

Copyright Board
Canada



Commission du droit d'auteur
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Regime Collective Administration of Performing Rights and of Communication Rights
Copyright Act, subsection 68(3)

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**Proposed
Tariffs
Considered** 16 – Background Music Suppliers (2007-2009)

Statement of Royalties to be collected by SOCAN for the public performance or the communication to the public by telecommunication, in CANADA, of musical or dramatico-musical works

Reasons for decision

I. INTRODUCTION

[1] Background music touches practically every aspect of our daily lives, from the tunes we hear in the elevator to the jazz we listen to over dinner at a restaurant to the most sophisticated surround sensory experience. As a reflection of this, many tariffs of the Society of Composers, Authors and Music Publishers of Canada (SOCAN) target at least in part some form of background music, including the tariffs applying to cinemas, receptions, sports arenas and skating rinks.

[2] Two tariffs deal explicitly with background music. Tariff 15.A (Background Music in Establishments Not Covered by Tariff 16) allows establishments to obtain a background music licence directly from SOCAN. Tariff 16 allows suppliers of background music services to

communicate the music to their subscribers and to authorize the public performance of the music in the subscribers' premises.¹

[3] The Board has not examined in detail Tariff 16 since 1996.² At that time, the Board decided that the tariff would license both the subscriber's performance and the supplier's communication. Since then, the tariff was certified with no change in 1997 for that year, and in 2008, for the years 1998 to 2006, as a result of agreements between SOCAN and potential objectors.

[4] In March 31, 2006, March 30, 2007 and March 31, 2008, SOCAN filed with the Board, pursuant to subsection 67.1(1) of the *Copyright Act* (the "*Act*"), statements of proposed royalties for the public performance or the communication to the public by telecommunication, in Canada, of musical or dramatico-musical works in 2007, 2008 and 2009. The proposed statements dealt among other things with the use of music supplied to and performed by an establishment as background music. The proposed tariffs were published in the *Canada Gazette* on May 20, 2006, June 23, 2007 and June 14, 2008. Each time, prospective users and their representatives were advised of their right to object to the proposals.

[5] Two main groups of users filed objections to the proposed tariffs. The Canadian Broadcasting Corporation, CHUM Satellite Services Inc. (CHUM) and DMX Canada (DMX) (collectively the "Services") supply pre-programmed musical content to commercial establishments across Canada. Bell ExpressVu, the Canadian Cable Systems Alliance, Cogeco Cable Inc., Rogers Communications Inc., Shaw Cablesystems G.P., Star Choice Television Network Inc. and Vidéotron Ltd. (collectively the "BDUs") are or represent cable and satellite broadcasting distribution undertakings who provide background music to some commercial establishments, in addition to audio and video signal packages to their mostly retail subscribers.

[6] The Canadian Restaurant and Foodservices Association, Canadian Satellite Radio Inc., Emedia Networks, PCM Technologies Inc. and Sirius Canada Inc. also objected to the proposed tariffs but either withdrew their objections or did not participate in the process. The Retail Council of Canada (RCC) participated in a limited fashion. EK3 filed a letter of comments.

[7] Hearings were held in January 2008 and lasted four days. The record was closed on May 8, 2008, when the parties filed their final additional information.

[8] Currently, SOCAN licences over 60 suppliers who provide their services to some 31,000 premises, including restaurants, hotels, shopping centers, banks, retail stores, factories and

¹ Throughout these proceedings, the parties used more or less indiscriminately "location", "office", "store", "client", "subscriber" and "establishment" to refer to the unit around which the current tariff is structured: "premises". We also use the terms somewhat indiscriminately, except in the parts of these reasons dealing with minimum fees and tariff wording.

² *SOCAN – Tariffs 16 (1994-1997) and others* (20 September 1996) Copyright Board [Decision](#) [*SOCAN 16 (1996)*].

professional offices. SOCAN estimates that Tariff 16 generates approximately \$1.4 million in royalties annually.

[9] The profile and business model of the background music suppliers vary considerably. Some have thousands of clients, others only a few dozens. Some transmit music through cable, satellite or the Internet. Others deliver music on physical media, be they CDs or hard drives. Some expressly offer to purchase for the subscriber the SOCAN licence required to perform the music supplied in the subscriber's premises. Others do not. The tariff must be crafted so as to accommodate every profile and model.

II. PARTIES' POSITION

[10] Currently, Tariff 16 authorizes the performance and communication of SOCAN's repertoire in connection with the supply of a background music service, including telephone music on hold. Royalties are 4.75 per cent of subscription fees for industrial premises and 7.5 per cent for all other premises, net of any amount paid for equipment. The annual minimum fee varies. Set at \$48 per separate premise, it is lowered for suppliers who comply with the tariff, from \$48 to \$45.60 when a supplier serves 3 to 10 premises, and eventually to \$33.60 when the number of premises served is over 1,000. The minimum drops to \$20 for other premises with no more than five permanent employees if the charge for the music service does not exceed \$10 per month.

[11] SOCAN wishes to (a) abandon the industrial premises categories; (b) increase the royalty rate to 15 per cent; (c) include in the rate base not only subscription fees, but also the fees suppliers receive to include advertising in the service; (d) switch to a minimum fee per licensee, thereby abandoning the reduction in minimum fees for suppliers who comply with the tariff; (e) limit the deduction for subscriber equipment costs to amounts that are "reasonable and verifiable"; (f) add music reporting requirements; and, (g) modernize and simplify the wording and application of the tariff.

