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To: The Standing Committee on Industry, Science and Technology, House of Commons, Canada

Re: Statutory Review of the *Copyright Act*

December 10, 2018

I have undertaken a number of economic studies of the Canadian music industry and other copyright industries in Canada that should be useful to the Committee in considering steps to modernize Canada's *Copyright Act*. My recent analysis has focused on measuring the size of the Value Gap in the music industry in Canada, identifying its causes, and ascertaining its consequences for artists and other music stakeholders. This work, as with this brief, has been prepared at the request of Music Canada, and is submitted by me in my capacity as an independent expert.

The "Value Gap" refers to the disparity between the market value of creative content accessed by consumers and the revenues received by the artists and businesses who create it. The Value Gap occurs when third parties commercially exploit artists' creations online without fully compensating them for their market value, or at all. My analysis confirms not only that the Value Gap exists, but also that it is considerably greater than many observers have previously concluded. Furthermore, the Value Gap continues to increase, even with the growing popularity of music streaming services. I have further shown that the Value Gap will continue to grow unless federal policymakers in Canada implement measures to prevent the unauthorized commercial exploitation of creative works and thereby ensure that creators are compensated fairly. Specific solutions are outlined further below.

The Value Gap can be boiled down to three key numbers (in CAD):

- **$19.3 billion**: the cumulative Canadian recorded music industry Value Gap over 20 years since 1997.
- **$1.6 billion**: the music industry Value Gap in Canada in 2017 alone. Absent this gap, 2017 music industry revenues would have reached $2.2 billion – nearly four times the actual revenues of $570 million.
- **$82 million:** the average annual increase in the music industry Value Gap from 1997 to 2017 in Canada.

Canadian Copyright Law and the Value Gap

The Value Gap is caused by the many exceptions and limitations to copyright in Canadian law that have led to the situation where the authorization of rights holders is effectively not required for use of creators' works. The requirement of consent provides the basis for vibrant markets in creative content.

Recent technological developments make such markets possible, removing past justifications for music copyright exceptions. Since the mid-1990s, the digitization of content and spread of the Internet, together with developments in artificial intelligence, machine learning, blockchain and fintech mean it is possible to have markets involving micro payments to copyright owners for their consent to full, partial, or incidental use of music. Internet intermediaries indeed already meticulously track online behaviours, and collect, analyse and sell the metadata generated 24/7. The key reason, or obstacle preventing the development of mass online markets in music is the lack of incentives Internet intermediaries have to develop them. The numerous exceptions, limitations and immunities to copyright are the source of these weak incentives. At the same time, the digitization of content and spread of the Internet has also made it easier than ever to copy and distribute creative works *without* consent, thereby reducing the effective level of copyright protection. Adequate protection and enforcement of copyright is therefore both more possible and essential to an efficient legitimate market today than ever before.

In Canada, properly functioning digital marketplaces have been undermined by a weak legislative framework for copyright that is poorly adapted to the digitization of content and today's digital economy. A significant source of this weakness is found in the "safe harbours" exceptions in the *Copyright Act* that exempt active intermediaries like YouTube from paying market royalties to creators when recordings are commercially exploited on their service. This undermines the ability of right holders to enforce their rights in digital music distribution, thereby allowing these commercial intermediaries to avoid compensating rights holders, wholly or in part. I estimate the Value Gap or deficit between the market value of the music distributed by YouTube and what it pays to creators as a result is approximately $550 million per annum in Canada.

Other exceptions in the *Copyright Act* increase the gap between the market value generated by music consumption and payments to right holders. In each case, commercial music users exploit recordings for commercial gain, but little to none of the economic value is passed on to creators. Examples include:

- The radio royalty exemption, which exempts commercial radio stations broadcasting sound recordings from paying royalties on their first $1.25 million in advertising revenue (other than a nominal $100). This exemption is estimated by Music Canada to cost artists and record labels $8 million annually. From 1997 to 2014, the losses are estimated by Music Canada to total $122 million (Music Canada 2017 Value Gap report).

- The definition of a "sound recording" used in TV and film soundtracks, which effectively exempts royalty payments to performers and creators (but incongruously, not songwriters, composers and music publishers) when their recordings are played in TV and film soundtracks. This exemption is estimated by Music Canada to cost artists and record labels $45 million in annual revenue (Music Canada 2017 Value Gap report).

The Broader Economic Impact of Inadequate Copyright Protection

Using a "top down" method of calculating the Value Gap – the difference between actual realized revenues and the amount that would have been realized had revenues kept up with inflation and GDP since 1997 – demonstrates that music revenues in Canada would have reached $2.2 billion in 2017. That figure is 3.86 times more than the actual 2017 revenues of $570 million -- a $1.63 billion Value Gap.

