

Afterword



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The mandate of the Telecommunications Policy Review Panel was to recommend a modern policy and regulatory framework to ensure that Canada continues to have a strong, internationally competitive telecommunications industry that delivers world-class products and services at affordable prices for the economic and social benefit of all Canadians. In conducting its review, the Panel was asked to focus on three key areas: telecommunications regulation, access to broadband, and information and communications technology (ICT) adoption. In this final report, the Panel recommends the actions required in each of these areas to meet the overall objectives of the review.

In this Afterword, the Panel deals with two related issues that were not specifically made part of its mandate, but that significantly affect the future of the Canadian telecommunications industry:

- the implications of the technology and market trends that are transforming the telecommunications industry for Canada's broadcasting policy and regulatory framework
- the current policies that restrict foreign ownership and control of telecommunications common carriers and broadcast distribution undertakings.

The technology and market trends discussed in Chapter 1 affect both the telecommunications and broadcasting industries, and many of the major players in the Canadian telecommunications industry, such as BCE Inc., Rogers Communications Inc., Shaw Communications Inc. and Vidéotron ltée, are also major players in the Canadian broadcasting industry. The continuing convergence of Canada's communications industries, with former "cable TV" companies and "telephone companies" both offering a similar range of voice, data and video services on broadband Internet Protocol (IP) platforms, will significantly increase competition between the telecommunications and broadcasting industries. The entry of wireless companies into the video distribution business will intensify this competition.

This convergence of telecommunications and broadcasting markets brings into question the continued viability of maintaining two separate policy and regulatory frameworks, one for telecommunications common carriers like the incumbent telephone companies and one for their competitors in most of the same markets, the cable telecommunications companies.

The second issue relates to the restrictions on foreign ownership and control of Canadian telecommunications carriers. The policy debates on this issue generally involve different considerations from the issue of restrictions on foreign ownership or control of Canadian broadcasters. In the case of Canadian carriers, the policy considerations include increasing competition, economic efficiency, access to capital and technology, as well as concerns about Canadian employment, control of head office functions and national security. The broadcasting ownership debates focus on issues relating to creation and distribution of Canadian content, access to Canadian sources of information and cultural sovereignty.

Over the past years, the networks of both Canadian telecommunications carriers and broadcasting distribution undertakings have increasingly been used to provide both broadcasting services and other telecommunications services. Thus, questions of whether to liberalize restrictions against foreign ownership or control of these facilities inevitably bring into play two very different sets of policy considerations and interests.

Although the Panel was not specifically asked to provide recommendations on either of these issues, there are clear linkages between them and the objectives of the telecommunications policy review. These linkages have led the Panel to use this Afterword to suggest possible future approaches that the government might use to resolve the long-standing policy debates over the issues.

Market Convergence

Many of the major trends revolutionizing the telecommunications industry, which are identified in Chapter 1 and discussed throughout this report, apply equally to the broadcasting industry. These trends include:

- the shift to IP-based communications networks
- the greater reliance on open network architectures
- the convergence of information and communications technologies and content industries.

The effect of these trends is particularly noticeable in the cable industry, which provides both telecommunications and broadcasting services. However, they are beginning to affect traditional broadcasters and other producers of audio and video content as well. Not surprisingly, therefore, a number of submissions to the Panel raised issues about the relationship between telecommunications and broadcasting policy and regulation.

Submissions from various parties pointed to the significant challenges these trends pose for the current Canadian system of “parallel regulation,” which is based on largely separate policy, legislative and regulatory frameworks for the broadcasting and telecommunications industries.

One major Canadian broadcasting company stated, “it will become increasingly difficult for regulators to ensure that a more diffuse distribution architecture can effectively deliver on the current obligations extracted from Broadcasting Distribution Undertakings [BDUs] under the existing regulatory framework.”¹ Some representatives of the cable industry suggested that the increasing convergence of the telecommunications and broadcasting industries should lead the Panel to recommend the increased harmonization of Canadian telecommunications and broadcasting policy and regulation. A number of parties submitted that Canadian telecommunications

¹ See Astral Media Inc. submission of August 15, 2005, p. 8. Available online at: [http://www.telecomreview.ca/epic/internet/intprp-gecrt.nsf/vwapj/Astral_Media_-_Submission.pdf/\\$FILE/Astral_Media_-_Submission.pdf](http://www.telecomreview.ca/epic/internet/intprp-gecrt.nsf/vwapj/Astral_Media_-_Submission.pdf/$FILE/Astral_Media_-_Submission.pdf)

and broadcasting regulatory frameworks should take greater account of copyright, given the increased importance of all forms of content transmitted over telecommunications and broadcasting networks.

There were a variety of other perspectives on how, if at all, the Panel should deal with the interface of broadcasting and telecommunications policy and regulation. Some parties, including representatives of Canadian audiovisual unions and some broadcasting companies, submitted that the Panel should limit its recommendations to telecommunications policy and should not deal with broadcasting policy matters.

The Panel has decided that, for a number of reasons, it would be inappropriate for it to make specific recommendations to change the Canadian broadcasting policy and regulatory framework. It was not part of the Panel's mandate to address these issues. Broadcasting policy involves a complex interplay of cultural, industrial and trade issues that the Panel has not studied in detail. In addition, parties affected by such issues would feel justifiably concerned if the Panel made specific recommendations on matters that affected their interests, without a full review of the implications of such recommendations — and a full opportunity to make submissions relevant to them.

At the same time, the Panel recognizes that the changing environment is increasing the cross-impacts and the tensions between Canada's existing telecommunications and broadcasting policies. These changes in the technological and market environment threaten to undermine the current system of parallel regulation, particularly as it applies to the former "telephone" and "cable TV" companies that are major players in the new converged telecommunications industry. The changes also threaten to undermine the current policies and regulatory measures that support and promote the development of Canadian broadcasting content. The Panel considers it important for Canadian economic competitiveness and cultural sovereignty, as well as for the integrity of the Canadian regulatory system, to ensure that measures to promote development and distribution of Canadian content are effective — and realistic — given the technological and market environment in which they operate.

The Panel believes the Government of Canada should not wait until the viability of the current broadcasting regulatory framework is undermined by technology and market changes. The government should act now to review its broadcasting policies to reflect the obvious changes occurring in the broadcasting environment.

Changes in the Broadcasting Environment

While there is a vigorous debate about the speed of change, no one can deny that the Canadian broadcasting industry is facing revolutionary technological and market changes. The IP revolution will soon make it possible for consumers to access much of the audio and video content they have traditionally obtained from Canadian broadcasters over a variety of distribution networks — some subject to current broadcasting regulation, others not.

Canadian regulators and policy makers are justifiably proud of their leadership role in creating a space for diverse national broadcasting content, in the shadow of the dominant U.S.-based North American video production and distribution industries. Other countries are increasingly cognizant of the social, cultural, educational and economic benefits of producing their own electronic content instead of simply importing it from the market leader in broadcasting and Internet content — the United States.² There is no reason why Canada, with its diverse and creative population, should not play a leading role in developing new electronic communications content for global communications networks.

However, changes in data, video and audio distribution technologies and markets raise increasing concerns about whether the current broadcasting policy approaches will be the best way, or even a viable way, to pursue such leadership in the future. In the Panel's view, these changes call for a major reassessment of the Canadian broadcasting policy and regulatory framework.