[12] According to SOCAN, the tariff as it currently stands fails to fully account for the modern use of music by suppliers and their subscribers. The proposed tariff is more consistent with its closest counterpart, Tariff 15.A, which is the most appropriate proxy for Tariff 16. On average, Tariff 15.A generates three times as much royalties per establishment than Tariff 16 (\$148 versus \$46); this discrepancy is unacceptable for SOCAN.

[13] SOCAN also maintains that the proposed increase would not have a significant financial impact on Tariff 16 licensees. Most of them appear to have flourished financially over the last decade. This success can be attributed to their more focussed and extensive use of SOCAN music on sound systems that are much more technologically advanced. Access to SOCAN's repertoire has allowed them to develop niche musical formats that cater to niche audiences. New technologies have allowed the services to do this with greater efficiency than before.

[14] The BDUs ask that the rate remain at 7.5 per cent of the amount paid to a background music supplier, less any amounts paid with respect to equipment. They do not object to the removal of the industrial premises category or to the proposed changes to the minimum fee. They ask that a preferential rate be set for small systems. They argue that a BDU that does not authorize the use of music as background music cannot be made liable for its customers' public performances. They also argue that SOCAN is fully compensated for the use of its repertoire from the value of the public performance and therefore, that the communication right should not attract any additional payment.

[15] According to the Services, there has been no change in their operations that would justify an increase in the rate. A tariff increase would have a devastating financial impact on the Services because of increased competition and market fragmentation. That impact would be even greater if SOCAN's proposed changes to the minimum fees were accepted.

[16] The Services also argue that an increase in the rate would overlook the value that they contribute to SOCAN's repertoire by screening, selecting and packaging the appropriate musical works; that programming function adds value and is the single most important factor that contributes to the success of a background music supply business. An increase would also fail to take into account the administrative benefits and almost perfect compliance that accrue to SOCAN from being able to collect royalties from a limited number of suppliers rather than from a large number of actual and potential users under Tariff 15.A.

[17] Finally, the Services argue that Tariff 15.A is not the appropriate proxy for at least two reasons. First, that tariff allows many more uses of music than Tariff 16 does. Second, it provides a commercial establishment with access to SOCAN's entire repertoire of music; in contrast, Tariff 16 only concerns that part of the repertoire that suppliers actually use.

[18] RCC's concern was limited to ensuring that if SOCAN's approach to minimum fees were accepted, it would be made clear that the minimum applies to each supplier, not to each premises. EK3 essentially opposed any change to the existing tariff.

III. EVIDENCE

A. SOCAN

[19] SOCAN relied on the evidence presented by three expert witnesses.

[20] Walid Hejazi, Associate Professor of Business Economics at the Rotman School of Management at the University of Toronto, prepared a report on the Canadian background music industry. Professor Hejazi came to four main conclusions. First, SOCAN royalties have grown more slowly than the industry. This conclusion is reached, somewhat surprisingly, by noting that over the period 2001 to 2006, royalties collected pursuant to Tariff 16 increased by 50 per cent.

In the same period, the number of licensed premises increased by 22 per cent, the number of licensed music suppliers by 45 per cent and the number of establishments attracting the minimum fee by 92 per cent.

[21] Second, Tariff 16 represents too small a share of a supplier's total costs, given the importance of the background music to the business. This, in itself, could be a reason to increase the tariff.

[22] Third, suppliers have experienced strong performance both in terms of revenue and of number of subscribers. In many cases, their income has increased significantly faster than SOCAN's revenues. The strong growth in the number of music suppliers is an indication of significant entry into the industry, which is also a sign of strong profitability. Doubling the rate would thus not significantly affect the industry.

[23] Fourth, the current structure of the tariff encourages manipulation, even though there is no evidence that this has occurred. This is mainly due to the fact that the current tariff does not encompass all of the revenues stemming from the delivery of background music; it excludes revenues from the sale or rental of equipment used to receive the service. Increasing equipment rental charges and lowering subscription fees would decrease royalties without affecting overall revenues. At a minimum, there should be a limitation on the supplier's ability to exclude income from equipment rentals and sales.

[24] Professor Richard Michon, from the Ted Rogers School of Retail Management at Ryerson University, testified about the effects of music in retail settings. His report reviewed the current scientific literature concerning the effects of music on customers in the retail and service sectors. The literature concludes that appropriately selected music favourably impacts customers' mood and perception of their environment. As a result, they are likely to stay longer in a store, to buy more and to have a positively enhanced perception of merchandise and customer service. The right background music can even foster a stronger sense of customer loyalty.

[25] Professor Abraham Hollander, from the Université de Montréal, dealt with the economic aspects of Tariff 16. More specifically, he examined two factors that could explain why the average licence fee per establishment is lower for Tariff 16 than for Tariff 15.A. First, the value of the repertoire may be less for Tariff 16 uses. On the contrary, Professor Hollander concluded that the higher added value provided by music suppliers, who are able to compile music by genre as well as to provide advice and expertise to their clients, justifies higher, not lower fees. Second, administrative efficiencies created by centralizing some royalty collection activities with the suppliers might explain the difference. Professor Hollander also discarded this factor. In his opinion, suppliers would be willing to act as collecting agents for free and to pay SOCAN royalties similar to Tariff 15.A for two reasons. First, the additional cost of collecting royalties is

low in comparison to the competitive advantage a supplier gains by doing so. Second, competition in this market is fierce.

