Copyright Board Canada

Commission du droit d'auteur Canada

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Regime Copying for Private Use
Copyright Act, subsection 83(8)

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

Tariff of levies to be collected by CPCC in 2003 and 2004 on the sale of blank audio recording media, in Canada, in respect of the reproduction for private use of musical works embodied in sound recordings, of performer's performances of such works and of sound recordings in which such works and performances are embodied

Reasons for decision

I. INTRODUCTION

These reasons explain the Board's decision about the levies proposed by the Canadian Private Copying Collective ("CPCC") in respect of the reproduction for private use of sound recordings embodying performances of musical works ("private copying") for the years 2003 and 2004.

A. THE PROCESS LEADING TO THIS HEARING

This decision is the latest in a series dealing with the matter. In 1999, the Board issued its first decision[1] regarding the tariff for private copying levies, and in 2001, issued its second decision.[2] In 2002, the Board, on application, reconsidered its second decision on the ground that a material change had occurred in the nature of the market for blank audio recording media, and amended the tariff accordingly.[3]

Although the Board's earlier decisions are helpful to understand the background to these proceedings, it is not necessary to describe in detail their contents. For present purposes, it is sufficient to recall that for the years 1999 and 2000 the Board set the levy rate at 23.3¢ for each audiocassette, 5.2¢ for each CD-R and CD-RW and 60.8¢ for each Audio CD-R and CD-RW and

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[1] *Tariff of levies to be collected by CPCC, in 1999 and 2000, for the sale of blank audio recording media in Canada*, www.cb-cda.gc.ca/decisions/c17121999-b.pdf, 4 C.P.R. (4th) 15, application for judicial review dismissed, *AVS Technologies Inc. v. Canadian Mechanical Reproduction Rights Agency*, (2000) 7 C.P.R. (4th) 68; 257 N.R. 283.

[2] *Tariff of levies to be collected by CPCC, in 2001 and 2002, for the sale of blank audio recording media in Canada*, www.cb-cda.gc.ca/decisions/c22012001reasons-b.pdf, 10 C.P.R. (4th) 289.

[3] *Application to vary the tariff of levies to be collected by CPCC, in 2001 and 2002, for the sale of blank audio recording media, in Canada*, www.cb-cda.gc.ca/decisions/c09042002-b.pdf, (2002) 18 C.P.R. (4th) 345.

each MiniDisc. For the years 2001 and 2002, the rate increased to 29¢ for audiocassettes, 21¢ for CD-R and CD-RWs and 77¢ for CD-R and CD-RWs Audio and MiniDiscs.

On March 9, 2002, the Board published in the *Canada Gazette*, pursuant to section 83 of the *Copyright Act* (the "*Act*"), CPCC's statement of proposed levies to be collected for the years 2003 and 2004 and a notice concerning the right to object. Due to unavoidable delays, and at the request of CPCC, the Board did not hear this matter prior to the beginning of 2003. Therefore, also upon CPCC's request, the Board established an interim tariff. It is essentially identical to the tariff for the preceding year, as amended. The interim tariff remained in force until the issuance of this, the Board's third substantive decision.

B. THE PARTICIPANTS' POSITIONS

The Board received over 1500 comments about CPCC's proposed levies, all of which were borne in mind throughout these proceedings. Initially, there were over one hundred objectors to the proposed tariff. Many withdrew before the hearing for various reasons, most of which were procedural. Objectors in the broadcasting and educational communities withdrew as a result of assurances from CPCC that the zero-rating program would be extended. This is discussed below. None of the blank media users from the first proceedings participated in the latest hearings, presumably because of the current zero-rating program. The participants who submitted formal statements of their cases take the following positions.

CPCC relies generally on an updated version of the approach taken by the Board in past proceedings. It also seeks to levy items not previously subject to a tariff. These items are blank DVDs (Digital Versatile Disks) and various formats of removable memory and non-removable memory used in MP3 players and similar devices. It proposes a significant increase in the rates applicable to media currently subject to the levy, develops a similar rate for blank DVDs and suggests a graduated rate structure, based upon capacity, for removable and non-removable memory.

Ultimately, CPCC proposes rates of 51¢ for each audiocassette, 59¢ for each CD-R of 100 megabytes (Mbs) or more, 49¢ for each CD-RW of 100 Mbs or more, $1.15 for each CD-R Audio and CD-RW Audio or MiniDisc, and 65¢ for each blank DVD. For removable electronic memory cards, or a removable hard drive, CPCC seeks a rate from 0.221¢ to 0.55¢ for each Mb. For (a) removable electronic memory cards sold bundled with a music device, or a removable micro hard drive sold bundled with a music device, or (b) non-removable memory incorporated into a music device, or a hard drive incorporated into a music device, CPCC proposes rates from 0.193¢ to 1.08¢ for each Mb depending on capacity.

The Canadian Storage Media Alliance (CSMA) objects to CPCC's proposal, as it did in the first two previous hearings. It focusses its submissions on the scope of the levy, the quantum of the rates and CPCC's zero-rating program. It disputes that all items but audiocassettes, recordable and rewritable CDs and MiniDiscs are properly subject to a levy. In any event, it submits that all proposed rates are too high. It also argues that CPCC's zero-rating program is flawed and illegal, and urges the Board not to consider the program in establishing the levy rates.

For the first time, the Board heard from a coalition of retailers of blank audio recording media.

This group is comprised of Costco Wholesale Canada Ltd., Future Shop Ltd., InterTan Inc. (RadioShack Canada), London Drugs Limited, The Business Depot Ltd. (STAPLES Business Depot), Wal-Mart Canada and the Retail Council of Canada (collectively, the "Retailers"). The Retailers argue that the private copying regime, or a part thereof, is constitutionally invalid as either *ultra vires* the legislative competence of Parliament or as an improperly enacted tax. In the alternative, the Retailers submit that the proposed tariff is flawed and unfair. They argue that a levy ought not to apply to most of the items identified in CPCC's proposal, but even if such items were leviable, the levy rate should be calculated as a proportion of their sale price (*ad valorem*).

The Retailers are also opposed to CPCC's zero-rating program. They ask the Board to prohibit the program outright or substitute its own mechanism within the tariff.

Other participants raise a range of arguments. Almost all dispute the proposed application of the levy to certain items or criticize generally CPCC's methodology as problematic and its proposed rates as excessive and not justified by evidence.

Many users of items proposed to be levied made their concerns known to the Board. This group includes companies such as Cognos Inc., Vencon Technologies Inc., represented by Mr. Mark Venis, and Hydraulic Design, represented by Mr. James Carruthers. It also includes individuals such as Messrs. Tom Trottier, Richard Pitt, Jeremy Hellstrom, Martin Hemmings, Brian Hunt and V. Kuz.

Most end users express reservations about the administration and application of CPCC's zero-rating program. In principle, they support some form of an exemption. However, objectors generally indicate a preference for a program without registration restrictions or fees, and with a scheme through which they may buy zero-rated blank media wherever they choose.

The breadth of application of the levy is another common theme throughout the submissions of objectors. Almost all complain that CPCC's proposal and its definition of items to be subject to the levy are ambiguous and arbitrary. For example, some explain that there is no technical distinction between items sought to be levied and items proposed to be exempt. Others add that there is no valid distinction between removable and non-removable memory. Generally, objectors point out a trend toward multi-functional items that are difficult to classify.

Concerns about the potential application of the levy are shared by participants representing manufacturers, marketers and others in industries affected by the proposed levy. For example, the Canadian Wireless Telecommunications Association (CWTA) submits that any extension of the definition of blank audio recording medium must be tightly constrained, and should not encompass cellular phones. CWTA discontinued its participation once it became clear that CPCC is not seeking to levy memory in cellular phones.

The Consumer Electronics Marketers of Canada (CEMC), represented by Mr. Ken Elsey, is among the objectors that submit the levy would negatively affect the consumers' electronics market by driving business to the United States and hindering the development of new technologies in Canada. Most objectors suggest that the levy would threaten Canadian innovation and technology industries, and that it is unfair that technology industries and users subsidize the music industry.

Objectors urge the Board not to assume that all blank media are used for copying music. They also point out that some copying is of licenced samples, public domain material, ineligible repertoire, or may be fair dealing. They ask the Board to account for these facts. Some suggest that certain activities of reproduction, including backing-up collections or transferring formats, should not give rise to a levy.

Many question the harm done to the music industry as a result of Internet downloading. The Board also heard concerns about the distribution of the funds collected and the benefits or lack thereof to Canadian emerging and independent artists.

C. FACTS: THE EVIDENCE AND RECENT DEVELOPMENTS

The Board read many volumes of evidence and heard numerous witnesses for nearly 12 full days. The topics addressed were mostly similar to those addressed in previous hearings, and related to, among other things, the collection and distribution activities of CPCC; characteristics of new and emerging technologies; the private copying habits and perceptions of Canadians; all aspects of the model upon which CPCC's proposal is based; the nature and structure of relevant markets and industries; the current and potential impact of the levies on those industries and the economy generally; and foreign private copying regimes.

Much of the Board's insight into the private copying habits of Canadians was gleaned from the survey work of CPCC's expert, Mr. Benoît Gauthier of *Réseau Circum*.[4] Also, CMSA and the Retailers engaged Léger Marketing to conduct their own survey.

Private copying technologies were described by Mr. Basskin for CPCC, by a panel of industry representatives Messrs. Bourrier, Manenc, Ballinger and Ng for CSMA, as well as by others including Mr. Carruthers. Objectors' witnesses Messrs. Lawrence, Burger and Van der Vorm explained digital rights management (DRM) systems and technological protection measures (TPMs).

The Board gleaned information about blank media markets from Ms. Smith and Mr. Ciric for CPCC, from CSMA's panel, from Ms. Goddard and Mr. Kubas for CSMA and the Retailers and from Mr. Levy and Ms. Brisebois for the Retailers. End users such as Messrs. Elsey, Pitt, Trottier and others also gave the Board their perspective.

Messrs. Stohn and Audley, who are the engineers of CPCC's valuation model, and Dr. Michael Rushton provided insight into economic and theoretical aspects of the levies. The Board also considered an abundance of written evidence prepared by economists, scholars, domestic and foreign governments and others with knowledge of the relevant issues.

The four areas described below deserve particular attention. The Board is aware that this is an area of constant evolution, and new developments will have again occurred by the time these reasons

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[4] Circum surveyed over 1000 Canadians per month for at least 21 months, and the Board understands that this work is ongoing. During the last half of 2001 and the first half of 2002, Circum spoke to over 12,000 people.

are published.

i. Technological Developments

There has been a continued shift in the types of products used for private copying, and new technologies are emerging for that purpose.

At the time of the first decision on private copying ("*Private Copying I*"), more than 90 per cent of copies were made onto audiocassettes. Current evidence indicates that the share of copies made onto audiocassettes is less than one fifth, while recordable and rewritable CDs account for more than 75 per cent. It is clear, therefore, that the overwhelming majority of private copies are now made using blank CDs. All other products are used in much smaller proportions; the figures do not account for copies made onto personal computers.

These trends are attributable, at least in part, to the growing penetration of CD burners in personal computers in Canada. Moreover, hardware and software continue to be developed that makes copying music easier. Whereas previously private copying most often involved synchronizing cassettes in a dual deck machine, programs now exist that allow people to find, acquire, manage and copy whole libraries of music simply and conveniently on their personal computers.

Also, new media that might be used for private copying continue to emerge. These include, for example, recordable and rewritable DVDs. Blank DVDs look and function much like blank CDs; the primary distinction is storage capacity. The typical capacity of a blank DVD is 4.7 Gbs, compared to the 650-700 Mbs of capacity on most blank CDs.

Currently, various formats of blank DVDs compete for acceptance in an emerging market. Some can only be recorded to once, including DVD+R, developed by Phillips and Sony, and DVD-R, developed by Panasonic, Hitachi, Pioneer and Phillips. DVD-R(A) ("authoring") and DVD-R(G) ("general") are two subtypes of DVD-R that are mutually incompatible with each other. Other formats can be recorded to multiple times. DVD-RAM, developed by Hitachi, Toshiba and Panasonic was created for backing up computer data, and therefore, can be rerecorded approximately 100,000 times. DVD-RW, developed by Pioneer, and DVD+RW, developed by HP, Phillips and Sony, are also rewritable.

For now, technical distinctions among the formats mean that each is compatible only with specific writers and players. The battle between competing formats appears similar to that which occurred between the VHS and BETA formats of videotapes. The expectation is that this war will end at some point, but it is unclear just when or which format will emerge as the industry standard.

Contrary to the blank DVD market, the prerecorded DVD market is growing by leaps and bounds. Consumers seem to be embracing DVD technology for movies, and sales of DVD players are brisk. However, at present, most of the installed base of DVD players cannot play recordable or rewritable DVDs.

Some expect that stand-alone DVD recorders will replace VHS recorders, but that day is not yet here. At this time, most DVD writers come in the form of an optional drive in higher-end personal computers. Most of these can record only to specific disc formats. As a result, it is probably

common to record and play recordable or rewritable DVDs on the same machine. The evidence also indicates that there are currently no portable DVD players that can read compressed audio files from recordable DVDs.

Regarding compressed audio files, the Board alluded in previous proceedings to the growing popularity of MP3[5] music files, and the fact that MP3 players were becoming more widespread. MP3 continues to be the most dominant and well-known format for compressed digital music. However, other formats also exist, including Sony's ATRAC3, Windows Media Audio (WMA) and Advanced Audio Coding (AAC). In respect of MP3 files, it is generally accepted that one minute of music can be compressed and stored using 1 Mb of memory. Uncompressed music requires 10 Mbs.

CPCC refers to devices intended for use primarily to record and play music as "MP3 players". As explained below, in these reasons the Board targets products with non-removable memory capable of, and ordinarily used for, recording digitally any format of music and refers to them simply as "digital audio recorders".

Some products have no internal memory, and only have slots that accept removable types of memory.[6] These products are players. Some products have only internal memory, or internal memory and slots that accept removable memory. These are recorders. Although the Board heard that the trend was toward producing digital audio recorders that only contain non-removable internal memory, products still exist on the market that accept removable memory.

At present, there are two general types of digital audio recorders. One incorporates a spinning hard-disk drive that is technically no different than those in personal computers. The capacity of the memory within such products presently ranges from about 5 to 225 Gbs. These digital audio recorders may be portable, in-car or in the form of a central server. The Apple iPod is among the most familiar of this type of product.

The other type of digital audio recorder incorporates solid state memory that does not contain any moving parts. Most products of this type currently on the market contain between 32 and 128 Mbs, or sometimes 256 Mbs, of storage capacity. Often, these products also have expansion slots that can accept additional removable memory.

