

# Entertainment Law

## RECENT DEVELOPMENTS OF IMPORTANCE

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### Terms of Trade Agreement: Dawn of a New Era between Canadian Producers and Broadcasters

In April of 2011, after considerable cajoling by the Canadian Radio-television and Telecommunications Commission (the “CRTC”), the Canadian Media Production Association (the “CMPA”) successfully concluded negotiations and entered into a Terms of Trade Agreement (the “Agreement”) with five of Canada’s largest private television broadcasters, namely, Astral Television Networks, Bell Media Inc. (CTV), Rogers Broadcasting-Limited, Shaw Media Inc. (Global) and Corus Entertainment Inc. (the “Broadcasters”). The Agreement came into force as of June 1, 2011, with the exception of certain parts related to the financing of television programs which came into force on August 1, 2011. Technically, there are really two Agreements, as there is one Agreement between the CMPA and the Broadcasters other than Corus and a separate Terms of Trade Agreement between the CMPA and Corus. However, the Corus Agreement contains no substantive differences from the Agreement. A Terms of Trade Agreement is also contemplated with the CBC and negotiations between the CMPA and the CBC will likely begin later in 2011.

### Agreement is Historic Deal

The CMPA is a non-profit national industry trade organization which represents Canada’s media companies that are engaged in the production and distribution of English language TV programs, feature films and interactive media content. The Agreement is a historic deal that redefines the relationship between Canadian producers (including both CMPA members and the entire Canadian independent media production sector) and the Broadcasters. It applies to all independently produced Canadian

television productions developed for and commissioned by the Broadcasters.

According to a recent CMPA update:

The deal applies to the entire life cycle of a show — from first pitch, through to development, production and broadcast on all platforms. Key areas covered by the deal include:

- Development and evaluation
- Licensing conditions
- Editorial control
- License term
- Rights
- Equity
- Super-license fees
- Producer tax credits
- Time frame and administration

The CMPA’s President and CEO, Norm Bolen, described the importance of the Agreement as follows (Playback Daily, July 8, 2011):

“This deal changes everything. It forever redefines the relationship between producers and broadcasters. But it isn’t worth the paper it is written on unless all independent producers show solidarity and strictly follow the terms of the agreement in their individual negotiations with broadcasters.”

To ensure that Canadian producers fully understand and comply with the Agreement, the CMPA organized a national “road show” in July and August of 2011 to discuss and explain the Agreement and CMPA senior staff met with Canadian producers across the country.

### What are “Terms of Trade”?

For years many independent Canadian producers have faced an imbalance in their bargaining power *vis-a-vis* Canadian broadcasters. Most are privately owned corporations with limited capital. On the other hand, Canadian broadcasters are almost all large publicly traded

organizations with considerable economic clout. This inequity in bargaining power has been further exacerbated by the recent consolidation of broadcasters in the Canadian English language market (*e.g.*, the recent acquisitions of CTV by Bell Media, Global by Shaw Media and City-TV by Rogers) which has created an oligopoly of giant Canadian media conglomerates, often horizontally or vertically integrated, which effectively control much of the country’s broadcast content.

The business model of Canadian independent producers is predicated on the optimal commercial exploitation of their programs across multiple formats and media. If Canadian broadcasters were able to use their tremendous bargaining power to acquire rights to independent productions on inequitable terms the viability of many Canadian independent production companies could be threatened.

The idea behind the Agreement is to restore a measure of balance in the negotiating power between the Broadcasters and the Canadian producers. In effect, the CMPA is acting much like a guild or union in setting minimum “scale” provisions for Canadian producers.

Given this rationale, it is not surprising that the focal points of the Agreement include a maximum license term, a prohibition on producers deferring their fees and overhead, the retention by producers of a share of film tax credit monies and an efficient mechanism for producers to license the Broadcasters programming distribution rights in multiple formats on terms that are fair to both producers and the Broadcasters.

### The Role of the CRTC

The CRTC has consistently exhorted Canadian broadcasters to conclude Terms of Trade Agreements with the CMPA. As time passed without any such agreements being reached, the CRTC toughened its stance and advised Canadian broadcasters that it would not renew their respective broadcast licenses unless Terms of Trade Agreements were first concluded. See, for

example, the following statement by the CRTC (Broadcasting Regulatory Policy CRTC 2009-406, Policy Determination Resulting from the April 27, 2009 Public Hearing, July 6, 2009, at Paragraph 84):

“The Commission recognizes the importance of [terms of trade] agreements in this era of consolidation and of the new platforms upon which content can be accessed. [It will] only consider [license] renewal applications from the [private corporate broadcast groups] for seven years with finalized Terms of Trade Agreements in place.”