[26] Professor Hollander also observed that background music is now more valuable than it was twenty years ago. This reflects a better understanding of the relationship between background music in retail stores and sales, allowing for better exploitation of the repertoire, and more specific audience targeting. Therefore, the Board should take this factor into account in establishing the rate. Professor Hollander also noted that suppliers who choose to communicate music by telecommunication to their clients benefit from this choice: suppliers should share some of these benefits with the rights owners. As a result, royalties should be higher when two rights, instead of one, are being used.

B. THE OBJECTORS

[27] Mr. Allan Schwebel, Vice-President, Affiliate Sales and Marketing at CHUM Satellite Services, Mr. Brad Trumble, Vice-President Canadian Operations at DMX Canada, and Mr. David Bennett, Director, Product Development at Galaxie all testified for the Services. Together, CHUM, DMX and Galaxie hold a significant portion of the background music supply market in Canada. The witnesses described the selection and assembly of musical works for delivery to commercial establishments, as well as the sales process and contractual relationship they establish with their customers.

[28] The witnesses also spoke of the increased competition with new entrants, which is largely the result of emerging technologies that have allowed smaller suppliers to enter and compete aggressively with existing ones. Competition also comes from other sources such as Internet music, satellite radio and the use of personal digital audio players. As a result, background music has been effectively commoditized, forcing Services to reduce their prices, sometimes by as much as 30 to 50 per cent for national customers.

[29] Competition has also led the Services to increase the value they bring to commercial subscribers. They service receiving equipment leased to the customer, clear rights with SOCAN, design and program the service to suit the needs of any particular commercial customer. Providing this level of customization limits the economies of scale the Services can enjoy.

[30] Ms. Sophie Lamontagne, National Director of Sales and Marketing at Bell ExpressVu, and Mr. Harry Villeneuve, National Director of Sales and Business Solutions at Cogeco testified for the BDUs. ExpressVu's background music service, called "Jukebox", uses Galaxie, the same service that is distributed to private residences. ExpressVu does not program any of the musical content on the signals, offer no guidance to commercial establishments on the use of pay audio signals as background music or install the equipment necessary to receive the programming. Cogeco distributes a Max Trax/Galaxie pay audio service to all its residential digital, bulk and commercial digital subscribers as part of its digital basic programming package which consists

primarily of television signals. Its commercial subscribers are informed that the monthly subscription fee does not include royalty payments to SOCAN or to the Neighbouring Rights Collective of Canada (NRCC) and that they must pay any performing rights royalties. To facilitate the licensing process, Cogeco provides commercial subscribers with SOCAN's contact information.

[31] The objectors asked Dr. Tasneem Chipty, Vice-President at CRA International, to evaluate the economic reasonableness of SOCAN's proposal. She did not consider Tariff 15.A to be an appropriate benchmark for Tariff 16. She identified three differences between the tariffs which she argued are significant and not accounted for in Professor Hollander's analysis. First, Tariff 16 covers only the use of music received from suppliers; Tariff 15.A covers more potential uses of recorded music. Second, in administering Tariff 16, SOCAN enjoys cost savings that are created by the music suppliers. Third, the higher average royalty paid pursuant to Tariff 15.A implicitly reflects the fact that many establishments are non-compliant and that suppliers are more efficient at collecting the tariff than SOCAN. All of these factors suggest that the average royalty paid pursuant to Tariff 16 should be lower than pursuant to Tariff 15.A.

[32] According to Dr. Chipty, the innovative technological developments that allow music suppliers to create efficiencies in administering the tariff should not lead to an increase in the tariff. Such an increase would constitute an expropriation of the returns on the technological improvements, and would be tantamount to a "hold-up" of returns on the sunk investments of the suppliers, creating perverse incentives that are contrary to public policy.

[33] Dr. Chipty maintains that Professor Hejazi failed to undertake an economic analysis that would appropriately evaluate the sustainability of the proposed rate increase or the subscribers' response to it. He also failed to assess the risk-corrected rate of return on the investment that would allow suppliers to stay in business. In her view, the issue is not whether suppliers have sufficient revenues to cover an increase in royalties, but whether, after passing on the increase to subscribers, who may leave as a result, suppliers would still earn sufficient revenues.

[34] Dr. Chipty saw no purpose in comparing growth rates in the number of Tariff 16 licensees and SOCAN licence revenues. There is no economic rationale to expect the two necessarily to grow at the same rate. A better, but still imperfect, approach would be to compare licence revenues to the number of subscribers; during the period, the former had grown faster than the latter.

[35] Dr. Chipty rejected Professor Hejazi's misgivings about the exclusion of equipment costs from the rate base. Far from "playing" the tariff, many suppliers subsidize equipment sales and rentals to stimulate sales of music services. This artificially inflates the rate base and benefits SOCAN without SOCAN bearing any of the cost.