Witnesses, including Messrs. Basskin and Ciric, predicted that hard disk based models will become increasingly successful compared to solid state products because of their larger capacity and speed, even though solid state memory contains no moving parts, consumes less power and is typically smaller in size.

Removable electronic memory comes in a variety of formats and may be used for a number of purposes. Some of the more popular removable memory comes in the form of cards sold under the names SmartMedia, CompactFlash, Secure Digital Memory (SDM), MultiMediaCards,

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[5] "MP3" is short for MPEG-3, or Motion Picture Experts Group, Audio Layer 3.

[6] Such products may have internal memory capable of storing ephemeral copies in order to facilitate music playing, but CPCC has not sought a levy on this memory.

MagicGate and MemoryStick. These formats, which utilize solid state memory and are sometimes called flash memory cards, have a capacity typically ranging from 32 to 512 Mbs.

Most removable electronic memory cards have different physical dimensions, and therefore, not all formats are compatible with all digital audio recorders. Indeed, although the evidence was not straightforward, it seems that some formats are compatible with few, if any, digital audio recorders. Some formats are seemingly compatible exclusively, or almost exclusively, with digital cameras, personal digital assistants or other non music related devices. Secure CompactFlash and Ultra CompactFlash appear to be examples of such formats.

Removable memory may also come in the form of micro hard disks, such as the IBM MicroDrive for example. Some removable micro hard disks are designed for use in car audio systems, but some are not currently compatible with any digital audio recorders. Like internal hard disk memory, these products typically have greater capacity than solid state memory.

The Board heard a considerable amount of evidence about another interesting technological development. TPMs and DRM systems are beginning to be used increasingly by rights-holders to control the distribution and use of, and access to, music and other content.

It is not necessary to go into detail about the technical aspects of the software and hardware that drive TPMs and DRM systems. Generally, TPMs are used to prevent unauthorized copying or distribution of content. They may also limit uses that can be made of the content. DRM systems use a similar set of technological tools to allow a person to use content according to his or her wishes, but within parameters that are often predetermined by the rights-holder. For example, rights-holders can use DRM systems to allow consumers to acquire the right to listen only once, or to listen for a whole month, or to make one, five, ten or an unlimited number of copies. DRM technology can thus empower a number of emerging business models.

Such developments were applauded by CPCC as a "holy grail".[7] They were also recognized by most other participants as representing a desirable method of ensuring compensation for rights-holders. DRM systems have facilitated the development of some legitimate online "stores", which are operated or authorized by those in the music industry. Some of the most publicized of these are Pressplay and MusicNet. Services are sometimes subscription-based, or sometimes allow anyone to download a single track, or an entire album. Each offers their own package(s) of rights associated with a subscription or purchase, some of which are more liberal than others.

Overall, the evidence indicated that TPMs and DRM systems have not been fully exploited. Many legitimate music services are not yet available in Canada. Moreover, technology has not affected consumers' ability to copy the vast majority of prerecorded CDs, unlike DVDs. Nor has it succeeded in shutting down peer-to-peer distribution networks, which are discussed below.

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[7] S. Stohn, transcripts at 1501, C. Brunet, transcripts at 2213.

ii. Private Copying Habits

It is difficult to say precisely how many music tracks are being copied in a given period.[8] What is clear is that the sources from which private copies are made have shifted dramatically. Evidence in these proceedings suggests that the Internet is now a dominant source of private copies, accounting for slightly under half of all copies made. Prerecorded CDs are a second significant source while some copies continue to be made from radio and other sources.

One explanation for this change relates to the increased number of Canadians with personal computers, and the penetration of the Internet in Canadian households. Recent data suggests that nearly half of the Canadian homes have access to the Internet. High speed connections, which are available in a growing number of households, make downloading music even more efficient.[9]

The growing number of personal computers with CD burners in Canadian households, the decrease of copying onto audiocassettes and the rarity of stand-alone CD recorders all point to another development. It would seem that not only do almost half of all tracks copied originate from the Internet, more than that are copied through a personal computer. That is, even where the original source of the copy is a prerecorded CD, the evidence suggests that many consumers copy that prerecorded CD onto a computer hard drive, and then copy tracks from the hard drive onto a blank CD. It may also be that some copies are not made through a computer's hard drive, but rather use temporary memory.

The purchaser of a prerecorded CD does not purchase the right to copy that CD. However, the Board heard evidence that a growing, but still small, proportion of tracks downloaded from the Internet are explicitly or implicitly accompanied by the right to make private copies. Music downloads are usually acquired in one of three ways.

First, they may be obtained through peer-to-peer networks, such as Napster, Kazaa, Grokster or Morpheus. Second, they may be purchased through legitimate distribution services, such as Pressplay, MusicNet and others. Third, objectors submitted evidence of authorized free download samples or promotions from various Web sites.

CSMA/Retailers' argument is that almost one third of Canadians have copied at least one promotional track onto a recordable CD. CPCC suggests that authentic free samples are relatively rare, accounting for only 3.5 per cent of downloads. The Board agrees with this assessment for the time being. Moreover, it is not clear whether free samples include the right to private copy.

Changes have also occurred in the uses that consumers make of blank media. According to Circum's research, 75 per cent of individuals stated that the last time they used an audiocassette, it was for the purpose of copying music. For recordable CDs, this figure is approximately 66 percent, and for rewritable CDs, about 50 per cent. The survey evidence of both CPCC and

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[8] In *Private Copying I*, the Board heard that roughly 934 million tracks were copied. In *Private Copying II*, curiously, the Board was told that this number dropped to near 570 million. In the survey period leading up to these proceedings, according to CPCC, Canadians copied just under 1.1 billion tracks.

[9] Exhibit CPCC-4 at pp. 9-10.

CSMA/Retailers shows that between 80 per cent and 90 per cent of individual consumers who buy blank CDs do so in some measure for the specific purpose of copying prerecorded music. Moreover, it appears that over 40 per cent of individuals use recordable CDs for no other purpose. Less reliable evidence suggests that the proportion of individuals who last copied music, as opposed to other content, onto electronic memory, as well as onto blank DVDs, is close to one third.

These figures do not purport to represent a proportion of the total market for such media, but are in relation to the number of media purchased only by individual consumers. To get a feel for the broader picture, it is necessary to consider other aspects of the blank media market.

iii. The Blank Media Market

In these proceedings there are significant discrepancies in the evidence describing the total size of the Canadian market for blank audio recording media.[10] Although the estimates of the market for all products are important to the Board, blank CDs are of particular interest, due to their emergence as the dominant format used for private copying. Consequently, the levy on this format generates the bulk of CPCC's revenues. Since there is a lag in reporting, the debate focusses on sales figures for the year 2001 and the first half of 2002.

Roughly speaking, CPCC collected a levy from manufacturers and importers paid on 90 million CD-Rs in 2001. However, CPCC notes that, according to data from the Santa Clara consulting group,[11] the total market size was approximately 102 million units. Members of the International Recording Media Association (IRMA)[12] say they manufactured or imported just under 50 million units in Canada in 2001. If, as the evidence suggests, they account for 40 per cent of the Canadian market, it would result in a total within the range of CPCC's submission. CSMA members report just over 50 million units during the same period. They represent close to 63 per cent of the total Canadian market. This means the total market would be about 84 million units. By contrast, according to the Retailers' figures, six major retailers representing 75 per cent of the total Canadian market purchased almost 194 million units. Adjusting to take account of the entire retail market, purchases could have been as high as a quarter billion units in 2001.

Much discussion also surrounded the size of the "individual consumer" market in proportion to the total market for blank media. CPCC claims 70.8 per cent of all blank CDs are purchased by individual consumers. CSMA maintains there is no evidence to show that this figure is higher than the 45 per cent used in the Board's last decision. This proportion is potentially important for two reasons. First, it might have an impact upon the Board's application of the definition of an "audio

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[10] Evidence on this subject is scattered throughout the record and the transcripts. The Board notes in particular Exhibits CPCC-17, CPCC-17A, CPCC-19 and CPCC-20, and CSMA-40 (Aid to Argument).

[11] Santa Clara consulting group uses information gathered on the global market to produce different reports. They consult media and writer manufacturers, original equipment manufacturers, regional sales offices, distributors and value added resellers. From the figures they obtain, they assess the Canadian market share and provide a Canadian Study.

[12] IRMA has access to information from its members, which control 80 per cent of the world media market. It provides a North American Study from which CPCC's experts estimate Canadian numbers.

recording medium". Second, it could be a consideration when setting the levy rates.

In contrast to the uncertainty surrounding the size of the blank media markets, there is little debate over prices and pricing trends. With the exception of audiocassettes, the price of which has remained stable, all types of blank media have experienced a downward trend in pricing.

Average Canadian wholesale prices for CD-Rs have fallen over 50 per cent since 1999, and consumers can now purchase a single CD-R at retail for under $1.50, or for about 50¢ each in a package of 100. Single rewritable CDs cost roughly three times as much as single recordable CDs, as do Audio CD-Rs. Audio CD-RWs and MiniDiscs are about $5 each. The price of a blank DVD depends greatly on its format, and ranges from about $10-$24 per unit.

The prices for removable memory and digital audio recorders also vary greatly, depending mainly on form and capacity. The price per Mb for removable memory ranges from roughly 50¢ to almost $4. Generally, the higher the capacity the lower the price per Mb. For non-removable memory embedded in digital audio recorders, the price per Mb might be from $2-$3 for solid state models, but can be as low as 3¢-4¢ for hard disk products. Thus, the retail price of a 32 Mb digital audio recorder is about $115, whereas a 10 Gb and a 20 Gb hard disk digital audio recorder can sell for $350 and almost $600, respectively.

Prices for most types of blank media vary from one retailer to another, both in and outside of Canada. Objectors submitted evidence of comparative pricing in the United States and Canada in an attempt to persuade the Board that incentives exist for cross-border shopping. The Board accepts that well-informed consumers can always find a bargain, but it is not apparent that one can routinely find better deals in the United States, especially when factoring in the exchange rate, costs of shipping and other tangible and intangible barriers.

iv. CPCC's Extended Zero-rating Program

Zero-rating is a mechanism, developed and administered voluntarily by CPCC, whereby organizations are made eligible by CPCC to purchase media directly from certain manufacturers, importers or special distributors levy-free.

The current program was implemented in response to objectors who claimed during the first proceedings that it was unfair for those who do not use media to copy music to pay the levy. Although only societies representing the perceptually disabled are exempt by legislation, CPCC undertook to accomodate other categories of purchasers.

The program currently applies only to audiocassettes, Audio CD-R and CD-RWs and MiniDiscs. CPCC invites certain persons or organizations including religious organizations, broadcasters, law enforcement agencies, courts, tribunals, court reporters, provincial ministers of education and members of the Association of Universities and Colleges of Canada, music and advertising industries, to apply for a certificate number allowing them to buy media levy-free. At present, CPCC imposes a minimum purchase requirement of 1000 units per year, although it may allow users to group their purchases. Purchasers must sign a contract agreeing to restrictions on their use of blank media, and allowing for audits to verify their activities. Purchasers cannot buy media through channels of their choosing, but can only buy from specific sellers, who must also be

approved and registered by CPCC.

Manufacturers, importers and certain distributors may be permitted by CPCC to sell media to zero-rated purchasers. If a distributor has signed an agreement with CPCC, it may sell media on a levy-free basis and claim back a credit or refund from the manufacturer or importer, who may in turn claim a credit from CPCC. CPCC may also designate as special distributors those who regularly sell a significant quantity of blank audio recording media to zero-rated users. Special distributors are eligible to purchase media levy-free from manufacturers or importers and avoid the credit/rebate procedures. To be eligible for the program, a seller must contractually agree to the conditions, including audit provisions, imposed by CPCC. As of last December, about 50 organizations had signed up to sell zero-rated media.

Shortly before this hearing, CPCC announced that it intends to make changes to its zero-rating policies. It promised to extend the program to include CD-Rs and CD-RWs, while grand-fathering the program for audiocassettes. It clarified that its list of eligible groups, under the extended program, was not exhaustive and that it would consider an application by any organization. It also said it plans to abolish the minimum purchase requirement. Instead, CPCC intends to require an annual registration fee of $15 for non-commercial users and $60 for commercial users. Although it was previously emphatic that retailers would not be able to participate in the program, during the hearing CPCC expressed a willingness to negotiate on this point. However, CPCC has maintained throughout that its program must be administratively workable, cost effective and not open to abuse.

Despite CPCC's announcement, the program was the subject of debate amongst the participants. Much of the debate, however, does not concern facts or evidence, but relates to legal and policy issues that are discussed below.

In sum, as a result of all the developments discussed above, this decision marks a crossroads for the Board. Therefore, before proceeding, it is worthwhile describing again the Board's understanding of the legal framework underlying the regime, in order to better focus the issues confronting everyone.

D. THE LEGALITY OF PRIVATE COPYING

Part I.A of *Private Copying I* describes the private copying regime. To recapitulate, Part VIII of the *Act* ("Part VIII") came into force on March 19, 1998. Until then, copying a sound recording embodying the performance of a musical work for any purpose not permitted in the *Act* infringed the copyright holder's reproduction right. In practice, copyright owners were unable to prevent or license private copying. The private copying regime was set up as a practical answer to this problem.

Section 80 creates an exception to the exclusive reproduction right; it legalizes private copying onto audio recording media. Section 81 entitles eligible authors, eligible performers and eligible

makers to remuneration as compensation for the expropriation of their exclusive rights.[13] Section 82 imposes on those who manufacture or import blank audio recording media for the purpose of trade liability to pay a levy. Section 83 permits a collective society to propose tariffs, and requires the Board to consider and certify the tariff and its terms and conditions.

Certain issues concerning Part VIII have come to light since the enactment of the regime. The Board was asked expressly to comment upon several nuances relating to the legal framework, and in particular upon its relevance to peer-to-peer networks, the application of fair dealing exemptions and other matters.

The exemption in section 80 applies only when a copy is made for the private use of the person making it. This expressly excludes selling, renting out, exposing for trade or rental, distributing, communicating to the public by telecommunication, or performing in public the copy made.[14] This means that making a copy of a CD of the latest release by the hottest star to give to one's friend is still an infringing action, as it is not a copy for personal use. In the same vein, distributing this same copy to friends online is prohibited.

In these proceedings, the liability of persons uploading, distributing or communicating music through these services is not at issue. Nor is the liability of those providing software, operating networks or Internet connections.[15] Peer-to-peer distribution on the Internet is not addressed as such in the regime. In this respect, other copyright considerations certainly apply. However, we are only dealing here with the end copies.

The regime does not address the source of the material copied. There is no requirement in Part VIII that the source copy be a non-infringing copy. Hence, it is not relevant whether the source of the track is a pre-owned recording, a borrowed CD, or a track downloaded from the Internet.

