



Telecom Decision CRTC 2016-443

PDF version

Reference: Telecom Notice of Consultation 2016-180

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Review of the rates for Northwestel Inc.'s Wholesale Connect service

The Commission directs Northwestel to file revised Phase II cost studies for all its Wholesale Connect service speeds, for all community types, reflecting the determinations and costing assumptions set out in this decision. The cost studies will result in Wholesale Connect service rates that reflect the most current costing information and that are expected to enable other service providers to offer more competitive services to their customers.

Background

1. Northwestel Inc.'s (Northwestel) Wholesale Connect service provides for the transport of telecommunications traffic across communities served by the company's fibre or high-capacity microwave radio transport links. The service is available at different bandwidth levels in 30 communities in Northwestel's operating territory, categorized into 4 distinct types of bands.¹ Competitors can use the Wholesale Connect service to connect their points of presence in those communities for the purpose of providing telecommunications services to their own end-users.
2. In Telecom Order 2013-93 and Telecom Regulatory Policy 2013-711, the Commission made several determinations regarding Northwestel's Wholesale Connect service, including establishing certain costing assumptions to be used in the company's cost studies.
3. The Commission received an application from Northwestel (Tariff Notice 923), dated 28 January 2015, in which the company proposed to introduce new speeds of 150 megabits per second (Mbps) and 200 Mbps in Type A and Breakout communities for its Wholesale Connect service (the new speeds). Northwestel also proposed to add 24 Type B and C communities to its Wholesale Connect tariff. The

¹ Type A band consists of core communities served by fibre transport links (e.g. Whitehorse, Y.T. and Yellowknife, N.W.T.). Type B band consists of communities connecting to Type A communities using fibre transport links (e.g. Fort Providence, N.W.T.). Type C band consists of communities connecting to Type A communities using a combination of high-capacity microwave radio and fibre transport links (e.g. Dawson, Y.T.). The Breakout band consists of communities outside of Northwestel's operating territory (e.g. High Level, Alta.).

Commission approved Tariff Notice 923 on an interim basis in Telecom Order 2015-39.

4. As part of the Tariff Notice 923 process, interveners² challenged the rates proposed by Northwestel, in part on the basis that Northwestel's costs needed to be updated because they no longer reflected current circumstances. In response, Northwestel filed a revised cost study with adjustments that resulted in a reduction in its proposed rates of approximately 17% on average for both new speeds (150 Mbps and 200 Mbps).
5. Northwestel's existing approved rates and the rates proposed in Tariff Notice 923 include a fibre cost factor (FCF) of 5.5, as established in Telecom Regulatory Policy 2013-711. The FCF is used to estimate the transport fibre costs associated with a service. This approach relies on the ratio of fibre cable investments to the related fibre electronic investments. For example, an FCF of 0.25 means that for every \$100 invested in fibre electronic equipment, \$25 will be spent on fibre cable investment.
6. In Telecom Decision 2016-117, the Commission made certain changes to the costing assumptions applicable to wholesale high-speed access (HSA) services. Specifically, the Commission made interim all existing wholesale HSA service rates and directed wholesale HSA service providers to file new cost studies in light of updated costing parameters, such as a revised annual traffic growth assumption and an adjusted annual capital unit cost change assumption.
7. The Wholesale Connect service is similar in many respects to wholesale HSA services. For instance, both types of service provide high-speed transport facilities that competitors can use to provide retail services, such as Internet access services, to end-users, and both employ similar switching and transport equipment.

Telecom Notice of Consultation 2016-180

8. In light of the above, the Commission issued Telecom Notice of Consultation 2016-180, initiating a proceeding to examine whether the rates for all of Northwestel's existing Wholesale Connect service speeds should be reviewed in light of information filed in the proceeding associated with Northwestel's Tariff Notice 923 and the Commission's determinations set out in Telecom Decision 2016-117.
9. The Commission received interventions from Northwestel and from the Canadian Network Operators Consortium Inc. (CNOc), the Government of Yukon (Yukon), Iristel Technologies Inc. (Iristel), and SSi Micro Ltd. (SSi). In some cases, the interveners made proposals that went beyond the specific issues raised in Telecom Notice of Consultation 2016-180. The public record of this proceeding, which closed

² The Canadian Network Operators Consortium Inc. and the SSi Group of Companies participated in the Tariff Notice 923 proceeding.

on 23 June 2016, is available on the Commission's website at www.crtc.gc.ca or by using the file number provided above.

