Canadian Radio-television and Telecommunications Commission
Conseil de la radiodiffusion et des télécommunications canadiennes

Telecom Decision CRTC 2007-124

Ottawa, 7 December 2007

Bell Aliant and Bell Canada – Application seeking recovery of the net incremental operating costs associated with the implementation of certain expanded local calling areas

Reference: 8678-B2-200711681

In this Decision, the Commission approves the use of an exogenous adjustment of $1.4 million per year for a three-year period to recover Bell Aliant Regional Communications, Limited Partnership's and Bell Canada's (collectively, Bell Canada et al.) net incremental operating costs associated with the implementation of expanded local calling areas for the cities of Ottawa, Gatineau, and Hamilton. However, the Commission denies Bell Canada et al.'s request to recover these costs from Bell Canada's deferral account.

Introduction

1. The Commission received an application by Bell Aliant Regional Communications, Limited Partnership and Bell Canada (collectively, Bell Canada et al.), dated 20 August 2007, requesting that the Commission approve the recovery of the net incremental operating costs, estimated at $3.7 million,[1] associated with the implementation of expanded local calling areas (ELCAs) for the cities of Ottawa, Gatineau, and Hamilton. Bell Canada et al. proposed to recover these costs by way of an annual exogenous adjustment of $1.4 million to be drawn down from Bell Canada's deferral account[2] over a three-year period.

2. The Commission received comments from MTS Allstream Inc. (MTS Allstream). The record of this proceeding closed on 1 October 2007 with Bell Canada et al.'s reply comments. The record of this proceeding is available on the Commission's website at www.crtc.gc.ca under "Public Proceedings."

3. The Commission has identified the following issues to be addressed in its determinations:

   - Does the implementation of the Ottawa, Gatineau, and Hamilton ELCAs qualify for exogenous treatment?

   - Is the proposed method for recovery of the net incremental operating costs associated with the implementation of ELCAs appropriate?

[1] This amount represents the total present worth of annual costs.
[2] The deferral account was introduced in Telecom Decision 2002-34 to mitigate the potential adverse effects that mandated rate reductions for local services might otherwise have on local competition.

Does the implementation of the Ottawa, Gatineau, and Hamilton ELCAs qualify for exogenous treatment?

Positions of parties

4. Bell Canada et al. noted that in Telecom Decision 2002-56, the Commission

   a) announced a new framework for the expansion of local calling areas (LCAs);

   b) considered that it would be appropriate to compensate incumbent local exchange carriers (ILECs) in those circumstances where there could be a material increase in net incremental operating costs as a result of the implementation of an ELCA; and

   c) noted that the most appropriate method of compensation would be to treat any material increase in net incremental operating costs as an exogenous adjustment on local rates in accordance with the regulatory framework applicable to the ILEC involved.[3]

5. Bell Canada et al. submitted that the net incremental operating costs associated with the implementation of the Ottawa, Gatineau, and Hamilton ELCAs were material to them, and therefore qualified for recovery pursuant to Telecom Decision 2002-56.

6. MTS Allstream submitted that Bell Canada et al.'s request was inappropriate and should be denied given that many of the affected exchanges were now subject to local forbearance. MTS Allstream submitted that Bell Canada et al. were fully able to adjust their rates to recover their costs in whatever manner they saw fit in these exchanges. MTS Allstream further submitted that no other competitor operating in these exchanges had the regulatory protection of being made whole and Bell Canada et al. could not expect such preferential regulatory treatment in a forborne environment.

Commission's analysis and determinations

7. The Commission notes that in 2006 and 2007, pursuant to the framework set out in Telecom Decision 2002-56, it granted interim approval to Bell Canada et al.'s applications to create the Ottawa, Gatineau, and Hamilton ELCAs,[4] as well as to temporary surcharges for residential and business local exchange services required to compensate toll providers for foregone toll revenues. Subsequent to these approvals, in Telecom Decision 2007-65, the Commission forbore from the regulation of residential local exchange services in portions of these ELCAs.

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[3] In Telecom Decision 2002-56, the Commission noted that for ILECs subject to Telecom Decision 2002-34, the application for any exogenous adjustment will be in accordance with paragraphs 667 and 668 of that Decision.

[4] The Commission approved Bell Aliant Tariff Notice 60 and Bell Canada Tariff Notice 7003 for the City of Ottawa ELCA in Telecom Order 2006-340; Bell Canada Tariff Notice 7004 for the City of Gatineau ELCA in Telecom Order 2007-164; and Bell Canada Tariff Notice 7031 for the city of Hamilton ELCA in Telecom Order 2007-168.

8. The Commission considers that the temporary surcharges, approved prior to forbearance from the regulation of residential and business local exchange services in these ELCAs, were intended to compensate both competitors and Bell Canada et al. for foregone toll revenues due to the implementation of these ELCAs. Consequently, the Commission disagrees that no other competitor operating in these exchanges has the regulatory protection of being made whole.

