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6 April 2006

Ms. Diane Rhéaume  
Secretary General  
Canadian Radio-television and  
Telecommunications Commission  
Gatineau, Quebec  
K1A 0N2

Dear Ms. Rhéaume:

Re: Application 2005-1516-6 (the "Application") by YTV Canada, Inc. to renew the licence of the national English language specialty programming undertaking known as YTV, expiring 31 August 2006. Broadcasting Notice of Public Hearing CRTC 2006-3, Item 7.

**A) Introduction**

1. This is the intervention of the Directors Guild of Canada (DGC), the Writers Guild of Canada (WGC), and the Alliance of Canadian Cinema, Television & Radio Artists (ACTRA) (the Unions) concerning the Application. The DGC is a national labour organisation that represents key creative and logistical personnel in the film and television industries. Its membership includes over 3,800 individuals drawn from 47 different craft and occupational categories covering all areas of direction, production, editing and design of film and television programming in Canada. The WGC is a national association representing more than 1,800 writers working in film, television, radio, and multimedia production in Canada. Members of the Guild are professionals who write dramatic TV series, feature films, MOWs, documentaries, animation, comedy and variety series, children's and educational programming, radio drama, as well as digital productions for the Internet and cell phones. And, the Alliance of Canadian Cinema, Television and Radio Artists (ACTRA) is a national organization of professional performers working in the English-language recorded media, representing the interests of 21,000 members across Canada.
2. The Unions acknowledge the contributions that YTV and its owner Corus have made during the last licence term. As part of the renewal process, YTV has made a variety of proposals, the majority of which the Unions will not address.
3. However, YTV proposes to maintain its current Canadian Programming Expenditures (CPE) percentage at 35% of the prior year's revenue, notwithstanding the Commission's policy laid out in Broadcasting Public Notice CRTC 2004-2. The Unions oppose this status quo



situation and recommend that the CPE percentage be increased to 41% of revenue in keeping with established Commission policy. The Unions also recommend the implementation of safeguards relating to the relationship between YTV and independent producers, both with respect to expenditures and exhibition. Finally, the Unions recommend that the Commission look more closely at the issue of management fees. The Unions wish to appear at the public hearing relating to this matter.

**B) *Expenditures on Canadian programming***

4. In *Broadcasting Public Notice CRTC 2004-2*, the Commission laid out the CPE regime for the renewals of 22 specialty services and established a going forward regulatory framework. In deciding to focus on increasing the amount that those services spend on Canadian content rather than increasing the overall amount of such programming, the Commission stated that it

...is satisfied that this approach is balanced and fair to all parties, taking into account the past financial performance of each service, and its projections going forward.

5. This approach has been applied in a number of specialty service licence renewals since that time. For example, last summer the Commission renewed the specialty service licence of Astral's Canal D (Broadcasting Decision CRTC 2005-441). In so doing, the Commission stated the following:

In Public Notice 2004-2, the Commission set out a graduated approach to Canadian programming expenditure requirements that the specialty services referred to therein would be required to meet during renewed licence terms. This approach was fully addressed by the applicant and interveners in this proceeding, and the Commission considers it appropriate to adopt it in this case. The Commission is satisfied that this approach is balanced and fair in that it takes into account a service's past financial performance and future projections, and relates its Canadian programming expenditure requirements directly to its profitability. The Commission does not consider it appropriate to base it on consolidated profits as suggested by APFTQ but on a service by service basis. For a specialty service such as Canal D, which has been in operation for more than one licence term, the Commission considers it is appropriate to calculate the average PBIT margin for all the years that have elapsed under the current licence term.

The Commission notes that Canal D's average PBIT margin for the last licence term is between 30% and 34%, which is within the range for which the Commission, in the past, set an increase of five



percentage points for Canadian programming expenditures. In Canal D's case, the Commission determines that a five percentage point increase from 40% to 45% is appropriate in the circumstances. The Commission notes that Canal D, whose Canadian programming expenditure requirements are increasing because of this approach, should realize reasonable profit margins over the next licence term.