Issues

10. The Commission has identified the following issues to be addressed in this decision:

- Should the 17% rate reduction proposed by Northwestel for the new speeds also apply to all existing Wholesale Connect service speeds, for all community types?
- Should the FCF established in Telecom Regulatory Policy 2013-711 be updated?
- Should the Commission's determinations in Telecom Decision 2016-117 with respect to the costing assumptions applicable to wholesale HSA services also apply to Northwestel's Wholesale Connect service?
- If Northwestel is required to file revised cost studies, should the existing rates for its Wholesale Connect service be made interim?
- Should the additional proposals by SSI and Iristel be considered in the context of this proceeding?

Should the 17% rate reduction proposed by Northwestel for the new speeds also apply to all existing Wholesale Connect service speeds, for all community types?

11. As noted above, Northwestel's proposed rates for its new speeds in Type A and Breakout communities were reduced by 17% as a result of the company's revised cost study. The Commission asked interveners to comment on whether this rate reduction should also apply to Northwestel's existing Wholesale Connect service speeds, for all community types.
12. No intervener supported the application of a broad 17% rate reduction across all speeds and community types.
13. Northwestel proposed that, rather than simply applying the reduction to existing speeds, it would file updated cost studies for existing and new speeds using a new five-year study period, which would start on 1 January 2017, and using an approach similar to the one that led to the 17% rate reduction for the new speeds. The company submitted that it expects that the overall reductions to rates will exceed 17% when all cost updates are taken into account.
14. Specifically, Northwestel submitted that the updated costs would be based on the unit costs from the previous studies, expressed in 2017 dollars, as the starting point. These costs would reflect the revised assumptions regarding the maximum switching equipment capacity (i.e. 10,000 Mbps) submitted in Tariff Notice 923, as well as

assumptions consistent with those identified in the other questions raised in Telecom Notice of Consultation 2016-180. Northwestel submitted that the resulting rate reduction would likely not be the same across all speed tiers. There would be larger decreases to the monthly equivalent costs for high-bandwidth services, as usage-based switching and transport costs make up a bigger percentage of the overall costs for the larger circuits associated with such services.

15. The interveners other than Northwestel submitted that Northwestel should file revised cost studies for all its Wholesale Connect service speeds. SSi added that the studies should also reflect the costing assumptions outlined in the cost study by Lemay-Yates Associates Inc. entitled *Backbone Costs for Northern Locations* (the LYA report), which SSi included in its submission dated 13 June 2016.

Commission's analysis and determinations

16. In the absence of revised cost studies, it would not be appropriate to assume that an across-the-board 17% rate reduction would lead to rates for some speeds that are cost-based. The Commission considers that Northwestel's proposal to update its cost studies, as outlined above, is necessary. However, as explained in greater detail later in this decision, these cost studies should also reflect the revised assumptions with respect to annual traffic growth and annual capital unit cost change. Where Northwestel expresses unit costs from previous cost studies in 2017 dollars, it should apply the revised annual capital unit cost change assumption. This practice would be consistent with the Commission's rationale for revising that assumption.
17. The Commission therefore **directs** Northwestel to file revised Phase II cost studies for all existing and new Wholesale Connect service speeds, for all community types. The revised cost studies must reflect the following: (i) a five-year study period starting 1 January 2017; (ii) maximum switching equipment capacity of 10,000 Mbps; (iii) any unit costs from previous cost studies expressed in 2017 dollars, using the annual capital unit cost change assumption set out in this decision; and (iv) all other determinations made in this decision.

Should the FCF established in Telecom Regulatory Policy 2013-711 be updated?

18. As noted above, the FCF is used to estimate the transport fibre costs associated with a service. In Telecom Regulatory Policy 2013-711, the Commission determined that an FCF of 5.5 should be used in estimating Northwestel's Wholesale Connect service costs and establishing the rates for the service. This FCF is based on five years of the company's historical data (i.e. 2008-2012).
19. All interveners submitted that the FCF should be updated, as it was based on historical data that is no longer current. Iristel submitted that the update should reflect data from 2011 to 2015.
20. Northwestel submitted that it would update the FCF in the revised cost studies it proposed to file.

