Copyright Board Canada

Commission du droit d'auteur Canada

Date 2002-03-15

Citation FILES: Public Performance of Musical Works 1997, 1998, 1999, 2000, 2001, 2002
FILE: Public Performance of Sound Recordings 1998-2002

Regime Public Performance of Music
Copyright Act, subsection 68(3)

Members Mr. Justice John H. Gomery
Mr. Stephen J. Callary
Mrs. Sylvie Charron

Proposed Tariffs Considered 1997 to 2002 for SOCAN and 1998 to 2002 for NRCC

Statement of Royalties to be collected by SOCAN and by NRCC for pay audio services

Reasons for decision

I. INTRODUCTION

These reasons deal with the proposed Tariff 17.B of the Society of Composers, Authors and Music Publishers of Canada (SOCAN) for the years 1997 to 2002, and the proposed Tariff 17 of the Neighbouring Rights Collective of Canada (NRCC) for the years 1998 to 2002. Proposed statements of royalties were published in the *Canada* G*azette*, as were notices outlining the right to object pursuant to subsection 67.1(5) of the *Copyright Act* [the "*Act*"]. Both target primarily digital pay audio ("DPA") services.[1]

The hearings into these tariffs took place over 13 days ending in May 2001. The collective societies (SOCAN and NRCC) as well as the two Canadian DPA service providers, DMX Canada ("DMX") and Galaxie, participated in the hearings, as did two groups of distribution undertakings[2]: the direct-to-home satellite companies, Bell ExpressVu and Star Choice (hereafter

[1] The CRTC speaks of pay audio services and pay audio programming undertakings. During these proceedings, objectors referred to non-broadcast radio services. Proposed statements of royalties target pay audio radio services or non-broadcast radio services.

[2] The *Broadcasting Act* defines distribution undertaking as "an undertaking for the reception of broadcasting and the

"DTH"), as well as the Canadian Cable Television Association (CCTA) and Shaw Communications, representing the interests of cable system operators.[3]

A. DPA: ITS ORIGINS AND NATURE

The birth of DPA in Canada was long and painful. First, two service providers were licensed in 1993. However, after Cabinet directed it to reconsider the decision, the Canadian Radio-television and Telecommunications Commission (CRTC) denied both applications. Then, after a further round of hearings, four licences were issued in 1995. Again, Cabinet directed a reconsideration; this time, the CRTC confirmed its decision in August 1996. A further appeal to Cabinet failed. Subsequently, only two of the four licensees began operations, both in 1997: DMX and Galaxie.

At first, the licensees adopted very different marketing strategies. DMX strove to be a standalone, fully discretionary service available only on request. Galaxie wanted to become a low-priced, high penetration service. Galaxie's approach has prevailed. At present, DPA services are offered at no extra cost to digital cable subscribers, and as part of the basic package to all DTH subscribers.[4] To date, the success of DPA has been largely dependent on DTH penetration, as digital packages are only purchased by 10 per cent or so of cable subscribers.

DPA offers unique, premium music services, unprecedented in sound quality. It comes in a vast variety of highly specific programming formats.[5] This is attractive not so much because subscribers wish to tune in to all of them, but because each listener is able to find one or two signals that closely match his or her specific preferences. Still, the evidence indicates that video signals, not DPA, are what drive purchasing decisions. DTH uses DPA to distinguish itself from cable, while cable offers it to its digital subscribers to match the DTH offering.

Basically, two creative inputs are used in producing a DPA signal: published sound recordings and the programmers' skills.[6] Other expenses include signal delivery, marketing and regulatory costs. DPA is a capital intensive industry; costs increase little, if at all, as the number of

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retransmission thereof by radio waves or other means of telecommunication to more than one permanent or temporary residenceor dwelling unit or to another such undertaking".

[3] The DPA service provider and the distribution undertaking are jointly and severally liable for the public telecommunication that occurs when a work is transmitted through a distribution undertaking on a DPA signal: paragraph 2.4(1)(*c*) of the *Act*.

The Digital Media Association objected to the SOCAN tariff but did not participate in the proceedings. Objections from background music service providers, a cableradio station and others were eventually withdrawn.

[4] A few small systems offer DPAs in a FMformat.

[5] DMX and Galaxie each provide 30 channelscovering a variety of highly specific genres.Pop Classics, Baroque, Classics Masters and Chamber Music each have their own channel; so do music from the '70s and music from the '80s.

DPA offering may change substantially in the near future. Already, there is talk of a joint management agreement between DMX and Galaxie, which would result in distribution undertakings being offered a single bundle of 40 signals. At the time of the hearings, however, the future of this proposal remained uncertain. It is therefore unnecessary to take it into account in this decision.

[6] Other "products" that could be used in the future, but that are mostly absent at present,include live spoken word, unpublished sound recordings, live music and sound recordings of non-musical works.

subscribers increases. Reliance on ready-made music allows service providers to keep programming costs very low. Because of the extensive use of computer technology, operations require minimal plant and staff.