Although the source of the copy does not matter, the destination does. The Board believes that section 80 creates an exemption that applies as long as two conditions are met: the copy must be for the private use of the person making it, and it must be made onto an audio recording medium, as defined in section 79.

Some might argue that the exemption requires a certified tariff on a particular kind of medium, or a levy paid on a particular unit, and that media which have never been the subject of a proposed

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[13] Pursuant to section 85 of the *Act*, eligible rights-holders are authors of musical works in which copyright subsists in Canada, as well as performers and makers who are citizens or residents of Canada or of a country referred to in a ministerial statement. No such designation has been made to date.

[14] Subsection 80(2) of the *Act*.

[15] Canadian courts are dealing with related issues in the context of the review of another of the Board's decisions: see *SOCAN Statement of Royalties, Public Performance of Musical Works 1996, 1997, 1998 (Tariff 22, Internet) (Re)*, [1999] 1 C.P.R. (4th) 417; *Society of Composers, Authors and Music Publishers of Canada* v. *Canadian Assn. of Internet Providers* (C.A.) (2002) 4 F.C. 3, application for leave to appeal to the SCC granted, [2002] SCCA No. 289. American courts have also considered some of these issues recently: see for example *Metro-Goldwyn-Mayer Studios Inc. et. al. v. Grokster, Ltd. et. al.*, CV 01-08541-SVW, (C.D. Cal. 2003); and *A and M Records, Inc* v. *Napster, Inc.* 239 F.3d 1004 (9th Cir. 2001).

tariff are not covered by the exemption. The Board does not agree.

It would indeed seem illogical that the scope of the exemption could depend on the rights-holders' unilateral choice to propose or not a tariff. For instance, simply because the Board has not been asked to certify a tariff on hard disks in personal computers, it does not follow that private copies made onto such media infringe copyright. Moreover, to argue that a private copy on a particular kind of medium is legal only if a levy was paid on that particular unit would be to add a condition that is not currently included in section 80.

However, an audio recording medium to which no tariff applies because the Board has decided that such a medium is not of a kind ordinarily used by individuals for recording music is, in the Board's opinion, removed from the ambit of the exemption. For instance, in *Private Copying I*, the Board decided that audiocassettes of less than 40 minutes do not attract a levy. Considering the wording of section 80, this means that copying music onto such cassettes infringes copyright. It is, however, for the courts of civil jurisdiction to ultimately determine whether or not there is an infringement of copyright for private copies made onto a specific medium, unless the legislator intervenes.

Another point to discuss relates to other exemptions within the *Act*, in particular fair dealing pursuant to sections 29 or 29.1. The Retailers argue that much private copying is, and always was, fair dealing. They suggest that many consumers "research" potential purchases by first making private copies. Hence, according to the Retailers, such activities should be accounted for in determining the levy rates.

It is not necessary for the Board to comment on the scope of the fair dealing exemption in this case. In the Board's view, it is irrelevant whether or not some private copying was previously fair dealing. All private copying is now exempt, subject to a corresponding right of remuneration. Put another way, any private copying that might formerly have been fair dealing is now subsumed within the express exemption in section 80 of the *Act*.

E. ZERO-RATING PROGRAM: JURISDICTIONAL ISSUES

The Board explained in previous decisions that the private copying regime, in particular section 82, is universal. By this it meant that a levy is payable on every blank audio recording medium manufactured or imported in Canada for the purpose of trade. One limited exemption aside,[16] the law states that every manufacturer or importer acting for the purpose of trade is liable to pay the levy on every audio recording medium, regardless of the ultimate purchaser's identity or the medium's ultimate use. It is generally accepted that the costs of the levy are passed on to end users. Yet, it is an open question whether Parliament intended all end users to bear the burden, or merely those individual consumers who copy music.

Some believe that the regime cannot survive, in its current form, without some reprieve for those who do not private copy. Since the *Act* provides no formal mechanism to accommodate those

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[16] Section 86 exempts sales to societies representing the perceptually disabled. Such societies are entitled to a refund if they purchase media not directly from a manufacturer or importer.

persons, CPCC submits the task falls to it. By removing those who cannot copy music from the effects of the regime, CPCC likens itself to Michelangelo removing marble to reveal a pre-existing sculpture.[17] That is, Parliament must have intended CPCC to insulate them from the scope of the regime through zero-rating.

The Board believes that if Parliament intended to insulate non copiers from the effects of the regime, it could have and would have established mechanisms within the *Act*. Yet Part VIII includes only one exception, to accommodate perceptually disabled persons. The Governor in Council has the power to exclude from the regime media that would otherwise be subject to a levy. That power has not been exercised. Alternatively, Parliament might have provided the Board with the tools to accommodate those who do not use blank media to copy music. But the *Act* delegates no such authority to the Board.

All of these considerations suggest strongly that, under the existing legal framework, only those mentioned expressly were intended to be exempt from payment of the levies. It is not for the Board, nor CPCC, to assume the role of the legislator by implying additional exemptions, reasoning that they should be implied from the wording of the *Act*. In another context, when asked whether the right to make ephemeral recordings was implicitly included in the right to broadcast a performance, the Supreme Court of Canada stated that: "Furthermore, an implied exemption to the literal meaning of s. 3(1)(d) is all the more unlikely, in my opinion, in light of the detailed and explicit exemptions in s. 17(2) (now s. 27(2)) of the *Act*...". It also added that: "if such a change is to be made to the *Act*, it should be made by the legislature, and not by a forced interpretation."[18] As submitted by the Retailers, even if the *Act* allowed some form of implied exemption scheme, then responsibility for it would certainly lie with the Board and not with the regime's primary beneficiaries.

As outlined above, CPCC has undertaken voluntarily to "zero-rate" certain transactions. There are three recurring themes throughout the arguments on this topic.

First, some objectors have concerns that are either principled or pragmatic. They question the appropriateness of a voluntary exemption designed and administered directly by the beneficiaries of the levy. Most of them take the position that the Board has jurisdiction to deal with this issue, and must not leave the matter to CPCC. They propose various ways for the Board itself to address the issue, including a zero-levy or a refund scheme.

Others objectors do not object to the concept of zero-rating *per se*, but insist that the Board ensure the program is fair and equitable. It must not be too onerous, bureaucratic and time-consuming. Some specifically take issue with audit requirements and registration fees, and complain that zero-rated media are only available from limited sources.

Second, manufacturers, importers and retailers all say zero-rating is illegal and inherently unauthorized. They argue that the Board and CPCC have only the jurisdiction conferred upon them

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[17] C. Brunet, transcripts at 3414.

[18] *Bishop v. Stevens*, [1990] 2 S.C.R. 467 at 485. See also *Harvard College v. Canada* (*Commissioner of Patents*), [2002] S.C.J. No. 77 (QL) *per* Binnie (dissenting) at para. 55.

by Parliament, and exemptions can only be created by statute. They emphasize that had Parliament intended there to be more than one exemption in the statute, it would have said so. According to this argument, it is not within the purview of the Board, nor CPCC, to assume the role of lawmaker. The Retailers add that the zero-rating program simply disguises inherently flawed legislation.

The Retailers submit, in the alternative, that if zero-rating is necessary, then the Board itself must use its "blank cheque" to address the issue within the tariff.[19] They argue that it is illegal for the Board to delegate responsibility for this program to the beneficiaries of the levy. At the very least, according to the Retailers, the Board must exercise its "supervisory responsibility"[20] and establish guidelines for the program.

From a practical standpoint, the Retailers' objections focus on the market distortions that zero-rating creates; they do not want to lose retail sales to customers who must buy only from authorized suppliers of zero-rated media. Hence, they argue that CPCC's current program, which excludes them from participating, is also unfair and arbitrary. Manufacturers' and importers' concerns are similarly practical; they do not want to be burdened with the administrative inconvenience that zero-rating creates.

Third, rights-holders said in the first proceedings that the Board cannot create exemptions; the Board cannot say that manufacturers and importers need not pay a levy on sales to certain end users. However, rights-holders recognized that some might consider it unfair for certain non-copiers to pay the levy and undertook to remedy the problem. In the second proceedings, their arguments in respect of zero-rating were mainly economic. In effect, they wanted the Board to compensate for this program by raising the levy rates.

In the present proceedings, rights-holders argue that the Board has no control over, or power to stop them from, zero-rating. Once zero-rating has occurred, they say it is fair and equitable that they not suffer as a result. In short, rights-holders say zero-rating is only relevant to the Board as a market reality that should be accounted for after it has occurred. They submit that their program is implicitly in accordance with the purposes of the regime. Indeed, because the *Act* is silent, CPCC submits it must accommodate those who cannot copy music.

The Board's predicament is as follows. If it creates an exemption in the tariff, it will hear cries that it acted beyond its jurisdiction. If it does not, it will be accused of failing to exercise its jurisdiction and refusing to act fairly and equitably.

Much turns on the interpretation of the legal framework surrounding the regime. If Parliament intended the burden of the levy to be borne by all end users, except those specifically exempted by legislation, then zero-rating goes against that purpose. If instead Parliament intended the costs of the levy to be borne ultimately only by those end users who engage in private copying, then zero-rating works toward that end. The question that would follow is whether the Board can legitimately

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[19] H. Knopf, transcripts at 3763. For example, although there was little evidence in this respect, the suggestion was made to effectively "zero-rate" all CDs sold in packages of more than 100, or perhaps 400. H. Knopf, transcripts at 3762.

[20] H. Knopf, transcripts at 3758.

leave this task to rights-holders.

There are valid arguments in favour of zero-rating. By definition, a business or other organization cannot engage in private copying. Thus, from a policy standpoint, they may not be the purpose for, nor the beneficiaries of the private copying regime. A mechanism that removes such stakeholders from the ambit of the levies might further strengthen the nexus between the regime and its goals, and might also reduce the incentive to turn to foreign suppliers for blank media purchases.

There are less compelling reasons for an exemption for individual consumers who do not private copy. The evidence suggests, for example, that 80-90 per cent of consumers use some blank CDs to copy music, and 40 per cent use blank CDs for no other purpose. Although not all individuals use all media for that purpose, we must bear in mind that the rate is discounted to reflect this fact.[21] Also, the *Act* legalizes private copying in Canada; there is value in the option to private copy, even for those who choose not to exercise that option.

Regardless, the question is not whether or not zero-rating is desirable, but whether or not the Board, or CPCC, is legally authorized to initiate such a program. Because there is no legislative guidance to the contrary, the Board believes it does not have the legal authority delegated from Parliament to exempt those who are, under the *Act*, liable for the payment of levies. As structured, the zero-rating program creates exemptions. For all these reasons, the Board considers that the program has no legal basis and is therefore illegal. The Board is greatly relieved that lawmakers have recognized the problems associated with this issue in the recent report on the provisions and operation of the *Act*.[22]

The Federal Court of Appeal has held recently that the Board has broad discretion when establishing terms and conditions related to tariffs.[23] Should zero-rating implicitly be an intrinsic part of the private copying regime, then the Board should administer the exemption, not CPCC. Thus, if zero-rating is indeed a necessary component of a workable regime, then the Board could incorporate the program as part of the "terms and conditions related to [the] levies as the Board considers appropriate".[24] CPCC could then administer it as part of the tariff. As the *Act* now stands, the most untenable response is to delegate ultimate control to the beneficiaries of the regime.

Aside from the lack of legal support for zero-rating, the Board has some serious reservations about the fairness of the proposed implementation of CPCC's extended program. The program has been tested on the audiocassette market, to the extent that end users complain much less about the levy on that medium. However, its possible effects on other markets, especially blank CDs, cause grave concerns.

First, the stakes are much higher in the context of blank CDs because of the number of units that

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[21] See for instance *Private Copying II* at 14.
[22] See Exhibit RETAILERS-28, Government of Canada, Supporting Culture and Innovation: Report on the Provisions and Operation of the *Copyright Act*, Ottawa, 2003.
[23] *Neighbouring Rights Collective of Canada v. Society of Authors, Composers and Publishers of Canada*, (2003) FCA 302; [2003] F.C.J. No. 1094 (QL).
[24] *Act*, s. 83(8)(*a*)(ii).

might be zero-rated. CSMA and the Retailers made clear that zero-rating creates serious distribution problems, because it forces sales outside the normal supply chain. The number and breadth of types of organizations that might be zero-rated are much greater than in the audiocassette market. CPCC's own estimates, which it acknowledges are only rough guesses, puts the number of potential registrants in the thousands. By even the most conservative estimates, one would not be surprised if tens of millions of units were diverted from existing channels of distribution. Second, objectors expressed reluctance to pay any registration fees. Some objectors also expressed concerns about the potential for arbitrary application of the program.

Another concern relates to possible future compensation for the program. The Board's role is to establish the levy rates and their related terms and conditions. Once that is done, the Board cannot compel CPCC to collect the levies, if it has so decided. CPCC has indicated that it intends to ask for compensation for zero-rated CDs in the next tariff. The Board is concerned about the impact of such a request on the level of the levy rate. However, it must be noted that in this instance, CPCC has not asked the Board to increase the levy rate on CDs in anticipation of the extended zero-rating program.[25]

The potentially serious effects of zero-rating on the CD market are themselves sufficient to explain the change in the Board's views. Yet, to be blunt, the reason that the Board has reconsidered its response to zero-rating is that it could not foresee the effects of the program. During the last proceedings, zero-rating was not the pivotal issue it is now. The Board heard little argument on the topic, and there was little indication of its broader implications. This decision is based upon a more complete record.

II. CONSTITUTIONAL MATTERS

The constitutionality of Part VIII of the *Act* was addressed in *Private Copying I*. At that time, there were three principal attacks on the regime. First, it was alleged that the regime is not copyright law, and hence *ultra vires* the legislative competence of Parliament. Second, it was argued that the regime is merely a disguised tax, which was not enacted following proper procedural requirements. Third, it was submitted that the regime violates paragraph 2(*a*) and section 15 of the *Charter of Rights and Freedom*.[26]

In these proceedings, the Retailers reiterate only the first two of these attacks. The Board is not persuaded that any of the arguments are genuinely novel, and therefore it adopts the reasoning from its previous decision. Nevertheless, some nuances should be addressed.

A. IS PART VIII COPYRIGHT LAW?

The allegation that Part VIII is not, in pith and substance, a matter of copyright law is again put forward. It is once again submitted that there is no connection between those who are liable to pay the levy (the manufacturers and importers) and those media which may or may not be used to private copy. Furthermore, it is alleged that the regime is cast too broadly: those who must pay the

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[25] See, for example, D. Collier, transcripts at 1919-1920; C. Brunet, transcripts at 1839.
[26] Schedule B of the *Canada Act* (U.K.), 1982, c. 11.

levy have no control over the use to which the blank audio recording media will be put.

