

Achieving greater support for Canadian programming within a group-based approach to the licensing of television services:

A proposed framework

The use of Canadian programming expenditure (CPE) requirements for Canadian pay and specialty services has been one of the great success stories of CRTC regulation. As the revenues of those services have steadily increased so, too, have Canadian programming expenditures, consistent with paragraph 3(1)(s) of the *Broadcasting Act*. However, since 1999, CPE requirements have not applied to over-the-air (OTA) television services. Nor have they applied to Category 2 digital services (to be included in the future Category B tier of services).

The regulatory approach proposed in this document builds on the successful use of CPE requirements for pay and specialty services, but removes anomalies and applies a CPE level to all services, including OTA television.

- 1. A CPE level, not to include licence fee top-up, should be placed on all the OTA TV services owned by a group. However, the priority programming rules could be removed and the overall Canadian content scheduling quota could be reduced from 60% to 55%.**

The CPE level for OTA television would be set by examining the Canadian content expenditures actually made by the over-the-air TV services in the group over the past three years, as a proportion of those services' total revenues. In 2008 CTVglobemedia, spent about 25.5%, Canwest about 26.6% and Rogers about 26.8% of gross revenues on Canadian programming. Based on 2008 numbers, the starting point for developing the CPE level would therefore appear to be at least 26% although, as noted below, there are good reasons to propose a higher percentage. By establishing a floor for Canadian program spending, this CPE requirement could obviate the need for a cap on non-Canadian program expenditures, which would have raised difficult allocation issues and possible trade irritants.

The definition of revenues, which are the denominator in CPE calculations, should be broadened to include new revenues from "fee for carriage" or other signal revenues as well as Local Programming Improvement Fund revenues. Since the expenditures enabled by these revenues would be included in the numerator, the revenues themselves have to be included in the denominator. These added Canadian program expenditures should therefore lead to a higher CPE level than the 26% suggested above.

An OTA CPE requirement would make it feasible to adopt a 55% overall scheduling quota in lieu of the long-standing 60% overall rule for exhibition of Canadian content programming on the OTA services, as the Commission has suggested doing. This would

provide additional programming flexibility for the broadcasters. However, the 50% evening threshold must be maintained, as that is the time of day with the highest Homes Using Television (HUT) levels. It would be inconsistent with the goals of the Act for OTA broadcasters to air a majority of non-Canadian programming during that time period.

An OTA CPE requirement would further facilitate removal of the priority program scheduling rules for OTA broadcasters, provided group-based safety nets for Canadian dramas, documentaries and children's programming are put in place. These are outlined below.

2. Individual scheduling, niche, and Canadian program expenditure (CPE) levels customized for each discretionary service would be retained to respect each service's integrity and original licensing rationale, consistent with the timetable established for liberalizing such services in the recent BDU-Discretionary Services Decision. However, CPE levels for discretionary services should be recalculated to remove any credit for licence fee top-up, and adjusted to reflect PBIT levels.

The Commission has asked whether it would be appropriate to replace individual CPE levels set for each specialty service with a single, flexible CPE requirement for integrated corporate undertakings as a whole—or, in what comes to much the same thing, to allow CPE requirements to be transferred between services within a corporate group. The argument is made that establishing a group CPE level would allow group owners the flexibility to allocate Canadian expenditures between their various services, although double counting would be precluded by the accounting rules established in Public Notice CRTC 1993-93 (still in force),¹ which would apply to the group CPE.

On balance, the proper conclusion is the same one arrived at when the Commission last posed this question, in Broadcasting Notice of Public Hearing CRTC 2007-10,² and answered it in Broadcasting Public Notice CRTC 2008-100.³ Maintaining the existing approach with individual CPE levels for each pay or specialty service is preferable for a number of reasons. They include the following:

- First, each of the individual CPE levels was calibrated to the individual circumstances of the service and was set after a competitive licensing hearing. Each niche serves a particular audience and a particular need. It would not be in the public interest to allow the owner of, say, a history service, to reduce Canadian spending on that genre, in order to increase spending on its sports service. And this could easily happen. Imagine a sports service which acquired (likely in partnership with others) the rights to the Olympic Games. That would trigger enormous Canadian content expenditures in a particular year which would

¹ *The reporting of Canadian programming expenditures*, Public Notice CRTC 1993-93, 22 June 1993.

² *Review of the regulatory frameworks for broadcasting distribution undertakings and discretionary programming services*, Broadcasting Notice of Public Hearing CRTC 2007-10, 5 July 2007.

³ *Regulatory frameworks for broadcasting distribution undertakings and discretionary programming services*, Broadcasting Public Notice CRTC 2008-100, 30 October 2008.

then justify reducing expenditures on other specialty services owned by the same corporate group. There is no policy justification for such a result. Another possibility would be an extraordinary news event, such as a war, terrorist act or natural disaster that caused extraordinary expenses on a news service in a given year. Why should these result in lower expenditures on other commonly-owned specialty services? Other examples could be noted. But the common result would be that, if the individual CPEs were merged into a group CPE, the unique purpose and role of each particular service could be severely undermined.