9. The Commission finds that the implementation of the Ottawa, Gatineau, and Hamilton ELCAs satisfies the criteria for an exogenous event initially set out in Telecom Decision 2002-34, and retained in Telecom Decision 2007-27. Therefore, the Commission finds that the net incremental operating costs incurred by Bell Canada et al. for the implementation of these ELCAs qualify for exogenous treatment.

Is the proposed method for recovery of the net incremental operating costs associated with the implementation of ELCAs appropriate?

Positions of parties

10. Bell Canada et al. submitted that drawing down from Bell Canada's deferral account to recover the net incremental operating costs associated with the implementation of the ELCAs was appropriate. In their view, Bell Canada would incur all of these costs for the Gatineau and Hamilton ELCAs, and the majority of the costs for the Ottawa ELCA. Bell Canada et al. submitted that the implementation of the ELCAs would benefit customers who were located within the operating territory from which Bell Canada's deferral account funds were collected.

11. Bell Canada et al. submitted that the net incremental operating costs were related primarily to the costs that Bell Canada incurred to modify Bell Canada et al.'s billing systems to enable billing of the approved temporary surcharges for recovering the foregone toll revenues associated with the implementation of the ELCAs.

12. Bell Canada et al. noted that Bell Canada started incurring costs to implement the first ELCA (i.e. Ottawa) in the summer of 2006. Bell Canada et al. requested that Bell Canada be permitted to recover the costs in question through an annual drawdown, estimated at $1.4 million, from its deferral account for a three-year period, starting 1 June 2006. Bell Canada et al. noted that 1 June 2006 represented the start of the last year of the five-year price cap period that was in effect from 1 June 2002 to 31 May 2007.

13. MTS Allstream submitted that the Commission determined, in Telecom Decision 2006-9, that proposals to fund the provision of discretionary services through the deferral accounts could provide the ILECS with an undue advantage and such initiatives should not be funded from the deferral accounts.

14. MTS Allstream submitted that Bell Canada et al.'s request to recover the net incremental operating costs associated with the implementation of the ELCAs was not competitively neutral and would result in preferential regulatory treatment for Bell Canada et al. In MTS Allstream's view, a competitor who mirrored Bell Canada et al.'s ELCA must either raise its local rates or absorb the associated losses. MTS Allstream noted that ILECs without positive deferral account balances were unable to draw down the costs of LCA expansion. Upon elimination of the deferral account monies, the costs of future LCA expansions would be paid for by local residential consumers.

15. In reply, Bell Canada et al. submitted that their application was analogous to the Commission's determinations related to the recovery of costs that were incurred by ILECs for the implementation of the mandatory teletypewriter (TTY) upgrade program for pay telephones. In Telecom Decision 2004-47, the Commission determined that these costs qualified for exogenous adjustment, and in Telecom Decision 2005-23, it approved the use of deferral account drawdowns as a means of recovering such costs.

Commission's analysis and determinations

16. In Telecom Decision 2002-34, the Commission established the deferral account mechanism and stated that the use of the deferral account would be an efficient means of addressing regulatory adjustments. The Commission also stated that the amounts in the deferral accounts should be cleared in a manner that would contribute to achieving the Commission's objectives for the next price cap period, including balancing the interests of the three main stakeholders in the telecommunications market – customers, ILECs, and competitors.

17. The Commission notes that, in Telecom Decision 2005-23, it determined that it was appropriate to use the deferral account to recover exogenous amounts associated with installing TTY units in pay telephones. However, it noted that it would not be appropriate to assign TTY costs to pay telephone services because the rates for these services remained frozen. The Commission also notes that the upgrading of pay telephones with TTY units was implemented for social policy reasons in that it improved accessibility to telecommunications services for persons with disabilities. The Commission considers that drawing down from the deferral account to recover these costs was appropriate in this regard.

18. In Telecom Decision 2002-56, the Commission found that, for the implementation of an ELCA, the most appropriate method was to treat any material increase in net incremental operating costs as an exogenous adjustment of local rates. The Commission noted that compensation through the use of surcharges in specific exchanges often resulted in the application of many different rates in an ILEC's operating territory. The Commission considered that it was generally preferable to adopt a simplified company-wide rate structure. While this company-wide rating approach could result in local rate increases for subscribers who did not benefit from an ELCA, the Commission did not expect that these increases, if any, would be substantial.

19. To ensure that funds did not continue to accumulate in the deferral accounts, the Commission, in Telecom Decision 2006-9, directed all ILECs, with the exception of Télébec, Limited Partnership, to file proposed changes to monthly rates for primary exchange services (PES) and optional services in the Residential Local Services in non-HCSAs (high-cost serving areas) basket in order to eliminate the recurring amounts in their deferral accounts. The Commission considers that, while business customers in the ELCAs for Ottawa, Gatineau, and Hamilton would benefit from the implementation of these ELCAs, drawing down from Bell Canada's deferral account would unjustly result in residential subscribers absorbing all of the ELCA costs since it would reduce the amount of the rate reductions for residential subscribers pursuant to Telecom Decision 2006-9.