[36] Dr. Chipty concluded that SOCAN did not provide sufficient economic rationale to justify raising the rate. Implementing SOCAN's proposal would substantially increase tariff payments, which could cripple suppliers. Some would exit the market, leading to higher costs and less compliance for SOCAN, who would have to enforce Tariff 15.A. Increasing the rate could also act as a barrier to entry, limiting competition in the industry.

IV. ANALYSIS

A. SELECTING A BENCHMARK

[37] SOCAN argues that Tariff 15.A more accurately represents the value of background music than Tariff 16, which undervalues it. An average royalty payment closer to that paid pursuant to Tariff 15.A would result in a fairer and more equitable tariff. For this argument, SOCAN essentially relies on Professor Hollander, who discarded the two possible reasons that, in his view, might account for the difference.

[38] The Board addressed similar issues in the past when it examined NRCC Tariff 3 which deals with all uses of background music, whether or not supplied by a music service. When it certified this tariff, the Board concluded, among other things, that:

Subject to our earlier comments concerning situations where two rights are involved, we agree with NRCC that the tariff should, as much as possible, result in the payment of the same amount of royalties regardless of the manner in which background music is obtained. This minimizes the (somewhat theoretical) risk of users seeking to obtain their music in one way rather than another based solely on tariff considerations.³

[39] We agree with this conclusion. It applies equally to SOCAN Tariffs 15.A and 16. Consequently, SOCAN's proposed approach might be useful. In this instance, however, the analysis is incomplete. Other factors could also explain the discrepancy in average royalty payments. The objectors pointed to a few. The argument that Tariff 15.A allows more uses of the repertoire than Tariff 16, while theoretically valid, is of marginal relevance at best. However, the second and third factors mentioned by Dr. Chipty, concerning administrative cost savings and to the increased rate of compliance achieved by using suppliers as collecting agents, are both valid and potentially significant. There may be others, such as the fact that Tariff 15.A sets a much higher minimum. Finally, we know that in the past, SOCAN has concluded agreements with some larger retailers for the use of background music targeted in Tariff 15.A.⁴ Since no rational

³ *NRCC Tariff 3 (Use and Supply of Background Music) for the Years 2003-2009* (20 October 2006) Copyright Board [Decision](#) at para. 133 [NRCC 3].

⁴ See e.g. *SOCAN – Tariff 15.A (Background Music) for the Year 2005* (2 June 2006) Copyright Board [Decision](#) at para. 9.

user would consent to pay more than the price set in the tariff, it is reasonable to infer that some retailers pay significantly less than the rates set in the tariff.

[40] All of these factors need to be considered before reaching a conclusion. The analysis should also account for the possibility that the average payment made pursuant to Tariff 15.A may be too high, rather than assuming that Tariff 16 is too low. Neither SOCAN nor the objectors proposed how to assess the impact of these or any other additional factors. We can nevertheless conclude that the potential impact of all additional factors is such as to make it impossible for us to rely on the analysis provided by SOCAN in support of Tariff 15.A as a benchmark.

[41] As is too often the case, the objectors were content on the whole to challenge SOCAN's approach and did not propose an alternative approach for establishing a fair rate. Under these circumstances, the existing rate of 7.5 per cent is the most reliable starting point.

B. ADJUSTING THE BENCHMARK

[42] Two adjustments could be made to the starting point. The first accounts for the fact that suppliers have become much more efficient at delivering their services. The second concerns the multiple uses of the SOCAN repertoire that are sometimes involved in delivering background music. Each adjustment is examined in turn.

i. Increased efficiency

[43] We agree with SOCAN that background music suppliers have become much more efficient at delivering their services. Sound quality has improved. Music programming is more adapted to the specific tastes of target client groups. In short, the entire music experience is vastly improved and therefore more valuable to subscribers. It is true these improvements are mainly the result of efforts by the music suppliers. They have nevertheless led to an increase in the fundamental value of music and in our opinion, as we have found in the past, part of this higher value should flow to rights owners in the form of higher royalties.

[44] Assessing how much more SOCAN should get to account for the more efficient delivery of background music services requires that we examine a number of factors. The record of these proceedings provides little guidance on how to evaluate any of them. Consequently, we are unable to bring any correction to the existing rate on this account.

[45] Royalty increases that account for new efficiencies can be significant. Recently, the Board certified an increase of 19 per cent to account for both a historical undervaluation of music and a greater efficiency in its use by commercial radio stations.⁵ While that decision did not segregate

⁵ *SOCAN-NRCC Tariff 1.A (Commercial Radio) for the Years 2003 to 2007 [Re-determination]* (22 February 2008)

each factor, the decision it replaced attributed approximately half of the same increase to efficiency changes.⁶ Had the record contained enough evidence to allow us to perform the correction in this instance, we would also have considered whether the industry's financial health is sufficiently solid to allow it to absorb the increase.

ii. Accounting for multiple uses of the repertoire

[46] When a background music service is delivered by transmitting a signal, two different uses of SOCAN's repertoire are made. Transmitting the signal triggers a communication of the music, while playing it in the subscriber's establishment triggers a performance of the same music.