21. SSi submitted that if Northwestel proposes an FCF higher than 0.7, it should place on the public record adequate and detailed information that will allow interested persons to properly review and comment on the underlying data and the validity of the proposed FCF. Along the same lines, Iristel submitted that Northwestel must provide sufficient disclosure of the costing information to enable interested persons to comment on any new cost studies in a meaningful manner.

Commission's analysis and determinations

22. An updated FCF would help to ensure that Northwestel's rates for its Wholesale Connect service reflect current circumstances and remain cost-based. Accordingly, any updated FCF should be based on the most recent five years of historical data currently available to Northwestel.
23. With respect to SSi's and Iristel's comments regarding the disclosure of costing information, the FCF is developed based on company-specific information, which is consistently treated by the company and the Commission as confidential. However, the level of disclosure should also provide for a meaningful opportunity for interveners to comment. The Commission considers that the guidelines established in Telecom Regulatory Policy 2012-592, which, among other things, require the FCF itself to be disclosed, achieve the appropriate balance between these different interests.
24. The Commission therefore **directs** Northwestel to (i) file its updated FCF, based on its most recent five years of historical data, for the Commission's review and approval; (ii) use the updated FCF in its revised cost studies; and (iii) disclose costing information consistent with the guidelines set out in Telecom Regulatory Policy 2012-592.

Should the Commission's determinations in Telecom Decision 2016-117 with respect to the costing assumptions applicable to wholesale HSA services also apply to Northwestel's Wholesale Connect service?

25. In Telecom Notice of Consultation 2016-180, the Commission sought comments on whether its determinations in Telecom Decision 2016-117 with respect to the annual traffic growth assumption and the annual capital unit cost change assumption applicable to wholesale HSA services should also apply to Northwestel's Wholesale Connect service, for all community types. The Commission also called for comments on the ability to recover certain costs when service rates are revisited prior to the end of an original study period.
26. CNOC, Iristel, and SSi submitted that those determinations should be applied to Northwestel's Wholesale Connect service.
27. Northwestel submitted that, for the annual traffic growth assumption, it would be appropriate to apply the determinations in Telecom Decision 2016-117 to its Wholesale Connect service.

28. However, Northwestel argued that it would not be appropriate to apply the determinations regarding the annual capital unit cost change assumption to its Wholesale Connect service. The company proposed instead to continue to use the assumption approved in Telecom Order 2013-93, namely 50% of the value approved for Bell Canada at the time of that order, or -5%.³ In that order, the Commission acknowledged that Northwestel had higher installation costs than other incumbent local exchange carriers (ILECs), owing to the nature of its operating territory, which Northwestel submitted is still the case.
29. SSI submitted that, based on the LYA report's cost analysis of backbone services from Yellowknife/Whitehorse to High Level/Fort St. John, Northwestel's current Wholesale Connect service rates are 7 to 10 times higher than is appropriate. SSI relied on the LYA report's conclusion that it is appropriate to use the assumptions from Telecom Decision 2016-117, based on household data growth rates reported by the Commission and on the similarity of the equipment used to deploy wholesale HSA and Wholesale Connect services.
30. Iristel submitted that end-user Internet behaviour is not region specific and that the Scott report,⁴ upon which the revised annual capital unit cost in Telecom Decision 2016-117 was, in part, based, remains a reliable source of information.
31. In reply, Northwestel submitted that the LYA report's conclusions were unsupported by the evidence.
32. Finally, with regard to the recovery of costs, Northwestel submitted that there would be no unrecovered costs if its revised cost studies have a study period beginning 1 January 2017.

Commission's analysis and determinations

33. Based on the record of this proceeding, the Commission considers that the determinations in Telecom Decision 2016-117 with respect to the annual traffic growth assumption for wholesale HSA services should apply to Northwestel's Wholesale Connect service. Northwestel and all the other interveners supported this approach.
34. With regard to the annual capital unit cost change assumption set out in Telecom Decision 2016-117, this assumption resulted from a proceeding with a fulsome record in which ILECs, cable companies, and other interested persons provided input, and it reflects the evidence of current equipment price trends. Further,

³ In Telecom Decision 2016-117, the Commission determined that a value of -26.4% was appropriate for wholesale HSA services.

⁴ J. Scott Marcus, *The Economic Impact of Internet Traffic Growth on Network Operators*, 24 October 2014

Northwestel has not disputed that its Wholesale Connect service is similar in many respects to wholesale HSA services.

