TELEVISION ADVERTISING AND THE INCOME TAX ACT

AN ECONOMIC ANALYSIS OF BILL C-58

DRAFT REPORT

Prepared by Arthur Donner
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Mel Kliman

For the Department of
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Note. This report was prepared using information confidential to Canadian broadcasters and others. This information includes financial and operating statements filed annually with Statistics Canada by Canadian broadcasters, information acquired directly from Canadian broadcasters on a confidential basis, and proprietary reports and studies also acquired on a confidential basis.

To protect the confidentiality of these data, parts of this report have been deleted, but in a manner not to detract from the completeness of this report or the relevance of its findings.

ACKNOWLEDGEMENTS

We have been aided in the preparation of this report by a large number of people involved in all segments of Canadian television, both in the private and public sectors. Representatives of U.S. border stations also provided essential information. For their interest in our work and for their generosity in taking the time to prepare material and talk with us, we offer our sincere thanks.

TABLE OF CONTENTS

LIST OF TABLES

EXECUTIVE SUMMARY

Television Advertising and the Income Tax Act: An Economic Analysis of Bill C-58

This study assesses the financial impacts of Bill C-58 on Canadian and U.S. TV broadcasters. Bill C-58 was an amendment to the Canadian Income Tax Act which came into effect in January of 1976. It disallowed the treatment of advertising expenditures as deductible business expenses if the advertising is directed primarily to a Canadian audience but is placed in a foreign periodical or on a foreign broadcasting station. As it relates to television, the tax amendment was designed to bring Canadian advertising expenditures on border stations in the United States back to Canada in order to strengthen the financial position of the Canadian broadcasting industry.

An earlier study by Donner and Lazar Research Associates* concluded that in Canadian currency U.S. broadcasters lost $16.3 million in 1978 and $23.4 million in 1979 of net advertising revenue as a result of the tax amendment. It was assumed that the net revenue gains of Canadian broadcasters were of the same order of magnitude. But the broadcasting environment in Canada has changed considerably since that earlier assessment of Bill C-58 was completed. This study indicates that the use of simultaneous substitution by Canadian TV broadcasters has increased extensively since 1978, and that the combined effects of both Bill C-58 and simulcasting policies have powerfully improved the revenue position of both the newer and relatively established private TV broadcasters in Canada. This study estimates that both policies together increased Canadian net TV revenues by from $49.2 to $53.7 million in 1982, with Bill C-58 revenue gains ranging between $28.2 and $32.7 million. Simulcasting policies generated about $9 million of net revenues in 1975 and about $21 million in 1982.

The basic core of this conclusion can be found in the accompanying three tables of statistics. The estimates set out in Table A indicate that by 1982 the flow of net TV advertising revenues (in Canadian currency) to U.S. border markets had practically regained its former 1975 level. In 1975 the total flow of net Canadian revenues to U.S. border stations amounted to about $16.5 million in Canadian currency, whereas by 1982 the border leakage amounted to $15.2 million. However, in real terms (1975 Canadian dollars) the decline of net Canadian business on U.S. border stations amounted to about 50 percent between 1975 and 1982.

One can see the powerful impact of the changed policy environment in another respect. In 1975 the Buffalo TV broadcasters accounted for about 13.2 percent of Canadian TV advertising in Buffalo, Toronto and Hamilton. By 1982 their share of the local Canadian market had declined to 2.8 percent. Station KVOS in Bellingham has seen the local market share of Canadian net TV revenues decline from 36.2 percent in 1975 to 14.9 percent in 1982, while the Burlington/Plattsburg stations experienced a revenue erosion from 6.5 percent in 1975 to 2 percent by 1982.

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*Donner & Lazar Research Associates, An Examination Of The Financial Impacts Of Canada's 1976 Amendment To Section 19.1 Of The Income Tax Act (Bill C-58) on U.S. and Canadian TV Broadcasters, January 1979.

The figures in Table B indicate the potential U.S. revenue losses in 1982 due to the increased use of simulcasting and the impact of Bill C-58 since 1976. Our preferred estimates are found under columns a. Potential revenue estimates for 1982 were established on the basis of the market shares which existed in 1975 prior to the introduction of Bill C-58. The potential revenues and losses set out under columns b were calculated by projecting the growth of border TV Canadian revenues at the rate of increase of TV cost inflation in Canada. This latter method provides a somewhat lower estimate of potential revenues and potential border station losses, and is included in this table only for validation purposes. Using our preferred estimates, the three major U.S. markets which attracted Canadian advertising revenues in 1982 lost about $37.2 million relative to their potential in 1982 because of the increased use of simulcasting in Canada and because of Bill C-58.

The assumption was made that U.S. revenue losses translate into revenue gains for Canadian television broadcasters. The gains from Bill C-58 and simulcasting are set out in Table C. As noted above, according to our rough estimates, the tax advantages due to Bill C-58 generated from $28.2 million to $32.7 million of net revenues for Canadian television broadcasting in 1982. The requirement that cable systems carry out the simultaneous substitution of programs as requested by the broadcasters added a further $21 million of net advertising revenue that year. The combined effects of both policies amounted to 6-7 percent of total broadcasting revenues in Canada and 34-38 percent of the pre-tax profits of private stations. It is quite apparent that these two policy instruments have contributed substantially to the financial health of most Canadian TV broadcasters and, at the margin, to the survivability of a number of new stations founded in the 1970s.

Our aggregate estimates of revenue gains due to Bill C-58 ($28-33 million in net revenues in 1982) can be compared with rough estimates that some broadcasters provided to the authors in a series of interviews. Fifteen Canadian broadcasters indicated to us the amount by which their total revenues would be reduced if Bill C-58 were repealed and if nothing else were changed. Separately they predicted revenue losses ranging from zero to 25 percent. Applying their percentages to the Department of Communications statistics on actual advertising revenues for 1982, the aggregate amount of revenue lost by these 15 stations would have been $32.6 million in 1982. Since there are many more stations potentially affected by Bill C-58, this amount underestimates the broadcasters' views of the value of the policy. Thus their view of the importance of Bill C-58 for their industry is considerably higher than our own estimate of $28-33 million in 1982.

The remainder of the summary section describes the topics in the report which serve as background for the analysis. Section 2 discusses the importance of the 41 U.S. private TV border stations which reached Canadian population centres in the spring of 1983. The importance of cable TV penetration in Canada, as well as market fragmentation, are also discussed in this section. Section 3 considers the rationale for

protecting the Canadian TV broadcasting industry, and traces this need to Canadian content policies, to scale economy differences in program production costs between the U.S. and Canada, as well as to Canadian viewer preferences for U.S. produced programs. In the absence of any protection, Canada's broadcasting policy objectives could not be achieved and a larger share of Canadian advertising expenditure would flow to U.S. broadcasters. Private TV broadcasters in Canada have been quite profitable in recent years, a fact which complicates the case for protection but does not contradict it. The profit picture for private broadcasters is also reviewed in this section.

The various protective measures now in effect or which are being promoted are discussed in Section 4. Such measures include commercial deletion, simultaneous substitution, non-simultaneous substitution, the leapfrogging of signals and alternative tax measures. The role of simulcasting in diverting audiences and revenues to Canadian broadcasters is discussed at length in Section 5.

Section 6 outlines how Bill C-58 has changed the incentive to advertise on a border TV station. Aside from the obvious impact of nearly doubling the Canadian cost of advertising on a border station, the Bill also provides Canadian advertising agencies with a separate incentive to favour Canadian over U.S. stations. Offsetting these effects have been the reductions in advertising rates by the border stations.

Section 7 reviews the simple analytics of broadcast protection. The supply and demand theory helps explain why:

1) border stations will reduce their advertising rates, but not by the full amount of the tax in every case (it depends on the demand situation faced in each separate market);

2) some Canadian advertising will continue to flow to border stations;

3) advertising dollars will flow back to Canada; and

4) the prices of Canadian advertising will rise..

In section 8, the study sets out the results of a survey of 15 Canadian TV broadcasters vis-à-vis the impact of Bill C-58 and simulcasting on their own operations. The findings are summarized in the text and are compared to our own estimates in the study.

Section 9 reviews a survey of large Canadian advertisers undertaken for us by the Association of Canadian Advertisers. Based on a very limited response, it would appear that large national advertisers in Canada avoid using U.S. border stations, with the exception of station KVOS in Bellingham which is regarded as a necessary buy for the Vancouver/Victoria market.

Section 10 discusses how Bill C-58 is enforced by Revenue Canada. Section 11 outlines the various steps and assumptions used in arriving at the estimates of Canadian revenues flowing to border stations, and the separate effects of Bill C-58 and simulcasting on such flows. A compromise tax proposal promoted by several U.S. broadcasters is discussed in Section 12. While specific dollar estimates are not provided, the proposal appears to be a cumbersome and inequitable way to alter the policy environment.

A note of caution must be offered. As in the case of the original Donner and Lazar study, the statistics on flows of Canadian advertising to U.S. border stations were compiled from a variety of sources. They are rough approximations. While the authors attempted to maintain consistency, a series of important assumptions were necessary in order to make the projections and to disaggregate the U.S. border statistics into their various markets. We were able to check the validity of our assumptions through many interviews with people in the broadcasting industry.

Despite these considerations, the study confirms that Bill C-58 has substantially improved the financial wellbeing of private broadcasters in Canada. The effect of simulcasting is also substantial, though our calculations indicate that it may be less than that of Bill C-58.

Bill C-58 has benefitted both newer and older television stations, though in different ways. The newer stations gained in both price and volume terms, the older stations gained primarily by way of extra increases in advertising prices. Both old and new stations have been able to take advantage of simulcasting and it is difficult to make a case that the policy favours one group over another.

TABLE A

The Flow Of Canadian Net TV Advertising Revenues

To U.S. Border Markets, 1975 and 1982

(Millions of Canadian $'s)

	Estimated Revenues	
	1975	1982
Buffalo	7.1	4.7
Burlington/Plattsburg	2.2	1.8
Bellingham	5.0	7.3
Total Revenue - 3 U.S. Markets	14.3	13.8
Other Markets	2.2	1.4
Total	16.5	15.2
Total (1975 $'s)	16.5	8.0

*Inflation adjustment based on Canadian CPI.

TABLE B

Net Canadian TV Advertising Revenue Losses To U.S. Border Stations In 1982 Due To An Increase In Simulcasting and Bill C-58

(Millions of Canadian $'s)

	Estimated Revenues		Projected 1982 Revenues Based On		1982 Revenues Foregone Based on	
	1975	1982	(a)	(b)	(a)	(b)
Three Major Markets	14.3	13.8	45.4	33.9	31.6	20.1
Other Markets	2.2	1.4	7.0	5.2	5.6	3.8
Total	16.5	15.2	52.4	39.1	37.2	23.9
Total (1975 $)*	16.5	8.0	27.7	20.7	19.7	12.9

(a) Constant market share approach.

(b) Media cost increase approach.

* Inflation adjustment based on Canadian CPI.

TABLE C

Estimated Effects Of Simulcasting And Bill C-58 On Total Canadian Net TV Revenues In 1982

(Millions of Canadian $'s)

	Policy Impacts In 1975	Policy Impacts In 1982	Policy Impact Relative to 1982 Pre-Tax Profits	Policy Impact Relative to 1982 Total TV Revenues (Including CBC)
Simulcast Revenues	12	21	14.7%	2.7%
Bill C-58 Revenues	n.a.	28.2-32.7	19.7%-22.9%	3.6%-4.2%
Combined Policies	12	49.2-53.7	34.4%-37.6%	6.3%-6.9%

TELEVISION ADVERTISING AND THE INCOME TAX ACT: AN ECONOMIC ANALYSIS OF BILL C-58

1. Introduction

Bill C-58, an amendment to the Income Tax Act, was passed in 1975 and came into effect in January 1976. It disallowed the treatment of advertising expenditures as deductible business expenses if the advertising is directed primarily to a Canadian audience but is placed in a foreign periodical or on a foreign broadcasting station. As it relates to television, the tax amendment was designed to bring Canadian advertising expenditures on border stations in the United States back to Canada in order to strengthen the financial position of the Canadian broadcasting industry.

To understand the rationale for this policy and its impact it is necessary to consider a larger context that accounts for the Government's cultural objectives as they relate to television: the desire to have an indigenous broadcasting service that mirrors Canadian culture and supports Canadian talent. These objectives must be achieved within a powerful constraint that exists because of the taste for American television programming on the part of the majority of the population. Thus we have the classic contradiction of Canadian broadcasting policy, a CRTC requirement that Canadian TV stations have at least 60 percent Canadian content in their programming, while the cable companies, whose offerings are entirely regulated, carry American signals to improve the quality of their reception and to allow the American networks to be viewed in areas of the country that could not receive them off air. In such a context it is easy to view the support offered by Bill C-58 as desirable. It was intended to offset some of the burden placed on broadcasters by Canadian

content regulations and to help financially vulnerable stations. In the mid-1970's the CRTC had licensed several new independent stations in major markets in Alberta, British Columbia and Ontario and their prospects were not uniformly good. It was hoped that these additional outlets would increase the viewing of Canadian-produced programs. Bill C-58 was to enhance the probability that they and other Canadian stations would survive.

What follows is an evaluation of Bill C-58 in terms of how well it supports home-grown television. The report begins with a description of the U.S. border stations that compete with Canadian broadcasters. A fuller discussion of the rationale for some form of protection follows, including a description of the various forms of protection which are now used or which could be introduced. Because simultaneous program substitution interacts in an important way with Bill C-58 in providing protection from U.S. competition, its operation is discussed in a separate section. A detailed discussion of how Section 19.1 of the Income Tax Act affects advertisers' decisions in regard to television is then presented, followed by an analysis of the implications of the change in the Act in a supply-and-demand framework.

The above analysis provides the essential background for the sections of the report that deal directly with the financial results of Bill C-58. These sections consist of a discussion of the attitudes to the legislation of Canadian broadcasters and of advertisers, a description of how Canadian broadcasting has fared financially since the mid-1970's, and a set of estimates of the effects of Bill C-58 on advertising revenues.

2. U.S. Border Stations: The Source of Competition

According to a BBM survey, the signals of 41 private U.S. border television stations reached Canadian population centres in the Spring of 1983. Not all of those stations had a significant viewing presence in the Canadian market, nor did all of them earn Canadian revenues. Some of the stations are quite small. Prior to the introduction of cable television, relatively few border stations made significant penetrations into Canadian viewing markets. The Toronto market was the clear exception.

Most of the U.S. border markets are made up of affiliates of the three major networks and the educational network. In eastern Canada, stations in Bangor, Maine reach throughout the Maritime provinces, signals from Burlington, Vermont and Plattsburgh, New York are watched in Montreal and Quebec city, Rochester stations are carried on cable system in Ottawa/Hull, the Buffalo stations serve the large southern Ontario market and those in Detroit and Erie, Pennsylvania are watched in western Ontario. In western Canada, stations in North Dakota reach into Winnipeg, southern Manitoba and Saskatchewan. Spokane, Washington serves the Alberta cable systems and stations in Seattle and Bellingham, Washington are watched in the Vancouver area.

While the border stations originally established key Canadian markets by way of off-air reception, their recent expansion and the development of new markets has been by way of cable. In 1977 46 percent of Canadian households were connected to a cable system; in 1982 the number had grown to 58 percent. The Canadian Cable Television Association projects that 67 percent of households will have cable TV in 1990. Much

of this growth occurred because of the availability of U.S. stations on cable service. In 1970 U.S. stations in total had an 18.4 percent share of the English-speaking Canadian audience; in 1980 the share had grown to 24.5 percent.*

This increase in the American market share occurred during a period when some Canadian markets were being further fragmented due to the entry of new Canadian stations and when the protective policies discussed in this report were coming into effect. One can assume that the U.S. audience share would be bigger yet if it were not for these phenomena. It also means that the U.S. audience share has been geographically re-distributed in recent years. Significant audiences now exist in areas where off-air reception of U.S. signals was too inferior to allow markets to develop before cable companies brought the signals in. This has been offset by declining audience shares elsewhere. For instance, the audiences of all U.S. stations combined in the Toronto area declined from 43 percent in 1973 to 29 percent in 1981 and in Vancouver from 56% in 1970 to 43 percent in 1981.** In Edmonton the share grew from 7 percent in 1972 to 29 percent in 1981, in Winnipeg from 10 percent to 30 percent and in Halifax from 1 percent to 29 percent. More detail on the audience shares of border stations is provided in Table 1.

It is important to be aware of the sizes of markets in which U.S. stations operate, relative to the Canadian markets in which they compete for advertising. Because market size affects advertising rates,

*Paul Audley, Canada's Cultural Industries (Ottawa: Canadian Institute for Economic Policy, 1983), p. 266.

**The U.S. penetration data were provided to the authors from a special BBM tabulation in the summer of 1983.

Table 1

Cable Penetration and Average
Audience Share of U.S. Stations in
Major Canadian Markets, 1971 - 1981

CP = Cable Penetration (% of households)

AS = Percentage Share of Audience to U.S. stations

	1971		1973		1975		1977		1979		1981	
	CP	AS	CP	AS	CP	AS	CP	AS	CP	AS	CP	AS
Vancouver	67	56	75	53	84	55	87	46	86	41	86	43
Edmonton	na	na	38	14	63	24	66	24	68	27	81	29
Calgary	3	3	42	18	70	29	71	30	73	29	79	27
Winnipeg	27	9	42	11	68	27	73	30	77	35	79	30
Toronto	36	40	57	43	69	38	70	35	71	28	77	29
Ottawa	60	17	66	22	65	18	72	21	72	28	72	30
Montreal	22	9	27	9	34	13	41	13	44	14	51	16
Halifax	na	na	30	13	61	23	61	24	68	28	74	29

Source: BBM data provided to the authors, summer 1983.

Table 2

Locations of U.S. Stations Viewed in Selected
Canadian Cities and Their Metropolitan Populations (1,000's)

1981

Canada	Halifax	Montreal			Ottawa		Toronto/Hamilton		
Population	274	2718			728		3410		
U.S.	Bangor, Me.	Plattsburgh, N.Y., Burlington, Vt.			Rochester, N.Y.		Buffalo, N.Y.		
Population	85.1	82*		118	973		1226		
Canada	Winnipeg				Calgary	Edmonton	Vancouver		
Population	594				543	597	1158		
U.S.	Devils Lake, N.D.		Fargo, N.D.	Valley City, N.D.	Spokane, Wash.		Bellingham, Wash.		Seattle, Wash.
Population	13*		140	14*	351		111		1640

*Population of county in which city is contained

Sources: BBM data provided to the authors and Standard Rate and Data Services, Inc., Spot TV Rates and Data, June 15, 1983.

relative size is likely to determine whether border stations sell advertising in Canadian markets. Detroit is the largest of the U.S. border market, followed by Seattle and Buffalo. Most border U.S. markets are, however, relatively small in terms of the American broadcasting industry and are usually smaller than their Canadian counterparts. For example, in 1980 the Buffalo stations ranked 33rd among U.S. markets in revenue generation and 42nd in profit generation. Seattle ranked 17th and 14th in terms of revenue and profit.* Table 2 shows population sizes for major television markets in Canada and for the U.S. centres participating in those markets. The table indicates that, among large Canadian markets, only Ottawa and Vancouver have smaller potential viewing audiences than their American counterparts and, in the case of Vancouver, this is true only relative to Seattle, while Bellingham has a strong presence in the Vancouver market.

