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

Telecom Decision CRTC 2005-67

Ottawa, 10 November 2005

TELUS Communications Inc. - 2005 application to increase the capital cost of the service improvement plan and related matters

Reference: 8638-C12-73/02

In this Decision, the Commission ***approves with changes*** *TELUS Communications Inc.'s 2005 application to adjust its total subsidy requirement and draw-down from its deferral account to reflect an increase in its projected service improvement plan capital expenditures.*

1. The Commission received an application by TELUS Communications Inc. (TCI), dated 31 March 2005, and amended on 9 May 2005, for approval of its 2004 service improvement plan (SIP) tracking report. The application was filed pursuant to Part VII of the *CRTC Telecommunications Rules of Procedure,* and to *Regulatory framework for second price cap period,* Telecom Decision CRTC 2002-34, 30 May 2002 (Decision 2002-34).

2. TCI requested approval of (a) an increase of $6.8 million in its projected SIP capital expenditures to a revised total of $30.3 million, (b) related adjustments to its total subsidy requirement (TSR) for high-cost serving areas (HCSAs) and draw-down from its deferral account for non high-cost serving areas (non-HCSAs), and (c) an accelerated draw-down schedule from the deferral account. TCI also provided its accomplishments for 2004 and its projected capital expenditures for 2005 and 2006.

Process

3. On 25 August 2005, the Commission issued an interrogatory. On 2 September 2005, TCI filed its response.

4. The Commission received no comments with respect to the application.

Background

5. In *Telephone service to high-cost serving areas*, Telecom Decision CRTC 99-16, 19 October 1999 (Decision 99-16), the Commission examined the level of telecommunications service in Canada and concluded that it was, in general, very high. The noted exceptions were the HCSAs, which are generally found in remote, rural regions and in the Far North. The Commission noted that telephone service to these areas was generally more costly to provide and was often of lower quality than service in other regions.

6. The Commission determined that it was appropriate to define a Basic Service Objective (BSO) to ensure that a basic level of telephone service would be available to the public throughout Canada.

7. In Decision 99-16, the Commission defined the BSO as comprising:

   (a) individual line local service with Touch-Tone dialling, provided by a digital switch with capability to connect via low-speed data transmission to the Internet at local rates;

   (b) enhanced calling features, including access to emergency services, Voice Message Relay service, and privacy protection features [included in call management services (CMS)];

   (c) access to operator and directory assistance services;

   (d) access to the long distance network; and

   (e) a copy of a current local telephone directory.

8. In order to implement these goals, the Commission directed all incumbent local exchange carriers (ILECs) to file SIPs for approval, or to demonstrate that the BSO had been and would continue to be achieved in their territories. The ILECs were directed to consult with stakeholders prior to preparing their SIPs.

9. In Decision 2002-34, the Commission addressed the implementation of TCI's SIP. The Commission:

   (a) approved a SIP for unserved premises for TCI of $10.6 million in capital expenditures. The Commission stated that it intended to review TCI's progress in implementing its SIP on a yearly basis, as reported in its tracking plan, to determine whether additional capital and funding were required and directed TCI to commence rolling out its SIP in 2002;

   (b) directed TCI to add its Phase II SIP costs for HCSAs to the costs that flow into its TSR calculations;

   (c) allowed the explicit recovery by TCI of the Phase II costs associated with its SIP in non-HCSAs by means of a draw-down from its deferral account; and

   (d) directed TCI to start a project in a locality if it met the following criteria: (a) the maximum average cost per premises was $25,000 using a 100 percent take rate; and (b) at least one customer requested service and was willing to contribute $1,000. The Commission also directed TCI to start with those localities that had the highest demand.

10. In *Follow-up to price cap Decision 2002-34: TELUS' revised service improvement plan*, Telecom Decision CRTC 2003-64, 25 September 2003 (Decision 2003-64), the Commission approved a revised SIP for TCI of $21.4 million and a revised roll-out period of 2003 to 2006.

11. In *TELUS Communications Inc. - Application to increase the capital cost of the service improvement plan and related matters,* Telecom Decision CRTC 2004-76, 16 November 2004 (Decision 2004-76), the Commission approved TCI's application to increase the capital cost of its SIP to $23.5 million, and also approved the following related matters: (a) an adjustment to the company's annual SIP TSR associated with its draw-down from the National Contribution Fund (NCF); and (b) an annual SIP draw-down from its deferral account.