- Second, the individual CPE levels for each service have worked very well, and were not altered by the Commission after a thorough hearing in 2008 at which the possibility of a variant of a group CPE was canvassed.⁴ The Commission specifically considered putting various services with similar genres in a “bucket” of “like” services that would then all have a common CPE. After close examination, that idea was rejected. If the Commission did not choose to tinker with the longstanding CPE formula in a recent and lengthy hearing dedicated to examining the BDU/specialty policy framework, it is difficult to see what new facts or reasoning would lead it to do so now.
- Third, the CRTC intends—apart from genres designated as competitive, which thus far consist of national news and mainstream sports—to maintain niche protection, but may allow competition in individual cases provided the would-be competitor matches or exceeds the levels applicable to the incumbent service. (An example was the licensing of Super Channel to compete with The Movie Network and Movie Central in 2006.) However, this approach requires that each niche maintain its own customized benchmark requirements, and not be subsumed into a group number.
- Fourth, maintaining individual numbers facilitates the calculations when individual services are sold or added to a group.
- Fifth, if a group CPE were to apply to discretionary services it would also need to apply to all Category B services in the group, to preclude gaming by the group owner.⁵ That would require a complex calculation. This would be a different calculation from merely establishing a CPE for individual Category B services that have been in operation.

For all these reasons, and notwithstanding the substantial progress towards a group-based regulatory approach which the suggestions below would achieve, it does not appear to be possible at this time to harmonize existing discretionary CPE requirements at the group level without allowing broadcasters to undermine Canadian program production in the diverse content and programming genres specific to each service.

⁴ *Regulatory frameworks for broadcasting distribution undertakings and discretionary programming services*, Broadcasting Public Notice CRTC 2008-100, 30 October 2008.

⁵ Otherwise, the Cancon expenses for programs seen on both Category A and B services would all be loaded on the Category A services, thereby artificially increasing the profit in the Category B services.

Accordingly, and knowing that the Commission initiated in Broadcasting Public Notice CRTC 2008-100 a separate process of harmonizing requirements for competitive genres which will facilitate additional group-based approaches as the system evolves, the continuance of individual CPE levels for each niche specialty and pay service is strongly recommended at this time. The same reasoning applies to the scheduling and genre rules for these services, which are central to the “niche” that is protected for each service and were crucial in the original CRTC decision to grant a licence for the service. A good example is Showcase’s requirement that the period from 7-10 pm be entirely devoted to Canadian drama.

Although the CPE requirements for Category A pay and specialty services would be left at their current levels, they would be subject to two adjustments.

First, the CPE numbers would be adjusted so that they do not include any licence fee top-up allocation from the Canada Media Fund (formerly the Canadian Television Fund). To be transparent and non-discriminatory, the CPE numbers need to be based on real dollar expenditures. The time to make this important adjustment is at licence renewal as the Commission sets the CPE levels for the ensuing licence term.⁶

Second, the CPE numbers would be adjusted for services enjoying high profitability, following the approach set out in Broadcasting Public Notice CRTC 2004-2. That approach established a schedule for increases in CPE levels as PBIT margins increase:⁷

As indicated earlier, the average PBIT margin earned by the specialty industry last year stood at a very healthy level. Traditionally, the Commission has considered it appropriate that a broadcaster’s profitability be taken into account when assessing the contribution it should be called upon to make to the Canadian broadcasting system. At the same time, the Commission agrees with those who suggested that it would be unfair and, over the long term, potentially counter-productive, for the Commission to increase the requirements imposed on profitable specialty licensees to a degree that would unduly penalize their entrepreneurial success and undercut their motivation to continue pursuing increased profit margins....

Licensees whose historical PBIT levels have been in the 20 to 24% range will be required to increase their minimum annual expenditures on Canadian programming by an increment of three percentage points over the amounts specified in their existing conditions of licence. Increments of four and six percentage points

⁶ To be fair, at the renewal hearing each pay and specialty service should be given an opportunity to indicate the extent to which the licence fee top-up policy was crucial to their viability in the past licence period, and have this taken into account in setting their CPE level for the next term.

⁷ *Introduction to Broadcasting Decisions CRTC 2004-6 to 2004-27 renewing the licences of 22 specialty services*, Broadcasting Public Notice CRTC 2004-2, 21 January 2004, paragraphs 7-17.

will be required of licensees whose historical PBIT levels have been between 25 and 29%, and 35 and 39%, respectively. Licensees with historic PBIT levels above 40% will be required to increase their minimum annual expenditures on Canadian programming over the amounts specified in their existing conditions of licence by an increment of seven percentage points. Licensees having a historical PBIT of less than 20% will be required to make minimum expenditures on Canadian programming at the same levels required by their existing conditions of licence.⁸

In that regard, the calculations should not allow licensees to avoid such increases through the manipulation of management fees to artificially lower PBIT levels.

3. A group CPE floor would be established for Canadian drama. This drama requirement, which would apply to corporate groups irrespective of whether they have OTA holdings, would rise over time to an appropriate level.

