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January 11, 2019

The Broadcasting and Telecommunications Legislative Review Panel
c/o Innovation, Science and Economic Development Canada
235 Queen Street, 1st Floor
Ottawa, Ontario K1A 0H5

Dear Chair and Panel Members:

Re: Review of the Canadian Communications Legislative Framework

1. OUTtv Network Inc. operates the CRTC-licensed discretionary service OUTtv. First licensed in 2001 as the digital specialty service, Pridevision, OUTtv was the world's first television network licensed specifically to cater to the needs of the under-served LGBTQ2 community and their allies. OUTtv remains Canada's only LGBTQ2-focused television network.
2. OUTtv is a member of the IBG/GDI. We have worked in conjunction with the IBG/GDI to develop its submission. We agree entirely with its contents and will defer to its recommendations in respect to specific legislative drafting. We will try not to duplicate the arguments made in the IBG/GDI submission but to augment them and provide context.
3. Our goal is to provide what we consider important information and details on what independent broadcasters – which may soon be all Canadian broadcasters – will require to survive and to thrive in the future. We believe it is possible to create a legislative and regulatory framework within Canada that gives our industry a chance to be competitive both in our marketplace and in world markets as well. However, the Panel will need to understand the real structural changes going on in order to thoughtfully create laws to manage them.

The OUTtv Situation

4. The core theme of this submission is to give the Panel insight into what independent broadcasters need from legislation and the regulators, and why.
5. The problem for independent broadcasters is that it has always been a double-edged sword in talking about your current situation: If you are not doing well and are asking for "protection" it is because you are not competitive/smart/good enough; If you are doing well then why are you asking for help? Either way, you cannot win.

6. Nonetheless, OUTtv had a very good year in 2018. Our business grew in virtually every area. On the broadcasting side our revenue was up by just over 10%. This is certainly remarkable in a system that is shrinking overall. We would like to credit it on the intelligence and hard work of our team, but we mostly attribute it to luck: at first it was bad luck that had a major carrier putting us in a terrible package that caused a major CRTC dispute. Now we have the good luck of finally seeing the benefits of that correction many years later.
7. We do credit our team for the huge increase in viewing on OUTtv over the past two years. Our audience numbers are up nearly 300% overall and 200% in prime time. In a normal business situation this would result in a rise in subscriptions, but it is hard to correlate. Maybe we could negotiate new agreements with the BDUs based on performance? No such luck, as no one is giving out increases.
8. What about advertising? Well, things are better but it is still not enough to overcome our overall lack of market penetration. Now, there is a thought! During our free preview last year our audience numbers were up by nearly 400%. Our advertising sales group told us that if we had that level of market penetration the entire year we could sell at least \$500,000 per year more in advertising and perhaps as much as \$1,000,000 more. This would cost the system nothing, and, as an additional benefit, OUTtv would be obligated to spend 40% of this additional revenue on Canadian content production. However, increased market penetration is non-negotiable for independent broadcasters.
9. None of this is a surprise to us. We know the failings of the broadcasting system well, so we have begun building our business outside of it. In 2016 we launched a direct-to-consumer subscription-video-on-demand service in Canada called OUTtvGo. The service has just completed its second year and is doing very well. Subscriptions are up year over year by 353%. While they are growing from a small base, the revenue is significant enough that it now falls behind only Bell, Rogers and Shaw on a monthly basis and is quickly narrowing the gap.
10. We have used OUTtvGo as a springboard to launch in international markets. Our strategy outside Canada has been to get branded placement inside local on-demand platforms. Last year we launched in New Zealand through TVNZ and in Australia through Channel 7 with second and third providers coming soon in that territory. We will also officially launch in South Africa in 2019 after running a test in the market in 2018. Currently we are negotiating with platforms that would bring us into 23 other countries.
11. Much of the content is Canadian content and most of that is OUTtv original content. Our business model is to make programs and sell them through as many platforms in as possible in as many countries as possible. It is no different than any other business, as we try to make the programs for less than we sell them for. However, this does make us rare among Canadian broadcasters – particularly compared to the vertically integrated companies who have limited export businesses despite their size and scale. Yet they receive enormous amounts of money from Canadian sources like the CMF. Last year Corus received \$43 million and Bell Media \$36 million from the CMF. OUTtv received nothing.

