

PUBLIC NOTICE – CAVCO 2007-01

Canadian Film or Video Production Tax Credit (CPTC)

(For treaty co-productions, please refer to guidelines issued by Telefilm Canada)

This document sets out the Department of Canadian Heritage's positions on issues raised for public consultation in Public Notices CAVCO 2005-01 and CAVCO 2006-02.

Context

In November 2003, the government announced changes to the CPTC designed to simplify the tax credit mechanism and ensure that tax assistance is appropriately targeted. As part of those changes, it was announced that the Department of Canadian Heritage would review the requirement under the *Income Tax Regulations* that the production corporation have "ownership of copyright" in the production. The draft legislation released at that time also stated that the Minister of Canadian Heritage would issue guidelines with respect to the "acceptable share of revenues from the exploitation of the production in non-Canadian markets" that the production corporation must retain.

In Public Notices CAVCO 2005-01 and CAVCO 2006-02, the Department called for public comments regarding "copyright ownership" and the "acceptable share of revenues," in addition to other questions relevant to the administration of the CPTC. In Public Notice 2006-02, the Department set out its position with respect to a number of issues raised during the consultation process, notably concerning (i) Canadian broadcasters retaining their prescribed status under the Regulations of the *Income Tax Act*; (ii) waiving copyright ownership requirements for foreign tax-based incentives; (iii) adopting different approaches for theatrical and television productions; and (iv) creating a CAVCO Advisory Committee. The positions set out in that second Public Notice on these particular issues are hereby maintained. This document sets out the Department's positions on the following additional issues:

Positions

Copyright ownership

1. In accordance with the "excluded production" definition in subsection 1106(1) of the *Income Tax Regulations*, it continues to be a requirement that the eligible Canadian production corporation (whether alone or jointly with prescribed persons) retains the "*exclusive worldwide copyright ownership in the production for all commercial exploitation purposes for the 25-year period that begins at the earliest time after the production was completed that it is commercially exploitable.*"

The Department of Finance is presently considering a proposal from the Department of Canadian Heritage to clarify, in the *Income Tax Regulations*, the circumstances under which copyright ownership may be shared with other eligible

entities and the conditions under which investors can participate in the profits of exploitation of the production.

Acceptable share of revenues

2. The draft amendments of the *Income Tax Act* released in November 2003 provide that the Minister of Canadian Heritage will issue guidelines to clarify that a “Canadian film or video production certificate” is (*inter alia*) one that is issued where the “Minister is satisfied that (a) except where the production is a prescribed treaty co-production (as defined by regulation), an acceptable share of revenues from the exploitation of the production in non-Canadian markets is, under the terms of any agreement, retained by (i) a qualified corporation that owns or owned an interest in the production, (ii) a prescribed taxable Canadian corporation related to the qualified corporation, or (iii) any combination of corporations described in (i) and (ii)”

The expression “acceptable share of revenues” is interpreted to mean that producers must retain at least 25% of the net profits from the exploitation of the production in non-Canadian markets. In determining whether this requirement has been met, CAVCO will consider a number of relevant factors, including, among other things:

- i) whether distribution fees and expenses are contracted at rates that are in keeping with established industry standards;
- ii) where a broadcasting entity is also granted distribution rights, whether the allocation of funds as between the broadcast licence and the distribution licence is commercially reasonable;
- iii) whether the profit participation in any non-Canadian territory granted by the producer to certain investors is in keeping with established industry standards, as well as the intent of this policy guideline.

Non-Canadian showrunners

3. The Canadian producer must control the production as set out in the “producer” definition at subsection 1106(1) of the *Income Tax Regulations*. Any non-Canadian performing functions that derogate from that control will render the project ineligible. The Production Control Guidelines appended to this Public Notice set out the criteria that will be applied to determine whether the producer meets this requirement.

Any non-Canadian who may be commonly referred to as a “showrunner” will be required to submit an affidavit (on a CAVCO-approved form) declaring that any work performed is done only under the direction and control and with the full knowledge of the Canadian producer. In addition, the producer will be required to submit to CAVCO the contract entered into with this individual evidencing the work to be performed and the conditions of employment.

Format programs

4. Programs based on popular concepts or formats initially produced and exploited in a territory outside of Canada, and intended to be produced in Canada by a Canadian producer under a licence issued by the non-Canadian owner of the underlying rights, are eligible to the CPTC. However, the Canadian producer must clearly demonstrate that he or she controls the initial exploitation of the Canadian version of the production. Where the licence of rights permits the exploitation of the Canadian version of a format program outside of the Canadian territory, no one other than the Canadian producer can control its initial exploitation outside of the Canadian territory.