Once again, the Board must reiterate that the dominant feature of Part VIII, when one looks at its pith and substance, is within the scope of copyright law. It is irrelevant that some sections of the private copying regime, namely, sections 81 and 82, do not explicitly mention the word "copyright". This regime is clearly a subject-matter for copyright.

Mr. Pitt notes that section 81 makes it clear that the remuneration paid by importers and manufacturers of blank audio recording media is "in respect of the reproduction for private use of ...musical works".[27] To the Board, the words "in respect of" indicate that Parliament recognized that payers of the levy do not themselves engage in the reproduction of musical works. This alone does not mean that the regime is not copyright law. Instead it means the Board must strive to correlate the amount of the levies with private copying habits, the value of consumers' exemption from liability, the remuneration due to rights-holders and other underlying rationales for the private copying regime.

Section 82 sets out clearly who will pay the levy, to whom and why. It is clearly linked to the preceding section, and to the overall regime. To claim that these sections, and the concept of "blank" media, are somehow "anti-copyright" is simply wrong. To determine the pith and substance of Part VIII, two aspects must be examined: the purpose of the legislation, and its legal effects.

The purpose of the private copying regime was examined above; it is clear that its existence depends on the reproduction right, and the inability of rights-holders to enforce it in the context of mass infringement. This goes to the "mischief" or the problem that Parliament sought to solve through the legislation.[28]

The effects of the regime are also clear; rights-holders are remunerated, and individual Canadians who indulge in private copying now do so legally. That the price for doing so is borne, in part, by those who do not private copy is not relevant in deciding whether the regime is copyright law in pith and substance. Viewed from its purpose and its effects, Part VIII is a valid exercise of Parliament's jurisdiction over copyright law. All sections of the regime are clearly and tightly linked to Parliament's goal to compensate rights-holders in respect of the reproduction of music for private use.

B. IS THE PRIVATE COPYING LEVY A TAX?

Once again, the argument that the private copying levy is a tax has been put forward.[29] For reasons stated in *Private Copying I*,[30] and adopted here, the Board does not believe that the levy is a tax. Nothing material has been brought forth since then to warrant a change in the Board's analysis of

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[27] R. Pitt, transcripts at 2262-2273.
[28] *Reference re: Firearms Act*, [2000] 1 S.C.R. 783.
[29] Should this contention be right, then Part VIII was improperly enacted, as its introduction did not comply with sections 53 and 54 of the *Constitution Act*, 1867.
[30] *Private Copying I*, at 13-17.

this issue.

However, the question of nomenclature should be addressed. Much has been made about the difference or similarity between the nouns "levy", "royalty" and "tax", in both English and French. In particular, the Retailers submit that the only overlap in the translations of "levy" and "*redevance*" involves the word "tax". The Board rejects this argument, as it would attach too much importance to mere labels. The analysis is better served by asking whether the regime is, by design or in practice, a tax or a type of regulatory charge.

The Retailers describe a royalty as "financial consideration paid for the right to use the copyright or patent or to exercise a similar incorporeal right..."[31] In essence, this description mirrors a user fee. According to CPCC, a user fee is only one type of regulatory charge. That is, even if the levy is not a user fee, it can still be a regulatory charge and hence not a tax. In *Westbank First Nation* v. *British Columbia Hydro and Power Authority*,[32] the Supreme Court commented on an earlier judgment, *Eurig Estate (Re)*.[33] In this judgment, Major J. stated that, "[a]nother factor that generally distinguishes a fee from a tax is that a nexus must exist between the quantum charged and the cost of the service provided".[34] The Court in *Westbank* described this "nexus" requirement as "another possible factor to consider"[35] when attempting to distinguish a tax from a user fee. It held that a user fee is merely "a subset of regulatory charges".[36]

According to CPCC, *Westbank* suggests that the "nexus" requirement is not necessarily applicable in this case, as nobody is suggesting that the levy is a user fee. CPCC submits that the Retailers have concentrated on the wrong sort of regulatory scheme; the absence of a nexus between the amount charged and the cost of the service provided is not always indicative of a tax.

The Board agrees with CPCC's interpretation of the Supreme Court's comments in *Westbank*. Hence, the fact that CPCC recognizes it does not provide any service to manufacturers or importers in exchange for payment of the levy (the reason for which it claims it does not collect nor remit goods and services tax on the levies) does not necessarily mean that the levy is a tax.

Even if the Board is mistaken in this conclusion, however, it continues to believe, for the reasons discussed in *Private Copying I*, that a sufficient nexus exists to render the levy a regulatory charge rather than a tax. The Board also continues to believe that the levies are not imposed by a public body, since the Board can neither set the tariff process in motion nor collect any amounts owing. Moreover, although the *Act*, like any other statute, was enacted at least in part to benefit the Canadian public, it is inaccurate to say the levies are for a public purpose.

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[31] J. Macera, transcripts at 3331.
[32] [1999] 3 S.C.R. 134.
[33] [1998] 2 S.C.R. 565.
[34] *Ibid*., para. 21.
[35] *Westbank, supra* note 32 at 22.
[36] *Ibid*.

III. DEFINITION OF AN AUDIO RECORDING MEDIUM

A. LEGAL INTERPRETATION

The definition of an "audio recording medium" in section 79, which applies only to Part VIII, describes products subject to a levy. It reads as follows:

> 'audio recording medium' means a recording medium, regardless of its material form, onto which a sound recording may be reproduced and that is of a kind ordinarily used by individual consumers for that purpose, excluding any prescribed kind of recording medium.

There are two aspects of this provision that are relevant to the Board in these proceedings. The first relates to the proper interpretation of the phrase "ordinarily used by individual consumers for that purpose". The second relates to the relevance of a medium's physical attributes ("a recording medium, regardless of its material form"), particularly the significance of its incorporation into a device. Also, a related nuance concerns the notion of "blank" media.

i. "Ordinarily Used by Individual Consumers for that Purpose"

The first aspect of this provision has been dealt with on two occasions by the Board, and considered by the Federal Court of Appeal in *AVS Technologies Inc.* v. *Canadian Mechanical Reproduction Rights Agency*.[37] In that case, Linden J.A. stated:

"The key point is whether the Board had to decide the meaning of "ordinarily used" by looking at the products generally, as contended for by the applicant, or by considering the use by individual consumers of that product. In my view, it is the usage by individual consumers that must be ordinary, not the use of the product generally, because of the insertion of the words "by individual consumers", which have to be given some meaning. If these words were not there, the applicants' contention would have been more solidly grounded. The French version is consistent with this interpretation as there is also a reference to use by "*consommateurs*", who are generally considered to be individuals, not corporations or institutions.

[...]

The applicants argued that the interpretation of the term "ordinarily" should be guided by dictionary definitions such as "usually" or "commonly" and by certain authorities from other contexts they cited, which indicated it should be defined as "chiefly" or "mainly". Later, they suggested that a number approaching 50 per cent of the products used in this way might be considered to be used ordinarily. In my view, these definitions and cases are not very helpful. Nor is the percentage approach, for that would be arbitrary. Moreover, it would mean that the artists would receive no compensation at all for the infringement of their copyrights until nearly one-half of all the products are so used. This would hardly be consistent with the object of the legislation."

Objectors suggest that these particular comments are not binding on the Board. The Federal Court

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[37] *Supra* note 1.

of Appeal reviewed the Board's decision on a standard of patent unreasonableness; it does not follow that the Board's first decision was correct. Moreover, some objectors submit that a reviewing court might look more closely at this decision of the Board.

The task at hand is to interpret and apply the provision at issue. In this interpretive exercise, strictly speaking, the Court's comments may be *obiter dicta*. This does not mean that these remarks should not be given weight. The Court's insight into this provision confirms the Board's own view of the matter.

The phrase "ordinarily used" cannot be seen as purely quantitative.[38] Linden J.A. confirmed that a percentage approach would be arbitrary, and the Board believes the same can be said of other solely quantitative benchmarks. A qualitative and quantitative approach is more in line with the purpose of Part VIII, in that it allows the levy to more easily adapt to market realities and the private copying habits of Canadians. It is also consistent with the established interpretation of other provisions of the *Act*.[39]

Some stakeholders are seeking a bright line marker. However, the language, context and purpose of section 79 do not support such an approach. It is clear that Parliament desired, above all, sensitivity to market realities and the flexibility to adapt to a changing environment.

In the Board's view, therefore, there are a number of factors that will determine whether a given kind of medium is ordinarily used by individual consumers for copying sound recordings. Among these are the apparent purpose of the medium, as evident from its invention, design and promotion, and its actual use, as indicated by surveys, testimony or other evidence. The Board might also take account of its current or potential rate of adoption in the market.

As confirmed by the Federal Court of Appeal, individual consumers are key in this analysis. The Board's focus on individual consumers includes consideration of both the extent to which the media is used by consumers for copying sound recordings in contrast to other uses, and the extent to which consumers, when copying sound recordings, use that media in contrast to other media. Moreover, the Board is concerned more with individual consumers as a group than with the habits of any particular person. In this respect, the sheer volume of a kind of media that are used for private copying might suffice to qualify its use as "ordinary", irrespective of percentages.

Thus, in *Private Copying I*, the Board held that recordable and rewritable CDs were ordinarily used by individual consumers, even though, as a proportion of total blank CDs sold, individual consumers accounted for a relatively small share. The evidence clearly established that individual

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[38] The Board stated in *Private Copying I*, at page 29, "the ordinary character of an occurrence is not necessarily a function of quantity, but rather a matter of consistency." Mr. Carruthers characterised the concept in an apt manner: he suggested something was ordinary if "it isn't weird ... and it is done by many many people." J. Carruthers, transcripts at 3094.

[39] Such as the notions of "substantial" part, "fair" dealing and "public" performances, for example. See *CCH Canadian Ltd.* v. *Law Society of Upper Canada*, [2002] 4 F.C. 213 at paras 92-97, leave to appeal to the SCC granted, [2002] SCCA No. 317; *Édutile Inc.* v. *Automobile Protection Assn.*, [2000] 4 F.C. 195 at para. 22; *Ladbroke (Football), Ltd.* v. *William Hill (Football) Ltd.*, [1964] 1 All E.R. 465 at 469, 473 (H.L.); and Vaver, D., *Copyright Law* (Toronto: Irwin Law, 2000) at 145.

consumers who did use blank CDs, often used them for copying music, and that, in total, a very substantial number of CDs were used for that purpose. Moreover, the Board predicted (correctly so in hindsight) that blank CDs would become a dominant media in the world of private copying. By contrast, the evidence suggested that some media, including Digital Audio Tapes (DAT) for example, were used almost exclusively by professionals, and their uses were not expected to change significantly.

ii. Medium or Device

A second aspect of the definition of an "audio recording medium" relates to the form of the medium. This issue is important because the Board was asked to establish a levy on memory in devices, although not on devices themselves. Hence, the question at this stage is whether or not the incorporation of a product into a device can affect its status as an audio recording medium.

CSMA argues that upon being incorporated into a digital audio recorder, memory becomes integrated in, and inseparable from, the device, and thus loses its separate identity. In support of this position, CSMA cites anti-dumping decisions rendered by the U.S. Department of Commerce.[40] For their part, the Retailers submit that CPCC's proposal does not and cannot distinguish between devices and media. Other objectors point to the lack of technical distinctions between certain products proposed to be levied and certain products that are not, and the lack of meaningful distinctions between removable and non-removable memory.

According to CSMA, the Retailers and other objectors, the Board has no jurisdiction under Part VIII to certify a private copying tariff on devices. More particularly, the Retailers argue that the legislative history in Canada indicates that only a medium, and indeed only audiocassettes, were intended to be covered by the *Act*. Objectors submit that, in other countries, devices are subject to a tariff, if at all, only as the result of deliberate legislation.

Regardless, the Board is concerned here with the Canadian *Act*, which contains its own instructions about which products are subject to a levy. In part for this reason, neither foreign legislation nor American anti-dumping decisions are determinative. The starting point is to read the words of our *Act* "in their entire context, and in their grammatical and ordinary sense harmoniously with the scheme of the *Act*, the object of the *Act*, and the intention of Parliament."[41]

As regards the physical characteristics of the product itself, the definition of an "audio recording medium" could hardly have been drafted more broadly. Specifically, the English version of the

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[40] Department of Commerce, International Trade Administration, "Notice of Final Determination of Sales at Less Than Fair Value - Static Random Access Memory Semiconductors from Taiwan" A-583-827 (23 February 1998), available online: http://ia.ita.doc.gov/frn/9802frn/a583827.htm; and Department of Commerce, International Trade Administration, "Notice of Final Determination of Sales at Less Than Fair Value - Static Random Access Memory Semiconductors from Korea" A-583-828 (23 February 1998), available online: http://ia.ita.doc.gov/frn/9802frn/a580828.htm.

[41] E. Driedger, *Construction of Statutes*, (2nd ed., 1983) at 87; *Barrie Public Utilities v. Canadian Cable Television Association.*, [2003] S.C.J. No. 27 (QL) at para. 20; *Bell ExpressVu Limited Partnership* v. *Rex*, [2002] 2 S.C.R. 559 at para. 26; s. 12, *Interpretation Act*, R.S. 1985, c. I-21.

text contains the clause, "regardless of its material form". To the Board, the plain and ordinary meaning of this phrase rules out the possibility that the levy was intended to apply only to "removable" media, let alone only to audiocassettes.

This language also demonstrates that it is not determinative whether the medium is affixed, incorporated or otherwise integrated in a device. Its breadth supports the conclusion that liability to pay a levy cannot be dependant upon physical characteristics alone. A medium that is incorporated into a device remains a medium.

In addition to the express statutory language that demands such an interpretation of this definition, the Federal Court of Appeal recently confirmed that, "[w]here its language and underlying rationale permit, legislation should be interpreted in a way that takes account of technological developments."[42] Notably, these remarks, made in the course of judicial review of another of the Board's decisions, pertained specifically to the *Act*. To limit the application of the levy to only removable kinds of media would be to restrict the definition of "audio recording medium" in a manner inconsistent with this principle. Thus, the context and purpose of this particular provision, which was to provide remuneration for rights-holders whose music is copied onto such products, only confirms this conclusion.

The Board realizes that Parliament could not have imagined recent technological developments when this regime was enacted.

The Board is also aware that American jurisprudence advises caution in this respect.[43] Nevertheless, the Board is bound to follow the guidance of Canadian courts, especially given Parliament's clear intention to make section 79 technologically neutral.

However, the Board is comforted that the definition excludes any media of a kind prescribed by the Governor in Council. Thus, although this section has not yet been invoked, the *Act* contains an internal mechanism whereby the Board's conclusion on this matter can be considered and easily altered, if so desired, by those better situated to deal with this controversy.

iii. "Blank" Media

Some participants suggest to the Board that certain media are not subject to a levy because they are not technically blank. In particular, the evidence established that certain media, including memory integrated into Apple's iPod for example, undergo testing as part of the manufacturing process. Such testing involves recording sounds onto the media.

