



# Unlocking Growth: Liberalizing Canada's Telecom Sector for Dynamic Competition

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Ted Woodhead

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# Introduction

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Recent essays have considered the evolution of Canadian telecommunications policy, including the so-called “fourth player” policy and the inherent flaws of its assumptions when the country’s market structure is compared to peer jurisdictions.<sup>1</sup> The overarching theme of the series has been that Canada’s current policy framework is wrongly rooted in a conception of static competition rather than a more dynamic understanding of how markets work in telecommunications.

This paper aims to build off this previous analysis by setting out the key parameters of an alternative policy framework that aims to cultivate sustainable, market-based competition in the telecommunications sector. In particular, it outlines amendments to the foreign ownership restrictions under the Telecommunications Act as well as accompanying changes to spectrum and wholesale policies that would need to be part of an overall agenda to open up the industry.

The goal of such a shift in telecommunications policy would be to achieve a greater balance between the objectives of investment, connectivity, and consumer pricing by enabling the market to determine the best outcomes.

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<sup>1</sup> Sean Speer and Taylor Jackson, “DeepDive: It’s time for the government to trust the market and stop micromanaging Canada’s telecom sector,” *The Hub*, October 1, 2024, <https://thehub.ca/2024/10/01/deepdive-its-time-for-the-government-to-trust-the-market-and-stop-micromanaging-canadas-telecoms-sector/>; Robert D. Atkinson, “DeepDive: Why Canada doesn’t need another broadband provider,” *The Hub*, October 15, 2024, <https://thehub.ca/2024/10/15/robert-d-atkinson-why-canada-doesnt-need-another-broadband-provider/>.

# A Brief History of Telecoms Policy

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Canadian telecommunications policy has vacillated between a stronger and weaker role for market forces over the past few decades. Prior to the early 1990s, the industry—particularly the services segment—was viewed as a monopoly and regulated accordingly.

That remained the case until some academic and industry voices began to question the underlying assumption of monopoly and the regulatory monolith that had grown and governed it for the better part of a century.<sup>2</sup>

This new thinking in Canada partly found its way into the 1993 Telecommunications Act, which notably included a greater reliance on market forces and a forbearance from regulation power which the Canadian Radio-television and Telecommunications Commission (CRTC) was tasked with overseeing.

The passage of the new Act followed a number of court rulings which brought about hope among pro-market proponents that there would be significant change to how telecommunications was regulated in Canada.

Without burdening readers with the numerous decisions and the considerable volume of work that went into comprehensively examining each of the services offered by the telecommunications carriers, the years following the Act's proclamation were spent opening the various markets within the telecommunications industry to competitive entry. The decision to rely on market forces to protect the interests of users eventually led to the deregulation of long-distance, local landline and wireless services.

The results were transformative. Unshackled from the most onerous aspects of regulation and facing new competitors — both traditional and unanticipated technological disruptors — prices dropped, and new and innovative services were offered. Legacy services with few customers could be de-standardized without time-consuming and lengthy reviews by the CRTC. To many who viewed these developments as positive, a new day had dawned. A new philosophy of market-based competition was now reflected in telecommunications policy.

Yet this progress eventually stalled early in this century. Successive governments and the CRTC gradually shifted back to a top-down policy approach.

In particular, as has been discussed elsewhere in the series, beginning in 2008, Canadian governments have enacted a series of policy interventions, including mandating wholesale requirements on the existing network operators to allow resale competitors to emerge, in the name of inducing more competitors in the marketplace. In technical terms, the "fourth-player" policy has chosen to preference a model of competition involving more service competitors over facilities-based competition in which competitors are investing in their own networks.

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<sup>2</sup> "Explainer: A brief history of foreign ownership restrictions in Canada's telecom sector," *The Hub*, October 18, 2024, <https://thehub.ca/2024/10/18/explainer-why-is-canadas-telecoms-market-so-closed-to-competition/>.

