



Broadcasting Public Notice CRTC 2007-53

Ottawa, 17 May 2007

Determinations regarding certain aspects of the regulatory framework for over-the-air television

In this public notice, the Commission sets out its determinations regarding certain aspects of the regulatory framework for Canadian over-the-air (OTA) television. The Commission's key determinations include the following:

- *The Commission will not adopt a fee for the carriage of OTA television stations by broadcasting distribution undertakings (BDUs).*
- *The Commission will increase the number of advertising minutes that OTA television stations may broadcast. Specifically, it will increase the 12 minute per hour limit on traditional advertising to 14 minutes per hour in peak viewing periods (7 p.m. to 11 p.m.) effective 1 September 2007. The limit will be increased to 15 minutes per hour for all viewing periods effective 1 September 2008, and eliminated altogether as of 1 September 2009.*
- *Television licensees will be authorized to broadcast only digital OTA signals after 31 August 2011, although exceptions may be made in northern and remote communities where analog transmissions will not cause interference.*
- *The Commission will examine Canadian programming expenditure plans and exhibition commitments by licensees at the time of licence renewal.*

This public notice is one of two issued today following the Commission's examination of issues set out in Broadcasting Notice of Public Hearing 2006-5, and that were considered at a public hearing in the National Capital Region that began on 27 November 2006. The other public notice is A new policy with respect to closed captioning, Broadcasting Public Notice CRTC 2007-54, 17 May 2007.

Introduction

1. In Broadcasting Notice of Public Hearing 2006-5 (the OTA Notice), the Commission announced it would hold a public hearing commencing on 27 November 2006 to examine certain elements of the regulatory framework for over-the-air (OTA) television, and invited comments on the issues set out in the OTA Notice.
2. In the OTA Notice, the Commission described current developments in technology and expressed its view that forthcoming changes in technology and in viewer demands and behaviour may yet have the greatest impact on OTA television.

3. Accordingly, the Commission stated:

In order for OTA television licensees to prepare for the upcoming renewals of their licences, it is appropriate for the Commission to seek public comment, on an industry-wide basis, on how Canadian OTA television should respond to the pressures for change. The regulatory framework for television is based on a balance between ensuring appropriate contributions to the social and cultural objectives of the [Broadcasting] Act while creating conditions for a healthy private sector. Ensuring that this balance is appropriately calibrated given the existing and expected structure of the industry will be the underlying goal of this proceeding.

4. In the OTA Notice, the Commission also indicated that while certain aspects of the regulatory framework for the OTA television sector, such as Canadian programming expenditures, advertising regulations, and the transition to digital, would be considered in this proceeding, the Commission was not reviewing the 1999 Television Policy¹ in its entirety. The Commission stated that it considered that those aspects of the 1999 Television Policy not identified for review in the OTA Notice remained appropriate.

5. Finally, the OTA Notice set out the following objectives for this review:

- A. To ensure that OTA television licensees contribute, in the most effective manner possible, to the production, acquisition and broadcast of high quality Canadian programming that attracts increasing numbers of viewers.
- B. To provide Canadian OTA television licensees with greater clarity regarding regulations that affect certain costs and revenues so that they are in a position to propose maximum contributions to the production, acquisition and broadcast of high quality Canadian programming.
- C. To examine options for the most effective means of delivering Canadian digital/high definition (HD) television to Canadians.
- D. To examine the current and future economic status of small market television stations.

6. The Commission received several hundred written comments in response to the OTA Notice, and 54 parties made oral presentations at the hearing. Participating parties included members of the public, unions and guilds, commercial and not-for-profit television broadcasters, licensees of broadcasting distribution undertakings (BDUs), representatives of the independent production industry, and other stakeholders. The public record of this proceeding, which includes the comments and supporting evidence submitted by the parties, is available on the CRTC Web site at www.crtc.gc.ca under "Public Proceedings."

¹ *Building on success – A policy framework for Canadian television*, Public Notice CRTC 1999-97, 11 June 1999

7. After considering all of the written and oral comments made in the course of this proceeding, the Commission finds there are three primary issues and some secondary issues to be addressed in its determinations:
- What are the most appropriate measures to ensure that OTA television broadcasters have sufficient revenues to maximize contributions to the production, acquisition and broadcast of high quality Canadian programming?
 - What is the most effective regulatory approach to ensure that Canadians have access to digital/HD television?
 - What are the most appropriate mechanisms to ensure that OTA television licensees contribute in the most effective manner possible to the production, acquisition and broadcast of Canadian programming?

Secondary issues:

- Does the Commission's current approach to small market OTA television stations remain appropriate?
- Should there be any changes to the benefits policy?

Sufficient revenues for OTA broadcasters

8. In the OTA Notice, the Commission stated that between 1998/99 and 2004/05, Canadian pay and specialty services increased their share of viewing from 23% to 35.8%, while the viewing share for OTA television services decreased from 47.2% to 41.4%. However, the Commission notes that much of the decline in OTA viewing share occurred early in this period, and it has remained at between 40%-42% since 2002/03. According to BBM/Neilson metered data, OTA television services captured approximately 40% of all viewing in 2005/06. Therefore, it is important to emphasize the key role that the OTA television sector continues to play in the Canadian broadcasting system, both in terms of audience reach and support for Canadian programming.
9. While viewing to pay and specialty services, as a sector, is approaching that of the OTA sector, this viewing is spread over dozens of channels. Conversely, the vast majority of viewing to OTA television is to nine conventional services: CTV, CanWest MediaWorks Inc.'s (CanWest's) Global and CH brands, CHUM Limited's (CHUM's) City and A-Channel stations, TVA, TQS and the Canadian Broadcasting Corporations' (CBC's) English- and French-language services. Therefore, while conventional television represents only a small fraction of the television channels now available to most television viewers, individual OTA television services continue to attract the largest audiences and, therefore, the most significant advertising revenues.