It is not appropriate to replace individual CPE requirements with a general group CPE for the reasons set out above. However, even where an individual CPE level is established for each service, including the OTA services owned by a group, corporate groups still have the incentive and opportunity to reduce their OTA spending on the riskier and more expensive Cancon, and focus their OTA spending on categories which do not compete with Hollywood, such as news and sports. Accordingly, safety nets need to be established for certain types of programming of national interest that are under-represented, risky, and hard to finance: Canadian drama, Canadian long-form documentary and Canadian children's programming.

In the case of drama, the Commission has indicated that "Canadian drama should be a cornerstone of the Canadian broadcasting system." But unless there is a distinct requirement for Canadian drama, broadcasters will tend to focus their OTA expenditures on less risky fare. The best solution is to develop and impose a group CPE for Canadian drama.

There are many benefits to the use of a group CPE for drama. In a paper delivered by Peter Grant to the Broadcasting Invitational Summit on June 19, 2009, the author outlined five advantages for this approach:

- (i) It does not dictate the number of hours, or the cost per hour. It gives the group owner complete flexibility in regard to the kind of drama to be financed. The licensee can opt for a larger volume of cheaper drama. Or it can elect to support a smaller number of higher-cost dramas, even Canadian feature films, which have long been under-supported by our

⁸ *Introduction to Broadcasting Decisions CRTC 2004-6 to 2004-27 renewing the licences of 22 specialty services*, Broadcasting Public Notice CRTC 2004-2, 21 January 2004, paragraphs 12 and 14..

OTA sector. The licensee can make the “quality vs. quantity” trade-off, but in the end it must still spend the dollar amount required.

- (ii) The amount required to be spent is based on a percentage of the previous year’s overall revenue, so it automatically adjusts upwards or downwards if ad or subscription revenue changes.
- (iii) The CRTC does not have to concern itself with how the cost is allocated between the services, as long as no double counting occurs.
- (iv) This approach takes advantage of the massive consolidation of ownership that has taken place in the last few years. Despite the decline in OTA revenue, the group owners each have profitable specialty services under their wing. This approach enlists their support to fund under-represented Canadian programming.
- (v) With a drama expenditure requirement, the focus for the licensee will turn away from the accountant’s question, “how can I get away with spending less?” and towards the programmer’s question, “since I have to spend the money anyway, which Canadian drama will get me more viewers?” This is a profound change in attitude, but will come only if there is an expenditure requirement for drama.

As the drama expenditure to be required is expressed as a percentage of revenue, it should be expected to grow annually even if no increase in the percentage were mandated. The traditional 5% flexibility and carry-forwards would be used.⁹ And, because the group drama CPE would have been calculated by multiplying each service’s drama expenditure by its weight in the group (in terms of revenue), recalculating group CPE when an individual service joined or left a group would be straightforward.

With respect to which services are in a group, the questions of linguistic markets and of ownership structures must be addressed.

On linguistic markets, the Commission has noted “the different conditions under which English- and French-language broadcasting operate and the different requirements that those may have while sharing common aspects”.¹⁰ English- and French-language television markets are distinct from one another. Accordingly, it is appropriate to approach English-language and French-language service groups separately. For instance, a company like Astral, which has multiple French-language services and multiple

⁹ *New Flexibility With Regard to Canadian Program Expenditures by Canadian Television Stations*, Public Notice CRTC 1992-28, 8 April 1992 (“The Commission will permit a licensee to underspend with respect to Canadian programming, in each year of the licence term other than the final year, by an amount representing no more than 5% of the minimum amount otherwise established for that year by condition of licence. If a licensee utilizes this flexibility to underspend in a given year, the amount by which the licensee has underspent must be added to the amount required to be spent, by condition of licence, for the following year.”).

¹⁰ *Policy proceeding on a group-based approach to the licensing of television services and on certain issues relating to conventional television*, Broadcasting Notice of Consultation CRTC 2009-411, 6 July 2009 paragraph 3.

English-language services, would have two groups—an English-language group, and a French-language group—and would have to report separately for each of these groups. This would prevent it from strategies such as increasing its French-language drama expenditures to offset lower English-language drama expenditures.

On ownership structures, while many services are fully owned by single corporate entities, others are joint ventures. The Commission's test for locating the effective control of a given service can be applied to determine whether a widely-held service falls into a given group. Where a service is owned 50/50 by two groups, and the Commission's control test has not identified clear-cut control, that service would not be allocated to either group.

Expenses which are currently counted as eligible Canadian programming expenditures and which are incurred by the licensee itself—Canadian program inventory write-down, Canadian non-telecast script and concept, and Canadian programming loss on equity—should continue to be included in eligible Canadian program expenditures.¹¹ However, the drama CPE would not include licence fee top-ups. The Commission should not allow other people's money to be used to satisfy the drama CPEs of any particular licensee.¹² These amounts vary and a particular group's ability to attract Canada Media Fund support should not give it a regulatory advantage over its competitors. The opportunity to remove this inequity is at licence renewal time when it can be eliminated in a manner that is transparent and fair to each licensee.