Previous essays in the series have documented the conceptual and empirical problems with this approach, including the disincentives for network investment and the long-run challenge to the government's connectivity goals. These are the facts that animate and recommend a new approach to the regulation of Canada's telecommunications industry. But it is not new per se. It is ultimately about restarting the stalled trend towards deregulation in the name of enabling sustainable, market-based competition.

While space does not permit a full review of recommendations for reform of all of the arcane and labyrinthine rules, requirements and constraints imposed on the telecommunications sector, what follows are a select number of policy changes that would need to be part of an overall agenda to support greater market-based competition.

In the author's view, these changes would support further investment in the digital infrastructure and contribute to significantly addressing Canada's lagging productivity, as well as support increased investment in information and communication technologies that are key to restoring Canada's labour productivity and overall standard of living.

# Policy #1: Remove Remaining Foreign Ownership Restrictions, Subject to Minimal Constraints

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The Telecommunications Act stipulates that firms are required to be owned and controlled by Canadians. After 2012, an exception exists for telecommunications carriers whose annual revenue from the provision of telecommunications services does not exceed 10 percent of the total revenues from the provision of all telecommunications services in Canada. But larger firms (with more than 10 percent market share) are subject to a legal mandate of Canadian ownership of 80 percent of a company's voting shares. As well, Canadians must hold 80 percent of director positions and there must be no indirect control by non-Canadians. If the corporate investor is a subsidiary, the parent company must be incorporated in Canada, and Canadians must hold a minimum of 66.6 percent of the parent company's voting shares.

If the government wants to shift Canada's telecommunications policy in a more market-based direction, the first step is liberalizing these foreign ownership restrictions. In practice, this means removing the 10 percent revenue limit on ownership through acquisition or otherwise to allow greater foreign ownership participation. In addition, it should lower the requirement for Canadian participation in the voting interest of the carrier. It could ostensibly be lowered to less than half or eliminated altogether. The board requirement could be preserved or adjusted accordingly.

It is beyond the scope of this analysis, but the government could consider whether such legislative changes are limited to the Telecommunications Act or extend to the Broadcasting Act, given that some telecommunication firms are captured under both statutes.

It is important to emphasize that liberalizing the foreign ownership restrictions under the Telecommunications Act (or the Broadcasting Act) would not change the fact that any major transaction involving a Canadian company would be subject to the net benefit test and national security provisions under the Investment Canada Act.

But otherwise the telecommunications market would be fully open to foreign investment and foreign competition. This would expand the pool of capital for Canadian companies and create competitive pressure to invest in their networks and provide high-quality and affordable services to the customer. The key point, though, is such competition would be driven by market forces rather than the artificial and counterproductive form of competition that has been marked by the fourth-player policy.



# Policy #2: The Need for a New Incentive-based Approach to Facilities-based competition

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It's not enough, however, to simply liberalize the foreign ownership restrictions under the Act. Opening up the market requires that policymakers also de-regulate the auxiliary policies of the fourth-player policy. One of the biggest is the wholesale regime. In simple terms, this refers to government policy that oversees the wholesale access to incumbents' networks to third-party companies who then use the access to sell services directly to companies.

This approach—what is sometimes referred to as “wholesale-based competition”—stands in contrast to facilities-based competition which involves companies competing based in part on the quality and reach of their own network infrastructure.

Canadian policy has required large incumbent telephone and cable companies to provide wholesale access to their networks for more than 20 years. But in recent years, we have seen several policy decisions that have expanded the regime in the name of adding more market players without adequate diligence paid to the long-run effects on capital investment.

In any case, a policy framework that relies heavily on whole-based competition—particularly with mandated wholesale rates—is by definition not market-based competition. It is a form of competition that exists based on government's regulatory intervention.

Successive decisions have expanded the government's wholesale policy and made it increasingly more prescriptive. A good example is the CRTC's 2021 decision with regards to Mobile Virtual Network Operators (MVNOs) which required incumbent wireless operators to provide wholesale access to regional competitors at mandated rates that are below market value.