The current broadcasting policy and regulatory framework was developed in response to the prospect of domination of the Canadian broadcasting markets by U.S.-based broadcasting and video distribution networks. In the face of a flood of attractive and low-priced broadcast programming content from the U.S., promotion of Canadian programming became a key tenet of Canadian broadcasting policy — particularly in English-speaking Canada. Promoters of Canadian programming content pointed out that, without regulatory intervention, Canadian radio and television broadcasters and BDUs could distribute high-quality, U.S.-produced TV programs, particularly drama programs, for one-tenth or less the cost of producing domestic content. Consequently, there seemed to be little financial incentive for privately owned Canadian broadcasters and BDUs to distribute Canadian programming in genres such as drama or children's programming.

These and similar concerns led to strong regulatory intervention in Canadian broadcasting content distribution markets. In the 1970s, under the chairmanship of Pierre Juneau, the CRTC introduced minimum quotas for airplay of Canadian music on radio stations.³ That intervention is widely credited with creating the modern Canadian music industry. Since that time, the CRTC has introduced a range of different broadcast distribution rules, moving beyond radio to video, and beyond quotas to measures such as those requiring priority carriage of Canadian signals, tiering and linking of cable channels, simultaneous substitution of ads on U.S.-carried cable channels, etc.

The current rules governing distribution of programs by off-air broadcasters and distribution of channels by cable, satellite and other BDUs have provided an effective means of supporting production and distribution of Canadian content. Broadcasters and BDUs were, and continue to be, licensed subject to conditions requiring preferential carriage, quotas and direct monetary contributions to support the production and distribution of Canadian programming.

² Canada took a leadership role in the development of the *Convention on the Protection and Promotion of Cultural Expressions*, which was adopted by UNESCO's General Conference in October 2005. See UNESCO, "Canada Becomes the First State to Ratify the Convention on the Protection and Promotion of the Diversity of Cultural Expressions," December 23, 2005. Available online at: http://portal.unesco.org/culture/en/ev.php-URL_ID=29555&URL_DO=DO_TOPIC&URL_SECTION=201.html

³ Canada's national music awards continue to be called "Junos" in honour of Mr. Juneau's regulatory initiatives.

However, these rules are rooted in an era when the broadcasting and telecommunications sectors occupied separate market niches with different service providers. The broadcasting regulatory framework, as embedded in the *Broadcasting Act*, was conceived in an era when channels for distribution of broadcasting content were limited, and discrete networks were used for the distribution of radio, television and telecommunications. Broadcast programs could be received by the public only on devices dedicated to that purpose, primarily radio and television sets.

Technology and markets are clearly eroding the distinction between the broadcasting and telecommunications industries, as well as the distinctions between the types of devices used for both purposes. Cable TV networks, formerly dedicated to “broadcast distribution,” are increasingly being used to provide high-speed Internet access and other broadband telecommunications services, including voice over Internet Protocol (VoIP) based telephone services. “Telephone” networks are increasingly used to transmit high-speed data and video content, including content previously distributed on network television. Today, laptop computers, iPods, cell phones, BlackBerries, PDAs, and a range of other devices can be used interchangeably for broadcasting, data, voice and other telecommunications purposes.

More importantly, the number of channels for distributing broadcasting, or “electronic” content, is no longer limited. We have gone well beyond the 100-channel universe, toward a marketplace where the concepts of “channels” and “circuits” seem outdated. The widespread digitization of cable, satellite, wireline and wireless networks, combined with IP-based infrastructure supporting all forms of communication and content, has irrevocably changed broadcasting distribution markets.

More and more in today's world, there is no longer a shortage of channels, and technology is enabling direct access to audio and video content of all kinds in a manner that defies the traditional notion of a radio station or TV channel. Converged broadband cable, wireline, wireless and satellite networks deliver everything from voice telephony to broadcasting and the Internet. All forms of content are increasingly available on demand on IP-based platforms running over a variety of different regulated and unregulated networks.

Asymmetrical Regulation of a Converged Industry

Maintaining traditional broadcasting-type restrictions on the distribution of video or audio content over converged networks will become increasingly problematic. CRTC-regulated broadcasters and BDUs are understandably concerned about competition from unregulated services.

Concerns have also been expressed about the potential application of broadcasting-type content rules to online services, as well as about the impact such rules would have on the development of telecommunications network infrastructure, and the adoption and take-up of online services in Canada.

Strict application of the rules in the current *Broadcasting Act* could significantly impact telecommunications networks and online services. Producers are already delivering audio and video content via websites and even cell phones. Radio stations and music are widely available on the Internet. Many businesses and individuals make audio and video content available to the public from websites or through email, providing information, assistance and even entertainment to clients, friends or open user lists.

Absent the CRTC's *Exemption Order for New Media Broadcasting Undertakings*,⁴ the carriers, Internet service providers (ISPs), and other businesses and individuals involved in these activities would fall within the restrictions on content distribution imposed under the *Broadcasting Act*. The CRTC's exemption order provided timely clarity and certainty, which has helped foster the growth of advanced online services in Canada. However, recent calls for review of the exemption in response to the marketing of new services have started to undermine that certainty and clarity. Some parties have suggested that the CRTC should extend broadcasting regulation to new services that compete with those currently regulated under the *Broadcasting Act*. Conversely, others have suggested that the better course would be to start adapting the regulatory framework to enable currently regulated broadcasters to better compete in the new IP network environment.

At the same time as the benefits of the current form of broadcasting regulation are being reduced as its effectiveness erodes in the face of technological change, it must be recognized that the costs may be increasing. Broadcasting regulation can impose costs on the industry and on Canadian society and the economy as a whole. It can impede competition in broadband telecommunications markets, and impose artificial constraints on the capacity and utilization of BDU networks. For example, BDUs must reserve capacity and implement measures to prioritize and tier the delivery of various channels, to promote Canadian services. Such constraints inevitably affect the capacity of network operators to innovate and deploy the most efficient types of broadband networks. As more network operators add broadcasting distribution services, such rules will apply to an increasing number of networks. Yet, with the emergence of broadband IP networks, such measures are likely to become increasingly ineffective.

Although the constraints of broadcasting regulation apply to all forms of BDUs, they are arguably borne disproportionately by the cable industry. Cable telecommunications BDUs play a central role in the provision of advanced broadband telecommunications services in Canada. Their early introduction of cable modem services propelled Canada into its leadership position in the global race to deploy broadband access networks. Their current rollout of increasingly functional IP-based platforms is similarly important to the development of a competitive Canadian ICT industry. In the long run, Canada may lose more by restrictive regulation of cable telecommunications networks to advance a declining form of broadcast content delivery than it could gain by embracing the full potential of new cable-based IP platforms.

The Panel believes, in order to realize the full potential of broadband services in Canada, the asymmetry between the broadcasting and telecommunications regulatory frameworks should be examined.

⁴ Public Notice CRTC 1999-197, December 17, 1999.

International Trends

An increasing number of countries are developing integrated regulatory frameworks that take into account the convergence of telecommunications and broadcasting distribution from consumer, technological and market perspectives. Some countries, such as those in the European Union, are severing the policy link between regulation of broadcasting content and regulation of the telecommunications or “carriage” services used to provide access to broadcasting content.