[47] In *SOCAN 16 (1996)*, the Board set a single rate for both uses. The principal use was the performance; the purpose of the transaction was for background music to be heard in a store. The communication was an incidental adjunct to the performance. The Board decided that this incidental right would have no additional value:

Put another way, the copyright owner is fully compensated for the use of the music by the payment of the royalty that is set for the purposes of the principal use (the performance in the store) irrespective of whether or not a prior, incidental use (the communication to the store) is involved in the process. Any value to the composers is already accounted for by setting the price based on the purchaser's use.⁷

[48] The Board discarded this approach in 2006 in *NRCC 3*. The analysis that led the Board to reverse its position can be found in paragraphs 98 to 117 of that decision and need not be repeated here. We agree with it. The next step is to apply the new approach in this case.

[49] Suppliers provide their service in ways that do not all involve the same uses of the repertoire. Delivery is done mainly by cable or satellite. However, where reception via cable or satellite is not possible or when the installation of a satellite dish is problematic, a supplier can deliver a CD or a hard-drive-based system to its clients. This form of delivery is becoming more common. Suppliers should not pay for transmissions if they do not transmit.

[50] Also, not all services purport to authorize their subscribers' performances. A supplier should not (and probably cannot) be charged for an authorization it does not provide. Consequently, if a supplier that warns its commercial clients not to play the transmitted music without paying royalties to SOCAN does not authorize the public performance of SOCAN's repertoire,⁸ the

Copyright Board [Decision](#).

⁶ *SOCAN-NRCC Tariff 1.A (Commercial Radio) for the Years 2003 to 2007* (14 October 2005) Copyright Board [Decision](#).

⁷ *SOCAN 16 (1996)*, *supra* note 2 at 27.

⁸ The issue may not be as clear cut as the BDUs wish it to be. A background music supplier is entitled to presume

supplier may be liable for transmitting the music but not for music being played. The tariff must take this into account.

[51] The solution is to set two rates: the first for transmitting a signal, the second for authorizing clients to play in public music provided by the service. Those who do both will pay both rates. Those who do one but not the other will pay only one. Those who do neither will pay nothing. The determination of who does what will be left to SOCAN, to the suppliers and, ultimately, to the courts.⁹

[52] The rate for the performance will be the current rate of 7.5 per cent. The rate for the transmission must now be set.

[53] At the outset, the parties did not inform us of how they would account for both uses. We asked them to provide evidence on the relative value of the transmission that is sometimes involved in delivering a background music service.

[54] The objectors argued that the tariff should not allocate separate values for the performance and the transmission. The BDUs added that since both rights are licensed by SOCAN and used by the suppliers, the allocation would serve no purpose. The Services added that, in any event, the communication was only accessory and of little value relative to the public performance.

[55] SOCAN first submitted that its proposed rate is intended to capture the value of all three rights that can be involved in this tariff: communication, performance and authorization of a performance. SOCAN argued that it was not necessary to make an allocation of the value to these individual rights, since neither it nor the objectors were asking for such allocation and no meaningful evidence was available to effect such allocation. Were the Board to make the allocation, SOCAN suggested a ratio of between 0.5 to 0.33, by reference to earlier instances where the Board, either expressly or impliedly, set ratios between connected uses. SOCAN added that in its view, the best comparison probably would be with commercial radio.

[56] For the reasons already stated, certifying separate rates for both uses potentially involved in this tariff is necessary. We say both uses, even though SOCAN correctly speaks of three rights. Accounting separately for the authorization of the subscriber's performance would be both

that its signals will be used in accordance with the law. On the other hand, a BDU that supplies signals for a purpose that necessarily triggers a subsequent use of SOCAN's repertoire could, on that basis alone, be authorizing that use irrespective of any legal arrangement with its clients. Finally, since section 2.3 of the *Act* provides that a person who communicates a work is not *by that act alone* deemed to authorize its performance, that same person can both communicate the work and authorize its performance if more than the simple act of communication is involved [emphasis added].

⁹ Users often complain about copyright fragmentation. Clearly, in this instance, fragmentation is dictated by market decisions, to the benefit of users who thus are not required to pay for uses they do not make.

unnecessary and incorrect, given the special nature of the relationship between the right to authorize and the right to perform. A performance may involve two *rights* but only one *use*. With this in mind, the solution that SOCAN proposes is the most appropriate.

[57] In *CSI – Commercial Radio Stations for the years 2001 to 2004*, the Board set royalties for the copies of musical works that stations make on their servers and elsewhere. Clearly, the Board considered that copying musical works was not as central to a station’s activities as transmitting it; implicitly, a ratio was set between the (existing) rate paid to transmit music and the (new) rate paid to copy it.¹⁰

[58] In *SOCAN – Tariff 24 (Ringtones) for the years 2003 to 2005*, the Board did the opposite. Market transactions had already determined what ringtone suppliers pay to copy musical works. The Board was asked to set the price for transmitting the ringtone. The Board concluded that in this market, the copy was worth more than the transmission, and expressly set the (new) SOCAN tariff at half the average (existing) price of a copy.¹¹

[59] Finally, in *CSI – Online Music Services*¹² and *SOCAN 22.A*,¹³ the Board set the price to be paid for both the copies and transmissions made when online music services supply permanent downloads, limited downloads and on-demand streams. Again, the Board took into account the relative importance of each use in each type of service.

[60] The table that follows summarizes the ratios set in, or derived from, these decisions.

