

COMMENTARY

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Canadian Content Is Dead; Long Live Canadian Content!

by Steven Globerman

The current dispute between Netflix and the CRTC, ostensibly arising from Netflix's refusal to provide the CRTC with confidential subscriber data, could ultimately be settled in court. The essential issue that the court would address is whether the activities of Internet broadcasters are covered by the Broadcasting Act (Brownell, 2014a, September 23).

To date, the CRTC has chosen not to apply to Internet broadcasters the same regulations that conventional broadcast distributors must obey. The latter include Canadian content programming quotas, as well as obligations to fund domestically produced entertainment programming.¹ Notwithstanding the exemption it has

given Internet broadcasters thus far, the CRTC believes it has jurisdiction over the Internet and, hence, over Internet broadcasters such as Netflix.

If the dispute between Netflix and the CRTC does go to court, the court's decision regarding the CRTC's jurisdiction over the Internet is likely to be decided on relatively narrow and legalistic interpretations of the Broadcasting Act. In fact, the dispute presents a timely opportunity for government policymakers to address the issue of whether fundamental changes should be made to the way that broadcasters are regulated, with the option that existing regulatory and legal barriers be dismantled so that open and fair competition in broadcasting can be given serious consideration.

¹ For a full discussion of rules and regulations applied to Canada's broadcasting industry, see Globerman, 2014.

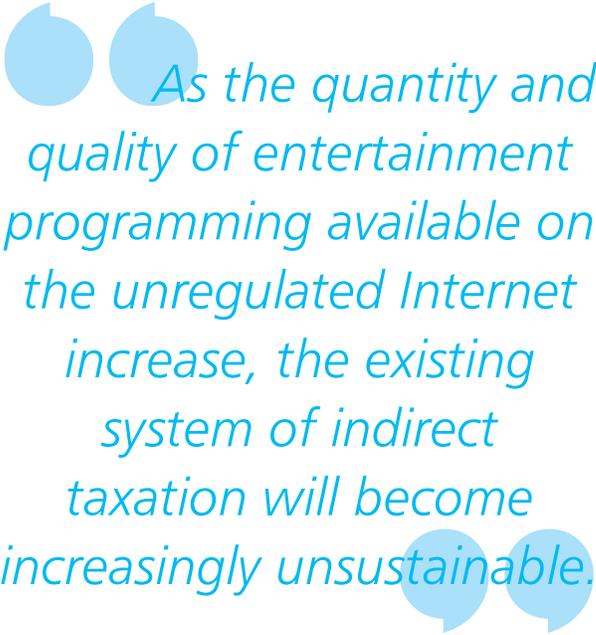
While it appears that the Harper government is disinclined to consider proposing fundamental changes to broadcast policy at this time, it is only a matter of time before such changes will have to be made. This is because “indirect taxation” is the financial basis upon which current broadcast policy rests, and increasing competition from unregulated Internet broadcasters will undermine the existing regime of indirect taxation.

At present, regulated broadcast distributors are required to distribute more Canadian content than they would freely choose to do because of Canadian content quotas and the preponderance and simultaneous substitution rules that the regulation imposes. Cable and satellite broadcasters are also mandated by Canada Heritage to contribute funding to the Canadian Media Fund. The latter is a non-profit agency that finances content creation for the television and digital media industries.² These rules and regulations force Canadian broadcasters to carry more Canadian content than they would like to do, and to fund more Canadian content than they would find profitable to fund.³ The quid pro quo is that Canadian broadcast distributors are protected from direct competition in the form of signals generated by US broadcasters. Preponderance rules also mean that Canadian program producers are more likely to have their programs carried by Canadian cable and satellite distributors than would otherwise be the case which, in turn, generates revenues for those producers. The revenues arguably are paid for by Canadian subscribers who are obliged to buy access to packages that contain those programs. In addition, the simultaneous substitution rule and the provi-

² For a full discussion of regulations and other rules applying to the Canadian entertainment industries, see Globerman, 2014.

³ Were this not the case, content regulations and the like would not be necessary.

sion of the Income Tax Act that prohibits Canadian companies from deducting as an expense any advertising purchased on a non-Canadian broadcasting outlet primarily to reach Canadian audiences both generate additional revenue for Canadian broadcast distributors which, in turn, provides the financing needed for broadcasters to meet their regulatory obligations.



As the quantity and quality of entertainment programming available on the unregulated Internet increase, the existing system of indirect taxation will become increasingly unsustainable.