12. OUTtv also has digital distribution deals with most of the major technology companies. We sell content in Canada and abroad through iTunes and Google Play. We sell content through Amazon Prime in a number of countries. Our OUTtvGo app is on many platforms including Apple TV, Chromecast and Roku. In 2018 our digital business was up 235%. We project that in 2019 this part of our business will grow in percentage terms by much more than that.
13. Normally this is where the independent service crowds about their accomplishments and declares that they are immune from market forces and are not worried about the future, but that is not us. We are here to tell you that we are very scared about the future.
14. What are we scared of? We are not scared of the digital future. We understand that and are transitioning our business to meet those challenges. We are scared of monopolization and the forces of anti-competition. We are scared that our regulations don't respond to the economics of competition in their sectors. While this is a bold statement, the evidence of the past decade – and the past two major broadcasting hearings looking at competition – demonstrates they don't.

What do we want?

15. What we want, and what Canada needs in our broadcasting system, is competition. We desire the opportunity to compete, but not in a so-called fairy tale 'free market', where the field is tilted against us or where the house sets the rules so it always wins. To use a sports analogy, we want to work in a system where the referees understand the game and where the rules are designed for everyone to be able to compete on a level playing field.
16. We want broadcasters (or programming service providers, as we should now be called) to be able to compete over audience and subscribers within a platform. We also want access to all platforms – Canadian and foreign - on fair commercial terms. We may also need rules that redress imbalances to restore competition or for other policy reasons, including the promotion of diversity and other social goals.
17. In many areas of our society we accept that rules are required to maintain competition. Often these rules redress imbalances or create different types of competition. For example, we accept that in the NHL the team that finishes last place gets a better chance at the first pick in the next draft. Boxers and weight lifters compete in different weight and size classes. Golfers have handicaps. There are men's and woman's leagues, amateur leagues and pro leagues, and leagues for people of different ages.
18. We accept this is fair and that we all gain as a result. We accept in sports and in life that not all competition is bare and absolute. After all, the goal of competition is not to create winners and losers but to allow all of us to strive to be better. In a market, competition allows us to develop better products and services and to foster innovation and creativity. There is no capitalism without competition.

Understanding Two sided markets

19. In order to propose changes that would re-establish a competitive marketplace our regulations have to meet the dynamics of a two-sided market like the Broadcasting system.

A two-sided market is one in which an intermediary company or platform provides network benefits to each side of the network. The key feature of a two-sided market is that there are two separate and somewhat distinct markets.

20. Two-sided markets are found in many industries. The most common everyday form is found in almost any retail business. The role of the store is to negotiate for goods with suppliers and to sell those goods to consumers. It is always a good business model if you can build a sizeable marketplace because you know the prices on each side of the economic equation.
21. However, we have seen how problems can arise when the intermediary grows too powerful. The impact of Walmart on the retail business over the past 30 years is a prime example. As their market share grew larger, suppliers could not survive without them. This allowed them to push prices down to cost or even below cost for some suppliers. Walmart even got into the business of encouraging US businesses to set up in China to lower costs.
22. US regulators did not interfere because they came believe that so long as the consumer side of the industry was happy – and Walmart maintained low prices – everything was fine. However, to achieve them Walmart laid waste to many businesses -both local suppliers and local retailers - and to many communities. No one bothered to look at the supplier side.
23. Amazon is now successfully challenging Walmart by moving retail online. Much like Walmart it has also moved into the business of creating its own products and competing against its own suppliers in certain product categories. In some industries it has gained such a dominant position it is being called a monopopoly – where a market only has one buyer. One example is the book industry where they control such a large percentage of sales no book publisher can do without their market reach. However, prices have been driven down so low no one can make living.
24. This is where we all lose. If authors can't make a living then we are deprived of their works and a new generation of writers are discouraged from pursuing their craft.
25. In the broadcasting system the intermediary is the BDU, which provides the delivery for the channels and also the product to the consumer. Like in retail, the markets are linked but again, can operate very distinctly.
26. Again, the markets function together but can be very different on both sides. For example, a consumer might see a package of 10 channels available for \$10.00 from their BDU. The consumer sees the package – quite rightly – as offering the channels at \$1.00 each. However, in the wholesale market things are different. One channel may receive \$9.91 from the BDU with the other 9 only costing \$0.01. While this example is extreme, it more accurately reflects the reality than the consumer's assumption. Of course in Canada, the costlier channels would be the services owned by a vertically integrated company.
27. To maintain competition, two sided markets must be properly regulated at both the wholesale and retail level – particularly when they are highly concentrated. Failure to properly regulate the wholesale side and restore competition has potentially disastrous consequence for suppliers – as it has for Canadian independent broadcasters.