The distribution of air time sales in border markets is also of interest. Most border stations rely quite heavily on spot sales. For instance, as the figures in Table 3 indicate in 1980 spot sales in Buffalo accounted for 55.6 percent of revenues, a figure larger than average for a market with four or more stations. While the Canadian portions of spot TV sales cannot be broken out of the available data for all stations shown in Table 3, we were informed that for Buffalo in 1980 Canadian revenue accounted for 12-16 percent of their $24.8 million spot revenues (in U.S. currency).** The changes in proportions of local and national spot sales

*The U.S. publication, Broadcasting, periodically provides such data. For instance see Broadcasting, August 10, 1981.

**A Buffalo broadcaster indicated to us that most border stations agreed to report Canadian revenue as part of "national spot revenue" for purposes of consistent statistical reporting, though a small amount may be included in the "Local" category. (Interview with L.G. Arries, Jr., President, WIVB Buffalo, May 19, 1983).

Table 3

Distribution of Air Time Sales, Selected U.S. Television Markets

Market	Spot				Local				Network			
	1972	1975	1979	1980	1972	1975	1979	1980	1972	1975	1979	1980
Top 3 Markets												
New York	75.8	64.0	49.3	48.6	16.7	29.3	45.8	47.0	7.4	6.8	4.9	4.4
Los Angeles	61.7	59.0	47.3	48.6	33.7	36.5	49.5	48.4	4.6	4.6	3.2	3.0
Chicago	69.2	65.3	63.2	62.6	24.9	29.4	33.1	34.0	5.9	5.3	3.7	3.5
Buffalo and Equivalent Markets												
Buffalo	69.1	64.6	54.7	55.6	22.3	27.6	38.0	37.0	8.6	7.7	7.3	7.4
Cincinnati	48.9	43.8	41.6	42.9	38.2	45.6	51.5	50.6	12.9	10.6	6.9	6.4
Portland, Oregon	55.0	55.3	57.3	54.8	35.3	36.7	38.2	40.9	9.7	8.0	4.4	4.3
Providence, R.I.	53.0	48.5	51.0	51.1	33.3	37.9	35.5	36.1	13.7	13.6	13.5	12.8
San Diego	50.9	54.3	53.4	53.9	41.3	36.3	39.7	39.4	7.8	9.3	6.9	6.7
Rochester, N.Y.	45.8	45.1	49.5	47.5	39.7	43.0	43.0	45.2	14.5	11.9	7.5	7.3
Burlington-Plattsburg and Equivalent Markets												
Burlington-Plattsburg	50.4	50.0	50.3	na	26.5	29.5	33.6	na	23.1	20.5	16.0	na
Fargo/Valley City	29.1	29.5	35.7	36.5	50.4	54.2	53.1	52.4	20.5	16.3	11.2	11.1
Baton Rouge	22.7	25.5	30.8	34.9	63.4	62.6	59.1	54.6	13.9	11.9	10.1	10.5
Huntsville-Decatur	35.8	40.0	40.2	41.3	47.5	45.5	49.9	47.7	16.7	13.7	9.9	11.0
Johnson City	41.4	37.9	47.8	52.3	41.6	45.3	38.7	33.8	17.0	16.8	13.6	13.9
Erie Pennsylvania and Equivalent Markets												
Erie	29.6	27.9	27.0	29.2	48.8	52.1	56.8	53.0	21.5	20.0	16.2	17.9
Joplin, Mo.	31.2	31.4	40.7	41.8	41.2	44.1	38.7	38.3	27.6	24.5	20.8	19.9
Rochester, Minn.	29.7	34.0	39.9	39.2	46.9	45.8	45.6	44.9	23.4	20.2	14.5	15.9

Source: Donner & Lazar (1979) and Broadcasting, Sept. 2, 1974, Sept. 8, 1975, Aug. 2, 1976, Nov. 24, 1980.

Table 4

Profits to Revenue Ratio In Selected U.S. Markets

Market	Profits/Revenue (%) 1980	1979	1978	1975
Top 3 Markets				
New York	26.1	32.2	23.8	23.1
Los Angeles	28.3	32.5	28.8	17.2
Chicago	26.3	29.7	29.4	28.0
Buffalo and Equivalent Markets				
Buffalo	19.3	25.2	30.3	31.5
Cincinnati	31.1	36.0	32.8	25.9
Portland, Oregon	25.0	28.0	29.6	20.3
Providence, R.I.	11.2	23.7	28.7	25.4
San Diego	37.4	40.1	32.8	22.0
Rochester, N.Y.	-18.5	12.5	41.0	27.0
Burlington-Plattsburg and Equivalent Markets				
Burlington-Plattsburg	na	26.1	21.7	18.9
Fargo/Valley City	15.6	21.5	19.7	11.5
Baton Rouge	na	27.5	15.9	7.2
Huntsville-Decatur	-1.2	3.1	15.5	1.9
Johnson City	24.9	24.3	26.0	20.9
Erie Pennsylvania Equivalent Markets				
Erie	0.9	5.3	5.1	7.3
Joplin	na	18.2	18.7	14.0
Rochester, Minn.	5.0	26.5	24.8	19.0
Other U.S. Border Markets				
Bangor, Maine	10.5	12.8	8.8	
Fargo, N.D.	15.6	21.5	19.7	
Spokane, Wash.	37.6	38.3	na	
Seattle/Tacoma	38.0	41.7	na	

Source: Donner & Lazar (1979) and Broadcasting, Nov. 24, 1980, Aug. 10, 1981.

since 1975 for Buffalo are consistent with the expected impact of the Canadian policies being studied in this report. A drop in Canadian spot revenues apparently led to an increase in the importance of local advertising in the Buffalo area. The adjustment within the other border markets shown were less pronounced.

The data on profit ratios (pre-tax profits/broadcast revenues) shown in Table 4 are also consistent with the predicted effects of Bill C-58. Prior to the change in tax law (and to the introduction of other policies to be discussed below), the profit ratios for the Buffalo market and the Burlington-Plattsburgh market were considerably higher than those of similar U.S. markets. In Buffalo the ratio fell sharply after 1975. In Burlington-Plattsburgh the profit ratio rose after 1975 but no longer surpassed the ratio in similar markets to the extent it had before.

3. The Need for Protection

a) The Economics of Canadian TV Broadcasting: The desire to provide Canadian broadcasters with some measure of protection is based on the particular economics of Canadian television, combined with the Canadian content requirements. The cost of producing a television program of given quality in either Canada or the U.S. is bound to be similar. In the U.S., however, this fixed cost can potentially be spread over ten times more viewers than are available to Canadian exhibitors. The resulting economies of scale for program producers mean that, per unit of audience delivered, the cost of producing a television service is lower in the U.S. than it is in Canada and this lower cost means lower purchase prices for networks and TV stations. To complicate matters further, in many cases Canadian viewers prefer American programs, presumably, to a large degree, because the bigger audience allows U.S. producers to spend more and make better programs in the eyes of the viewer.

Having a lower cost per viewer, American producers are able to supply their offerings at attractive prices in the Canadian market. If pivately-owned Canadian broadcasters were allowed to program as they like, they would presumably buy more imported programming than they now do. Given the Canadian content regulations, they face the choice of spending large amounts on Canadian programs that will attract audiences big enough to cover their costs or else to lose viewers on their Canadian programming. Whichever choice is made, Canadian television stations have to charge more per unit of advertising than their American counterparts

simply to cover their programming and general overhead costs.*

This competitive disadvantage is made worse by the fact that the U.S. stations are generally not in similar situations. As already noted, in most cases Canadian stations compete with U.S. stations that operate in smaller markets. Such stations are likely to have lower costs for two reasons in addition to those already noted. First, local programming costs tend to be lower for stations in small centres: less may be provided, the manpower required to produce local programs is likely to be paid less, and the technical quality of production tends to be lower. Second, the cost of directly purchased programming, determined by negotiations between the station and program distributors, is likely to be lower than for Canadian stations in larger centres. While evidence on this is difficult to provide, it is conventionally believed that the prices paid for programming by U.S. border stations do not fully reflect the Canadian audiences that view them.** That is, if the negotiations on program purchase accurately accounted for all relevant facts, the border station would pay a price that reflects the size of its combined U.S. and Canadian audiences. This apparently does not happen. Local conditions tend, then, to increase the competitive advantage of the U.S. stations in many Canada-U.S. market pairs.

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*How this choice is made--whether to take the risk of spending large amounts to produce better Canadian programs or simply accept lower audiences for Canadian shows but make up the revenues by buying higher quality American programs--is an important but very complicated question that is not approached in this study. One aspect of it is, however, worth noting in the present context. Because the Canadian content requirements are defined in quantity terms they act as a special constraint on broadcasters who are capable of producing a few expensive programs that would attract large audiences. The 60 percent requirement means that funds are spread more thinly than they would be if broadcasters and program producers were able to decide on the quality-quantity trade-off more freely.

**An important exception to this hypothesis is the case of KVOS in Bellingham, Washington. Most of its viewers are in the Vancouver/Victoria market and the station apparently pays prices for its programs that reflect the size of its Canadian audience.

In sum, because of economies of scale to program production, the Canadian content requirements and particular conditions in local and regional markets, many U.S. border stations have the capacity to sell their product to Canadian advertisers at less than the cost of competing services in Canada, while still making a profit. In the absence of any protection, a larger share of Canadian advertising expenditure would flow to U.S. broadcasters; the amount and quality of Canadian television service would be less.

b) Industry Profitability: The argument that, in the absence of special measures, Canadian broadcasters would be at a competitive disadvantage, must be placed in perspective. It does not mean that the Canadian television industry is unprofitable. It is, on the contrary, highly profitable on average. Broadcasting is an industry to which entry is not free. A limited number of video channels are available and their assignment for use is restricted by the CRTC. Thus, because of the regulatory process, each broadcaster is granted a degree of market power in a particular area. Unlike some other regulated industries, the prices of TV services are not controlled with a view to preventing excess profits. Thus, as a working hypothesis, in either Canada or the U.S., one would expect rates of return on capital to be high, at least in centres where potential audiences are large. In the Canadian case, special measures have been taken to offset the competition from border stations and the inability of Canadian broadcasters to take full advantage of scale economies in program production.

The above hypothesis is supported by the data. A study using 1975 statistics reported an average rate of return on capital for 59

television corporations in excess of 30 percent per annum, well above rates of return in other industries that are subject to similar risk.* There is, however, considerable variance in the rates of return across broadcasters. Thus, any lessening of protection could mean an end to firms at or near the margin of profitability, even though some broadcasters might continue to earn high profits.

While high profit rates complicate the case for protection, they do not contradict it. The basic objective of protection is to support Canadian program production. The licensing of new outlets in the 1970's was viewed as contributing to this end. Without the extra revenue that has been generated by the Government's policies, some of these stations may not have survived. In regard to the more profitable stations, it is likely that some of the extra revenue has supported more or better Canadian program production in these cases as well. If some of it also happened to contribute to unusually high profits, that is a byproduct of the policies that might be remedied by other means (i.e., finding ways to channel abnormal profits into programming) but not something that eliminates the basic rationale for protection.

The recognition that television is a profitable industry focuses attention on the fact that the protective measures being discussed here are not of the sort upon which the very existence of an industry depends. The private Canadian television industry would not be wiped out if all forms of protection were removed. There is clearly a large audience for some kinds of Canadian programming (e.g., news, live Canadian sports) which

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*See S. McFadyen, C. Hoskins and D. Gillen, Canadian Broadcasting: Market Structure and Economic Performance (Montreal: Institute for Research in Public Policy, 1980), Chapter 8.

cannot be produced cheaply by U.S. stations. They have a competitive disadvantage for that kind of programming. Furthermore, American stations have only so much excess capacity to sell (though in the long run new stations could presumably be founded with a view to serving Canadian markets, as they have been in the past). But, despite these limits, there is considerable scope for competitive pricing on the part of the border stations. The most important evidence of this is that some advertising dollars have continued to flow to American stations since Bill C-58 and other protective measures appeared on the scene, even though they have reduced rates to compensate for the tax effect.

c) Property Rights and Sovereignty: The above arguments for protection, based on cultural policy and economics, are further supported by a legal argument based on the assumptions of sovereignty and property rights. The assignment of a video frequency, and the granting of the right to exploit it commercially, applies within national borders and not across them, at least in the absence of specific agreements to the contrary. Implicit in Canadian government action is the assumption that American broadcasters do not have the right to sell their service to Canadian advertisers in the same sense that Canadian broadcasters have. A related argument is the claim that the purchase of Canadian rights to a given program are exclusive. Canadian viewers served by the owner of such rights should not then be able to see the program when it is broadcast by American stations.

These arguments are more ambiguous than the preceding ones. The fact that the CRTC explicitly grants cable companies rights to distribute signals from U.S. stations would seem to be at odds with the claim to sovereignty over the use of broadcasting frequencies. In regard

to program rights, they are exclusive to the Canadian purchaser in principle, but there is a grey area in this principle caused by the realities of broadcasting. Programs are purchased in the knowledge of the spillover that occurs across the border in both directions. A program distributor interviewed for this study has claimed that, were effective exclusivity to be achieved, the negotiated prices of programs would surely be higher.

d) The American View: The border broacasters' position against Canadian protective measures appear to rest on two arguments.* First, Canadian protection, such as Bill C-58, is an unfair restraint of trade, discriminating against U.S. suppliers in the Canadian market for television services and, therefore, subject to retaliatory actions by the President and Congress under U.S. law governing international trade. Secondly, Canadian advertising expenditures have provided payment for a product that Canadians have been consuming since the early 1950's. To cut this payment substantially by government action is arbitrary and unjust.

While no attempt is made here to conclude which of the legal arguments for and against Bill C-58 are valid and which are not, the appropriateness of having some economic policy measures to support Canadian television is accepted. Canadian programming of high quality, in sufficient quantity to compete with the large volume of American television that is easily available, can be produced only if the flow of advertising revenue into the Canadian broadcasting industry is sustained at a high level. Just as the Canadian government has in the past supported transportation,

*See, for instance, the Statement of U.S. Border Broadcasting Licensees Before the Subcommittee on International Trade of the Committee on Finance of the U.S. Senate on S.2051, May 14, 1982.

manufacturing and other industries in order to foster Canadian products, it is legitimate to institute structural measures that help to direct the flow of Canadian advertising dollars into Canadian production rather than foreign production. Indeed in the case of the production of information, education, entertainment and cultural services, the case for protection is even stronger.

4. Forms of Protection

The protective measures now in effect flow out of a policy position taken by the CRTC in 1971.* At that time the Commission requested that the Government amend the Income Tax Act to remove deductibility of expenditures for advertising on stations not licensed in Canada. While Bill C-58 responded to this request in 1975, two other measures were initiated by the Commission: commercial deletion and program substitution.

The commercial deletion policy required cable companies to delete commercials on a random basis from programming imported on signals from American stations. The deleted commercial can be replaced by either a public service announcement, a Canadian commercial or simply a slide.

*CRTC, Policy Statement on Cable Television: Canadian Broadcasting 'A Single System', July 16, 1971.

The actual arrangements are worked out in an agreement between the cable company and the Canadian station affected, subject to the approval of the CRTC. The practice was first implemented in late 1972 in Calgary and by Rogers Cable Television in Toronto in 1973. The latter company stopped its deletion policy after it was challenged in the courts by a group of U.S. broadcasters. Eventually the Supreme Court of Canada upheld the legality of commercial deletion, but by that time the CRTC had agreed not to implement the policy in other areas, pending an evaluation of alternative measures.* This moratorium has continued to the present and, since Rogers Cable never recommenced its deletion program, the only place where it occurs is in Alberta.** Because of this, and because the number of commercials actually deleted is small, the effect of the policy on advertisers is thought to be small.***

Much more important is the CRTC's requirement that cable companies with more than 6000 subscribers accede to the request of a

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*CRTC Annual Report '76-'77, p. 9.

**Even there the policy applies haphazardly. In Calgary it is arranged so that the TV stations do not have to depend on the cooperation of the cable companies, since they are allowed to implement the deletions themselves. In Edmonton the cable companies were to carry out the deletions. One of the two companies providing service does not do so and has not been required to comply. Consequently half the city sees a commercial that is blotted out for the other half.

***One of our informants has indicated that stations in Spokane are now responding directly to the deletion policy. They will guarantee prime time exposure to Canadian advertisers by monitoring the random deletions and automatically providing a replacement spot for every one that is deleted. (Letter from B. D. Alloway, Sunwapta Broadcasting Ltd., July 7, 1983.)

broadcaster to substitute its signal for a foreign signal when the latter is carrying the identical program. (The floor was originally set at 3000 subscribers but was increased to 6000 in 1980.) Thus the Canadian station can sell advertising on the basis of the combined audience within Canada watching the two stations. Simultaneous substitution is now used extensively and is considered valuable by Canadian broadcasters. Its nature and impact are discussed more fully later in this report, though one issue is worth noting immediately. Because the use of simultaneous substitution as a marketing tool has gone through a period of development since the mid-1970's, its impact on broadcasting revenues is intertwined with those of Bill C-58. It is difficult to isolate the individual effects of the two policies on the performance of broadcasting enterprises, though an attempt is made later in this report.

An extension of the simultaneous substitution policy, non-simultaneous substitution, was also approved by the CRTC,* but has not been implemented. Substituting the Canadian version of a program even when it is not being run simultaneously would be valuable for broadcasters because it is impossible to simulcast every imported program. One reason is that a given Canadian station may purchase two programs which are run opposite each other on two U.S. networks. Difficulties are also created by differing approaches to scheduling across time zones in the two countries. In general, the schedules of Canadian stations are now heavily influenced by U.S. network scheduling. Non-simultaneous substitution would reduce this dependence and increase the ability of Canadian stations to keep the audience for which they have purchased program rights.

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*CRTC Annual Report '71-'72, p. 22.

To understand the complexity of non-simultaneous substitution, consider a given program that has been purchased by a Canadian station for playing at a time different from that of its American competitor. When it is played on the competing border station, the cable companies carrying that signal (or perhaps some sort of rebroadcast centre run by the cable companies and/or the television stations) would replace the U.S. transmission with a tape supplied by the Canadian station and containing its commercials. Various versions of the proposal have been put forward. One would have the substituted tape be the same program. The advantage of this is that the viewer is little affected -- only the commercials are different. The disadvantage is that the program producer and the performers are likely to count this as an extra "play", and charge for it. The effect of the policy would then depend on the relative market power of the purchasers and sellers of programs. The gains would be shared between the two and in some cases the program producer is likely to get a large share. Another version would have an entirely different program substituted.* Commercial time (though likely of lower value) would also be available on this program and at least a part of the Canadian audience that would have watched the U.S. show will presumably be diverted to the Canadian showing of it at a different time. The disadvantage of this approach is that the viewing audience is more likely to object strenuously.

The cable industry is strongly against non-simultaneous substitution, even if the broadcasters cover the technical costs, as required by the original CRTC policy statement. They fear that some cost is still

*One informant suggested that reruns of Canadian programs would be desirable. They would cost less and would be an additional way of fulfilling Canadian content objectives.

bound to fall on them. If nothing else, it may reduce the demand for their services, since greater choice in U.S. programming is one thing that they are selling. It is also likely that the broadcasters who say that they would be willing to cover technical costs are underestimating their magnitude. When one considers a market in which there are multiple stations and multiple cable companies all substituting at the same time, and not necessarily against the same border stations, it becomes clear that non-simultaneous substitution is likely to be costly and cumbersome.

A more manageable policy that has not been tried (except as a byproduct of other decisions) is the control of the sources of the signals distributed by cable companies so as to reduce competition from the U.S. Even where signals are available off-air, Canadians rely heavily on cable for television reception. As Table 1 indicates, the proportion of the potential market that is actually wired into the cable system is very high, 70-80 percent in many major markets. The signals delivered by most cable companies are typically those that happen to be close by, those that were available at lowest cost given the technology that existed when cable service began. While some extra cost is still involved, the ability to bring in more distant signals has certainly increased. Thus it would be possible to choose sources from U.S. advertising markets where prices are higher than in Canadian cities. The U.S. stations in those markets would find Canadian sales unattractive.