10. It is because of this ability to attract mass audiences that OTA television remains the dominant force in the provision and production of Canadian programming. OTA television broadcasters accounted for approximately \$1.2 billion of spending on Canadian programming, or 57% of the \$2.1 billion spent on Canadian programming by all Canadian licensees, in 2005-2006.
11. OTA television stations also play a vital role in the broadcasting system by providing local television programming that reflects the interests and needs of the communities they are licensed to serve.
12. Yet, in spite of its key role in the broadcasting system, this sector faces a number of challenges. With audience fragmentation and technological changes, OTA stations will continue to experience a decline in audience share, major changes in the form and delivery of advertising, and additional costs related to the digital transition. In the OTA Notice, the Commission expressed its concern that the higher costs associated with the conversion to digital/HD, combined with a possible reduction in advertising revenues, could result in the inability of OTA television licensees to increase their contributions to Canadian programming when it is important that the maximum investment possible be made in the production of high quality HD Canadian programming.
13. In light of these concerns, the Commission asked
 - if it should consider permitting a subscriber fee for the carriage of OTA signals by BDUs to ensure that OTA television broadcasters have sufficient revenues to make appropriate contributions to the production of Canadian programming;
 - if the apparent failure to monetize out-of-market tuning is a serious problem and, if so, what regulatory measures could be introduced to address the problem; and
 - what amendments should be made to the *Television Broadcasting Regulations, 1987* (the Television Regulations) respecting advertising.

Fee for carriage of local stations

Overview of arguments

14. All of the large English-language television broadcast groups – CTV Inc. (CTV), CanWest and CHUM – supported the introduction of a subscriber fee for the carriage of local OTA stations by BDUs. A subscriber fee was also supported by Quebecor Media Inc. (Quebecor) and Cogeco Inc. (Cogeco), each of which controls cable BDUs and OTA television stations in Quebec.
15. The English-language OTA television groups argued that such a fee is essential for their long-term viability in the face of the increasing audience fragmentation that is eroding their advertising bases. Quebecor and Cogeco agreed, and indicated they would have no problem passing through subscriber fees from their cable BDUs to their affiliated OTA television stations and those of other broadcasters.

16. Most of the private broadcasters who supported a subscriber fee based their support on economic need, and offered no assurance that the additional revenues would be used specifically to increase or even maintain the amount of Canadian programming they currently broadcast. The exception was CTV, which proposed that 50% of the revenues from such a fee be expended on incremental Canadian priority programming and the other 50% could be allocated to other initiatives approved by the Commission.
17. The proposed rate of a subscriber fee-for-carriage of OTA television stations ranged from \$0.10 to \$1.00 per month per station, although Quebecor proposed that the rate of such a fee should be determined through negotiations between broadcasters and distributors. It was of the view that negotiations with all programming services would minimize any overall increase in subscriber fees. CanWest cited the results of a consumer survey conducted by Pollara Inc. indicating public support for paying up to \$4.96 more per month, on average, to access a package of local Canadian television stations. CTV pointed to research conducted by Strategic Inc., which found that a fee of less than \$1.00 had a high level of consumer acceptance and that CTV's proposed \$0.10 fee would result in minimal cost increases.
18. The CBC submitted that an OTA television subscriber fee is also essential for the public broadcaster to ensure it can continue to fulfil its regulatory obligations. It submitted that the increased revenues should be dedicated to public interest objectives, such as more Canadian programming, but recommended that the specific rate and use of such a subscriber fee be explored during the licence renewal process.
19. Production industry associations and unions supported fees for the carriage of OTA television stations, provided that the increased revenues to these stations would be dedicated to increasing the amount of Canadian programming that is produced and broadcast.
20. A number of licensees of discretionary services – Alliance Atlantis Communications Inc., Astral Media inc., Faith & Spirit Media Inc. (Vision TV) and Allarco Entertainment Inc. – opposed a fee for the carriage of OTA television stations. They submitted that such a fee would put downward pressure on the affiliation fees that BDU operators are willing to pay, and could cause subscribers to reduce the number of programming services they buy due to the resulting increase in their monthly bills for service from cable and direct-to-home satellite (DTH) BDUs.
21. BDU operators, including Rogers Cable Communications Inc. (Rogers), Shaw Communications Inc. (Shaw), Bell ExpressVu Limited Partnership² (Bell ExpressVu), and Telco TV, representing Telus Inc., Saskatchewan Telecommunications, and MTS Allstream Inc., all opposed the imposition of a fee for the carriage of OTA

² Bell ExpressVu Inc. (the general partner), and BCE Inc. and 4119649 Canada Inc. (partners in BCE Holdings G.P., a general partnership that is the limited partner), carrying on business as Bell ExpressVu Limited Partnership

television stations, citing the increases in subscriber fees that would result from such a measure. They contended that subscribers would react negatively to a fee increase with no commensurate added value, and might reduce their take-up of specialty services or seek out grey and black market distributors.

22. A number of parties also submitted that the Commission lacked jurisdiction under the *Broadcasting Act* (the Act) to introduce a fee-for-carriage. They further submitted that the copyright regime as well as international laws prevented the Commission from doing so. Some of them also suggested that a fee-for-carriage would in effect introduce a tax that is *ultra vires* the Commission's powers under the Act.

