Broadcasting Decision CRTC 2005-30

Ottawa, 31 January 2005

Encore Avenue Ltd.
British Columbia, Alberta, Saskatchewan, Manitoba, Nunavut, Yukon Territory and Northwest Territories

Application 2003-1664-7
Broadcasting Public Notice CRTC 2004-35
28 May 2004

Encore Avenue and Comic Strip – Licence amendment

*The Commission **denies** the application by Encore Avenue Ltd. to amend the broadcasting licence for its pay television programming undertaking in order to permit its two channels, one known as Encore Avenue and the other as Comic Strip, to be provided as an unencrypted service that can be distributed on discretionary analog tiers of broadcasting distribution undertakings.*

The application

1. The Commission received an application by Encore Avenue Ltd. (formerly MovieMax! Ltd.) for an amendment to the broadcasting licence for its English-language pay television programming undertaking that broadcasts on two channels, one known as Encore Avenue and the other as Comic Strip (hereafter referred to as Encore). The applicant requested authorization to permit Encore's channels to be provided as an unencrypted service that can be distributed on discretionary analog tiers of broadcasting distribution undertakings (BDUs).

Background

2. Encore is authorized to serve western Canada on an encrypted discretionary basis. It provides programming that is packaged by theme for delivery by BDUs to their subscribers on multiplexed program channels. Encore's channels consist primarily of feature films copyrighted at least five years prior to the year of their exhibition on the service. Encore Avenue Ltd., the licensee company, is indirectly owned by Corus Entertainment Inc. (Corus).

3. The Commission originally licensed the Encore undertaking (originally known as MovieMax!) as well as another pay television programming undertaking (now known as MoviePix), which was authorized to provide a similar movie service in eastern Canada,

in *Approval of New Pay Television Services: "The Classic Channel" and "MOVIEMAX"*, Decision CRTC 94-278, 6 June 1994. In that decision, the Commission stated that "it expects each licensee, consistent with its business plan, not to permit its service to be offered as part of any unencrypted high penetration tier."

4. On 2 March 2000, the Commission issued a letter setting out its determination on a complaint concerning the marketing and distribution of MoviePix on high penetration unencrypted tiers of BDUs. The Commission found that MoviePix's unencrypted distribution was limited to two BDUs in southern Ontario and that MovieMax had not been distributed on unencrypted tiers. The Commission reiterated that the licensees of MoviePix and MovieMax must not market or permit their respective services to be distributed on unencrypted tiers. The Commission also advised each licensee to include in its upcoming licence renewal application a rationale for why, in the new licence term, it should be able to market its service for distribution on unencrypted high penetration tiers of BDUs and to permit distribution on that basis.

5. The licence renewal application for the Encore undertaking did not include a request or rationale proposing that the service be marketed or distributed on unencrypted high penetration tiers of BDUs. In *Licence renewal for MovieMax!*, Decision CRTC 2001-731, 29 November 2001, the Commission renewed the licence for the undertaking to 31 August 2008.

The applicant's rationale

6. In support of the present application, Encore Avenue Ltd. submitted that the distribution restrictions imposed on Encore have created a competitive imbalance in the marketplace because many other discretionary programming undertakings that offer similar programming are not required to provide their services for distribution on an encrypted basis. The applicant further contended that authorizing the distribution of Encore on an unencrypted basis would provide distributors with the flexibility to distribute Encore on an analog tier and, thereby, enable them to be more responsive to their subscribers' preferences.

7. The Encore service is currently subject to a condition of licence requiring that at least 20% of all programming exhibited on the service between 6:00 p.m. and midnight, and at least 20% during the remainder of the time that it is in operation, be Canadian. Further, by condition of licence, at least 25% of Encore's previous year's gross revenues must be spent on the acquisition of, or investment in, Canadian programming. As part of the application process, the Commission asked the applicant if it would agree to adhere to higher minimum requirements for the exhibition of, and expenditures on, Canadian programming.