6. In the view of the Unions, it ought to be a simple matter to apply the policy. Indeed, in the Commission's deficiency letter of February 1, 2006 to YTV, that very issue was raised and YTV was asked to re-run its numbers using a 40% CPE percentage rather than the current 35%. YTV had suggested that rather than move from a 35% to a 40% percentage for CPE, it would "guarantee" a floor of \$222 million on Canadian programming expenditures over the licence term. It also undertook to set up a New Media Technology Investment Fund (that would not be part of YTV's CPE expenditures) with a budget of \$5 million over 7 years. YTV indicated that both of those commitments would be removed if the Commission moved from the 35% to the 40% CPE percentage.
7. The Unions appreciate the value in the two promises noted above that were made by YTV, but nonetheless feels that the Commission should continue with the application of its policy. YTV argues in its Supplementary Brief that increasing the CPE percentage to 40% in conformity with Commission policy would be "counterproductive" for the following reasons. They are not persuasive.
  - (a) YTV argues that it expects its revenues will fall over the licence term and therefore the floor of \$222 million in CPE over the licence term is better from the point of view of the Canadian broadcasting system. The Unions would respectfully suggest that its members are prepared to absorb that downside risk in exchange for the possibility that revenues will actually be higher than those projected by YTV. The Unions would encourage the Commission to stay the course as well.
  - (b) YTV argues that the CPE percentage fee for Canadian programming is a form of rate of return regulation that is not appropriate in a competitive non-monopoly environment. With respect, the fact that specialty services have their CPE requirements pegged to profits is not a form of rate of return regulation. ROR regulation would regulate the profits that YTV would be permitted. Instead, the Commission is simply looking at those returns, whatever they might be, as the basis for suggesting that more be spent on Canadian content in the ensuing licence term. Obviously, YTV must have had an average PBIT of between 30% and 35% over the licence term in order to trigger the Commission's deficiency question. Nothing prevents it from repeating those stellar performances in the next licence term, so one should not mistake this for rate regulation.



- (c) YTV states that the proposed increase “punishes” Corus for its success, inhibits growth and suppresses investor interest. The Commission dealt with this type of argument in setting the CPE policy in the first place and, as noted above, found that it correctly balanced the various parties’ interests.
  - (d) YTV suggests that to raise the CPE would fail to recognize the contribution Corus has made at Nelvana. This is a red herring that ought not to be taken into consideration. What Corus did at Nelvana may be laudable but not the cause for the Commission to fail to adhere to its own policy. Moreover, the fact that Corus did not increase the allocation of costs from Nelvana to the licensee company in the form of artificially higher licence fees is not a reason to keep the CPE percentage at 35%. This type of inappropriate practice was not undertaken (as is acknowledged by YTV in its Supplementary Brief) because it is bad practice and because it would have been punished in the marketplace. There should not also have to be a regulatory “thank you”. That said, having now been alerted to the possibility of such a practice, the Commission should move to close off that possibility, and the appropriate safeguards will be described in the next section.
  - (e) YTV argues that Corus is accomplishing a great deal and for the Commission to ignore this would be counter-productive. While the Unions understand the point YTV is making, this is a substantially narrower discussion and this argument is one that the Commission dealt with and overcame both in setting the policy and in subsequently applying it.
  - (f) YTV will establish a New Media Technology Investment Fund if the Commission allows it to stay at 35% CPE. While it may be desirable, it is a less than desirable trade-off. The total capitalization of the fund would be \$5 million over the 7 years, with 40% of that coming in the last two years. The fund is described in only the sketchiest detail in the Supplementary Brief, saying that it will be accessible by independent producers only to help them develop and create new media platforms for the programs that are licensed by YTV. (It is not clear if it will “only” be accessible to independent producers or whether it will be accessible to independent producers “only” to develop and create multimedia platforms). On the other hand, and this is why that fund is such a bad trade-off, if the Commission were to increase the CPE from 35% to 40%, the financial projections of the applicant indicate that an incremental amount much greater than that would be spent on CPE. The Unions estimate the difference to be more than \$30 million over the licence term that would be spent on Canadian programming as opposed to new media ventures relating to programming on YTV.
8. The idea of a CPE floor is not without a certain appeal, of course. It is interesting that YTV would offer a floor of \$222 million in expenditures on CPE if the Commission leaves the CPE percentage at 35% but will not agree to a floor--even the same floor, let alone a



higher one-- if the Commission raises the CPE to 40%. Since the floor costs YTV nothing, and since the chances of having to call on the floor guarantee are no greater or less if the CPE percentage is at 35% or 40%, the withdrawal of the floor must be seen as a chip in exchange for exempting YTV from the usual policy. As can be seen, this would be a bad trade, and the Commission should continue to apply its policy in the usual manner.