The Commission's authority to mandate a fee-for-carriage

23. The Commission has carefully examined the legal arguments put forward by the parties opposing the fee-for-carriage, but cannot agree with them. To implement the wide-ranging policy objectives of the Act, the Commission has been entrusted with very broad regulation-making powers, as well as the power to subject licences to the conditions that it deems appropriate. The Commission considers that the introduction of a fee-for-carriage is within its mandate and authorized under the Act.

Should a fee-for-carriage be introduced?

24. The Commission has carefully considered the arguments presented in support of a fee for the BDU carriage of local OTA television stations. These include arguments by broadcasters that advertising revenues are no longer sufficient to sustain the OTA television business model, and that additional revenues from subscriber fees are essential.
25. Although, according to their annual returns filed with the Commission, Canadian private OTA television stations, as a group, experienced a decline in both revenues and profits before interest and taxes (PBIT) in the 2006 broadcast year, they reported compound annual revenue growth of 3.8% and an average PBIT margin of approximately 10% respectively over the broadcast years 2002-2006 inclusive.
26. In particular, revenues of French-language private OTA television increased 1% from 2005 to 2006 for a reported compound annual revenue growth of 3.8% between 2002 and 2006. Although PBIT declined by 36% in 2006, the sector's average PBIT over the 2002-2006 period was approximately 11%.
27. For English-language private OTA television, although revenues declined by 0.6% from 2005 to 2006, revenues for the five-year period 2002-2006 nevertheless experienced a compound annual growth of 3.8%. Although PBIT declined by 70% in 2006, this sector's average PBIT over the 2002-2006 period was approximately 10%.

28. Considering the 2006 decline in both revenues and PBIT in the context of the industry's financial performance over the entire 2002-2006 period, the Commission is not convinced that this one year's financial performance constitutes a permanent decline in the profitability of OTA television. In this regard, the Commission notes the cyclical nature of the broadcasting business, which is dependent on the audience appeal of each programming line-up at a given point in time.
29. The Commission also considers that consumer acceptance of a subscriber fee has not been addressed to the extent necessary to properly assess the ultimate impact on the overall system of an OTA television fee for carriage. The Commission notes in particular that while the specialty services sector experienced an overall PBIT margin of approximately 22% in 2006, much of this profit can be attributed to the strong performance of the 49 analog services. In fact, the 87 digital specialty services had an average PBIT margin of -9% in 2006. Given that the digital specialty services rely on subscriber revenues for more than 80% of their total revenues, the Commission is particularly concerned with the impact that an OTA television fee may have on subscribers' take-up of these services.
30. In the absence then of reliable and persuasive data that a fee for OTA television services would not adversely affect the financial health of specialty services, particularly the digital services, and their ability to fulfil their regulatory obligations, the Commission is not persuaded that there would be a net benefit to the broadcasting system, both in terms of increased expenditures on Canadian programming and the availability of Canadian programming services to viewers.
31. Accordingly, the Commission is not convinced that the case has been made for the making of such a fundamental change to the revenue structure of the broadcasting system at this time, or that the proposal would ultimately further the objectives of the Act.

Distant signals

32. CTV submitted that in addition to a fee-for-carriage of local signals, broadcasters should also have the right to refuse the distribution of their OTA stations as distant signals if they are unable to negotiate fair compensation with BDUs. OTA stations are considered to be "distant signals" in markets that are outside of their licensed coverage area. In the view of CTV, carriage of distant signals should be treated as a free market business issue.
33. Currently the Commission permits the carriage of distant signals by BDUs, subject to certain regulatory provisions designed to protect the program rights acquired by local and regional television stations for their markets. The Commission considers that the protection of program rights purchased by Canadian television programming undertakings is fundamental to maintaining the integrity of the Canadian rights market and to the protection of the advertising base of local and regional television stations so that they can fulfil their commitments to Canadian programming.

34. DTH BDUs are permitted to distribute any conventional television station under the provisions of section 39(a) of the *Broadcasting Distribution Regulations* (the BDU Regulations). In order to protect the program rights of local stations, the Commission imposed requirements on DTH BDUs under the BDU Regulations for simultaneous substitution (section 42(1)(a)), simultaneous deletion (section 42(1)(b)) and non-simultaneous deletion (section 43).
35. The Commission has also authorized certain terrestrial BDUs, by way of conditions of licence, to distribute distant signals of conventional television stations on a digital discretionary basis. In order to protect program rights of local stations, the Commission also made these terrestrial BDUs subject to the requirements for program deletion set out in section 43 of the BDU Regulations with respect to these signals.
36. Subsequently, the Commission relieved DTH and terrestrial BDUs of the requirements to perform program deletions and established alternative measures. In the case of DTH, this included, for example, requirements to distribute small market television stations and to contribute to a small market local programming fund. In the case of terrestrial BDUs, these included the approval of agreements with the Canadian Association of Broadcasters (CAB) intended to protect program rights. These arrangements all expired in August 2006, but have been extended or continued pending the outcome of this proceeding.
37. In the Commission's view, CTV's proposal to allow broadcasters to refuse carriage of distant signals could cause the negotiation process to take into account new factors including matters that extend beyond the protection of the rights acquired by local broadcasters. The Commission is not persuaded that a departure from its current approach to provide compensation for negative impact on advertising in the local market is warranted.
38. The Commission expects that parties will re-launch negotiations of agreements with respect to the suspension of program deletion requirements, now that the review of the Commission's television policy has been completed. The Commission is of the view that the purpose of such agreements should be to ensure that local and regional OTA broadcasters receive fair and equitable compensation for the impact that distant signals have on the program rights that they have acquired. In the event that parties are unable to reach agreements, they may wish to seek the Commission's assistance, including availing themselves of the Commission's dispute resolution processes, to resolve any outstanding issues. The Commission, when acting in the context of a dispute resolution process, considers compensation for negative impact to be the key issue and would take the following into account in its consideration of the matter:
 - analyses provided by parties that quantify the impact on local broadcasters resulting from the importation, by way of distant signals, of programming for which those broadcasters hold rights for the local market;
 - the impact of time-shifting and the inability of a DTH BDU to perform simultaneous substitution because a local signal is not carried as part of its service;