Licence renewal is also the appropriate time at which to evaluate a licensee's attainment of public policy objectives and, where appropriate, to recalibrate the means used to achieve them. As noted above, a group-based drama CPE requirement provides a more flexible and, therefore, potentially more successful instrument for realizing Canadian broadcasting policy objectives:

While greater flexibility may have a positive impact on the viability of the Canadian television industry, it is also appropriate that this flexibility should result in greater support for Canadian programming, including original programming, particularly in

¹¹ According to CRTC figures for 2008, these expenditures as a proportion of eligible Canadian drama expenditures reported to the CRTC stood at 8.3% for English-language discretionary services, and approximately 1.6% for English-language over-the-air broadcasters. (As the CRTC publishes over-the-air broadcasters' data regionally but not by language, the latter figure is approximated by taking figures for all of Canada except Quebec, and multiplying by 105% to account for the Quebec English-language market. Of course, the latter multiplication does not affect ratios.)

¹² According to CRTC figures for 2008, licence fee top-up as a proportion of eligible Canadian drama expenditures reported to the CRTC stood at 11.9% for English-language discretionary services, and approximately 26.8% for English-language over-the-air broadcasters. (As the CRTC publishes over-the-air broadcasters' data regionally but not by language, the latter figure is approximated by taking figures for all of Canada except Quebec, and multiplying by 105% to account for the Quebec English-language market. Of course, the latter multiplication does not affect ratios.)

categories that continue to be under-represented in the Canadian broadcasting system, such as drama and documentaries.¹³

For over-the-air services it is important to note that, in 2004, the Commission established an incentive-based instrument whose objective was

an increase in the spending on Canadian drama by the English-language conventional television industry, as a percent of total revenues, from 4% to 6% over a five-year period...

CTF “top-up” funding will be excluded from the calculations for [this] Incentive[.]¹⁴

However, in 2008, CTV only spent about 4.1% of its OTA revenues on Canadian drama, CanWest only 2.5% and Rogers only 1.3%.¹⁵ Accordingly, the overall group CPE for Canadian drama should be set for the upcoming licence term with a higher level imputed for the OTA services’ contribution to it. OTA services’ contribution to group drama CPE should then continue to increase steadily over the term of the new licence until it reaches 6%.

For discretionary services, the group-based drama CPE would, in accordance with Recommendation 2 above, take into account the approach set out in Broadcasting Public Notice CRTC 2004-2 by which the overall, non-genre-specific CPE requirement of individual discretionary services is to rise for services with high historical PBIT levels. Since it takes into account a broadcaster’s profitability when assessing the contribution it should be called upon to make to the Canadian broadcasting system, that approach remains appropriate in a group-based framework. Consistent with Broadcasting Public Notice CRTC 2008-100, discretionary services in non-competitive genres will continue to play a role as niche services, with some experiencing greater success than others. The renewal-time review of profitability to assess appropriate contribution level must, for niche services, continue to proceed on a service-by-service basis.

If a service’s Canadian programming expenditures are required to rise then it is consistent that its drama programming expenditure requirement rise accordingly. For those services whose historic PBIT levels exceeded 20%, it is therefore appropriate that, rather than remain static at a 2008 level, their contribution to the group drama expenditure requirement increase in the manner described in Broadcasting Public Notice CRTC 2004-2, discounted according to the proportion of drama in that service’s overall Canadian programming expenditures.

¹³ BNC 2009-411, paragraph 10.

¹⁴ *Incentives for English-language Canadian television drama*, Broadcasting Public Notice CRTC 2004-93, 29 November 2004, paragraph 87 and Appendix. For further background to this policy history, please refer to McCarthy Tétrault LLP, “The Story So Far” (prepared for ACTRA, CFTPA, DGC and WGC, August 2009).

¹⁵ Net of licence fees, with other eligible Canadian programming expenditures allocated uniformly according to aggregate OTA figures for Canada except Quebec.

Although the approach to establishing a group drama CPE outlined here will require a number of methodological choices and assumptions, it is a feasible exercise which, properly undertaken, will create a flexible framework for better achieving public policy goals in a way that minimizes allocation issues and opportunities for regulatory gaming.¹⁶ To illustrate its feasibility, the Appendix to this framework document demonstrates one way in which it might be implemented.

4. Each group owner would be responsible for the production/airing of a minimum number of original long-form documentaries each year; alternatively, a long-form documentary CPE would be established if numbers become available.

The production of long-form documentaries is another under-represented area of policy importance which, therefore, needs special attention. These kinds of programs are supported by certain specialty services, e.g. *History Television* and *documentary*. However, they also need to be part of the fare of OTA television.¹⁷ An approach will need to be finalized to support long-form documentaries once figures become available, both with respect to dollars and hours devoted to long-form documentaries in the past. It is not just interveners who are handicapped in this regard. The Commission is lacking sufficient data as well, both with respect to the number of hours of long-form documentaries to be aired and with respect to their cost.

The Commission should seek from applicants for licence renewals the accurate figures relating to original long-form documentaries and make those publicly available to enable an open discussion regarding an appropriate threshold going forward.