8. The applicant responded that Encore's current minimum level of Canadian content should be maintained until such time as it achieves the level of revenue forecast for 2004. At that time, it would be willing to accept a condition of licence to provide a minimum of 25% Canadian content during both time periods noted above, if it were granted the carriage status proposed in its application. The applicant, however, specified that any such increase would be contingent upon an amendment to Encore's condition of licence defining its nature of service in order to add the following program categories to its list of authorized program categories: 7(a) (On-going dramatic series) and 7(b) (On-going comedy series). All programming distributed from these categories would be copyrighted at least five years before its distribution.

9. The applicant contended that an increase in its minimum requirements for Canadian programming expenditures would not be warranted because Encore is currently experiencing declining revenues and has not achieved the revenue projections filed in 2002 as part of its licence renewal application.

The interventions

10. The Commission received eight interventions in connection with this application: one in support, six in opposition and one that commented on the proposed licence amendment.

11. The Canadian Cable Telecommunications Association (CCTA) supported the application. In the CCTA's view, the distribution restrictions imposed on Encore are outdated and no longer necessary. The CCTA stated that, over the past ten years, a large number of specialty services have been introduced into the Canadian broadcasting system, and the broadcasting distribution market has also become much more competitive. The CCTA contended that increased flexibility to package programming services is critical in such a competitive environment and submitted that approval of this application would provide hybrid analog-digital cable distributors with the additional packaging flexibility that is currently available to all digital BDUs.

12. The opposing interventions were filed by Astral Broadcasting Group Inc., CTV Inc., CHUM Television, Craig Media Inc., the Directors Guild of Canada, and Friends of Canadian Broadcasting.

13. According to the opposing interveners, the approval of the proposed distribution model would essentially change every aspect of Encore's service, including its business plan, the basis on which it was licensed, its carriage status and its nature of service. The interveners further maintained that the applicant did not demonstrate a financial need for the proposed amendment. They contended that Encore's profit before interest and tax (PBIT) margin of 52.03% is among the highest of all specialty, pay and pay-per-view services, and more than double the average PBIT margin (19.45%) of analog specialty services.

14. The opposing interveners also noted that Corus, Encore's owner, is a corporate affiliate of Shaw Communications Inc. (Shaw), the dominant cable operator in western Canada, Encore's authorized service area. The interveners expressed concern that, in the circumstances, Shaw could grant preference to Encore and subject unaffiliated programming services to an undue disadvantage. In the view of the opposing interveners, it would be difficult for the Commission to prevent such conduct after the fact.

15. The opposing interveners argued that permitting Encore's distribution on unencrypted discretionary analog tiers of BDUs would have a significant negative impact on analog specialty services. Encore, which is subject to substantially lower requirements for the exhibition of, and expenditures on, Canadian programming than those imposed on specialty services, would be in a position to compete directly with analog specialty services for viewers and programming rights. Furthermore, the distribution of Encore on this basis could result in the displacement of both analog and digital specialty services. Encore is multiplexed on two separate channels, and if both channels were distributed on analog tiers, such distribution would use a capacity equivalent to that used by 15 to 20 Category 2 digital services.

16. The opposing interveners pointed out that, in accordance with the Commission's distribution and linkage requirements[1], Encore, as a Canadian pay television service, may be linked in a given discretionary tier with five channels of any non-Canadian services set out in the lists of eligible satellite services[2]. In the interveners' view, the distribution of Encore on an unencrypted basis on discretionary analog tiers of BDUs would, therefore, severely affect the balance of services provided by BDUs. Additionally, the interveners contended that the applicant's plans to package Encore in a tier with services from Section B of the *List of Part 2 Eligible Satellite Services*, services which are reserved exclusively for packaging with pay television services, would allow the migration of additional services from this list to analog carriage and, thereby, exacerbate channel capacity constraints on BDUs.

17. In the view of the opposing interveners, the applicant's proposal conflicts with the objectives of the Commission's policy of encouraging the deployment of licensed Canadian digital programming services, and an approval would represent a step backwards in the cable industry's conversion to digital technology. Finally, the interveners contended that the applicant should have addressed the issue of Encore's distribution at the time of its last licence renewal application, as the Commission had advised in its determination letter of 2 March 2000.