Past CRTC decisions and Two-sided markets

28. Two recent CRTC policy decisions failed to understand this fully, which is why they both failed to achieve their goals.
29. The first of these decisions was, in fact, a series of ownership transactions that have resulted in the major BDUs coming to control the large majority of broadcasting services. This decision was intended to make the Canadian system “more competitive” and to create “Canadian champions” by placing both sides of the market in the control of a few companies.
30. Of course, with full control of the Canadian market these companies simply pursued their competitive advantage against the independent sector. They used it to buy up more US and other foreign content and were happy to simply monopolize Canada. As a result, they never focused on the development of an export strategy for original programming. For this part, they have themselves to blame.
31. Vertical integration has always ended badly, as controlling both sides of the market leads to conflicts of interest, monopoly, rent seeking and discourages innovation. Professor Timothy Wu’s excellent book, *The Master Switch*, on the history of U.S. information industries and documents how vertical integration corrupted and weakened them all.
32. We are clearly in the middle stages of the unwinding of vertical integration and can now clearly see the failings of the it as a way to champion our cultural industries. We have set out the reasons for this elsewhere and refer you to our articles in CARTT for greater detail. In fact, it is reasonable to speculate that its unwinding will test the Government’s resolve on maintaining Canadian ownership, as the vertically integrated or BDU-related companies seek relief from these regulations to salvage their financial share positions or divest of their broadcasting assets.
33. The Let’s Talk TV decision was different but similarly lacked a complete understanding of the structure of the Industry. Its focus was entirely on the fixing the consumer side of the equation and using customer choice to fix the wholesale side. Even a simple understanding of how two-sided markets function would show this assumption to be dubious, but in a vertically integrated market it was a hopelessly naïve.
34. In any event, the consumer-driven Let’s Talk TV decision failed to live up to its promises that consumer choice would move the system to a market-driven utopia. The proof is easy enough to see. There remain a large number of channels owned by the vertically integrated companies simply taking up space and collecting rent. They have few staff, little or no new programming and no one watching. BDUs still have a remarkable power to keep prices high, and if Canadians want pricing relief, a lot of them just leave the system entirely.

Meet the New Boss, Not the Same as the Old Boss

35. 2019 will bring perhaps the biggest challenge to the broadcasting system since the arrival of Netflix and the first streaming services. The launch of the new virtual BDUs will start this

spring and will continue over the next few years. These services will be the first non-Canadian challenge to the previously protected BDU ecosystem.

36. The competitors will be the tech giants including Amazon, Apple, Google, and eventually Facebook Watch. Long term we will see more from other tech giants such as the Chinese firms Tencent and Alibaba. It is important to note that these will be the first BDUs not owned by Canadians operating in Canada since the 1970s. It is therefore particularly important that they are regulated to form part of the broadcasting system.
37. It would be impossible to bet against their success. How successful and how quickly they will gain market share is anyone's guess, but we would be remiss in not preparing for the day when their share is the majority of Canadian households. These companies have distinct advantages over our current BDUs and one of them is very important for regulators to understand. The first two competitive advantages are well known: scale and network effects.
38. The size and scale of the large Internet companies entering the broadcasting space is well known. Internet traffic is dominated by FAANG (Facebook, Apple, Amazon, Netflix and Google) and other giant companies that include Microsoft, Ebay and Chinese firms such as Tencent, Alibaba and Baidu. The only non-US or Chinese firm in the top 20 is Swedish Spotify that ranks 20th. The scale and size of these companies is staggering. They are among the largest companies in the world by market capitalization with 7 of these companies – Apple, Amazon, Alphabet, Microsoft, Tencent, Alibaba and Facebook - being in the top ten.
39. They also bring powerful network effects – the term used to provide the utility of their customer base. Network effects were first studied with the telephone system and later fax machines, where the product is only as powerful as the number of people that use it. Facebook has over 2 billion members, giving it powerful network effects.
40. Neither of these two advantages can be subject to Canadian regulation, except perhaps in regards to concentration. However, there is a third competitive advantage that is critical to understand for the purposes of regulation – feedback effects.

Feedback Effects

41. The third advantage that is not as often discussed or studied is the most important for consideration as part of broadcasting regulation. This advantage is called the “feedback effect” and it occurs whenever a computer system uses feedback to learn. Specifically, this is the use of the data derived from anything from spelling correction, to audio commands to video plays that allows the data collector to improve their services.
42. In the broadcasting industry, feedback is critical for the development, production, distribution and monetization of content. The investments in original programming are enormous and very high risk. Information about the performance and audience of the content are of vital importance. It is therefore critical that broadcasters and creators have access to this information and that all platforms operating in Canada make it available.

