February 14, 2012

The Hon. Dwight Duncan
Minister of Finance
7 Queen's Park Circle
Frost Building South
7th Floor
Toronto, Ontario M7A1Y7

Dear Minister:

Thank you for the opportunity to submit the Canadian Independent Music Association's (CIMA) pre-budget recommendations as they relate to modernizing the ***Ontario Sound Recording Tax Credit***.

About CIMA

By way of background, CIMA represents more than 180 Canadian companies and professionals engaged in the worldwide production and commercialization of Canadian independent music, who in turn represent thousands of Canadian artists and bands.

CIMA's membership consists of ***Canadian-owned*** companies and representatives of Canadian-owned companies involved in every aspect of the English-language music and music-related industries. They are exclusively small and medium sized businesses which include: record producers, record labels, publishers, recording studios, managers, agents, licensors, music video producers and directors, creative content owners, artists and others professionally involved in the sound recording and music video industries.

Some of the great Canadian independent artists and bands represented by our members include Rush, Bruce Cockburn, Sarah McLachlan, Broken Social Scene, Feist, The Trews, Tokyo Police Club, K'Naan, Luke Doucet, Blue Rodeo, City and Colour, Chromeo, K-OS, Metric, Diamond Rings, Lights, Our Lady Peace, Said The Whale, Jenn Grant, Dan Mangan, Chilly Gonzales, Delhi to Dublin, Canadian Brass and Saidah Baba Talibah, to name but a few.

To put our industry's size in perspective, the Canadian independent music sector – taken as a bloc – is one of the largest in terms of sales in this country, second only to Universal Music Canada. According to Nielsen SoundScan sales figures, the independent sector accounts for approximately 24 percent of all music sales in Canada – larger than EMI (12 percent) and Warner Music (10 percent) sales combined, and greater than Sony Music (16 percent).

For 36 years, CIMA has dedicated its efforts to developing business opportunities through an international network of business contacts in the music and entertainment industries and in the associated media such as film, TV, new media and other users of music products. CIMA's mandate is to ensure the long-term development of the Canadian-owned music sector and to raise the profile of Canadian independent music both in Canada and around the world.

In short, our members are the owners and operators of small businesses who invest in the creation of intellectual property that spurs economic benefits in terms of jobs, increased GDP, positive contributions to our nation's trade balance, and are an integral component of Canada's culture as expressed through music. As Canada's economic sectors continue to evolve, CIMA believes that the creation and protection of intellectual property is one of the few potential growth areas for our economy, particularly through exports.

Background

Through countless research studies and submissions over the years from such groups and associations as the Conference Board of Canada, Statistics Canada, the Canadian Conference of the Arts, Heritage Canada, CIMA, Music Canada (formerly CRIA), IFPI and many others, it is an established fact that the creative sector contributes

- a positive effect on the development of local communities and social networks
- a net return on investment in terms of GDP and jobs
- a strong social and cultural identity for Canada, and
- a strong leverage for economic development and revitalization of communities

Consider that, according to the Conference Board of Canada, the creative economy in general contributes a significant economic footprint, which measured just over $84 billion, or 7.4 percent of Canada's GDP, in 2007. Further, the Conference Board stated in its*Valuing Culture* report:

- for every $1 of real value-added GDP produced by Canada's cultural industries, roughly $1.84 is added to the overall real GDP
- exported cultural goods and services amounted to approximately $5 billion in 2007, or about 1 percent of total Canadian exports to the world
- Canada's cultural sector plays a critical role in attracting people, businesses and investment; stimulating creativity and innovation; and distinguishing Canada as a dynamic and exciting place, where people can celebrate their heritage and realize personal and professional fulfilment
- cities that offer a high quality of life attract and retain firms and workers in the knowledge-intensive and creative fields
- cultural activities generate substantial consumer spending on culture goods and services. In addition, they generate significant indirect spending effects that are realized through related spending on, for example, restaurants, hotels and transportation services. Indirect benefits are also derived from culture employees spending their earnings, business owners spending (or investing) the profits they generate, and government spending the additional tax revenues generated by those wages and profits. In turn, these purchases lead to further increases in employment, wages, income and tax revenues that can be felt across a wide range of industries

Specifically, Canada's independent music industry contributes revenues, wages and jobs to the provincial and national economies. In many respects, the music industry is a key component of Ontario's entertainment and creative cluster, which is also an integral element of the digital media, information and communications industry.

The music industry is composed of a supply chain that includes labels, publishers, distributors, merchandise, booking agents and managers, tour promoters, retailers, musicians/performers, producers, engineers, live venues, studios, post-secondary music training institutions, etc. Thus, the music industry has numerous spin-offs, which amplify the economic impact of the sound recordings and music content it produces. With these creative and innovative spin-offs, social importance, and trickle-down industries in mind, the music industry should be viewed through a wider lens than merely, for example, assessing the income of the individual artists and independent labels.

Indeed, the music industry is arguably the foundation of most of the entertainment and creative clusters. Whether it is a television production, a film or video game, mobile app or ringtone, music will be embedded in the medium.