European telecommunications and spectrum laws increasingly provide the basis for regulating all telecommunications networks — or “electronic communications networks,” as they are now called. Under European Commission policy, no distinction is made between the regulation of telecommunications networks that originated as telephone networks and those that originated as cable TV networks. Separate rules govern production and distribution of broadcasting content, but these are applied equally to all telecommunications networks.

This form of more symmetrical or “technology neutral” regulation should allow network operators the freedom to invest in and develop the IP network infrastructure in the most efficient and effective way possible in response to market demand. At the same time, it should enable policies dedicated to the promotion of video content to focus on the measures best suited to the new network environment.⁵

Conclusions and Proposed Approach

Since the Panel was not asked to review Canada’s broadcasting policy, it would be inappropriate for it to make specific recommendations for changes to broadcasting or regulation.

While the Panel recognizes the increasingly close links between telecommunications and broadcasting policy, it believes substantial progress can be made to improve Canada’s telecommunications policy and regulatory framework without directly affecting broadcasting policy or regulation. The Panel does not believe implementation of its recommendations for telecommunications reform should be delayed to await a review of broadcasting policy.

However, the Panel’s work over the past ten months has persuaded it of the need for a comprehensive review of Canada’s broadcasting policy and regulatory framework by an independent group of experts. The world has changed significantly since the last major reviews of broadcasting policy,⁶ and another review should be undertaken before technological and market changes undermine the current policy and regulatory framework.

The Panel believes this review should, at a minimum, consider the following issues.

⁵ In 2002, the OECD suggested that Canada should move toward a more converged environment. See OECD, *Regulatory Reform in Canada: from Transition to New Regulation Challenges* (Paris: 2002). Available online at: <http://www.oecd.org/dataoecd/48/28/1960562.pdf>

⁶ For example, at the time of the last comprehensive review of broadcasting policy, completed in September 1986 by the Task Force on Broadcasting Policy, chaired by Gerald Caplan and Florian Sauvageau, few if any Canadians had heard of the World Wide Web or the “Internet.” Twenty years ago, almost no one foresaw the potential for IP networks to deliver video and audio broadcasting in competition with off-air and cable broadcasters.

Legislative Framework — Separating Carriage and Content

Canada was a global leader in recognizing the trend toward convergence of the telecommunications and broadcasting industries. In 1976, it established one of the earlier “converged” regulatory agencies, the “new CRTC” (Canadian Radio-television and Telecommunications Commission), which was given regulatory authority over the telephone, private line and satellite communications industries, adding to the authority of the “old CRTC” (Canadian Radio and Television Commission), which regulated the television, radio and cable industries. However, Canada has maintained “two solitudes” in the laws that govern the carriage of telecommunications and broadcasting content. The *Telecommunications Act* deals with the provision of telecommunications services, including Internet access services by “common carriers.” The *Broadcasting Act* deals with the provision of one type of telecommunications service — namely the distribution of broadcasting content, by stations, networks and BDUs, primarily those in the cable industry. While the cable telecommunications industry is subject to the *Telecommunications Act* for certain non-broadcasting “carriage” activities, such as the provision of Internet access services, its carriage activities and its network infrastructure remain substantially regulated under the *Broadcasting Act* as well. The different treatment of telecommunications and broadcasting carriage functions has persisted, although it is increasingly difficult, if not impossible, to distinguish between the two.

Other member countries of the Organisation for Economic Co-operation and Development (OECD)⁷ as well as developing nations have taken steps to harmonize their legislative frameworks for telecommunications and broadcasting — while separating carriage and content rules. The U.S. has had a single communications law for both industries since 1934.⁸ The member countries of the European Union have moved well along the way to implementing a converged regulatory approach to telecommunications “carriage” services provided by telecommunications common carriers and cable networks.

The EU’s 2002 Framework Directive⁹ for electronic communications networks does not differentiate among types of networks or technologies, except that networks making use of radiocommunications remain subject to spectrum licensing requirements. Because of its technological neutrality, and the use of the broadly defined terms “electronic communications networks” and “electronic communications services,” the new framework is consistent with technological and market convergence, particularly between conventional public telecommunications networks and cable television distribution networks.

The EU’s 2002 Framework Directive deals with “carriage” issues. A separate EU directive deals with “content.” Broadcasting or audiovisual programming policy for the EU is the subject of the “Television Without Frontiers Directive.”¹⁰

⁷ We note that a recent OECD report (OECD 2002, p. 49) suggests, “There is a scope for the government to further review developments in convergence between telecommunication and broadcasting, in particular as regards merging legal frameworks to ensure that carriage regulation comes within the scope of a single regulatory framework.”

⁸ The *Communications Act* of 1934 deals with telecommunications and cable undertakings in different parts or “Titles” of the Act, but recently the FCC has taken steps to adopt a more consistent and competitively neutral approach to regulatory treatment of both industries. The FCC recently removed the requirement for the resale of DSL lines in order to put these providers on an equal footing with cable-based services. See FCC, “*FCC Eliminates Mandated Sharing Requirement on Incumbents Wireline Broadband Internet Access Services*,” August 5, 2005. Available online at: http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-260433A1.pdf

⁹ Directive 2002/21/EC on a common regulatory framework for electronic communications networks and services, March 7, 2002.

¹⁰ Council Directive 89/552/EEC of October 3, 1989 “on the coordination of certain provisions laid down by Law, Regulation or Administrative Action in Member States concerning the pursuit of television broadcasting activities.”

This trend toward convergence of the policies and laws governing “carriage” of telecommunications and broadcasting, and establishment of a separate set of rules to promote audiovisual content, should be considered in any review of Canadian broadcasting policy. Such a review should consider the following issues:

- the merits of adopting unified legislation to deal in a consistent and non-discriminatory manner with all forms of “telecommunications”; that is, electronic communications “carriage” services, whether routed over the networks of former telephone, cable TV, satellite, terrestrial wireless or other facilities
- establishment of “content rules” that are clearly separate from but compatible with the unified telecommunications legislation, to deal with promotion of Canadian content services over all forms of electronic “carriage” networks
- updating the content rules to develop more targeted and effective means of promoting the production and distribution of Canadian content in light of the significant technological and market changes currently under way, especially the transition of BDUs, telecommunications common carriers and wireless telecommunications service providers to multi-service IP platforms.

Policy-making Framework — Developing a Consistent Approach

The Panel believes it is time to review the relationship between the federal government’s policy-making frameworks for broadcasting and telecommunications. As with regulatory convergence, Canada was an early leader in convergence of policy making. Canada established a unified Department of Communications (DOC) in the late 1960s with a mandate to develop policies for telecommunications, broadcasting and other aspects of wired and wireless communications. The DOC was abolished in 1993 as part of a general reorganization and reduction in the number of government departments. The DOC’s telecommunications policy-making functions were assigned to Industry Canada, and its broadcasting policy-making functions went to the Department of Canadian Heritage.