The CRTC was therefore instrumental in creating a conducive environment for the Broadcasters to enter into the Agreement.

### Parties Subject to the Terms of Trade

The Agreement applies to “all independent productions produced by English-language Canadian independent television producers” for the Broadcasters. For a producer to rely on the Agreement, it must satisfy five indicators of “control” enumerated in Section 4.10 of *CAVCO’s Canadian Film or Video Production Tax Credit Guidelines (March 31, 2010)*, namely: (i) control of development, (ii) control of all creative and financial elements, (iii) control over all aspects of production financing, (iv) control over negotiation of initial exploitation agreements, and (v) reasonable and demonstrable monetary participation in terms of budgeted fees and overhead, and participation in revenues of exploitation.

There are certain situations where the Agreement does not apply. For example, the Agreement does not apply to programs produced in-house by a Broadcaster or by its affiliate or to Broadcaster “service productions”, including productions where development is substantially undertaken by a Broadcaster or where the format rights are exclusively acquired by a Broadcaster and assigned to a producer or to digital

productions that are unrelated to a television program.

### Development and Evaluation

The Agreement provides guidance for the evaluation and development of programs.

The Broadcasters must make reasonable efforts to communicate with producers across Canada about the types of projects in which they are interested. They must identify on their websites their programming services and their personnel in charge of responding to program proposals with their applicable contact information.

The confidentiality of producers’ program proposals is safeguarded by the Agreement and a Broadcaster cannot request a waiver of any existing rights that a producer may have in its program proposal.

The rights to a program proposal are owned solely by the producer, unless there is a signed development agreement to the contrary. A Broadcaster may not require a producer to commence development before a development agreement is executed. However, once a development agreement is signed, a Broadcaster’s financial participation entitles it to certain exclusive rights, including the right to negotiate a license agreement. The development agreement may not incorporate the terms of a license agreement. These terms are only to be negotiated once the project has been fully developed or the Broadcaster has made an order.

Where a Broadcaster expresses an interest, the Broadcaster and the producer must use best efforts to execute a development agreement within 60 days. The Broadcaster has no more than 18 days following the receipt of development materials to inform the producer of whether it approves the submitted development materials. If the Broadcaster turns down the proposal, the Broadcaster is only entitled to reimbursement from the producer of its cash investment in the development of the project. If the project is ultimately greenlit by another Broadcaster, this reimbursement

is to be paid on the first day of principal photography or key animation.

Once the final deliverables have been received, the Broadcaster has six months to decide whether it wishes to license the project. At the end of this six month period, the Agreement requires the Broadcaster to either (i) order the project, (ii) agree with the producer to continue to further develop the project, or (iii) release its interest in the project in writing.

### License Conditions

When a project is greenlit by a Broadcaster, it may then engage in negotiations with the producer to license the project.

The Agreement provides the producer with a 90-day period, once the Broadcaster agrees to order the project, to confirm all other sources of financing for the production, subject to any mutually agreed extension for funding deadlines and “exigencies of production”.

The Broadcaster must sign a broadcast license agreement at least two weeks prior to the commencement of principal photography or key animation, provided that the producer has submitted “reasonable agreed-upon deliverables”.<sup>1</sup> The Broadcaster must then broadcast the program on a CRTC-licensed platform within 12 months of the commencement of the license term. If a Broadcaster wishes to order additional episodes of a program for a new season, the order must be made within six months of the first broadcast of the last commissioned episode of the preceding season.

A Broadcaster’s right of first negotiation (“ROFN”) and right of last refusal (“ROLR”) in both development and license agreements is limited by the terms of the Agreement. A ROFN provides the Broadcaster with the first right to negotiate to develop or license a program before the producer can enter into negotiations with another Broadcaster. The Agreement requires that that a ROFN must be exercised by the Broadcaster by a fixed start date or in reference to a clearly

# Entertainment Law

## RECENT DEVELOPMENTS OF IMPORTANCE

specified timeframe identified in the development or license agreement. If no timeframe is provided, then the timing of the exercise of the ROFN will be at the sole discretion of the producer. If negotiations with the Broadcaster are entered into as a result of the exercise of the ROFN, the duration of the negotiation will be the timeframe specified in the development or license agreement, but cannot exceed 45 days.<sup>2</sup>

A ROLR provides the Broadcaster with the right to license a project that it previously rejected by matching the terms offered by another Broadcaster. A ROLR can significantly limit the bargaining power of the producer. As a result this type of right is limited by the provisions of the Agreement. Specifically, a Broadcaster may only be granted a ROLR to (i) acquire exclusive exhibition rights for additional programs or (ii) to obtain an extension of the license term.