This option, sometimes referred to as "leapfrogging", occurs already in a few markets (in Vancouver, for instance, the U.S. network affiliates carried on cable are from Seattle, where prices are high enough so that little Canadian advertising is sold). The problems

associated with deliberately pairing each Canadian market with a higher-priced U.S. market are as follows:

1. There would be some resistance from the public, since some viewers will have developed loyalty to the local stations now watched. This could, however, be offset by viewer approval of the new stations, which would be from larger centres and would often offer higher quality local programming and overall signal production.

2. Where programming and technical production have improved, due to leapfrogging, some audience may be lost by Canadian stations to the new stations.

3. The question of who should bear the extra cost of bringing in distant signals has to be answered.

4. Since it may often be efficient to take the distant signals from a satellite distributor, the costs and political difficulties may be greater than expected. That is, unlike the case of off-air signals from the U.S., cable companies receiving signals from a satellite would have to pay for it. The jurisdiction of the U.S. government would also be different and, in the context of the border broadcasting dispute, this sort of change might elicit a response from Washington.

How some of these issues will affect the decision to use distant signals may soon be decided. At the time of writing of this report, the CRTC has before it a request from cable companies in Saskatchewan to replace the signals they now receive from stations in North Dakota with those carried on the CANCOM satellite from Detroit and Seattle. The cable companies simply wish to improve the quality of their transmission. If approved, however, it would also have the effect

of eliminating the competition of stations in North Dakota for broadcasters in Saskatchewan. At the hearings for this application held by the CRTC in Regina the major Canadian networks and the Canadian Association of Broadcasters argued against approval.* They are presumably concerned about point 2 above, but they especially stressed the worry that the practice would spread to other cable companies and would eventually give the stations in Detroit and Seattle that are providing the signals such a large Canadian audience that they could attract Canadian advertising. If this were to happen the "leapfrogging" argument set out above would no longer apply. That possibility can, however, simply be avoided by leapfrogging the signals from various U.S. cities and not allowing "super-border-stations" to develop.

Tax adjustments provide two variables that may be applied to different objectives. They raise revenue, which may be spent on progam-ming, and they have a disincentive effect on the activity to which they are applied. An example in the present context would be a tax on the importation of foreign produced programs, with the revenue from the tax channelled into the subsidization of Canadian programming. Canadian television programming would then be treated like many industries in the

*"CRTC faces dilemma of Service or Policy", The Globe and Mail, August 24, 1983, p. B1.

manufacturing sector which are protected by a tariff.

Such an alternative would be different from Bill C-58 in focussing more directly on program production. The funds that remain in Canada due to Bill C-58, rather than flowing to the border stations, either flow into general government revenue (i.e., this is the extra tax that is collected because expenditure on border station advertising that still occurs is not deductible) or into Canadian advertising. While some of the latter is likely to be used to support Canadian program production, it may also be profitable for Canadian broadcasters to use it to buy more expensive foreign programs or simply to increase profits directly. With the plan envisioned here, the application of funds would be more directed: first because of the direct subsidy and secondly because the effective price of imported foreign programs would rise relative to the cost of Canadian programs. It would become more desirable than it has been to increase the quality of Canadian programs. In fact the CRTC has recently announced a plan to reward quality production more directly.

There are of course inherent problems associated with alternative tax or subsidy plans. For example, unless the fiscal effects are extraordinarily large, the economics of the Canadian broadcasting business would still favour minimizing expenditures on Canadian production relative to less expensive imported programming. It is more than likely that even with new fiscal incentives to Canadian production, viewers in Canada will still favour U.S. programs over Canadian produced programs, and that such measures would hardly alter viewing patterns.

To make such a policy more attractive to Canadian broadcasters, it could be desirable to loosen Canadian content requirements. This

might reduce the quantity of Canadian production, but would allow resources to be shifted into higher quality production which could better compete with American programs. The overall thrust of the policy would be towards less control, a more positive type of support and more flexibility in the industry.

The federal Government has, of course, already taken a step in this direction by introducing a tax on cable services in its April 1983 budget, with the funds to be used to support program production. A tax on program importation would complement the cable tax. Its disincentive effect would work differently: the cable tax discourages the viewing of American stations via the cable system; the program import tax would discourage the presentation of foreign programs on Canadian stations. Both effects would thus help to support the demand for Canadian programming as the closest substitute for the taxed services.

5. The Importance of Simulcasting

As the preceding discussion suggests, simultaneous substitution is likely to be of considerable importance in terms of providing legislated protection for Canadian television. This section is concerned with evaluating that importance. Later in this report we present estimates of Canadian broadcasting revenues that occur due to simulcasting. These estimates require the adoption of some rather mechanistic assumptions, but it is possible to get an idea of the orders of magnitude involved from studies of audience diversions for particular stations.

In a rough way the effects of simulcasting can be seen in the way audience shares moved during the 1970's in markets where border stations had sizeable portions of the audience before program substitution began. For example, as already noted (see Table 1), the audience shares of Buffalo

stations in the Toronto viewing area declined between 1971 and 1982, despite the fact that cable penetration more than doubled during that period. Some of this decline is due to increased fragmentation of the market. The number of stations registering at least a 0.5 percent audience share increased from 10 in 1971 to 15 in 1981. But some of the increase is likely to be due to simulcasting. (Informants who commented on this question noted that there has been no deterioration in the quality of programs aired on the Buffalo stations since 1971.)

Studies that estimate the amount of audience gained by a station that simulcasts are available, and a special study of the experience of two stations was done for this report. Before turning to them, however, recognize that the standard measure of audience transfer is likely to have some error in it. It involves simply adding the audience estimated to be watching the simulcast program on the American station's cable channel to the Canadian station's audience at that time. As a measure of gain, there are two sources of error in this. First, when a Canadian station decides to simulcast, it loses the opportunity to pre-release or post-release the program for which it purchased Canadian rights. In the case of pre-release one would usually expect the Canadian station to have a larger audience than it gets through simultaneous release. Thus the simple addition of the border station's audience would overstate the actual audience gain.

The second source of error arises due to the way in which log-books are kept and reports prepared by BBM, the audience survey firm involved. Consider an example in which CHCH Hamilton broadcasts MASH at the same time as WGR Buffalo. A Canadian viewer contacted by BBM will

report one of the following three viewing preferences:

1. The viewer may be watching MASH on WGR, but because of simulcasting reports that he is watching it on CHCH, BBM allocates their viewing time to CHCH.

2. The viewer may be watching MASH on WGR and reports it that way, BBM allocates viewing time to CHCH.

3. The viewer may be watching MASH on CHCH and BBM allocates viewing time to CHCH.

In estimating the increased audience due to the transfer of audience from WGR to CHCH, there is no way of calculating the number of viewers in group 1 who misidentify that they are viewing a Canadian station when in fact they are viewing a U.S. station. Thus, due to this type of error, the survey would understate the audience gain.

These sources of error in audience estimates, plus difficulties in obtaining accurate information on the advertising rates that apply to particular programs, mean that estimates of the revenue contribution of simulcasting are approximate, though valid enough to provide some insight. The most useful studies available are those produced by Mediastats Inc., a firm that collects data on simultaneous substitution for the broadcasting industry. Mediastats revenue estimates are based on the audience diversions for each station studied, as reported in the periodic BBM surveys of U.S. television viewing in Canada. The total revenue for each simulcast program is obtained by using the spot advertising rates published by the stations in Canadian Advertising Rates and Data and some simple assumptions regarding capacity usage. (For more details, see the Mediastats report in Appendix 1.) This revenue is then multiplied by the percentage of the total audience

that is due to simulcasting in order to calculate the portion of the revenue due to simulcasting.

Such an estimate assumes that broadcasters are able to set their rates in a way that fully and proportionally reflects the audience diversions due to simulcasting. Since so much effort is put into acquiring audience information, there is no obvious reason to doubt that both seller and buyer in the advertising market are aware of the direct effects of simulcasting and take it into account in their decisions. Thus, if there is a bias in this type of revenue estimate, it is likely to be downwards, because it does not take into account the interactions between the values of simulcast programs and programs that are not simulcast. Spots on simulcast programs are typically sold in packages with spots on programs that have smaller audiences. Thus, some of the revenue attributed to the latter programs by this estimation method is actually attributable to simulcasting.

With these observations in mind, we set out a synopsis of five studies of simulcasting, three from Mediastats Inc., and two from the CBC.

a) Mediastats Study for the Canadian Cable Television Association, March 1981: This is the most comprehensive report available, since it provides audience diversions for all English language stations that requested simulcasting in the Spring of 1979 and the Fall of 1980. (Some simulcasting is done by French language stations as well, but it is across stations within Canada and, therefore, not relevant in the present context.) The average audience diversions by station reported in the study is reproduced in Table 5. It indicates that simulcasting is far more important for CTV and independent stations than it is for the CBC and

its affiliates. On average, 3.6 percent of the total hours tuned to the 15 CTV affiliates were attributed to simulcasting. The corresponding number for independent stations was 8.5 percent. For CBC stations, those operated by the CBC and affiliated stations taken together, it was 1.0 percent. Of the 10 million hours of tuning attributed to simulcasting in total in 1980, the CBC accounts for only 5.9 percent. Note, however, that Canadian content regulations imposed upon the CBC are more stringent than those imposed upon the private broadcasters. Consequently their opportunities for simulcasting are more constrained.

Table 5 also indicates that there was considerable growth in the contribution of simulcasting between 1979 and 1980. For all stations combined the simulcast audience grew by 44 percent between the two surveys.

Table 6 uses the method described above to assign dollar values to simulcasting in 1980, based on surveys in Fall of that year. Of the 41 stations covered in Table 5, 34 are included in Table 6. Those excluded were omitted either because their simulcasting was against other Canadian stations or because of other technical reasons associated with very low levels of simulcasting. It follows that the figures shown in Table 6 cover virtually all the simulcasting against U.S. stations in Canada for the sample period. Thus, for 1980, $20 million provides a rough estimate of the whole industry's annual gain from simulcasting.

(b) Mediastats Inc., Specially Commissioned Study, July 1983: In this specially commissioned short report (reproduced in Appendix 1) the values of simulcasting for CFTO Toronto and CHCH Hamilton based on Spring 1983 data have been estimated. Based on the Spring schedule, the study estimates that simulcasting yielded CFTO approximately $2.6 million on an

Table 5

COMPARISON OF SIMULCAST AUDIENCE AS A PERCENT OF TOTAL HOURS OF TUNING FOR ENGLISH TV STATIONS REQUESTING SUBSTITUTIONS

STATION	FALL 1980 ALL PERSONS 2+ TOT HRS TUNED (000)	FALL 1980 TOTAL SIMULCST HOURS (000)	FALL 1980 SIMULCST HRS AS % TOTAL HOURS	SPRING 1979 ALL PERSONS 2+ TOT HRS TUNED (000)	SPRING 1979 TOTAL SIMULCST HOURS (000)	SPRING 1979 SIMULCST HRS AS % TOTAL HOURS
CBC O & O						
CBLT, Toronto	11,112	139	1.2	12,618	282	2.2
CBMT, Montreal	6,020	58	1.0	5,796	81	1.4
CBOT, Ottawa	3,503	32	0.9	3,277	35	1.1
CBUT, Vancouver	6,352	44	0.7	6,539	151	2.3
CBXT, Edmonton	4,789	2	-	4,478	*	
TOTAL	31,776	275	0.9	32,708	549	1.7
CBC AFFILIATES						
CFPL-TV, London	5,575	109	2.0	5,824	138	2.4
CHEC-TV+, Kelowna/Kamlp	2,513	13	0.5	2,542	16	0.6
CHEK-TV, Victoria#	3,210	57	1.8	3,550	96	2.7
CHEX-TV, Peterborough	2,416	23	1.0	2,193	47	2.1
CJIC-TV, Sault Ste Marie	412	5	1.2	530	13	2.5
CKNX-TV, Wingham	1,977	18	0.9	2,171	20	0.9
CKPG-TV, Prince George	778	10	1.3	812	4	0.5
CKPR-TV, Thunder Bay	1,018	6	0.6	1,152	10	0.9
CKRD-TV, Red Deer	1,064	16	1.5	1,145	10	0.9
CKVR-TV, Barrie	4,910	21	0.4	4,680	45	1.0
CKWS-TV, Kingston	1,505	25	1.7	1,722	37	2.1
CKBI-TV, Prince Albert	1,555	13	0.8	1,471	*	
CKNC-TV+, N Bay/Sud/Tim	2,943	23	0.8	6,075	*	
TOTAL	29,376	339	1.1	33,867	436	1.3
CTV						
ATV, Maritimes	18,989	344	1.8	19,134	138	0.7
CFCF-TV, Montreal	16,066	509	3.2	15,286	378	2.5
CFCN-TV, Cal/Leth/M Hat	7,765	181	2.3	6,291	75	1.2
CFQC-TV, Saskatoon	4,510	36	0.8	4,541	24	0.5
CFRN-TV, Edmonton	8,766	127	1.4	8,298	75	0.9
CFTO-TV, Toronto	17,612	926	5.3	15,646	748	4.8
CHAN-TV, Vancouver	14,069	928	6.6	13,364	832	6.2
CHFD-TV, Thunder Bay	680	46	6.8	1,054	33	3.1
CICI-TV+, N Bay/Sud/Tim	3,375	179	4.6	4,331	81	1.9
CJOH-TV, Ottawa	9,052	415	4.6	9,076	430	4.7
CJON-TV, St. John's	5,572	78	1.4	5,099	16	0.3

* No programs were requested to be substituted during survey period.

\# Was an affiliate during the survey time, now is a CTV station.

(Table 5, Cont.)

COMPARISON OF SIMULCAST AUDIENCE
AS A PERCENT OF
TOTAL HOURS OF TUNING
FOR ENGLISH TV STATIONS REQUESTING SUBSTITUTIONS

STATION	FALL 1980 ALL PERSONS 2+ TOT HRS TUNED (000)	FALL 1980 TOTAL SIMULCST HOURS (000)	FALL 1980 SIMULCST HRS AS % TOTAL HOURS	SPRING 1979 ALL PERSONS 2+ TOT HRS TUNED (000)	SPRING 1979 TOTAL SIMULCST HOURS (000)	SPRING 1979 SIMULCST HRS AS % TOTAL HOURS
CTV continued						
CKCK-TV, Regina/M Jaw	4,487	60	1.3	4,668	43	0.9
CKCO-TV, Kitchener	8,837	482	5.5	8,853	477	5.4
CKCY-TV, Sault Ste Marie	407	41	10.1	338	35	10.4
CKY-TV, Winnipeg	6,976	233	3.3	7,626	133	1.7
TOTAL	127,663	4,585	3.6	123,605	3,518	2.8
INDEPENDENT						
CFAC-TV, Cal/Leth	4,067	47	1.2	3,096	18	0.6
CFMT-TV, Toronto	1,257	27	2.1	*		
CHCH-TV, Hamilton	13,294	990	7.4	14,695	875	6.0
CITV-TV, Edmonton	5,505	87	1.6	4,025	-	
CITY-TV, Toronto	8,232	1,002	12.2	5,418	533	9.8
CKGN-TV, Global Ntwk	17,735	1,712	9.7	14,284	392	2.7
CKND-TV, Winnipeg	5,553	140	2.5	4,505	153	3.4
CKVU-TV, Vancouver	4,910	1,163	23.7	3,880	733	18.9
TOTAL	60,553	5,168	8.5	49,903	2,704	5.4
TOTAL ALL STATIONS	249,868	10,367	4.1	240,083	7,207	3.0

* Was not on the air at this time.
- Did not ask for substitution during survey period.

SOURCE: BBM Bureau of Measurement Reach Report and Report on Estimated TV Audiences transferred by cable substitution, Spring 1979 and Fall 1980.

Table 6

Potential Value of Simulcast

Programs - Yearly Basis, 1980

STATION	TOTAL $	SIMULCAST PORTION $
CJON	2,471,100	139,836
ATV	4,593,600	351,708
CFCF	8,446,500	1,002,852
CJOH	4,533,300	414,216
CFTO	7,265,100	1,440,204
CKCO	3,842,400	688,692
CICC+	744,000	139,740
CKCY	851,700	268,032
CHFD	357,000	113,640
CKY	4,053,000	416,568
CKCK	2,106,000	133,284
CFQC	2,032,500	63,960
CFCN	4,905,000	510,252
CFRN	1,739,400	141,600
CHAN	5,553,000	1,699,080
CBLT	681,000	163,200
CBMT	294,000	83,580
CBOT	222,000	46,740
CKWS	234,000	24,660
CHEX	144,000	12,924
CKGN	11,646,000	4,172,972
CHCH	6,840,000	1,639,620
CITY	2,706,720	948,216
CFPL	306,600	55,632
CKNC+	126,000	37,776
CJIC	27,900	11,364
CKPR	88,800	17,616
CBXT	32,400	5,472
CKND	2,550,000	327,288
CFAC	1,152,000	203,568
CITV	1,374,000	189,816
CHBC/CFJC	105,000	21,324
CBUT	252,000	67,548
CKVU	6,900,000	4,442,604
TOTAL	89,176,020	19,995,584

Based on Canadian Advertising Rates & Data, December 1980 and BBM Fall 1980 Report on Estimated TV Audiences Transferred by Cable substitution and BBM Fall 1980 TV Market Reports.

Five, 30 second commercials per quarter hour were assumed and the audience data over the three-week survey period was multiplied by 12 for a yearly estimate.

annualized basis, approximately 5.8 percent of estimated annual revenue. This amount represented 18.3 percent of the revenue of the programs that were simulcast. For CHCH the equivalent annual gain due to simulcasting was 4.5 million, representing 11 percent of total estimated revenues and 29.1 percent of the revenue value of the programs simulcast.

(c) Mediastats Inc., Study prepared for the Canadian Cable Television Association, March 1978: In this case Mediastats reviewed the amount of simulcasting done by CFTO Toronto, the Atlantic Television System in the Maritimes, and CKVU in Vancouver in 1977. According to their estimates, the ATV Maritime network earned on an annual basis approximately $159,000 of additional revenue in 1977 because of simulcasting. In the CKVU Vancouver case, the additional revenues exceeded $5 million. Due to time differences between regions in Canada, there is less opportunity to take advantage of simulcasting in the Maritimes than there is in Ontario and Vancouver where prime time schedules on U.S. and Canadian stations more easily coincide (though the lower revenue contribution in the Maritimes will also be due merely to the smaller size of its market). CFTO in Toronto earned about $1.5 million from simulcasting based on the fall 1977 schedule.

The importance of these transferred revenues to the individual stations was calculated by estimating a total advertising revenue figure for each of the same three stations. Simulcasting revenues amounted in 1977 to about 1 percent of ATV advertising revenues, 7.1 percent of CFTO's revenues, and 38 percent of CKVU's revenues in the fall of 1977.

(Proprietary information deleted.)

(Proprietary information deleted.)

6. The Effect of Bill C-58 on Advertising Cost

While the arithmetic of Bill C-58 is straightforward, it should be reviewed here in order to facilitate further discussion. Most corporations in Canada face a marginal tax rate of 46 percent. (Those with taxable profits less than $150,000 pay only 25 percent. Since firms that advertise on television are likely to be large, our analysis is based on the 46 percent rate. This introduces an upward bias in the examples that follow, but it is likely to be small.) Thus when expenditure on non-deductible advertising is compared with deductible advertising, if the rates are the same the after-tax cost of the former will be almost double the latter.