43. The creation of content is not like other products. It cannot be easily tested before it is produced. Any performance metrics available to the content creator is helpful. It is well known that Netflix relies heavily on its data to determine its original production slate. At OUTtv we have found the data provided by our OTT service OUTtvGo invaluable for our development slate.
44. Not all data is equal. There is a difference between data around the viewership of a particular program and the level of details one has on the individual viewers. We can and should develop policies that consider all these factors.
45. It is critical that broadcasters have access to all key data relating to the viewing of programming, and basic audience information. This data is critical to the development and production of content, marketing of content and to revenue streams such as advertising and merchandising. Without it program makers take greater risk and miss potentially valuable revenue opportunities.
46. It is simply nonsensical that in Canada, where we invest public money in film and television production, that broadcasters and creators should be denied access to the information on program performance. Yet services like Netflix do not share information with producers of content. Some others do, but if one service gets away with it then the likelihood is that the refusal to share program performance data will eventually become the standard.

“So far, regulators have focused mostly on the scale and network effects and have yet to grasp the gravity of the threat to markets posed by the feedback effect. Services based on machine learning systems fueled by feedback data “buy” innovation at diminishing cost as the user base grows. It feels strangely alchemistic: turning a by-product of usage in the raw material of improvement, like converting lead into gold.”

Viktor Mayer-Schönberger,
Reinventing Capitalism in the Age of Big Data Pg. 166

Other related issues

47. There are other issues related to the technology that will need to be addressed and no doubt new ones will emerge. Two simple and real recent examples are good illustrations of the future.

De-monetizing LGBTQ content

48. Last year a very large technology company began de-monetizing LGBTQ content. The company is based in the US and it was rumoured that they were giving into pressure from advertisers who were being attacked by extremists when their ads appeared next to LGBTQ content. This incident happened in both the US and Canada. As most of this advertising is programmatic it was believed that the company simply changed their algorithm to avoid the issue. All of this took months to discover and for a correction to take place.

49. The company did finally admit they were wrong and apologized, but the lost revenue was never replaced. This US company operates unregulated in Canada. We have companies poised to enter from other countries like China as well. If this issue fell under Canadian regulations then the technology company would expect it as the price they pay for operating in Canada. They could tell the extremists to go talk to our Government. However, absent regulation, we become subject to the values of other countries, whether they conflict with ours or not.

Pay to Play

50. Another different but also relevant example is around marketing within a service. In our opinion, the CRTC is still behind in understanding the ability of BDUs to influence consumer decisions through marketing practices. However, what is coming in the near future is light years more advanced than the current broadcasting system.
51. OUTtvGo is carried on a number of technology platforms and is direct-to-consumer online. Our view is that the consumer decides on their platform first and their content second. We have noticed for the past year that we lagged considerably on one platform in comparison to its Canadian market share. It was a clear outlier in terms of market penetration.
52. We had several theories, but the prevailing one was that we had not signed up for their direct payment method. Instead, we relied on customers with their aggregation service to sign in and make payments through our website. This saved us the 30% commission the platforms take from the subscription fee. Furthermore, we had never marketed through their platform – something they encourage.
53. We decided to change both these approaches. We signed up for their payment system and then ran a marketing campaign through their marketing group. The resulting increases were dramatic. We have huge increase in subscriptions on this platform. The increase was in the thousands of percent. It was remarkable – or was it?
54. These companies have the ability to hide you from their customer base. They want to receive their share of subscription fees and they want you to pay for marketing with their team. We are happy with the results, but this example does raise serious long-term concerns. How do we control their revenue share? What if they decided to raise their commission to 50% or to 75%? What if the marketing dollars were set up so we just received enough subscribers to justify return on investment but no more – they imposed a cap? How would we know?
55. The emergence of these platforms is a new phenomenon and right now they are all on their best behaviour. Sadly, dealing with the all the technology companies is generally easier than working with the Canadian BDUs. However, all this could change in the future as one or two gain market dominance. History has shown that market dominance leads to abuse.
56. We have to prepare for this eventuality now. All of these are clearly economic issues that relate to the broadcasting system. The Commission needs the power to regulate economic issues and all of the above examples show why this is critical.