The Agreement further addresses a Broadcaster's entitlement to share in any surplus financing proceeds beyond the original approved financing plan and/or in any production underages. Where the producer receives surplus funds for a project after the Broadcaster has approved the project's financing plan, the Broadcaster and the producer must give good faith consideration to whether the surplus funds should form part of the financing of the production. The Agreement provides that under no circumstances will the surplus entitle the Broadcaster to require a reduction in its licence fee. The Broadcaster is, however, entitled to a share of the surplus funds in proportion to any equity investment it has made. Further, where a program is produced under budget, the Broadcaster is entitled to a pro-rata share of the underages proportional to its investment in the financing.

### License Term

The Agreement provides for specific limits on the term of a broadcast license. Specifically, a broadcast license can only have a maximum duration of five years

(subject to a possible ROFN and ROLF as described below). This five-year term must commence no later than the earlier of (i) six months from the delivery of the program (or the last episode of the program in the case of a series), or (ii) the first telecast of the program (or any episode of the program in the case of a series).

While previously, a Broadcaster could negotiate an automatic extension of the original license term for the original season if additional seasons were ordered; this is no longer permitted by the Agreement. For example, a Broadcaster can no longer automatically extend the term of Season One once it orders Season Two to ensure that the licenses for both Season One and Two end simultaneously. This ensures that producers do not lose the potential value of exploiting earlier seasons as new seasons are produced and broadcast.

A Broadcaster is permitted to have a ROFN and a ROLF in order to extend the original five year term of the license, but only if a fair market value license fee is paid to the producer for the extension. Each subsequent license extension is for a maximum period of up to five years. The Broadcaster may exercise its right to extend the license as of the earlier of (i) six months prior to the expiry of the third year of the original five year licence term, or (ii) three months following the execution of the licence agreement for a subsequent season of the program.

### Editorial Control

The Agreement provides that, subject to certain permitted customary Broadcaster approval rights, it is the producer that retains ultimate control over a project. A Broadcaster, however, is entitled to exercise its standard creative, financial and technical approvals, which approvals must be published on the Broadcaster's website. Consultations and requests for approvals must be made in a timely manner, so that both parties have sufficient time to respond and there is no unreasonable delay in the development or production process.

There are circumstances where a Broadcaster may request changes to creative elements or propose additional creative elements that were not contemplated at the time the license agreement was initially entered into. To exercise this editorial control, it must provide the producer with an enhanced license fee proportionate to the scope of the new work required. This enhanced license fee is meant to cover the additional costs associated with the creative changes that were not contemplated by the original approved budget. The Broadcaster is also required to give the producer written notice of its requests for creative changes or additional creative elements as soon as possible.

The Agreement also clarifies the screen credits to which a Broadcaster and its representatives may be entitled. While the Broadcaster and its personnel are entitled to recognition in the screen credits of the program, credit placement and titles must be in conformity with industry standards. Broadcaster's representatives are entitled to be accorded traditional screen credits such as "Executive in Charge of Production", but not screen credits customarily reserved for the producer such as "Producer" or "Executive Producer" credits.

### Broadcaster and Producer Rights

A Broadcaster is entitled to certain exploitation rights in return for its payment to the producer of a fair market value license fee. These rights are exclusive to Canada and are applicable to all languages in which the Broadcaster is licensed to operate. The primary right of exploitation is linear broadcast rights on all CRTC licensed television services owned or affiliated with the Broadcaster. Broadcasters are also entitled to various additional exploitation rights that must all be geoblocked to Canada, namely: (i) linear streaming rights on all platforms that are simultaneous or non-simultaneous with the broadcast channels, (ii) free-to-consumer non-linear on-demand exhibition on all platforms, (iii) subscription-based non-linear on-demand exhibition on all

platforms, and (iv) the creation and operation of a program website, which includes the creation of original free-to-consumer or subscription-based content for the website.<sup>3</sup> The foregoing rights are exclusive during the license term and the Broadcaster is also granted a holdback against the “exploitation of the format” during the license term.