The explosive growth in the penetration of DTH in this country has meant that Canadian DPA has not experienced the difficulties that apparently continue to plague its American counterparts. Though launched much earlier than in Canada, DPA south of the border is still perceived by many as a startup industry with an uncertain financial future. Canadian DPA, by contrast, enjoys substantial profit margins which, because of its cost structure, are predicted to grow significantly over the next few years.[7]

B. THE PARTIES' POSITIONS

NRCC suggests that equitable remuneration necessarily reflects the price that a willing seller and a willing buyer would come to in a competitive market. To derive this, it proposes four approaches. First, assess the proportion of the total value of DPA accounted for by recorded music; in this regard, NRCC points to DPA's almost total reliance on such recordings. Second, examine how much other subscription broadcasting services, and especially pay and pay-per-view, spend for program content. Third, set the royalties so that DPA's rate of return is similar to commercial radio and other subscription broadcasting services. Fourth, as an alternative, set the royalties at how much a service provider would be willing to pay to acquire a monopoly. NRCC then relies on the private copying tariff to ask that performers, makers and authors/composers each get a third of the royalties before any eligible repertoire adjustment.

SOCAN generally adopts NRCC's submissions except on the issue of the relative value of the repertoires. SOCAN argues that authors and composers should get the same as performers and makers. The approaches put forward by the collectives would result in a rate of between 30 and 40 per cent of a distribution undertaking's affiliation payments.

The objectors maintain that the commercial radio tariff should serve as starting point. They perceive striking similarities between commercial radio and DPA, such as their "almost identical" reliance on music. They argue that DPA services are of accessory value in the world of digital offerings. They also ask that the tariff reflect the advantages conferred by statute to commercial radio with respect to so-called neighbouring rights royalties. This would result in a rate in the order of between 3 and 5 per cent.

C. THE EVIDENCE

The evidence that is on the record of these proceedings is both abundant and varied. SOCAN's witnesses offered background information on DPA as well as their view of the user's perspective. Others provided a detailed overview of the development and characteristics of Canada's broadcasting industry, with a special insistence on the emergence of DPA. NRCC's witnesses provided a detailed overview of DPA's profile in the media and in advertising. NRCC

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[7] The profitability of DMX is reduced because of an agreement with its Americanparent, though not to such extent that the general assessment made here is affected.

also filed the results of a consumer survey dealing with the place of DPA in Canadian homes and its potential impact on CD-purchasing and radio-listening habits. This and other evidence were used as backdrop in developing the collectives' proposed model for valuating the relevant repertoires.

Objectors offered evidence from experts and others, including survey evidence, that tended to cast doubts on NRCC's approach and to favour a valuation based on royalties paid by commercial radio. They also offered a significant amount of background, financial and historical industry information that helped put DPA, its emergence, its relevance and relative importance to distribution undertakings in context.

Both sides provided extensive evidence and comment on the financial situation of DPA service providers. Given the small number of participants in the industry, most of this had to be heard in camera. This explains to some extent why references to financial data in the rest of this decision are only as specific as absolutely required for the purposes of the decision.

The extensive evidence of the economists retained by participants helped to highlight the complexity of the issues involved in this file, and the diversity of ways in which they could be tackled. The analysis of this evidence represented a difficult, but necessary and helpful step in allowing the Board to reach its decision. The Board especially appreciated the considerable efforts these witnesses made to be helpful and to provide open-minded perspectives. In the end, however, the analysis that underscores the Board's conclusions must be the Board's own.

As informative as the evidence provided may have been, and for reasons stated below, the analytical framework and the approach used by the Board to derive the tariff rate make it unnecessary to review this evidence in detail.

II. ANALYSIS

A. THE "PRICE" SUBSCRIBERS PAY FOR DPA

Throughout the hearings, DPA was often referred to as being free to the subscriber. It should be stated at the outset that this is simply incorrect. No programming that is offered as part of a set package, including the basic package, is free to subscribers. Subscribers pay for what is included in any package, whether or not they know it, and even if they are unaware that they are getting it.

B. THE PROPOSED STARTING POINTS

In essence, collectives and objectors proposed two types of starting points.[8] The first are the prices paid or rates of return achieved in a number of real or theoretical free markets. The second are the prices set by the Board for what arguably are similar uses or uses in similar (or competing) industries.

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[8] Participants also referred to them as proxiesor even methodologies. Given the conclusion the Board reaches as to their usefulness, nothing would be served by engaging in that debate.

In the Board's view, none of the comparisons offered is clearly preferable to the others. All of them are sufficiently weak, or in need of sufficiently large corrections, to make the use of one or a combination of them highly problematic. Proposed free-market comparators are dramatically different from telecommunication rights for music and sound recordings. The tariffs put forward as starting points target industries that do not compete with DPA and whose business models are so far removed from that of DPA as to make comparisons difficult, if not irrelevant.

The price that would be arrived at by a willing buyer and a willing seller in a real or hypothetical free market is useful as a starting point only when it offers some basis for comparison with the industry under examination. This is why the Board was able to use the price of the A&E signal in developing the retransmission tariff.[9] Even with all the adjustments the Board has applied, the similarities between the pre-recorded CD and private copying markets are striking. Nothing of the sort exists in this instance.

Thus, it would not be appropriate to set the tariff by looking at what television pay and pay-per-view services spend on movie rights, even though these services do present certain similarities with DPA. Both depend on a single, externally sourced category of content: music and movies. Neither produces content; they package someone else's intellectual property. Both operate on similar, extremely lean infrastructures. Both compete for available bandwidth. However, contrary to music rights, movie rights are sold in a competitive market, with some level of exclusivity. This alone is significant enough to discard the comparison. Even if the comparison were used, it would require a rate correction of 50 per cent or even more.