Consider an example in which a firm has gross income of $100,000 and plans to buy $10,000 worth of advertising. In Example A all of it is spent on Canadian media. Because the firm's taxable income is reduced by $10,000 the net cost of the advertising to the firm is $5,400. In Example B $2,000 is spent on U.S. media; the tax saving is $920 less and the net cost of advertising is $920 more. In such a case, if the firm can find $2,000 of Canadian advertising with approximately the same impact it will surely buy it instead. Alternatively it might reduce its total purchase of advertising, assuming the original decision was made on the basis of the $5,400 net expenditure. Speculating on such alternatives quickly becomes intractable, however, because one would assume that the original $100,000 of pre-advertising gross income depends on the volume of publicity bought.

	Example A		Example B	
Gross Income	$100,000		$100,000	
Payments to Media	10,000	(deductible)	8,000	(deductible)
			2,000	(non-deductible)
Net Taxable Income	90,000		92,000	
Tax Payable	41,400		42,320	
Net Income	48,600		47,680	
Net Cost of Advertising	5,400		6,320	

The important possibility to consider is that the border stations will have reduced their rates to compensate for the tax effect. In the example, the U.S. television station involved would have to sell the spots it formerly sold for $2,000 Canadian for $1,080, reducing its price by 46 percent. While hard price data are not available, it is widely known that border stations did decrease their rates. Suppose for the moment that the full 46 percent reduction was made in the typical case. Theoretically one might expect that the advertisers would be ready to buy spots on border stations to the same extent as before the enactment of Bill C-58. For two reasons this is not likely to have happened.

First, advertisers are sensitive to government policy. Numerous informants made it clear that the passing of Bill C-58 told Canadian corporations in dramatic fashion that it was desirable to support Canadian broadcasting and that this has had an effect on their decisions. Advertising on American stations when Canadian substitutes are easily available is looked upon as bad corporate citizenship. We even encountered a few bits of anecdotal evidence that "delinquent" corporations have been approached by people in the broadcasting industry and asked to account for their bad behavior. While this kind of persuasion, explicit or implicit, has not totally deterred advertisers from spending on U.S. stations, we believe it has had some impact.

This effect, due to the corporate desire for good public relations, is reinforced by the nature of many television advertising markets, where the coverage of the audience by U.S. stations is lower than that of Canadian stations. In these markets it is more efficient to buy spots on Canadian stations. In metropolitan Toronto, for instance, (based on data for 1981) CFTO, CBLT, CHCH, CITY and CKGN all have higher average audience shares than the three network and one independent station from Buffalo. In Winnipeg in 1981 CKY, CBWT and CKND respectively had 26, 17 and 25 percent of the audience on average while the three American commercial stations had 12, 9 and 7 percent. These kinds of differences are enough to make media buyers look to Canadian stations first and they make it easier for corporate advertisers to have their "Buy Canadian" preferences satisfied.

That the preceding argument enters into the behavior of advertising agencies is borne out by a memorandum on the purchase of U.S. advertising written by a Toronto advertising agency for one of its clients. This excerpt is relevant:

> ...with some exceptions in the Maritimes and the Niagara Peninsula and Vancouver/Victoria, the numbers of hours tuned to a U.S. station are considerably less than those tuned to a Canadian station. Most U.S. stations will reach 35 percent of market viewers, who will watch about 3.5 hours per week on that station. A typical Canadian station, on the other hand, will reach about 85 percent of a market's viewers, and those people will spend about 8.5 hours per week with the Canadian station... In most markets, because more people tune to Canadian stations for a longer period of time, we have a much greater probability of reaching the target audience. Since most schedules call for a 50 percent reach into the target audience, we find that Canadian

> stations will achieve all schedule delivery requirements. It simply has been unnecessary to buy U.S. stations to achieve advertising goals.*

This kind of reasoning indicates why an American informant claimed that stations on the Canadian side were always "first choice", with border stations taking the residual demand for advertising.

Bill C-58 introduced a second incentive, in addition to good corporate citizenship, for searching for available capacity on Canadian stations and avoiding U.S. purchases. It exists because advertising agencies generally earn their fees as 15 percent of the advertising expenditures of the client. The tax cost of buying time on U.S. stations will be included in the advertiser's budget, but not in the expenditure that flows through its agency. Thus one would expect agencies to prefer to place their business on Canadian media.

To illustrate this, consider again Examples A and B set out above but suppose now that U.S. border stations have reduced their rates for Canadian clients by 46 percent to compensate for tax losses. The package of advertising assumed under example B ($8,000 in Canada, $2,000 in the U.S.) could now be bought for a net cost of $5,400, as under Example A. I.e., the expenditures would break down as follows:

Advertising on Canadian stations:	$8,000
Advertising on U.S. stations:	1,080
Payments to advertising agency:	9,080
Tax saving (= 0.46 x 8000)	- 3,680
Net cost of advertising	$5,400

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*Hayhurst Advertising Ltd., Television Buying on U.S. Stations, May 1983 (mimeo).

But the agency commission would be less than before. On $10,000 of advertising it would be $1,500; on the same volume of advertising newly priced at $9,080, the agency commission would be $1,362. On the $2,000 that was switched, the fee falls from $300 to $162. That is, other things equal, a gross advertising expenditure on a Canadian station yields almost twice the fee that it would on an American station.

When we sought the opinion of advertisers on the potential role of this fee differential, some were skeptical. These argued that an advertising agency is most concerned about delivering the best package it can to its client, so as to assure continuity of its accounts. Since only a portion of any given budget, sometimes a very small portion, will go to border stations anyway, the agency will not jeopardize long-term profits by passing up good buys, simply to escape the fee differential we have identified. Such an argument no doubt applies in circumstances where the available spots on U.S. stations are clearly better than those on Canadian stations. But there are bound to be many instances in which similar impact can be obtained by buying on either side of the border. In these cases we believe the fee differential will play a role, though the motivation for choosing the Canadian purchase may well be described otherwise. The important point to see is that, due to the way agency fees are paid, an incentive exists that helps to achieve the objectives of Bill C-58.

7. The Simple Analytics of Broadcasting Protection

In the preceding discussion we have supposed that the border TV stations dropped their prices in order to compensate for the effect of Bill C-58. While this is plausible, the price adjustments were likely more complicated. A reduction in U.S. advertising rates to maintain competitiveness in such a situation is certainly to be expected, but it need not be so large as to offset the total value of the tax deduction. Further, one would expect Canadian advertising rates to change as well. Simultaneous substitution would also influence Canadian and American rates, as would the attempts of corporate advertisers to be 'good Canadian citizens'. We attempt now to clarify these expected price changes and to consider their likely effects.

While the border broadcasting dispute does not correspond exactly to the classic supply-demand model of economic theory, it is a highly competitive market and the traditional theory can tell us something of what to expect. Suppose for the moment that a simple unit of homogeneous TV advertising time exists, that its price in a Canadian television market is determined by the normally-sloped demand and supply curves D_1^c and S_1^c in Figure 1a, and that its price in the corresponding border station market for Canadian advertising is determined by the curves D_1^u and S_1^u in figure 1b. Initially, then, the price of a spot on a Canadian station will be P_1^c and on a U.S. station P_1^u. (Assume that the exchange rate is given and that both prices are measured in Canadian dollars.)

Suppose that advertisers are working with total TV budgets that are fixed, at least in the sense that any change in the market situation will not cause them to decrease their total advertising expenditure. In

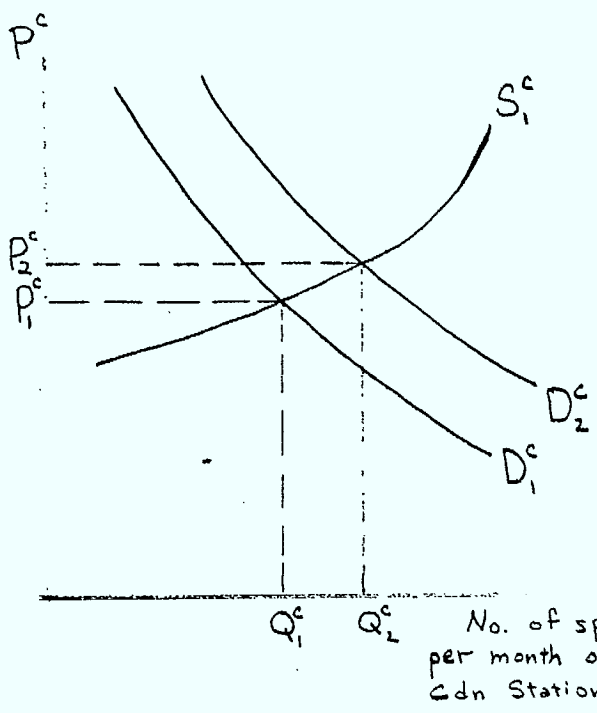

Figure 1a

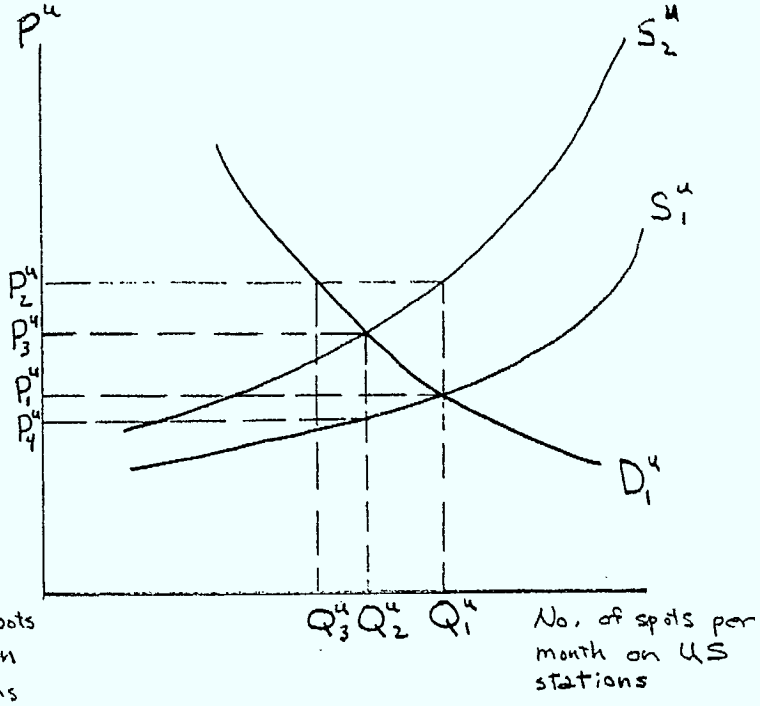

Figure 1b

simple terms, if a dollar is not spent on advertising in the U.S., it will be spent in Canada. On the other hand, suppose that at least some firms will tolerate an increase in their budgets due to tax effects.

Under these assumptions, the effect of Bill C-58 is analogous to the imposition of an excise tax on U.S. advertising but not on Canadian advertising. For any given price, Canadians would have to pay it, plus 46 percent times the price, if they still want to purchase a unit of advertising. This can be represented by a shift upward along the price-axis of the supply curve, from S^u_1 to S^u_2. The shift is not parallel because the absolute tax effect is larger the higher is the price. At the original U.S. price, P^u_1, the effective price P^u_2 now applies. At that price the

quantity of advertising demanded by Canadians in the U.S. drops off drastically to Q_3^u. With excess capacity border stations begin to drop their prices and the decrease in the quantity demanded is less, the equilibrium quantity falling only to Q_2^u.

Meanwhile, on the Canadian side the demand curve will have shifted out, from D_1^c to D_2^c, as the decline in border station demand moves to Canadian stations. Assuming that capacity is available, more spots will be purchased. But competition for them will push up their prices. This higher price helps to keep some advertisers on the American side.

Eventually substitution between markets will bring the adjustment to an end and the new equilibrium prices and quantities will prevail. In Canada more advertising will be done, Q_2^c instead of Q_1^c and at a higher price, P_2^c instead of P_1^c. Bill C-58 has helped the Canadian broadcaster not only by bringing home $(Q_2^c - Q_1^c) \times P_2^c$ dollars, but also because advertisers that were already buying Canadian spots will pay more for them, to an amount totalling $(P_2^c - P_1^c) \times Q_1^c$ dollars.

In the U.S. the price received by the TV station has fallen from P_1^u to P_4^u, but the effective price paid by Canadian advertisers has risen from P_1^u to P_3^u. A smaller number of spots is bought. The revenue lost by the border stations is $(Q_1^u - Q_2^u) \times P_1^u$ per time period due to the smaller volume of advertising bought, plus $(P_1^u - P_4^u) \times Q_2^u$ due to the lower price paid to the broadcaster for what still is bought.

The idea that Bill C-58 put downward pressure on border station advertising rates and upward pressure on Canadian advertising rates is easy to accept. The interesting question is how much both sets of prices were likely to move. The conventional view in the broadcasting industry

is that border stations dropped their rates by the full amount of the tax. On the other hand, few broadcasters call attention to higher domestic prices resulting from Bill C-58. Are these plausible views? If supply-and-demand analysis is applied to the question, the answer depends on what one believes about the shapes of the curves in each market. For instance, if one believes that the supply curve for Canadian spots is very flat, it is then plausible to argue that no increase in Canadian rates took place.

There is every reason to believe that the demand for advertising of a specific type is price-elastic, but not infinitely so. That is, one expects the demand curves in Figure 1 to be negatively-sloped, but neither vertical nor horizontal. The reason is that any particular type of television spot has desirable attributes for at least some advertisers, but there are, on the other hand, likely to be close substitutes for it in the case of many other advertisers. For example, if the price of television spots rise, some advertisers are likely to shift dollars from TV to print media. Others, going for a particular audience that can be more efficiently reached via television, will simply absorb the higher price. Such arguments regarding substitution due to price changes apply plausibly to the choice between Canadian and border TV stations represented in our two diagrams. When the U.S. price is increased, many Canadian buyers are likely to switch to Canadian stations immediately. Others who are working on a target audience to which the border stations are well suited will pay the higher price. For example, in the Toronto market the Buffalo stations are important in reaching children; in Manitoba beer and wine ads are not allowed on Canadian stations before 10 p.m. In sum, it is reasonable to argue that demand curves with negative slopes of intermediate magnitudes apply to the problem at hand.

With regard to supply curves it is useful to think of the individual TV station. Operating in a purely competitive environment, one would expect the individual broadcaster to have a supply curve of the sort shown in Figure 2. Before all available spots of a given type are sold, the marginal cost of an additional one is low and constant. At some point close to full capacity (Q_1) the marginal cost might rise slightly (e.g., due to staffing costs associated with tight scheduling), and at full capacity (Q_2), a level determined by government regulation on the maximum number of minutes of commercials per hour, the curve becomes vertical because no more spots of this type are available.

The actual broadcast industry is not purely competitive, but some aspects of it appear to be very competitive, involving processes that cause prices to adjust in response to changes in demand and supply. The interaction between media buyers in advertising agencies and station

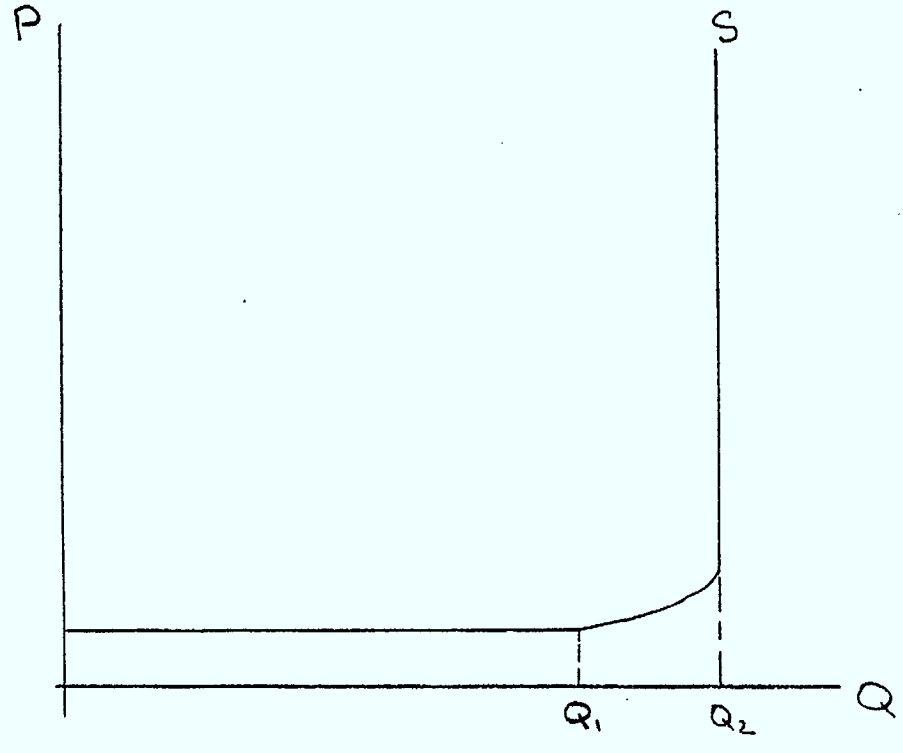

Figure 2

representatives facilitates a flow of information and an adjustment of the terms of sale that appears analogous to the market clearing functions performed by brokers and traders in share or currency markets. The phenomenon is more complicated because different units of advertising are differentiated products that are typically sold in packages. Thus sometimes the price of a constant product might adjust; other times the price is held constant and the content of the package changes through negotiation. Either way some competitive adjustments occur.