**C) *Safeguards***

9. The Unions believe that the Commission should not only impose the standard 75% requirement (i.e. the percentage of programming to be acquired from independent producers) but should also, in light of the comments made in the Application, require that the amount spent by YTV on programming that has been produced by it or by a related party should not exceed 25% of its annual expenditures on Canadian programming.
10. The CRTC's application form for licence renewal asks the following question:

If the Commission were to impose a condition of licence requiring a minimum percentage of programming other than news, current affairs and sports, which is produced by non-related production companies, indicate what percentage you think would be appropriate and why...
11. At page 19 of 37 of the Application, YTV responded as follows:

Given the safeguards already in place in YTV's conditions of licence as outlined above, it is not necessary to impose a condition of licence requiring a minimum percentage of programming be produced by non-related production companies.

In addition, please refer to our Supplementary Brief-Appendix 1A- for a complete review of the intentions of the applicant and the implications of such change.
12. However, the conditions of licence to which the applicant refers do not actually contain safeguards. They require that YTV distribute a minimum of 90 hours of original first run Canadian programs acquired from the independent production sector each year. YTV also must spend one-third of its Canadian programming expenditures on original first run Canadian programs commissioned from the independent production community.
13. It appears to suggest that YTV is arguing that because it has to acquire 90 hours a year from independent producers, it should be exempt from the usual requirement that 75% of all non-news, current affairs and sports programming come from independent producers. YTV airs some 8,760 hours of programming a year, of which 60% (or 5,256



hours) must be Canadian. It is no answer to point to a 90 hour a year exhibition requirement.

14. This is especially true when YTV repeatedly speaks of the importance of its sister company, Nelvana. For example, on page 40 of the Supplementary Brief, YTV notes that;

Our programming content arm, Nelvana, is far and away the largest producer of Canadian dramatic content in Canada (albeit in one genre-children's animation) and is probably the most successful Canadian producer in world markets. Our shows are seen in over 100 countries.

and

In the annual Playback magazine 17<sup>th</sup> Annual Report on Independent Production, May 9, 2005, Nelvana ranked third among all Canadian producers at \$55 million in annual production volume, behind only Alliance Atlantis and Lions Gate Entertainment. Nelvana is far and away the largest producer of animation programming in Canada.

15. While this should be a source of great pride, it should also be a subject of some concern. In Broadcasting Decision CRTC 2003-522, two other Corus licensees (SuperChannel and MovieMax!) were granted relief from an outright prohibition against airing programming produced by a related company. However, the Commission imposed the following (standard) condition of licence:

The licensee may exhibit programming that has been produced by the licensee or by a person related to it, provided that in each year, the amount of such programming, exclusive of filler programming, does not exceed 25% of its overall Canadian programming schedule.

16. In addition, however, and relevant to the YTV situation, the Commission also took into account the dominance of Nelvana and imposed a special condition of licence relating to expenditures on Canadian programming. The Commission stated the following:

The Commission considers appropriate the suggestion put forward by interveners that there should also be a cap on the licensees' annual expenditures on programming acquired from themselves or related persons. Accordingly, the licences for SuperChannel and MovieMax! shall each be subject to the additional condition of licence set out below:



In each year, the amount spent by the licensee on programming that has been produced by it or by a related party, exclusive of filler programming, shall not exceed 25% of its annual expenditures on Canadian programming.

17. The Unions request that the Commission do likewise in this case. It is especially germane considering that YTV has specifically placed the Commission on notice of the possibility that it could artificially inflate the licence fees paid by YTV to Nelvana. In inviting the Commission not to raise the CPE to 40% of revenue, YTV said the following in its Supplementary Brief:

We could have diminished the earnings of YTV by increasing the internal allocation of costs from Nelvana to the licensee company (in the form of higher licence fees) but the investment community would have punished us. Paying ourselves above market licence fees would have also been a poor business practice as it would have meant subscribing [sic] an unrealistic market price to certain programs simply to meet a regulatory goal. **We would rather have the Commission take into account our overall contribution rather than take this step.** [emphasis ours]

18. Since this is reason number 5 of 7 given by YTV as to why the Commission should not increase the CPE percentage from 35% to 40%, one must assume that YTV is implying that the Commission should leave the CPE at 35% or YTV may have to inflate the licence fees after all. It is not clear how else the phrase in bold could be read.
19. Since the appropriate step for the Commission to take is to apply its traditional policy and raise the CPE percentage from 35% to 40% (i.e. the Commission would "not take into account our overall contribution"), the foregoing means that it is even more important that the Commission impose the same self-dealing prohibitions on YTV by way of condition of licence that it imposed on SuperChannel and MovieMax! in Broadcasting Decision CRTC 2003-522.