Music is a product unto itself. Moreover, it is increasingly seen as an active component to drive audiences and users to interactive digital media (eg: electronic games) and as part of the growing use of video on the Internet. Music should also be considered important within the context of innovation and the transition of individual creative industries to the digital world.

In other words, Canada's, and in particular Ontario's independent music industry is an important and fundamental foundation for the cultural sector, and therefore plays an integral role in the nation's and provincial economies.

Recommendations

There are a number of ways that Ontario government policies and investments can contribute to a vibrant independent music sector. Indeed, it is the government's stated intention that it is seeking policies and programs that will serve to achieve a sustained economic recovery, create quality jobs, not increase taxation and lead to a balanced budget. It is CIMA's view that continued strategic investment in the independent music sector will indeed positively contribute to a growing economy.

CIMA is recommending that the government ***modernize its Ontario Sound Recording Tax Credit (OSRTC) regime***, in an effort to better align it with the realities and needs of today's business plans and structures within the Canadian-owned independent music sector. These recommendations are a cost-effective way of providing much-needed and valuable assistance to the music sector without raising taxes or impacting the treasury; in fact, the OSRTC is proven to provide a positive boost to the provincial economy in terms of GDP growth and jobs.

CIMA recommends that the Government of Ontario modernize the Ontario Sound Recording Tax Credit by:

1. Increasing the tax credit rate so that it corresponds with tax credit rates for the other creative sectors (ie: 30, 35 or 40 percent from its current level of 20 percent).

2. Increasing the eligibility of international marketing expenditures to match domestic expenditures (ie, 100 percent eligible).

3. Including other specific costs as eligible expenditures, e.g. touring, manufacturing, and rights tracking.

4. Providing some form of collateral or guarantee on OSRTC, to facilitate cash flow financing.

5. Providing advances on tax credits to help established companies.

6. Reducing any real or perceived administrative burdens with the OSRTC application process.

Note: *A full analysis of the recommendations can be found in the accompanying research document,* ***Analysis of the Impact of the Ontario Sound Recording Tax Credit****, prepared for CIMA by Toronto/Ottawa-based Nordicity in January 2011.*

Ontario Sound Recording Tax Credit

Since 1999, the music industry in Ontario has enjoyed the benefit of the highly successful Ontario Sound Recording Tax Credit (OSRTC). Administered by the Ontario Media Development Corporation (OMDC) and the Ontario Ministry of Finance, the tax credit has consistently provided approximately $1.5 million in annual financial support for sound recording projects.

The OSRTC is a refundable tax credit available to eligible Ontario-based sound recording companies, for up to 20 percent of the eligible production and marketing expenditures that they incur for the development and promotion of emerging artists.

Eligibility requirements dictate that a company must have been in operation in Ontario for at least 12 months, have earned more than 50 percent of its taxable income in Ontario, and demonstrate that more than 50 percent of its business was in the sound recording industry. Eligible expenses include artists' royalties, musician session fees, graphics, digital scanning; costs of producing a music video directed by a Canadian or made at an Ontario production facility; and direct marketing expenditures.

This tax credit is vital for the independent music industry, as these companies are***exclusively small and medium sized enterprises which are particularly sensitive to cash flow issues***.

However, the current structure and level of the tax credit do not wholly reflect the realities or needs of the independent music sector in Ontario. It is CIMA's position, based on the extensive research of Nordicity and communications from our membership that the OSRTC is in dire need of modernization, in terms of raising the level of the credit as well as expanding the eligibility requirements for production and marketing. A modernized tax credit regime will serve to boost the economic viability of the independent music industry with corresponding positive spinoffs to the Ontario economy.

Recommendation 1

1. Increase the tax credit rate so that it corresponds with tax credit rates for the other creative sectors in Ontario (ie: 30, 35 or 40 percent from its current level of 20 percent).

Currently, the OSRTC is the lowest of several tax credits given to the creative industries in Ontario, with book publishing receiving a 30 percent credit, film/television at 35 percent and interactive digital media at 40 percent. Aside from the parity issue, CIMA's economic analysis shows that the sound recording tax credit can increase to 30 percent without a negative impact on the provincial treasury, and only a negligible to modest impact should it be raised to 35 percent or 40 percent. Rather, increasing the tax credit from its current level of 20 percent will lead to a significant increase in revenues for the industry, increase GDP, wages and indeed jobs.

The Ontario government collected $1.27 in revenues for every dollar it invested in the music industry through the OSRTC. As such, there appears to be room to increase the tax credit and maintain a fiscal breakeven position for the Province, regardless of the existence of any knock-on effect from a tax credit rate increase, according to Nordicity's research.

Recommendations 2 & 3

2. Increase the eligibility of international marketing expenditures to match domestic expenditures (ie, 100 percent eligible).

3. Include other specific costs as eligible expenditures, e.g. touring, manufacturing, and rights tracking.

Nordicity has calculated that the OSRTC leads to a $21.7 million increase in the province's GDP annually, $16.5 million in additional wage income and has created more than 500 jobs. In addition, the multiplier effect provides further stimulation on the province's economy. "Our research indicates that…one-third of OSRTC supported projects would not proceed without OSRTC financial support. Furthermore, our analysis indicates that the tax credit helps companies expand their marketing expenditures and sales. We found that each dollar of marketing expenditure leads to two more dollars of music label revenue."

