ONTARIO ENERGY BOARD

EB-2013-0234

IN THE MATTER OF the Ontario Energy Board Act, 1998, S.O. 1998, c.15 (Schedule B);

AND IN THE MATTER OF an application by Toronto Hydro-Electric System Limited for an order pursuant to section 29 of the Ontario Energy Board Act, 1998.

Interrogatory Responses to

Energy Probe Research Foundation

Dr. Marc Van Audenrode
Analysis Group

April 2, 2014

4-Energy Probe-1

Reference: Analysis Group Report (Dr. Van Audenrode) Page 20, Para 54

Interrogatories:

a) *The second sentence in paragraph 54 begins: "Hence, the relevant product market comprises access to THESL's network of utility power and …" Please confirm that the reference to THESL's network is to its network of utility power poles.*

This is a typo, the second sentence in paragraph 54 should read: "Hence, the relevant product market comprises access to THESL's network of utility **poles** and …"

b) *Please confirm that under Dr. Van Audenrode's approach to the hypothetical monopolist test ("HMT"), the starting point for product market definition is poles of the type currently owned and/or controlled by THESL, rather than THESL's poles per se.*

Dr. Van Audenrode's conclusion from the Hypothetical Monopolist Test (HMT) is that THESL would find it highly profitable to impose, and sustain, a 5% increase in the rate of wireless pole attachments to its poles. Hence, the product market does not extend to similar types of poles owned and/or controlled by parties other than THESL.[1]

c) *Please also confirm that the HMT, as proposed by Dr. Van Audenrode, then considers whether a hypothetical monopolist over such poles would impose a significant and non-transitory increase in the attachment price for all attachers (i.e., an across-the-board increase).*

The HMT in Dr. Van Audenrode's report considered whether THESL would find it profitable to impose, and sustain, a significant and non-transitory increase in the rate for (all) wireless pole attachments for its network of utility poles.[2]

d) *Suppose it were known that, based on the proper statistical evidence, the demand for pole attachment was price-inelastic. Would that knowledge be sufficient to conclude that the relevant product market consisted only of poles?*

No. Price-inelastic demand indicates that the hypothetical monopolist would find it profitable to impose a SSNIP. However, the HMT framework additionally requires that the hypothetical monopolist can sustain such a price increase, which requires information about barriers to entry and the supply response within the market.

[1] "In particular, if a single supplier of the entire supply of the firm's product could profitably raise its price by a small but significant amount, the product market definition should not extend beyond that product." (Trebilock, M., R.A. Winter, P. Collins and E.M. Iacobucci (2002): *The Law and Economics of Canadian Competition Policy*, (University of Toronto Press, Toronto), p. 71).

[2] The focal product in Dr. Van Audenrode's analysis is a wireless pole attachment.

e) *Is Dr. Van Audenrode's application of the HMT premised on the inability of the hypothetical monopolist to charge different attachment rates to different classes of attachers?*

No. Dr. Van Audenrode's report considered whether THESL would find it profitable to impose, and sustain, a SSNIP for *all* wireless pole attachment. Submarkets may exist if THESL can - and is allowed to - discriminate by type of wireless attachment and can impose and sustain a SSNIP in submarkets. There is however insufficient evidence to evaluate THESL's ability to impose a SSNIP in submarkets.

f) *If the answer to e) above is no, does Dr. Van Audenrode believe that the ability to price-discriminate leads, in principle, to the delineation of separate relevant markets by class of attacher? Further, would such delineation tend to narrow the size of each such market or broaden it, as compared with the relevant market established on the basis on non-discrimination?*

The ability to discriminate by class of wireless pole attachment could results in distinct relevant product markets.[3] It is Dr. Van Audenrode's understanding that different wireless technologies have similar technical considerations in regard to siting alternatives.

g) *Instead of starting the delineation with a single product (i.e., poles) and asking whether that market should be expanded, could the HMT start with the largest possible set of products and then ask whether that market should be smaller by applying the "smallest market principle"? If the HMT is properly applied, would Dr. Van Audenrode expect that the resulting market would be the same regardless of which route were taken?*

It is common practice for the starting point in the market definition exercise to be the product that raises competition concerns, i.e. the provision of access to THESL's network of poles.[4]

h) *Would Dr. Van Audenrode agree that the "broad market" to which Dr. Church refers is a product market?*

The "broad market" to which Dr. Church refers to is not a relevant antitrust product market in which THESL supplies pole access for wireless attachments.[5]

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[3] "An additional pitfall [of market definition] is related to the phrase '*the* relevant market.' In merger cases or, for example, abuse-of-dominance cases, it is often misleading to think of the relevant market as being unique. […] [T]he market must be well-defined in the sense of including all sufficiently close substitutes for the product in question, but it need no encompass all or most of the goods and services produced by the respondent." (Trebilock, M., R.A. Winter, P. Collins and E.M. Iacobucci (2002): *The Law and Economics of Canadian Competition Policy*, (University of Toronto Press, Toronto), p. 77).