- any impact that is material and causally related to the impact of the importation, by way of distant signals, of programming for which local broadcasters hold rights for the local market; and
- factors offsetting the impact of the importation of such programming, such as an estimate of the amount of viewing to the imported programs that can be monetized and/or the value of alternative forms of compensation (e.g., distribution requirements) arising from the requirements set out in Public Notice 2003-37.

Advertising

39. Most parties had no objection to deregulating non-traditional forms of advertising such as product placement and “virtual advertising,” or the digital alteration of images. CTV, Quebecor and CanWest recommended the 12 minute per hour limit on commercial messages be eliminated, either immediately or eventually.
40. On the other hand, TQS inc. (TQS), a number of licensees of specialty services, and independent small market television broadcasters opposed the elimination of the time limit. They submitted that such a move would likely benefit the established national OTA networks at the expense of smaller networks, independent operators, and specialty services. The Association of Canadian Advertisers also opposed the elimination of the advertising time restrictions on the grounds that it would result in excessive clutter and reduce the effectiveness of commercial messages.
41. While the Commission does not consider the imposition of a subscriber fee to be warranted at this time, it acknowledges that the financial outlook for the conventional television sector is uncertain, and that audience fragmentation will continue to put downward pressure on OTA television advertising revenues.
42. The Commission also recognizes that, for the foreseeable future, OTA television services will continue to provide the largest audiences and make the most significant contribution to the production and exhibition of high quality Canadian programming, including local programming.
43. Therefore, the Commission considers it essential that OTA broadcasters have the flexibility to maximize advertising revenues to respond to the negative impact of audience fragmentation. For this reason, the Commission will take the following steps to ensure that OTA broadcasters have such flexibility:
 - remove non-traditional advertising (product placement, virtual ads) from the calculation of the maximum number of advertising minutes that may be broadcast; and

- increase the 12 minute per hour limit on traditional advertising to 14 minutes per hour in peak viewing periods (7 p.m. to 11 p.m.) effective 1 September 2007. The limit will be increased to 15 minutes per hour for all viewing periods effective 1 September 2008. Time restrictions will be eliminated altogether as of 1 September 2009, unless significant contrary factors are brought to the Commission's attention.
44. This incremental approach to the deregulation of traditional advertising messages will provide time for the market to adjust, and ensure that the value of the additional advertising inventory is optimized.
 45. In order to implement these measures, the Commission will issue, and seek comment on the wording of, a proposed amendment to the Television Regulations. It is expected that the amendment will become effective on 1 September 2007.
 46. The Commission intends to review the impact of the increased advertising time limits during the licence renewal hearings in the Spring of 2008 to ensure the increased flexibility results in a net benefit to the broadcasting system.
 47. The Commission notes that it will retain its regulatory oversight of advertising content, and that broadcasters must continue to adhere to all applicable industry standards and codes. Since popular foreign programs already contain more than 15 minutes of program interruptions in each hour, increasing the hourly advertising limit from 12 minutes should not result in an increase in program interruptions.
 48. The Commission expects that the additional revenues resulting from this measure will enable conventional television licensees to increase their contributions to the production and exhibition of Canadian programming.
 49. The changes to the advertising time limits will affect the drama incentive programs established in Public Notices 2004-93 and 2005-8. However, given the incremental nature of the changes, the Commission hereby eliminates the current 14 minute per hour limit on advertising that may be broadcast through the use of the drama credits, for broadcasters who wish to continue benefiting from the drama incentive programs in the interim.

Transition to Digital/HD broadcasting

50. In the OTA Notice, the Commission stated that since the release of Public Notice 2002-31, which adopted a market-driven approach to the transition to digital television broadcasting, the pace of transition in Canada has been slow, particularly in comparison with the U.S. It also noted that this approach, with no mandated digital conversion deadline, is in contrast to the U.S., which has set 17 February 2009 as the date by which analog transmission will cease and all OTA television signals must be transmitted digitally.

51. The Commission also expressed concern that viewers who have invested in HD receivers and subscribe to HD services offered by Canadian BDUs are finding little Canadian programming offered in HD. Such viewers may turn to foreign services, and it may be difficult to repatriate them to Canadian services even when more Canadian HD programming is available.
52. The Commission noted the concerns expressed that the cost of replacing existing analog transmission facilities may be one of the barriers to a more rapid transition to digital/HD. It also noted the argument that it would be more appropriate to spend money on the production of Canadian HD programming for distribution by BDUs than on the construction of digital OTA transmitters, particularly in view of the relatively small proportion of Canadians who still rely on OTA reception.
53. In light of these issues, the Commission sought comment on the most appropriate and effective means of delivering Canadian digital/HD signals to Canadians. It also requested that OTA licensees provide specific information with respect to the cost of upgrading existing analog transmission facilities to digital transmission facilities.
54. After consideration of the comments related to the transition to digital/HD broadcasting, the Commission considers that the following key issues should be addressed:
 - Should there be a shut-down date of OTA television analog transmitters to expedite the conversion from analog to digital transmission?
 - To what extent should the Commission mandate the roll-out of OTA television digital facilities?