Objectors point out that the *Act* requires payment of a levy only on "blank" audio recording media, which are defined as follows:

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[42] *SOCAN* v. *CAIP*, [2002] 4 F.C. 3 at para.122. See also *Théberge v. Galerie d'Art du Petit Champlain inc.*, [2002] S.C.J. No. 32 at para. 113 *per* Gonthier J. (dissenting).
[43] *Sony Corp. of America v. Universal City Studios, Inc.*, 464 U.S. at 431.

‘blank audio recording medium’ means

(*a*) an audio recording medium onto which no sounds have ever been fixed, and

(*b*) any other prescribed audio recording medium;

Since, they submit, certain media have had sounds recorded upon them, such media are not leviable.

A tariff proceeding before the Board is not the proper forum in which to resolve this debate. The key reference to *blank* media is in section 82, which imposes liability for the levy on a manufacturer or importer of a blank medium. The notion of a “blank audio recording medium” appears nowhere in the context of its obligation to establish the levies. The Board’s duties are, among certain other things, to determine the manner of calculating the levies and their related terms and conditions. In the present context at least, it is not for the Board to determine whether or not an “audio recording medium” is blank.

It might contravene common sense if one could avoid payment of the levy through testing procedures designed to ensure that a medium can record sounds as intended. The *Act* contains a mechanism to counteract any potential absurdity. If appropriate and desirable, the Governor in Council can by regulation include such a medium within the scope of the levy.

B. ANALYSIS

Not much time was spent analysing or criticising the proposed levy rates on audiocassettes, and most participants concede these are properly subject to a levy.

MiniDiscs and CD-R and CD-RWs Audio have been subject to a levy in the past. In these proceedings, the Board questioned whether this was appropriate. The Board has previously operated on the unproven assumption that 95 per cent of this type of medium are used by individual consumers. However, CD-R and CD-RWs Audio might also be used by professionals. A number of indicia point to this inference, including the apparent lack of perceptible quality benefits to the average consumer, the higher price point, the limited availability and other specialized characteristics of this format. Nevertheless, in the absence of proof, the Board maintains the status quo and certifies a tariff on these media. It should not be taken for granted that the Board will do the same in the future.

Given that CD-Rs and CD-RWs now are overwhelmingly the dominant format onto which individuals copy music, by even the lowest standard advocated by the main participants in these proceedings, these media are leviable.

The existing tariff applies to all CDs, irrespective of their storage capacity. In its proposed tariff, CPCC restricts the application of its tariff to CD-Rs and CD-RWs of 100 Mbs or more of storage capacity. However, no evidence was submitted to that effect other than to mention that CPCC has started to voluntarily forego collecting the levy on these small capacity CDs. In addition, CPCC’s proposed tariff is ambiguous with respect to the application of the levy to CD-Rs Audio and CD-RWs Audio of less than 100 Mbs. Indeed, CD-Rs and CD-RWs Audio of less than 100 Mbs are

not excluded from the proposed rates. However, the definition of "blank audio recording medium" in the proposed tariff considers CD-Rs and CD-RWs Audio as recordable compact discs for which such exclusion would apply.

There was also new evidence, in these proceedings, about "mini-CDs" that have a capacity of only 185 Mb.[44] It was suggested, without supporting evidence, that these CDs might be used by businesses for promotional purposes.[45] The Board also heard testimony that mini-CDs are used in certain cameras.[46] Yet the Board was also told that these CDs are indeed used for copying music.[47] It was also suggested, and CPCC appears to agree, that a reduced levy rate should apply to mini-CDs. We do not know however if CDs of less than 100 Mbs ought to be included in this mini-CD category. Given the conflicting evidence the Board believes it best to maintain the status quo, but looks forward to hearing more in the next proceedings. Hence, the tariff will again apply to all blank CDs, regardless of their memory capacity.

CPCC also proposes a levy on all types of recordable or rewritable DVDs. There is some survey evidence that suggests DVDs are being put to similar uses as CDs were early in their life product cycle. However, the relevant surveys are based upon small samples, and therefore, have relatively large margins of error. Responses also demonstrate that some respondents did not understand the technologies involved. Many consumers indicated they could put audiocassettes in their DVD machines.[48] Also notable is that some questions about consumers' uses of blank DVDs failed to list video amongst the choices of responses.[49] Although select evidence shows that DVDs are sometimes promoted, in part, for music use, this evidence is not representative of the overall marketing of DVDs.

The Board is more convinced by the evidence showing that the uses for blank DVDs are different from the uses for blank CDs. In particular, the Board believes that blank DVDs are used almost exclusively for recording video, and only marginally, if at all, for recording audio.[50]

There are relatively few players, especially portable players, capable of playing music from burned DVDs. The vast majority of existing DVD recorders are found in personal computers. Given the ever-growing installed base of DVD players, it seems unlikely that consumers would upgrade their machines in the near future. DVD recording, even of video, is still in its infancy and likely will not develop fully until competition amongst formats is resolved.

In addition, the primary attraction of blank DVDs as compared to blank CDs is larger capacity, which is most desirable for copying video and backing up data. Unlike in the context of blank CDs, where the switch to digital from analogue cassettes brought substantial incentives for rapid

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[44] Apparently, these have 150 Mb of useable space.
[45] H. Knopf, transcripts at 1879-1880.
[46] R. Bourrier, transcripts at 1954-1955.
[47] P. Audley, transcripts at 1772; R. Hofley, transcripts at 3645.
[48] B. Gauthier, transcripts at 1298-1300.
[49] See Exhibit CPCC-5 at b-65.
[50] Note that a soundtrack that accompanies video does not qualify as a "sound recording" for present purposes: see *Act*, s. 2.

adoption, the Board does not expect that consumers will massively shift to use blank DVDs for music copying in the immediate future. Consequently, the Board is not persuaded, at this time, that a DVD qualifies as an audio recording medium ordinarily used by consumers to private copy music. As previously explained, this determination means that copying music onto a DVD infringes copyright.

CPCC proposes a levy on removable electronic memory or micro hard drives capable of use with MP3 players or similar devices. It also seeks a levy on memory or hard drives incorporated into devices that are intended for use primarily to record and play music. CPCC concedes that the levy would not include cellular phones, personal digital assistants, desktop, laptop and handheld computers and a host of other devices that most reasonable people would not consider intended for use primarily to record and play music.

Some types of removable memory might sometimes be used to copy music, but it is impossible to generalize. There is a plethora of often incompatible formats, including different brands of cards and micro hard disks of various shapes, sizes and capacities. There are a breadth of potential uses, ranging from digital photography to document storage to medical or military applications to music copying. Ultimately, there is a lack of straightforward evidence demonstrating which formats are capable of which uses with which devices. Especially because these media are removable, it is impossible to identify with any accuracy the uses to which they will be put. In this regard, memory cards and micro hard disks are distinguishable from CDs or audiocassettes. With CDs and audiocassettes, the slight variations in format and capacity that exist for each, do not preclude generalization in their use for copying music.

Based on the record before the Board, it cannot be said that all formats of removable memory are ordinarily used by individual consumers for copying music. Therefore, to include all types of removable memory under the rubric of an “audio recording medium” is simply not justified by the evidence in these proceedings. In addition, insufficient evidence was placed before the Board to demonstrate that any particular type of removable memory qualifies under the *Act*.

Applying the definition to embedded memory, either solid state or hard disk, represents a somewhat different challenge. Embedded memory may exist in dissimilar formats, and in a variety of devices that have different functions. Hard disks in personal computers are technically indistinguishable from those in some digital audio recorders. It appears, therefore, inappropriate to generalize about the uses of all embedded memory. However, the distinction, in the Board’s view, is that where a medium is permanently incorporated into a certain type of device, it becomes possible to categorize that medium and evaluate its use as a unique “kind” of “audio recording medium”, based on the intrinsic characteristics of the device into which the medium has been incorporated.

It is not as easy, however, to classify a medium as one “kind” or another based upon extrinsic criteria such as packaging. For this reason, removable memory “bundled” with any particular product should not be distinguished from the same removable memory sold separately.

Intrinsic physical attributes of the device, including its size, convenience and compatibility, are helpful to determine whether the device’s medium is ordinarily used by individual consumers to copy music. Thus, media of a kind embedded into certain devices may be ordinarily used by

individuals for copying music, whereas the same media embedded in other devices may not. This can be true, notwithstanding that the essential attributes of the media itself, for instance, solid state memory or hard disk, remain relatively constant.

Objectors allege that the primary deficiencies in this aspect of CPCC's proposal are a lack of clarity and precision. CPCC suggests that a levy should only be placed on memory in devices that are "intended for use primarily to record and play music". It points out that this standard is distinct from, and indeed higher than, "ordinarily used".

It is beyond the Board's jurisdiction to incorporate a second standard into the definition of an audio recording medium. Nor can it implicitly exempt memory in certain devices by adopting CPCC's suggestion within the tariff. If the Board cannot expressly create exemptions, then it cannot do so implicitly either.

The Board believes that, on the standard of ordinary use, memory in a large number of devices does not qualify as an "audio recording medium". Such products include an obvious and non-exhaustive list of devices such as heart-rate monitors, digital cameras, personal digital assistants, telephones, etc.

In contrast, non-removable solid state or hard disk memory, when incorporated into digital audio recorders, as that term is understood by the Board, is ordinarily used by individual consumers for copying music. In this respect, the Board does not view the standard of ordinary use quite so "low" as some participants have mistakenly understood. This is not simply a trivial threshold. When the Board speaks of a digital audio recorder, it speaks of a device that is designed, manufactured and advertised for the purpose of copying sound recordings of musical works. It follows that non-removable memory permanently embedded in such a device falls within the definition of an "audio recording medium" under the *Act*.

Few products have one exclusive function. Indeed, many digital audio recorders also feature games, calendars, personal organizers and other ancillary features. Since the trend is toward multi-functionality, there will be grey areas. However, at least for the period of this certified tariff, the Board believes that a relatively small proportion of products are truly at the margin between a digital audio recorder and another device.

The most significant ambiguity arises in the context of memory in personal computers. Several participants, notably Mr. Carruthers of Hydraulic Design, showed the Board that this memory is technically identical to that in some digital audio recorders. As already indicated, the evidence in these proceedings demonstrates that memory in personal computers is being used by individual consumers to copy music. For the time being, CPCC's proposal does not include memory in personal computers. As these questions involve significant public policy considerations, legislators might wish to explore and settle the issues before the Board is formally called upon to do so itself.

In sum, the Board finds that each audiocassette of more than 40 minutes in length, CD-R, CD-RW, CD-R Audio, CD-RW Audio, MiniDisc, and non-removable memory (solid state and hard disk) permanently embedded in a digital audio recorder fall within the meaning of an "audio recording medium" under the *Act*. The evidence does not establish the same in respect of blank DVDs, nor removable memory.

IV. SETTING THE LEVY RATES

In *Private Copying II*, the Board used the existing valuation model and updated it to set the rates to reflect the evidence presented during the hearing. In these proceedings, because of uncertainties raised by the evidence and other market and policy considerations, the Board cannot set the rates by solely updating the valuation model. However, for the sake of clarity and information, the Board analyses certain aspects of the valuation model to point out where it finds the evidence is either unclear, lacking or unconvincing.

A. VALUATION MODEL

CPCC's proposal is based on an updated version of the valuation model developed by Messrs. Stohn and Audley that the Board adopted in its two previous decisions. Generally, this model attempts to capture the value of each private copy of a sound recording, to estimate the average number of private copies made onto each audio recording medium, and thus calculate rights-holders' remuneration as a fixed rate per unit

Both CSMA and the Retailers suggest that the Board adopt an *ad valorem* levy rate (a proportion of the sale price), consistent with similar proposals made in previous proceedings. However, other than the fact that this approach is followed in the United States, they offer little justification for it. Moreover, they fail to suggest specifically how levy rates would be established.

The Board has previously rejected *ad valorem* levy rates primarily because the value of underlying intellectual property does not rise or fall with changes in the price of blank media.[51] Moreover, that the levy rate is linked with the value of the rights and benefits at the core of the private copying regime strengthens the nexus between the levies and the regime as a whole. An *ad valorem* rate would not have this advantage.

i. Remuneration from Prerecorded CD Sales

The model begins with the estimated remuneration received by rights-holders from the sale of a typical prerecorded CD. The Board agrees with CPCC that relying on authorized music downloads as a proxy might be more accurate but would be premature at this time. There is currently no established market for authorized downloads in Canada. Even in the United States, that market is only beginning to develop.

CPCC argues that the withdrawal of one of Canada's two record clubs from the market in 2000 would have an impact on the calculation of authors' remuneration. CPCC acknowledges that there was no evidence to show how much, if any, impact this development had on the market.

CPCC also argues that inflation has increased the price of a prerecorded CD, and consequently, the remuneration flowing to performers and makers. However, CSMA points out that under current market conditions in the industry, the price of prerecorded CDs is more likely to remain constant,

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[51] *Private Copying I* at 42.

if not decline.

For its part, CSMA proposes that the proxy should reflect royalty discounts that may apply in the case of singles. Here, the Board agrees with CPCC that the singles market has all but disappeared in Canada today.

Changes, if any, to other parameters in this section, such as per-song royalty rates or the average number of tracks on a CD for example, are negligible. Therefore, should the model be used to set the levy rates, there would be no substantial changes to make concerning the average remuneration flowing to authors, performers and makers from prerecorded CD sales.

ii. Ineligible Repertoire

Some private copies are of recordings whose authors, performers and makers are not eligible for remuneration pursuant to Part VIII. In the case of authors, most of the recordings copied are eligible. In determining performers' and makers' eligible repertoire, CSMA submits that the Board should no longer rely equally on radio airplay and record sales data. It claims Canadian content regulations distort the figures. For the reasons already outlined in earlier decisions, the Board rejects CSMA's submission. The Retailers argue that CPCC ought to have found better information about the music that is actually copied by Canadians, but did not present any evidence of their own. In the absence of any direct evidence on the eligible repertoire that is copied, the Board would retain the approach used in past decisions. Also, the Board would use the new data submitted by CPCC. Indeed, this evidence was not contested.

iii. The Ancillary Nature of Private Copying

Since its first decision, the Board has believed firmly that a fair and equitable levy rate cannot be determined without regard to the value that individual consumers place on private copies of sound recordings. Consumers are not willing to pay the same price for a private copy of music as for an original published sound recording. In some circumstances, a consumer might place only slightly less value on a private copy. In many others, a consumer would be willing to pay nothing at all; he/she would simply not make private copies.