Long-form documentaries will need to be re-defined in a manner that precludes the use of programs like W5 to satisfy obligations relating to CPE. There may be other issues that come to light as the rules are drafted.

5. Each group owner would be responsible for the production/airing of a minimum number of original children's programs each year; alternatively, a children's CPE would be established if numbers become available.

As with drama and documentaries, the availability of quality Canadian children's programming is a desirable outcome from a policy standpoint but one which the market will not achieve on its own, therefore requiring Commission intervention. While YTV, Treehouse, and certain other specialty services support this genre of programming, they

¹⁶ That is why we do not recommend limiting a group drama CPE to original, first-run Canadian drama. First, the CRTC statistics only track all Canadian drama expenditures, so there would be no benchmark on which to base such a requirement. Second, and more importantly, broadcasters typically pay a single licence fee to the producer/distributor which covers multiple runs; it is left to the broadcaster as to how to amortize the total cost over the various broadcast runs. If there were a CPE only for the first run, broadcasters could simply game the system by allocating all or most of the overall licence fee to the first run. As long as the group drama CPE is not set at an unreasonably low level, a drama CPE on all drama expenditures will generate new drama, as the only way to spend significant dollars on drama is to commission new drama—achieving the intended policy goal.

¹⁷ Note that in Australia, the three commercial TV networks are each required to air at least 20 hours a year of first release Australia documentaries.

also need to be part of the fare of OTA television.¹⁸ Figures will need to be made available before an approach can be finalized, but such an approach should reflect both the hours and dollars historically devoted to children's programming. As with long-form documentaries, both interveners and the Commission are handicapped in this regard. The Commission should seek from applicants for licence renewals the accurate figures relating to original children's programming, both with respect to the number of hours of children's programming aired and their cost, and make those publicly available to enable an open discussion regarding an appropriate threshold going forward.

- 6. New Canadian drama and documentaries commissioned by virtue of Recommendations 3 and 4 must air at least once on the group's OTA services between 8-11 pm. New Canadian children's programming commissioned by virtue of Recommendation 5 must air at least once on the group's OTA services at an appropriate time. This should take place within two years of the time when the licensee has acquired the programming and the right to air it.**

The 8-11 pm period is the most popular time for watching television. The goal of creating original high-cost Canadian programming of national interest is to have it aired and available for viewing by large audiences of Canadians. By having a scheduling requirement of this nature, broadcasters will provide a window for viewing at a popular viewing time.

Children's programming, by its nature, is targeted at a different audience and should be scheduled at a time when children are expected to be watching in significant numbers.

- 7. At least 75% of the Canadian drama, documentaries and children's programming proposals outlined above must be from independent producers, as measured both by number of hours and by expenditures.**

This is an adaptation of the longstanding requirement, applied to "priority programming", that 75% of priority programming must be produced by independent producers. With the disappearance of priority programming, the independent production community requires the continuation of some form of requirement to ensure that the *Broadcasting Act's* requirement of a significant contribution from the Canadian independent production sector is met. Expenditures as well as hours need to be specified in order to preclude cost misallocations and self-dealing.¹⁹

¹⁸ In Australia, in addition to an adult drama requirement, the three commercial TV networks are each required to air at least 130 hours per year of first release Australia children's programming, of which at least 25 hours must be drama.

¹⁹ This addresses an issue noted in the paper delivered by Peter Grant to the Broadcast Invitational Summit on June 19, 2009:

"There is one last accounting problem that needs to be addressed in order to protect the position of independent producers. Currently the CRTC has an expectation that at least 75% of the priority programming broadcast in the year by CTV or Canwest be produced by independent production companies. But this does not distinguish between originals or reruns and does not prevent misattribution of program cost.

8. CPE levels should be set for all Category B specialty services that have operated for a full licence term.

At some point, there ceases to be a policy rationale for distinguishing between Category A and Category B services with respect to Canadian programming expenditures. At inception, Category B services have a “step-stair” of 15%, then 25% and finally 35% in respect of Canadian content exhibition requirements. This reflects the fact that they have no genre exclusivity or access rights. But after an initial licence term, they have achieved access (or they would not have been issued a licence) and they should have begun to establish themselves. Category A specialty services get a “free pass” for the first year of their licence before their CPE obligations come into effect. An entire licence term should be sufficient for Category B services to benefit from their Canadian content spending holiday, particularly where the service or its corporate group has experienced good profitability.²⁰ The Commission might wish to consider establishing an exemption to this rule if the service has been unprofitable over the last three years.

9. New CPE levels should be set for all PPV and subscription VOD services that are equivalent in nature to scheduled services.

Video on demand services, and, to a certain extent, some PPV services have proposed and in some cases have aired programming which mimics traditional scheduled (linear) services. The Commission has another proceeding underway to consider the issues raised by VOD but these services should not be permitted to undermine the contributions of scheduled services, nor allow for the arbitraging of the difference in CPE levels between scheduled services and such PPV and/or VOD services.