18. While neither supporting nor opposing the application, Global Television Network Inc. (Global) commented that, if the Commission allowed Encore to be distributed on an unencrypted basis and to broadcast programming from categories 7(a) and 7(b), such programming should be limited to 10% of the broadcast week. Global added that the

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[1] The Commission's requirements are most recently set out in *Distribution and linkage requirements for Class 1 and Class 2 licensees*, Broadcasting Public Notice CRTC 2003-42, 29 July 2003.

[2] The most recent lists are set out in *Revised lists of eligible satellite services*, Broadcasting Public Notice CRTC 2004-88, 18 November 2004.

programming broadcast by Encore from categories 7(a) and 7(b) should have been copyrighted at least ten years prior to the date aired in order to prevent any disadvantage to the intervener's specialty service Prime TV, which offers programming targeted to men and women 50 years of age and over. Global also supported imposing higher minimum Canadian content requirements on Encore.

The applicant's reply

19. In response to the opposing interveners, the applicant submitted that the current restrictions on Encore's distribution are no longer necessary because numerous conventional and specialty television services now offer a vast array of movies copyrighted five or more years earlier, competing directly with the service Encore is licensed to provide.

20. The applicant pointed out that Encore is licensed as an analog service, not as a digital service. Accordingly, in the applicant's view, the approval of this application would not change the basis on which Encore was licensed.

21. The applicant noted that some of the interveners had focused on Encore's 2003 PBIT margin of 52.03%, stating that it is among the highest of the specialty and pay television services. According to the applicant, however, such percentages can be misleading and, in this case, do not reflect the erosion in subscribers and revenues experienced by Encore over the past several years, nor its significant underperformance in relation to analog specialty services that broadcast a substantial number of classic movies.

22. The applicant maintained that the interveners did not provide any evidence that the approval of this application would lead it or its parent company, Shaw, to contravene the provisions prohibiting undue preference set out in section 6 of the *Pay Television Regulations* and section 9 of the *Broadcasting Distribution Regulations*.[3]

23. With respect to the interveners' concerns about the impact of the proposed distribution model on specialty services, the applicant stated that its proposal is intended to provide additional carriage flexibility for western Canadian cable operators, which serve only about 38% of the cable subscribers in English-speaking Canada. Since those operators would make carriage choices on a system-by-system basis and their choices would be influenced by various factors, the applicant submitted that it was unlikely that the approval of the proposed amendment would cause wholesale displacement of analog specialty services.

24. The applicant stated that the Commission has consistently imposed lower Canadian content requirements on pay television movie services than on specialty services because of the limited supply of Canadian feature films. In the case of Encore, obtaining

[3] Section 6 of the *Pay Television Regulations* and section 9 of the *Broadcasting Distribution Regulations* stipulate that no licensee shall give an undue preference to any person, including itself, or subject any person to an undue disadvantage.

Canadian feature films is even more challenging because the service is restricted to broadcasting feature films copyrighted five or more years before their exhibition on the service.

25. With respect to the interveners' concerns about the impact of the proposed distribution model on the balance of services in the Canadian broadcasting system, the applicant noted that, while Encore is licensed as an analog service, it is distributed as part of the digital service of many western cable BDUs in order to stimulate the growth of cable digital tiers. The applicant contended that, whether Encore's carriage on an analog tier would use additional analog spectrum in any system would depend on whether it were added to an analog tier or substituted for a service already on that tier. The applicant added that cable operators might choose to drop a non-Canadian service to make room for Encore.

26. The applicant stated that, although Encore is multiplexed and offers two channels, it would make only one of the two channels available for distribution on unencrypted analog tiers of BDUs. In addition, the applicant stated that it would agree that Encore be packaged with a Canadian specialty service on a 1:1 linkage basis. The applicant, however, submitted that cable operators should be permitted to choose a linkage partner from either Section A or Section B of the *List of Part 2 Eligible Satellite Services*.

