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Ontario

**Ontario Media
Development
Corporation**

**Société de
développement
de l'industrie
des médias
de l'Ontario**

1 September 2006

Diane Rhéaume
Secretary General
Canadian Radio-television and Telecommunications Commission
Ottawa, Ontario
K1A 0N2

Dear Ms. Rhéaume:

**Re: Broadcasting Public Notice CRTC 2006-72
 Call for Comments
 Future Environment Facing the Canadian Broadcasting System**

Ontario Media Development Corporation (OMDC) is pleased to file the attached comments in connection with Broadcasting Public Notice CRTC 2006-72 calling for comments on a request by the Governor in Council to prepare a report examining the future environment facing the Canadian broadcasting system.

OMDC is an agency of the Ontario Ministry of Culture that facilitates economic development opportunities for Ontario's cultural media industries. As the central catalyst for Ontario's cultural media cluster, OMDC promotes, enhances and leverages investment, jobs and original content creation through a variety of initiatives.

We now proceed to the substance of our submission and comments on the issues raised by the Commission in the Public Notice.

Sincerely,

Kristine Murphy
Chief Executive Officer (A)
Ontario Media Development Corporation

Introduction

1. Ontario Media Development Corporation (OMDC) is pleased to file comments in connection with Broadcasting Public Notice CRTC 2006-72 calling for comments on a request by the Governor in Council to prepare a report examining the future environment facing the Canadian broadcasting system.
2. OMDC is an agency of the Ontario Ministry of Culture that facilitates economic development opportunities for Ontario's cultural media industries, including the book publishing, film and television, interactive digital media, magazine publishing and music industries. As the central catalyst for Ontario's cultural media cluster, OMDC promotes, enhances and leverages investment, jobs and original content creation through a variety of initiatives including co-administration of the provincial tax credits.

Executive Summary

Audio-Visual Technologies and Their Predicted Evolution

3. The Canadian broadcasting industry is currently undergoing a transition from the distribution of analog to the distribution of digital signals. The number of Canadian digital subscribers has doubled since 2001 and will continue to increase. Services such as video-on-demand and broadband Internet are proliferating along with increased digital services, giving today's television audiences more options for accessing programming than ever before. The challenge will be for broadcasters and producers to continue to provide quality programming in as many platforms as possible, while at the same time finding ways to develop viable business models.

Use of Audio-Visual Technologies

4. Canadian audiences not only have more programming choices, they also have more options for ways to spend their leisure time. Seventy-two percent of all Canadians are Internet users and 56% are online seven or more hours per week. Internet users tend to spend less time than non-users watching television, and as 90% of Canadians aged 18-to-24 are online, this could have a significant impact on the television audience of the future.
5. Early and widespread adoption of the Internet meant that Canada once led the world in broadband penetration; however, this lead is beginning to slip. Canada is also lagging behind other countries in terms of adopting wireless technology. Until such time as the latest wireless technology is widely available in North America, the demand for programming delivered to handheld devices will continue to remain low. Producers and broadcasters are currently producing shorter programs that are more suitable for viewing on smaller screens and are sure to continue to adapt to and experiment with these new programming options.
6. While it is more than likely that the spread of wireless and broadband technology will lead to increased consumption of television programming over the Internet, through cell phones or over a wireless network, the fact remains that television distribution by satellite, cable and fixed wireless is quite efficient and will remain the dominant distribution system for television programming. While broadcasters strive to maximize the potential revenue opportunities that will come from the new viewing options that will be available to audiences, they must also ensure that independent producers are fairly compensated for the use of their intellectual property. If need be, the

regulator could consider ensuring that producers are not being unfairly pressured by broadcasters to sign away their digital and territorial rights without adequate compensation.

7. The growth in the digital universe is translating into growth in the audience for specialty channels and a corresponding increase in the specialty channels' share of the television advertising market. Internet advertising is also beginning to grow at double digit rates. Video-on-demand (VOD) and Digital Video Recording (DVR) services give consumers the ability to bypass advertising altogether. Conventional networks seeking to maximize advertising revenue in this environment must adapt to these realities and become even more creative in delivering audiences to advertisers.