10. New media broadcasting revenues and expenses—but not only one or the other—could be included in the CPE calculation.

Companies with new media broadcasting activities will have an incentive to allocate programming expenses to licensed activities and revenues to unlicensed activities. Although new media remains relatively small, its impact will certainly grow over the next licence term of the broadcasters such that close attention must be paid to the definitions and allocations of programming expenses and revenues now.

The solution is simple: have the 75% rule apply to both hours and value, instead of hours alone. In other words, if you have a drama expenditure requirement applicable to the group, simply say that at least 75% of the hours and 75% of the expenditure must be on independently produced drama. That addresses any misallocation of cost caused by self-dealing.”

²⁰ To prevent gaming by licensees who could simply apply for a new licence instead of operating under their existing one for more than a term, knowing that open-entry Category B licences are not difficult to obtain (especially where there is a precedent service), the Commission would likely have to adopt a procedure under which, where the same party applied for a licence similar to one that it held or had very recently held for a full licence term, the application would be treated as an application to renew, reinstate, or add a feed to the previous licence. Careful treatment of Category B applications to prevent gaming is already a well-established practice at the Commission: for instance, application of Broadcasting Circular CRTC 2006-1, in which the Commission stated that it would not generally review applications for licence amendments that are received within two years of the date that a new service has been implemented.

At the same time, broadcasters may want to increase their participation in Canadian new media broadcasting production by including production expenditures on Canadian “webisodes” and Internet licence fees for Canadian programming as part of their CPE. Including these new media broadcasting expenses could be allowed on the CPE numerator, provided the broadcasters also include new media broadcasting revenues as part of the CPE denominator. This approach deserves study since it could prevent the sorts of misallocations alluded to above, as well as support the creation of Canadian new media broadcasting content in a forward-looking manner.

Appendix: Implementing a Group-Based Approach to Required Expenditures on Canadian Drama

Recommendation 3 of the Proposed Framework suggests how a group floor for programming expenditures, reserved for Canadian drama, should apply to corporate groups irrespective of whether they have OTA holdings—and why the floor should rise over time to an appropriate level.

This group drama CPE would not require that groups invest in drama for services that do not air it. Rather, the starting point for determining a group drama CPE would be the actual Canadian drama spending (excluding licence fee top-up) for each of the group's conventional and discretionary services, as a portion of the same services' revenue.

Establishing the Baseline

Recommendation 3 proposes that the Commission's control test be applied to determine which services fall into a group. While this test is relatively conservative, it is straightforward. Its conservatism would not lessen contributions to Canadian drama programming, since the purpose of a group-based approach is to leverage a group's resources to better support Canadian drama, and discretionary services not in a group would continue to retain their individual requirements.

Canadian drama spending for services in a group is measured according to the Category 7 (Drama & Comedy) spending and gross revenue figures that are reported to the CRTC by all Canadian over-the-air and discretionary services.²¹ To allocate these on a per-group basis, the most straightforward approach is to:

- determine each service in the group's individual drama CPE, by dividing how much it spent on Canadian drama by its gross revenues, and then
- calculate how these individual drama CPEs fit into a whole group, by weighting each service according to its gross revenues.

For instance, CTVglobemedia's over-the-air revenues accounted for about 56% of its group revenues (including all discretionary services) in 2008, so for 2008 its OTA drama CPE (as reported to the CRTC) would account for 56% of its group drama CPE. Discretionary services accounted for about 44% of its group revenues, so discretionary services' CPEs would collectively account for that same 44%.²² This approach yields the same result as simply

²¹ Appendix I to *Definitions for new types of priority programs; revisions to the definitions of television content categories; definitions of Canadian dramatic programs that will qualify for time credits towards priority programming requirements*, Public Notice CRTC 1999-205, 23 December 1999.

²² A similar approach would likely be necessary in respect of the reallocation of individual TV stations in a network to a new controlling party, as has recently been proposed. This approach would take as its starting point the manner in which networks allocate expenditures across individual stations, such as on a per-population basis.

dividing all of a group’s drama expenditures by all of its gross revenue. But, by starting with individual services’ drama CPE results, it is easy to recalculate changes to each group’s drama CPE that result from a change of control in an individual service.

The figures used in the tables below, which are provided in order to illustrate how one might apply the method described in Recommendation 3, generally follow this approach. They are net of licence fee top-up. They include either actual eligible Canadian programming expenditures (program inventory write-down, non-telecast script and concept, and programming loss on equity) or, for over-the-air services, reasonable estimates of these expenditures.²³ It is clear that, in order to determine formally each group’s drama CPE, the CRTC would have to conduct a rigorous review of services’ ownership structures and apply the methodology described here on internal data available for such services in order to arrive at conclusive figures. Applying the approach set out above for 2008, group drama expenditures stood at about 7.3% of group revenues for Canwest, 4.9% of group revenues for CTVglobemedia and 0.7% for Rogers, as illustrated in Table 1 below.