Neither would it be appropriate to set the tariff by trying to match DPA's rate of return to that of commercial radio or other subscription broadcasting services. Subject to later comments on the structure of the information economy, the Board's function is not to regulate users' profitability. Profitability may be used to assess whether an industry is able to afford an otherwise fair tariff; it should be used only rarely to assess whether the tariff is fair and reasonable in the first place.[10]

It is not necessary to scrutinize the other two approaches put forward by NRCC: it rightly concedes that they cannot be used to derive the rate. Nevertheless, the Board finds it useful to comment on the "simulated auction" approach which was discussed at the hearing. This scenario calls for setting the price of music at what one would be willing to pay to acquire a monopoly over DPA. That approach must be set aside because it focuses again on profitability at the expense of all else.[11] This being said, the exercise is not without merit, if only because it highlights the important notion that in information industries, pricing tends to be based on the value to the buyer, not on cost to produce.

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[9] *Statements of Royalties to Be Paid for the Retransmission of Distant Radio and Television Signals in 1990 and 1991*, (1990-1994) C.B.R. 3; 32 C.P.R. (3d) 97, http://www.cb-cda.gc.ca/decisions/r02101990-b.pdf.

[10] Some participants argued that profitability should be analysed by looking only at the most profitable operations, and not every operator in the market. Were this true, everyventure capitalist and anyone involved in anindustry that depends heavily on research and development would rapidly run out of money.

[11] Similarly, this decision will not deal with the question of whether the provision of DPA services is a natural monopoly. It is difficult to believe that natural monopolieshave all but vanished, given that network effects present in the information economyand elsewhere do seem to favour the creation of monopolies, natural and otherwise.

The absence of a usable free-market starting point is not in itself problematic. While free market transactions are both important and relevant, they are not the only factor to look at. Thus, using another tariff set by the Board as a starting point will be helpful where industries can readily be compared. Participants looked at several other tariffs either as possible starting points or as reality checks.

Foremost among those was the commercial radio tariff. Those who favour this comparison rely on several arguments. DPA and radio are both audio services. DPA has been said to view itself as "radio, only better". Both use similar playlists and rotations. The principles governing selection and ordering of music are the same for both.[12] Close to 80 per cent of the average radio station's content consists of music. Music format stations account for the vast majority of radio listening in Canada, and most commercial stations emphasize music or music format as what drives them. A majority of people give music as the main reason for listening to radio, and most say that they would listen less if radio did not play sound recordings. Supporters of this approach also point to the fact that CRTC conditions of licence are often similar for radio and for DPA.[13]

Still, the Board concludes that what DPA provides is neither in competition with, nor a substitute for commercial radio.

Even though part of a "music continuum", DPA is not on the whole an economic substitute for most products within that continuum.[14] Two products are not substitutes for one another simply because they cannot be used at the same time or are competing for a person's time. A pre-recorded CD is not a substitute for radio, even though most would rather not listen to both at the same time: functional interchangeability should not be confused with substitutability. One true test of what is a substitute is cross-price elasticity: does an increase in the price of one result in an increase in the sales of the other? There are no signs of cross-price elasticity between commercial radio and DPA.

As demands on available bandwidth increase, DPA and distant radio signals available for retransmission may become substitutes for one another. The appropriate comparator would then be the radio retransmission tariff, which has always been set by consent at a seemingly very low amount.[15] Using an untested tariff as a starting point would not be useful or equitable.

The Board also believes that DPA does not compete with radio.

First, although music may be what radio mostly provides, that does not mean that it is radio's most important input. The most important part of programming is not necessarily what consumes the most airtime: sports are crucially important to a television station's profitability, but

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[12] This seems to run counter to Mr. Giunta's testimony, who found that working for Galaxie allowed him to "worry about ... things that commercial radio had long sinceforgotten about." Tr. p. 2087.

[13] This is something to be expected in anyevent, as both provide an audio output.

[14] Indeed, as can be inferred from what follows, most products within that continuum are not on the whole substitutesfor each other.

[15] Retransmitters pay 5¢ per year per subscriber for distant radio signals; that is less than one per cent of what they pay fordistant television signals.

generally represent a fairly small share of overall programming. Radio may be designed around the use of music and musical genres but as a cost, and (probably) as a drawing card, on-air talent is far more important. Commercial radio could reduce its expenses significantly by dispensing with on-air talent and making greater use of SOCAN's and NRCC's repertoires. If it does not, it must be because radio broadcasters consider that the lost advertising revenues would be greater than the cost savings. On-air talent creates the crucial identity link between station and audience. DPA has no on-air talent.

Second, DPA and radio are not in the same marketplace. Commercial radio sells "ears" to advertisers who want to promote a product in a local market. DPA sells national programming to distribution undertakings. DPA has no advertising.

Even from the listener's perspective, commercial radio and DPA do not compete. With DPA, the focus is aesthetic: its selling point is that it consists entirely of music. [16]Commercial radio's output is a package of information, chat, comment, advertising, other creative inputs and music. "Survival" programming (news, weather, traffic), local interest stories and the selection of on-air personalities are pivotal in a commercial radio station's operations, especially during peak listening hours.

Eventually, services will compete for bandwidth, and competition will emerge between DPA services and all other signals available to distribution undertakings, including distant radio signals available for retransmission. To date, however, the amount of digital content available to distribution undertakings to distinguish digital and analog offerings has been limited. Whether the recent introduction of new video digital services changes this remains to be seen. Meanwhile, distribution undertakings continue to purchase DPA and incur additional copyright liability in doing so, even though they could substitute distant radio signals for DPA at little or no cost. Under the circumstances, it is difficult to see how it may be argued that radio signals currently compete with DPA.