[4] "[M]arket definition is not an end in itself, but only an intermediate step in the analysis of competitive constraints. For market definition to be informative, the starting point must always be the product in relation to which the competition concern arises. […] The starting point for a relevant market is sometimes called the focal or labeling product (and geographic area)." (Niels, G., H. Jenkins and J. Kavanagh, *Economics for Competition Lawyers*, (Oxford: Oxford University Press), 2011, p. 47).

i) If the answer to h) above is yes, would he agree that any smaller subset of that broad market could also be a product market?

A relevant product market is defined as the smallest set of products for which a hypothetical monopolist would impose, and sustain, a small but significant, non-transitory increase in price (SSNIP). A relevant market is no bigger than necessary to satisfy this test.

j) In Dr. Van Audenrode's opinion, has Dr. Church tested his stated "broad market" against the smallest market principle?

Dr. Church did consider smaller product markets. He inferred however, based on the availability of alternative inputs and alternative sites, that "the elasticity of substitution between different inputs is likely to be high" and that "pole access for wireless attachments is not likely a relevant input market in its own right, but an input that is part of a broader relevant market."[6] He implicitly concludes that, in his view, THESL could not impose and sustain a SSNIP of 5% in a smaller product market consisting of only the provision of pole access for wireless attachments.

k) In Dr. Van Audenrode's opinion, has Dr. Church performed the HMT correctly or incorrectly?

There is no fundamental disagreement between Dr. Van Audenrode and Dr. Church on the application of the HMT framework. Dr. Church inferred from the availability of alternative inputs and alternative sites, that the elasticity of input substitution is likely high and concluded that the relevant market is broader than the provision of pole access for wireless attachments. Dr. Van Audenrode considered direct evidence of economic substitutability from buyers of pole access for wireless attachments in Toronto and other jurisdictions,[7] and concluded that the evidence is inconsistent with a highly elastic demand for wireless pole attachments as purported by Dr. Church.[8] THESL would find it highly profitable to impose a 5% increase in the rate of wireless pole attachments to its poles and the relevant upstream market containing pole access for wireless attachments is narrow, restricted to THESL/THESI's network of poles.[9]

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[5] "[T]here is a broad upstream "input market", and not a market defined by monopoly control over the input provision of pole access for wireless attachments." (Church Report, ¶17).

[6] *Church Report*, ¶139 and ¶143.

[7] Some of this evidence was not available to Dr. Church at the time of the writing of his expert report.

[8] The strategies and behavior of buyers are reliable indicators of the extent of economic substitutability among products and whether buyers would likely switch to other products in response to a SSNIP (*Merger Enforcement Guidelines*, ¶4.13).

[9] *Van Audenrode Report*, ¶74-77.

4-Energy Probe-2

Reference: Analysis Group Report (Dr. Van Audenrode) Page 23, Para 72

Preamble: Dr. Van Audenrode indicates that the regulated cost-based pole access rate is an appropriate proxy for the pole access rate that would allow firms to recover their long-run average cost of providing access.

Interrogatories:

a) *In Dr. Van Audenrode's opinion, was the attachment rate of $22.35 per pole per year set by the Board a good proxy for the attachment rate that would prevail at that time if the market for attachments were workably competitive?*

Since rates are regulated, neither competitive pole attachment rates nor current market-based pole attachment rates are available to implement the Hypothetical Monopolist Test (HMT). Pricing in competitive markets is such that firms recover their long-run average cost.[10] After reviewing pole attachment costs, the Board in its *CCTA Decision* has set the regulated rate for pole attachments at $22.35. Other jurisdictions have, using different methodologies, set regulated pole attachment rates similarly around $20.[11] For the purposes of the HMT and in the absence of contradicting evidence, the regulated rate is a reasonable proxy for the rate that would prevail in competitive markets.[12]

b) *Considering that, under the current regulatory framework, attachers pay the initial and continuing costs of attachment including costs that THESL must incur to accommodate those attachments, what are the remaining costs that THESL should be allowed to recover through the attachment rate?*

