Telecom Decision CRTC 2004-13

Ottawa, 26 February 2004

Société en commandite Télébec – Application regarding the adjustment to the total subsidy requirement for the termination of directory integrality

Reference: 8695-T78-200314229

In this decision, the Commission ***denies*** *a request by Société en commandite Télébec to increase its 2003 subsidy requirement by $0.9 million for the termination of the integrality adjustment related to its directory operation.*

1. The Commission received an application by Société en commandite Télébec (Télébec), dated 29 September 2003 proposing to increase its 2003 subsidy requirement by $0.9 million. Télébec submitted that the integrality adjustment to its subsidy requirement related to its directory operation should be terminated since it is no longer affiliated with its directory service provider.

2. Télébec presented two arguments in support of its request. First, Télébec submitted that it should be treated like TELUS Communications (Québec) Inc. (TELUS Québec) in *Implementation of price regulation for Télébec and TELUS Québec*, Telecom Decision CRTC 2002-43, 31 July 2002 (Decision 2002-43) with respect to the termination of the integrality adjustment. Second, Télébec submitted that its proposed adjustment was warranted due to the unfairness of the productivity factor that is applied to all revenues associated with services formerly classified as being in its Utility segment.

3. On its first point, Télébec stated that its directory service provider was no longer an affiliate of the company. Télébec noted that the directory services ceased to be provided by Télé-Direct, an affiliate of Télébec, during 2002, the first year the company was subject to price cap regulation. The company explained that the directory services have been provided since November 2002 by Groupe Pages Jaunes Cie., a company that is not affiliated with Télébec.

4. Télébec noted that in Decision 2002-43, TELUS Québec's proposed removal of the integrality adjustment was found to be appropriate, and was reflected in the determination of TELUS Québec's going-in revenue requirement. Télébec submitted that during the proceeding that led to Decision 2002-43, it was still negotiating the sale of its directory affiliate. Télébec indicated that it did not seek the removal of the integrality adjustment for the directory operations from the determination of its going-in revenue requirement. Télébec argued that since it was now no longer affiliated with its directory service provider, it should be afforded the same treatment as TELUS Québec.

5. On its second point, Télébec argued that it was being penalized relative to the other incumbent local exchange carriers (ILECs). Télébec noted that it must realize a productivity offset of 4.7%, while the other ILECs subject to price cap regulation are only required to realize a productivity offset of 3.5%. In Télébec's view, the regulatory adjustment for integrality, which it argued was no longer appropriate, added substantially to the already high productivity offset that it must realize. Télébec further noted that in its case, the higher productivity offset was applied to all of the revenues associated with services formerly classified as being in its Utility segment. Télébec noted that, in the case of the other ILECs, the productivity offset was applied only to specific baskets of capped services.

6. The Commission received no comments with respect to this application.

Commission analysis and determination

7. The Commission notes that as a result of Decision 2002-43, Télébec and TELUS Québec are now subject to price cap regulation. Under that regulatory framework, rates are adjusted on the basis of the price cap formula which includes inflation and a prescribed level of productivity. The price cap regulation regime adopted by the Commission also provides for the use of an exogenous factor in the price cap formula to reflect the financial impacts of specific events that are beyond the control of a company and are unique to the telecommunications industry. More specifically, Decision 2002-43 states that exogenous events should satisfy the following criteria:

   a) they are legislative, judicial or administrative actions which are beyond the control of the company;

   b) they are addressed specifically to the telecommunications industry; and

   c) they have a material impact as measured against the total company.

8. The Commission is of the view that Télébec's application can only be assessed pursuant to the criteria of an exogenous event under price cap regulation. The Commission notes that the severance of the affiliation link with the directory service provider does not meet the first criterion of an exogenous event as it does not constitute a legislative, judicial or administrative action which is beyond the control of the company. The disposition of Télébec's directory affiliate was, in the Commission's view, a corporate decision. Therefore, the Commission considers that Télébec's proposal to adjust its 2003 subsidy requirement to terminate the integrality adjustment related to its directory operation is not an exogenous event.

9. The Commission notes that Télébec's current situation under price cap regulation is different from that of TELUS Québec at the time of Decision 2002-43. In that decision, the Commission determined that TELUS Québec's directory service provider was no longer affiliated with the company. As a result, TELUS Québec's integrality adjustment was terminated and was reflected in setting its going-in revenue requirement under rate base/rate of return regulation, before the implementation of price cap regulation. When Decision 2002-43 was issued, Télébec and its directory service provider were affiliated as a result of common ownership.

This affiliation ceased only after the implementation of price cap regulation. Therefore, the Commission is of the view that the similarity of treatment is not applicable as a different regulatory regime was applicable when Télébec's affiliation to its directory provider ceased.

10. The Commission notes Télébec's argument that it is penalized under the current regulatory regime because it is required to realize a productivity offset of 4.7%, as compared to the productivity offset of 3.5% established for the other ILECs. The Commission also notes Télébec's argument that it is further penalized because the larger productivity offset is applied to all revenues associated with services formerly classified as being in its Utility segment rather than to the capped revenues in specific baskets.

11. The Commission made a number of determinations in Decision 2002-43 regarding the appropriate productivity factor to approve for Télébec. They included the following:

- Télébec had a residual going-in revenue requirement shortfall of $7.6 million for the Utility segment;
- the shortfall was to be funded through a transitional subsidy from the national contribution fund (NCF);
- the productivity offset applied to reduce the transitional subsidy should reflect the productivity gains achievable by the services formerly classified as being in Télébec's Utility segment; and
- a total factor productivity (TFP[1]) offset was more comprehensive than a productivity offset based on marginal cost trends, which is more suitable for individual baskets of capped services.

The Commission also noted that in *Price cap regulation and related issues*, Telecom Decision CRTC 97-9, 1 May 1997, a company-wide TFP approach was found to be an appropriate proxy for the Utility segment's productivity.

12. The Commission also notes that in the proceeding culminating in Decision 2002-43, Télébec indicated that it had no historical TFP data. Accordingly, the Commission relied on historical TFP data for the large ILECs other than Télébec and TELUS Québec, filed in the proceeding leading to *Regulatory framework for second price cap period*, Telecom Decision CRTC 2002-34, 30 May 2002, in developing the appropriate productivity offset to be used by Télébec while it was receiving monies from the NCF related to the transitional subsidy.

13. The Commission considers that Télébec is not being penalized by being subject to a higher productivity offset than those of the other large ILECs. In the Commission's view, the current circumstances of Télébec are different from those of the other large ILECs, and, as such, the two productivity offsets are not comparable. The Commission notes that Télébec, unlike the

[1] Industry TFP is defined as the measure of efficiency of the telephone companies taking into consideration all the inputs (labour, material and capital) and outputs (revenues).

other large ILECs in southern Canada, receives a transitional subsidy from the NCF to offset its going-in revenue requirement shortfall of $7.6 million. The Commission also notes that the 4.7% productivity offset in Decision 2002-43 is a more comprehensive productivity offset which is applied to the revenues of its former Utility segment in order to eliminate the transitional subsidy from the NCF. The 3.5% productivity offset used by the other large ILECs is applied to individual baskets of capped services. The Commission further notes that the 3.5% productivity offset will apply to Télébec once its transitional subsidy from the NCF is eliminated. Accordingly, the Commission is of the view that Télébec's argument on the fairness of the productivity offset is without merit.

14. Based on all of the above, the Commission **denies** Télébec's application to increase the 2003 subsidy requirement by $0.9 million for the termination of the integrality adjustment related to its directory operation.

Secretary General