Other differences exist. For reasons explained below, some, such as the differences in business models, are important. Others are less so, such as the fact that radio produces its own content, while DPA does not, or that each radio station offers one programming format, while DPA offers a broad choice of very focussed formats.[17]

Objectors argued that since the Board used the price of music to conventional television as a starting point for calculating the price of music for pay and specialty services, it should set the price of music for DPA as a function of that price to commercial radio. The decision reached for television was based on the proposition that copyright users operating in similar industries, competing in the same marketplace to acquire similar inputs so as to deliver similar products ought to pay the same price for their non-competitive inputs, to avoid creating a competitive imbalance. This reasoning does not apply to this case.

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[16] With the possible exception of a few spokenword programs on signals targeted at children.

[17] The Board gives little weight to the fact thatDPA markets itself as being different from conventional radio. Those who offer a new product always try to distinguish it from theexisting product that people, rightly or wrongly, are most readily going to associateit with.

First, for the reasons already stated, commercial radio and DPA are not similar industries and do not deliver similar products.

Second, the reason for linking the price of music between two sectors of the television industry was the existence of competition over inputs (especially creative inputs) other than music. DPA and radio do not compete for inputs. The right to play recorded music, the "thing" which both use most, is not something over which radio stations have to compete amongst each other or against DPA, because it is "sold" without any level of exclusivity.

Third, the rights which television stations purchase in a competitive market cost considerably more than music. Setting a different rate for DPA than for commercial radio will not create a competitive imbalance in the acquisition of competitive inputs, as the share of revenues DPA uses to pay for competitive creative inputs is, relatively speaking, much lower than that of commercial radio.

Using commercial radio as a starting point also raises problems if, as the record of these proceedings seems to indicate, radio now uses and emphasizes music much more than it did when the Board last examined that industry. If that is so, it could be argued that the commercial radio tariff may be too low, which would weaken its usefulness as a starting point.

Comparisons with SOCAN Tariffs 15 and 16 (background music) are not helpful either, if only because these target the use of music in commercial establishments, not the playing of music at home. In any case, it can safely be said that, given equivalent rate bases, the price paid for playing background music in shopping centres should be lower than the price paid to deliver foreground music to domestic subscribers.

This is a case where there are no useful proxies available to the Board. At most, there are a variety of marginally relevant indicators, all of which nevertheless serve to establish a "comfort zone" within which the Board, given all the circumstances, is able to exercise its discretion in setting the tariff. As counsel to the cable system operators put it, this is a case where tariff making involves looking at the characteristics of the industry and trying to figure out what makes sense at the time. In doing so, the Board will keep in mind its *raison d'être* which, contrary to what counsel to the DPA service providers stated, is not so much to supervise the rates charged by SOCAN's members as to balance the competing interests of copyright owners and users.[18]

III. VALUING THE RIGHTS

Under the circumstances, the Board intends to set the tariff in four steps. First, it decides on the relative value of the repertoires. This is necessary to the second step, which establishes the range within which a reasonable rate might be found, using the tools made available in the proceedings. Third, the Board will identify the factors which, in its view, tend to push the rate higher or lower within that range. Fourth, it will select a figure, to be adjusted to account for the

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[18] "[T]he Board properly understood its function when it stated that it had to regulate the balance of market power between copyright owners and users": *Canadian Association of Broadcasters* v.*SOCAN* (1994), 58 C.P.R. (3d) 190, 196g(F.C.A.).

eligible repertoires.

A. THE RELATIVE VALUE OF THE REPERTOIRES

For reasons outlined in earlier decisions, the Board finds that all things being equal, authors and composers should get the same as performers and makers.[19] Furthermore, the private copying tariff, being paid on account of the reproduction right, should not be used in the context of pricing the telecommunication right. [20]This being said, the non-exclusive character of remuneration rights is not a reason for discounting the remuneration. By denying to rights holders who are entitled to remuneration the ability to withhold the use of their property, Parliament only wished to guarantee access to the repertoire. Nothing indicates that Parliament thought the price should be less as a result.

B. THE RANGE

The bottom of the range can be established by doubling SOCAN's commercial radio tariff, or 6.4 per cent of gross revenues before adjustments to account for the ineligible repertoire. That rate would need to be increased to account for greater music use and differences in business models.

Adjusting for greater use does not run contrary to the notion of a blanket licence. The blanket character of the licence makes variations in use irrelevant after the price has been set, not before. There are numerous tariffs which account for different use patterns within that tariff or between tariffs. The Federal Court of Appeal has criticized the Board on one occasion for refusing to account for such differences.[21]

The objectors assert that different business models should not result in different prices, or that different purchasers should not pay different prices for the same input. This is simply incorrect as regards information in general and intellectual property in particular. The whole movie market is premised on the ability to price discriminate. The same is true of performing rights, whose price often is related in part to the importance of music to the activity being carried out. Finally, because of differences in revenue and cost structures, an equivalent price for one type of users may require a higher rate. As commercial radio stations like to point out, an important share of their revenues flow from programming which is not music; this hardly can be said to be an irrelevant circumstance.

The application of these factors would increase the rate at the bottom of the range from 6.4 per cent to somewhere between 15 and 20 per cent.

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[19] *Statement of royalties to be collected by NRCC for the public performance or communication to the public by telecommunication, in Canada, of published sound recordings embodying musical works and performers' performances of such works [Tariff 1.A - Commercial radio in 1998, 1999, 2000, 2001 and 2002]*, August 13, 1999, http://www.cb-cda.gc.ca/decisions/m13081999-b.pdf, pp. 30-32; (1999) 3 C.P.R. (4th) 350, 376-378.
[20] *Id*., 27 (C.B.), 373 (C.P.R.).
[21] *Canadian Broadcasting Corp.* c. *(Canada) Copyright Appeal Board* (1990), 109 N.R. 216, 30 C.P.R. (3d) 269 (F.C.A.).

