critical assessment as to whether market forces and competition can better meet the goals of telecommunication policy. Furthermore, it is reasonable to ask whether wholesale regulation can serve as a sufficient substitute for retail regulation. It is also rational to review the approach periodically. Moreover, it may be useful to provide for merit-based appeals to the judiciary.
3. However, the approach as outlined has several weaknesses. First, by making regulation solely dependent on the status of competition, it confuses means (markets and competition) with objectives of telecommunications policy. Regulation has several functions: economic regulation is primarily intended to reduce or eliminate market failure; social regulation is designed to realign the outcomes of unfettered market forces with overall societal preferences (that is, it is a means to cope with market deficiency in situations where markets and competition work in principle); technical regulation is in essence directed to reducing forms of coordination failure that might occur if stakeholders make decentralized decisions, for example, on standards. As forms of market failure other than the presence of significant market power exist, the role of economic regulation cannot be exclusively tied to the presence or absence of market power.

¹ See Bell Canada, Submission to the Telecom Review Panel, *Canadian Connection*, Appendix A-2, "Figure 1: Market Analysis Flow Chart".

4. A priori reliance on market forces, without further assessment of the presence or absence of other forms of market failure is therefore not a good guideline for policy. This is particularly the case in information and communication industries, where network effects, positive and negative network externalities, and switching costs are pervasive. Moreover, in advanced network infrastructures with their increasingly horizontal structure (physical platforms, logical payers, applications, and services), competition at higher levels of the network stack is dependent on appropriate decisions at lower levels, including choices guiding openness and interoperability. Vertical and horizontal relations in the value chain other than the immediate competitive structure of a market segment might have to be evaluated in designing an overall legal and regulatory approach. This is well recognized in other countries, which look at competition as a means to achieve efficiency but not a goal in and of itself (see also appendix A supra).

Guideline Two—Ex post regulation should be preferred over ex ante regulation wherever possible [*Canadian Connection, Appendix A-2, paragraph 17*]

5. There are no strong reasons to prefer ex post regulation over ex ante regulation in general. As it may be difficult to create an information record, reliance on ex post regulation could lead to complex and cumbersome procedures. A similar disillusionment happened after the introduction of price caps: while there were high hopes that they would reduce administrative burdens and simplify regulation, in many countries this expectation did not materialize. Moreover, most forms of regulation combine ex ante and ex post components. The real challenge is to find an appropriate mix of ex ante and ex post measures whenever regulation is warranted. Rather than requiring a preference for ex post regulation, the requirement should be that regulation is incentive compatible, that is, given the goals of telecommunications policy, creates the correct incentives under conditions of imperfect knowledge and uncertainty.
6. Having said this, it may in many cases be justified to rely more strongly on ex post design features. For example, price cap compliance is often better achieved ex post than ex ante. One of the strongest reasons for strengthening ex post components is that the regulatory agency may have insufficient information to adopt an efficient ex ante approach. It is also possible that the regulatory agency is captured by one of the stakeholders, including the incumbent service provider. Ex post regulation has the advantage that it enables suppliers to experiment with innovative business models. It also has the desirable feature that it generates actual performance data that may be used to evaluate the success or failure of a regulatory reform measure. In this sense, the proposal by the Consumer Groups to introduce safeguards when forbearing from the regulation of local services is a form of ex post regulation, as it only is triggered if certain expectations are not met.

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 [Canadian Connection, Appendix A-2, paragraph 18]

7. Boundaries on retail price discrimination are rooted in efficiency and equity considerations. From an efficiency perspective, the fact that infrastructure services often are associated with positive externalities could be used to legitimate prices that are uniform across large areas. In fact, many of the competitive service providers realize this. Mobile service providers worldwide expand access to the network by subsidizing handsets (and similar strategies are widely expected for WiMax). Furthermore, it needs to be noted that prices in competitive telecommunications services have become less differentiated by distance and location.
8. For example, Vonage offers the same choice options across all locations. Skype Out prices its services by destination and not the originating location. Mobile service providers offer one national plan across an entire nation. Price discrimination between geographic regions is only possible if a supplier has market power in an area and consumers do not have close substitutes available. Thus, it may be in conflict with the basic equity goals at the heart of telecommunications policy. On the other hand, price discrimination between consumer groups, for example, based on usage patterns, may be less in conflict with such goals as long as prices do not unfairly disadvantage certain groups.
9. Given these considerations, tying price discrimination exclusively to competition law misses the point. First, it presumes that effective competition exists across a territory, which is unlikely. Second, it overlooks the equity argument. However, in an environment with a growing number of service providers it would be justified to rethink how the goal of equitable prices and service quality is best achieved and to increase the room for some forms of price discrimination.