	Main use/Utilisation principale	Ancillary use/Utilisation accessoire	Ratio of ancillary to main use/Rapport entre utilisation principale et accessoire
Commercial radio/Radio commerciale	Communication 3.2%	Reproduction 1.0%	0.3
Permanent downloads/Téléchargements permanents	Reproduction 8.8%	Communication 3.4%	0.4
Limited downloads/Téléchargements limités	Communication 6.3%	Reproduction 5.9%	0.9

¹⁰ *CMRRA/SODRAC Inc. (Commercial Radio Stations) for the Years 2001 to 2004* (28 March 2003) Copyright Board [Decision](#) at 13-14.

¹¹ *SOCAN – Tariff 24 (Ringtones) for the Years 2003 to 2005* (18 August 2006) Copyright Board [Decision](#) at paras. 93-104.

¹² *CMRRA/SODRAC Inc. (Online Music Services) for the Years 2005 to 2007* (16 March 2007) Copyright Board [Decision](#) at paras. 77-78, 98, 103.

¹³ *SOCAN – Tariff 22.A (Internet – Online Music Services) for the Years 1996 to 2006* (18 October 2007) Copyright Board [Decision](#) at paras. 162-65, 169-70, 174.

Audio streaming/Transmissions de contenu audio	Communication 7.6%	Reproduction 4.6%	0.6
Ringtones/Sonneries	Reproduction 12%	Communication 6%	0.5

[61] All these decisions compared uses of SOCAN's repertoire to uses of the joint repertoire of CMRRA and SODRAC. Here, we are concerned with two uses of the same repertoire. This is a distinction without a difference. In all instances, uses were compared. The fact that the repertoires were administered separately was not taken into account: if, as is the case in some other countries, a single collective society administered both the performing/communication and reproduction rights, no one would suggest that someone who only copies should also pay to transmit, or vice versa.

[62] In this instance, the ratio should be lower than 0.4. Earlier ratios of 0.4 or more all involve situations where the lower priced use still is essential to the user's business model. Delivering downloads without transmitting is unthinkable; so is ringtone delivery without transmitting. Delivering background music without transmitting is possible; this part of the market is even growing according to the evidence.

[63] A ratio of 0.3 is more appropriate. The situation at hand is indeed much closer to that of commercial radio. For many years, radio stations transmitted music by playing records or CDs. In 2003, most stations could function without server copies but chose not to for reasons of efficiency. Similarly, transmitting is economically essential in part of the background music supply market, while in another, growing part of the market, transmitting simply does not occur.

[64] Consequently, transmitting a background music service to a subscriber will attract royalties of 2.25 per cent, while authorizing clients to play in public music provided by the supplier will attract royalties of 7.5 per cent.

[65] The BDUs went so far as to argue that those who transmit pay audio signals to commercial clients should get to use SOCAN's repertoire for free unless they authorize their clients' performances. In a nutshell, the argument goes as follows. Those who do not authorize a performance are not liable for that performance. SOCAN did not allocate its proposed royalties between communication and performance; the same rate would apply whether or not there is a communication. Since SOCAN cannot collect royalties for communications that do not occur, it must be proposing to collect royalties only with respect to the performance, whether or not a communication is also involved. Consequently, the tariff should apply only to suppliers that authorize the performance.

[66] This line of reasoning misses two points. First, SOCAN did propose a range of ratios for the two uses involved in the tariff, if only somewhat reluctantly, at our invitation. Second, and in any event, a supplier that transmits music needs a SOCAN licence even if it does not authorize its clients to play that music. The proposed tariffs clearly targeted the supplier's transmission as

well as the client's playing of the music contained in the signal. A failure from SOCAN to propose how to allocate royalties between two uses does not prevent us from setting separate rates for these uses, as long as SOCAN did target both uses.

C. MINIMUM FEES

[67] SOCAN proposed that the minimum fee be modified from \$48 per premises to \$500 per background music supplier. In effect, this would eliminate any minimum fee. In 2006, each licensed background music supplier had on average 510 subscribers. Using the current minimum rate, the average-sized supplier would be paying \$17,136 per year ($\33.60×510), a much higher number than the \$500 minimum proposed by SOCAN. Put another way, based on the current minimums, a supplier would pay the proposed minimum if it has only 12 subscribers.¹⁴ Indeed, SOCAN admitted the minimum would apply to only one of the 61 currently licensed suppliers.

[68] A minimum fee per supplier would have to be much more than \$500. Because the number of subscribers per supplier varies so much, such a minimum fee may be higher than the revenues of some smaller suppliers. To be fair, a royalty per supplier has to be established at a relatively low level, which makes it then payable by only a few suppliers.

[69] Alternatively, we could simply eliminate the minimum. This however would go against the Board's finding in several other cases with which we agree, where the importance of minimum tariffs is re-emphasized to ensure that SOCAN receives at least a floor price for its repertoire.

[70] A third possibility would be to set a minimum at a fixed amount, multiplied by a supplier's number of premises. A supplier for which the average payments are lower than the threshold would pay the minimum royalty rate per premises for all of its premises. This however would unnecessarily favour either SOCAN or the suppliers, depending on the threshold level we set for triggering payment of the minimum fee.