The top of the range can be set by performing a similar exercise with some of the higher figures (in the order of 60 per cent) put forward by the collectives and discounting them for factors such as the non-exclusive and non-competitive character of music telecommunication rights. This would set the rate at slightly higher than 30 per cent.

C. FACTORS THAT WOULD TEND TO FAVOUR A HIGHER ROYALTY RATE

In the Board's view, several factors tend to favour a rate that is in the higher part of the range.

First, distribution undertakings find DPA valuable. Objectors insist that DPA is relatively unimportant to them. Yet, DTH uses DPA signals to combat grey marketing and develop a competitive edge over cable, while cable operators offer them to match their digital offering to that of DTH. Anything that is perceived as giving a competitive edge or preventing a competitor from gaining such an edge has value. After all, why pay for something unimportant when additional distant radio signals can be retransmitted at no extra cost?

Second, rights holders are entitled to receive additional benefits from new uses of the repertoire. When someone creates new value by using a pre-existing asset, part of the value so created should flow to the owner of the asset. Where that value (which in information industries may sometimes be measured in part by looking at profit margins) [22]is substantial, that flow will tend to be greater. This proposition will come as no surprise to the service providers. In 1995, before the CRTC, Galaxie suggested that as DPA could exist on the leanest of infrastructures because it could rely almost entirely on the pre-existing music repertoire, a substantially higher portion of its gross revenue should flow to rights holders.

Objectors note that the Board once found "... some difficulty in conceding that .. repertoires acquire greater value because a more specialized use is being made of them".[23] This statement is quoted out of context; it was a response to an argument by SOCAN to the effect that niche programming increases the value of music to individual operators. In the present case, what increases the value of the repertoire is not that it is being used in a more specialized way; it is the fact that by its very existence, the repertoire allows a new and profitable use.

Third, the availability of the repertoires helps DPA to achieve efficiencies. Where an increase in productivity directly depends on using a repertoire, rights owners should share in the resulting gains. The remarkable efficiencies achieved by DPA are not solely the result of the judicious use of technology. DPA operations as they stand depend on unimpeded access to the complete repertoire of sound recordings and musical works. These services could not exist if the repertoires were not available.

Fourth, if DPA is a startup industry, it will not remain so for very long. Circumstances have made it so that in Canada, DPA launched more successfully and grew more rapidly than in the United States.

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[22] As stated earlier, pricing in information industries tends to be based on value to thepurchaser, not cost to produce.
[23] Final Report to the Minister of Consumer and Corporate Affaires for 1987, (1987) 15 C.P.R. (3d) 129, 138.

Finally, insofar as this may be relevant, DPA provides foreground services. Some of the distinctions participants attempt to make between background and foreground music are rather tenuous. Factors such as the amount of concentration or attention required to listen to a television signal may be intuitively attractive, but many among us "watch" television while eating or preparing food or doing other activities.

D. FACTORS THAT WOULD TEND TO FAVOUR A LOWER ROYALTY RATE

Some factors tend to favour a rate that is in the lower part of the range.

First, this is a new business. While it may not face economic difficulties, DPA remains in a state of flux. Uncertainty surrounds the future structure of the industry. The nature of the offering also is in a state of flux. The emergence of new competitors remains a possibility. Uncertainty has a price. As collectives share in the productivity gains achieved by DPA, they should expect to share in the price of the uncertainties faced by those who achieve those gains.

Second, collectives are not entitled to appropriate all of the efficiencies achieved by using their repertoires. Even if the availability of the repertoire were the sole reason for the DPA's success (which it is not), the service providers and the distribution undertakings would be entitled to some measure of profit. Service providers, not the collectives, seized the opportunity, took the risks (including the costs of applying to the CRTC) and provided the infrastructure, marketing, etc.

Third, some room must be left for other elements of copyright. Given the nature of copyright, the Board is unable in these proceedings to set a single price for everything that DPA service providers require to make use of sound recordings of music. The Board must assume that those elements, the price of which remains to be determined, such as the reproduction right, have value.

E. FACTORS THAT DO NOT INFLUENCE THE RATE

Participants alluded to a number of factors which, in the Board's view, are not relevant to these proceedings.

Mention was made of possible changes in the regulatory environment, of the emergence of American providers offering a range of services from all music to all talk, and of the impending availability of DPA in cars. It would be premature to take these matters into account. The tariff is being set only until the end of 2002. While imminent or predictable changes may be relevant, the focus should remain on the state of the industry as it stands at the time of the hearing. In any event, account has already been taken of the relative youth and state of flux of the industry.

Neither should any account be taken of the so-called accessory value of DPA in the world of digital offerings. The amount of royalties is a function of the price paid for these signals; presumably, distribution undertakings consider the relative importance of DPA to their business

before deciding whether to buy them, and at what price.[24]

F. THE PRE-DISCOUNT ROYALTY RATE AND THE FINAL ROYALTY RATE

As stated earlier, before accounting for the non-eligible repertoire, the lower end of the range within which the Board intends to set the rate is somewhat less that 20 per cent, while the higher end of that range is somewhat more that 30. In the Board's view, the factors that tend to increase the rate are more important than those that tend to decrease it. Under the circumstances, the Board has chosen a starting point of 26 per cent.