Initially, the Board estimated that consumers on average would pay half as much for a private copy. In its second decision, the Board was persuaded that where a private copy was of a track not already owned by the copier, a lesser discount of one quarter was warranted. This resulted in a higher levy rate. Now, CPCC presents an even more detailed structure that calculates different discounts (or, more accurately, no discount) for certain types of private copies.

CPCC submits that consumers place no less value on a private copy of a track that forms part of a compilation, than on the original track that is part of the complete album. The Board is not convinced that consumers hold "compilation" tracks on par with the value of original recordings.

According to those in the industry, prerecorded CDs are still "your best entertainment buy".[52] Indeed, there was new evidence in these proceedings concerning the quality of private copies. Compressed music is, in fact, of lower fidelity than uncompressed music. More importantly, consumers believe compressed copies to be of inferior quality, which affects the price they would pay.

The Board would prefer not to add twists to this already complex exercise by breaking down the "ancillary value" discount. It is not convinced that it is fair and equitable to micro-analyse or to quibble over technicalities. The ancillary value calculation is not capable of scientific quantification. It is meant to sense the quantitative and qualitative feelings of Canadian music consumers. The more technical and nuanced the exercise becomes, the further it strays from its core purpose.[53]

iv. Paid Downloads and Free Samples

Transactions in which the right to private copy is already acquired should be excluded in the calculation of the levy rates. In principle, levies may thus be phased out as paid downloads and free samples become more prevalent. For now, however, the Board has no convincing evidence on how extensive these transactions are.

v. Specific Media

a. Audiocassettes

Not much debate arose concerning the evidence on audiocassettes. In view of the above analysis, there would be no convincing reasons to change the rate applicable to these media.

Given that the Board considers that the zero-rating program is illegal, it can no longer compensate CPCC for the effect of the program on its revenues. This should lead, in theory, to a reduction of the audiocassette levy rate.

However, the audiocassette market has reached its maturity. Consumers have apparently accepted the levy on these media as an intrinsic component of the price. Thus, the rate should stay the same.

b. CD-R and CD-RW

CPCC argues that, in the 18 months preceding the hearing, the share of recordable CDs purchased by individual consumers, as opposed to organizations, went from 45 per cent to 70.8 per cent.

Réseau Circum's study, presented by CPCC, estimated the raw number of blank CDs purchased by individuals by asking consumers about their purchasing habits, and comparing that data to Mr.

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[52] D. Basskin, transcripts at 403 and 491.

[53] For additional discussion of the factors relevant to this topic, refer to *Private Copying I* at 48-49, and *Private Copying II* at 11-14.

Audley's adjustment to Santa Clara's estimate of the size of the total market. The figures were adjusted to remove outliers, attribute an average to any nil responses, and discount for consumers' inevitable overestimation (telescoping) when asked about their past purchases. In these proceedings, Circum applied a telescoping or reduction factor, of 70 per cent for recordable CDs. In *Private Copying I*, this adjustment was 78 per cent. In *Private Copying II*, it was 28 per cent. These numbers are derived from the apparent difference between the respondents' reported purchases of prerecorded CDs and CPCC's experts' estimate of the actual number of prerecorded CDs purchased by Canadians during the same period.

CSMA challenges the manner in which the proportion of "individual consumer" purchases was derived. For one, it notes that the total market size, used as the denominator, is far from settled. Furthermore, CSMA suggests that the number of media purchased by individuals, used as the numerator, is unreliable. It argues that statistical methods, some of which were not used in previous studies, diminish the data's reliability. CSMA criticizes the adjustment for telescoping by pointing out the inconsistencies that the technique produces with data about other products.

One only has to look at Circum's estimates of the markets for CD-RWs, blank DVDs and removable memory to conclude that the results are improbable in some cases, and impossible in others. The estimates of individuals' purchases of different types of blank media appear to be consistently overestimated by at least 64 per cent to 600 per cent. For example, Circum estimated that individuals purchased nearly 22 million CD-RWs during a period when all other indications, including the Retailers' numbers, put the total market at only about 4 to 7 million units.[54]

CSMA also points out that office products and computer dealers have recently increased their share of sales volume of blank CDs. If one can say that businesses are more likely to be customers of such entities, their purchases should have increased. Accepting Circum's figure would mean that not only do organizations now account for a smaller proportion of sales, but also that the number of units sold to them actually fell.

Ultimately, CSMA argues there is no evidence to depart from the Board's previous estimate of 45 per cent. The Board agrees that the proportion of all purchases accounted for by individual consumers is not as high as Circum suggests. Yet given all the ambiguity surrounding this issue it is very difficult to identify the correct figure, which is essential ultimately in determining the levy rate.

CPCC and CSMA ask the Board to establish, for the first time, different rates for recordable CDs and rewritable CDs. Various characteristics such as re-recordability, a higher price and more limited distribution suggest that CD-RW may be less likely to be used for private copying. Survey evidence confirms that there are some differences regarding the proportions of CD-R and CD-RW used by individual consumers for purposes other than music. The distinction between the results of Circum's survey and that of Léger Marketing is one of degree.

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[54] See Exhibits CPCC-6, CPCC-7, CPCC-20 and CSMA-37.

In this hearing, there is evidence that would justify different levy rates.

CSMA proposes additional discounts for CDs given away blank, and CDs given away after recording. CDs given away blank are ultimately used in the same way as the other blank CDs, so no discount is warranted in this respect. CSMA is correct that distributing CDs containing music, even as a gift, is not private copying; this activity should be excluded in the calculation of the levy rates. There is however no evidence to allow the Board to calculate it.

The submissions of CPCC and CSMA vary only minutely with respect to spoilage discounts, recording capacity and usage adjustments.

Given the uncertainties surrounding important figures, the Board would not be able to update the valuation model to set the rates for CD-Rs and CD-RWs.

c. CD-R Audio, CD-RW Audio and MiniDiscs

There is little specific evidence regarding these media. Previously, the Board has proceeded based upon assumptions. During this hearing, the Board questioned those assumptions, but was given little information in response. Therefore, the Board would be inclined to merge the rate for CD-Rs and CD-RWs Audio with other blank CDs. However, the lack of solid evidence justifies maintaining the status quo.

d. Non-removable memory permanently embedded in Digital Audio Recorders

It is first important to recall that the Board is approving a levy not on devices but on memory in certain devices. CPCC proposes a graduated structure of 1.08¢ for each Mb of memory up to and including 1 Gb, $7.76 per Gb for the 2nd through 5th Gbs, $5.81 per Gb for the 6th through 10th Gbs, $3.88 per Gb for the 11th through 20th Gbs and $1.93 per Gb for the 21st and all subsequent Gbs.

This per Mb or Gb structure is similar to the "per minute" rate rejected by the Board in *Private Copying I*. It is also overwhelmingly complex. Furthermore, almost all of the CPCC's figures pertaining to these media are based on speculation.[55]

The Board notes that there is a large range in storage capacity with this kind of media. Much depends upon the format; hard disk memory can typically hold much more music than solid state memory. For this reason, a tiered structure is desirable.

It is safe to say that as capacity increases, consumers are less likely to use all available memory space for copying music. Also, since consumers' demand for private copies is finite, there comes a point when more capacity simply is not useful for the purpose of private copying. Therefore, a per Gb rate is inappropriate beyond a certain point.

The Board also notes objectors' concerns about so-called "Moore's law", which basically suggests

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[55] See Exhibit CPCC-7 at pp. 32-37.

that prices decline, and capacity increases, on a rapid and regular basis. Thus, although the Board declines to set an *ad valorem* rate, it must consider the likelihood that major changes in price and capacity could soon occur with respect to this kind of media.

The Board does not wish to impede the development of the emerging market for these new technologies in Canada. The Board also is conscious that consumers may be more sensitive to a levy on this kind of media than on others, since the cost of this medium constitutes a higher proportion of their total income. It does not wish to encourage levy avoidance or evasion.

The levy must also be as simple as possible. Too complex a levy would put an onerous administrative burden on manufacturers and importers who must calculate their liability.

For the above reasons, the Board cannot set the rate based on the model proposed by CPCC. Instead, it establishes the rate by combining some of the principles underlying CPCC's proposal with other observations from the record about this kind of media.

The levy rate for non-removable memory permanently embedded in a digital audio recorder is set at $2 for each recorder that can record no more than 1 Gb of data, $15 for each recorder that can record more than 1 Gb and no more than 10 Gbs of data, and $25 for each recorder that can record more than 10 Gbs of data.

B. MARKET AND POLICY CONSIDERATIONS

In general, the Board feels uneasy with the record presented, and several uncertainties remain, as explained in the analysis of the model above. In addition, other considerations reinforce the Board's sense of hesitation to modify the levy rates and confirm the need for stability. These are discussed below.

i. Grey and Black Markets

A levy is payable on every blank audio recording medium manufactured or imported in Canada for the purpose of trade. Units disposed of for the purpose of trade, but levy-free, constitute the "black market" for audio recording media. The black market is illegal. However, anyone may freely import media and use them for any purpose except trade, even for copying music. Such activities are commonly referred to as the "grey market". The grey market is not illegal, although it may have undesirable effects.

As discussed earlier in these reasons, there is uncertainty about the size of the market for blank media, and in particular recordable CDs. The Retailers' numbers cannot be reconciled with those of CPCC and CSMA. The Retailers claim to have purchased nearly twice as many blank CDs as were reportedly sold by Canadian manufacturers and importers.

CPCC submits that the Retailers' numbers are simply wrong, although no evidence has led on this point. We are dealing here with major retailers who, it must be presumed, have accurate accounting procedures. There could be a combination of explanations for the discrepancies. Perhaps there was a significant lag in inventory, or there may be different reporting systems among the Retailers (although such hypotheses were not put forward by anyone during the hearing). Possibly,

significant levy evasion is also occurring in the market.

Any grey market would be in addition to this levy evasion. It is unclear whether grey market transactions are captured in any data before the Board. CPCC's estimates are based upon Santa Clara's estimates, which in turn are based upon market share information provided to it from those in the industry. Estimates pertaining to the Canadian market, however, likely do not include direct sales from foreign suppliers to Canadian end users. Moreover, those who do not wish to pay the levy are not likely to report their purchases to either CPCC, Santa Clara or industry associations.

There are additional reasons to suspect that grey and black markets exist. For one, CPCC and CSMA jointly asked the Board to amend the 2001-2002 tariff to address enforcement issues. At that time, both parties submitted that the level of levy evasion represented a "material" change in circumstances, important enough to justify reopening the tariff. CPCC and CSMA also submitted a joint request to the government to modify the *Act* in two respects. They asked that what are now legal grey market activities be made subject to the levy, and they sought penalties for those who purchase blank media on the black market. One could infer from this that those directly concerned with the issues believe that there are serious problems. Furthermore, CD burners are increasingly available, private copying is supposedly on the rise and there are numerous new uses for blank CDs. Yet CPCC believes that blank CD sales have risen only slightly despite these developments. This seems counterintuitive.

The Board heard testimony from one of CSMA's witnesses, Mr. Bourrier, that the general impression among those in the industry is that the number of levy-evaded product sales "is in the 30 per cent or higher than 30 per cent range". However, Mr. Bourrier also added that this number is "based on our feelings of what we see in the market in the activities of customers and retailers, it's not based on data that we can see real numbers."[56] In addition, it was shown that CPCC was already taking action in respect of the few brands Mr. Bourrier could identify.

According to CPCC, one of the reasons to believe that there is little or no grey market is that the price elasticity of demand is relatively low. CPCC's expert, Mr. Ciric, based this assumption largely on the fact that blank media constitute a low proportion of household spending. Hence, the levy could not be a probable cause of any grey market transactions. The Board does not disagree that most individual consumers are not highly sensitive to price fluctuations. However, businesses and other organizations are probably more responsive. One also should not ignore price elasticity for illegitimate manufacturers, importers and distributors in the black market.

It remains to be determined, however, just how significant the non-levied markets are. The lack of concrete evidence is not surprising to the Board, since the only persons with actual knowledge of such activities, i.e. those engaging in grey or black market transactions, have every incentive to avoid the Board if possible. In the end, the Board is persuaded that there are grey and black markets for blank CDs.

The Board must still determine whether this phenomenon is relevant. Grey and black markets are

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[56] R. Bourrier, transcripts at 1944.

of concern to the Board for a number of reasons. Black market activities are undesirable for all concerned, since CPCC will be deprived of revenues and legitimate manufacturers, importers, distributors and retailers will be deprived of sales. Grey market activities are not desirable either. Those involved in the distribution of blank media are significantly impacted when businesses turn to foreign suppliers for blank media purchases. Also, individuals who use grey market media for private copying defeat the purpose of the regime.

Objectors argue that a higher rate would result in a greater incentive to smuggle and resell blank media on the black market. They also submit that a higher rate would encourage grey market activities. In short, an increased rate might further destabilize the blank media market. For the moment, the best the Board can do is to proceed with caution. Keeping the rates at their current levels should avoid these pitfalls. In the future, the Board would expect to obtain a more accurate evaluation of the size of the relevant markets and of the impact that the levy has on rights-holders, the industry and consumers.

ii. Ability to Pay and the Public Interest

The ability of the market to bear the burden of the levy is a significant consideration for the Board. The Board must ensure that the levy is fair and equitable for all, including those to whom the costs of the levy are passed. The Board considers that this is presently the case. It is convinced that higher levies would represent a financial burden too important for consumers. Keeping the rates at their current levels enables the Board to ensure that consumers' capacity to pay is maintained.

iii. International and Levy Distribution Considerations

Some participants lament the fact that part of the revenues generated by the levy will ultimately leave Canada to be distributed to foreign rights-holders. The Board heard that international treaties, if ratified, will require this country to devote a portion of the levies not only to foreign authors, but also to foreign performers and makers. Objectors also claim that Canada has the highest levies anywhere in the world.

A survey of the evidence reveals that rates in Canada are not dramatically different than in other countries, save for the United States. Regardless, if Canadian rights-holders are among the most well-remunerated globally, that is an achievement to be applauded, as long as the levies are fair and equitable for all stakeholders.

Even if a large proportion of these private copying levy revenues do leave Canada, that is not a policy decision to debate before the Board. The Board is not in a position to evaluate the economic, social or political trade-offs Canadian lawmakers might have weighed when considering this matter. The Board's role is to ensure that levies are fair and equitable for those granted rights by the *Act* (whatever their nationality), for payers of the levy and for others. It is not to ensure that Canadians, rather than foreigners, ultimately receive the revenues; that is a legislative choice.