27. With respect to the interveners' argument that this request should have been raised at the time of the undertaking's last licence renewal, the applicant submitted that a number of factors have occurred in the intervening years that make it timely for the Commission to consider this matter at this time. The applicant added that it had filed its application in accordance with the *CRTC Rules of Procedure*.

28. In response to Global's comment, the applicant stated that it would accept the intervener's recommendation that the programming broadcast by Encore from categories 7(a) and 7(b) be limited to 10% of the broadcast week. The applicant also stated that it was willing to increase its Canadian content requirements to 25% overall and between 6:00 p.m. and 11:00 p.m., Mountain Time.

The Commission's analysis and determination

29. The Commission notes that, although Encore's revenues and PBIT have decreased in recent years, it still enjoys a high level of profitability. In 2003, Encore's PBIT margin was 52.03%, while the average 2003 PBIT margin for all English-language pay and specialty services was 13.9%. The average 2003 PBIT for all English- and French-language analog specialty services was 19.5%. The Commission recognizes that the Canadian broadcasting system has become increasingly competitive since the Encore undertaking was originally licensed in 1994, but is satisfied that the increased competition has not unduly affected Encore's financial situation. Accordingly, the Commission is not persuaded by the applicant's arguments that increased competition justifies a change in Encore's distribution status.

30. In the Commission's view, the distribution model proposed by the applicant would allow Encore to compete more directly with specialty services, which are subject to significantly higher requirements than Encore with respect to the exhibition of, and expenditures on, Canadian programming. The Commission notes that, on average, English-language analog specialty services are required to provide a minimum Canadian content level of 57% and to expend 42% of the previous year's gross revenues on Canadian programming. In comparison, Encore must provide a minimum of 20% Canadian content overall and 20% Canadian content between 6:00 p.m. and midnight, and spend 25% of the previous year's gross revenues on Canadian programming. Even if Encore's minimum Canadian content requirements were increased to 25% in both time periods, as proposed by the applicant if it were granted the carriage status requested in its application, the applicant's minimum requirements in this regard would still be substantially lower than those imposed on English-language analog specialty services. While the Commission recognizes that pay services' lower requirements with respect to Canadian programming reflect the limited supply of Canadian feature films, the Commission, nevertheless, finds that, given the substantial difference between Encore's requirements and those of most specialty services, it would not be appropriate to allow Encore to compete more directly with specialty services.

31. The Commission notes that analog trap technology would generally prevent Encore from simply being added to an existing tier. Furthermore, given the scarcity of available analog channels, the distribution status requested by the applicant would oblige most cable operators to remove or displace an existing service, and thereby cause disruption in the packaging of specialty services. The Commission's concern in this regard is aggravated by the fact that the cable BDUs operated by Shaw, the applicant's parent company, represent the vast majority of Encore's potential subscriber base. In the circumstances, the Commission considers that Shaw would have a strong economic incentive to move Encore to a high penetration analog tier. The Commission notes that Shaw did not provide any assurances or safeguards that it would not displace an existing specialty service with Encore, or would not otherwise treat the service preferentially. In the absence of such assurances or safeguards, the Commission finds that there is significant potential for the displacement of specialty services and preferential treatment of Encore.

32. As the applicant noted in its response to the opposing interveners, Encore is currently distributed as part of the digital service of many cable BDUs in western Canada. Pay movie services such as Encore are popular with subscribers and, when distributed as part of digital pay packages, serve as incentives to encourage subscribers to choose digital services. In the Commission's view, allowing Encore to be distributed on unencrypted discretionary analog tiers of BDUs could reduce the attractiveness of the digital pay packages offered by BDUs, and thereby serve as a disincentive in the deployment of digital services. The Commission finds that approval of this application would be inconsistent with the objectives of the Commission's longstanding policy of encouraging the cable industry's conversion to digital technology.

33. Based on all of the foregoing, the Commission **denies** the application by Encore Avenue Ltd. to amend the broadcasting licence for its English-language pay television programming undertaking in order to permit its two channels, one known as Encore Avenue and the other as Comic Strip, to be provided as an unencrypted service that can be distributed on analog tiers of BDUs.

Secretary General