DPA is entitled to use public domain music and non-eligible recordings at no cost. Participants agree that five per cent of musical works used on DPA are in the public domain and that only 45 per cent of sound recordings used on DPA are eligible to share in the remuneration. The rate is discounted accordingly.

The application of these principles yields a rate of 18.2 per cent, i.e.:

$$[((26 \div 2) \times 0.95) + ((26 \div 2) \times 0.45)]$$

Let us recognize that this is the first tariff to apply to this industry. As stated earlier, while DPA has been successful in establishing itself rapidly, these are early days. It is a well-known practice, when valuating companies, to account for the newness of an operation through a "risk" discount. DTH has invested heavily to attract customers by subsidizing hardware; all of this has been done at no cost to rights holders. Given the important share of revenues that rights holders will now receive from these users, it is normal that they share in the risk factor associated with this new industry. Accordingly, a discount of 10 per cent seems appropriate to account for this "newness" factor, bringing the final rate to 16.38 per cent (i.e., 11.115 per cent for SOCAN and 5.265 per cent for NRCC). This discounted rate will apply only for the life of the tariff in this initial phase.

G. THE RATE BASE

For reasons outlined in earlier decisions, the appropriate tariff base is the price paid by distribution undertakings and not the "price" paid by subscribers.[25]

IV. ABILITY TO PAY AND THE RISK OF DROP OFF

In the Board's view, those who are liable for the tariff can afford to pay it.

Ability to pay should be assessed by looking at those who are liable to pay royalties collectively,

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[24] Other issues or factors that are irrelevant to setting this tariff include: the impact of DPA on the sale of sound recordings; the argument that DPA uses a less valuable part of the repertoire; the value of DPA's efforts in "compiling" the repertoire into the various signals; the "rate is not a price" argument.

[25] *Statement of royalties to be collected for theperformance or communication by telecommunication in Canada of musical or dramatico-musical works in 1990, 1991, 1992, 1993, 1994 and 1995*, April 19, 1996, http://www.cb-cda.gc.ca/decisions/m19041996-b.pdf, pp. 17-18; (1996) 70 C.P.R. (3d) 501, 517-518.

not individually. Since the Board cannot apportion the burden of the tariff,[26] then those who share in that burden ought not to be able to debate ability to pay based on the assumption that one of them may be required to shoulder all of that burden. It is up to DPA service providers and distribution undertakings to decide among themselves how the burden of the tariff can be distributed in a way that makes it affordable to both. The fact that affiliation contracts apportion liability for the tariff in a variety of ways serves to confirm that they are able to do this.

In any event, this is not at issue here. DPA service providers make substantial profits, as do most distribution undertakings. The tariff represents a significant but not unreasonable share of DPA's profits. Even if it were to pay the tariff alone, Galaxie (for example) would be left with more revenues per subscriber than it projected when it applied for a licence; furthermore, providers have far more subscribers than expected. The tariff represents less than one-half of one per cent of what typical subscribers to DPA pay for the audio and video package they receive.

DTH are by far the largest purchasers of DPA services. They currently incur deficits. This is the result of an aggressive marketing strategy that involves subsidizing hardware. Rights holders should not have to support the cost of that business choice except to the extent of the rate reduction from 18.2 to 16.38 per cent for the life of this tariff.

The Board does not anticipate any significant drop off as a result of the tariff, even if that were an issue in this case. Signal drop-off matters mostly when it results in a reduction in the basic service. DPA is not part of the basic service that the CRTC requires any distribution undertaking to provide. In these circumstances, users and their clients should be expected to pay for the copyrights they use.

Many participants in the market seem to have already discounted the impact of the tariff. The issue has been the subject of one-on-one negotiations; agreements filed with the Board deal with the final burden of royalties in every manner conceivable. Significantly, many provide for one of the parties to shoulder the payment of the tariff alone, up to an amount that is higher than the one set by the Board.

Past experience shows that distribution undertakings rarely drop a signal once it has been offered to their customers. Furthermore, distribution undertakings no longer have a monopoly over a service area, and any drop-off could be viewed by competing distribution undertakings as an opportunity to differentiate their signal offering. In the long run, bandwidth availability may lead to different results, but this is simply not the case at this point in time.

Changes in the offering of digital signals may result in DPA being repackaged. Currently, DPA is financed solely through affiliation payments that are invisible to the consumer. A higher overall price might result in the price becoming visible. That may or may not be a disadvantage. What is more important, the industry is not there yet.

Finally, contrary to what some of the participants intimated, a rate of this magnitude is not

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[26] *Id.* pp. 37-38 (C.B.); 531-533 (C.P.R.); *Canadian Cable Television Association*. v. *Society of Composers, Authors and Music Publishers of Canada* (F.C.A.) (1997), 75 C.P.R. (3d) 376.

unprecedented. Importers of CD-Rs pay considerably more as a percentage of the wholesale or retail price of such a CD due to the private copying tariff.

V. PHASING-IN AND OTHER PREFERENTIAL TREATMENTS

There is no reason to extend to DPA the advantages afforded by law to commercial radio with respect to the remuneration right of performers and makers. No evidence suggests that a phasing-in of the tariff is necessary, even though NRCC appears prepared to accept one. Parliament afforded radio a preferential treatment to the exclusion of others. The extension of preferential measures always is at the expense of rights holders. Such measures should not be extended further than what Parliament intended unless a solid case is made in favour of such an extension.