35. On the other hand, in Telecom Order 2013-93, the annual capital unit cost change assumption was based on price trends set out in Telecom Regulatory Policy 2011-703. While Northwestel asserted that this assumption is still relevant, it did not elaborate on this view. The Commission considers that it is appropriate to use assumptions based on the most current changes in technology and capacity of the equipment.
36. In addition, in Telecom Decision 2016-117, the Commission stated that whenever labour costs are estimated using the capacity cost approach, it is appropriate to apply the annual capital unit cost change (i.e. -26.4%). Provided that wholesale HSA service providers properly account for and substantiate their installation time estimates and their labour increase factor, all costs associated with labour will be accounted for.
37. Accordingly, the Commission considers that its determinations in Telecom Decision 2016-117 with respect to the annual traffic growth assumption and the annual capital unit cost change assumption should apply to Northwestel's Wholesale Connect service.
38. In light of the above, the Commission **directs** Northwestel to include, in the revised Phase II cost studies for its Wholesale Connect service speeds, the following costing component assumptions, which are consistent with the determinations in Telecom Decision 2016-117:
 - in the first two years of the study period, use annual traffic growth rates per retail end-user that are consistent with historical levels, followed by a constant growth rate of 32% for each of the remaining years of the study period; and
 - use -26.4% as the annual capital unit cost change assumption per Mbps for traffic-driven equipment and labour costs in the study period.
39. Northwestel is to file its revised cost studies with a study period beginning on 1 January 2017. In light of this starting date, the Commission notes Northwestel's assertion that there will be no unrecovered costs.

If Northwestel is required to file revised cost studies, should the existing rates for its Wholesale Connect service be made interim?

40. Northwestel proposed that, until 1 January 2017, (i) the current rates for its existing Wholesale Connect service speeds (5 Mbps to 100 Mbps) remain final; and (ii) the rates for its new speeds (150 Mbps and 200 Mbps, currently approved on an interim basis) be revised to account for the reductions proposed during the Tariff Notice 923 proceeding and be deemed final.

41. Northwestel also proposed that on 1 January 2017, new cost-based rates for all its Wholesale Connect service speeds, based on its revised cost studies, be made final. In the event that the Commission were unable to rule on the various tariff filings by that date, Northwestel proposed that the Commission make interim the rates for all its Wholesale Connect service speeds, as they exist at that date.
42. SSi proposed that all of Northwestel's Wholesale Connect service rates, whether approved on an interim or a final basis, be made interim on a retroactive basis to no later than 28 January 2015 (the date that Tariff Notice 923 was filed).⁵ SSi submitted that it has been paying interim rates for a significant length of time and that it should only pay rates that are just and reasonable.
43. Yukon submitted that it would be appropriate to make Northwestel's existing Wholesale Connect service rates interim.
44. Iristel objected to Northwestel's proposal and submitted that the Commission should make all monthly rates for the Wholesale Connect service interim until they are approved on a final basis. Iristel submitted that the Commission must amend rates that are no longer just and reasonable as soon as possible.
45. CNOC submitted that the Wholesale Connect monthly rates should be made interim, as the existing rates are no longer just and reasonable in light of costing issues identified in the Tariff Notice 923 proceeding, which may be present across all service speeds.
46. Northwestel submitted that, in law, existing rates currently approved on a final basis cannot be retroactively adjusted. The company added that in Telecom Decision 2015-364, the Commission denied an application by SSi to re-examine the Wholesale Connect service rates approved in Telecom Regulatory Policy 2013-711, having found no basis at that time to conclude that rates were not just and reasonable or that they were unduly discriminatory.

Commission's analysis and determinations

47. The monthly rates for the existing speeds of Northwestel's Wholesale Connect service (5 Mbps to 100 Mbps) are currently approved on a final basis. Making a final rate interim on a retroactive basis is an extraordinary measure and, in the circumstances, the Commission considers that SSi has not justified its request. However, the record of this proceeding reveals sufficient cause for these rates to be made interim, effective the date of this decision, since Northwestel's costs, and hence its rates, are likely to change due to the adjustments in costing assumptions resulting from this decision.

⁵ Telecom Order 2015-39, in which the rates proposed in Tariff Notice 923 were approved on an interim basis, was issued on 11 February 2015 and specified an effective date for the rates of 27 February 2015.