Shut down of analog transmitters

55. There was broad agreement, but not unanimity, that a firm analog shut-down date should be established, with most parties favouring a date that followed the U.S. by approximately two years. CanWest stated that establishing a cut-off date would ensure competitive parity between broadcasters and enable them to plan future capital needs.
56. The Department of Industry (Industry Canada) submitted that, from the perspective of efficient and effective management of the radio spectrum, serious consideration should be given to specifying a date for the shut down of OTA analog television transmission. Such a date could be closely aligned within a North American market time frame with a view to ensuring that Canadians will be able to receive Canadian OTA digital television.
57. While most parties were in favour of a mandatory shut-down date, some recommended that the market-driven approach be continued. CTV submitted that the Commission should permit conventional broadcasters to gradually phase out analog transmitters.

58. TQS proposed that the Commission adopt the same approach as set out in Public Notice 2003-61, whereby a BDU may submit an application requesting the Commission's approval to cease the carriage of analog signals once 85% of its subscribers have the ability to receive digital services.
59. Shaw stated that, because a strong analog offering can be part of a successful business model, it did not agree that the Commission should specify a point at which analog OTA transmission should be shut down.
60. The Commission agrees that a firm analog shut-down date will enable broadcasters to plan future capital needs and put in place the necessary facilities for their post-transition operations. It also agrees with Industry Canada that, from the perspective of efficient and effective management of the radio spectrum, the date for the shut down of OTA analog television broadcasting should be closely aligned within a North American market time frame. Spectrum coordination would be very difficult if the U.S. has converted to all-digital transmission and Canada continues with a mix of analog and digital OTA television transmission. Therefore, the Commission considers that a near-term date for the termination of analog transmitters, approximately two years after the U.S. shut down, would best advance the digital transition.
61. Accordingly, the Commission has decided to adopt, for planning purposes, a shut-down date for analog television transmission of 31 August 2011. OTA television licences will only be issued or renewed for analog transmission until that date, and OTA television licences will be authorized only for digital transmission after that date.
62. The Commission is confident that the adoption of this date will provide the television industry with the necessary regulatory certainty to expedite the transition from analog to digital. This includes not only the transmission facilities, but also the production of Canadian programming in HD. Canada's production sector has only just begun to embrace the technology and it is vitally important that this aspect of the transition is also advanced.
63. The Commission recognizes that there will be some viewers who rely on OTA reception who will be disadvantaged by the shut down of analog television transmitters, particularly in those communities where no digital transmitters are established to replace them.
64. In this regard, the Commission notes that there may be northern and remote communities where analog transmitters could be maintained. Spectrum is not in short supply in these markets and, although frequency changes may be necessary, alternative channels in the new broadcast band should be readily available. In such markets, the analog transmitters could operate until such time as they reach the end of their useful life, or viewers have switched to another form of distribution technology.

65. To ensure that Canadians are not needlessly deprived of OTA television service, the Commission will be willing to consider, on an exceptional basis, the continuation of analog service in northern and remote communities where no digital OTA service will be provided. In considering such proposals, the Commission will conduct a public process and, after consultation with Industry Canada, make its decision.

Rollout of digital facilities

66. During this process, the Commission examined two options for the delivery of digital/HD programming to Canadians:
1. *The “hybrid” model.* Under this model, analog transmission facilities in larger markets would be replaced with digital transmitters, either through the construction of parallel facilities or the direct conversion of transmitters from analog to digital. In smaller markets, cable and satellite BDUs would be used to deliver digital/HD signals.
 2. *Elimination of all OTA transmission facilities.* Under this model, BDUs would distribute digital/HD programming services to all markets.
67. While the CBC and CanWest supported adoption of the hybrid model, a number of broadcasters submitted that it is no longer economical to build transmitters, given the declining number of viewers who receive television signals off-air rather than through the facilities of BDUs. Accordingly, they proposed that digital/HD programming be delivered by cable and DTH BDUs. However, they also submitted that their programming services should continue to receive priority carriage status, and that they should be able to request simultaneous substitution, even in the absence of providing local OTA services.
68. Relying solely on BDUs for the distribution of digital/HD programming may be cost effective for broadcasters, however the Commission considers that there are a number of consumer benefits in maintaining OTA transmission facilities. These benefits are as follows:
- There is no cost to viewers, so accessibility is provided to low income households and households with low levels of television viewing.
 - It can offer Canadian alternatives to viewers who continue to rely on OTA television reception and will have access to U.S. OTA border stations.
 - The quality of digital signals delivered by OTA transmitters is excellent.
69. The Commission notes that both DTH operators, Star Choice Television Network Incorporated (Star Choice) and Bell ExpressVu, stated that the distribution of OTA television HD signals will be severely limited by the lack of satellite capacity and the associated costs of distributing those signals. It further notes that cable and other

terrestrial distributors also face significant incremental costs associated with the carriage of HD programming, particularly to those in smaller communities that lack a sophisticated communications infrastructure.