Table 1
Canadian drama expenditures by group, 2008

Revenues (\$000,000)	Group	OTA	Cat. A	Cat. B	Overall	OTA Weight
1508	CTVglobemedia	4.1%	6.3%	0.3%	4.9%	55.3%
951	Canwest	2.5%	17.4%	3.0%	7.3%	61.5%
404	Rogers	1.3%	0.0%	-	0.7%	51.2%
351	Corus	-	9.8%	1.8%	9.4%	-
192	Astral	-	15.1%	-	15.1%	-

Notes: Percentages in “OTA”, “Cat A.”, and “Cat. B” refer to drama programming expenditures for services within that licensing category, weighted by proportion of gross revenues for that group’s English-language services in that licensing category.

“OTA Weight” refers to the proportion of a group’s gross revenues (and, accordingly, the proportion of a group’s drama CPE) accounted for by that group’s OTA services.

Each group includes a different mix of over-the-air and discretionary services. In turn, every discretionary service has a distinct niche and nature of service, including the type and categories of programming it is permitted to air and required Canadian programming expenditures, if any. Accordingly, the groups’ blended Category A and blended Category B drama expenditures—each of which aggregates individual discretionary services, weighted by gross revenues—are very different from one another in keeping with each group’s unique services, which range from sports-heavy services like TSN or Sportsnet to drama-heavy services like Showcase or YTV. To take an extreme example, a group whose only discretionary service is an all-news service will

²³ As other eligible Canadian programming expenditures are publicly available in respect of drama for over-the-air services only on an aggregate basis, it is assumed for the purposes of this exercise that every individual OTA service’s spending on these items was identical (1.6% of eligible drama programming expenditures, or 2.2% of the same expenditures net of top-up).

have far lower historical drama expenditures than a group whose only discretionary service is an all-movies service. Accordingly, the groups' overall drama CPEs differ.

Regulatory Obligations of English-Language Over-the-Air Services

Recommendation 3 notes that OTA services have fallen well short of the revenue allocations to Canadian drama expenditures that have been established as a policy goal. OTA services were to increase Canadian drama expenditures from 4% to 6% of revenues between 2004 and 2009. However, by 2008 CTV spent only about 4.1% of its OTA revenues on Canadian drama, Canwest about 2.5%, and Rogers about 1.3%.

A group-based approach would bundle these OTA services' contribution to drama spending with the contributions of their corporate parent's full portfolio of same-language television services, providing flexibility. However, this approach should not allow OTA services to continue to underspend on underrepresented programming. For the upcoming licence term, the overall drama expenditure obligation for English-language service groups should therefore immediately increase the contribution that OTA services are required to make. OTA services' contribution to group drama CPE should then continue to increase steadily over the renewal period until it reaches a level that is commensurate with the privileges granted to these services.

Table 2 proposes what, in view of the significant increases in contributions that will be necessary to attain the levels supported by public policy, is a relatively gradual approach to adjusting OTA services' contribution to group drama CPE. It models a seven-year licence term in which each OTA service's drama CPE contribution goes up each year at the rate required to attain 6% by the end of the licence term. This model is provided by way of explaining more fully the approach proposed in this framework, and can only be illustrative in purpose. For instance, it models the years ending 2009 through 2015, based on available 2008 data, whereas the CRTC's licence renewal hearings will address the years ending 2010 through 2016.

Notwithstanding the gradual approach advocated, services whose starting point is below 4% of gross revenues, as is the case for Canwest and Rogers, are exceptionally increased by 25% in the first year (instead of what would have been a 13.6% increase for Canwest, and a 23.9% increase for Rogers), for the reasons discussed in Recommendation 3. As a result, the rates at which the English-language OTA services' contribution to their group drama CPE increases over the course of the licence term becomes 11.8% annually for Canwest (only from 2010), 23.7% annually for Rogers (only from 2010), and 5.7% annually for CTVglobemedia, which was already spending about 4.1% of revenues on Canadian drama, over the full course of the term (that is, from 2009). Other approaches are possible.

Table 2
Canadian drama expenditures for English-language OTA services (adjusted), 2009-2015

2008	OTA Service	2009	2010	2011	2012	2013	2014	2015
4.1%	CTVglobemedia	4.3% (+5.7%)	4.5% (+5.7%)	4.8% (+5.7%)	5.1% (+5.7%)	5.4% (+5.7%)	5.7% (+5.7%)	6.0% (+5.7%)
2.5%	Canwest	3.1% (+25.0%)	3.4% (+11.8%)	3.8% (+11.8%)	4.3% (+11.8%)	4.8% (+11.8%)	5.4% (+11.8%)	6.0% (+11.8%)
1.3%	Rogers	1.7%	2.1%	2.6%	3.2%	3.9%	4.9%	6.0%

		(+25.0%)	(+23.7%)	(+23.7%)	(+23.7%)	(+23.7%)	(+23.7%)	(+23.7%)
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Notes: Bolded percentages indicate percentages of gross revenue.
 Percentages in parentheses show growth over previous year.

Regulatory Obligations of English-Language Discretionary Services

Table 3 presents a method for adjusting discretionary services’ contribution to group drama CPE to take into account their profitability. This method is applied to PBIT data available for the years to 2004 through 2008, as reported by the CRTC. Based on the approach set out in Broadcasting Public Notice CRTC 2004-2 and reviewed under Recommendations 2 and 3, drama expenditure requirements are increased in accordance with their historic profits before interest and taxes, reduced to apply only to the fraction of their Canadian programming expenditures which was devoted to drama.