Issues

Projected capital expenditures

12. TCI indicated that the total projected capital expenditures for its SIP had increased to $30.3 million, from the $23.5 million previously approved in Decision 2004-76. TCI provided details of the incremental projected $6.8 million in capital expenditures, indicating that they resulted from changes in project estimates and increases in demand. TCI also indicated that this $6.8 million increase in capital expenditures would result in incremental adjustments to the TSR and incremental adjustments to its draw-down from its deferral account. TCI filed a Phase II cost study to support its proposal.

Cost recovery in HCSAs

13. To recover the incremental HCSA SIP costs resulting from the incremental $6.8 million in capital expenditures, TCI indicated that the incremental adjustments to the TSR would be as follows:

Alberta Band E:	$0.32 per residential network access service (NAS) per month
Alberta Band F:	$0.35 per residential NAS per month
Alberta Band G:	($0.14) per residential NAS per month
B.C. Band E:	$0.31 per residential NAS per month
B.C. Band F:	$0.08 per residential NAS per month
B.C. Band G:	$0.65 per residential NAS per month

Cost recovery in non-HCSAs

14. TCI proposed the following accelerated draw-down schedule to recover all its non-HCSA SIP costs, including the end-of-study (EOS) amounts within the period 2004 to 2006:

(a) for each of the years 2004 to 2006, an annual draw-down from the deferral account of $6.0 million representing (i) Phase II costs of $1.74 million, and (ii) an EOS amount of $4.23 million, to recover the non-HCSA SIP costs resulting from the $23.5 million in capital expenditures approved in Decision 2004-76; and

(b) for each of the years 2005 and 2006, an additional annual draw-down from the deferral account of $1.5 million representing (i) Phase II costs of $0.34 million; and (ii) an EOS amount of $1.15 million, to recover the non-HCSA SIP costs resulting from the incremental capital expenditures of $6.8 million proposed in this application.

15. TCI identified that its proposal would result in the company recovering $20.9 million over the period of 2004 to 2006. TCI indicated that if its proposal were approved, it would no longer require any draw-down from its deferral account after 2006.

16. In response to a Commission interrogatory, TCI indicated that it was opposed to a cost recovery plan for its SIP in non-HCSAs that excluded an EOS adjustment. TCI noted that the Commission's proposed recovery plan entailed drawing down the Phase II annual equivalent costs, excluding the EOS adjustment, from the company's deferral account, namely, $1.74 million in 2004 and $2.08 million in 2005 and subsequent years. TCI argued that this plan presumed that it would be able to recover its non-HCSAs SIP costs over the service lives of the equipment and that the deferral account would be maintained beyond the end of the current price cap period. TCI submitted that increased competitive pressure, particularly in non-HCSAs, would undermine its ability to recover its SIP investment over an extended time period and would make the recovery of this investment over the service lives of the equipment uncertain.

17. TCI submitted that the Commission had clearly recognized that the ILECs and their customers were financing the SIPs. TCI noted that in HCSAs, the increase in costs resulting from the SIP was recovered from the NCF. TCI further noted that the funding for the SIPs in non-HCSAs was recovered from the ILECs' deferral accounts.

18. TCI submitted that competitive local exchange carrier (CLEC) revenues from customers in non-HCSAs do not provide any funds to the ILECs' deferral accounts. TCI asserted that as the ILECs lose customers to CLECs in non-HCSAs, the remaining ILEC customers were expected to continue to fund the SIPs until these costs are recovered. TCI submitted that while this funding model would have been sustainable in a monopoly environment or prior to cable company entry in the local exchange business, it cannot be sustained over the service lives of the equipment as competitive losses increase.

19. TCI submitted that the SIP costs in non-HCSAs must be funded internally by the ILECs' customers in non-HCSAs and yet, they are no different than the SIP costs in HCSAs that were funded through a competitively-neutral contribution mechanism. TCI submitted that the Commission's method of providing for recovery of SIP costs in non-HCSAs was not competitively-neutral and was, therefore, contrary to the Commission's own contribution policy. TCI submitted that the only equitable long-term funding model for the SIPs in non-HCSAs was to add the SIP cost recovery to the TSR funded through the NCF.