[71] We will therefore continue to apply a minimum tariff to each premises. To do so, we rely on what the Board has done in some of its recent decisions where it used a formula based on 2/3 of the actual average amount generated by the tariff per user to set the minimum rate. Information provided by the parties in answer to questions from the Board allows us to estimate at \$400 the average subscription revenue per premises per year. This results in minimums of \$20 per year for playing music and of \$6 for transmitting it.

[72] Since the minimum rates we set are less than the lowest discounted minimum that currently applies to the largest suppliers, we see no need to provide for a range of minimum rates based on the number of premises.

¹⁴ The minimum currently applicable for that number of subscribers is \$43.20.

D. SHARING THE EFFICIENCIES CREATED BY THE CURRENT ARRANGEMENTS

[73] In business terms, there is no doubt in our mind that the objectors are valuable SOCAN clients and that this relationship has a value. There are significant administrative and compliance efficiencies provided to SOCAN pursuant to Tariff 16 because SOCAN is able to collect its royalties from a limited number of licensees, rather than from a large group of disparate compliant and non-compliant users under Tariff 15.A.

[74] Neither do we doubt that the objectors benefit from the arrangement. Being able to offer a product to their subscribers that is legally licensed provides background music suppliers with an important competitive advantage. This explains why, from the start, suppliers asked for their own tariff, arguing it would help them sell their product.

[75] This business arrangement generates substantial benefits for both parties. There is no evidence on the record on the issue of quantification of these benefits. We suspect that providing such evidence might prove difficult. We also suspect that these benefits tend to mutually offset.

E. INDUSTRIAL PREMISES CATEGORY

[76] A lower rate applies to industrial premises. SOCAN seeks for the removal of this category. The objectors agree. Currently, this rate is applied to no one. We see no reason to maintain it. As SOCAN argued, we see no reason for the value of the music to be lower in this case than what it would be for all other users.

F. THE RATE BASE

[77] Some suppliers charge clients separately for including in-house advertising in the service. SOCAN asks that these revenues be included in the rate base. The objectors oppose it. Witnesses for the Services testified that these revenues are in general small, and are meant to recover what it costs to create the spots and embody them in the service. They also testified that in many instances these charges were already included in the subscription price.

[78] These revenues should be part of the rate base. They already attract royalties when a subscriber is not charged separately for the service. For now, excluding them from the rate base would imply an unjustifiable asymmetrical treatment of revenues according to whether they are explicitly charged to the subscribers or not. If these advertising revenues become more important, parties might need to propose ways to evaluate them.

[79] Both sides agree that a certain amount should continue to be excluded from the rate base to account for a subscriber's equipment costs. SOCAN wants to ensure that these amounts be "reasonable and verifiable". Imposing such a limit would be justified if there were indications that suppliers overcharge for equipment. On the contrary, suppliers tend to subsidize equipment

sales and rentals to stimulate sales of music services. As Dr. Chipty pointed out, this actually favours SOCAN. Consequently, we will not impose the proposed limit.

G. A PREFERENTIAL RATE FOR SMALL CABLE TRANSMISSION SYSTEMS

[80] Some BDUs are small cable transmission systems and as such, are entitled to a preferential rate pursuant to paragraph 68.1(4) of the *Act*. The BDUs propose a discount of 50 per cent. SOCAN agrees. So do we.

V. TOTAL ROYALTIES AND ABILITY TO PAY

[81] Though the rate set in the last certified tariff is 7.5 per cent, the effective rate is somewhat higher. The large application of minimum prices explains this. Indeed, some suppliers currently pay effective rates ranging from 10 to 15 per cent. With the adjustment in the minimum rates, we expect that some of the smaller suppliers will see their royalties decrease and that the effective rate will be much closer to the rate set in the tariff.

[82] The addition of the transmission rate will increase royalties, but only when a transmission is involved. Where both rates apply, the increase in royalties paid by a supplier will be no more than 30 per cent. SOCAN estimates that the current tariff generates \$1.4 million in royalties. Thirty per cent of that is \$420,000. In our opinion the industry has the ability to pay this amount.

VI. TARIFF WORDING

[83] The following comments may help the reader to better understand the tariff. As our decision requires important changes in the wording of the previous tariff, we consulted the parties prior to finalizing it.

A. HARMONIZING SOCAN 16 AND NRCC 3 TARIFFS

[84] To the extent possible, the administrative provisions of this tariff are harmonized with those in NRCC Tariff 3, in order to lighten the suppliers' reporting burden. Two important differences exist. First, for the reasons set out in paragraph 78, the rate base is different. Second, for the reasons set out in paragraphs 87 to 94, music reporting requirements are imposed even though none exist with respect to NRCC.

B. ESTABLISHING SEPARATE RATES FOR THE COMMUNICATION AND THE PERFORMANCE AUTHORIZATION

[85] The tariff sets one rate for transmitting a signal and another for authorizing clients to play music in public. The wording we use is similar to what is found in other tariffs involving

cumulative payments, including the recent *Satellite Radio Services Tariff*.¹⁵ SOCAN asked that the tariff state even more clearly that those who do both must pay both rates. We do not see the need to do so.