VI. THE TARIFF

A. AMBIT OF THE TARIFF

The proposed tariffs target "non broadcast radio services" or "pay audio radio services". During the hearings, some participants focussed on the digital or analog nature of the signals, as well as on whether the signals subject to the tariff should broadcast music exclusively or almost exclusively. Finally, some discussions related to whether the tariff should apply only to licensed services, as opposed to authorized services.

The evidence in these proceedings dealt almost exclusively with digital services. A few distribution undertakings convert the signals into an (analog) FM signal before transmitting them to their customers. These instances must be addressed. Consequently, the tariff targets all pay audio services.

The tariff also applies to all DPA signals, irrespective of their musical content or of their relative use of the repertoire. The rate already accounts for the fact that some signals use the repertoires far less than others.

The tariff should also apply to all signals, including those that are not specifically licensed by the CRTC. Some signals may be authorized without being licensed; it would not serve any purpose to allow for a debate over whether or not they are subject to the tariff. Furthermore, it would be unfair to let potential unlicensed operators gain access to the repertoire for free, while properly licensed operators have to pay royalties for that same access.

It is not the Board's intention that the tariff apply to non-broadcast audio services such as CHCR in Montreal, which distribution undertakings obtain for free. This explains the references to "pay" audio signals in the tariff.

The tariff does not apply to the use of DPA in commercial settings. As was explained in the context of SOCAN Tariff 16, what is important under those circumstances is not the communication *to* the store but the performance *in* the store.[27] Commercial premises that use

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[27] *Statement of royalties to be collected for theperformance or communication by telecommunication in Canada of*

DPA services must pay pursuant to some other relevant tariff, such as Tariff 15 or 16.

B. A SINGLE TARIFF, BUT NOT A SINGLE COLLECTING AGENT

From a legal perspective, when a published sound recording of a musical work is communicated to the public by telecommunication, the rights administered by SOCAN are quite different from those administered by NRCC. When acting individually,[28] authors and composers can control or even prohibit that telecommunication. Performers and makers are only entitled to receive equitable remuneration through a collective society. Still, when the rights over musical works are administered collectively, and for so long as users pay royalties set by the Board, SOCAN and NRCC are, for all practical purposes, in the same situation. Indeed, a single set of provisions sets out how both collectives obtain a certified tariff.[29]

The objectors ask for a single tariff, or at least for a mechanism that allows them to settle all relevant royalties through a single payment. The collectives argue that the Board is legally required to certify separate tariffs.

Users face an increasing number of demands from rights holders. A greater proportion of those whose rights existed before 1997 have started to assert them: requests for tariffs dealing with the reproduction of musical works are a case in point. New rights have also emerged. As a result, users require multiple authorizations or must make multiple payments even where only one "product" (such as recorded music) is used. As well, in the digital environment, the need to licence multiple types of works, each type requiring multiple authorizations, increases.

The Board is concerned with the burden which could result from the multiplication of tariffs. Understandably, users look for one-stop shopping. It makes sense to allow them, where appropriate and where the law allows it, to acquire what is for them a single product through a single payment. Parliament seemed to recognize this when it required that the remuneration to performers and makers be combined in a single payment. Knowing in advance how much "music" costs without the need for complicated calculations encourages transparency.[30] At a minimum, when rights are administered collectively, stating in a single tariff how much each collective society is entitled to get makes it easier for the user to make business decisions.

There are two issues to be addressed: whether to have a single tariff, and whether to collect royalties through a single collecting agent. The Board finds it appropriate to do the first but not, for the time being, the second.

Dealing with both sets of rights in a single tariff raises no particular practical or legal difficulties.

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musical or dramatico-musical works in 1994, 1995, 1996 and 1997, September 20, 1996, http://www.cb-cda.gc.ca/decisions/m20091996-b.pdf pp. 26-28; (1996) 71 C.P.R. (3d) 196, 217-218.

[28] Authors and composers can decide not toadminister their rights collectively; that option is not open to performers and makers.

[29] Sections 67 to 68.2 of the *Act*.

[30] A similar preoccupation with transparency may have led the Copyright Appeal Board to deal with the then two performing rights societies through consolidated hearings and to issue tariffs that were identical in all relevant respects.

Both proposed tariffs are filed pursuant to the same legal regime. The provisions are identical in all relevant respects to those in the retransmission regime, where the Board, originally confronted with several proposed tariffs, certified only one. The retransmission tariff deals in a single document with the remuneration rights for one type of use (retransmission) on all types of works. Here, a single tariff will deal with the remuneration rights of one type of use (public telecommunication of music) over two types of subject matter.

NRCC submits that since each collective is required to file a proposed tariff, the Board must certify each proposed tariff submitted to it. That argument raises doubts about the Board's current practice of dealing with each tariff item separately. If *the* tariff a collective files possesses such integrity, then the Board might be required to hold a single hearing for all the tariff items. This interpretation might also mean that the Board cannot create new tariff items of its own motion, by carving out uses covered by parts of existing tariffs, as was done with SOCAN Tariffs 3.C and 21. Finally, the argument would cast serious doubts on the otherwise solidly established legality of the retransmission tariff which the Board has certified for over a decade. These propositions run contrary to the general economy of the regime.

The matter of consolidating payments raises different issues. In this respect, the objectors all advocate some form of collection system but the collectives have been unable to agree.

From a legal perspective, the issue is not clear cut. If a collective dealing with joint and several debtors cannot be forced to collect royalties from one of them, then it could be argued that no collective can force that choice on the other.

