Regulations Defining "Advertising Revenues"
(SOR/98-447)

REGULATORY IMPACT ANALYSIS STATEMENT[i]
(*This statement is not part of the Regulations.*)

Description

Recent revisions to the *Copyright Act* provide that the Copyright Board is responsible for approving tariffs for the performance in public or the communication to the public by telecommunication of sound recordings of musical works (commonly referred to as the "neighbouring rights tariff").

Subsection 68.1(1)*(a)*(i) of the *Act* sets at $100 the amount of royalties that "wireless transmission systems" shall pay on their first 1.25 million dollars of annual "advertising revenues". Sub-section 68.1(3) of the *Act* gives the Board the power to define, by Regulations, the term "advertising revenues", while subsection 68.1(5) gives the Governor in Council the power to define, by Regulations, the term wireless transmission system".

By describing the meaning of the term "advertising revenues", these Regulations define the rate base that will be used to determine which part of a wireless transmission system's revenues benefits from the $100 special royalty rate.

Alternatives

The alternative to let the Board interpret the meaning of the term "advertising revenues" in the course of approving the relevant tariffs was considered. However, given the importance of this term in the context of neighbouring rights, the Board considers it preferable to define it by Regulations.

Benefits and Costs

These Regulations allow to determine clearly and precisely that part of a wireless transmission system's revenues which will benefit from the $100 special royalty rate intended to reduce the financial impact on the radio broadcasting industry of the introduction of a new tariff. There will be no associated costs to the broadcasting industry, to the recording industry or to Government due to these Regulations.

Consultation

On May 7, 1997, the Board asked comments on the appropriateness of using the definition of "gross income" found in the tariff already applicable to radio stations for the telecommunication of musical works. On September 24, 1997, the Board circulated a draft definition on which it asked them to comment. On February 6, 1998, the Board addressed a number of questions aimed at clarifying the comments the Board had received from them.

The following organizations were consulted: Alliance of Canadian Cinema, Television Radio Artists (ACTRA), American Federation of Musicians of the United States and Canada (AFM), Association canadienne de la radio et de la télévision de langue française (ACRTF), Association québécoise de l'industrie du disque, du spectacle et de la vidéo (ADISQ), Canadian Association of Broadcasters (CAB), Canadian Independent Record Production Association (CIRPA), Canadian Recording Industry Association (CRIA), Union des artistes (UDA), Society of Composers, Authors and Music Publishers of Canada (SOCAN), Artists'

Rights Coalition (ARC), Société de gestion des droits des artistes-musiciens (SOGEDAM) and Neighbouring Rights Collective of Canada (NRCC). Comments were received from all these organizations. The following issues were addressed, among others.

Narrow vs Broad Definition

Several organizations asked that the definition be narrowed or broadened in a number of ways. The Board has opted for a general definition, which is more responsive to market changes. The Regulations will be further refined later on if they prove difficult to interpret.

What Are Advertising Revenues?

In their comments, the organizations took widely divergent views of what are advertising revenues and what are not.

Thus, CRIA asked for the inclusion of advertising revenues from allied or subsidiary businesses. CIRPA asked that the definition cover all forms of revenue and income emanating from a system's business while also allowing the inclusion of new forms of revenue not currently in existence without any need to change the Regulations. AFM asked that the rate base include revenues derived from the production of commercial announcements as well as revenues derived from renting or leasing of facilities or personnel for such productions.

By contrast, CAB asked that the definition be articulated around the notion of "sale of airtime for broadcasting" rather than "value received to advertise". According to CAB, this would result in the inclusion of revenues from new musical programming services that are ancillary to the main broadcasting service, and the exclusion of revenues received for services other than airtime. CAB specifically asked the exclusion from the rate base of *(a)* revenues from datacasting, *(b)* production revenues, *(c)* revenues for leasing personnel or space for the purposes of production, *(d)* the value of goods received from which the system does not derive a benefit (e.g. prizes), *(e)* contra arrangements that are not of real value to the system, *(f)* goods that the station would not have otherwise purchased, and *(g)* airtime that is exchanged for the promotion of a system or its programming in another medium.

The Board intends that all forms of advertising revenues be included in the rate base. Given the ongoing evolution in this market, it seems preferable to adopt a general definition and see how the market develops in the long run.