70. Because of the cost and capacity limitations facing these re-distribution technologies, it may not be possible to ensure the delivery of all existing services to their entire markets in high definition. Therefore, complete reliance on BDU distribution would limit consumer access to local and regional programming services.
71. Furthermore, the Commission is of the view that the broadcasters presented worst case cost scenarios for their digital conversions, and considers there are more cost-effective solutions that make use of much of the existing transmission infrastructure. This is particularly the case in the major centres where OTA delivery still serves a significant number of viewers. The Commission notes that the major broadcasters have already constructed, or have indicated they plan to construct, OTA digital transmitters in at least one of the major markets they serve through analog transmitters.³
72. At the same time, the Commission recognizes that the cost of extending OTA service to rural and remote areas has always been high, and there may be no business case for providing digital OTA service to many of these communities, particularly in view of the declining number of viewers who rely on OTA reception.
73. A number of parties to this process addressed this issue by suggesting or requesting that the Commission no longer require the provision of digital OTA services. The Commission notes that it has established a number of regulatory mechanisms that benefit local and regional OTA stations, such as mandatory cable carriage and simultaneous substitution, and has linked the right to solicit local commercials in a community to the provision of OTA service to that community.
74. The Commission established a similar regulatory framework for digital OTA services in Public Notice 2002-31, where cable carriage rights were only granted to broadcasters who provided OTA digital services. While the provision of a digital OTA service was voluntary, the OTA Notice also stated that, if broadcasters did not take up their digital frequencies within a reasonable time frame, the frequencies could be awarded to another party.
75. The Commission is of the view that construction of OTA digital facilities should continue to be at the discretion of television licensees, however it will retain its current approach to regulatory privileges, such as priority carriage and simultaneous substitution, in order to encourage the extension of local and regional digital OTA services.

³ Toronto, Hamilton, Ottawa, Vancouver, Montréal or Quebec

76. The Commission acknowledges that the digital transition will have a direct impact on Canadian viewers. Consumers will either have to purchase digital TV sets and the necessary equipment to receive digital/HD signals, or a converter box to translate digital signals to analog format for display on their existing sets. In either case, they will be forced to upgrade their television sets at some cost in order to continue to receive the services they currently enjoy. It is noted that a consumer subsidy program is being put in place in the U.S. for households that rely on OTA television reception and that have not upgraded their analog equipment to digital or have not purchased an integrated digital set.
77. The Commission also acknowledges that there will be some disruption to viewers when analog services are shut down, particularly where they do not have access to replacement digital OTA services and the only alternative is a user-pay cable or DTH subscription.
78. Since many of the issues raised by the digital transition fall outside the Commission's jurisdiction, it intends to consult with Industry Canada and with the Department of Canadian Heritage. These consultations will address, in particular, the provision of HD broadcast services, particularly to remote and underserved areas, as well as the impact of the transition on Canadian consumers.
79. The Commission will also direct conventional broadcasters to provide digital roll-out plans in their renewal applications for the next licence term to ensure that Canadians have information regarding the extent to which they will have access to digital OTA television service, and to ensure that they have the opportunity to comment on those plans.
80. In addition to encouraging the transition of existing OTA television broadcasters to digital transmission, the Commission will continue to consider applications by new entrants who are prepared to construct only digital OTA broadcast facilities.

Contribution to Canadian programming

81. As noted previously, the OTA television sector continues to play an essential role in the Canadian broadcasting system as the dominant force in contributing to the production and provision of Canadian programming. In the OTA Notice, the Commission noted concerns expressed that the elimination of Canadian programming expenditure requirements in the 1999 Television Policy has been at least partially responsible for the decline in the production of Canadian programming, particularly drama series. The Commission also pointed out that the decline in Canadian drama production coincided with the collapse of the export markets and the rise in popularity of reality programming.
82. In the OTA Notice, the Commission asked what the most effective regulatory mechanisms would be to ensure an appropriate contribution to the production, acquisition and broadcast of Canadian programs, and if OTA licensees should be subject to an expenditure requirement on Canadian programs.

83. English-language broadcasters were opposed to the re-imposition of program expenditure requirements. CanWest cited the 1999 Television Policy, in which the Commission stated that expenditure requirements were complex and, in an increasingly competitive landscape, did not provide broadcasters with the flexibility they need to adjust their programming strategies to attract the largest possible audiences and advertising revenues. CanWest submitted that the landscape has only become more competitive since then, with the increased number of specialty services, foreign channels, and unregulated sources of video programming now available.
84. Instead of spending requirements, CTV proposed the creation of a 200% bonus to encourage the production and broadcast of new Canadian drama, and the revision of the priority programming definition to include human interest programs. The French-language OTA television broadcasters TVA Group Inc. (TVA) and TQS indicated that they would agree to the imposition of program expenditure requirements if the Commission were to eliminate other obligations, such as priority programming requirements.
85. Program production industry associations and unions pointed to the elimination of expenditure requirements as one of the key reasons for the reduction in the amount of Canadian drama and other priority programming available on OTA television today. These organizations contended that only through the reinstatement and enforcement of spending and exhibition requirements will Canadian broadcasters make an appropriate contribution to the production and airing of Canadian programming.
86. The Commission notes that, despite the elimination of expenditure requirements pursuant to the 1999 Television Policy, overall spending by OTA television licensees on Canadian programming has increased moderately and remained stable as a percentage of their revenues.
87. According to Commission financial data, Canadian programming expenditures by OTA television broadcasters have increased commensurately with increases in revenues, with English-language Canadian programming expenditures consistently averaging approximately 25% of revenues, and French-language OTA expenditures averaging approximately 36% of their revenues in the past five years.
88. However, while spending on Canadian programming by English-language OTA broadcasters has increased commensurately with revenues, they have diminished as a proportion of total programming budgets. Commission records indicate that, between 1999 and 2006, Canadian programming expenditures by English-language OTA broadcasters decreased from 50% to 40% of total programming expenditures. In contrast, French-language OTA television broadcasters consistently spent approximately 90% of their total programming budgets on Canadian programming over this time period.