An announced price that is above marginal cost and reflects some degree of market power may, on the other hand, be typical for some TV stations, or for certain parts of the sales of all TV stations. The power to maintain somewhat higher prices would be based on the limit on the number of channels in any given market and the particular attractions of the programming that a station is able to put together. If the population base in a market is large and general economic conditions are good, the power of a station to set prices above marginal cost will be greater because it will be difficult for media buyers always to deliver the package the advertiser wants in an efficient way. Such a situation is likely to mean that the price at which stations will provide spots is more demand determined; as demand rises or falls the profit maximizing broadcaster will periodically change his price. While this is not the same as saying that a supply curve consistent with pure competition exists, it does result in a "supply relationship" that is similar. Consider

Figure 3 to see the argument.*

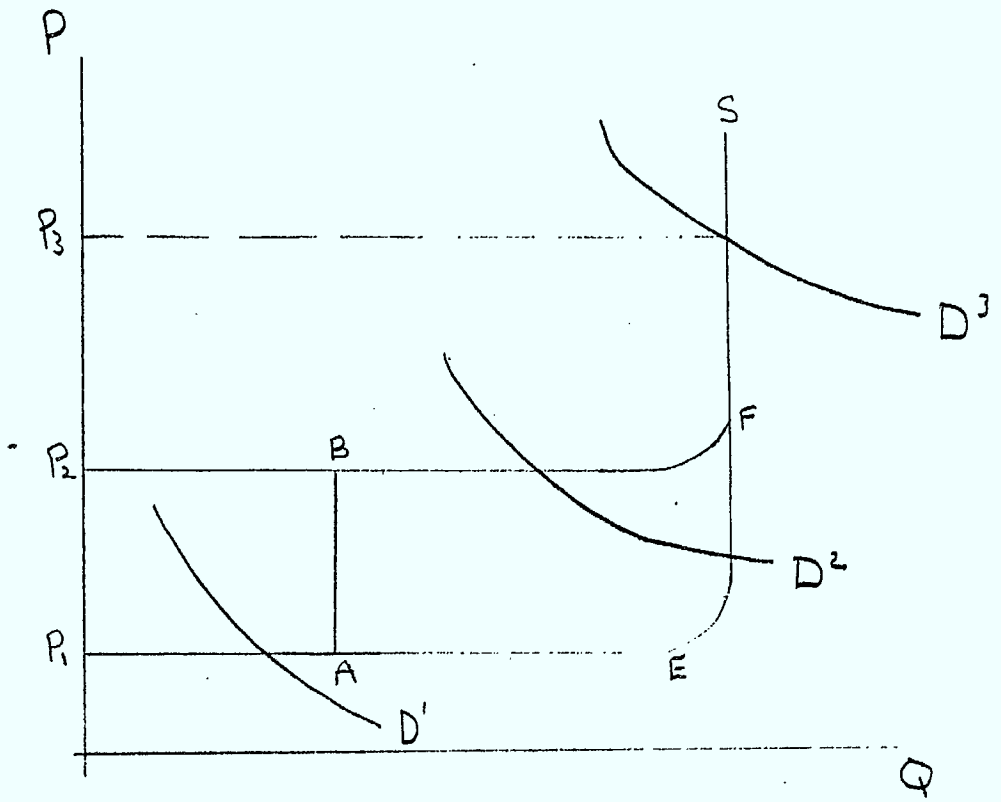

Figure 3

Suppose demand is very low, at D^1. This station will sell spots at a very low price; e.g. P_1. When it has announced the rate P_1, one can think of that defining the supply curve P_1ES. If advertising demand is generally higher the station may find it has excess demand at P_1, or merely that it can increase its revenue with a higher price even if full capacity has not been reached. E.g., let the demand curve be D^2 and suppose the firm sets the spot price at P_2. The supply curve now appears to be P_2FS. If demand were still higher, say at D^3, the firm would be able

*Economic theory shows that a supply curve is not determinate once a firm has some power to set its own price. Thus the graph in Fig. 3 is not a supply curve in the strict sense. It is still legitimate, however, to suggest how a firm will change its administered price as it reacts to selling more or less of its product. Fig. 3 can be thought of as such a "reaction function".

to set the higher price P_3 and still sell out this type of spot. Thus, if one observed the firm's behavior under these various demand conditions, it would appear that the firm has a stepped-supply curve, traced out roughly by P_1ABFS.

Such a supply relationship is consistent with the way pricing was described to us by the President of a Buffalo station. Before Bill C-58, if CFTO was selling a particular type of spot for $80-90, the Buffalo price would be $65-75. With the decrease in the quantity of Canadian demand due to the tax amendment, their price was dropped. But there are times when it is not kept low enough to compensate for the tax effect because spots can be sold to local American advertisers for a higher price. That is, the reduction in demand from Canada first causes the price to be dropped one step. If local demand is low enough it will be dropped a second step. (As already noted in Table 3, local sales have accounted for a bigger proportion of total revenue in the Buffalo market since 1975.)

Now consider adding together the reaction functions of the individual stations in a market such as Buffalo to get the total supply for our hypothetical type of spot. Since different stations will step up their prices at different quantities, the market supply relation will have more steps in it. That is it will be closer to a typical upward sloped supply curve of the type shown in Fig. 1.

The preceding discussion suggests that the standard supply-demand analysis does provide a rough approximation of the actual environment in at least some of the Canadian-border market pairs. One can, then, take its conclusions as reasonable explanations of what has happened. To reiterate,

with a tax amendment such as Bill C-58, we argue that:

1) border stations will reduce their rates, but not by the full amount of the tax in every case (it depends on the demand situation faced in each separate market);

2) some Canadian advertising will continue to flow to border stations;

3) advertising dollars will flow back to Canada; and

4) the prices of Canadian advertising will rise.

The analysis can be further extended to account for the combined effects of simulcasting and Bill C-58. Simulcasting increases the demand for advertising on Canadian stations. Thus, going back to Fig. 1, the demand curve will shift farther to the right than D_2^c and the increase in price will be greater. Secondly, it will cause the demand curve in Fig. 1b to shift to the left, as advertisers no longer will buy spots on simulcast shows. Thus, the border stations will decrease their rates by more. Indeed it is likely that the combination of C-58 and simulcasting is what explains why many stations reduced their prices enough to compensate fully for the tax effect.

Finally, the analysis also accounts for differential effects of the policy on different Canadian stations. To consider the simplest case, suppose two Canadian stations have a supply curve of the type shown in Figure 4, but one has the demand curve D^1 and one the demand curve D^2. When C-58 and simulcasting were introduced, both demand curves would shift to the right. The station with excess capacity would notice the effect by way of a reduction in excess capacity. It might also be led to increase its price. The station with no excess capacity would be

affected only by a new found ability to raise its price and still sell all its capacity. The important point is that both stations would benefit. In our discussion with people in the industry, there has been a tendency to view the independent stations, most of which were just getting established in the 1970's, as the gainers from Bill C-58. Our analysis suggests that the well established stations would also have been gainers. Without more detailed analysis of this kind it is not even possible to conclude which group was the bigger winner.

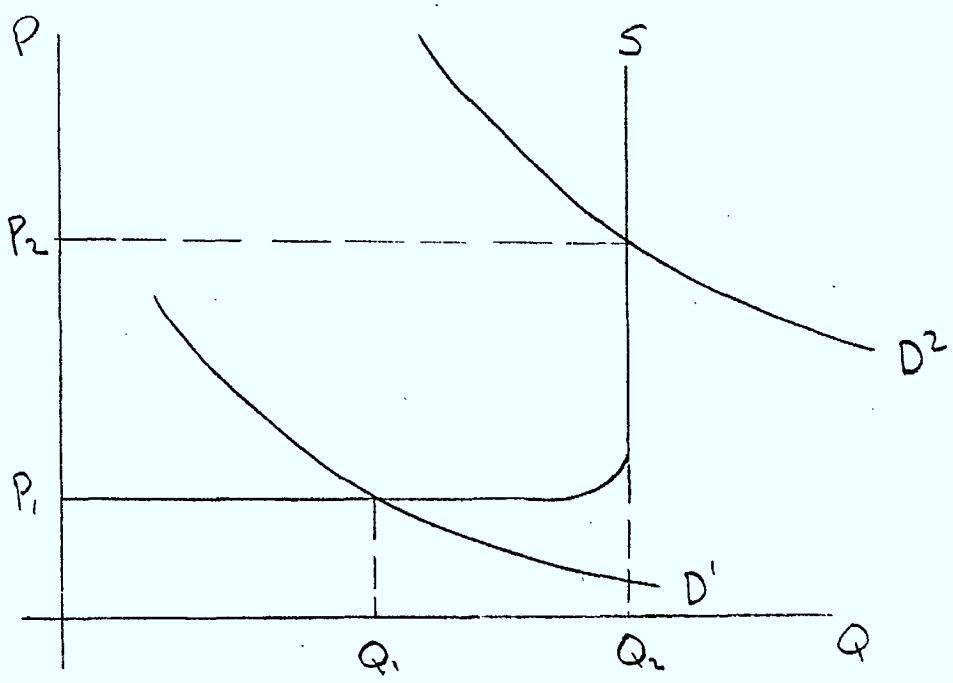

Figure 4

8. A Survey of Canadian Broadcasters

Conversations and correspondence with executive staff of television stations across the country contributed greatly to the information collected for this study. Facts and opinions provided in this way have served as useful inputs in every section of this report. In addition, however, since these contacts were extensive and involved similar questions in each case, it is worthwhile to report on them in a more comprehensive way in this section.

The people from whom data were collected do not represent a random sample of Canadian television stations. They are, however, representative of the industry in the sense that an effort was made to include stations with large audiences and stations from every geographical area. The list of stations contacted was prepared by an official of the Canadian Association of Broadcasters and the Association President asked the chief executive officer of each station on the list to respond to our request for information.

The questions set out in Table 7, intended to elicit judgements of the impact of Bill C-58 and of the importance of program substitution, were raised with each informant. Obtaining information in this way does, of course, involve problems. We were asking hard analytical questions (in greater number than those listed here), some of which contained "what if..." assumptions. E.g., what would your advertising revenue be if Bill C-58 were repealed? Furthermore, the interpretation of results is complicated, for if the government's policies work, many of the informants will have benefitted from them and their answers may be biased.

In regard to the interpretation issue, answers to the questions

Table 7

Answers to Common Questions
by Members of Management of Selected
TV broadcasting Stations

Questions:

1. When originally introduced, did the passage of Bill C-58 appear to cause an increase in the demand for advertising on your station?

2. Did a demand increase manifest itself in any other way? E.g., by a bidding up of the advertiser's cost per rating point?

3. Consider the hypothetical possibility that Bill C-58 were to be repealed and nothing else were changed. By what percentage would your annual advertising revenue fall?

4. Does simultaneous program substitution increase your advertising revenue?

5. How much of your weekly programming on average is simultaneously substituted on cable for programs from U.S. stations?

6. Would you be in favour of the non-simultaneous substitution of U.S. programming on cable?

Answers:

Station	(1) C-58 Quantity Effect	(2) C-58 Price Effect	(3) Estimated Current Impact (%)	(4) Sim. Sub. Revenue Effect	(5) Sim. Sub. (Hrs/week) Overall	Prime	(6) Non-Sim. Sub.
(Station names deleted.)	no	yes	10	yes	21	11	yes
	-	-	15	yes	19	9	yes
	no	yes	5-15	yes	8	4	yes
	†	no	10-15	yes	13	3	yes
	yes	yes	2	yes	7.5	3.25	yes
	yes	yes	10	yes	13.5	2	yes
	no	no	2	yes	22.5	12.5	yes
	no	yes	20	yes	12	na	yes

(Table 7 Continued)

(Station names deleted.)	-	yes	2	yes	10	na	yes
	no	no	8-12	yes	16.5	11.5	*
	yes	yes	25	yes	28	16	*
	yes	yes	10-20	yes	1.6	na	yes
	no	yes	†	yes	17	8	
	no	no	†	yes			*
	no	no	5	yes	27	11	yes
	no	no	less than 1%	yes	12	10	*
	no	no	0	yes	7	2	yes
	no	yes	†	yes	16.5	7.5	yes

- Question not applicable.
† Informant declined to answer.
* Though the answer given was not negative, serious reservations about the workability of non-simultaneous substitution were expressed.
na no answer available.

posed would be understood more fully if one had detailed historical data and applied the use of sophisticated statistical techniques. The very fact that full historical data were not available to us means that informed judgements based on more limited analysis are all the more important. Those judgements can obviously be made most knowledgeably by people in the industry. Many of our informants, who had our questions in hand in advance of interviewing, had taken them very seriously and put in some effort to prepare their answers. With regard to bias, there are clearly constraints within which it must work as well. A claim that a very large percentage of a broadcaster's revenue depends on Bill C-58 would simply not be plausible. More importantly, so long as one is aware of the possibility of bias, having the views of those in the industry affected by the policies being studied is an essential part of understanding them.

One aspect of Bill C-58 that comes out clearly in Table 7 is the view that it had little effect on the quantity of advertising time demanded in Canada when it originally took effect. For most stations, no increase in advertising was perceptible in the early years of its application, though this should not be taken to mean that broadcasters thought that it was having no effect. In a number of cases, informants noted that the years after 1975 were a period of rapid growth that could be attributed to more than one source. In Western Canada, for instance, higher than average general economic growth contributed to the growth of television market. The development of simultaneous program substitution through these years was also likely to have been important, though, oddly enough, our informants tended not to focus on this source of extra revenue. The effect was also masked in other ways. For instance, cable systems in

Alberta added U.S. stations and increased their market penetration in the mid-1970's. In this situation, the question becomes "How many advertising dollars were retained, that otherwise would have been lost due to Bill C-58?", which is probably more difficult to estimate. Market fragmentation that occurred because of additional Canadian stations in other parts of the country will have had the same effect.

(Passage deleted: information collected in confidence.)

(Passage deleted: information collected in confidence.)

Well established stations with network affiliation and low availability of advertising spots could also have benefitted from C-58 through a bidding up of prices, as illustrated in the theoretical discussion in section 7. A number of stations in the sample indicated that such a bidding up of the price per rating point, while not always obvious, probably did occur.

There remain a number of stations that did not respond positively to either of questions 1 or 2 and still estimate that revenue would fall if C-58 were to be repealed. While this may appear contradictory, it need not be. Even if it was impossible to separate out the effects of C-58, on either the quantity of advertising or its price, from the effects of other phenomena, informants could still have reason to believe that C-58 now influences some of their customers. At the same time, it might be reasonable to argue that those who answered both #1 and #2 negatively are likely to have benefitted less from C-58 than the other respondents. It also should be noted that some respondents cautioned forcefully in regard to putting much meaning on their answers to question 3 (the revenue effect of C-58), even though they were willing to make rough estimates.

If one is willing to give credence to the estimated impact of

C-58 on each station's revenue as indicated by the answer to question 3, it is possible to generate a dollar volume of predicted losses if C-58 were to be removed. Each percentage estimate was multiplied by the revenue for the station to which it applied for 1982. Thus total estimated revenue loss based on the hypothetical removal of Bill C-58, assuming 1982 business volumes, for 15 stations would be $32.6. This figure, of course, excluded three stations which were interviewed, and all of the remaining TV broadcasters in Canada.

In answering question 4, every informant indicated that simultaneous program substitution increases advertising revenue. The answers to question 5 are consistent with this, in that much substitution is done. (To see that these are large numbers, remember that substitution is possible only on the 40 percent of programming that may be imported. Thus a station that averages air time of 18 hours per day would be able to substitute a maximum of 50 hours per week. Recall also that substitution is constrained by the ability of stations to link their schedules to the schedules of more than one U.S. border station.)

Informants were also asked to estimate how much of their advertising revenue could be attributed to simultaneous substitution. Such an estimate is complicated, however, and few would venture to quote a number. Estimation is difficult not only because a detailed series of audience diversions must be analyzed but also because, as various informants pointed out, substitution is an important marketing device. Packages containing less desirable spots are worth more if substituted programs are included. Despite the lack of quantitative estimates, we inferred in more general terms that broadcasters believe that substitution is an

important asset.

An illustration is provided by comments from our informants at Global Television. They studied five of their programs in an attempt to estimate the effect of simulcasting. Of the audience for these five shows, the portion coming from viewers diverted from U.S. signals ranged from 60 to 82 percent. They believe that advertising rates on these shows would have to be lowered by 20-30 percent if simulcasting were not possible. The effect is greater, however, because they were packaged with shows that had lower ratings. In a seperate letter, our informants at Global attributed 30 percent of their revenues directly to the effects of simulcasting.

(Passage deleted: information collected in confidence.)

Since this comparison was not included in the list of questions sent to every station in the sample, we cannot tell whether the industry in general would attach greater importance to substitution than to Bill C-58. That view would be less likely for some stations outside the Eastern time zone and for some independent stations that find program substitution more difficult and costly. For instance, the General Manager of station CFRN in Edmonton argues that substitution has been of minimal benefit, whereas they place much value on Bill C-58. He sees that value increasing due to the delivery of U.S. signals by satellite, since"...there

appears to be no deletion or substitution restorative measures available to inhibit delivery of commercials on U.S. stations which in effect are being parachuted into Canada via every earth dish receiver." Informants at CITY in Toronto pointed out that it is difficult to maintain simultaneous substitution opposite non-network programs. The timing of a series of movies, for instance, can be juggled by CITY's Buffalo competitor to thwart its attempt to divert audience. In sum, the relative importance of Bill C-58 and simultaneous substitution appears to vary from station to station.

Our question on non-simultaneous substitution was asked in an unqualified way, without an attempt to draw attention to the difficulties and costs associated with it. Perhaps this helps to explain why no station was against the idea and most were quite positive about it. Some informants indicated that they would expect to bear costs of implementation. The General Manager of CKCK in Regina noted that his station had proposed to "provide a line" to the cable companies carrying programs for non-simultaneous substitution (in other words, bear all the direct costs) but that was disallowed by the CRTC. He argued that replaying the program in this way is the right of a station that has bought the program for showing in Canada. This view is shared by some other broadcasters as well, though not those who were skeptical about the practicality of non-simultaneous substitution (i.e. the four stations noted with an asterisk in Table 7). Among the latter is the President of Global Television, who proposes an alternative form of substitution that would apply especially to "strip programming". For a given series, the Canadian station would play the program at the same time as the U.S. station, but not necessarily the

same episode. This would remove the possibility that the U.S. station could thwart substitution by juggling episodes (as is the case with simultaneous substitution) but would not have the costly logistical problems of non-simultaneous substitution. The system could also be used for one-per-week network or syndicated programs so long as the program release dates for the Canadian station are flexible enough.

Informants were also asked for their views on "leap-frogging" as an alternative form of protection. (These findings are not summarized in Table 7.) The typical response was to view it as a double-edged sword, with the protection from border station competition having to be set against possible increased competition from better quality service. One informant pointed out that it is a less desirable device than program substitution because the latter reduces the general spillover effect of U.S. advertising, while leapfrogging or Bill C-58 do not.

Finally, many informants commented on the view that C-58 has operated in part by way of clearly communicating the Government's desire that Canadian advertisers not buy time on border stations. They all believed that the effect of this moral suasion was strong, offsetting in part the effect of the reduction in rates by the border stations. In some cases this effect has been enhanced by direct approaches to advertisers whose commercials have been viewed on border stations.

9. A Survey of Advertisers

The Association of Canadian Advertisers, in response to our request, surveyed some of its member corporations to see if there was a significant change in their allocation of advertising between Canadian and U.S. television since the inception of Bill C-58 and simulcasting. The response to the questionnaire was small: even though anonymity was assured, only 9 of 32 large advertisers replied.

One large advertiser, Procter and Gamble, reported openly that since 1973 they have allocated no business at all to U.S. border stations. Eight other companies reported that they had spent amounts ranging from nearly zero to 2.8 percent of their national budgets on U.S. stations between 1978 and 1980, and from zero to 5.3 percent in 1981 and 1982. They did not, however, provide any data for earlier years that would allow a "before-and-after" comparison to be made.

Almost all of the allocations referred to in these figures were spent in the Vancouver market. In 1978-80 four of the respondents spent between 5 and 9 percent of their Vancouver budgets in the U.S. Since it is known that the Seattle stations are high-priced alternatives relative to Vancouver stations and to KVOS in Bellingham, we assume that virtually all of it was placed with KVOS. These numbers thus provide some corroboration for the view that KVOS is an exception to the rule that large Canadian advertisers avoid border stations in an effort to be good corporate citizens. An executive member of the ACA, as well as some broadcasters we interviewed, confirmed this. They noted that KVOS carried on an extensive public relations campaign that was intended to convince advertisers that it constituted a Canadian company. This is

believed to have played an important part in the station's maintenance of its flow of dollars from the Vancouver market.

Of the nine large advertisers, only one used the Buffalo stations to reach the Toronto market between 1981 and 1982, though it allocated only 0.5 percent out of its Toronto market budget. One other advertiser used U.S. stations to reach into Montreal, but the budget allocation was extraordinarily small.

In sum, large Canadian advertisers still use U.S. stations to reach Canadian audiences, but to a limited extent. This limited survey indicates that the most important entry point is via station KVOS in Bellingham.

10. The Problem of Compliance

The question of compliance with the income tax law as it has been affected by Bill C-58 was discussed with interested parties in the industry and with officials of Revenue Canada.

(Passage deleted: information collected in confidence.)