The Board also intends to exclude from the rate base revenues that are clearly not advertising revenues. The Regulations achieve this through the reference, in section 1, to "compensations ... received ... to advertise goods, services, activities or events, for broadcasting public interest messages or for any sponsorship". This excludes from the rate base *(a)* subscription revenues, *(b)* production revenues and, *(c)* revenues for leasing personnel or space for the purposes of production.

As to compensations in kind, paragraph 2*(a)*, which provide that goods and services are valued at their fair market value, is sufficient to deal fairly with all the other concerns raised in this respect.

Section 1 and paragraph 2*(a)* of the Regulations, when read together, also allow a system to exclude from the rate base the fair market value of the production services provided under a "key in hands" contract pursuant to which the system provides both advertising and production services.

Agency Commissions and Discounts

Some organizations asked that agency commissions be included in the rate base. Others asked that they be capped or expressly limited to "fair market value" commissions, so as to reduce the risk of collusion between persons not dealing at arms length. The Board considered the imposition of a ceiling. However, nothing to date in the experience with similar tariffs leads to believe that this provision might result in abuses. The issue will be revisited if necessary.

One organization asked that discounts be expressly excluded from the rate base. The Regulations already achieve this, since discounts are never "received" by the system.

Bad Debts

NRCC asked that bad debts be included in the rate base, while CAB asked that they be excluded explicitly. The Board is of the view that bad debts should not be part of the rate base. Again, the Regulations already achieve this, since bad debts are never "received" by the system.

System vs Service

CAB asked that the definition be articulated around the concept of service rather than system. The Board cannot circumvent the *Act* by articulating the Regulations around a notion other than that which is used in the legislation.

Ambit of Paragraph 2*(b)*

The application of the equivalent provision in SOCAN's Tariff 1.A is limited to groups of stations "which do not constitute a permanent network". Some organizations maintained that this proviso achieves several purposes. It ensures that broadcasting stations pay their share of the tariff and avoids double counting. It ensures that networks are not used to shelter advertising revenues from the rate base. Finally, it prevents revenue splitting that could result in revenue being sheltered under the $100 payment that should pay at the tariff rate.

In the Board's view, there is no need to limit the application of the provision to non-permanent networks. Where any network does not have a separate licence, the network's revenues should be allocated among all the member stations using generally accepted accounting principles. If that proved not to be the fact in practice, the Board intends to amend the Regulations or to allow for the adoption of a network tariff in order to correct the situation.

Interpretation Clause

Some organizations asked that an interpretation clause similar to that found in SOCAN's Tariff 1.A be included in the Regulations so as to specifically exclude from the rate base:

(a) the recovery of any amount paid to obtain the exclusive broadcast rights, if the system can establish that it was also paid normal advertising revenues;

(b) income accruing from investments, rents or any other business unrelated to the system's broadcasting activities;

(c) amounts received for the production of a program that is commissioned by someone other than the system and which becomes the property of that person.

These organizations maintained that the provision would help clarify the Regulations and avoid disagreements. SOGEDAM took the opposite view, stating that such a provision should not be included in the Regulations, and that it was not needed given the wording of sections 1 and 2.

An interpretation clause of this nature is not necessary: such revenues are clearly not "advertising revenues", and the proposed Regulations are not intended to include them in the tariff base.

Audit Clause

NRCC asked for the inclusion of an audit clause in the Regulations, arguing that the tariff's audit clause would not allow a collective to verify whether any exclusion of revenues from the regulatory rate base was legitimate. The Board disagrees; the audit clause that will eventually be included in the tariff will provide collectives with sufficient means to verify whether the exclusion of any revenues from the rate base is legitimate.

Comments received after pre-publication

Comments were received from the Canadian Association of Broadcasters on the regulations pre-published in the *Canada Gazette*, Part I, on July 4, 1998. The comments reiterated some of the arguments already made by the Association during the earlier consultation process. The Board decided not to reflect those comments for the reasons it had given earlier.

Compliance and Enforcement

The Board will apply these Regulations defining "advertising revenues" in the context of its tariff-approval procedure. Enforcement mechanisms are not required.

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[i] Published in the *Canada Gazette* Part II on September 16, 1998.