Since that time, these two departments have operated, far more than they should, as “two solitudes” — with often conflicting policy agendas. This complete separation of policy-making functions for broadcasting and telecommunications does not seem to be best suited to advancing the broader Canadian objective of becoming leaders in all areas of ICTs.¹¹ In this context, the Panel believes the review of Canadian broadcasting policy should include the following issues:

- The advantages and disadvantages of establishing a “converged” policy-making role to cover telecommunications, broadcasting, and other aspects of ICT policy should be examined.

¹¹ A recent OECD report (OECD 2002, p.12) notes that the CRTC reports to Parliament through the Minister of Canadian Heritage (the Ministry responsible for broadcasting policy). The report notes, “This Department is not responsible for economic regulation but for cultural policy so that it is not evident that this is the best way for the CRTC to report to Parliament.”

- Given the importance of ICTs to the future of Canadian prosperity and culture, consideration should be given to assigning this converged policy-making role to a separate new “Department of Information and Communications Technologies.” Such a department could become the unified centre, within the Government of Canada, for all major policy making and programs related to building and maintaining Canada’s leadership in ICTs. Alternatively, the unified policy-making function could be assigned to an existing department, such as Industry Canada or Canadian Heritage. In any event, the function should be coordinated with that of the National ICT Adoption Centre recommended in Chapter 7 of this report.

Regulatory Framework — Recognizing Convergence

While the CRTC has had authority to regulate both the telecommunications and broadcasting industries since 1976, it has done so under two completely separate mandates, set out in broadcasting and telecommunications legislation. The Commission staff responsible for broadcasting and telecommunications regulation have largely worked in separate branches, with little day-to-day contact. Commissioners have had somewhat greater exposure to both broadcasting and telecommunications issues, but most commissioners, other than the chair and vice chairs, have traditionally focused on one industry and have relatively little depth of experience in the operations of the other.

At the same time, neither “branch” of the Commission has developed any real expertise in dealing with the intellectual property issues that are becoming increasingly important in regulation related to content provided over both broadcasting and telecommunications networks, especially over the Internet and other IP-based platforms.

In December 2005, the Commission announced a staff reorganization, aimed in part at increasing the coordination of its telecommunications and broadcasting regulatory mandates. The Panel recognizes the benefits of this reorganization but considers that there may be advantages in moving further. Accordingly, the proposed review of Canadian broadcasting policy should examine the following issues:

- further reorganization of the CRTC to develop an increased capacity to deal with both the broadcasting, telecommunications and broader ICT industry implications of decisions related to its “broadcasting” and “telecommunications” mandates
- better coordination of the copyright-related functions of government with its ICT policies and regulations, including a consideration of possible consolidation of the regulatory functions carried out by the Copyright Board with the communications regulatory functions of the CRTC.

Foreign Ownership

One of the new objectives of Canadian telecommunications policy set out in the 1993 *Telecommunications Act* is to “promote the ownership and control of Canadian carriers by Canadians.” The Act provides that non-Canadians shall not control any telecommunications common carrier that owns or operates transmission facilities. It also limits holdings by non-Canadians to 20 percent of the voting shares in an operating company and $33\frac{1}{3}$ percent in a holding company.

Foreign Investment Rules in the Canadian Telecommunications Sector

The 1987 Policy Framework for Telecommunications in Canada, which first established foreign investment rules for telecommunications common carriers, was given the force of law in the 1993 *Telecommunications Act*. Section 16 of the Act requires that, in order to be eligible to operate in Canada, a telecommunications common carrier must be a “Canadian-owned and controlled corporation incorporated or continued under the laws of Canada or a province.” Subsection 16.(3) of the Act establishes the following Canadian ownership and control requirements for corporations that are Canadian carriers:

- not less than 80 percent of the members of the board of directors of the corporation must be individual Canadians
- Canadians must beneficially own, directly or indirectly, in the aggregate and otherwise than by way of security only, not less than 80 percent of the corporation’s voting shares issued and outstanding
- the corporation is not otherwise controlled by persons that are not Canadians.

The *Canadian Telecommunications Common Carrier Ownership and Control Regulations* of 1994 set the minimum Canadian ownership level for ownership at the holding company level at $66\frac{2}{3}$ percent of voting shares. This means that a foreign company that holds 20 percent of the voting shares of a Canadian telecom operating company (direct ownership) can also hold a $33\frac{1}{3}$ -percent stake in the voting shares of a company that holds the remaining 80 percent voting shares of the Canadian telecommunications operating company (indirect ownership), provided that the foreign company does not exercise control.

Resellers are not subject to Canadian ownership and control requirements. Nor do they apply to satellite earth stations or international submarine cables. Non-Canadian-owned or -controlled satellite operators may also provide services in Canada, if authorized to do so by Industry Canada.

The Panel’s approach to considering the ownership and control rules in the telecommunications sector is based on the same principles that have guided it in approaching other telecommunications regulatory issues within its mandate. The Panel believes, at this stage in the evolution of the telecommunications sector, Canada should rely primarily on market forces to achieve its telecommunications policy objectives. Where they are necessary, regulatory measures should be efficient, proportionate to their purpose and interfere with the operation of market forces to the minimum extent necessary to meet their objectives.

The Policy Debate

Canada is one of a small and declining number of OECD countries that still place explicit foreign investment restrictions on domestic telecommunications service providers.¹² While legal barriers to foreign investment in telecommunications carriers have been lifted in many countries, some still maintain various types of *de facto* controls through ownership of incumbent carriers, public interest tests for foreign investment and other less explicit policies. Nevertheless, it is clear that Canada ranks among the most restrictive countries in the OECD when it comes to explicit restrictions on foreign ownership of voting shares or on other means of controlling domestic telecommunications carriers.

The maintenance of these significant restrictions on foreign investment in Canadian carriers has been the subject of extensive debate since the restrictions were first announced in 1987 and enacted in the 1993 *Telecommunications Act*.

The debate was brought into sharp focus during 2003 when separate reports by two House of Commons committees (the Standing Committee on Industry, Science and Technology and the Standing Committee on Canadian Heritage) reached opposite conclusions on the merits of maintaining the telecommunications foreign investment restrictions.

The Standing Committee on Industry, Science and Technology, in its report *Opening Canadian Communications to the World* (April 2003),¹³ recommended that Canadian ownership requirements applicable to telecommunications common carriers should be entirely removed, including the prohibition against foreign control. It also recommended that any changes made to the Canadian ownership and control requirements applicable to telecommunications common carriers should be applied equally to broadcasting distribution undertakings.

The Standing Committee on Canadian Heritage, in its report *Our Cultural Sovereignty: The Second Century of Canadian Broadcasting* (June 2003),¹⁴ recommended that the existing foreign ownership limits for broadcasting and telecommunications should be maintained at current levels. The committee stated that it was convinced “any relaxation of the existing foreign ownership rules in broadcasting or telecommunications could have an adverse affect on the Canadian broadcasting system.”