For instance, Corus’s MovieCentral had an aggregate 25.8% PBIT margin for 2004-2008, and drama accounted for 96.9% of its Canadian programming expenditures in 2008. Because its historical PBIT level is between 25% and 29%, its overall CPE is increased by four percentage points, as outlined in Broadcasting Public Notice CRTC 2004-2’s step-stair approach. However, because drama accounted for 96.9% of its Canadian programming expenditures, only 96.9% of those four points are allocated to MovieCentral’s drama CPE—which rises from 10.6% to 14.5% (after rounding) for a 37% increase.

The individual discretionary services whose contribution to group drama CPE rose greatest on the basis of 2004-2008 PBIT data, due to a combination of high profitability between 2004 and 2008 and a high proportion of expenditures devoted to drama in 2008, were YTV (Corus), MovieCentral (Corus), The Movie Network (Astral), The Comedy Network (CTVgm), The Family Channel (Astral), Space (CTVgm) and Mpix (Astral). Any conclusive accounting would, of course, require more fulsome consideration of which years of data to use—which should not be constrained by which data have been filed in the past—and careful calculation on the part of CRTC staff using PBIT data for a full licence term, among others.

Table 3
 Canadian drama expenditures for English-language discretionary services
 (adjusted in light of historic PBIT levels), 2009-2015

Group	Category A	Category B	All Pay & Specialty
CTVglobemedia	7.0% (6.3%)	0.4% (0.3%)	6.6% (6.0%)
Canwest	17.6% (17.4%)	3.4% (3.0%)	15.2% (15.0%)
Rogers	0.0% (0.0%)	-	0.0% (0.0%)
Corus	12.7% (9.8%)	2.0% (1.8%)	12.1% (9.4%)
Astral	18.4% (15.1%)	-	18.4% (15.1%)

Notes: Percentages in parentheses show actual 2008 drama expenditures as a proportion of gross revenues for all services in category. Bolded percentages show proposed level for 2009-2015.

Group Drama CPE for English-Language Services Groups

Having reviewed the performance of services licensed to corporate groups involved in the current renewal proceedings in Table 1, and the ordinary renewal period assessment of contributions and commitments in Tables 2 (over-the-air services) and 3 (discretionary services), the final step is an overall approach integrating these. The blended group drama expenditure requirements modelled in Table 4 therefore combines the approaches set out above for OTA, increasing drama CPE to attain 6% by the end of the licence term, and for discretionary services, adjusting drama CPE in light of historic profitability. For the purposes of this illustrative model, group revenues are assumed to grow at the rate of 3% annually.

Table 4
Canadian drama programming expenditures by English-language group
(with adjustments to OTA and discretionary services),
2009-2015

2008	Group	2009	2010	2011	2012	2013	2014	2015
4.9% (74)	CTVglobemedia	5.3% (83)	5.5% (88)	5.6% (93)	5.8% (98)	5.9% (104)	6.1% (110)	6.3% (116)
7.3% (69)	Canwest	7.7% (76)	8.0% (80)	8.2% (85)	8.5% (91)	8.8% (97)	9.1% (104)	9.5% (111)
0.7% (3)	Rogers	0.9% (4)	1.1% (5)	1.3% (6)	1.6% (7)	2.0% (9)	2.5% (12)	3.1% (15)
9.4% (33)	Corus	12.1% (44)	12.1% (45)	12.1% (47)	12.1% (48)	12.1% (49)	12.1% (51)	12.1% (52)
15.1% (29)	Astral	18.4% (36)	18.4% (37)	18.4% (39)	18.4% (40)	18.4% (41)	18.4% (42)	18.4% (43)
208	Total	242	255	269	284	300	319	339

Note: Percentages indicate required group drama expenditure as proportion of gross revenues; whole numbers indicate millions of dollars of Canadian drama expenditures (not including licence fee top-up).

The overall group drama CPE requirements described in Table 4 differ substantially from group to group. As described above, the reasons for this stem for two factors.

First, due to the gradual ramp-up in the OTA service's contribution to the group drama CPE, OTA services become harmonized (at 6%, net of licence fee top-up) only by the final year of the licence term. This factor accounts for between 51% and 62% of the group drama CPE figure (see Table 1, above).

Second, each group has a unique mix of distinct niche services, each of which has a different nature of service, unique programming category allowance, and other distinct conditions of licence. The group drama CPE that comes from discretionary services should not be expected to

be uniform from group to group. As described in Recommendation 2 above, it is consistent with neither a public policy which supports a diverse ecosystem of programming services, nor with the Commission's recent, exhaustive review of discretionary services,²⁴ to flatten these niches and permit the creation of competing discretionary services, outside those genres designated as competitive in that review or as a result of future applications.

²⁴ *Regulatory frameworks for broadcasting distribution undertakings and discretionary programming services*, Broadcasting Public Notice CRTC 2008-100, 30 October 2008.