In any event, it is far from settled that a significant amount of money does currently, or will in the future, flow out of the country. It is pointless to speculate on what Parliament may or may not do concerning its treaty obligations. The Board interprets and applies Canadian law as it is, and does not take account of any treaty that has been signed but not yet ratified. Thus, it is irrelevant to the

Board whether or not Canadian officials have suggested that Canada intends to ratify, at some point, international treaties, which themselves are open to debate regarding their proper interpretation. Recall also that the *Act* permits the Board to reconsider the tariff upon proof of a material change in circumstances.[57]

Regarding distribution of the proceeds of the tariff, the private copying regime is barely five years old; the first tariff was certified just over three years ago. Revenues are, understandably, being distributed only now. This is very timely, especially compared to other countries. The Board feels that CPCC should be congratulated. It would clearly be inappropriate to discount the rates because of CPCC's allegedly deficient distribution practices. It is also clearly wrong to suggest that payers of the levy are entitled to the interest earned on undistributed levies.

iv. Digital Rights Management (DRM) Systems and Technological Protection Measures (TPM)

TPMs and DRM systems were described earlier in these reasons. Such systems are not yet utilized on a wide basis in the context of music. However, much of the discussion surrounding these developments related to the incompatibility of such mechanisms with private copying levies.

The Board was told that levies exist because rights-holders cannot effectively control private copying activities, and that such an assumption must be reevaluated in light of technological developments. The Retailers argue that levies act as a disincentive to rights-holders to adopt what they submit are preferable mechanisms to address private copying. Thus, they submit, levies should be eliminated as technology makes it possible for rights-holders to offer legitimate downloads, regardless of the extent to which they actually do.

This particular argument is more appropriately made to legislators than to the Board. Likewise, the Board's hearings are not the appropriate forum to debate fears that TPMs and DRM systems mean the end of the public domain, fair dealing and other "user-rights" concepts.

The Board declines to alter the levy rates based upon the extent to which DRM systems and TPMs are merely available. The Board has already described above how it would account for the extent to which the right to make private copies has been paid for. The level of actual deployment of TPMs and DRM systems in the context of music has an indirect bearing on this calculation. The more widespread TPMs and DRM systems become, the more rights-holders are likely to make content available legitimately, and therefore, the more consumers can be expected to have otherwise paid for private copying rights.

C. CERTIFIED TARIFF

Considerations outlined in these reasons lead the Board to maintain the levy rates at their current levels for the years 2003 and 2004. The Board is simply not comfortable enough with the evidence presented to justify any increase in the rates. The Board believes that the rates established

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[57] *Act*, s. 66.52.

previously were, and are still, as fair and equitable as possible for all parties. It is not certain that the same could be said of higher rates.

Thus, the tariff as certified contains rates of 29¢ for each audiocassette of greater than 40 minutes, 21¢ for each CD-R and CD-RW, and 77¢ for each Audio CD-R and CD-RW and each MiniDisc. For the non-removable memory permanently embedded in a digital audio recorder, the Board adopts rates of $2 for each recorder that can record no more than 1 Gb of data, $15 for each recorder that can record more than 1 Gb and no more than 10 Gbs of data, and $25 for each recorder that can record more than 10 Gbs of data.

The Board is conscious that the rate certified for low-capacity recorders is higher than the rate proposed by CPCC. This decision is unavoidable considering the Board's wish to simplify the rate structure for those particular media as much as possible. Finally, given the small difference between the proposed and the certified rates (a matter of a few pennies or a dollar per recorder, at most), the Board is of the view that the unfairness created by overly complicating the rate structure would far outweigh any increased benefits that may result of capping the rate to the amounts proposed by CPCC.

V. TERMS AND CONDITIONS OF THE TARIFF

A. Apportionment of the Levies Amongst Collective Societies

As the Board heard no discussion on this issue, the Board apportions the levy in the same way as in the previous private copying decision. Therefore, collective societies representing eligible authors are entitled to 66 per cent, eligible performers to 18.9 per cent and eligible makers to 15.1 per cent.

B. Retroactivity

The certified tariff is effective from January 1, 2003 until December 31, 2004. It replaces the interim tariff certified on December 19, 2002. The only significant change from the interim tariff relates to non-removable memory permanently embedded in digital audio recorders.

Some objectors asked that the new tariff take effect 30 days or more after these reasons are released. Others, relying on paragraph 83(8)*(c)*, maintain that the application of the private copying tariff can only be prospective.

Paragraph 83(8)*(c)* provides that the Board is required to "certify the tariff as the approved tariff, *whereupon* that tariff becomes for the purposes of this Part the approved tariff". That being said, the interpretation put forward in these proceedings leads to absurd consequences in at least one respect. A proposed private copying tariff (as indeed any proposed tariff filed with the Board) must provide that the levies are to be effective for periods of one or more calendar years. As a result, the certified tariff must also be effective for one or more calendar years. Were a provision to prevent the retroactive application of the private copying tariff, rights-holders would lose the right to remuneration for a whole year should the Board fail to issue its decision before January 1 of that year.

The fact that the tariff is certified after it comes into force does not create any difficulties of a practical nature since the levy rates remain the same for media that are already subject to the tariff. Furthermore, CPCC has already confirmed to the Board that for the period from January 1, 2003 to the date of this decision, it does not intend to collect any increase in the levy rates that might be set by the Board on media already levied.

As for non-removable memory permanently embedded in digital recorders, CPCC also undertook not to seek to collect royalties on media that would be subject to the tariff for the first time in respect of sales made before the tariff is certified. The Board feels it can rely on that undertaking. There remains the request that the tariff not be triggered for 30 or more days in respect of these newly levied media. The Board does not think this appropriate, given the relatively small number of media that would be targeted by this provision. It leaves it up to the protagonists to come to some sort of arrangement, if such an arrangement is indeed required.

C. ADMINISTRATIVE PROVISIONS

CSMA asks the Board to allow its members to deduct the administrative costs of the levy from the amounts payable to CPCC. It also suggests the terms for payment of the levies be extended to 90 days following the applicable accounting period.

The regime envisions some transactional costs to be borne by all parties. As such, the Board feels it is inappropriate for payers to deduct their administrative costs. Given that the Board intends not to change any other aspect of the existing tariff, save for the new levy on non-removable memory permanently embedded in digital audio recorders, the Board denies CSMA's request to change the accounting and payment periods. Moreover, there is no evidence to justify that such a change is necessary.

On another matter, the Board decides to modify the wording of the interest on late payment clause to be consistent with its most recent decisions. Thus, interest is now calculated daily rather than monthly.

VI. CONCLUSION

In these proceedings, the Board was faced with a difficult challenge. It heard conflicting evidence concerning the Canadian market for blank audio recording media, and is no longer comfortable with its grasp of the true situation. It was required to interpret and apply a general legal definition to new technologies not contemplated at the time the law was enacted. It was presented an increasingly complex valuation model and that is ill-suited to deal with compressed music and high-capacity storage. It had to address a controversial zero-rating program with no legislative foundation, guidance from Parliament nor the tools to deal adequately with the underlying problems. It heard about DRM systems and TPMs, which call into question the fundamental assumptions underlying the need for private copying levies. It dealt with various other criticisms, even constitutional attacks, of the entire private copying regime. It was also presented an unsettling evidentiary record that did not justify the increases that were proposed. Consequently, the Board believes fairness and equity demand relative stability.

The fact that the levy rates have not increased does not necessarily mean that rights-holders'

remuneration will not increase. On the one hand, if in fact private copying is on the rise, more blank media will be sold, which in turn will result in greater revenues for CPCC. On the other hand, the Board recognizes that revenues could be negatively affected by the breadth of the extended zero-rating program. The Board cannot foresee what the final impact on CPCC's total revenues will be.

Claude Majeau
Secretary General

DISSENTING OPINION BY VICE-CHAIRMAN CALLARY

I. INTRODUCTION

I am generally in agreement with my colleagues' analysis of certain of the major issues in their decision. I agree with their reasoning on constitutional issues. I am also in agreement with the section dealing with the definition of what constitutes an audio recording medium and therefore fully support their conclusion that DVDs and removable memory are not ordinarily used by individual consumers for copying music, at least for the time being.

I share some of their views on the interpretation of the private copying regime contained in the section on the Legislative Framework. For instance, I agree with them that the regime was meant to be universal. However, I also think that the regime was meant to be workable. In other words, it is perfectly legitimate in my view to rely on the zero-rating program to target as much as possible those who copy music, and hence to make the private copying regime acceptable to a vast number of Canadians who cannot use the media to make private copies. Public acceptance is integral to the regime's workability.

I do not share my colleagues' views on three crucial aspects of their decision. First, I cannot agree with their conclusion that because of uncertainties raised by the evidence and other market and policy consideration, the Board cannot set the rates by updating the valuation model.

Second, I do not feel the same uneasiness with the record and the uncertainties in the data on media sales in Canada presented at the hearing, and I do not share my colleagues' misgivings about the relative importance of transactions in which payment of the levy is either avoided or evaded (the so-called grey and black market transactions).

Third, I disagree with the majority's analysis of the Board's discretion to take into account CPCC's zero-rating program in setting the levy rates.

II. CPCC'S VALUATION MODEL AND THE LEVY RATES

The application of CPCC's valuation model warrants some detailed explanation of the elements

of evidence that I used in making my calculations. Full details are found in Appendix I of these reasons.

A. AUTHORS' REMUNERATION

The first element in this calculation is the mechanical licence royalty rate, per song, per top-line CD. CPCC indicates that the 2003 mechanical licence royalty rate is 7.7¢ per song. As no other party objects on this point, I accept CPCC's position. Also, since no new evidence was provided regarding the number of songs on a typical prerecorded CD, I would continue to use the estimate of 14 tracks, at an average length of 4 minutes, 10 seconds.

As in past decisions, a discount of 25 per cent is applied to the top-line mechanical royalty rate to account for record club and budget-line record sales, which were estimated previously to account for 40 per cent of prerecorded CD sales. CPCC notes that one of Canada's two record clubs withdrew from the market in 2000, so they estimate that record club and budget-line record sales have likely declined to no more than 30 per cent during 2001-2002. CPCC acknowledges, however, that they did not have access to the necessary data to establish this percentage precisely. Consequently, a mid-point estimate of 35 per cent might be more appropriate.

CSMA proposes that two new discounts apply when estimating authors' remuneration. According to CSMA, the proxy should reflect royalty discounts that may apply in the case of singles and/or digital downloads. Hence, CSMA suggests a "singles" discount of roughly 25 per cent and a "technology" discount of 10 per cent. CPCC opposes the adoption of these discounts because the singles market has all but disappeared in Canada today, and a digital download market is yet to be established. I agree with CPCC.

Based on these determinations, the average remuneration paid to authors for a prerecorded CD is estimated to be 98¢ (line F, appendix 1).

B. PERFORMERS AND MAKERS' REMUNERATION

Performers' and makers' average remuneration is calculated as a percentage of the suggested retail list price (SRLP) of a top-line prerecorded CD, estimated to be $19.98 in 2000. CPCC suggests that an annual inflation adjustment of 2.5 per cent would increase this figure to $20.49. The CSMA points out that the assumption that the SRLP is increasing, while at the same time record sales are declining and online downloads are sharply increasing, flies in the face of logic. I agree with the CSMA, and therefore assume that the SRLP for top-line CDs remains constant at $19.98.

Based on these determinations, the average remuneration paid to performers and makers is estimated to be $1.96 (line M, appendix 1). Combined with the 98¢ paid to authors, the average remuneration paid to all rights-holders for a typical prerecorded CD is $2.94 (line N).

C. QUALIFYING REPERTOIRE ADJUSTMENT

As in the majority's decision, I would also rely equally on radio airplay and record sales data to determine the percentage of private copies that are of performers' and makers' eligible repertoire. Based on the figures updated by CPCC, eligible repertoire is estimated to account for 47 per cent

of all music privately copied. As a result, the imputed remuneration for eligible rights-holders for a typical prerecorded CD is estimated to be $1.38 (line S).

D. THE ANCILLARY NATURE OF PRIVATE COPYING

I generally agree with the majority on the need to continue to take into account this adjustment in the determination of the levy rates. I would slightly increase the adjustment to take into account some new evidence on the lower quality of MP3 files. Hence, I would put the discount at a value of 40 per cent, compared with 37.5 per cent that was used in the last decision.

Applying that discount to the imputed remuneration leads to an adjusted remuneration of 82.56¢ (line W). This is below 86.5¢, the value the Board used in the last decision, as a result of that higher discount.

E. LEVY RATE FOR AUDIOCASSETTES

I would use essentially the same figures as in the last decision. Taking into account the zero-rating program in calculating the rate for audiocassettes, I would have certified a levy rate of 28¢ (line AC), 1¢ below the previous rate.

F. LEVY RATE FOR CD-RS AND CD-RWS

The first area where I do not share my colleagues' view is the determination of the proportion of blank CDs purchased by individual consumers. The Circum study, presented by CPCC, suggested that 70.8 per cent of all recordable CDs are purchased by individual consumers. This compares with the proportion of 45 per cent used in the last decision. My colleagues arrive at the conclusion that they cannot certify any rate increase based on evidence that they perceive to be too ambiguous. The figure of 70.8 per cent put forward by CPCC certainly seems to be too high, probably partly as a result of methodological problems with the manipulation of the survey data. It is worth noting here that the manipulation and use of survey data can never be done without problems, in this decision as well as in the preceding private copying decisions. Nevertheless, considering the evidence on the current prevalence of private music copying, there is no doubt in my mind that this proportion has increased since the last Board's decision. I am prepared to accept that 60 per cent of all CD-Rs or CD-RWs are being purchased by individual consumers.

The second area where I disagree with my colleagues is with respect to the proportions of CD-Rs and CD-RWs used by individual consumers for music copying. In the previous decision, the Board accepted the estimate of 56 per cent for both formats. In these proceedings, Circum found that 66 per cent of individuals last copied music onto CD-Rs, while Léger Marketing found such proportion to be 53 per cent. For CD-RWs, the findings were 49 per cent and 31 per cent respectively. Considering this relatively consistent evidence, I would tend to use the figures of 60 per cent for CD-Rs and 40 per cent for CD-RWs and certify different rates for CD-Rs and CD-RWs.

CPCC suggests that a 12 per cent spoilage discount is no longer appropriate. It notes that consumers are becoming increasingly adept at copying music onto blank CDs, especially given technological developments and more user-friendly copying software. CSMA agrees that this

discount should fall, but suggests 8.14 per cent as opposed to CPCC's 5 per cent. I would use 7.5 per cent. No discount is needed for CD-RWs, as this media is re-recordable.

As can be seen in Appendix 1, taking all of the above factors into account, I would have certified a rate of 29¢ for CD-Rs (line AF) and 21¢ for CD-RWs (line AI). This is respectively 8¢ more and the same as the previous rates.