¹² Most European countries significantly liberalized their telecommunications markets and removed ownership restrictions on foreign investors during the 1990s. Most of those countries that have retained foreign ownership restrictions are located outside Europe, specifically South Korea, Mexico, New Zealand, Australia and Turkey. In the late 1990s, the United States significantly liberalized its foreign ownership rules as they apply to investments by other WTO member countries. See FCC, “Commission Liberalizes Foreign Participation in the U.S. Telecommunications Market,” November 25, 1997. Available online at: http://www.fcc.gov/Bureaus/International/News_Releases/1997/nrin7042.html

¹³ Available online at: <http://www.parl.gc.ca/InfoComDoc/37/2/INST/Studies/Reports/instrp03/03-cov2-e.htm>

¹⁴ Available online at: <http://www.parl.gc.ca/InfoComDoc/37/2/HERI/Studies/Reports/herirp02-e.htm>

Submissions to the Panel took very different and strongly opposing positions on the foreign investment rules. Some strongly opposed any liberalization of the foreign investment rules in the telecommunications sector. Most favoured liberalization, but differed on how this could be best accomplished.

The major concerns about liberalization of the rules related to the potential impact of removing foreign investment restrictions in the telecommunications sector on owners of BDUs who use their facilities to provide telecommunications services as well as broadcasting services. The foreign ownership rules for BDUs are similar (although not identical) to those for telecommunications carriers. Section 3.(1) of the *Broadcasting Act* declares, “the Canadian broadcasting system shall be effectively owned and controlled by Canadians.” The foreign ownership rules are set out in a Directive to the CRTC from the Governor-in-Council.¹⁵

Cable TV companies were originally authorized to construct facilities for the purpose of distributing broadcasting services. In recent years, they have upgraded these facilities so that they can also provide telecommunications services, such as high-speed Internet access and telephone service. However, because these telecommunications services are provided by companies that are licensed as BDUs, the ownership and control of their facilities is subject to the provisions of the *Broadcasting Act*, not the *Telecommunications Act*. BDUs could therefore potentially be disadvantaged if ownership rules were relaxed or abolished under the latter Act, but not under the former.

Because the facilities they own are now used to carry broadcasting services as well as telecommunications services, some of Canada’s largest telecommunications common carriers, such as Bell Canada and TELUS Communications Inc. are now licensed as BDUs. Thus, even if the *Telecommunications Act* were amended to permit greater foreign ownership or control of Canadian telecommunications common carriers, these companies would remain subject to the foreign ownership and control provisions of the *Broadcasting Act*. This could potentially disadvantage their shareholders, in terms of the benefits that might result from a transfer of ownership, and weaken their competitive position in the Canadian telecommunications marketplace.

In summary, asymmetrical liberalization of Canada’s foreign investment rules — that is, liberalizing foreign investment rules for telecommunications carriers but not BDUs — could leave cable companies and some telecommunications companies in an unfair competitive disadvantage.

¹⁵ Direction to the CRTC (Ineligibility of Non-Canadians). Available online at: <http://www.crtc.gc.ca/eng/LEGAL/NONCANAD.HTM>

Benefits and Risks of Liberalization

General Benefits of Foreign Investment

The economic evidence establishing a positive link between foreign direct investment (FDI) and economic efficiency is generally strong, at least at the economy-wide and industry-wide levels. The economic case for liberalization of FDI is so well established in Canada and other OECD countries that the main area of economic debate is not whether it boosts domestic competitiveness and productivity, but by how much.

FDI can lead to improved economic efficiency in a number of ways. The entry and growth of foreign firms adds to competitive pressures on all firms in a market. Foreign investment often brings financial, technological, human resources, or other assets that domestic firms can access to improve their own performance. FDI can also provide an incentive for domestically owned firms to take initiatives to reduce or eliminate inefficiencies in their business practices and activities in order to compete with foreign-owned entrants. Foreign investment can be a driver of economic efficiency in several ways¹⁶:

- the “adoption” of foreign technology by domestically owned firms, for example, through (legal) copying or imitation, embodied in inputs purchased from multinational affiliates doing business in the host economy, or technology transfer by scientists, engineers or other employees of multinational affiliates who leave to start their own companies in the host economy or to join a domestically owned company
- the “appropriation” by domestically owned firms of training and other investments in general human capital, where some of that human capital investment is paid for by multinational affiliates but where the affiliates do not recapture their investments, either because the trained employees leave to start their own businesses or go to work for domestically owned firms
- the adoption of strategic management, marketing, human resources management and other managerial functions by domestically owned firms that contribute to efficiency improvements in the latter.

FDI is often associated with a wide range of other economic benefits. However, a direct causal linkage between FDI and these benefits is more difficult to establish, and the extent of the potential benefits is more difficult to measure. Examples include employment generation, the stimulation of positive balance-of-payments effects including import-replacing domestic production, and support for domestic investment (i.e. gross fixed capital formation).¹⁷

¹⁶ Steven Globerman, “Implications of foreign ownership restrictions for the Canadian economy — A Sectoral Analysis,” Discussion Paper 7 (Industry Canada: April 1999), pp. 3–4. Available online at: [http://strategis.ic.gc.ca/epic/internet/ineas-aes.nsf/vwapi/dp07e.pdf/\\$FILE/dp07e.pdf](http://strategis.ic.gc.ca/epic/internet/ineas-aes.nsf/vwapi/dp07e.pdf/$FILE/dp07e.pdf)

¹⁷ See Donald G. McFetridge, “Evaluation of Current Policy Towards Inbound FDI,” Paper prepared for CTPL, Trade and Investment Conference, University of Ottawa, November 19, 2004 (Ottawa: Carleton University, Department of Economics, revised December 2004), p. 2. Available online at: <http://www.carleton.ca/ctpl/conferences/documents/EvaluationofCurrentPolicyTowardsInwardFDI-McFetridge.pdf>

Foreign Investment in the Telecommunications Sector

Much attention has been paid by economists and governments to the economic benefits for host economies of foreign direct investment. However, much of the research has been at the economy-wide level. Less attention has been paid to quantifying the impact of foreign ownership restrictions in the telecommunications sector, particularly in industrialized economies like Canada's. However, the available research does suggest that liberalizing foreign investment rules in telecommunications can help improve economic efficiency and enhance consumer choice in telecommunications markets.

A number of submissions to the Panel cited a 2003 study by Network Research Inc.,¹⁸ which estimated that foreign ownership restrictions increase the cost of capital by at least \$1.06 per month per subscriber for an incumbent telephone company and by at least \$2.61 per month per subscriber for Canadian cable companies. The Panel notes that the Industry, Science and Technology Committee of the House of Commons concluded, on the basis of this study and anecdotal evidence from industry participants, that Canada's foreign investment rules in the telecommunications sector raise the cost of capital and create a disincentive to investment.

The Panel has also considered evidence that Canada's foreign investment rules impact negatively on the financing structures of Canadian telecommunications common carriers. In limiting a company's ability to raise equity outside Canada, the foreign investment rules provide an incentive for greater reliance on debt than equity capital and for raising a larger share of equity capital in Canada than firms otherwise might do.

A number of telecommunications companies, particularly those in emerging market segments in the wireless telecommunications field, have argued that the existing foreign investment rules are a disincentive for foreign investors to purchase non-voting shares (i.e. shares that are not directly subject to the foreign investment rules) no matter how attractively priced it is. Restrictions on the purchase and sale of voting shares certainly discourages investment by strategic investors. In some circumstances, strategic foreign investors can certainly add value to investments in providers of new services in the telecommunications and technology fields. In this regard, it has been said¹⁹:

They [strategic investors] may specialize in high-risk situations or they may be potential suppliers of expertise, technology or reputation. Transfer of strategic assets is complex. A simple royalty agreement is generally insufficient. Agreements to transfer strategic, intangible assets often involve a meaningful (i.e. voting) equity stake. This is not simply a bargaining issue. An agreement of this form is in the mutual interest of both parties in the transaction. The alternative may be either no transfer or one that is much delayed.