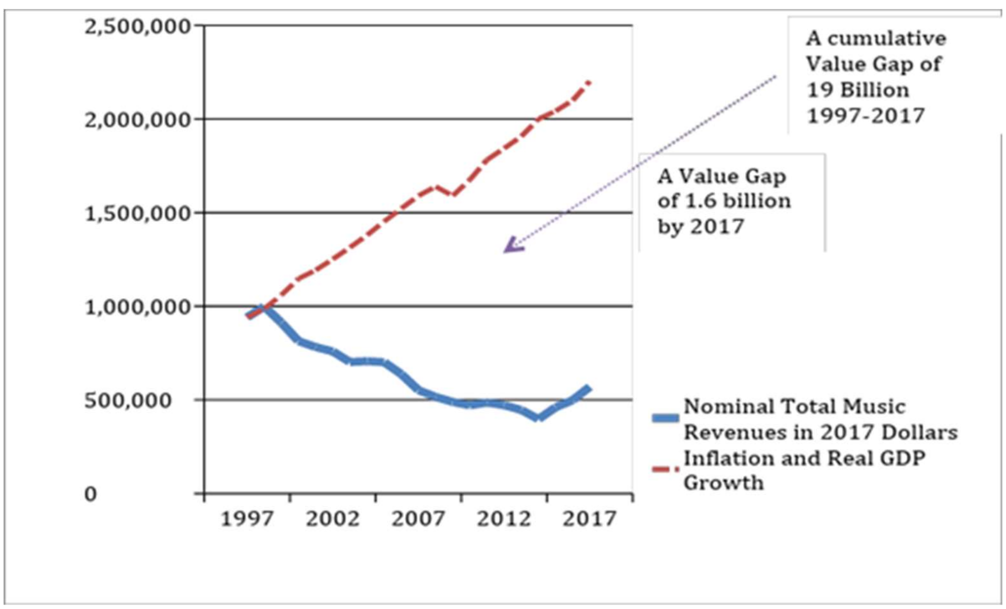
The cumulative recorded music Value Gap in Canada over the 20-year period since 1997 is estimated at $19.3 billion. This is the sum of the annual difference between actual realized revenues and the amount that would have been realized had revenues kept up with inflation and GDP since 1997. The annual loss averaged $919 million over the 20-year period, growing by an average of $83 million a year.

The situation has improved moderately in recent years with the rapid consumer uptake of streaming music services. Canada's overall recorded music market posted a compound annual growth rate of almost 3.9% from 2013 to 2017, according to IFPI's 2018 Global Music Report. At face value, one might conclude that Canada's music industry is well on its way to recovery from its well-known challenges during the previous two decades. But this 3.9% growth rate is lower than the growth in nominal GDP over the 20-year period 1997 to 2018, which was 4.13% per annum. So, compared to inflation and GDP growth, the Value Gap is only likely to continue growing.

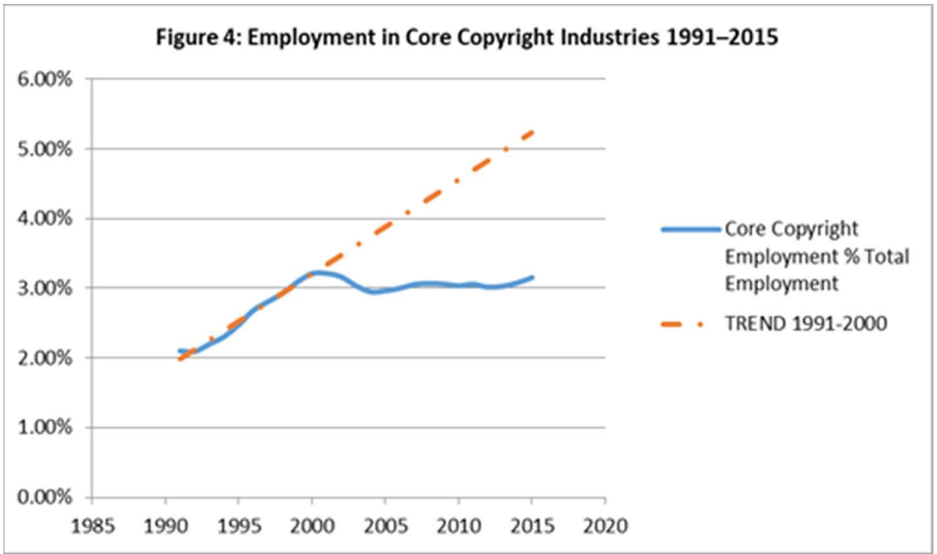
In truth, music industry revenues today remain far behind the revenues posted before the digital revolution, as demonstrated above. And despite the recent nominal gains, the Value Gap has continued to expand by an estimated $25 million annually over the past two years after accounting for inflation and GDP growth. Thus, despite the recent, robust growth of streaming music revenues, the Value Gap continues to increase.