G. LEVY RATE FOR CD-RS AUDIO, CD-RWS AUDIO AND MINIDISCS

Based on most of the same assumptions as in the previous decision, the rate I would be ready to certify for these media is 72¢ (line AL).

H. LEVY RATE FOR NON-REMOVABLE MEMORY PERMANENTLY EMBEDDED IN DIGITAL AUDIO RECORDERS

I agree with the principles set up by the majority to determine the rate to apply to this type of media. I also agree with the rate certified by the majority.

I. TOTAL AMOUNT (QUANTUM) OF ROYALTIES GENERATED AND CAPACITY TO PAY

The levy rates I am proposing imply, of themselves, an increase in the total amount of royalties CPCC would be able to collect. Not taking account of the extended zero-rating program proposed by CPCC, these rates could generate as much as $47 million for the year 2004. However, since CPCC has publicly committed to implement the extended zero-rating program as soon as this Board's decision is issued, it is realistic to estimate that CPCC's royalties would rather be in the order of $30 to $35 million.

A rate of 29¢ on CD-Rs does not appear to be excessive in my view. First, as many business users would be able to benefit from the zero-rating program, they would not have to pay any levy. Individuals would have to pay. However, since purchases of CDs would still remain a very small proportion of any consumer's budget, the consumers' ability to pay the extra 8¢ per blank CD would not appear to be at stake.

III. LEVY AVOIDANCE AND LEVY EVASION

I do not share my colleagues' preoccupation with grey market considerations and data inconsistencies, and I do not agree with their conclusion that significant levy evasion currently exists in the market to the extent that it would justify a need for levy rate stability. Personally, I continue to view the CPCC and Santa Clara media sales data to be reliable, although I agree that more efforts could be made to further test their validity next time around. And I am of the view that even if some degree of levy evasion already exists, it is not to the extent that my colleagues suggest.

It does not seem to me that the Retailers' data alone should raise issues about the size of the black market in Canada. If a black market existed to the extent that the Retailers' data would suggest, then surely it would be common knowledge. Witnesses would have come forth to testify. The media would have been full of reports on how purchasers are saving money by buying CDs through

alternate channels. I am convinced that the grey and black market does not amount to more than 10 to 15 per cent of the overall market. In addition, many of the participants in that market would have been eligible for zero-rating had they chosen that route.

In my view, my colleagues' conclusion on the existence of a significant grey and black market is reached mostly through intuition and inferences. For one, nobody argued that the retailers' numbers meant that grey and black market was at least as important as the currently known market. The majority nevertheless takes this view in spite of concordant evidence and data by CPCC, CSMA and IRMA.

As for the amendments proposed by CPCC and CSMA for the 2001-2002 tariff, and their joint request to amend the *Act*, they are perfectly justified by the existence of grey and black markets in the magnitude of 10 to 15 per cent of the total market.

Finally, the growth in sales of CD burners, when looked at carefully, is not that much out of sync with the growth in sales of blank CDs suggested by CPCC. In addition, because many of these CD burners come built into most models of home computers and are often left unused, we cannot expect a perfect correlation between sales of CD burners and sales of CD-Rs.

IV. THE ZERO-RATING PROGRAM

In my view, the Board should proceed from the proposition that Parliament enacted a regime that is meant to be workable and fair and that achieves its underlying goals. The zero-rating program has become an intrinsic part of the regime, and as a result, a levy rate that does not account for it will be unfair to rights-holders. By setting a rate that is based on the expectation that all purchasers of blank media will pay it, and then having CPCC collect only from a percentage of those purchasers results in a devaluation of the owners' rights. In such situation, rights owners are being unfairly underpaid for the expropriation of their right.

If the zero-rating program has become an intrinsic part of the regime, it is largely as a result of the Board's own admonitions and decisions. The Board ruled that it could not set up the program; at the same time, it strongly encouraged CPCC to do so. CPCC having complied, the Board took full account of the program in setting the levy rate on audio cassettes. By doing so, the Board implicitly signalled that the regime could and should be articulated so as to become more targeted.

This scenario is in accordance with the way I have always understood the regime to be designed to work. In my view, and with respect, it is the only one that is consistent with the Board's earlier decisions dealing with the private copying regime. In *Private Copying II* (page 16 and 17), the Board said:

"The Board continues to believe that it cannot itself create exemptions but concludes for legal, practical and public policy reasons that it is permissible to take the zero-rating scheme into account by excluding audio cassettes that are sold levy-free from the calculation of the levy.

[...]

Second, a tariff that did not take the zero-rating scheme into account would not be a fair tariff. In

practice, the private copying regime's continued existence depends on the availability of some exemption scheme. Including zero-rated media in the calculation of the levy imposes on authors the cost of not collecting the levy as well as the cost of maintaining the administrative structure required to operate what is now an essential element of the system."

The majority says that they have reconsidered the Board's response to the zero-rating because it could not foresee the effects of the program in *Private Copying II*, and that the current decision is based upon a more complete record now before it. To the extent such new evidence exists, I do not find it convincing at all, and hence, will not change my view on the necessity to take the zero-rating program into account in determining the levy rates.

To be fair and equitable to everyone, to consumers who copy music for their private use, to consumers who purchase blank media for purposes other than copying music for their personal use, and to rights-holders who have had their rights expropriated by the regime, requires that the Board take into account the effect of CPCC's zero rating program on the quantum that the levy will generate.

The record tends to confirm that in Canada, the levy is being passed through to the ultimate users of blank media. Zero-rating allows those who by definition cannot private copy (i.e. organizations) relief from the levy. Accounting for zero-rated sales in the levy rate increases the burden on those who are most likely to private copy. It cannot be unfair to structure the market in such a way that those who can make private copies pay most of the price for those copies. My colleagues note that the option to make private copies has value for all consumers, including those who never exercise it. I agree. For that reason, it is not unfair to increase the rate on all media purchased by individual consumers.

I am conscious that this could leave a certain number of users who cannot private copy paying the levy at a higher rate than would otherwise be the case. This is intrinsic to the structure of the regime and cannot be avoided. The private copying regime has been called a system of "rough justice". The Board's task is not to make the regime perfectly fair, but to make it as fair as possible.

I cannot agree with my colleagues' statement that the zero-rating program is illegal and that by setting it or accounting for it in the levy rate, CPCC or the Board assume the role of the legislator by implying additional exemptions into the Act. By implementing the program, CPCC did not undermine the regime; it heeded a direct message sent by the Board, and responded to a hard reality in the marketplace. By saying that the program ought to be taken into account in setting the rates, I am not suggesting that the Board usurp a role that Parliament has either kept for itself or assigned to others (namely, Cabinet). I am merely suggesting that the Board ought to accept the unavoidable consequences of its own actions and take into account the reality of the levy's application.

I believe it is within the Board's discretion to take note of innovations introduced by the collective society representing rights-holders and which ultimately render the regime fairer and less controversial. Many objectors in these proceedings insisted to say that they considered the extended zero-rating program to be essential to them. Objectors might have indicated a preference for a program without restrictions or fees, but they nevertheless insisted on the necessity that such a program be made available. For instance, the zero-rating program was the sole purpose of the objections of the Council of Ministers of Education, Canada, the Association of Universities and

Colleges of Canada, the Association of Canadian Community Colleges, the Canadian Teachers' Federation and the Canadian School Boards Association. Also, Mr. Denis Makepeace from Cognos Inc. clearly stated that "the zero-rating is an integral part of the position that specific consumers of CD-R are relying upon with respect to their Statement of Case." Mr. Trottier said: "I think the zero-rating idea is good because it removes the levy from many significant media uses which do not involve private copying of Canadian works."

Also, some initial objectors, such as CBC, withdrew from the proceedings on the basis that they were satisfied with the assurances that CPCC would implement its extended zero-rating program. The Canadian Association of Broadcasters, who was also initially an objector, has been making available to its members the details of the extended program, as proposed by CPCC, even before the issuance of this decision. The users clearly consider that the extended program is an integral part of the market.

The very essence of being an administrative tribunal is to carry out the wishes of the legislator that not only the tariff, but also the collection programs are administered in a fair and equitable manner. I, for one, cannot look at one and close my eyes to the other. When dealing with the definition of an audio recording medium, the majority states that Parliament wanted the Board to show "sensitivity to market realities and the flexibility to adapt to a changing environment." I am suggesting that this same sensitivity and flexibility be applied to the issue of the zero-rating program.

The majority states that it is up to the courts of civil jurisdiction to determine whether or not copies made on non-qualifying media infringe copyright. Thus the Board may consider an act to be illegal under the *Act*, but that decision does not make that act *ipso facto* illegal. It would therefore follow that it is also for these same courts to determine the legality of zero-rating. I state this out of concern that the majority's decision on this issue may create a major disruption in the existing blank media marketplace and endanger the continued viability of the private copy regime as we know it. In addition, many organizations, such as the broadcasters, the educational institutions and the religious organizations, that have not appeared before the Board in these hearings and the previous hearings because they benefited from their exemption under the CPCC's zero-rating scheme, will now find themselves faced with a major unexpected potential liability.

There remains the question of when to account for any change in the program. Suffice it to say that, in my view, it may not be necessary to always wait until a change has been implemented and its impact actually assessed before accounting for it. The Board regularly issues prospective decisions based on imperfect (but reliable) information. In *Private Copying I*, the Board could not reliably estimate the eventual impact of the program. Here, by contrast, there is plenty of reliable evidence on the record that would have allowed the Board to assess the impact of an extension of the program to blank CDs.

This being said, the rates I am proposing only take the zero-rating program into account for audiocassettes. CPCC did not ask the Board to take their proposed extended zero-rating program into account in establishing the levy rates for the other media, hence I would not have done it.

Appendix I
Private Copying 2003-2004
Levy Rate Calculation

AUTHORS' REMUNERATION		
A	Mechanical licence royalty per song per top-line CD	$0.077
B	Average number of tracks per CD	14
C	Record club and budget-line sales percentage	35%
D	Record club and budget-line discount	25%
E	Adjustment for record club and budget-line sales [C × D] 0.35 × 0.25	8.75%
F	Authors' remuneration [A × B × (1 – E)] 0.077 × 14 × (1 – 0.0875)	$0.98

PERFORMERS' AND MAKERS' REMUNERATION		
G	Top-line CD suggested retail list price	$19.98
H	Royalty (in percentage)	18%
I	Applicable discounts (container, free goods allowance)	36.25%
J	Record club and budget-line discount	50%
K	Adjustment for record club and budget-line sales [C × J] 0.35 × 0.5	17.5%
L	Payments to the *American Federation of Musicians*	$0.07
M	Performers' and makers' remuneration [(G × H × (1 – I) × (1 – K)) + L] (19.98 × 0.18 × (1 – 0.3625) × (1 – 0.175)) + 0.07	$1.96
N	Total royalties per prerecorded CD [F + M] 0.98 + 1.96	$2.94

QUALIFYING REPERTOIRE ADJUSTMENT		
O	Eligible authors' weighted share of private copies [(F ÷ N) × % of private copies using eligible authors' repertoire] 0.98 ÷ 2.94 × 96%	32%
P	Eligible performers' weighted share of private copies [(M ÷ N) × % of private copies using eligible performers' repertoire ÷ 2] 1.96 ÷ 2.94 × 26% ÷ 2	8.7%
Q	Eligible makers' weighted share of private copies [(M ÷ N) × % of private copies using eligible makers' repertoire ÷ 2] 1.96 ÷ 2.94 × 19% ÷ 2	6.3%
R	Qualifying repertoire's weighted share of private copies [O + P + Q] 32 + 8.7 + 6.3	47%
S	Imputed remuneration of qualifying repertoire per CD [N × R] 2.94 × 0.47	$1.3818

ADJUSTED REMUNERATION (ANCILLARY NATURE OF ACTIVITY)		
T	Adjustment for copies made from copier-owned CDs [% of private copies × 50%] 37% × 50%	18.5%
U	Adjustment for copies made from MP3 files [% of private copies × 37.5%] 48% × 37.5%	18%
V	Adjustment for copies from all other sources [% of private copies × 50%] 15% × 25%	3.75%
W	Adjusted remuneration [S × (1 – (T + U + V))] $1.3818 × (1 – (0.185 + 0.18 + 0.0375))	$0.8256
X	Average length of prerecorded CD [B × 4'10"] 14 × 4'10"	58.33 min.

Y	Average percentage of recording time actually used on a pre-recorded CD	86%

LEVY RATE FOR AUDIO CASSETTES		
AA	Weighted average recording capacity	82.6 min.
AB	Recording capacity adjustment [((AA × Y) – X) ÷ X ÷ 2] ((82.6 × 0.86) – 58.33) ÷ 58.33 ÷ 2	10.9%
AC	Levy Rate on cassettes [W ÷ 2 × % purchased by individuals × % of purchases used to private copy × (1 + AB)] $0.8256 ÷ 2 × 0.95 × 0.65 × (1 + 0.109)	$0.28

LEVY RATE FOR CD-Rs		
AD	Average recording capacity	79.1 min.
AE	Recording capacity adjustment [((AD × Y) – X) ÷ X × 0.66] ((79.1 × 0.86) – 58.33) ÷ 58.33 × 0.66	11%
AF	Levy Rate on CD-Rs [W × % purchased by individuals × % of purchases of CD-Rs used to private copy × (1 – % waste) × (1 + AE) × (1 – % of paid downloads from Internet)] $0.8256 × 0.6 × 0.6 × (1 – 0.075) × (1 + 0.11) × (1 – 0.05)	$0.29

LEVY RATE FOR CD-RWs		
AG	Average recording capacity	79.1 min.
AH	Recording capacity adjustment [((AG × Y) – X) ÷ X × 0.66] ((79.1 × 0.86) – 58.33) ÷ 58.33 × 0.66	11%
AI	Levy Rate on CD-RW [W × % of CD-RWs purchased by individuals × % of CD-RWs of purchases used to private copy × (1 + AH) × (1 – % of paid downloads from Internet)] $0.8256 × 0.6 × 0.4 × (1 + 0.11) × (1 – 0.05)	$0.21

LEVY RATE FOR CD-Rs AUDIO, CD-RWs AUDIO AND MINIDISCS		
AJ	Average recording capacity	74 min.
AK	Recording capacity adjustment [((AJ × Y) – X) ÷ X × 0.75] ((74 × 0.86) – 58.33) ÷ 58.33 × 0.75	6.8%
AL	Levy Rate on CD-Rs and CD-RWs Audio and MiniDiscs [W × % purchased of CD-Rs Audio by individuals × % of purchases of CD-Rs Audio used to private copy × (1 – % waste) × (1 + AK) × (1 – % of paid downloads from Internet)] $0.8256 × 0.95 × 0.95 × (1 – 0.05) × (1 + 0.068) × (1 – 0.05)	$0.72