Implications for Independent Producers

8. The proliferation of specialty channels and the programming these channels require has had both positive and negative consequences for producers. The demand for content has expanded at a much faster rate than has the pool of money available. These means that licence fee negotiations between broadcasters and producers are becoming increasingly difficult, with broadcasters exerting downward pressure on the value of licence fees and upward pressure on the number of rights they are trying to acquire for those fees. This is especially true for programs produced in high-definition.
9. Independent producers are becoming adept at navigating the multi-window and multi-platform universe that is today's broadcasting environment. Many are already developing products that are intended for online distribution or distribution through mobile devices and are clearly ready and able to face the challenges and take advantage of the opportunities presented by new technologies. However, producers cannot be expected to bear the costs of dealing with these challenges alone; broadcasters must bear their fair share.
10. As delivery of programming over the Internet increases, the CRTC may wish to re-consider some of the assumptions about Canadian content and the impact of Internet distribution on over-the-air broadcasters that underlie the current new media exemption order.

Methodology

11. OMDC sent an electronic survey to all the film, television and interactive digital media clients in its corporate database. Thirty-three responses were received to this survey, representing a 12.4% return rate. A follow-up in-person consultation was then held on August 3, 2006 to elicit more detailed responses from the producers.
12. OMDC staff also consulted a wide variety of published research on the subject of the current state of the broadcasting industry and its predicted evolution. All sources are noted throughout the submission.

Audio-Visual Technologies and Their Predicted Evolution

13. The Canadian broadcasting industry is currently undergoing a transition period from the distribution of analog to the distribution of digital signals. In its 2006 *Broadcasting Policy Monitoring Report*, the Canadian Radio-television and Telecommunications Commission (CRTC) identified three stages for this transition. The first stage is characterized by the distribution of both analog and digital signals by a Broadcasting Distribution Undertaking (BDU). Most cable companies are currently in the first stage.¹ Satellite services are for the most part in the second stage, offering subscribers a mix that consists predominantly of low definition digital services with some high definition services. The third stage of the transition will be entered when high-definition digital signals predominate. This will not happen until consumer demand for high-definition programming has increased.
14. Between 2001 and 2005, the number of Canadian digital subscribers doubled to 5.3 million subscribers, representing 44 percent of TV households. Demand for digital services is being driven by increased programming and the increasing popularity of high-definition programming. Service providers are also encouraging consumer take-up by offering convenience and cost savings with bundling packages that include broadband Internet and telephone services. PricewaterhouseCoopers (PwC), in its most recent *Global Entertainment and Media Outlook*, predicts that there will be 9.3 million digital households by 2010, representing nearly three-quarters of all TV households in Canada.²
15. The increased penetration of digital cable has also led to an increased popularity of video-on-demand (VOD) services. The percentage of digital cable subscribers that use VOD has grown from less than 10 percent in 2002 to nearly 36 percent in 2005. These subscribers spent \$83 million on VOD services. Based on these take-up rates and the experience of VCR and DVD penetration, PwC predicts that total VOD spending will reach \$356 million by 2010, representing 61 percent of digital cable households.³
16. Canada also leads the world in the deployment of cable networks, which in turn has led to widespread adoption of broadband Internet access. Canada is ranked first among OECD countries in terms of cable Internet penetration. Currently, over 11.1 million Canadian homes – or 93.5 percent of the homes equipped with cable – have high-speed cable Internet access available to them, and there are over 2.8 million subscribers to the service.⁴ This represents 71 percent of all Internet subscribers in Canada, and the attraction of faster speeds and high-volume applications such as music downloads and online video games will continue to attract subscribers to broadband, so much so that PwC predicts that broadband household penetration will rise to nearly 80 percent of all Canadian households by 2010.⁵
17. Digital television services and access to broadband Internet services mean that today's television audiences can access programs in many different ways. While some viewers are content to view

¹ *Broadcasting Policy Monitoring Report, 2006*, Canadian Radio-television and Telecommunications Commission, 30 June 2006, p. 75.