5. *Screen credits*

This section of the guidelines replaces the “Non-Canadian Exemption Policy” section of the Producer Control Guidelines issued in 1996 (Appendix 1 of the CPTC Guidelines).

a) General

The Canadian producer(s) must be clearly identified and given prominence on screen, in the main titles, and in all billing blocks. The Canadian copyright notice must appear in the tail-end screen credits.

b) Production-related screen credits for non-Canadians

Non-Canadians may be given courtesy screen credits from Group A and/or Group B. While courtesy credits may be chosen from either group, such credits must not exceed the number of credits given to Canadians from the same group. For example, if a non-Canadian is given one Group A credit, a Canadian must be given at least one Group A credit. However, if a non-Canadian is given a Group B credit, a Canadian must be given a credit from either Group A or Group B. Credits within the same group are interchangeable.

Group A:

- Executive Producer
- Senior Executive/Executive in charge of production
- Supervising Producer
- Associate Producer

Group B:

- Supervising Executive
- Production Supervisor
- Production Executive
- Production Associate
- Executive/Production Consultant
- Creative Consultant

With the exception of a non-Canadian lead actor or individual working in the story department, any non-Canadian granted a production-related screen credit is limited to a maximum of 25% of the time on set.

With the exception of a lead actor, all other non-Canadian individuals accorded a courtesy will be required to file with CAVCO an affidavit, on a CAVCO-approved form, outlining the duties performed and declaring that those duties have been / will be carried out only under the direction and control and with the full knowledge of the Canadian producer. No screen credit will be allowed without an affidavit. In no circumstance can non-Canadians receive a “producer” or “co-producer” credit.

6. ***Production Control Guidelines***

The appended guidelines replace the Producer Control Guidelines (Appendix 1 of the CPTC Guidelines) issued in September 1996. They provide further guidance in the determination of the eligibility of productions to the CPTC.

PRODUCTION CONTROL GUIDELINES

(For treaty co-productions, please refer to guidelines issued by Telefilm Canada)

Producer¹

The definition of “producer” is set out in section 1106 of the *Income Tax Regulations*. The following guidelines provide guidance on the indicia that will be applied to determine whether the definition is met:

The producer controls and is the central decision maker of the production from beginning to end. The producer is involved in and ultimately responsible for: the acquisition and/or meaningful development of the story; the commissioning of the writing of the screenplay/series bible; the selection, hiring and firing of key artists and creative personnel; the preparation, revision and final approval of the budget; all overages; the binding of the production company to talent and crew contracts; the arranging of the production financing; the supervision of the filming/taping and post-production; final creative control (as per contract), production expenditures (as per contract), production bank accounts (sole and unfettered cheque signing authority subject to Indicator 3(a)(ii)); and the arranging of the commercial exploitation of the production.

To satisfy the requirement of production control, the following guidelines provide that the Canadian producer:

- i. Must have and maintain full control over the development of the project from the time at which the producer has secured underlying rights;
- ii. Must have and maintain full responsibility and control over all aspects (creative and financial) of the production of the project;
- iii. Must have and maintain full responsibility and control over all aspects of production financing;
- iv. Must have and maintain full responsibility and control over the negotiation of initial exploitation agreements; and,
- v. Is entitled to a reasonable and demonstrable monetary participation in terms of budgeted fees and overhead, and participation in revenues of exploitation.

¹ ***Line producer and production manager***

The functions of line producer and production manager are not sufficient to confer producer status. Furthermore, persons assuming these functions, as well as persons to whom they report, must be Canadian.

Interpretation of the guidelines

GUIDELINE 1: DEVELOPMENT

The Canadian producer must have and maintain full control over the development of the project from the time at which the producer has secured underlying rights.

Indicator 1(a):

The producer must demonstrate full responsibility for the development of underlying rights of the project from the date upon which the producer has secured the underlying rights.

- i. CAVCO will review the chain-of-title documentation to confirm that the producer is responsible for the development of the project. *
- ii. CAVCO will assess chain-of-title documentation against all relevant documents concerning creative decision-making and the hiring of creative talent (writer, director, consultants, script editors, etc.).
- iii. The producer must affirm that all documentation affecting his/her decision-making authority has been disclosed and submitted to CAVCO as part of the application.

* Provision to be made for industry-standard third-party approval rights (distributors, broadcasters, financiers, completion bonders, etc.).

Indicator 1(b):

Prior development of the project by non-Canadians is permitted. However, ongoing involvement of prior rights-owners in development, production or exploitation of the project subsequent to the producer securing the underlying rights will be presumed to indicate that such party retains a degree of responsibility and control.

- i. The producer must demonstrate control over the development of the project. If development of the project has been materially completed by or with the involvement of non-Canadians, the producer will have the onus of establishing, to the satisfaction of CAVCO, that the situation did not interfere with the producer's responsibilities and control.
- ii. Non-Canadian prior right holders may have ongoing involvement in the production in terms of consultation rights only. The producer will have the onus of establishing, to the satisfaction of CAVCO, that such ongoing involvement does not interfere with the producer's responsibilities and control.

GUIDELINE 2: PRODUCTION

The Canadian producer must have and maintain full responsibility and control over all aspects (creative and financial) of the production of the project.