The following figure shows the growing deficit between actual nominal Canadian recorded music industry revenues (the lower downward sloping line) and what revenues would have been in each year from 1997 had revenues kept up with the rate of inflation and economy-wide real GDP growth (the upward sloping line). The divergence in the two lines illustrates the Value Gap.

Total Canadian Recorded Music Industry Revenues



The Value Gap manifests itself not only in eroded revenues, but also in a two decade-long stagnation of employment growth in all copyright industries. As shown in the figure below, core copyright industries' (CCI) share of overall Canadian employment grew from 2% in 1990 to more than 3% in 2000 and then fell and stagnated, so that by 2015 it was lower than it was in 2001.



Reducing the Value Gap

The key to reducing the Value Gap are amendments to the *Copyright Act*. An optimal and balanced legal regime should ensure that unauthorized commercial exploitation of creative works is not permissible, and that creators are compensated fairly. Other jurisdictions worldwide, including the EU and the United States, are currently taking measures to create a functioning marketplace.

I understand that Canada's leading music stakeholders, including artists, have agreed on a common, modest package of immediate reforms, with the goal in the immediate term of limiting the growth of the Value Gap, rather than seeking to address the full $1.63 billion deficit. The following four actions have been proposed:

1. **Eliminate the radio royalty exemption from the *Copyright Act***.

   ● Estimated annual benefit to artists and their partners: $8 million (Music Canada Value Gap Report).

2. **Amend the definition of "sound recording" in the *Copyright Act***.

   ● Estimated annual benefit to artists and their partners: $45 million (Music Canada Value Gap Report).

3. **Create a fund for private copying**.

   - This would move Canada toward the global standard on private copying.
   - Estimated annual benefit to artists and their partners: $40 million.

4. **Extend the term of copyright for musical works**.

I can confirm that implementation of these measures would slow the continued widening of the Value Gap, and if Music Canada's estimates are right, possibly stop its further growth. Additional steps to create a properly functioning and efficient marketplace – notably the elimination of certain copyright exceptions and limitations and narrowing the scope of immunities shielding non-passive Internet intermediaries – should also be instituted.

The Benefits of Reducing the Value Gap

The narrowing of the Value Gap will produce significant economic benefits to artists, other music stakeholders and consumers.

The measures outlined above will provide partial financial relief to the many Canadian artists whose incomes have been sharply depressed by the Value Gap. They will also make more money available to music businesses to grow and invest in artist development and to offer skilled jobs and will increase the competitiveness of Canada's music industry in global markets.

These outcomes will lead to greater creative output over time. Fans and consumers will benefit from new Canadian recordings from current artists, as well as new artists who will be enabled and encouraged to enter a career in music.

I would be pleased to answer any questions you may have regarding this submission, the research it is based upon, or economic aspects of the Value Gap.

References:

For further details, please refer to the three papers upon which this brief is based. To the best of my knowledge, no other economic analysis of this type has been conducted in Canada.

Dr. George R. Barker, "The Value Gap in Online Music Markets in Canada: The Case of Music Streaming & The Role of the Law", October 3, 2018 (draft; publication forthcoming early 2019).

Dr. George R. Barker, "Testing for a Golden Age in Copyright Industries in Canada", March 20, 2017. (http://serci.org/congress_documents/2018/Barker.pdf).

Dr. George R. Barker, "A 'Golden Age' for the Creative Sector? The Effect of Digitisation and the Spread of the Internet on Creative Industries", August 28, 2016 (http://ssrn.com/abstract=3048349).

Where noted above, certain information was sourced from:

Music Canada, "The Value Gap: its Origins, Impacts and a Made-in-Canada Approach" ("Music Canada Value Gap Report"), 2017 (https://musiccanada.com/wp-content/uploads/2017/10/The-value-Gap-Its-Origins-Impacts-and-a-Made-in-Canada-Approach.pdf).

"IFPI, "Global Music Report 2018: Annual State of the Industry", 2018 (http://www.ifpi.org/downloads/GMR2018.pdf)