¹⁸ "The Implications of Foreign Ownership Restrictions Upon the Canadian Cable Television Industry" (Oakville, ON: February 12, 2003). Available online at: <http://www.ccta.com/CMFiles/26-03-cunningham50MAA-912004-6046.pdf>

¹⁹ McFetridge, p. 12.

During the hearings of the House of Commons Standing Committee on Industry, Science and Technology and in submissions to the Panel, some Canadian telecommunications firms (including wireless firms) stated that foreign ownership rules have limited their ability to attract strategic investors. There is anecdotal evidence available to support this view, although no directly relevant empirical studies were brought to the Panel's attention.

A number of studies have been conducted on the impact of foreign investment liberalization in the telecommunications sectors in other countries.²⁰ In general, these studies found positive associations between foreign investment liberalization and the economic performance of the telecommunications sector within the countries examined. For example, an econometric analysis undertaken by the OECD investigated the effects of entry liberalization and privatization on productivity, prices and quality of service in long distance (domestic and international) and mobile cellular telephony services in 23 OECD countries over the 1991–1997 period. The authors of the study²¹ concluded:

Controlling for technology developments and differences in economic structure, panel data estimates show that prospective competition (as proxied by the number of years remaining to liberalisation) and effective competition (as proxied by the share of new entrants or by the number of competitors) both bring about productivity and quality improvements and reduce the prices of all the telecommunications services considered in the analysis.

The Panel regards this and other international studies as providing only circumstantial support in favour of foreign investment liberalization in Canada's telecommunications sector. Very different and often unique circumstances affect the performance of telecommunications markets in different countries, including the state of development of the telecommunications supply sector, regulatory regimes and general economic circumstances. For this reason, the approach to foreign investment rules should take full account of the Canadian regulatory framework for telecommunications service providers, including their regulation under the broadcasting law, as well as the broader Canadian public interest in relation to the future development of the telecommunications system.

²⁰ See, for example, Steven Globerman, *Modern Telecommunications Infrastructure and Economic Performance* (2004); Steven Globerman, "Foreign Ownership in Telecommunications: A Policy Perspective," *Telecommunications Policy* 19 (1995): 2–28; Scott J. Savage, Alan Schlottman and Bradley S. Wimmer, *Telecommunications Investment, Liberalization and Economic Growth*, AEI-Brookings Joint Center for Regulatory Studies, Publication 03-30 (Washington, DC: December 2003), available online at: <http://www.aei.brook.edu/admin/authorpdfs/page.php?id=306>; Gary C. Hufbauer and Edward M. Graham, "'No' to Foreign Telecoms Equals 'No' to the New Economy," *International Economics Policy Briefs*, Number 00-7, September 2000, available online at: http://www.iie.com/publications/pb/pb00_7.pdf; and Micro-Economic Policy Analysis Branch, "Assessing Economic Impact of Foreign Ownership Restrictions in the Telecommunications Services Industry," Industry Canada, Ottawa, July 2001.

²¹ Olivier Boylaud and Guiseppe Nicoletti, "Regulation, Market Structure and Performance in Telecommunications," OECD Economic Studies No. 32, 2001/1 (OECD Publishing, 2000). Available online at: <http://www.oecd.org/dataoecd/24/33/2736298.pdf>

Canada's Performance in Wireless and Broadband Markets

In considering the potential benefits and risks of liberalization of Canada's foreign ownership restrictions, it is important to ask the questions:

- How are Canadian telecommunications markets performing today?
- Would they perform better if restrictions on foreign investment were relaxed?

If Canadian markets were leading the world in performance in all segments, the case for liberalization would not be as strong as it would be if Canadian markets were providing Canadians with fewer, poorer-quality or higher-priced services than markets in countries with fewer restrictions.

Chapter 1 of the report provides an overview of the performance of Canadian telecommunications markets relative to those in other OECD countries. Canadians have traditionally enjoyed among the highest quality and lowest prices of basic telephone services among OECD and G7 countries. The data in Chapter 1 indicate that Canadian telecommunications service providers have generally served the country well. Wireline telephone service is available to 99.5 percent of Canadian households, and 96 percent subscribe to the service. This number has come down slightly in recent years because of wireless substitution. Canada ranks seventh among OECD countries and second among G7 countries in the level of main telephone line subscribers per 100 population.

Canada has been a global leader in making broadband telecommunications services available to its citizens. In the mid-1990s, Canada was the first OECD country in the world to deploy DSL (digital subscriber line) technology and the second to deploy cable modem technology. Until 2003, Canada ranked second in the world in terms of the number of broadband subscribers per 100 population. However, Canada's role as a leader in broadband deployment is slipping somewhat. In June 2005, Canada was ranked sixth in terms of subscribers per 100 population, and sixth in terms of the lowest available broadband pricing among OECD countries. As described in Chapter 1, Canada risks slipping further behind as other countries including the U.S., Japan and South Korea move aggressively to deploy more advanced, high-speed networks using fibre-to-the-home (FTTH) technology with speeds up to 100 Mbps.

Canada's comparative performance has not been nearly as good when it comes to wireless telecommunications services. This is a troubling indicator, since wireless services, both mobile and fixed, are increasingly important to Canadian productivity and to the potential convenience, entertainment, security and other social benefits that individual Canadians obtain from telecommunications.

Today, Canada ranks second last of 30 OECD countries in terms of the number of wireless subscribers per 100 population. There are historical reasons for Canada's lagging performance, including Canada's comparatively low-cost wireline services and the fact that, in Canada, wireless providers do not charge on the calling-party-pays basis that is used in many other OECD countries. However, the same circumstances as in Canada apply in U.S. markets. In the third quarter of 2005, the U.S. wireless penetration rate of 67 per 100 population was well ahead of the Canadian rate of 50.6.²² In addition to having lower mobile wireless penetration than the U.S., Canada has much lower wireless usage — about 52 percent of the average U.S. usage, measured in minutes of use per month. As a related metric, the prices of Canadian wireless services are relatively high. Canada ranks tenth among OECD countries based on the prices to low-usage customers, seventh on prices to medium-usage customers and 13th on prices to high-usage customers.

There is evidence to suggest that emerging new telecommunications markets, particularly the fixed wireless broadband market, are developing and deploying new services faster in the U.S. and many other countries than they are in Canada. There has been rapid deployment of innovative new fixed wireless services in most OECD countries outside North America by service providers with regional and national licenses. For a number of reasons, Canada has not moved as quickly.

It seems likely that the quality, pricing and availability of wireless services — both mobile and fixed — would improve significantly if Canada's foreign ownership restrictions were liberalized. It has been pointed out to the Panel that Canadian telecommunications markets are not as competitive as those in the U.S. The number of cellular mobile service providers has shrunk to three, all of which are owned by wireline telephone or cable groups. Canada has been slow to adopt pro-competitive initiatives, as described in Chapter 1.