C. LIABILITY FOR AUTHORIZING A SUBSCRIBER'S PERFORMANCE

[86] When a supplier authorizes public performances in a subscriber's premises, SOCAN is entitled to collect royalties from either the supplier or the subscriber; however, as soon as one has paid the royalties, the other is no longer liable. The BDUs argued that the tariff should assume that the subscriber is liable for the performance unless the supplier pays the royalties on the subscriber's behalf. Yet, whether a supplier authorizes a subscriber's performance is not a function of whether the supplier chooses to pay SOCAN for the subscriber's public performance. In the end, we opted to make the tariff target neutral; it will be up to the parties (and ultimately the courts) to determine when the supplier's liability is engaged. The tariff only specifies that the supplier who authorizes a subscriber's performance is not required to pay royalties if the subscriber complies with SOCAN Tariff 15.

D. MUSIC USE INFORMATION

[87] SOCAN asked that suppliers of background music services now be required to provide music use information upon request. SOCAN asked for the date and time of transmission, the title of the musical work, the name of the author and the composer, the name of the performer or of the performing group, the running time, in minutes and seconds, and the record label. It wished to obtain that information in respect of at least 104 days per year.

[88] The objectors agreed with the principle but wished that their burden be as light as possible. Among other things, they asked that any such requirement be limited to 7 days per quarter, upon request. They questioned the value of supplying such detailed information and whether SOCAN would use it to distribute royalties. They saw no purpose in providing the date and time when a work is supplied.

[89] Some of the principles upon which the Board relies to determine whether users should be required to supply information to assist in royalty distribution are now well-known. Users must supply essential information even if it means getting it from someone else. When reporting obligations are imposed for the first time, information has to be supplied only if available to the user or to a third party from whom the user is entitled to get the information. Later on, users will be expected to adjust their data collecting practices and require their partners to do the same.

¹⁵ *Satellite Radio Services Tariff* (SOCAN: 2005-2009; NRCC: 2007-2010; CSI: 2006-2009), *Canada Gazette*, Part I, April 11, 2009.

[90] Two further principles are relevant in this instance. First, reporting obligations should be commensurate with the amounts at play. Second, users should be asked to report their music use only if the collective society actually puts the information to a legitimate use. In this instance, the amounts involved are relatively modest. Furthermore, we do not know to what use SOCAN will put the information. Under the circumstances, we are willing to require suppliers to provide information that is, on its face, relevant for the purposes of royalty distribution. That being said, SOCAN will be expected to demonstrate the use to which that information is put before the reporting requirements are maintained, extended or made compulsory.

[91] Since only available information will have to be provided, we standardized the reporting requirements with other tariffs by adding the title of the album and the UPC and ISRC. As in other tariffs, suppliers are required to provide music use information for 7 consecutive days every month. As we recently did for satellite radio, rather than leaving the choice of days to one of the parties, the tariff provides that the information is supplied for the last 7 days of each month.

[92] The tariff requires suppliers to report their music use only with respect to music they transmit, not music they supply on a medium. That part of the market, though growing, remains small. The amounts involved are modest. Furthermore, it would seem difficult to determine precisely what is played in the subscriber's premises. Under the circumstances, we conclude that information concerning transmitted music will be sufficient for now.

[93] SOCAN asked that a common reporting format be imposed on the suppliers. Given the little we know about how suppliers gather and retain information, this is not possible. Neither is it advisable to leave it to SOCAN to determine that format. Instead, this tariff, as many others, provides that music use information must be filed in electronic format, in plain text or in any other format on which a supplier and SOCAN may agree.

[94] Small cable transmission systems are dispensed to report on their use of music. So are suppliers that only provide pay audio services whose music use is already reported pursuant to the *SOCAN-NRCC Pay Audio Services Tariff*.

E. SUBSCRIBERS' LIST

[95] Most suppliers already provide their list of subscribers to SOCAN as a matter of course. This makes sense: neither SOCAN nor a supplier wishes to annoy clients who are already authorized to play background music on their premises. Now that the tariff is split between the two uses it targets, it becomes necessary to specify that only suppliers who authorize a client to play the music they supply are required to supply a list.

[96] SOCAN asked that each list come with an indication of subscribers' additions and deletions. We do not see the need to impose such a requirement at this time. The obligation to provide the list in electronic format should make it easier to track changes in subscription over time.

F. AUDITS

[97] The audit clause is identical to that which is found in most SOCAN tariffs. The Services asked that the audit right be confined to records relating to the period proposed in the tariff, but failed to explain the purpose served by such a limitation.

G. TRANSITIONAL PROVISIONS

[98] Initially, the BDUs asked for 90 days to pay royalties and provide information relating to the period before the publication of the certified tariff. SOCAN agreed. Later on, the Services asked for 120 days. The BDUs supported that request. We conclude that 90 days should be ample time for the suppliers to adjust.

[99] The Services argued that since they pay royalties on behalf of their subscribers, they should not be required to pay an increase in royalties if, having made reasonable efforts to apply the tariff, they are unable to collect royalties from their subscribers. Insofar as the Services act for the benefit of their subscribers, they do so only with the subscribers' performance of the music they receive. In this respect, the rate remains the same. The communication is clearly a use on the suppliers' part; they should be fully liable for it.

[100] The additional retroactive payments will not be subject to interest. We conclude that the strong competition confronting the background music industry justifies this decision.

A handwritten signature in black ink that reads "Claude Majeau". The signature is written in a cursive, flowing style.

Claude Majeau
Secretary General