² PricewaterhouseCoopers *Global Entertainment and Media Outlook: 2006-2010*, 2006, p. 159.

³ *ibid.*, p. 217.

⁴ Telecommunications Policy Review Panel, *Final Report*, March 2006, p. 1-5.

⁵ PwC, *Outlook*, p. 364.

programs at the time and in the way that the broadcasters decide, other viewers are seeking more control over their viewing experience. This means that, “for the short- and mid-term future, the TV industry will be marked by a bimodality among consumers: those who are mainly passive viewers and those who demand a more interactive media experience.”⁶ The challenge will be for broadcasters and producers to continue to provide the same amount quality programming in as many platforms to reach as many audiences as possible, while at the same time finding ways to develop viable business models for each of the platforms.

Usage of Audio-Visual Technologies

18. In addition to their increased programming options, Canadian audiences have many more options for ways to spend their leisure time than ever before. Seventy-two percent of all Canadians are Internet users, spending an average of 13.5 hours per week online. The majority of Canadians are also heavy Internet users, with 56% being online seven or more hours per week. While Internet users spend slightly fewer hours per week than do non-users accessing certain traditional media, such as television, radio, magazines and newspapers, overall the Internet appears to supplement rather than replace more traditional use. All Canadians spend significant amounts of time watching television, listening to music and listening to the radio. However, Internet users spend the largest portion of their media time on the Internet, while non-users spend the largest portion of their media time watching television. Internet users spend less time than non-users with television, radio, magazines and newspapers, but they still spend a considerable amount of time with all of them. They also spend slightly more time than non-users reading books, going to the movies, watching movies at home, listening to music offline and talking on their cell phones. It appears as if the Internet serves more as a supplement to traditional media than a replacement, with Internet users being more media-oriented than non-users.⁷
19. That being said, younger users are more likely than older users to report that Internet use has decreased their television viewing. And since 90% of Canadians aged 18-to-24 are online, this could have a significant impact on the television audience of the future. Heavy users are also more likely to report a decline in television viewing and those in the 18-to-24 age category are online more than 17 hours per week.⁸ As Canadians in this age bracket continue to develop media habits that include lower levels of television viewing, broadcasters may find that their audiences are continuing to shrink and will find it increasingly difficult to generate ad revenue from those audiences.
20. Among the countries participating in the World Internet Project, Canada is second only to the United States in terms of Internet use (76% to 72%).⁹ Canadians were also some of the earliest users of the Internet, along with early adopters in the United States and Sweden. Globally, the amount of time users spend on the Internet is relatively high in Canada and the United States, where users are

⁶ IBM Business Consulting Services, *The End of Television as We Know It: A Future Industry Perspective*, IBM Institute for Business Value, January 2006, p. 11.

⁷ *Canada Online! A Comparative Analysis of Internet Users and Non-Users in Canada and the World: Behaviour, Attitudes and Trends 2004*, Canadian Internet Project (Charles Zamaria, André H. Caron, Fred Fletcher), October 2005, pp. 69-71.

⁸ *ibid.*, p. 37

⁹ *ibid.*, p. 11.

predominantly heavy users who spend the most time online. This is also true in Germany, Spain and South Korea.