There are a number of steps an advertiser could take to get

around the requirements of Bill C-58. In the case of a multi-national firm, for example, its U.S. branch or head office could pay for the advertising time which would be directed towards the Canadian audience. Secondly, a Canadian advertiser could set up a U.S. subsidiary and have the subsidiary purchase its advertising time. Thirdly, a Canadian advertiser could buy U.S. advertising as part of a larger package dominated by advertising in Canada and not separate out the U.S. expenditure. This is illegal but special effort would be required if it is to be detected. Finally, there is the grey area caused by the exemption of advertising that is directed to foreign audiences but that may also have Canadians as a target. For example, an advertiser whose message is really directed to Canadian audiences would claim that a wide range of material would be relevant for the U.S. tourist in Canada

An indication that the C-58 provisions do not receive special attention is that they do not constitute an item which is assigned a separate computer number in the processing of tax returns. (This explains why Revenue Canada was unable to assist us in coming up with an estimate of the amount of Canadian advertising expenditure that flows to the U.S.) As the tax accounting is now done, it would, furthermore, be difficult to separate the required information. Suppose that a firm spends $1,000 on advertising, $500 in Canada and $500 in the U.S. Normal accounting practices deduct the $1,000 and then add back $500 as a non-deductible expense item. The difficulty is that it is consolidated with other non-deductible expenses.

Revenue Canada officials candidly admit that surveillance of Bill C-58 is given a low priority because of the limited amounts of funds

involved. There is an operations manual that provides help to the auditors in treating such provisions, but it is confidential and a request to see the relevant parts was denied. We did, however, discuss their interpretation of Section 19.1 of the Act. The key matter of defining the meaning of "expenditures primarily directed to the Canadian market" is handled by using various criteria to make a judgement in each case: the wording of the message, the normal listening or viewing audience involved, the concurrent use of Canadian media to an equivalent extent to reach Canadian viewers, and the role of attracting tourists in the advertising program considered.

Between the taxation years 1975 and 1982, a total of 75 taxpayers with large advertising budgets had claims for advertising expenses disallowed under Section 19.1 of the Act. The 75 companies had to pay about an extra $1 million of tax for the extra $2 million of additional income which had been added back by the Revenue Canada officials. Revenue Canada notes that the amounts disallowed are insignificant relative to other adjustments, which is one of the primary reasons for not giving a higher priority to this issue.

11. Estimating the Effects of Bill C-58

This section is concerned with providing a quantitative picture of the impact of Section 19.1 of the Income Tax Act on television advertising revenue. In order to provide a context for the dollar estimates, trends in Canadian advertising rates and television advertising revenues are briefly described for the period since Bill C-58 was passed. A discussion of estimation methodology follows and this includes a review of the problems faced in generating our estimates. Finally our quantitative results are presented.

a) Media Cost Inflation and Advertising Revenue Increases: Since 1975 the cost of reaching an audience by way of television has risen considerably. As shown in Table 8, in nominal terms the cost of reaching an audience of 1,000 (the CPM) increased in every year from 1976 through 1982. When an adjustment is made for the rate of consumer inflation, the cost index for TV advertising increased quite sharply in 1977, 1978 and 1982. Decreases occurred only in 1977 and in the estimate for the year 1983. The average annual increase in nominal terms was 13.1 percent and in real terms 3.5 percent. TV was the only medium to have cost increases higher on average than increases in the Consumer Price Index between 1975 and 1982. TV cost increases were greater than CPI increases in six out of seven years ending 1982.

Moreover the CPM for television advanced on average since 1975 at higher rates than the corresponding costs in magazines, radio, and newspapers. The largest relative change occurred in the relation between TV and magazine advertising. (See Table 9). In 1975 the CPM for magazines was five times the CPM for TV. By 1983 the ratio had fallen to

Table 8

Media Cost Increases (CPM's) In Canada, 1975-1983

Medium	1976	1977	1978	1979	1980	1981	1982	1983[e]	Average Annual 1975-1982	Average Annual 1975-1983
Magazines	8.1	5.2	4.0	8.0	9.1	7.3	9.7	6.0	7.3	7.2
TV	10.5	14.9	15.5	3.4	12.3	14.7	21.4	-2.6	13.1	11.0
Radio	-1.0	10.0	14.8	-2.5	7.7	12.3	21.2	6.4	8.6	8.4
Newspapers	13.2	4.9	5.4	6.5	6.7	8.3	14.0	15.3	8.3	9.2
Change in CPI	9.4	7.8	6.4	7.9	10.0	12.7	11.8	5.5[e]	9.6	9.0[e]
TV index minus CPI change	1.1	7.1	9.1	-4.5	2.3	2.0	9.6	-8.1	3.5	2.0

Source: Hayhurst Advertising Ltd., Summer 1983; Bank of Canada Review, June 1983.

Table 9

Shifts In Relative Media Costs (CPM's), Selected Years, 1973-1983

	1973		1975		1978		1980		1983	
Magazines	$9.53	(4.6)	10.95	(5.0)	12.95	(4.0)	15.27	(4.1)	19.07	(3.8)
TV	2.07		2.19		3.21		3.73		5.06	
Radio	1.64	(0.8)	1.92	(0.9)	2.40	(0.7)	2.52	(0.7)	3.65	(0.7)
Newspapers	7.31	(3.5)	8.88	(4.1)	11.11	(3.5)	12.62	(3.4)	17.97	(3.6)

Note: The figures in brackets are the ratios of the given CPM to the CPM for TV.

Source: Hayhurst Advertising Ltd., Summer 1983.

3.8. On the other hand, the CPM's for all of the other media rose relative to the TV CPM between 1973 and 1975.

It is interesting to note that the relatively large advertising cost increases for TV during the years 1975 through 1978 occurred at a time when the Canadian economy was not growing rapidly and when the Anti-Inflation Board was restricting price increases. Indeed Canadian broadcasters complained that advertising price increases were curtailed by the AIB. While other factors may also have influenced the statistics, these absolute and relative CPM cost increases are consistent with the hypothesis that the combination of Bill C-58 and the growth of simulcasting caused TV advertising rates to rise more briskly than they would have otherwise.

Table 10 compares growth rates in advertising revenues with various media cost increases since 1973. Revenues for the four media expanded considerably more quickly than the corresponding CPM's. The spread between revenue gains and CPM gains for TV was quite large, with average rates of increase of 18.4 percent and 10.8 percent respectively over the period 1973-1982. This implied measure of real activity (revenue gains less media cost gains) was exceeded only by a comparable spread in the magazine industry. Recall that Bill C-58 was having an effect in both industries. In both cases new media vehicles that could more effectively compete with U.S. concerns were undertaken; e.g. Maclean's magazine in print jounalism and CITY, Global, CKVU and CITV to compete with the U.S. border stations. Thus some of the spread between TV revenue gains and advertising rate increases is bound to reflect the creation of new TV stations in Canada.

Table 10

A Comparison of Canadian Media Cost and Advertising Revenue Increases 1973-1982

(Average Annual Rates of Increase)

		1975-1979	1979-1982	1973-1982
(1)	Media Cost Increase			
	Magazines	6.3	8.7	7.3
	TV	11.0	16.1	10.8
	Radio	5.1	13.6	8.5
	Newspapers	7.4	9.6	8.8
(2)	Net Advertising Revenues			
	Magazines (general)	18.2	13.6	21.3
	TV	18.7	13.9	18.4
	Radio	14.1	9.2	12.4
	Newspapers (Daily)	10.0	11.7	11.7
(3)	Consumer Price Index	8.3	11.1	9.8

Sources: (1) Hayhurst Advertising Ltd., (mimeo, Summer 1983).

(2) Maclean Hunter Research Bureau, Advertising Revenues In In Canada, November 1982.

(3) Bank of Canada Review, June 1983.

b) Revenue Increases and Profitability by Market: Table 11 focuses on the advertising revenues of private sector television stations in selected urban markets in 1975 and 1982. Table 12 highlights the experience of specific broadcasters which are of interest either because they are relatively new independents that were expected to benefit because of Bill C-58, or because they are in the large urban markets of Montreal, Toronto or Vancouver. In the case of CKGN, the data actually refer to the whole Global network (i.e. its revenues are generated in markets throughout southern Ontario). The newly-founded independent stations have experienced rapid rates of revenue increase since 1975. In some respects survival required rapid expansion, and indeed an examination of profit statistics later in this report will show that these stations experienced some rocky periods in the 1970's.

The figures in Table 13 indicate the composition of total revenues within these major Canadian markets. Total advertising revenues are broken down into local, national and the much smaller network payments. (In the group of stations considered, network payments were primarily important for stations in the CTV network.) Table 14 shows the importance of local revenues for the same group of stations set out in Table 12.

In 1975, local television advertising represented 27.9 percent of the total advertising revenues earned by private stations in these markets. By 1982, the local revenue percentage had declined to 23.7 percent. The declining reliance on local as compared to national TV advertising in Canada was one of the predictions made by critics of Bill C-58 when it was originally proposed. But this development did not spread equally to all markets, and in some cases the reverse occurred.

Table 11

Total Private TV Advertising Revenues In Various Urban Markets, Millions of $'s

Market	1975	% of Total	Rank	1982	% of Total	Rank	Annual Rate of Change 1975-1982
	18.6	15.2%	3	79.2	18.8%	3	23.0%
	15.1	12.4	4	37.3	8.9	5	13.8
	31.7	25.9	1	86.0	20.4	2	15.3
(Information deleted.)	9.3	7.6	5	23.5	5.6	6	14.2
	3.2	2.6	8	9.4	2.2	8	16.5
	31.3	25.6	2	124.0	29.4	1	21.7
	8.8	7.2	6	41.8	9.9	4	24.9
	4.3	3.5	7	20.7	4.9	7	25.1
Total	122.3			421.9			19.4
National CPI							9.6

Source: Department of Communications, Unpublished Data, Summer 1983.

Table 12

Private Canadian Television Broadcasters-Advertising Revenue

Growth At Annual Rates Selected Stations

Station	1976	1977	1978	1979	1980	1981	1982	Average Annual Growth Rate 1975-1982
	33.1	17.8	19.6	12.0	11.5	17.2	11.3	17.3*
			26.8	26.0	27.3	16.9	9.8	21.2
	22.2	16.3	17.0	21.0	19.1	22.2	13.4	18.7
	49.2	29.6	23.2	25.2	28.5	26.9	30.4	30.2
(Station names deleted.)	22.2	15.6	16.4	18.8	2.5	17.2	5.2	13.8
	18.0	7.7	15.0	18.1	7.0	13.9	8.8	12.6
	13.2	21.4	40.6	40.5	28.5	38.8	38.7	31.3
	81.0	39.5	34.7	9.1	17.5	18.4	14.1	28.8
	26.7	12.2	12.5	13.6	8.4	18.6	17.5	15.1

* (Proprietary information deleted.)

Source: Department of Communications, Unpublished Data, Summer 1983.

Table 13

Composition of Private TV Advertising Revenues Within Various Urban Markets, Millions of $'s

	Total Revenues		Local		National		Network Payments		Local as % of Total Revenue (%)	
	1975	1982	1975	1982	1975	1982	1975	1982	1975	1982
(Information deleted.)	18.6	79.2	9.3	29.3	7.6	45.4	1.7	4.5	50.0	36.9
	15.1	37.3	1.4	1.3	13.7	36.1			9.3	3.4
	31.7	86.0	12.4	31.1	17.4	49.1	1.9	5.8	39.1	36.1
	9.3	23.5	2.2	2.7	5.7	17.9	1.3	2.9	23.6	11.5
	3.2	9.4	1.7	3.8	1.2	4.6	.3	1.0	53.1	40.4
	31.3	124.0	3.3	14.4	26.1	103.3	2.1	6.3	10.5	11.6
	8.8	41.8	2.1	11.2	6.0	28.0	.8	2.7	23.9	26.8
	4.3	20.7	1.7	6.3	2.1	13.3	.5	1.1	39.5	30.4
Total	122.3	422.0	34.2	100.1	79.7	297.6	8.6	24.3	27.9	23.7

Source: Department of Communications, Unpublished Data, Summer 1983

Table 14

The Importance of Local Advertising Revenues to Selected Private Canadian Television Broadcasters, Millions of $'s

Station	Total Revenues		Local Revenues		Local as % of Total Revenue	
	1975	1982	1975	1982	1975	1982
	8.8	27.0	2.1	5.1	23.9%	18.9%
		14.8		6.1		41.2
	6.2	20.6	3.0	6.2	48.4	30.1
	3.2	20.1	1.8	9.0	56.2	44.8
(Station names deleted.)	15.1	37.3	1.5	1.3	10.0	3.4
	17.3	39.6	1.0	0.5	5.8	1.3
	3.4	22.9	0.8	7.6	23.5	33.2
	10.5	29.4	2.8	9.2	26.2	31.3

Source: Department of Communications, Unpublished Data, Summer 1983.

In the expensive Toronto market the local advertising share of total revenues actually increased. (Information deleted.) In contrast, Local revenues became less important for the established stations (deletion) in this period. A similar pattern is evident in Vancouver, (Information deleted.)

It is likely that the distribution of local and national revenues also changed in other markets. New stations in Calgary and Winnipeg made it possible in these markets as well. In densely populated areas, where signals from different cities overlap, there is considerably more scope for local advertisers,who previously might have found it too expensive to place spots on large stations, to find substitutes on smaller Canadian stations.

Table 15 shows annual rates of growth in expenses for the same collection of large private stations already considered. On average total expenses rose nearly as rapidly as advertising revenues between 1975 and 1982, 18.7 percent compared with 19.4 percent.

The ratio of operating income (total revenue minus total expenses before depreciation and interest) to advertising revenue is used as a rough proxy for profitability in the television industry. From these ratios as shown in Table 16, it is possible to trace the improving financial health of the new independent stations, the fortunes of which are usually associated with, among other things, help from Bill C-58. Based on 1982 figures, only (deletion) appears to have an abnormally low profit ratio.

Table 15

Selected Private Canadian Television Stations-Total Expense
Growth At Annual Rates

Station	1976	1977	1978	1979	1980	1981	1982	1975-1982
	31.1	24.4	31.5	23.8	14.8	14.1	9.6	21.1
			5.8	8.3	30.0	13.7	12.6	
	14.6	12.5	14.3	33.6	8.5	37.3	18.0	19.4
(Station	-6.5	16.2	14.0	25.9	21.1	50.6	18.8	19.0
names								
deleted.)	18.8	33.2	15.7	22.6	33.1	-0.4	9.6	18.4
	8.6	11.5	51.0	0.3	12.2	6.2	10.7	13.4
	4.2	60.6	27.0	13.6	23.0	16.5	28.0	23.7
	22.4	21.0	50.9	6.3	26.2	11.9	11.8	20.8
	14.8	20.0	8.7	26.1	5.6	12.2	12.3	14.1
Total Major Markets	17.6	28.2	25.5	13.7	20.5	13.7	12.9	18.7

Source: Department of Communications, Unpublished Data, Summer 1983.

Table 16

Private Canadian Television Broadcasters Profit Ratios 1975 to 1982
(Operating Income/Advertising Revenues) Selected Stations

Station	1975	1976	1977	1978	1979	1980	1981	1982
	29.5	30.6	26.7	27.5	20.6	16.8	22.7	23.0
			-17.6	6.1	17.1	13.0	14.4	13.4
	35.2	40.2	44.5	44.3	38.7	44.0	37.3	34.3
(Station	-51.0	-1.4	5.7	12.1	11.0	18.2	19.5	39.8
names								
deleted.)	32.7	34.9	24.2	23.9	21.8	8.8	23.0	20.3
	43.6	46.9	48.8	44.1	42.8	39.5	45.8	44.8
	3.9	6.6	-23.3	-1.2	17.4	15.3	29.3	34.9
	-34.0	11.9	27.4	25.4	24.8	23.6	26.1	26.4
	31.7	36.5	32.0	34.1	26.9	29.0	32.9	36.0

Source: Department of Communications, Unpublished Data, Summer 1983.

The figures in Table 17 indicate that 20 private broadcasters in major urban markets collectively experienced a substantial increase in their profits ratios (the ratio of profits to advertising revenues) between 1975 and 1982. The profit gains for the entire sample of 20 stations was heavily influenced by marked improvements in the Alberta, Montreal and Toronto markets. Performance for the Vancouver stations was, on the other hand, quite poor relative to the combined total for all of the markets. It is also interesting to observe that the broadcasters in large urban markets earned higher profits relative to advertising revenues in 1975 than all other remaining stations in Canada, and that the favourable gap actually widened quite considerably between 1975 and 1982. This is interesting, for the profit gap rose when Canadian economic conditions were quite weak between 1975 and 1979, and dramatically weak during 1981 and 1982. In line with the sharp improvements in advertising revenues. (Information deleted.)

also sharply increased their profit ratios in recent years. Two (deletion) stations, (deletion) also earned improved profits in 1982 relative to their 1975 position.

c) Estimation Methods and Data: The key estimate which is required to assess the effect of Bill C-58 is the amount of advertising revenue that has accrued to Canadian television broadcasters since the beginning of 1976 that would otherwise have been attracted to the U.S. border broadcasters. Various approaches to such an estimate are possible. Perhaps the most obvious and tenable one would be to develop an equation that predicts the expected amount of annual advertising revenue for a typical TV station by plugging in the values of various independent

Table 17

Profit Ratios (Operating Income/Advertising Revenues) for Twenty Private Broadcasters, 1975-1982 (Percentages)

	1975	1976	1977	1978	1979	1980	1981	1982
Main Markets								
	29.5	30.6	13.8	21.1	19.4	15.4	19.8	19.6
(Market names deleted.)	20.1	29.4	29.5	29.9	28.2	32.3	30.7	37.5
	32.4	32.5	31.0	30.0	30.9	34.3	39.4	41.6
	29.9	23.3	27.3	30.7	28.9	27.4	31.6	31.0
	18.4	30.4	32.5	30.4	31.5	26.6	31.4	34.1
	32.7	34.9	24.2	23.9	21.8	8.8	23.0	20.3
	14.0	10.7	11.3	7.4	11.6	13.5	18.7	23.0
	31.8	36.1	28.1	31.9	27.0	38.9	43.9	42.8
(1) Weighted Average	25.1	30.5	26.5	27.4	26.4	26.9	31.5	33.3
(2) All Other Markets	20.9	23.5	21.7	22.4	21.9	22.5	22.6	22.1
Ratio (1)/(2)	1.20	1.30	1.22	1.22	1.21	1.20	1.39	1.51

Source: Department of Communications, Unpublished Data, Summer 1983.

variables, such as the size of the station's potential audience in the year concerned, the number of competing stations which share the market, a measure of slack in the economy, and so on. If the necessary data were available the parameters of this type of equation would be estimated for a period before Bill C-58 was passed. It could then be re-estimated for the period 1976 to 1982 and the changes in the parameters of the equation would be a measure of the impact of Bill C-58. Put a different way, the original equation could be used to calculate what levels of revenue would have been generated in each year from 1976 to 1982 by plugging in the values of the independent variables that applied during those years. These "predicted" revenue amounts would then be compared with the actual revenue figures and the difference would be attributed to Bill C-58.*

While some of the relevant data for such a quantitative analysis are available, there are no data for some of the key variables in relevant time periods. The two major gaps are as follows:

1) As already noted, simulcasting in Canada became an important source of broadcasting revenue during the same period in which the effects of Bill C-58 occurred. This would not be a problem if consistently defined data on the amount of simulcasting by each station for each year were available. Since they are not it is impossible to account for this important effect on a year-by-year basis.

2) Still more importantly the excellent data series that are now collected by Statistics Canada, including various advertising revenue statistics, only extend back to 1975 on a consistent definition. In order to

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*Indeed the approach could be made even stronger by estimating similar equations, before and after 1976, for the Canadian revenues flowing to U.S. stations.

estimate an equation that is independent of the effects of Bill C-58, it would be necessary to have data for a series of years before 1976, long enough so it would be possible to infer how advertising revenue responded to the variables that determine it in the industry as it was before the tax change.