In addition to these basic exploitation rights, a Broadcaster may also negotiate to acquire additional rights. However, the acquisition of such additional rights is normally subject to a 50/50 gross revenue share between the Broadcaster and the producer.<sup>4</sup> The additional rights that a Broadcaster may license are: (i) transaction based (meaning on a per episode or discrete program basis) non-linear on-demand exhibition on all platforms, where the consumer secures temporary or rental access to the content, as opposed to a permanent copy, (ii) electronic sell through or download to own on all platforms where the consumer secures a permanent copy of the content, (iii) in-flight and (iv) DVD and home video.

If a Broadcaster acquires any additional rights, but does not exploit them within 12 months of the start of the license term, the rights so acquired automatically revert to the producer. If the foregoing rights are retained by the producer, they are subject to a 12-month holdback commencing at the start of the license term.<sup>5</sup>

In addition, a Broadcaster may acquire rights in certain types of producer-created digital content, such as websites, webisodes and mobisodes, if it either pays an additional license fee or it and the producer participate in a 50/50 revenue split. For the additional license fee, the Broadcaster may acquire Canadian rights to free-to-consumer original digital content produced by the producer. For the 50/50 revenue split, and at the discretion of the producer, the Broadcaster may also acquire Canadian rights to revenue-generating digital content produced by the producer.

Broadcasters are precluded from acquiring or having a profit participation in “any other rights”. A non-exhaustive list of

these other rights that are exclusively retained by the producer is provided in the Agreement. For example, a Broadcaster may not acquire rights in: French-language and other language,<sup>6</sup> format, theatrical, music publishing, non-promotional games and merchandising, all other non-theatrical, Canadian and international retransmission, Canadian and international sublicensing and distribution, and publishing of books, e-books or similar materials.

### Recoupment of Broadcaster Equity Investments

In order to encourage equity investment by a Broadcaster in producer-created content, and to ensure that its recoupment of such an investment is fair, the Agreement provides for the circumstances where a Broadcaster may recoup its equity investment in a project. Two scenarios are contemplated by the Agreement: (i) equity investments in television programs other than “programs of national interest” and (ii) equity investments in “programs of national interest”.<sup>7</sup> It should be noted that the Agreement does not apply to equity investments in feature films.

For television programs, other than “programs of national interest”, the Broadcaster will recoup its equity investment *pari passu* with the producer and on a “most favored nations” basis with other equity investors. Broadcasters are only entitled to recoup following the recoupment of any distribution advance in the financial structure. It should also be noted that, for recoupment purposes, Canadian film tax credits are treated as an equity investment of the producer.

If a Broadcaster makes an equity investment in a “program of national interest” and has also paid a license fee that is in excess of the Canadian Media Fund (“CMF”) threshold license fee for the applicable genre, different rules apply with regard to the Broadcaster’s recoupment of its investment. If the equity investment is C\$500,000<sup>8</sup> or more and constitutes 30 per cent or more of the production budget,

then the recoupment terms must be negotiated with the producer. If the equity investment is C\$500,000 or more and constitutes less than 30 per cent of the production budget, then the Broadcaster’s equity investment will be recouped as provided in the CMF Guidelines. The CMF Guidelines require that recoupment is *pari passu* with all other equity investors, including the producer’s provincial tax credit investment but excluding the producer’s federal tax credit investment, following recoupment of any distribution advance in the financial structure.

### Super-License Fees

The payment of a “super-license fee” allows the Broadcaster to negotiate for additional rights with the producer beyond those otherwise permitted to be licensed under the Agreement. The Agreement defines a “super-license fee” as the lesser of (i) the then current combined CMF threshold license fee for the applicable genre plus the maximum licence fee top-up for that genre or (ii) a licence fee representing at least 60 per cent of the project’s production budget.

If a super-license fee is paid, the Broadcaster may negotiate for a higher revenue share of certain rights and for a share of the profits from the producer’s exploitation of rights that are otherwise exclusively reserved for the producer. The Broadcaster may obtain a higher revenue share, meaning its participation rate can be increased from 50 per cent to a maximum of 75 per cent, for the following rights: transaction-based non-linear on-demand exhibition on all platforms, electronic sell-through or download-to-own platforms, in flight, DVD and home video, and producer-created revenue-generating original digital content.