21. Early and energetic adoption of the Internet meant that Canada once led the world in broadband penetration. Until 2003, Canada ranked second among OECD countries in terms of broadband subscribers per 100 inhabitants but by June 2005 that rank had fallen to sixth. Canada is also lagging behind other countries in terms of adopting wireless technology: wireless penetration in Canada ranks second last in the OECD, and represents fewer than 50 subscribers per 100 inhabitants.¹⁰ Today there are significantly more wireless service subscribers in the world than fixed wireline subscribers. Canada, and to a lesser degree the United States, has fallen far behind European countries in the implementation of wireless services and especially in the implementation of third-generation (3G) high-speed data services. To date, 3G rollout has only taken place in a limited way in a few large Canadian cities. It is 3G technology that will enable Canadians to use their portable devices for accessing more and higher quality content, including television programming and video games.
22. Until such time as this technology is widely available in North America, the demand for programming delivered to handheld devices will continue to remain low. The results of a recent poll published in the *Los Angeles Times* indicate that about half of young adults and four in 10 teenagers, the two groups one would expect to be most interested in the possibilities of new technology, said they were uninterested in watching television shows or movies on computers, cell phones or handheld devices such as iPods. The two main reasons given for this disinterest were the cost and the uneven quality of the experience.¹¹ As wireless technology improves and becomes more prevalent, the quality of the wireless content is likely to improve and the cost is likely to decrease, undoubtedly leading to increased demand. Until this happens, producers and broadcasters are experimenting with shorter programs that are more suitable for viewing on smaller screens. These may be spin-offs from existing programs or may be stand-alone properties. The production values for these programs are quite different from conventional broadcasts as producers need to consider things like the size of the viewing frame.
23. While it is more than likely that the spread of wireless and broadband technology will lead to increased consumption of television programming over the Internet to a personal computer, through cell phones, or over a wireless network to some sort of other handheld device, the fact remains that television distribution by satellite, cable and fixed wireless is quite efficient and will remain the dominant distribution system for television programming.¹² Broadcasters and BDUs will be able to rely on the revenue generated by their current business practices for the next few years.
24. However, this is also the time for broadcasters and BDUs to start thinking about the future. They must begin to explore opportunities to maximize revenue from new audience viewing options. And they must ensure that they treat the independent producers who supply the content that attracts those new audiences fairly. Independent producers are creative entrepreneurs who can adapt to the needs of broadcasters attempting to reach audiences in a digital universe. However, they should be fairly compensated for the use of their intellectual property. Broadcasters who wish to purchase ancillary and territory rights for the purposes of exploitation should ensure that producers are properly compensated for those rights. Broadcasters who wish to lock up ancillary rights because they may be

¹⁰ Telecommunications Policy Review Panel, *Final Report*, March 2006, p. 1-12.

¹¹ "No Big Demand for Small Screen," by Matea Gold, *Los Angeles Times: latimes.com*, August 10, 2006.

¹² Nordicity Group Ltd., *Green Paper: The Future of Television in Canada*, Prepared for the Banff World Television Festival 2006, June 8, 2006, p. 14.

able to exploit them at some future time should consider leaving those rights for producers who may wish to explore opportunities for exploiting those rights immediately. Ancillary rights should not be locked up for indefinite periods of time if no one is exploiting them. If broadcasters will not engage in this fair and equitable behaviour on their own, then it is the role of the regulator to step in and ensure that producers are not being unfairly pressured by broadcasters to sign away their digital and territorial rights without adequate compensation.