Indicator 2:

Documentation must demonstrate that, with the exception of standard approval rights from broadcasters, distributors, financiers and completion-bonders, the producer has exercised full control (direct or indirect) and holds final decision-making authority over creative and financial aspects of the production, including:

- *the project budget;*
- *the production schedule;*
- *the selection and hiring of above- and below-the-line cast and production personnel and the negotiation of the terms thereof;*
- *the selection and contracting for production services (camera package, sound package, post-production facilities, etc.) and the negotiation of terms thereof;*
- *the negotiation of agreements with unions and guilds;*
- *the post-production elements.*

- i. Where a non-Canadian has the right to overrule any decision by the producer, the producer will have the onus of establishing, to the satisfaction of CAVCO, that the situation does not interfere with the producer's responsibilities and control.

GUIDELINE 3: FINANCING

The Canadian producer must have and maintain full responsibility and control over all aspects of production financing.

Indicator 3(a):

Documentation must demonstrate that the producer has exercised full control (direct or indirect) and holds final decision-making authority over:

- *the financing plan of the project;*
- *the securing of all third-party financing, including, without limitation, domestic and foreign equity, domestic and foreign subsidies, domestic and foreign pre-sales and the negotiation of the terms thereof;*
- *the securing of interim financing (i.e. production financing) and the negotiation of the terms thereof;*
- *the cash-flow schedule of the project;*
- *the management of the banking of the project and sole and unfettered control over the bank account(s) of the project and cheque signing authority.*

- i. Where a non-Canadian has the right to overrule any decision by the producer, the producer will have the onus of establishing, to the satisfaction of CAVCO, that the situation does not interfere with the producer's responsibilities and control. *

- ii. Delegation of banking authority by the producer to a person(s) over whom the producer exercises final authority shall not be deemed to constitute a contravention of this indicator.

* Provision to be made for industry-standard third-party approval rights (distributors, broadcasters, financiers, completion bonders, etc.).

Indicator 3(b):

Documentation must demonstrate that the producer has assumed and retained the commercial risks associated with the financing and production of the project.

- i. Where a significant share of production financing is provided by a single non-Canadian party (or multiple parties with common ownership and/or control), the producer will have the onus of establishing, to the satisfaction of CAVCO, that the situation does not interfere with the producer's responsibilities and control.
- ii. Where a single non-Canadian party (or multiple parties with common ownership and/or control) has acquired exploitation rights to territories representing most or all of the exploitable value of the production (with the exception of Canada), the producer will have the onus of establishing, to the satisfaction of CAVCO, that the situation does not interfere with the producer's responsibilities and control.
- iii. Where a non-Canadian party has agreed to reimburse or indemnify the producer, e.g. with respect to budget overages, the producer will have the onus of establishing, to the satisfaction of CAVCO, that the situation does not interfere with the producer's responsibilities and control. *

*Provision to be made for industry-standard completion guarantees.

GUIDELINE 4: EXPLOITATION

<p>The Canadian producer must have and maintain full responsibility and control over the negotiation of initial exploitation agreements.</p>
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Indicator 4:

Documentation must demonstrate that the producer has exercised full control (direct or indirect) and holds final decision-making authority over the terms pursuant to which any party acquires rights to the initial exploitation of the project, regardless of territory, media and term.

- i. Where there is evidence of any arrangements between third parties with respect to the exploitation of the project (a) that are made prior to the acquisition of rights to the project by the producer; and (b) that are to remain effective following such date [i.e. such third party(ies) will remain involved with the exploitation of the project subsequent to the producer's acquisition of rights], the producer will have the onus of establishing, to the satisfaction of CAVCO, that the situation does not interfere with the producer's responsibilities and control.

- ii. Where the non-Canadian prior owner of the underlying rights retains exploitation rights to more than one significant territory, e.g. U.S., Europe, Asia, Latin America, after the producer has acquired the underlying rights, the producer will have the onus of establishing, to the satisfaction of CAVCO, that the situation does not interfere with the producer's responsibilities and control.

GUIDELINE 5: PRODUCER REMUNERATION

The Canadian producer is entitled to a reasonable and demonstrable monetary participation in terms of budgeted fees and overhead, and participation in revenues of exploitation.

Indicator 5(a):

The producer must demonstrate an equity ownership in the project.

Indicator 5(b)

The producer must retain at least 25% of the net profits from the exploitation of the production in non-Canadian markets.

Indicator 5(c)

Where, in addition to acquiring broadcast rights in the production, an entity acquires distribution rights and/or holds an interest in the production, the producer must demonstrate that each of the amounts advanced in respect of those rights and/or that

interest in the production has been allocated at fair market value as between the non-recoupable broadcast licence fee, the distribution rights and/or interest. It should be noted that an interest in a production does not constitute copyright ownership and that it remains a requirement under the Income Tax Regulations that the producer have ownership of copyright.

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