In effect, Canadian broadcast policies rest on the ability of domestic broadcast distributors to earn net revenues above those that would be earned in a competitive market and then to use those additional net revenues to subsidize the production and distribution of Canadian content. As the quantity and quality of entertainment programming available on the unregulated Internet increase, the existing system of indirect taxation will become increasingly unsustainable. Simply put, the unregulated portion of the broadcast industry can escape the cost burdens borne by the regulated portion of the industry, which provides the former with a competitive advantage that can help Internet broadcasters “compete

away” customers from “conventional” broadcasters. The resulting loss of revenue suffered by cable and satellite broadcasters will undermine their financial ability to meet their regulatory obligations.⁴

Cultural nationalists might argue that the system of indirect taxation is sustainable if Internet broadcasters are regulated in the same way as conventional broadcasters. Such regulation of the Internet would require a substantial expansion of the size and scope of the CRTC, and it is technically feasible, as evidenced by the censorship of the Internet carried out in countries such as China and Iran.⁵ Whether Canadians would accept Internet censorship as readily as they have accepted existing restrictions on their access to foreign broadcast signals and programming is a matter of speculation. What is less a matter of speculation is that the regulatory regime outlined above has fundamentally failed to achieve its ostensible public policy objectives and has evolved into an inefficient device to redistribute income from consumers and taxpayers to a relatively small number of participants in Canada’s broadcast and entertainment industries.

The ostensible goal of the legal and regulatory regime surrounding the broadcast industry is to promote the output of Canadian content and thereby strengthen Canada’s “national identity.”⁶ While the concept of national identity has never been clearly defined by the government or the

regulator, there is substantial evidence that Canadians do not consider Canadian entertainment programming or Canadian entertainers as prominent national symbols or sources of pride in the nation. Institutions such as Canada’s health care system and multiculturalism rank much more highly as relevant national symbols for Canadians.⁷ Furthermore, the frequently

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heard argument that Canadian producers of entertainment programming cannot compete against US producers because of the smaller size of the Canadian domestic market ignores the important changes that digital technology has wrought upon the industry. In particular, the costs of producing and distributing entertainment content have decreased substantially over the past two decades, such that small production companies, and even individual entertainers, can gain international audiences operating from small domestic markets and on very limited budgets.⁸

⁴ Canadian cable companies are well aware of this threat. See, for example, Brownell, 2014b, September 9.

⁵ These two examples are chosen quite deliberately to illustrate the inevitable risk to political freedom that arises from censoring information available to society.

⁶ A representative statement of this fundamental position is the claim attributed to Tom Hennighan that “if Canada stops supporting its culture, it will be endangering its survival as an independent nation” (1996: 3).

⁷ For a discussion of some relevant evidence, see Globerman, 2014.

⁸ Bill Gates has been quoted as saying that putting an hour of video online cost US \$400 in the late 1990s, while today it costs around two cents (*Economist*, June 29, 2013).

This is not to deny that entertainment programming featuring major stars and relatively large budgets still account for the largest share of revenues of the entertainment industry. However, there is no reason to believe that “blockbuster” entertainment programs geared for worldwide audiences do more to promote Canada’s national identity than does more specialized programming geared to niche markets that deal with identifiable Canadian institutions and issues. Furthermore, there is no firm basis for arguing that the production of blockbuster entertainment programming has a larger impact on the Canadian economy than the production of a much larger number of relatively specialized programs.⁹

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In weighing the available theory and empirical evidence, a strong case can be made that regulation of Internet broadcasting is exactly the wrong policy for the government to pursue, although it would clearly mean a larger budget for the regulator, which creates an incentive for the regulator to expand the scope of its activities into Internet broadcasting. At the same time, Canada’s conventional broadcasters have a legitimate complaint that meeting the regulation imposed upon them, but not imposed on Internet broadcasters, puts them at a competitive disadvantage, and the asymmetry invites the possibility of inefficient competition. The preferred policy option in this context is to deregulate the conventional broadcasting sector. In particular, Canadian content rules should be eliminated along with requirements that cable and satellite distributors carry a preponderance of Canadian programs. Foreign ownership restrictions in broadcasting should be eliminated, which would expose existing broadcast distributors to the threat of unwanted takeovers by more efficient foreign companies. The latter initiative would further increase de facto competition in the broadcast industry.

In recommending the full deregulation of broadcasting, it must be acknowledged that a certain share of “public service” programming might be jeopardized were the indirect system of taxation described earlier to be eliminated. While there is no evidence that there would be too little of such programming produced and distributed were existing broadcast regulations eliminated, the preferable way to encourage production of programming that indeed better informs Canadians about their political and social institutions is through direct subsidization of such programming with the costs paid from general tax revenues. While it is beyond the scope of this essay to discuss the role of the CBC in a deregulated

⁹ For a discussion of how commercially profitable, albeit relatively low cost TV programming can be created, see Winter, 2013.

environment, I have suggested elsewhere that the CBC might be a more efficient instrument for identifying and distributing programming of a “public goods” nature than regulated privately owned commercial outlets (Globerman, 2014).

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