Impact on the Broadcasting System

25. Digital technology is influencing virtually every segment of the entertainment and media industry. This growth in the digital universe is translating into growth in the audience for specialty channels as more people have access to those channels. As audiences move to the specialty channels, so does a share of the television advertising market. Over the past five years, advertising on specialty channels has risen at double-digit annual rates, including an increase of 13.2 percent in 2005. Over-the-air networks attracted 74 percent of television advertising in 2005, but the growth on this side of the market has slowed considerably, dropping to a rate of 0.8 percent in 2004 and 1.1 percent in 2005.¹³ Internet advertising is also beginning to grow at double digit rates, although it has not yet replaced advertising in traditional media. Major advertisers are increasingly turning to online options as a way to allow individual consumers to delve into content in non-linear ways that are more responsive to their interests and needs than traditional television programming. Internet advertising rates on a per-user basis do not yet match those of television's per-viewer rates, but television networks will need to adapt if they wish to remain a credible and cost-effective advertising vehicle.¹⁴
26. The CRTC's own audience figures reflect the decline in advertising revenues for conventional television but also suggest that this decline may have leveled off for the time being. Audience growth for English-language pay and specialty service has slowed but nevertheless increased to a 37.6% viewing share in 2005. The 29.4% viewing share achieved by English-language private Canadian conventional services in 2005 is consistent with the level of previous years and indicates that the downward trend in these stations' audiences has leveled off since 2000-01.¹⁵ These numbers indicate that in spite of the new channels and new options available to audiences, there is still a place in the broadcasting universe for the conventional stations. These stations will have the advantage of using their established positions to launch themselves into the new multi-channel, and multi-platform, universe.
27. In addition to competition from the Internet and specialty channels, broadcasters also face challenges from the new technologies that are part of the packages of services offered by BDUs. Video-on-demand (VOD) and Digital Video Recording (DVR) services offered by cable and satellite companies give consumers the ability to bypass advertising altogether. DVR technology is already having an impact on the television advertising market globally:

As the DVR makes advances – not just in the U.S., but also the U.K., Germany, France, Spain and Italy – ad skipping is taking off as, one by one, viewers opt out of advertising content. Ad skipping is expected to lead to losses of 6 percent in U.S. TV annual advertising revenues in

¹³ PwC, *Outlook*, p. 159.

¹⁴ Nordicity Group Ltd., *Green Paper*, p. 11.

¹⁵ *Broadcasting Policy Monitoring Report, 2006*, CRTC, p. 44.

2009. Even with a slower roll-out in other regions, DVRs are still expected to have a material impact on advertising, with depressed annual revenues ranging from 2.4 percent in Germany to 6 percent in the U.K. in 2012.¹⁶

Broadcasters seeking to maximize advertising revenue in this environment must become even more creative in delivering audiences to advertisers. The increasing prevalence of product placement in television programming is an example of this creativity. The broadcasters who will be most successful in retaining market share in the coming years will be the ones who are most successful in finding the workable business models out of the many that are being experimented with in a variety of digital platforms.

Implications for Independent Producers

28. The proliferation of specialty channels and the programming these channels require has had both positive and negative consequences for producers. On the one hand, the never-ending search for content has meant there is a need for more programming. Unfortunately, the pool of money available for such programming has not expanded at the same rate, so licence fees are not keeping pace and cover smaller portions of program budgets. Intense competition for audiences also means that broadcasters are even more focused on acquiring programs that will deliver large audiences. A 2004 study commissioned by the British Television Distributors' Association summarized the situation well:

The proliferation of new channels with thousands of hours of airtime to fill has boosted demand for international programming. However, the impact on program acquisition prices has been double-edged. The combination of low program budgets for the new channels and increasing viewer scarcity has exerted deflationary pressure on the prices paid for the majority of "readily-substitutable" programming.¹⁷

These means that licence fee negotiations between broadcasters and producers are becoming increasingly difficult, with broadcasters exerting downward pressure on the value of the licence fee and upward pressure on the number of rights they are trying to acquire for those fees. Most of the producers who responded to the OMDC survey identified this pressure as one of the greatest challenges they face in operating their businesses. It is a universal concern that needs to be addressed by the industry and its funding bodies, including the relevant federal and provincial departments and their related agencies. The regulator should be aware of the impact its decisions has on these bodies in order to ensure that an integrated approach to support for the broadcasting system is maintained.

29. Independent producers are becoming adept at navigating the multi-window and multi-platform universe that is today's broadcasting environment. Many are already developing products that are intended for online distribution or for distribution through cell phones and other mobile devices. All of the survey respondents currently producing traditional television programs and films indicated that

¹⁶ IBM Business Consulting Services, *The End of Television as We Know It*, p. 4.