20. The Commission notes that Bell Canada et al. indicated that Bell Canada incurred the majority of the costs for implementation of the ELCAs and both companies proposed that the total costs be attributed to Bell Canada. The Commission therefore **approves** the allocation of these costs to Bell Canada but **denies** Bell Canada et al.'s request to draw down the net incremental operational costs from Bell Canada's deferral account.

21. The Commission considers that allocating these costs to the appropriate services, as indicated below, is the most appropriate methodology for recovering the exogenous adjustment.

22. The Commission notes that business and residential PES are included in certain bundled services that are uncapped. The Commission considers that single-line bundled services fall into the same product markets as individual residential and business line PES, and therefore customers who subscribe to such bundles are equally likely to benefit from ELCAs.

23. The Commission is of the view that, similar to the approach taken in Telecom Order 99-239, network access services (NAS) would be the best means of allocating the ELCA costs to residential and business PES. The Commission considers that using NAS as an allocator would be appropriate as each NAS would be assigned the same level of costs. Accordingly, the Commission considers that Bell Canada's ELCA costs should be allocated to the Residential Services basket (HCSA and non-HCSA sub-baskets), the Business Services basket, the Uncapped Services basket, the Other Capped Services basket and services that are forborne from regulation on the basis of residential and business NAS attributed to these baskets or forborne services.

24. The Commission notes that Bell Canada et al. proposed to recover the ELCA costs over a three-year period. The Commission considers that this request is similar to the three-year period over which ELCA-related foregone toll revenues are permitted to be recovered. The Commission therefore considers that Bell Canada et al.'s proposal is reasonable.

25. The Commission notes that the Policy Direction[5] requires, among other things, that when relying on regulation, the Commission use measures that are efficient and proportionate to their purpose and that interfere with the operation of competitive market forces to the minimum extent necessary to meet the policy objectives set out in the *Telecommunications Act* (the Act). The Commission considers that its directives above will permit minimal rate changes and therefore would result in minimal interference with the operation of competitive market forces.

26. The Commission notes that the use of an exogenous adjustment provides Bell Canada with the flexibility to determine its rates, and relies on market forces in the determination of those rates. Accordingly, the Commission considers that such an approach would enhance the efficiency and competitiveness of the Canadian telecommunications industry and foster an increased reliance on market forces for the provision of telecommunications services, consistent with paragraphs 7(*c*) and 7(*f*) of the Act.

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[5] The Governor in Council issued *Order Issuing a Direction to the CRTC on Implementing the Canadian Telecommunications Policy Objectives*, P.C. 2006-1534, 14 December 2006.

Conclusion

27. In light of the above, the Commission **approves** the use of an exogenous adjustment of $1.4 million per year for a three-year period to recover Bell Canada et al.'s net incremental operating costs associated with the implementation of the ELCAs for the cities of Ottawa, Gatineau, and Hamilton, but **denies** Bell Canada et al.'s request to recover these costs from Bell Canada's deferral account.

28. The Commission directs Bell Canada to issue an update to its 2007 price cap filing to reflect the allocation of costs associated with the implementation of the ELCAs for the cities of Ottawa, Gatineau, and Hamilton across the service baskets identified above within 30 days from the date of this Decision.

Secretary General

Related documents

- *Bell Canada – Applications for forbearance from the regulation of residential local exchange services*, Telecom Decision CRTC 2007-65, 3 August 2007
- Telecom Order CRTC 2007-168, 14 May 2007
- Telecom Order CRTC 2007-164, 9 May 2007
- *Price cap framework for large incumbent local exchange carriers*, Telecom Decision CRTC 2007-27, 30 April 2007
- Telecom Order CRTC 2006-340, 14 December 2006
- *Disposition of funds in the deferral accounts*, Telecom Decision CRTC 2006-9, 16 February 2006
- *Follow-up to* Access to pay telephone service, *Telecom Decision CRTC 2004-47, 15 July 2004: Requests to recover costs associated with upgrading pay telephones with teletypewriter units*, Telecom Decision CRTC 2005-23, 14 April 2005
- *Access to pay telephone service*, Telecom Decision CRTC 2004-47, 15 July 2004
- *Framework for the expansion of local calling areas*, Telecom Decision CRTC 2002-56, 12 September 2002

- *Regulatory framework for second price cap period*, Telecom Decision CRTC 2002-34, 30 May 2002, as amended by Telecom Decision CRTC 2002-34-1, 15 July 2002

- *Local competition start-up costs proceeding, Telecom Public Notice CRTC 98-10*, Telecom Order CRTC 99-239, 12 March 1999