Under the circumstances, the Board chooses not to designate a single collecting agent for both collectives. The tariff will state what each collective is owed, and will leave open the matter of collection. However, the Board finds the practical arguments in favour of designating a single collecting agent compelling. Apparently, NRCC and SOCAN already have some common dealings with respect to commercial radio stations. A decision on the part of the collectives to voluntarily set up an integrated payment system would be constructive.

C. TARGETING

There is considerable disagreement as to whom the tariff should target for the purposes of payment. The services do not wish to be targeted. DTH offer themselves as target. Cable operators are willing to act as they do with respect to non-broadcast television services. All ask that the same target be identified in respect of both collectives. NRCC wishes to target DPA, while SOCAN wishes to target distribution undertakings.

Collecting royalties from either the distribution undertakings or the service providers presents advantages and difficulties in either case. In the end, however, there is no need to review them or to decide the issue. Each collective has the right to seek payment from either the distribution undertaking or the DPA, whether or not the tariff targets one or the other. Each would be perfectly free to seek payment from the distribution undertaking in one instance, and from the service provider in another. Under the circumstances, the only reasonable approach is to say nothing.

This does not mean that the industry is helpless when it comes to deciding who should be the payee of choice. No collective can require that payment be made from anyone before payment is due. That being the case, the debtors would be free to decide who will pay a collective. As long as payment is made on time, then the collective probably has no other choice but to accept it.[31]

From a practical perspective, distribution undertakings already pay retransmission royalties and Tariff 17.A royalties to SOCAN. Under the circumstances, it may be easier for SOCAN to collect all royalties on account of the provision of DPA services from the distribution undertakings. This would offer the further advantage that a distribution undertaking can readily set-off the service provider's share of the royalties against affiliation payments. NRCC's share could then be forwarded to it.

D. DISCOUNT

The retransmission and 17.A tariffs expressly provide for a discount when services are provided to certain institutional premises (e.g., hospitals) and to hotels. Owners of these premises pay less for their cable service. That lower price is not automatically reflected in a tariff that is set at a fixed amount per premises served. In this instance, the tariff is set as a percentage of what distribution undertakings pay for DPA. Distribution undertakings are quite capable to account for the lower price they get from institutional premises in their negotiations with DPA service providers. Therefore, it can be assumed that the rate is self-adjusting and does not require discounting.

E. SMALL SYSTEMS

Subsection 68.1(4) of the *Act* provides that small cable transmission systems are entitled to a preferential rate. That rate was set at $10 per year per system in SOCAN Tariff 17.A.

Previous preferential rates were set at a fixed amount partly because the main rates were themselves set at so many cents per month per premises served. In a tariff that is set at a percentage of a rate base, it seems simpler and fairer to afford the preference required by statute by providing a discount to what would otherwise be payable. For one thing, a preferential rate that is set at a fixed amount necessarily means that the preference afforded gets less important as the system has fewer subscribers.

Small systems shall pay at half the rate of other systems (i.e., 5.56 per cent to SOCAN and 2.63 per cent to NRCC). Anything less may not be sufficient to satisfy the requirement set out in the Act. Anything more is unnecessary given the discretionary nature of the services offered. At the collectives' request, small systems will pay royalties only once a year.

The wording of the definition of "small cable transmission system" was adjusted to take into account the recent *Exemption Order for Small Cable Undertakings* (Appendix I, Public Notice CRTC 2001-121, December 7, 2001).

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[31] Indeed, it may well be that a creditor alwaysmust accept payment in full from either joint and several debtor, even once the debt is due.

F. SOUND RECORDING USE INFORMATION

At first, the Board intended to ask DPA suppliers to provide the collectives with whatever information they maintain pursuant to CRTC requirements. It then appeared that the content of playlists maintained for the purpose of the CRTC was not at all clear. Participants agreed on setting out the specific information that should be maintained for the purposes of the tariff.

There then remained the matter of how much information should be supplied. DPA suppliers argued that requesting anything more than one week six times a year would be cumbersome. The collectives asked for one week per month. The Board remains uncertain as to why the information that is displayed on the subscriber's screen when a musical work is played cannot be systematically supplied to the collectives. Issues of server programming may be involved, which will have to be explored more fully at a later date. In the meantime, DPA suppliers will be required to report for one week each month.

G. FINALIZATION OF TARIFF WORDING

The Board made considerable changes to the wording of the tariff in order to reflect the many and various conclusions reached in the decision. In this respect, cooperation from counsel for the parties was solicited repeatedly. The participants' assistance at this stage of the process helped considerably in arriving at a text that reflected the Board's intentions without raising unforeseen difficulties in its day-to-day application. The Board is grateful for that assistance.

H. TRANSITIONAL PROVISIONS

The tariff contains certain transitional provisions made necessary because the tariff takes effect on January 1, 1997 for SOCAN and January 1, 1998 for NRCC, even though it was approved much later. A table sets out interest factors or multipliers to be used on sums owed in a given month. The multiplying factors were derived using previous month-end Bank Rates covering the period January 1997 to March 2002 as published by the Bank of Canada (rates for March, April and May 2002 were set equal to the current rate). The Board considers that a penalty over and above the interest factor should not be imposed on retroactive payments in this matter, as there was no way for DPA services to estimate the amounts payable until the tariff was approved. Interest is not compounded. The amount owed for any given month is the monthly amount of the approved tariff multiplied by the factor set out for that month. The Board hopes that this will greatly simplify the users' calculations and the collectives' verifications.

Claude Majeau
Secretary General