The consequence of this policy approach is to disincentivize investment into network infrastructure. It is a key reason why many jurisdictions have prioritized facilities-based competition instead of wholesale mandates in the wireless sector.

Furthermore, if, as this series has explored in previous papers, a policy objective is to promote sustainable competition, wholesale regimes like the MVNO fail to provide any incentives to keep resellers in the market without continuous regulatory intervention.<sup>3</sup>

Therefore, as part of an overall plan to shift Canada's telecommunications policy framework in a more market-driven direction, policymakers should be more cautious in the use of wholesale policy and, when implemented, rely on commercial terms rather than government diktats.

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<sup>3</sup> Speer and Jackson, “DeepDive.”

# Policy #3: On a Level Playing Field, Radio Spectrum Should be Allocated in Free and Open Auctions

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Radio spectrum in Canada for commercial mobile wireless use is typically awarded for license terms of 10 or 20 years by way of auction. This system of allocating spectrum has generally operated efficiently.

As part of the fourth-player policy, however, successive spectrum auctions have been subject to different forms of “set asides” or “caps” whereby the government has reserved certain amounts of spectrum in each geographical tier for acquisition only by a new entrant.

This has led to a constrained pool of available spectrum for other bidders who are prohibited from bidding on set-aside spectrum, which in turn has led to higher spectrum acquisition costs. This policy has caused Canada to be cited as an “extreme outlier” in terms of spectrum acquisition cost in a number of international studies.<sup>4</sup>

Conversely, for those bidders designated as “new entrants” they are able to acquire the reserved spectrum at or near the reserve cost. Given finite capital budgets, this likely had the perverse effect of reducing the areas where spectrum was deployed for the benefit of Canadians. Where its impact would be most acute would be in rural and remote areas where deployment costs are higher and return on investment is lower than other more densely populated and profitable urban areas. Rural and remote areas are coincidentally the areas where enhanced digital connectivity infrastructure would be most beneficial.

The beneficiaries of the subsidized spectrum have in recent memory primarily, if not entirely, been cable companies and conglomerates who were late to roll out wireless services and whose balance sheets could well support participation in the wireless industry without subsidy.

Moving to a market-based model for spectrum auctions (i.e. no set asides or caps) could alone add hundreds of millions of dollars of investment capital for the expansion of networks and deployment of enhanced wireless technologies by the incumbent wireless providers. A proper spectrum auction design would therefore eliminate set-aside auctions entirely. Spectrum auctions should function on market terms between the buyers and the seller.

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<sup>4</sup> Rupert Wood, “Falling Behind: Comparing 5G Spectrum Policies in Canada and OECD Countries,” *Analysys Mason*, August 2, 2021, [https://www.analysismason.com/contentassets/3142cca88f924253be79605a6703503a/analysys\\_mason\\_5g\\_spectrum\\_canada\\_nov2021\\_rdnt0.pdf](https://www.analysismason.com/contentassets/3142cca88f924253be79605a6703503a/analysys_mason_5g_spectrum_canada_nov2021_rdnt0.pdf).



# Key Takeaways

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As a recent series has documented, the fourth-player policy has distorted the market and produced underwhelming outcomes. The problem lies in its assumption that the government can intervene in the market in order to produce precisely the right number of players. A far better approach would be to resume the process of deregulation that started in the early 1990s. It would leave it to market forces to determine such an outcome. Similarly market-based competition would enable a dynamic process of balancing key objectives such as capital investment, access to new technologies, and competitive consumer pricing.

Realizing this vision of sustainable, market-based competition will require a new telecommunications policy framework. The first step is to liberalize the foreign ownership restrictions under the Telecommunications Act. But it cannot stop there. It will also require adjustments to spectrum and wholesale policies such that the principle of market-driven competition is expressed throughout the policy framework.

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**Ted Woodhead** is a Telecom Consultant and Executive based in Ottawa with over 30 years experience in regulatory matters with the CRTC, TELUS and Rogers.

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