20. TCI submitted that, additionally, in the proceeding initiated by *Review and disposition of deferral accounts for the second price cap period*, Telecom Public Notice CRTC 2004-1, 24 March 2004, it proposed the elimination of the deferral account at the end of the price cap period. TCI noted that the current price cap period may be extended by up to two years as a result of the proceeding initiated by *Proceeding to consider extending the price regulation regime*, Telecom Public Notice CRTC 2005-3, 13 May 2005. TCI proposed that the timing of the draw-downs from the deferral account be matched to the progress and completion of the deferral account initiatives.

21. TCI submitted that, for the reasons mentioned above, the EOS adjustment for its SIP in non-HCSAs must be recovered from the deferral account over the period 2004 to 2006.

$1,000 customer contribution

22. TCI indicated that the Phase II costs that were filed in previous tracking reports did not include any effects related to the $1,000 customer contribution revenue. TCI provided details of the customer contribution revenue information used to reduce a particular year's draw-down requirement.

SIP roll-out

23. TCI noted that it had become apparent that SIP projects typically span two years from the initial customer contact to the in-service date for a given community. TCI further noted that this reflected the time and resources required to provide service to unserved communities, and the constraints imposed by the geography of the communities and associated seasonal conditions. Accordingly, TCI submitted that SIP projects started in 2006 would not be completed until 2007.

Commission's analysis and determinations

Projected capital expenditures

24. Pursuant to the determinations in Decision 2002-34, the Commission expected that the size of the ILECs' SIPs would vary over time during the roll-out periods. The Commission notes that the $6.8 million increase results from changes in project estimates and increases in demand. The Commission finds that the changes are reasonable and **approves** the $6.8 million increase in projected capital expenditures, which results in a new SIP total of $30.3 million.

Cost recovery in HCSAs

25. The Commission has reviewed the Phase II cost studies that support the requested incremental adjustments to the TSR for the draw-down from the NCF for HCSAs and finds that they are satisfactory. Accordingly, the Commission **approves** the cost studies and incremental adjustments.

Cost recovery in non-HCSAs

26. The Commission notes TCI's assertion that recovery of its SIP investment would be compromised if it was not allowed to recover its costs during the 2004 to 2006 period. Given TCI's current dominant position in the residential local service market, the Commission is of the view that an accelerated recovery of these costs would not be appropriate. The Commission notes that, pursuant to Decision 2002-34, its standard practice has been to allow the recovery of SIP costs in non-HCSAs from the deferral account over the life of the equipment. Furthermore, the Commission has approved a SIP cost study for Bell Canada that provides for recovery of their SIP costs over the life of the equipment.

27. The Commission considers that its practice established in Decision 2002-34 to recover SIP costs over the life of the equipment continues to be appropriate. Accordingly, the Commission **denies** TCI's proposal that all the non-HCSA costs be recovered within the 2004 to 2006 period.

28. The Commission notes that, based on the evidence, the annual draw-down amounts to recover the SIP costs over the life of the equipment would be (a) $1.74 million for 2004; and (b) $2.08 million for 2005 and onwards. In light of the above, the Commission **approves** these annual draw-down amounts from the deferral account.

$1,000 customer contribution

29. In Decision 2004-76, the Commission noted that TCI had incorrectly credited the $1,000 customer contribution to the capital cost of its SIP. The Commission directed TCI to treat the $1,000 customer contribution as revenue rather than a credit to the capital cost of the SIP. The Commission stated that it planned to examine TCI's application of the Commission's direction during the review of the 31 March 2005 SIP tracking report.

30. The Commission has examined TCI's methodology for crediting the customer contribution to revenue and finds that it has correctly applied the Commission's direction in Decision 2004-76.

SIP roll-out

31. Pursuant to Decision 2003-64, the Commission approved a roll-out period of 2003 to 2006. The Commission notes TCI's statement that, due to the time and resources required to provide telephone service to unserved communities, SIP projects started in 2006 would span two years, and therefore would not be completed until 2007. The Commission finds that this revised schedule is acceptable. Accordingly, the Commission **approves** TCI's revised roll-out period.

32. The Commission recognizes that the prolonged labour stoppage that started in July 2005 may have an effect on the roll-out of TCI's SIP. Notwithstanding this labour stoppage, the Commission expects that the vast majority of the SIP projects not yet completed should be completed by the end of 2006, and that the SIP should be completed by 2007.

Secretary General