¹⁷ Television Research Partnership, Tim Colwell and David Price, *Rights of Passage: British Television in the Global Market*, Commissioned by the British Television Distributors' Association and U.K. Trade & Investment, September 2004, p. 10.

they intend to continue doing so over the next three years. But in addition to the continuation of these core business activities, the survey respondents also indicated the following plans for the future:

- more than twice as many respondents than are currently doing so are planning to produce programs intended for online distribution in the next three years;
- 50 more respondents than are currently doing so intend to produce interactive products intended for online distribution in the next three years;
- almost three times more respondents than are currently doing so are planning to produce programs intended for distribution through cellular phones or mobile devices in the next three years; and
- twice as many respondents than are currently doing so are planning to produce interactive products intended for distribution through cellular phones or mobile devices in the next three years.

These Ontario producers are clearly ready and able to face the challenges and take advantage of the opportunities presented by the new technologies that are part of today's broadcasting world. However, producers cannot be expected to bear the costs of dealing with these challenges alone. Broadcasters who wish to exploit new programming opportunities need to increase the licence fees they pay for all the programming they are acquiring, no matter how it is delivered to the audience.

30. One obvious area where licence fees are not keeping pace with production costs is High-Definition Television (HDTV). All of the surveyed producers who indicated they are producing HD programming for broadcasters also said this programming is more expensive to produce, with more than half (53%) indicating that HDTV programs cost between 21 and 50% more than standard programs. At the same time, 90% of those producers said that these costs are not covered by broadcasters through increased licence fees.
31. Producers are also bearing the costs of a more complex development process. In addition to the traditional elements of program development, producers must now also take into account new delivery platforms and new elements such as interactivity that may need to be integrated into traditional programs. While producers are incurring greater costs for this increased complexity, there are not yet revenue models for these additional features and broadcasters are attempting to acquire these features for free. Since no one yet knows what the features are worth, policies that require "fair market value" for exploitation of intellectual property in order to access government funding are virtually meaningless. During this time of transition, there may be a more active role for the regulator to play in ensuring that broadcasters treat all producers fairly and equitably.
32. As delivery of programming over the Internet increases, this could have profound implications for independent producers and the entire Canadian broadcasting system. Since the Internet is unregulated by the CRTC, there are no domestic expenditure or Canadian content safeguards. In the proceedings that led to the exemption order for new media broadcasting undertakings in 1999, the Commission considered the availability and the visibility of Canadian content online as well as the potential impact of Internet programming on over-the-air broadcasters. At that time the Commission felt that there would be a strong Canadian presence on the Internet and that the impact on broadcasters' advertising revenue would be minimal.¹⁸ The Commission's 2003 Report to the Governor General in Council on

¹⁸ *Broadcasting Public Notice CRTC 1999-84: New Media*, 17 May 1999 and *Public Notice CRTC 1999-197: Exemption order for new media broadcasting undertakings*, 17 December 1999.

Internet retransmission also considered the implications of widespread program delivery for the protection of programming rights on broadcasters and producers. At that time, Internet programming was seen as a complement to rather than a replacement for television broadcasting.¹⁹ While the complementary nature of Internet programming is unlikely to change in the near future, its increasing popularity and the corresponding growth in share of Internet advertising revenues is challenging some of the assumptions made in the original new media exemption order. The current review is an excellent opportunity for the Commission to reconsider some of those assumptions.

Conclusion

33. Canadians and the Canadian broadcasting system have shown themselves to be willing to adopt emerging communication technologies. Canadians use the Internet more than most people in the world and broadband penetration is widespread throughout the country. Broadcasters are already exploring the new options being presented to them by digital distribution and producers are demonstrating that they are up to the task of providing innovative programming. The challenge for the future will be in determining which programming and delivery options are commercially viable while ensuring that all involved receive appropriate compensation for the production and distribution of their cultural products.

¹⁹ *Broadcasting Public Notice CRTC 2003-3: Internet retransmission: Report to the Governor General in Council pursuant to Order in Council P.C. 2002-1043*, 17 January 2003.