Since the above-described technique could not be used, a simpler and more approximate approach was adopted. It is essentially the same one as that used in the earlier review of Bill C-58 for the year 1975-78 by Donner and Lazar. The major steps are as follows:

1) The amounts of Canadian advertising revenues received by U.S. border stations for the years 1975 through 1982 were roughly estimated.

2) The potential placement of advertising on U.S. border stations in 1982, assuming that the Canadian environment had not changed due to Bill C-58 and due to increased use of simulcasting, was projected. Two alternative approaches for this projection have been used, one based on media cost increases in Canada and one on market shares. Both approaches are based on four markets, rather than on the total Canadian TV industry. These are Montreal, Toronto/Hamilton, Vancouver and a group of smaller markets for which we were able to collect data. The last market is referred to as "Other" and is not quantitatively important in the analysis.

The media cost approach simply assumes that the actual amounts of revenue flowing to border stations in 1975 in each market would have grown each year through 1982 by the increase in a cost index for

television advertising. In the market share approach the border station revenues were added into total market revenues in each case. It was then assumed that in 1982 the border stations would have had the same percentage market share as they had in 1975 if Bill C-58 had not been passed and the utilization of simulcasting had not increased.

3) Actual estimated revenue flows to the U.S. in 1982 were subtracted from potential revenue flows as defined above. The difference is our estimate of the foregone revenues of the border broadcasters due to the combination of Bill C-58 and the increased use of simulcasting.

4) A rough estimate was made of the loss in revenue to border broadcasters due to the greater use of simultaneous substitution.

5) The estimate under (4) was subtracted from the estimated foregone revenues under (3). The bulk of the difference was assumed to have accrued to Canadian TV broadcasters and is an estimate of advertising expenditures repatriated to Canada due to Bill C-58. This assumes, of course, that advertisers did not adjust the total size of their TV budgets, and that they did not switch funds to other media, due to Bill C-58. Our interviews with media buyers and broadcasters in Canada indicated that the above assumption is a reasonable one. If one believes the contrary, however, our estimates should be scaled down accordingly.

Unlike the preferred but unusable techniques described earlier, our approach unavoidably places great weight on the environment in a single year, 1975, the last full year before Bill C-58 was passed. We see no strong reason, however, to believe that 1975 was an unusual year as far as television advertising is concerned. Both Canada and the U.S. experienced a recession that year, but Canada's was relatively mild. If

the decline in economic activity did affect the volume of advertising, there is no obvious reason to believe it affected the proportions of television advertising going to Canadian stations and U.S. stations. If, for instance, the U.S. recession led to more price cutting by border stations, this could well have been offset by competition from new stations in the Canadian industry. So long as Canada-U.S. market shares were not significantly affected, the 1975 recession should not have affected our projections based on market shares, in our view the more important of the two sets of numbers.*

The strength of the analysis is, of course, also dependent on the quality of the data. This varies from very good to very rough. A brief description of data sources is set out in Table 18.

The estimates of actual advertising flows to border stations presented the most difficult problem. While it might be possible in theory to extract them from income tax returns, the Department of National Revenue does not treat the portions of advertising going out of the country as a separate item. Neither are these data provided from other public agencies or sources. Thus our only recourse was to request information from those involved in the industry on both sides of the

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*It might be argued that a special condition also prevailed due to the 1982 recession, in that many corporations experienced sharp reductions in taxable income and thus would have been less affected by a tax incentive. In our interviews such a change from 1981 to 1982 was never mentioned and was denied in a few cases in which the question was asked directly. Moreover one would not expect the "good corporate citizenship" argument to recede simply because an advertiser had no taxable income in one particular year. Other adjustment lags would also apply. Finally our own figures in Table 19 indicate no break in a trend between 1981 and 1982.

border and piece together information from a variety of sources. Estimates for 1975, 1977 and 1978, put together in a similar manner, were available in the 1979 Donner and Lazar report.

We attempted to formalize the process by sending out a questionnaire to all of the commercial stations included in BBM's survey of Canadian viewing of U.S. stations. (See Appendix 2) They were asked to report their Canadian receipts for each year from 1975 to 1982. The direct

Table 18

Data Sources For Various Estimates
Required in the Calculations

Data Required	Data Sources
A. Estimates of the Actual Flow of Expenditures to Border Stations Between 1975 and 1982	The 1979 Donner & Lazar report was used in the preparation of 1975 estimates. The 1983 Donner & Kliman survey letter provided estimates for 6 large stations (in aggregate only) and eleven other stations for the period 1975 to 1982. A series of interviews in 1983 with U.S. stations, Canadian stations, advertising agencies and representative houses in Canada were used to help disaggregate the 6 station figures into three markets.
B. Canadian TV Revenues, By Station and Market, 1975 to 1982	The Department of Communications provided us with this data. A Statistics Canada document is available, but it does not break the figures down by markets or by stations.
C. TV Media Cost Increases, 1975 to 1982	The advertising industry formally maintains and collects such data. Annual CPM data were provided by Hayhurst Advertising Ltd.
D. Simulcasting Revenues For Canadian Stations	The primary source is Mediastats Inc. of Toronto. A series of studies were commented on in this report and it was necessary for the authors to estimate the amount of simulcasting revenues which were earned in 1975 and 1982.

response to the questionnaire was small, with eleven stations providing the estimates requested. These data were importantly supplemented by figures provided by a group of six stations in three key border markets. These are the stations which have supported the Washington lobby against Bill C-58: WKBW, WGRZ and WIVB in Buffalo, WCAX, the CBS-affiliate in Burlington, Vermont, WPTZ, the NBC-affiliate in Plattsburg, N.Y., and KVOS in Bellingham, Washington. The revenue data, shown in Table 19, were provided only as aggregate amounts for the six stations combined.

Although our data are based on only 17 of the 41 stations contacted, we believe that they catch up the bulk of the Canadian advertising flow to U.S. border stations since 1975. (The one exception that may be of an important magnitude are the stations in Spokane, Washington, that serve the Alberta market.) In addition to the fact that our respondents include the border stations that have been most heavily involved in the lobby against Bill C-58, the figures which they provided us are roughly consistent with quantitative observations made by numerous people with whom we talked in the course of our research. We held interviews with Canadian and U.S. broadcasters, Canadian advertising representatives of U.S. broadcasters, and executive staff at advertising agencies. Rough estimates given to us by these people helped us to disaggregate the figures provided by the six station group mentioned above into three separate markets.

Data on Canadian broadcasting revenues are very dependable because they are derived from the Annual Return that broadcast licencees must file. The media cost increases are based on data that are privately collected but are widely used in the advertising industry. The

simulcasting figures we use in our estimating process have also become almost part of the public domain, and we are satisfied that the original simulcasting revenue calculations were made in a consistent and reasonable way.

d) Calculating the Revenue Effects of Bill C-58: The data in Table 19 indicate that the 17 border stations included in our sample experienced a sharp decline in their Canadian advertising revenues after 1975, from $17.9 million in 1975 to $9.5 million in 1977 and 1978. (Though these figures were originally provided in U.S. dollars, our analysis will be in terms of Canadian dollars unless otherwise noted.) Bill C-58 took initial effect in January 1976 but a "grandfather clause" allowed a tax deduction to continue in some cases into 1977. The flow to the U.S. began to increase again in 1979 and, in nominal dollars, was close to the 1975 level by 1982.

Much of this increase is, however, due to inflation. If the change in the CPM shown in Table 8 is taken as an index of advertising rate increases (and it is recognized that this is not a totally appropriate index for this question--the correct one is not available), they more than doubled between 1975 and 1982. By this criterion, on a "physical volume" basis, using 1975 prices, advertising to the border stations had fallen to $6.7 million in 1982. If the Canadian Consumer Price Index is used as the measure of inflation, the current dollar figure of $16.0 million for 1982 becomes $8.5 million in terms of 1975 dollars. Using the U.S. CPI on the U.S. dollar amount, in 1975 dollars the flow moves from $17.6 million (US $) in 1975 to $7.5 million (US $) in 1982. The problem of correcting for inflation is very complicated in the present

Table 19

Gross TV Advertising Revenues Received by U.S. Border Stations,
Estimates Based on Response to Questionnaires
(Millions of dollars)

	Millions of U.S. $'s				Millions of Current Year Canadian $'s	
	Six Large Broadcasters* (Three Markets)	Eleven Other** Broadcasters From Survey Letters	Total	Exchange Rate Cdn $'s/US $'s (Average Noon)	Six Large Broadcasters	Total
1975	17.4	0.2	17.6	1.0173	17.7	17.9
1976	15.9	0.1	16.0	0.9861	15.7	15.8
1977	8.7	0.1	8.9	1.0635	9.3	9.5
1978	8.2	0.1	8.3	1.1402	9.3	9.5
1979	10.2	0.1	10.3	1.1715	11.9	12.1
1980	9.8	0.2	10.0	1.1690	11.5	11.7
1981	11.5	0.4	11.9	1.1990	13.8	14.3
1982	12.5	0.5	13.0	1.2341	15.4	16.0

*Buffalo (WKBW, WGRZ, WIVB)
Bellingham (KVOS)
Burlington/Plattsburgh (WCAX, WPTZ)

**WUAB Cleveland, WSEE Erie, WHEC Rochester, WIXT Syracuse, WKBD Detroit, WXYZ Detroit, WJRT Flint, KDLH Duluth, KTHI Fargo, KXJB Valley City, KIRO Seattle

Source: The six large broadcasters replied with aggregate figures only. Eleven other broadcasters provided separate data. One broadcaster provided data for 1982 only, which are not reported in this table.

context because a different inflation index is required in order to focus on different questions, as is suggested by the use of three different indices in this paragraph. Furthermore, the CPM index is not really appropriate here, except as a very rough measure. Consequently the rest of the analysis is presented in nominal or current year dollars. This should be kept in mind where comparisons of figures applying to different years are involved.

As in the earlier Donner and Lazar report, the projections that underlay our estimates of repatriated advertising dollars emphasize the three major U.S. border markets for Canadian advertising. The data in Table 20 show the estimated amounts of actual Canadian revenue received in these markets in 1975 and 1982. The breakdown by market in the earlier report, along with information collected through interviews with broadcasters, allowed us to hypothesize a disaggregation of the figures provided by the six largest stations in these markets (i.e., the aggregates shown in the left-hand column of Table 19). In Table 20 small adjustments, based again on interview information, were made to account for the fourth station in the Buffalo market and the third station in the Burlington-Plattsburg market.* Based on eight stations instead of six, border broadcasters in these three markets attracted approximately $18 million of Canadian advertising in 1975 and $17.2 million in 1982.

The advertising revenues shown in Table 20 are gross revenues. That is, they include advertising agency and representative commissions, which typically amount to about 20 percent of the total. We assume that,

*In Buffalo WUTV had 2 percent of the Toronto audience in 1975 and 6 percent in 1981, WEZF, the ABC affiliate in Burlington, Vermont, had 1 percent of the Montreal audience in 1975 and 3 percent in 1981.

Table 20

Estimate of Canadian Gross TV Advertising Revenues
Received In Three U.S. Border Markets-1975 and 1982
(Millions of Canadian Dollars)

	Estimated 1975	Estimated 1982
Buffalo	8.9 (4 stations)	4.6 (3 stations) 5.9 (4 stations)
Burlington/Plattsburg	2.4 (2 stations) 2.7 (3 stations)	1.7 (2 stations) 2.2 (3 stations)
KVOS in Bellingham	6.3	9.1
Total for Three Markets	17.7 (6 stations) 18.0 (8 stations)	15.4 (6 stations) 17.2 (8 stations)
Other Markets	2.7	1.8
Total All Markets	20.7	19.0

Note: The 6 stations aggregate was taken from the survey reported in Table 19. Adjustments were made to the figures to add in the effect of one Burlington/Plattsburg station in 1975 and 1982. One additional Buffalo station had an impact in the 1982 figures, but virtually no effect in 1975.

in the case of Canadian advertising on U.S. stations, virtually all of these commissions go to Canadian based firms. Thus, if we want to calculate the potential revenue that has been lost by U.S. broadcasters and repatriated to Canada, we should base the calculations on net revenues. We obtained net revenues for U.S. markets by multiplying the figures in Table 20 by 0.8.

The next step in calculating repatriated revenues requires the estimation of potential revenues for 1982 under the assumption that Bill C-58 and other policies were not in place. Table 21 shows potential or projected net revenues calculated according to the two techniques already described: the market share approach and the media cost approach. The media cost projection assumes that border station revenues for the three markets would have grown at the same rate as our TV advertising cost index for Canada. Since the volume, as well as the price, of advertising has grown, the media cost approach provides a rather low estimate of what advertising receipts would be in 1982 if the environment had not changed.

The estimated actual total revenues of Canadian stations and U.S. stations in each market are shown in the first two columns of Table 21 for 1975 and 1982. The third column shows projected revenue for 1982, calculated by multiplying the total actual advertising revenue in 1982 by the border percentage for 1975. Thus, while the actual net revenues of Buffalo stations in 1982 were estimated at $4.7 million, they would have been $21.9 million if the Buffalo stations had maintained the market share they had in 1975. The three markets together would have had net revenues of $45.4 million, instead of the estimated actual $13.8 million.

Table 21

Private Sector Net TV Advertising Revenues in Three Markets
Of Canadian and U.S. Stations, Actual and Projected, 1975 and 1982
(Millions of Canadian $'s)

	Estimated Revenues				Projected Revenues 1982		1982 Revenue Foregone Based on	
	1975		1982		Constant Market Share (a)	Media Cost Increase (b)	(a)	(b)
Buffalo	7.1	13.2%	4.7	2.8%	21.9	16.8	17.2	12.1
Toronto/Hamilton	46.5	86.8%	161.4	97.2%				
Total	53.6		166.1					
Burlington/Plattsburg	2.2	6.5%	1.8	2.0%	5.7	5.2	3.9	3.4
Montreal	31.7	93.5%	86.1	98.0%				
Total	33.9		87.9					
Bellingham	5.0	36.2%	7.3	14.9%	17.8	11.9	10.5	4.6
Vancouver	8.8	63.8%	41.8	85.1%				
Total	13.8		49.1					
Total Revenue-3 U.S. Markets	14.3		13.8		45.4	33.9	31.6	20.1

Source: Canadian revenue data were provided by the Department of Communications. The U.S. data were compiled by the authors as explained in earlier tables. The 1982 projected revenues were obtained in two ways: (1) by assuming that the 1975 market shares would have applied to the 1982 total revenues and (2) by applying the rate of growth in a national TV cost index between 1975 and 1982 to the 1975 amount for each set of U.S. stations.

Table 22

Net Canadian TV Advertising Revenue of U.S. Border Stations: Estimated, Projected and Projected Losses for 1982 (millions of Canadian $)

	Estimated Revenues		Projected 1982 Revenues Based on		1982 Revenues Foregone Based on	
	1975	1982	(a)	(b)	(a)	(b)
Three Major Markets (see Table 21)	14.3	13.8	45.4	33.9	31.6	20.1
Other Markets	2.2	1.4	7.0	5.2	5.6	3.8
Total	16.5	15.2	52.4	39.1	37.2	23.9
Total (1975 $)*	16.5	8.0	27.7	20.7	19.7	12.6

a) constant market share approach

b) media cost increase approach

* Inflation adjustment based on Canadian CPI

Table 22 includes our estimated and projected revenues for other border markets, as well as the three major markets. The Other Markets figure for 1975, $2.2 million, was increased by the TV cost index and a market share factor as well. To do the latter we assumed that revenue in the "Other Markets" category would have grown at the same rate on average as potential revenue in the three major markets.

Based on constant market shares, net advertising revenue would have climbed to $52.4 million, as compared to an estimated actual revenue of $15.2 million. The difference, $37.2 million, is an estimate of the revenues foregone by the border stations due to the changed environment. The corresponding figure based on the media cost approach is $23.9 million.

Recall again that revenues foregone by the border stations are due to the combination of Bill C-58 and simultaneous substitution. Thus the next step is to account for the portion of the foregone revenues that can be attributed to increased simulcasting between 1975 and 1982. As already noted, a time series on simulcasting revenues does not exist. In the absence of a better statistical base, we depend on the Mediastats estimate that the 34 stations simulcasting in 1980 earned an extra $20 million of gross revenue due to this practice.* The equivalent net revenue is $16 million. To account for possible growth since 1980, we increase this number by the 31.5 percent increase in total net advertising revenue between 1980 and 1982. On this basis we assume that the contribution to net revenue due to simulcasting in 1982 was $21.0 million.

It is more difficult to estimate what was the simulcasting contribution to 1975 revenue. There is fragmentary evidence that suggests there were large increases between 1975 and 1982. For example,

*See Table 6.

the total number of simulcast hours in Toronto rose 66 percent over the four years ending 1981, according to a Mediastats estimate. Consequently, it is probably safe to assume that the simulcast revenue rose at least 75 percent for all Canadian TV broadcasters between 1975 and 1982. As a result, we estimate that the net simulcast related earnings for Canadian broadcasters in 1975 amounted to about $12 million (or $15 million in gross terms).

Thus, between 1975 and 1982 we estimate an increase of $9 million dollars (21 m. - 12 m.) of net annual revenue due to simulcasting. It is questionable, however, to argue that this amount was totally lost by border broadcasters since they of course sell their spots in the U.S. anyway. One cannot know whether Canadian advertisers would have advertised accordingly more on border stations if they had not been able to take advantage of their audiences by way of simulcasting. It is also possible, and likely in many cases, that Canadian advertisers simply could not have bought the equivalent spots on border stations. At the same time, some portion of the revenue surely should be considered as diverted due to simulcasting. Suppose, that is, that Bill C-58 had not been passed, but that simultaneous substitution was still allowed. Even with the tax deduction possible, Canadian advertisers would have decreased their purchases on U.S. stations.

Without any further knowledge on specifically how to treat the incremental increase in the simulcasting environment, we decided, in order to illustrate the possible effects, to subtract two amounts to account for simulcasting: one-half of the increase in the net simulcast revenues between 1975 and 1982, $4.5 million, and the full increase of

$9 million.

Based on this, and using the market share approach, the portion of the $37.2 million of foregone revenues due to Bill C-58 (including that part of its effect due to good corporate citizenship) would range from $28.2 million to $32.7 million.

Looking at the question from the viewpoint of Canadian broadcasters, it is interesting to compare total simulcasting revenues for 1982 with our estimate of the effect of Bill C-58. That is, from a public policy perspective, were the policies in the same category of importance? According to our rough estimates simulcasting brought in extra net revenues of $21 million in 1982. Bill C-58 added between $28 million and $33 million.

The separate and combined impacts of simulcasting and Bill C-58 in 1982 are presented in Table 23 relative to private station profits, net revenues, and total net revenues for all TV stations, including the CBC. Thus the Bill C-58 effect fell in the range of 19.7 percent to 22.9 percent of TV broadcasters profits in 1982, and about 4.2 percent to 4.9 percent of net advertising revenues. Bill C-58 resulted in a 1982 gain in total advertising revenues, including CBC revenue, of from 3.6 percent to 4.2 percent. When the Bill C-58 effect is combined with the simulcasting revenue gains, the total TV broadcasting system's revenues were from 6.3 percent to 6.9 percent greater in 1982 than they would otherwise have been.