What we Need

57. The Canadian Broadcasting system can survive and potentially thrive if we work to restore competition. However, this requires an understanding of competition that is more complex and nuanced. It is not absolute and rejects the notion that market forces solve all problems. The following is a list of broader recommendations and considerations that we feel are critical to this process and the final outcome.

“Markets of any type must be actively shaped in order for knowledge to be governed in ways that produce the market outcomes that we as a society want. Indeed, regulation is not about interference, as commonly perceived, but about managing a process that produces the best results for society as a whole.”

Mariana Mazzucato, *The Value of Everything* p 221.

- A. Confirm up front that the broadcasting system has always been and remains a public good.
- B. Regulations should be based on principles, not complex rules.
- C. Regulations should promote competition because that promotes the diffusion of economic power and political freedom.
- D. Common carriage and Net Neutrality principles should be sacrosanct. Consider a ‘separations principle’ as advocated by Professor Tim Wu in *The Master Switch*.
- E. Vertical integration should face significant hurdles and, where possible, be prevented and undone.
- F. We need to understand that all concentrations of power are dangerous and have historically led to corruption. Where we can’t break up concentrations of power, we must monitor them and contain their effects.
- G. There is an overwhelming need to restore trust and transparency in the system. Data needs to be shared between the parties. Any other result will create a broken system.
- H. Access to the Canadian market is not a right, but a privilege. All parties need to play by the rules and contribute financially to the system.
- I. We must re-evaluate the role of competition law in relation to the broadcasting sector. Competition law should promote competition, but for too long it has allowed concentrations of power that prevent it, and slow innovation.

Independent Broadcasters

58. Market Access – for far too long Canadian Independent services have been denied access – or at least total access - to their own marketplace. The history is complicated but is time

for a reset. Capacity issues are no longer of concern to the system as technological improvements in computer storage, processing and bandwidth have progressed so far that it is no longer an issue.

59. Currently the BDUs control access but in the future it is conceivable – in fact probable – that we will be negotiating for access to most of our market through foreign technology giants. In the end, the vertically integrated services will be in the same position as independent services. We should make it a rule that all channel platform services must carry the licensed Canadian services approved by the CRTC. Why would we not maintain control of this?
60. Competition should be about pursuing audience, not about gaining access to the system or improving your position in the wholesale market.
61. Canadian Production Financing – the current system of Canadian financing is supported by payments made into the system primarily by the BDUs in exchange for their regulatory benefits. This system should gradually be replaced by payments made by the new virtual BDUs and the OTT services like Netflix, CBS All-Access and others – coming soon. The current Canadian Programming Expenditure system is effective, but simply must be supplemented by foreign market participants.
62. A base set of simple, standard commercial terms is needed. The current Wholesale Code is a good start, but it is impossible for Canadian broadcasters to negotiate on an even footing with foreign technology platforms. A baseline set of commercial terms needs to be available.
63. Transparency – data and other relevant information needs to be made available to programming services and to producers of content. It is critical to remain competitive, but it will also improve trust and confidence in economic relationships. To date, the technology platforms have been miles ahead of the traditional industry in this regard. The time is now to make it a fundamental principle of the system.

Own the Podium

64. At the time the current *Broadcasting Act* was created, there was very little film and television production in Canada, apart from our indigenous programs produced primarily by the CBC. Runaway production had just started in Vancouver, with shows like *MacGyver*, *21 Jump Street* and later *The X-Files* putting Canada on the production map. Since that time we have grown into one of the world's leading producers of content, with Vancouver and Toronto ranking as the 3rd and 4th biggest centres in the world.
65. A complex set of systems have developed over these past decades including funds like the CMF, tax credits both nationally and in many provincial jurisdictions and other programs. We have invested billions of dollars in building one of the world's most successful Industrial clusters. However, we could do better.
66. We urge the panel to recommend to the Government that we develop a program similar in mindset to the "Own the Podium" Olympic program. World content markets are

enormous. Canada is well positioned to be a major player and to build upon what we have already achieved. The broadcasting industry should be a springboard for this development and a cornerstone of our strategy.

Conclusion

67. OUTtv appreciates this opportunity to make this submission to the Panel, and we look forward to working with the Panel and other stakeholders to create a new legislative framework that serves the interests of Canadians and ensures that Canadian values, voices and stories will continue to be heard.

68. We would be happy to meet with the Panel to review this submission.

Yours truly,

OUTtv NETWORK INC.

Brad Danks, CEO

A large, handwritten signature in black ink, appearing to be 'Brad Danks', is written over the printed name and extends to the right.