Canada is one of very few, if any, OECD countries where major international wireless operators do not participate actively in the supply of wireless services. The major multinational wireless operators have brought significant new technology transfers, capital, marketing and management know-how to the U.S. and most other OECD countries — but they are not able to participate fully in Canadian markets. Based on the experience of other countries, it seems difficult to dispute that their presence would significantly improve the range, quality and pricing of wireless services available to Canadians.

²² Source: Merrill Lynch, Global Wireless Matrix, 3Q2005.

The Panel believes the same would be true in the case of fixed wireless broadband markets — markets that are key to Canada’s ability to provide broadband connectivity to its citizens, and to roll out productivity-enhancing services to Canadian business. Accordingly, the Panel believes the case for liberalization of Canada’s foreign investment restrictions is strongest in the newer, emerging markets, where Canadian performance lags that of other countries — such as those in the mobile and fixed wireless markets.

Public Interest Considerations

The economic reasons for liberalization of the foreign investment rules in Canadian telecommunications markets are strong, particularly in newer, emerging markets, where global technology and other transfers of “know-how” could accelerate the deployment of advanced services. However, the Panel has also considered the concerns expressed by some parties that liberalization will constrain Canada’s ability to achieve other policy objectives and protect the public interest in a number of other respects. These concerns have often focused on the significant place that Canada’s largest telecommunications carriers occupy in the Canadian telecommunications and broadcasting markets. Two companies, BCE Inc. and TELUS Corp., account for 80 percent of all revenues in the telecommunications segment,²³ and two other companies, Rogers Communications Inc. and Shaw Communications Inc., account for approximately 70 percent of cable telecommunications segment revenues in Canada.²⁴ Three of the same four firms, BCE, TELUS and Rogers, account for 92 percent of the mobile wireless market in terms of subscribers (85 percent in terms of revenues).²⁵

Four examples of public interest concerns about foreign control of Canadian telecommunications carriers, although certainly not the only ones, relate to retention of head offices and head office functions for telecommunications firms in Canada, retention of employment and highly talented and skilled employees in the telecommunications sector, retention of research and development (R&D) activity in Canada, and protection of Canada’s public safety and national security.

Head Office Location and Functions

There is a concern that in some cases a foreign acquisition of a Canadian company may result in the transfer out of Canada of the target company’s head office functions to the U.S. or other foreign jurisdiction of the new parent company. There are examples where this has occurred in the past. The highly networked nature of telecommunications services facilitates the centralization of some management and network control functions. However, these functions may be established in different locations, either in Canada or another country, and it is not clear that Canada would be a net loser of head office or network control functions, even if some Canadian carriers became controlled by non-Canadian firms.

²³ Source : Based on OECD Communications Outlook 2005.

²⁴ Source : National Bank Financial, Communications and Media, January 5, 2006 (Rogers Communications and Shaw Communications).

²⁵ Source : Based on company financial results.

Nevertheless, a concern remains, particularly in the case of the large Canadian telecommunications companies with extensive head office functions, that the transfer of ownership to U.S. or other foreign company could lead to a transfer of positions for skilled and well-paid positions out of Canada. Similarly, there is a concern that a foreign-owned company would no longer rely, to the same degree, on Canadian engineering, financial, management consulting and other advisory services that are ancillary to head office functions.

Mobile Talent and Employment

As a related matter, the Panel notes that Canada faces a significant demographic challenge. Canada is moving from a surplus labour market to a deficit labour market where it can expect to face shortages of labour across all sectors and regions of the country.²⁶ In this context, concerns have been expressed that foreign acquisition of major Canadian telecommunications carriers could lead to the loss of highly skilled personnel or a decline in new employment opportunities — beyond those related to head office functions.

In the telecommunications sector, it is not clear that such a job loss would occur, given the strong incentives for the foreign acquirer to retain and attract highly qualified individuals to run the knowledge-intensive telecommunications business. It is also noted that new “greenfield” investment, domestic or foreign, in the Canadian telecommunications sector would likely create new employment. Such investment could also provide incentives for increasingly mobile and talented individuals to stay in Canada rather than migrate to other locations around the world.

Research and Development

R&D activity in the telecommunications sector, and more broadly in the ICT industries, is important for the telecommunications industry itself, but more generally for Canada’s future economic prosperity. As discussed in greater detail in Chapter 7, in the absence of a strong telecommunications (and ICT) R&D base, Canada will lack the people, ideas and knowledge networks to effectively shape and implement ICT adoption strategies throughout the Canadian economy.

In this context, the weight of the economic evidence is that foreign investment can bring important R&D capabilities into Canada, including and not only greenfield investments. Nevertheless, in a foreign takeover of some existing Canadian telecommunications carriers, the implications for Canadian R&D performance could be a matter of public interest. The focus of concern may not necessarily be connected with the R&D undertaken directly by a telecommunications carrier acquired by a foreign firm, but rather with future willingness to purchase innovative new products and technologies from other Canadian companies that have formed part of its supply chain, instead of from the supply chain companies of the foreign acquirer.

²⁶ According to the Department of Finance, “currently there are more than five people of working age (15 to 64) for every person of retirement age (65+). Within the next 15 years, this ratio is projected to fall to four to one, and to be less than two and a half to one by 2050.” Department of Finance, *A Plan for Growth and Prosperity* (Ottawa: November 2005), p. 57. Available online at: <http://www.fin.gc.ca/ec2005/ec/ecce2005.pdf>

Public Safety and National Security

A number of submissions to the Panel raised the issue of the impact of foreign investment liberalization in the telecommunications sector on Canada's ability to protect its public safety and national security interests. The Panel also notes that the existing foreign investment rules for telecommunications, which are founded on voting share restrictions, may not fully address national security concerns.

Canada has not been immune from the concerns about national security that have increased around the world in recent years. The Panel notes that on June 20, 2005, the Minister of Industry tabled in the House of Commons Bill C-59, *An Act to amend the Investment Canada Act*, which would "enable the government to review foreign investments in those rare instances where they might compromise Canada's national security."²⁷ Bill C-59 was not passed before Parliament was dissolved in December 2005.

Telecommunications infrastructure plays a vital role in every country's national security. Most of the concerns about national security can and should be dealt with through the implementation of effective legislation dealing with wiretapping, cybercrime and general criminal law. However, in the heightened security environment of the early 21st century, it is likely that the foreign acquisition of the major telecommunications carriers of OECD countries such as the U.S., U.K., France, Germany and Japan could nevertheless raise concerns about national security, depending in part on the nationality and motivation of the acquirer. These countries maintain explicit or implicit controls on foreign investment in their telecommunications carriers.

Impacts on Broadcasting Policy

While the foregoing public interest concerns have been raised in the context of liberalization of Canada's foreign ownership restrictions on telecommunications common carriers, the strongest concerns that have arisen in recent years concern the impact of such liberalization on the effectiveness of Canadian broadcasting policy.

In this context, the Panel notes that in the same year that the House of Commons Standing Committee on Industry, Science and Technology recommended liberalization of the foreign ownership restrictions on telecommunications carriers, the House of Commons Standing Committee on Canadian Heritage recommended maintaining the existing rules "in order to protect Canada's broadcasting system from foreign domination." Similar concerns have frequently been expressed by members of Canada's broadcast production community and related organizations.