48. The monthly rates for Northwestel's new Wholesale Connect service speeds (150 Mbps and 200 Mbps) are currently approved on an interim basis as of 27 February 2015. The Commission considers that, as these rates are expected to change in light of the determinations made in this decision, they should remain interim.
49. The Commission therefore makes the following determinations regarding Northwestel's monthly Wholesale Connect service rates:
- for the existing speeds of 100 Mbps and lower, by community type, the rates are hereby made interim, effective **8 November 2016**; and
 - for the new speeds of 150 Mbps and 200 Mbps, for Type A and Breakout communities, the rates are to remain interim, effective **27 February 2015**, as specified in Telecom Order 2015-39.
50. The Commission will assess whether, and how, retroactivity will apply to these interim rates when it considers Northwestel's new tariff notices, with accompanying cost studies, in support of the company's revised existing and new Wholesale Connect service rates.

Should the additional proposals by SSi and Iristel be considered in the context of this proceeding?

51. In its submissions, SSi proposed that Northwestel be required to provide a wholesale Ethernet virtual private line service as an alternative to Wholesale Connect service,⁶ with speeds of up to 1,000 Mbps. The proposed service would run between, at a minimum, the Type A communities⁷ and the Breakout communities, and would include Fort St. John, B.C. as a Breakout community. SSi added that the rates for this service should be established in line with the principles set out in Telecom Decision 2016-117 and as per the costing assumptions detailed and supported in the LYA report.
52. SSi also proposed that the Commission establish a streamlined tariff process whereby rates for Northwestel's Wholesale Connect service are decreased parallel to decreases in its retail Internet service rates.
53. Iristel and Yukon supported SSi's proposals; however, Iristel submitted that rates must always be cost-based and not be based on any type of "retail-minus" pricing.
54. In addition, Iristel proposed that the Commission initiate a proceeding to review the broader terms of service associated with Wholesale Connect service, such as

⁶ SSi specified that such a service should support multiple point-to-point Ethernet virtual private line services multiplexed across a single user-network interface.

⁷ The Type A communities are Yellowknife, N.W.T.; Whitehorse, Y.T.; Hay River, N.W.T.; and Fort Nelson, B.C.

restrictions on class of service, service level agreements for basic class of service, and redundancy safeguards.

55. Northwestel submitted that SSI's and Iristel's proposals are outside the scope of this proceeding. With respect to SSI's request to include Fort St. John as a Breakout community, Northwestel submitted that companies can contact its Carrier Services group if they wish to pursue this option.

Commission's analysis and determinations

56. Telecom Notice of Consultation 2016-180, which initiated the current proceeding, is narrowly focused on specific costing issues associated with Northwestel's existing Wholesale Connect service speeds. Given this situation, the interveners' additional proposals are beyond the scope of the current proceeding.

Conclusion

57. The Commission **directs** Northwestel to file a new tariff application, supported by a Phase II cost study for each Wholesale Connect service speed, reflecting the determinations in this decision, by **9 January 2017**.

Secretary General

Related documents

- *Review of the rates for Northwestel Inc.'s Wholesale Connect service*, Telecom Notice of Consultation CRTC 2016-180, 12 May 2016
- *Review of costing inputs and the application process for wholesale high-speed access services*, Telecom Decision CRTC 2016-117, 31 March 2016
- *SSI Group of Companies – Application concerning Northwestel Inc.'s Wholesale Connect Service rates*, Telecom Decision CRTC 2015-364, 7 August 2015
- *Northwestel Inc. – Interim approval of a tariff application*, Telecom Order CRTC 2015-39, 11 February 2015
- *Northwestel Inc. – Regulatory Framework, Modernization Plan, and related matters*, Telecom Regulatory Policy CRTC 2013-711, 18 December 2013
- *Northwestel Inc. – Wholesale Connect Service*, Telecom Order CRTC 2013-93, 25 February 2013
- *Confidentiality of information used to establish wholesale service rates*, Telecom Regulatory Policy CRTC 2012-592, 26 October 2012

- *Billing practices for wholesale residential high-speed access services*, Telecom Regulatory Policy CRTC 2011-703, 15 November 2011; as amended by Telecom Regulatory Policy CRTC 2011-703-1, 22 December 2011