

1 **Wirebury Connections Inc. INTERROGATORY #23**

2
3 **Interrogatory**

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5 In its evidence, Networks refers to destructive competition from the early 1900s as a
6 reason for the Board to avoid using overlap in the 2003 market.

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8 Reference: Appendix A, p.2, L4

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10 Please define destructive competition and describe the number and severity of the
11 occurrences referred to in Networks' evidence and explain how these occurrences would
12 be relevant in today's market.

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15 **Response**

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17 Destructive competition would be described as follows. The incumbent utility, which
18 enjoys a legally sanctioned monopoly and has capitalized in a business environment
19 without risk, faces competition from a new entrant, without the new entrant having to
20 provide compensation to the incumbent. At the same time, the new entrant is able to build
21 the efficiency of its own operation without the burden of providing financial
22 compensation to the incumbent distributor. In addition, the new entrant, in the absence of
23 the burden of paying any entrant costs or stranded debt obligations to the incumbent, has
24 the advantage of competitive rate pricing. As a result, the existing customers of the
25 incumbent migrate to the new market entrant. The new entrant thereby is able to weaken
26 the incumbent by reducing its revenue without the incumbent being able to address its
27 fixed costs, with the resulting financial demise of the incumbent. (See Networks' Exhibit
28 J8-11-4 and the Exhibit' attachments.)

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30 The scenario above existed at the beginning of the 20th century and has the potential of
31 having parallels to the current situation where applicants are pursuing service territory
32 expansion through licence amendment applications. This destructive competition is
33 expressed in three forms: 1) the desire for quasi-annexation of territory without
34 compensation; 2) competition in overlapping service territory; and 3) new embedded
35 service territory (whether overlapping or through quasi-annexation).

36
37 In the early history of Ontario's electric industry, the Municipal Act had been amended in
38 1899 in order to prevent destructive competition and protect existing electric utility
39 bonds. (S.O. 1899, c. 26, S. 35, ss. 4). This amendment extended to electricity
40 distribution the existing legislative preclusion on municipalities from establishing their
41 gas and water utilities where they had granted a franchise for the same service. If a
42 municipality wanted to establish its own utility it had to buy out the franchise operator at

1 an arbitrated price. However, with the passage of the Power Commission Act, 1906,
2 municipal electric commissions were exempted from the strictures of the Municipal Act
3 (S.O., 1906, c. 15, S. 10), and in the result weakened the business case for the franchise
4 electric distribution utilities. In the most notorious case, the City of Toronto established
5 Toronto Hydro by by-law in 1907 and did so in direct competition with the already City-
6 sanctioned franchise of Toronto Electric Light Company. The municipal commission and
7 the franchise duplicated their systems and competed for the same customers at the
8 expense of the franchise until the situation was ended in a negotiated settlement near the
9 end of the franchise term in 1921. In other municipalities, the franchises were either not
10 renewed or the municipality bought out the franchise.

11
12 The historical example demonstrates that the business risk created by competition for this
13 industry of high fixed cost caused disruption for this otherwise stable business, affecting
14 the financial viability of the utility under threat. It also resulted in no costs for the new
15 market entrant, arbitrated or negotiated.

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