Guideline Four—Regulations should only be applied to retail services if wholesale regulation of bottleneck services is not sufficient to address significant market power [Canadian Connection, Appendix A-2, paragraph 19]

10. The proposal to allow retail service regulation only if wholesale regulation cannot cope with significant market power is misleading. The correct test should be whether wholesale regulation alone is capable of securing the objectives of telecommunication policy.

Guideline Five—Regulatory regimes should not place marketing restrictions on service providers designed to protect competitors [Canadian Connection, Appendix A-2, paragraph 20]

11. In the medium and long-run, if competition unfolds as anticipated, it is desirable to eliminate such restrictions as they reduce competitive options available to ILECs. However, it is necessary to keep in mind that consumers always may contact incumbent service providers to switch service back on their own initiative, if desired. In that sense, the ILECs may compete for former customers indirectly, for example by promoting their superior services to the public at large.
12. In their submission in the CRTC proceeding “Forbearance from regulation of local exchange services” Public Notice 2005-2, filed 22 June 2005, the “Consumer Groups” as represented by PIAC, filed comments that address the questions raised in relation to this guideline. The three stages in the Consumer Groups’ proposed transitional regime are described at paragraphs 122 thru 124 of the Consumer Groups’ submission.
13. This position is a cautious middle ground for a transition to an eventual elimination of the marketing rules and balances the interests of consumers and service providers.

Guideline Six—Competitors should be encouraged—and indeed given incentives—to make their own interconnection and wholesale arrangements free from regulatory review [*Canadian Connection, Appendix A-2, paragraph 21*]

14. It is reasonable to rely on private negotiations in many cases. However, negotiating power is unevenly distributed and especially smaller competitors may be disadvantaged unless certain safeguards are put in place. Appropriate measures include Reference Interconnection Offers (RIO) as used in the member states of the European Union and time limits on negotiating periods combined with a dispute resolution role of the regulator.

Guideline Seven—Regulation should be restricted to basic and essential services; there should be no economic regulation of discretionary services [*Canadian Connection, Appendix A-2, paragraph 23*]

15. A standard that limits regulation to essential services is exceptionally vague. There is no unique way of delineating essential from discretionary services. In an environment of 24/7 connectivity, services that may have been considered non-essential in the past, such as voice mail or call forwarding, may become essential. A more clear-cut approach to delineate services subject to regulation from those not subject to regulation is the competitive situation in the respective market.
16. If services are offered in a non-competitive markets but considered non-essential, forms of regulation that provide maximum flexibility to the service provider might be used. Moreover, in such instances, regulations should be applied symmetrically to any service provider. In any case, the classification of services as essential and non-essential would have to be reviewed periodically.

B. Proposals to reform institutions

[Canadian Connection, Appendix A-2, paragraph 41-48]

17. Besides the Guidelines themselves, I shall also briefly address the closely related area of telecommunications regulatory “Institutions”, as outlined by Bell in Canadian Connection, Appendix A-2, paragraphs 41-48.
18. Bell Canada proposes shifting significant tasks from the regulator to the competition authorities. Whereas there are some reasons to consider such an institutional change, not least the need to better integrate regulatory principles with competition law, there are also serious reasons against such a model. Most importantly, telecommunications regulation requires a level of technical expertise that is not available in competition authorities (although such expertise could be developed if sufficient additional resources are made available). Furthermore, involvement of two agencies almost certainly will increase the transaction costs of regulation. For that reason, most countries continue to rely on the regulatory agency to assess the state and the prospects of competition.
19. Moreover, economic regulation is not exclusively a response to market power, which is the domain of competition authorities. It also deals with other forms of market failure, such as public good issues or externalities. Whereas some of these may fall under the categories of social or technical regulation, not all cases do. Furthermore, the administrative principles followed by regulatory agencies and competition authorities differ. Whereas regulatory agencies can build their decisions on a substantive record of filings, testimony, and cross-examination, competition authorities typically need to discover much of the relevant information. Thus, shifting some components of economic regulation to the competition authorities would require fundamental changes in operating procedures.
20. It is not clear what purpose would be served by the proposed designation of telecommunications and broadcasting Commissioners. Specialization is certainly required but could be achieved at the staff level. One might also ask what the optimal number of commissioners is. Responding to industry developments and the cost of fragmented regulation, several countries have recently reorganized regulatory competencies by integrating telecommunications and media regulation (e.g., the U.K. or Australia). Thus, at a time when industry convergence has become widespread and the telephone and cable industry are considered one by industry experts² it seems odd to separate expertise in the proposed fashion.

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² See *ibid.*, appendix A-1, paragraph 8.