89. Annual expenditures on Canadian drama by English-language OTA television broadcasters also decreased from approximately \$62 million, or 4% of revenues, in 2001 to approximately \$40 million, or 2.3% of revenues, in 2006. However, expenditures on Canadian drama by French-language OTA television licensees increased from \$22 million, or 6% of revenues, in 2001 to peak at \$35 million, or 8.5% of revenues, in 2003, and have averaged approximately \$33 million, or approximately 7% of revenues, since then.
90. Based on this information, the Commission is satisfied with the Canadian programming expenditures of French-language OTA television broadcasters, and commends their commitment and contribution to the production and acquisition of Canadian programming.
91. Although English-language OTA licensees have maintained Canadian programming expenditures as a percentage of revenues, the continuing reduction in the proportion of total programming expenditures allocated to Canadian programming is cause for concern.
92. The Commission remains of the view that, in an increasingly competitive environment, licensees require high quality programming to win audience loyalty and will, therefore, make the necessary expenditures to acquire such programming. Furthermore, the Commission does not consider that increasing regulatory obligations is appropriate at a time when the OTA television sector must respond to the ever-increasing challenge of competing with new and largely unregulated sources of audio-visual programming.
93. However, the Commission notes that section 3(1)(f) of the Act states that each broadcasting undertaking shall make maximum use, and in no case less than predominant use, of Canadian creative and other resources in the creation and presentation of programming. Therefore, the Commission intends to discuss this aspect of programming expenditures with English-language OTA broadcasters at the time of their licence renewals to ensure that an appropriate proportion of their financial resources will be allocated to the production and acquisition of Canadian programming.
94. The Commission notes that the focus of this review was primarily on the financial aspects of the OTA television sector, and therefore considers the appropriate context for examining exhibition issues to be during the licence renewal process for the major OTA broadcast groups, which is scheduled for Spring 2008.
95. At that time, the Commission intends to review its approach to the exhibition of Canadian programming to ensure that OTA licensees have sufficient flexibility to operate in an increasingly competitive communications environment, while maximizing their contribution in the most effective manner possible to the broadcast of Canadian programming.

Independent production

96. The OTA Notice sought comments as to whether the Commission's current approach to independent production is appropriate to ensure that the broadcasting system includes "a significant contribution from the Canadian independent production sector," as set out in the Act. Organizations representing the creative community voiced their support for the Commission's current approach to independent production and, specifically, the expectation that 75% of priority programming broadcast by the major broadcast groups be sourced from independent producers.
97. While noting the importance of independent production in fulfilling their priority programming obligations, broadcasters also expressed their desire for more flexibility. TVA stated that, to reach its business goals, it needs to produce more priority programming in-house than is contemplated under the current guidelines. As multi-platform distribution of audiovisual content increases in importance, broadcasters seek to control these rights as a means of monetizing content across varied platforms. While broadcasters expressed a desire to exert more control over ancillary rights, the production community claimed that broadcasters' market power makes it difficult to conduct equitable negotiations over those content rights.
98. Independent producers submitted that they are being asked to surrender ancillary rights for little or no compensation, and suggested that the Commission encourage the development of guidelines that would outline acceptable terms of trade similar to other industry protocols such as those on violence or gender portrayal. The Canadian Film and Television Production Association (CFTPA) also recommended a dispute resolution mechanism, similar to that established by the Commission for contractual disputes between BDUs and programming services, to deal with rights agreements between independent producers and broadcasters.
99. The Commission is of the view that terms of trade agreements would provide stability and clarity to all concerned, and encourages the development of such agreements between broadcasters and independent producers. The Commission will expect licensees to provide draft, or signed, terms of trade agreements with independent producers as part of their licence renewal applications. The Commission will examine the role of independent production at the time of licence renewal.

Small market stations

100. In the OTA Notice, the Commission noted that, while the Canadian OTA television sector is generally healthy, profits are concentrated in the major urban centres. The impact of DTH BDUs, competition from other programming services and declining local advertising revenues are making it increasingly difficult for both English- and French-language small market stations to serve their audiences and invest in the transition to digital broadcasting.

101. The Commission outlined a number of measures that it has adopted to help small market stations deal with the migration from OTA to DTH viewing. These include the DTH carriage of a number of small market stations and the establishment of a fund to permit DTH licensees to assist independently owned small market stations in contributing to Canadian programming and, in particular, to meeting their commitments to local programming (the Small Market Programming Fund). The Commission asked, among other things, if the measures adopted to assist independently owned small market stations are having their desired effect, and what measures might be appropriate to ensure that small market stations controlled by larger broadcast groups continue to fulfil their local programming obligations.
102. The independent small market broadcasters stated that the Small Market Programming Fund is very effective, and has allowed them to maintain or increase the amount of local programming they can provide to their communities. They submitted that the continuation of this fund on an indefinite basis is essential to their long-term viability.
103. CanWest stated that, while its small market stations should and do benefit from the resources and economies of scale from being part of a large group, this type of cross-subsidization is not acceptable or sustainable in the long term.
104. As previously noted, the Small Market Programming Fund was implemented as part of a package of measures that also includes negotiated agreements with the OTA broadcasters to give DTH operators relief from the program deletion requirements set out in the BDU Regulations.
105. Although the condition of licence providing relief from the programming deletion requirements expired on 12 August 2006, Bell ExpressVu applied for and received an extension of the condition until six months after the date of issuance of this public notice. Star Choice is continuing to make contributions to the Small Market Programming Fund as per the terms of its condition of licence, which also expired in August 2006.
106. The Commission considers that independent broadcasters play an important role in providing local programming outside of major markets. In order to provide local programming of high quality, they need the financial strength that results from reasonable affiliation agreements and financial support. The Commission is of the view that the Small Market Programming Fund is achieving its objectives by enabling independent small market stations to provide local programming to the communities they serve, and should be included in the package of measures that is scheduled to be negotiated between the DTH operators and OTA broadcasters now that this public notice is released.
107. During this proceeding, Corus Entertainment Inc. submitted that its Kingston and Peterborough stations should be eligible recipients for revenues from the Small Market Programming Fund, since both of those markets have populations below 300,000, the figure cited by the Commission as the threshold between large and small markets. However, the Commission notes that Corus was not identified as an “independent”