**D) *Management fees***

20. Finally, the Unions wish to draw the Commission's attention to the issue of management fees. As noted above, in January 2004, the Commission implemented a policy of pegging the percentage increase in CPE required of specialty licensees to the PBIT in the previous licence term. One way that a licensee can "manage" its PBIT is for the parent company to charge "management fees" to the licensed entity.
21. The Unions note that a Commission deficiency question asked YTV to explain the "significant increase in administrative expenses when compared to levels experienced in the previous licence term." YTV's response included the following statement:



This licence term, includes increased corporate YTV management fees for the full licence term. The prior licence term, 2000 to 2006, includes these corporate YTV management fees only for the latter three years of the licence term.

22. The Unions respectfully request that the Commission look very closely at the possible implications of what is being said in this response. In January of 2004, the Commission unveiled its new policy and applied a PBIT based increase in CPE. Licensees could be excused if they did not immediately start looking for ways in which to deflate their PBIT numbers. The most immediately obvious starting point would be management fees.
23. It would appear from the response above that Corus got the message. Starting in August 2004, it began charging YTV "management fees". Judging from the financial projections filed for 2006 and beyond, those figures appear to be at least \$1.8 million per annum. It would appear that for almost two decades, YTV was able to manage itself without large corporate management fees. Even for the first few years of Corus' stewardship, no such fees were apparently charged.
24. All of a sudden, months following the Commission's new policy, almost \$2 million per year begins disappearing from YTV's PBIT. The Unions think that the Commission should be asking Corus some pointed questions in this regard. It is particularly important for the following reason. If YTV's PBIT over the previous licence term exceeds 35%, the 5% increase in CPE becomes 6% according to CRTC policy. While the 2005 figures for YTV are unfortunately not available yet, the five year figures for the 2000-2004 period are on the Commission's website. They reveal that the only reason that YTV does not have an average PBIT that exceeds 35%, and therefore triggers the higher PBIT increase of 6% rather than 5% for the next licence term, is the management fees that YTV began paying after it found out about the PBIT based regulatory regime.
25. With respect, this cannot be what the Commission intended. Nor should it be condoned. The Commission has always required licensees to file their annual returns on a consistent basis. In the view of the Unions, in the absence of an acceptable explanation, the correct percentage increase should be 6% not 5% so the new rate would be 41% not 40% for the ensuing licence term.
26. That difference of 1% would mean Canadian content expenditures of about \$6 million. It would be ironic if by paying itself management fees in the \$6 million range, YTV were able to avoid paying an equivalent amount in Canadian programming expenditures. One has to ask oneself why does a parent have to charge a wholly owned subsidiary company a management fee at all, let alone one sufficient in size to move it down a rung.
27. Finally, and this depends on the 2005 financial figures that will be released shortly, the appropriate CPE percentage for the ensuing term might well be 41% of revenues in any



event. The reason for that is that the Commission appears to have included the entire year 2000 in its calculations, even though the renewal term only began in June 2000. Accordingly the revenues and expenses for 2000 should only take into account one quarter of that year's results, if any at all. The previous nine months did not constitute part of the renewal term. If 2000 is eliminated, YTV shoots up over 35% PBIT for the balance of the licence term even if the management fees are not discounted or eliminated.

28. The Unions will be watching the impending release of the Commission's financial data for YTV closely and will provide updated thoughts at the public hearing relating to this renewal.

**E) Conclusion**

29. As a result of the foregoing, the Unions recommend that the Commission impose a 41% of revenue CPE condition of licence on YTV for the ensuing term. We also recommend that the Commission impose the same type of self dealing prohibitions on YTV that it did on SuperChannel and MovieMax!
30. All of which is respectfully submitted.
31. A copy of this intervention has been sent to the applicant.

Yours truly,

A handwritten signature in black ink that reads "Pamela Brand".

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