Dr. Van Audenrode has not reviewed any cost allocation methodologies for setting regulated pole attachment rates.

c) *From an economic perspective, should those remaining costs recovered in a regulated attachment rate cover any of THESL's costs that it would incur even without the attachment.*

A network of utility poles exhibits economies of scope. Joint production of electricity distribution and telecommunications is less costly than producing each product individually.[13] Hence, rates set such that each product recovers its direct, incremental cost of production are

[10] "The ability to profitably raise prices over competitive levels implies the ability to raise prices above average cost, a level that reflects the requirement of firms to break even and is a useful definition of a competitive market even when firms are not perfectly competitive (*Church Report*, footnote 35).
[11] *Van Audenrode Report*, Table C-1.
[12] Dr. Van Audenrode's conclusions related to market delineation and THESL's market power would not be affected if instead one were to implement the HMT using THESL's estimates of its direct and indirect costs associated with pole attachments (*Van Audenrode Report*, Appendix D - Confidential Material).
[13] *Van Audenrode Report*, ¶27.

insufficient to cover total cost. Common costs need to be shared following some methodology.[14]

[14] In its *CCTA Decision*, the Board recognized that a case can be made for different cost sharing methodologies, but preferred an equal sharing methodology (*CCTA Decision*, p. 7).

4-Energy Probe-3

Reference: Analysis Group Report (Dr. Van Audenrode) Page 18, Para 48.

Preamble: At para 48, Dr. Van Audenrode discusses the approach of the Canadian Competition Bureau to defining an essential facility. At the end of para 48, Dr. Van Audenrode's footnote 64 refers to his footnote 33, which itself references the Telecom Decision CRTC 2008-17. At para 11 of that decision, the CRTC refers to a submission by the Competition Bureau.

Interrogatories:

a) *Is it Dr. Van Audenrode's view that the Bureau was suggesting how regulatory policy should approach the question of essential facilities or was the Bureau stating a position on essential facilities under competition policy?*

In its *Telecom Public Notice CRTC 2006-14*, the CRTC invited parties to comment on whether it should adopt the definition of essential facility proposed in the Competition Bureau's draft *Information Bulletin on the Abuse of Dominance Provisions as Applied to the Telecommunications Industry*. In response, the Bureau proposed a conceptual framework, based on competition principles, for wholesale service regulation under the Telecommunications Act. In the Bureau's view, "the economic principles underlying the approach to essential facilities in the Bureau's draft *Information Bulletin on the Abuse of Dominance Provisions as Applied to the Telecommunications Industry* […] can be applied, with appropriate modification, in the regulatory context to determine whether a particular wholesale facility, function or service is 'essential'."

b) *In Dr. Van Audenrode's view, is there an essential facilities doctrine in Canadian competition policy?*

An "essential facilities doctrine" does not exist in Canada. The Commissioner of Competition can apply to the Competition Tribunal under Sections 78 and 79 of the Competition Act (Abuse of Dominant Position) to challenge an anti-competitive act such as the "pre−emption of scarce facilities or resources required by a competitor for the operation of a business, with the object

of withholding the facilities or resources from a market."[15] There exists limited jurisprudence as abuse of dominance cases are rarely contested in Canada.[16]

c) *If the answer to b) is yes, please provide a citation to the relevant competition statute or guideline of the Competition Bureau.*

See answer to b) provided above.

[15] *Competition Act*, s. 78 (1) e.

[16] The most closely related cases that explicitly considered denial of a facility are *Interac* and *CREA*, both cases settled by consent order. (*Canada (Director of Investigation and Research) v. Bank of Montreal et al.* [1996], 68 C.P.R. (3d) 527 (Comp. Trib.); *The Commissioner of Competition v. The Canadian Real Estate Association*, CT-2010-002). In *CREA*, the Bureau argued that the Canadian MLS system "has become a key input to the provision of residential real estate brokerage services" and that no reasonable substitutes are available (*CREA*, Notice of Application). In addition to the two cases mentioned, Dr. Church considers *TREB* an essential facilities case. (Expert Report of Jeffrey Church, July 27, 2012, *The Commissioner of Competition v. The Toronto Real Estate Board*, 2013 Comp. Trib. 9; rev 2014 FCA 2. On February 3, 2014, the Federal Court of Appeal granted an appeal by the Commissioner of Competition, sending the case against the Toronto Real Estate Board back to the Competition Tribunal for reconsideration).