broadcaster in the original agreement between Bell ExpressVu and the CAB, which was the basis for the Commission's criteria for stations that would have access to the fund. The Commission considers that the context has not changed since the implementation of the Small Market Programming Fund. Consequently, Corus' Kingston and Peterborough stations will not be eligible to receive money from the fund.

108. Independent broadcasters and large broadcast groups alike submitted that DTH carriage of all small market stations was essential to ensure their ongoing viability. The Commission considers that the most appropriate context in which to deal with this issue is the forthcoming review of the regulatory framework for DTH undertakings.

Benefits policy

109. The Commission currently requires applicants applying to transfer ownership or control of television undertakings to make commitments to clear and unequivocal tangible benefits that represent a financial contribution of 10% of the value of the transaction, as accepted by the Commission (the benefits policy). In the OTA Notice, the Commission stated that benefits related to such transfers have injected over half a billion dollars into the broadcasting system since 1999, and that much of this money has been directed to the production of Canadian programming. The Commission then asked what changes, if any, should be made to its benefits policy with respect to OTA television undertakings.
110. The majority of parties did not propose any major changes to the benefits policy. However, CanWest submitted that the benefits policy should be eliminated, as it was for BDU ownership transactions, or at the very least, the amount of the required contribution should be reduced to 6% of the value of the transaction, in line with the benefits policy in effect for radio. Independent small market broadcasters recommended that the Commission exempt from the benefits policy OTA television stations earning less than \$10 million in annual revenues.
111. In the 1999 Television Policy, where the Commission set out its expectations regarding the consideration of applications to transfer the ownership or control of a television undertaking, it outlined the rationale behind its benefits policy as follows:

Because the Commission does not solicit competing applications, the onus is on the applicant to demonstrate that the application filed is the best possible proposal under the circumstances and that the benefits proposed in the application are commensurate with the size and nature of the transaction.
112. The Commission remains of the view that, in the absence of a competitive process for ownership transactions, the contribution of benefits in the amount of 10% of the value of an ownership transaction is still an appropriate mechanism for ensuring that the public interest is served. However, the Commission is conscious of the economic challenges

faced by independent small market broadcasters. Accordingly, the Commission hereby revises its policy to exempt those television stations earning less than \$10 million in annual revenues and who are, or could be, eligible to receive support from the Small Market Programming Fund from the application of the benefits test.

113. Several industry associations, including the Directors Guild of Canada, the Alliance of Canadian Cinema, Television and Radio Artists, the CFTPA, and the Coalition of Canadian Audio-Visual Unions, urged the Commission to revise the benefits policy to prevent the recurrence of a situation similar to an ownership transaction approved in Decision 2006-309, involving Bell GlobeMedia Inc. (now known as CTVglobemedia Inc.). In that case, no benefits were required because the transaction constituted a “change” rather than a “transfer” of control.
114. The Commission is of the view that the circumstances of the Bell Globemedia Inc. transaction were very unique, and that the possibility of such a situation recurring is very unlikely. The Commission does not consider that decision to be a precedent. Therefore, it does not consider that a change to the benefits policy is warranted. The Commission also notes that, in Decision 2006-309, it acknowledged the concerns expressed by parties concerning multi-step transactions and reserved the right, in the case of such transactions, to review the entire sequence of previous transactions to determine the appropriateness of any proposed benefits package.
115. A number of parties, including the British Columbia Institute of Technology, the Canadian Broadcast Museum Foundation, the Canadian Media Research Foundation Consortium, and the Shaw Rocket Fund, requested explicit Commission recognition, and in some cases, the designation of a minimum percentage of contributions, in support of their respective activities.
116. With respect to initiatives involving research and capital expenditures, the Commission notes that such proposals are already eligible for benefits contributions, subject to the conditions set out in Public Notice 1993-68.
117. Therefore, after examining the various submissions on the public record relating to benefits, the Commission is satisfied that its approach to eligible initiatives, as set out in Public Notice 1993-68, remains appropriate. It is noted, however, that the Commission will further examine the benefits policy in the context of its Diversity of Voices proceeding, announced in Notice of Public Hearing 2007-5 on 13 April 2007.

Conclusion

118. The Commission considers that the measures announced today will enable the over-the-air television sector to further the objectives set out in the Act, while ensuring that it is able to operate effectively in a rapidly changing and increasingly competitive communications environment.

119. It further considers that these measures will enable OTA television broadcasters to prepare licence renewal applications that propose the maximum realistic contributions to the support of Canadian programming for the next licence term.

Secretary General

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