While this is good news, and reflects the positive attributes of the OSRTC, the fact is the industry has evolved since the introduction of the tax credit, with a much stronger business focus and reliance on international marketing and touring, along with rights tracking in order to identify the various royalty streams due to the artists and the businesses representing them. Currently, only 50 percent of international marketing expenses is eligible for the tax credit.

Yet, program statistics as well as the results of Nordicity's research show that marketing – and out-of-province marketing in particular – is growing in importance. The share of OSRTC expenditures comprised by marketing activities rose from 47 percent to 59 percent between 2006-07 and 2009-10. This is not surprising since 69 percent of respondents of Nordicity's survey of CIMA members reported that they use their tax credit to increase their marketing. The number of projects with out-of-province marketing expenditures jumped to 43 percent in 2009-10 from 11 percent in 2006-07. Music labels are seeking to maximize the value of the product they create. This often requires labels to hire foreign public-relations and radio-relations professionals to help them promote their sound recordings internationally. Therefore, with a greater proportion of their resources being dedicated to out-of-province activities – which generate a large return on investment – CIMA believes that the OSRTC eligibility requirements governing these expenditures must be expanded.

According to CIMA's report, the success of the OSRTC was evaluated in terms of the impact it has on the long-term development of Ontario's sound recording industry. The OSRTC leads directly to the creation and marketing of new sound recordings, and thereby generates impacts on the Ontario economy when the production and marketing budgets are spent in Ontario. However, for the OSRTC to have a positive impact on the sound recording industry in the long-run, it must affect sound recording companies' ability to grow their revenues, diversify their revenues away from slow-growth segments, lead to more artist signings and foster greater exports.

Nordicity found more intensive users of the OSRTC had higher rates of revenue growth, a larger share of revenues from digital platforms and better revenue diversification across lines of business. More intensive use of the OSRTC was also associated with higher rates of artist signings and higher rates of international touring. However, despite this higher rate of international touring, there was no positive relationship between OSRTC use intensity and international revenues (share of total revenues from outside of Canada). The absence of a correlation between OSRTC use intensity and international sales may be related to out of-province marketing and promotion expenditures being discounted by 50 percent in the OSRTC guidelines.

While Ontario sound recording companies can reach a large share of Canadian audiences through Ontario-based marketing campaigns, they require out-of-country marketing support and extensive touring to reach international audiences. With a tax credit design that excludes tour costs and may discourage out-of-country marketing, Ontario sound recording companies may not have the resources or incentives to build international audiences.

Recommendations 4 & 5

4. Provide some form of collateral or guarantee on OSRTC, to facilitate cash flow financing.

5. Provide advances on tax credits to help established companies.

The economic analysis of the OSRTC concluded, "Ontario's indie labels are adapting their business models and pursuing…new revenue streams as vigorously as their international counterparts; however, their corporate development is not free of complication. Cash flow pressures and the challenge of growing international sales remain the two most top-of-mind issues for Ontario's indie labels. Without a rolling portfolio of projects, Ontario's indie labels can easily experience cash flow shortages. Improved cash flow can have a real impact on music companies' competitive position and financial performance…As little as an additional $20,000 can often mean the difference between the signing and not signing an artist by an indie label."

Therefore, it is vitally important for the rules governing the OSRTC to be expanded in order to accommodate greater cash flow for the recipients of the tax credit.

Recommendation 6

6. Reducing any real or perceived administrative burdens with the OSRTC application process.

Program statistics show that use of the OSRTC has been relatively consistent over the last four years. With the exception of 2008-09, the tax credit has typically supplied around $1.5 million in annual financial assistance to roughly 100 projects with total expenditures reaching a value of $8 million. Participation among Ontario music labels has also been relatively consistent – with the exception of 2008-09. Approximately one-quarter of Ontario's 64 music labels use the OSRTC. For those three-quarters that do not use the OSRTC, most report that the ***legal and administrative burden associated with the tax credit*** was the primary reason they did not seek assistance from it.

Summary of Recommendations

CIMA recommends that the Government of Ontario modernize the Ontario Sound Recording Tax Credit by:

1. Increasing the tax credit rate so that it corresponds with tax credit rates for the other creative sectors (ie: 30, 35 or 40 percent from its current level of 20 percent).

2. Increasing the eligibility of international marketing expenditures to match domestic expenditures (ie, 100 percent eligible).

3. Including other specific costs as eligible expenditures, e.g. touring, manufacturing, and rights tracking.

4. Providing some form of collateral or guarantee on OSRTC, to facilitate cash flow financing.

5. Providing advances on tax credits to help established companies.

6. Reducing any real or perceived administrative burdens with the OSRTC application process.

Thank you very much for the opportunity to present CIMA's prebudget submission. If you have any questions or comments, you may contact Stuart Johnston, President, at (416) 485-3152 ext. 232 or stuart@cimamusic.ca.

Yours sincerely,

Stuart Johnston
President

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