Broadcasters may also, upon payment of a super-license fee, negotiate for a share of the profits from the exploitation of the rights that are exclusively reserved for the producer, such as the exploitation of non-promotional games and merchandising. A Broadcaster’s profit participation in such

# Entertainment Law

## RECENT DEVELOPMENTS OF IMPORTANCE

reserved rights may not be greater than 1.5 times its dollar investment expressed as a percentage of the budget that is over and above the combined CMF threshold license fee for the applicable genre plus the maximum license fee top-up for that genre, to a maximum of 30 per cent.

### Other Key Areas of the Agreement

The Agreement provides guidance as to a producer's permitted fees and overhead, as well as its retention of a share of film tax credits. Producer fees and overhead must be industry standard, as accepted by Canada Revenue Agency ("CRA").<sup>9</sup> Further, producer fees and overhead may not be deferred by the producer or invested.

The Agreement similarly protects the producer by limiting its permitted investment of film tax credits. A Producer may only invest up to a maximum of 75 per cent of eligible film tax credits in a project.

### Timeframe and Administration

As mentioned above, the Agreement is in full effect with respect to all of its

provisions as of August 1, 2011. It remains in force with respect to each Broadcaster until the expiry of the longest of the next issued license terms of the Broadcasters (excluding Astral).

In terms of ongoing administration, the CMPA and the Broadcasters have agreed to meet on a semi-annual basis to discuss new issues or current provisions of the Agreement which are no longer effective.

### Dispute Resolution

A Dispute Resolution Provision is attached as Appendix "A" to the Agreement. The parties must refer a matter in dispute to a sole private mediator for mediation. If the mediation effort fails after thirty days or, as an alternative to mediation, the party initiating the dispute so desires, the matter will be referred to arbitration by a sole arbitrator.

### Conclusion

The Agreement represents a watershed in the relations between Canadian producers and the Broadcasters. It sets new

"rules of the road" for both their legal and business relationships. It provides clarity regarding the rights which the Broadcasters may acquire from Canadian producers and the compensation which they must pay for those rights.

There will no doubt be some disagreements between the parties regarding the Agreement and the need for further clarifications (for example, the Canada Media Fund recently announced that its eligibility rules would be revised in order to conform to the Agreement as they contradicted it in several respects). However, ultimately, the Agreement benefits both Canadian producers and the Broadcasters by establishing clear legal criteria and business terms for their agreements. Most importantly, it establishes a key framework for the Canadian media industry to move forward and prosper in the age of digital distribution and multiple media formats and platforms. Finally, and as a bonus, it is good news for entertainment lawyers too (as new and complex rules always are). ■

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1. No definition is provided for "reasonable agreed-upon deliverables".
2. The 45 day period does not apply to the decision to initially license (s. 3(k)), the decision to renew an order for a program (s. 4(i)), or the decision to extend a license term (s. 5(c)).
3. Note that the producer retains a ROFN to develop and produce the original, free-to-consumer content for the program website.
4. The Broadcaster may be entitled to more than 50 per cent of gross revenues if a "super-license fee" is paid to the producer.
5. A "holdback" allows a Broadcaster to restrict exploitation by the producer or its licensees during the applicable holdback period. Regarding the holdback for "the exploitation of the format", there is no definition of "format" in the Agreement, but this presumably refers to a format based upon or derived from the licensed program which cannot be exploited by the producer in Canada during the applicable holdback period.
6. The Broadcaster may acquire these rights if the Broadcaster broadcasts in French or other languages.
7. The CRTC defines a "program of national interest" as including programs that belong to category 2(b) Long-form documentary (original works of non-fiction, primarily designed to inform but may also educate and entertain, providing an in-depth critical analysis of a specific subject or point of view over the course of at least 22 minutes) and category 7 Drama and Comedy (productions of a fictional nature, including dramatizations of real events that must be comprised primarily of dramatic performances), as well as award shows of national or regional scope that celebrate Canadian creative talent and/or cultural diversity and achievements in Canadian arts and culture.
8. The C\$500,000 threshold can be met when more than one Broadcaster makes an equity investment and collectively they invest C\$500,000.
9. The CRA *Application Policy FAS 2009-01* states that producer fees for producers that have an ownership interest in the production company are generally considered reasonable if they are within the reference threshold of "10% of the actual B (production) + C (post-production) costs" (15 per cent for low-budget productions totalling C\$500,000 or less).



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