Table 23

Estimated Effects of Simulcasting and Bill C-58 On
Total Canadian Net TV Revenues In 1982
(Millions of $'s)

Private Net Advertising Revenues		$ 670.8
Total Revenues, Including CBC		$ 779[e]
Total Profits (Private Stations-Pre-tax)		$ 142.9
Total Profits (Private Stations-After-tax)		$ 75.4
Revenue Gains Related to Simulcasting		$ 21
Revenue Gains Related to Bill C-58		$ 28.2 to $32.7
Simulcast Revenues As % of	Total Profits (pre-tax)	14.7%
	Net Private Revenues	3.1%
	Total Net Revenues	2.7%
Bill C-58 Revenues As % of	Total Profits (pre-tax)	19.7% - 22.9%
	Net Private Revenues	4.2% - 4.9%
	Total Net Revenues	3.6% - 4.2%
Combined Policies As % of	Total Profits (pre-tax)	34.4% - 37.6%
	Net Private Revenues	7.4% - 8.0%
	Total Net Revenues	6.3% - 6.9%

12. A Compromise Tax Proposal

While this study has considered alternative ways to achieve the objectives of Canadian broadcasting policy, (see Section 4, Forms of Protection, above) it has not been specifically concerned with the progress of the border station debate in the context of current Canadian-American relations. While it is beyond the scope of the study to comment on how the dispute might be resolved at the inter-governmental level, at this point in response to a request from the Department of Communications, we consider a specific proposal. A group of U.S. border stations have suggested that Section 19.1 be amended to require the pro-rating of tax deductibility on American stations according to a formula based on the distribution of audience. A Canadian buying a spot on a border station would be able to deduct a portion of the cost equal to the percentage of the station's audience that is in the U.S.

The theoretical rationale for this is presumably an assumption that, since the advertising is seen by the total U.S. plus Canadian audience watching the station, the advertiser intends that to happen. Bill C-58 contains an exemption for advertising primarily directed at U.S. audiences. Why make this an all or nothing exemption? Instead pro-rate the exemption according to how much U.S. audience and how much Canadian audience watches the spot.

While the theoretical rationale is not strong (since it ignores the typical advertiser's primary concern with reaching a Canadian audience and likely unwillingness to pay the going rate to reach the U.S. audience that comes with it), such a suggestion may be acceptable to the opponents of Bill C-58 merely as a compromise. Our concern here, is the prospective

effects of this compromise proposal.

Under Section 19.1 as it now stands, we have shown that the prices of advertising spots on U.S. border stations are lower than they would otherwise be, though not necessarily by the full amount of the tax deduction, If pro-rating were to be introduced it would cause the prices to rise again but not all the way back to their original level. (This assumes, of course, that the effects of inflation and other such changes are corrected for.) Suppose that a border station has 75 percent of its audience in the U.S. and 25 percent in Canada. In principle, 75 percent of the original price reduction would be restored. In fact, various factors could cause the border station spot price to rise by more or less than the pro-rated portion, For instance, current market conditions might lead a border station to increase rates by slightly less than the pro-rated tax effect in order to increase the station's competitive edge relative to Canadian stations,

According to BBM and Nielson data for the Autumn 1982, the total viewing share of the 41 stations broadcasting into Canada was about 76.3 percent in the U,S. and 23.7 percent in Canada. There is, however, large variance across markets and individual stations. The data in Table 24 show the U.S. audience shares for stations in the three largest markets. The three border stations that serve the Montreal market have an average U.S. audience share of 41.6 percent, the Buffalo stations 53.4 percent and KVOS in the Vancouver market has only 22.6 percent of its audience in the U,S. Within the Buffalo market the U,S. audience share varies from 28,8 percent to 60.6 percent.

Thus it is evident that this compromise proposal will have

Table 24

Canadian And U.S. Audiences In The Three Principal Markets*

Cdn./U.S. Market	Canadian Audience (000's)	US Audience (000's)	US % of Total
Montreal/Burlington-Pl.			
WPTZ	44	23	34.3%
WCAX	37	42	53.0%
WEZF	27	12	30.8%
(Total-3 stations)	108	77	41.6%
Toronto/Buffalo			
WIVB	61	86	58.5%
WGR	73	76	51.0%
WKBW	67	103	60.6%
WUTV	47	19	28.8%
(Total-4 stations)	248	284	53.4%
Vancouver/Bellingham			
KVOS	41	12	22.6%
(Total-1 station)	41	12	22.6%
(Total - 41 stations)	869	2794	76.3%

*Significantly viewed stations as defined by BBM and Nielson. Audience refers to the number of persons who watch the surveyed signal in the U.S. or Canada at any time during the survey week in the fall of 1982.

quite different effects in different markets. The stations with the smallest U.S. audiences will benefit least from the proposal and the Canadian stations that are their competitors will be hurt least by it. For example, if the price and revenue effects worked out exactly according to the pro-rated portions of the tax deduction to be allowed to Canadian advertisers, KVOS Bellingham, WUTV Buffalo and WPTZ Plattsburgh would recover 23, 29 and 34 percent of their lost annual revenues respectively. On the other hand, the three large Buffalo broadcasters would recover revenues in the 50 to 60 percent range. Of these stations in the three major markets, KVOS had the largest amount of projected lost revenue, but would benefit least in proportional terms.

On the Canadian side, there would be a correspondingly unequal distribution of the effect of the compromise proposal. For instance, Vancouver stations would suffer less than average due to the compromise, the Toronto broadcasters more. There are costs from the Canadian point of view due to the cumbersomeness of the scheme. The deductible allowances will be subject to change due to changes in audience shares. Revenue Canada, advertisers, agencies and others would have to contend with the complications due to differential tax deductions in different markets. These complications could also have the effect of lessening the total amount of advertising that would return to the U.S. stations. One possible alternative would be to accept a single benchmark year for the audience shares; e.g. 1975 or the year in which the amendment to the tax act is made.

The proposal also has an odd effect on the competitive relations between Canadian and U.S. stations. Suppose a Canadian station employs

a successful competitive strategy, through better programming and pricing, to take Canadian audience away from a border station. It would then find that part of its competitive edge is removed when the deductibility ratio is updated, since the border station will have a bigger share of its audience in the U.S. than before.

The complexity of the scheme, its arbitrariness (despite the hypothetical argument on which it is based), the possibility of undesirable effects on the process of competition, and the differential way in which it will affect Canadian stations make it less than attractive. If a compromise is actually desired, one that pro-rates the benefits of Bill C-58 on an equitable basis for all the participants can be easily defined. That is, if pro-rating is the solution it can be done more efficiently and equitably than this proposal suggests. It seems implausible that, if the federal government desired to remove some of the advantages of Bill C-58 to Canadian broadcasters, it would choose to do so on such an uneven basis in terms of its effects on both sides of the border.

13. Concluding Remarks

This study has demonstrated that Bill C-58 and the practice of simultaneous substitution have contributed to the fulfillment of Canadian broadcasting policy. According to our rough estimates, the tax advantages due to Bill C-58 generated from $28 million to $33 million of net revenues for Canadian television braodcasting in 1982. The requirement that cable systems carry out the simultaneous substitution of programs as requested by the broadcasters added a further $21 million of net advertising revenue. The revenue effects of the two policies combined amounted to 6-7 percent of total broadcasting revenues and about 35 percent of pre-tax profits of the private stations. Thus these two policy instruments of the Federal Government and the CRTC have contributed to the financial health and, at the margin, to the survivability of Canadian television stations.

In our view Bill C-58 should be seen as part of a complex picture shaped by industry characteristics and government policies. Given the regulations on Canadian content, the relatively small total audience, which makes it difficult to cover the cost of large scale program productions, consumer tastes for American television and other aspects of the industry, policies were designed in the early 1970's to help Canadian broadcasters. Bill C-58 became a key element of support in an effort to cope with the peculiar economics of Canadian television. That it has provided such support has been demonstrated, among other ways, by the evidence that the Bill sharply reduced the flows of Canadian advertising revenue to U.S. border stations.

Canadian critics of Bill C-58 predicted that it would result in a tightening of available advertising time and spot prices in large urban

markets, causing local advertisers to be deprived of the use of television. While both prices and volumes have been affected for particular stations (by both Bill C-58 and simulcasting), the development of new independent stations has minimized the adverse effects on local advertisers. The older larger stations rely more on national advertising, local spots play a larger role for the new outlets. Although it is not possible to identify precisely the revenue gains of specific Canadian stations, we believe that both old and new stations have benefitted from Bill C-58, the older stations through higher rates, the new ones through higher rates and expanded volumes.

Looking at the three largest television markets, we estimated revenue losses in 1982 for the corresponding border broadcasters due to C-58 and simulcasting combined. Using our preferred assumptions (see Section 11, parts (c) and (d)), the revenue losses amounted to $17.2 million for the Buffalo stations, $3.9 million for the Burlington/Plattsburg stations and $10.5 million for KVOS, Bellingham. If one assumes that all of the lost revenues converted into revenue gains for Canadian broadcasters, the Toronto, Montreal and Vancouver stations benefitted by equal amounts respectively.

Our aggregate estimates of revenue gains due to Bill C-58 ($28 - 33 million in net revenues in 1982) can be compared with rough estimates that some broadcasters provided by way of our interview survey. Fifteen of the broadcasters contacted estimated for us the amount by which their total revenues would be reduced if Bill C-58 were repealed and if nothing else were changed. Seperately they predicted revenue losses ranging from zero to 25 percent. Applying their percentages to Department of Communications statistics on actual advertising revenues for 1982, the

aggregate amount of revenue lost by these 15 stations would have been $32.6 million in 1982. Since there are many more stations potentially affected by Bill C-58, this amount underestimates the broadcasters' views of the value of the policy. Thus their view of the importance of Bill C-58 for their industry is considerably higher than our own estimate of $28 - 33 million in 1982.

APPENDIX 1:

THE ESTIMATED DOLLAR VALUE CONTRIBUTION OF SIMULTANEOUS PROGRAM SUBSTITUTION TO CFTO-TV AND CHCH-TV

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July 14, 1983

This analysis, for Arthur Donner, provides data on two Toronto-Hamilton TV stations to demonstrate the possible dollar value contribution of simultaneous program substitution to a TV station's total revenues.

The following assumptions were made:

A) The BBM three-week spring 1983 survey was used to establish a typical period to assess the contribution of substitution to the published audience estimates.

B) Although CRTC regulations allow six 30-second commercials per one-quarter hour period only five were used in the calculations in order to be conservative in estimating the overall value of substitutions.

C) Because of summer and volume discounts, the three-week survey estimates were only multiplied by 12 to arrive at a yearly figure.

The results of this analysis indicate that the dollar value contribution of simulcast programs for CFTO-TV was $2,552,803 which is 18.3 percent of the value of their simulcast properties. For CHCH-TV, simulcast programs contributed a dollar value of $4,493,547 which is 29.1 percent of the value of the programs.

The dollar value contribution of simulcast programs to the total estimated yearly revenue was for CFTO-TV $2,552,803 or 5.8 percent and for CHCH-TV was $4,493,547 or 11.0 percent.

TABLE 1

ESTIMATED DOLLAR VALUE CONTRIBUTION

OF

SIMULTANEOUS PROGRAM SUBSTITUTION

PROGRAM	DAY	TIME	SRV WKS	ALL PERSON 2+ STN TOTL (00)	ALL PERSON 2+ SIML CAST (00)	SIMUL % TOTAL	30 SEC RATE $	NO OF COMMERCIALS PGM	NO OF COMMERCIALS SURVEY	NO OF COMMERCIALS PER YEAR	$ VALUE/YEAR TOTAL	$ VALUE/YEAR SIMUL PORTION
CFTO-TV TORONTO												
Another World	M-F	200p- 300p	1-3	1195	180	15.06	415	20	300	3600	1494000	224996
Bring Em Back	Sat	800p- 900p	1	1406	153	10.88	1175	20	20	240	282000	30682
Close Encount	Mon	800p-1100p	3	6971	552	7.92	1175	60	60	720	846000	67003
Dukes Hazzard	Fri	800p- 900p	1+2	3994	764	19.13	1175	20	40	480	564000	107893
Dynasty	Wed	1000p-1100p	2+3	5592	844	15.09	1175	20	40	480	564000	85108
Falcon Crest	Fri	1000p-1100p	1+2	3927	891	22.69	1175	20	40	480	564000	127972
Fall Guy	Wed	900p-1000p	2+3	2884	388	13.45	1175	20	40	480	564000	75858
General Hosptl	M-F	300p- 400p	1-3	1872	444	23.72	415	20	300	3600	1494000	354377
Hart To Hart	Tue	1000p-1100p	1-3	3818	560	14.67	1175	20	60	720	846000	124108
It Takes Two	Thu	930p-1000p	1+2	1457	408	28.00	1175	10	20	240	282000	78960
Knight Rider	Fri	900p-1000p	1-3	5029	1083	21.54	1175	20	60	720	846000	182228
Magic Planet	Thu	800p- 900p	3	2763	202	7.31	1175	20	20	240	282000	20614
Magnum	Thu	800p- 900p	1+2	5537	904	16.33	1175	20	40	480	564000	92101
Matt Houston	Sun	800p- 900p	1-3	4016	483	12.03	1175	20	60	720	846000	101774
Mov/Star Trek	Sun	900p- Mdnt	1	6214	425	6.84	1175	60	60	720	846000	57866
Peoples Choice	Thu	900p-1100p	3	4849	1275	26.29	1175	40	40	480	564000	148276
Peoples Court	M-F	500p- 530p	1-3	1231	481	39.07	415	20	300	3600	1494000	583706
Square Pegs	Mon	800p- 830p	1	3286	809	24.62	1175	10	10	120	141000	34714
Voyagers	Sun	700p- 800p	1-3	3409	220	6.45	1175	20	60	720	846000	54567
											13929000	2552803
CHCH-TV HAMILTON												
"A" Team	Tue	800p- 900p	1+3	4353	1923	44.18	1000	20	40	480	480000	212064
Chips	Sun	800p- 900p	2+3	4130	874	21.16	1000	20	40	480	480000	101568
Days Of Lives	M-F	100p- 200p	1-3	1087	327	30.08	525	20	300	3600	1890000	568512
Entertn Tonite	M-F	700p- 730p	1-3	2475	1188	48.00	1000	10	150	1800	1800000	864000
Event: Jazz	Sat	900p-1130p	2	4070	593	14.57	1000	50	50	600	600000	87420
Event M.A.D.D.	Mon	900p-1100p	3	4943	894	18.09	1000	40	40	480	480000	86832
Event Nite Brd	Mon	800p-1100p	2	2895	585	20.21	1000	60	60	720	720000	145512
Event SP Bulle	Sun	900p-1100p	3	4120	636	15.44	1000	40	40	480	480000	74112
Event Who Will	Mon	900p-1100p	3	7947	1667	20.98	1000	40	40	480	480000	100704
Hee Haw	Sat	700p- 800p	1-3	2002	597	29.82	1000	20	60	720	720000	214704
Hill St Blue	Thu	1000p-1100p	1-3	5298	1367	25.80	1000	20	60	720	720000	185760
Little House	Mon	800p- 900p	3	3239	1288	39.77	1000	20	20	240	240000	95448
One Life Live	M-F	200p- 300p	1-3	798	273	34.21	525	20	300	3600	1890000	646569
Powers M Star	Fri	800p- 900p	1-3	3115	805	25.84	1000	20	60	720	720000	186048
Rips Believe	Sun	700p- 800p	1-3	3207	575	17.93	1000	20	60	720	720000	129096
Simon & Simon	Thu	900p-1000p	1+2	4579	1270	27.74	1000	20	40	480	480000	133152
St Elsewhere	Tue	1000p-1100p	3	2619	853	32.57	1000	20	20	240	240000	78168
T.J. Hooker	Sat	800p- 900p	1+3	3173	526	16.58	1000	20	40	480	480000	79584
Trapper John	Sun	1000p-1100p	1	2608	685	26.27	1000	20	20	240	240000	63048
USFL Football	Sun	300p- 615p	2	2193	545	24.85	550	65	65	780	780000	193830
USFL Football	Sun	130p- 445p	3	1428	453	31.72	550	65	65	780	780000	247416
											15420000	4493547

TABLE 2

ESTIMATED YEARLY REVENUE

BASED ON TIME PERIOD

MONDAY-SUNDAY 800AM-1100PM

STATION	TIME PERIOD		30 SEC RATE $	NO OF 1/4 HRS	COM/ 1/4 HR	WKS/ YEAR	$ VALUE PER YEAR
CFTO-TV	M-F	800a- noon	125	80	5	36	1,800,000
	S+S	800a- noon	225	32	5	36	1,296,000
	M-F	noon- 100p	225	20	5	36	810,000
	M-F	100p- 600p	415	100	5	36	7,470,000
	S+S	noon- 400p	275	32	5	36	1,584,000
	S+S	400p- 600p	415	16	5	36	1,195,200
	M-Su	600p-1100p	1175	140	5	36	29,610,000
TOTAL				420			43,765,200
CHCH-TV	M-Sa	800a-1000a	100	48	5	36	864,000
	Sun	800a-1230p	325	18	5	36	1,053,000
	M-F	1000a-1230p	325	50	5	36	2,925,000
	Sat	1000a- 500p	100	28	5	36	504,000
	Sun	1230p- 700p	550	26	5	36	2,574,000
	M-F	1230p- 100p	325	10	5	36	585,000
	M-F	100p- 500p	525	80	5	36	7,560,000
	M-Sa	500p- 700p	525	48	5	36	4,536,000
	M-Su	700p-1100p	1000	112	5	36	20,160,000
TOTAL				420			40,761,000

SOURCE: July 1983 Canadian Advertising Rates And Data.

APPENDIX 2: Survey Letter to U.S. Border Stations

Dear Sir:

In 1976 the Canadian Government passed a bill that removed the right of Canadian firms to claim a tax deduction for television advertising aired on stations along the U.S.-Canadian border. Shortly after, a study for the Department of Communications attempted to estimate the impact of this amendment in Canadian tax and broadcasting law.

That study is now being updated. In order to understand the effect of the amendment in the longer term, and to deal with questions that have been raised about it in both countries, it is essential to have an accurate view of the allocation of advertising funds in Canadian and U.S. markets. As one of the stations affected by the present policy, could you aid us in constructing the estimates that are needed?

Answers to only three questions will help to fill an important gap in our information:

(1) How much Canadian advertising revenue has your station been receiving annually since the law was amended?

(2) Based on your careful view of the market involved, how much Canadian revenue do you think your station would have received in 1982 if the advertising tax deduction had not been removed?

(3) Do you think your Canadian advertising revenue has been diminished by the simultaneous program substitution carried out by Canadian cable companies? If so, an estimate of the revenue lost in 1982 due to this practice would be appreciated.

If you are able to provide these numbers, fill in the table on the attached page and return it to us in the enclosed envelope. Even if data are not available for all of the years in the table, please provide them where possible (e.g., an estimate for your most recent accounting year would be helpful).

Thank you for your consideration of our request and for any information that you can provide. If you wish to discuss this further, we may be contacted at the above mailing address or by telephone.

Yours sincerely,

AD/zc
ENCL.

Arthur Donner.

ARTHUR DONNER CONSULTANTS INC.
307 RICHVIEW AVENUE
TORONTO, ONTARIO M5P 3G4
483-5131

ACTUAL REVENUE
FROM CANADIAN ADVERTISING
(including commissions)

1975	US $ _____
1976	_____
1977	_____
1978	_____
1979	_____
1980	_____
1981	_____
1982	_____

Estimate of 1982 revenue that would have occurred if Canadian advertisers had been able to claim a tax deduction: $ _____

Estimate of 1982 revenue that would have occurred if the substitute of your signals on Canadian cable companies had not occurred: $ _____

Any additional information on the effects of either C-58 or simulcasting on the operation of your business would be appreciated.

Station _____

Contact Person _____

Telephone Number _____