²⁷ "Minister of Industry Introduces Amendments to the *Investment Canada Act*" Industry Canada Press Release, June 20, 2005. Available online at: <http://www.ic.gc.ca/cmb/welcomeic.nsf/cdd9dc973c4bf6bc852564ca006418a0/85256a5d006b972085257026004f0c6!OpenDocument>

The concern is based in part on the reasonable assumption that removal of foreign investment restrictions on telecommunications common carriers would require the government to also remove restrictions on foreign investment in the BDUs that operate in the same market as them.

Since telecommunications common carriers increasingly compete in the same markets as BDUs, the Panel agrees that it would be competitively inequitable and financially damaging to the BDU industry to retain foreign ownership restrictions on them while removing them from telecommunications common carriers. To the extent that removal of the restrictions would lead to greater- or lower-cost access to foreign capital markets, the regulatory framework for foreign ownership should treat both types of competitive players fairly.

However, the Panel believes it should be possible to develop a phased and flexible approach to liberalization of Canada's foreign ownership restrictions. Such an approach should treat the major players in both industries equitably, while permitting Canada to benefit in the short term from foreign investments in new and smaller players, especially in emerging markets where such investments are likely to substantially improve the efficiency and performance of our telecommunications markets.

Conclusions and Proposal

Among OECD countries, Canada has maintained one of the most restrictive and inflexible set of rules limiting foreign investment in the telecommunications sector. However, the Panel notes that countries that have removed, or significantly liberalized, their foreign investment restrictions in their telecommunications sectors have generally not relinquished all capacity to respond to public interest considerations related to foreign investment in their telecommunications markets. Other OECD countries have in place explicit or implicit safeguards to ensure that foreign investment in their telecommunications markets serves and does not prejudice their national public interest.

In the U.S., for example, the *Communications Act* of 1934 allows the Federal Communications Commission (FCC) to deny radio licences to corporations with greater than 25-percent foreign investment if the public interest is served by this refusal. In the age of wireless communications, this public interest safeguard has a very broad application. In addition, the U.S. government retains considerable discretion over the review of all foreign direct investment for purposes of protecting national security.²⁸ The Panel has been advised that other oversight mechanisms can be used to screen foreign investments in key telecommunications infrastructure in EU and other OECD countries.

The Panel sees significant merit in removing Canada's current rigid and inflexible restrictions on foreign investment in telecommunications markets and replacing them with a more flexible regime that permits such investment where it benefits Canada and restricts investments that would not benefit Canada.

²⁸ Section 5021 of the U.S. *Omnibus Trade and Competitiveness Act* of 1988 amended Section 721 of the *Defense Production Act* of 1950 to provide authority to the U.S. President, commonly referred to as the Exon Florio provision, to suspend or prohibit any foreign acquisition, merger or takeover of a U.S. corporation that is determined to threaten the national security of the United States.

Such a regime could consider potential benefits of specific types of investments such as promotion of competition, better service and innovation in markets that are not performing as well as they should, as well as risks such as those described in the section of this Afterword dealing with public interest considerations. Other factors involving Canada's interests could be taken into account, such as security concerns and multi-sector trade negotiations or relations. For example, it may not be in Canada's interests to approve an investment from a country during a period when that country has in place non-tariff barriers to Canadian trade in other significant markets. A more flexible investment regime would permit a balancing of the Canadian public interest, and not preclude Canadians from achieving the real benefits that could be realized from foreign investment.

As the Panel notes, the relationship between Canadian broadcasting policy and telecommunications policy has been a major issue in the debates on liberalization of Canadian foreign investment restrictions in the telecommunications industry. While removal of the telecommunications restrictions would increase the competitiveness of the telecommunications industry in key market segments, and would improve the productivity of Canadian telecommunications markets, concerns have consistently been raised about the impacts on Canadian broadcasting policy — particularly about the impacts on Canadian broadcasting of increased foreign investment in Canadian cable and satellite BDUs.

Earlier in this Afterword, the Panel suggests that the proposed broadcasting policy review should resolve issues related to the separation of Canadian broadcasting “content” policy from policies for the “carriage” of telecommunications. Such a separation would permit creation of symmetrical foreign investment rules for traditional telecommunications carriers as well as the cable and satellite undertakings that now operate in the same telecommunications markets.

Pending completion of this review, the Panel proposes that the government should adopt a phased and flexible approach to liberalization of restrictions on foreign investment in telecommunications service providers to the extent that they are not subject to the *Broadcasting Act*. Ownership and control of Canadian telecommunications common carriers should be liberalized in two phases:

- In the first phase, the *Telecommunications Act* should be amended to give the federal Cabinet authority to waive the foreign ownership and control restrictions on Canadian telecommunications common carriers when it deems a foreign investment or class of investments to be in the public interest.

- During the first phase, there should be a presumption that investments in any new start-up telecommunications investment or in any telecommunications common carrier with less than 10 percent of the revenues in any telecommunications service market are in the public interest. This presumption could be rebutted by evidence related to a particular investor or investment. The presumption should apply to all investments in fixed or mobile wireless markets as well as to investments in new entrants and smaller players (i.e. those below the 10-percent limit). To encourage longer-term investment, foreign investors should remain exempt from the foreign investment restrictions if they are successful in growing the market share of their businesses beyond 10 percent.
- The second phase of liberalization should be undertaken after completion of the review of broadcasting policy proposed by the Panel. At that time, there should be a broader liberalization of the foreign investment rules in a manner that treats all telecommunications common carriers including the cable telecommunications industry in a fair and competitively neutral manner. The proposed liberalization should apply to the “carriage” business of BDUs, and new broadcasting policies should focus any necessary Canadian ownership restrictions on broadcasting “content” businesses. The Cabinet should retain the authority to screen significant investments in the Canadian telecommunications carriage business to ensure that they are consistent with the public interest.

As indicated in its proposal, the Panel believes, in liberalizing Canada’s foreign ownership rules, it would be preferable to amend the *Telecommunications Act* to permit the foreign acquisition of a Canadian telecommunications common carrier, if it is in the public interest to do so. This would likely provide for a phased liberalization approach that would be better suited to the Canadian communications sector than if this authority was exercised under the *Investment Canada Act*. In particular:

- It would provide a better alternative to the economy-wide “net benefits” approach used under the *Investment Canada Act*, and would permit the development of Canadian policies favouring foreign investment in ways that reflect the telecommunications sector’s structure, regulatory environment and market circumstances. For example, it would facilitate introduction of the Panel’s proposed presumption that foreign investment in any new entrant or telecommunications common carrier with less than 10 percent of the revenues in the telecommunications service market would be in the public interest unless otherwise shown. Investments in such companies generally will not raise significant issues of competitive fairness for existing incumbents that are currently subject to the foreign investment restrictions of either the *Telecommunications Act* or the *Broadcasting Act*. Many of the relevant markets that would be covered under this presumption represent emerging and innovative sectors where new and patient capital is critical, such as new applications of fixed and mobile wireless technology.
- It would likely raise fewer potential trade and investment policy problems in relation to Canadian commitments under Chapter 11 of the North American Free Trade Agreement.
- It would permit the development of more transparent and concrete criteria for the application of a public interest test (including in the area of public safety and national security) than are currently available or contemplated under the *Investment Canada Act*.