
Economic Impacts of the Canadian Educational Sector's Fair Dealing Guidelines

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Contents

Executive Summary	3
1. Mandate.....	13
2. Core Report Structure	14
3. Scope of Review	15
4. Background.....	16
4.1 Basic Economic Theory of Copyright	16
4.2 Economic Rationale for Collective Licensing.....	18
4.3 Fair Dealing in Canada	18
4.4 Educational Institutions' Fair Dealing Guidelines.....	19
5. Profile of the Market.....	24
5.1 Publishing Value Chain.....	24
5.2 Profile of Creators	25
5.2.1 Importance of Income from Written or Visual Works.....	28
5.3 Profile of Publishers in Canada	31
5.4 Production and Consumption of Educational Published Works.....	35
5.4.1 Publisher-Based Production Model for K-12 Materials	35
5.4.2 Consumption in K-12 Schools	37
5.4.3 Publisher Production Model for Post-Secondary Materials	39
5.4.4 Consumption in Post-Secondary Institutions.....	39
6. Economics of the Market.....	42
6.1 Sales Revenues.....	42
6.2 Licensing Income.....	42
6.3 Economic Footprint of the Educational Publishing Market.....	44
7. Market Trends	48
7.1.1 Emerging Models for K-12 Materials	49
7.1.2 Emerging Publisher Business Models.....	52
7.1.3 Emerging Markets Are Driving International Investment.....	55
8. Economic Impacts of the Fair Dealing Guidelines	57
8.1 Licensing Income.....	58
8.1.1 Impacts on Publishers	59

8.2	Sales Income	69
8.2.1	Evidence of the Impact of the Guidelines on Sales Revenues to Date	71
8.3	Creators’ Decisions to Produce	76
8.4	Investment	83
8.5	Industry Economic Footprint	88
8.6	Industry Composition	89
8.7	Content Diversity and Quality	90
9.	Conclusions.....	94
Appendix:	Limitations	96

Executive Summary

PwC has assessed the actual and expected market impacts of the implementation of the Fair Dealing Guidelines (also referred to as “Guidelines”) adopted in 2012 by the Council of Ministers of Education, Canada (CMEC), Association of Universities and Colleges Canada (AUCC), and Colleges and Institutes Canada (CICan).¹ These Guidelines apply to K-12 schools and post-secondary institutions in Canada, excluding the province of Quebec.²

Our Assessment finds that, since implementation of the Fair Dealing Guidelines, the educational publishing industry in Canada has been subject to a significant negative impact. Licensing income is substantially reduced. Revenues from sales are experiencing an accelerated decline. These declines, we believe, will accelerate further, causing adverse structural change in an industry already weakened by numerous other negative developments in the educational content market.

Application of the Guidelines significantly compromises the ability of educational publishers to publish original materials and meet varied academic needs. Indeed, we expect that over time, the publishing of new content for K-12 schools in Canada will for the most part disappear, and the quality of the content used by school students will thereby decline. As for post-secondary institutions, we expect that the publishing of materials will be rationalized and consolidated to focus only on certain segments of the market. Specialty subjects will be underserved in favour of high-enrolment subjects, with a corresponding decline in the availability of Canadian content. Many small- and medium-size publishers that currently serve this market will be forced out of it in search of more profitable publishing areas. This development will lead to lower competition, less content diversity, and higher prices for what is produced. In short, fewer works will be developed by Canadian content producers, both creators and publishers.

The economic footprint of the educational publishing industry is shrinking. If present patterns persist, many relatively high-paying jobs are expected to disappear. Foreign publisher subsidiaries may be forced to transition from producing Canadian content in Canada to distributing U.S. content in Canada. The incomes of Canadian writers, authors, and illustrators from Canadian sources will decline, and as no immediate or eventual replacement is apparent, this income decline will drive many from the sector.

The Guidelines, and the resulting market impacts, impede the ability of content producers to seize digital opportunities and discourage innovation in the Canadian digital knowledge-based economy.

¹ Formerly, the Association of Canadian Community Colleges.

² Access Copyright’s sister collective, Société québécoise de gestion collective des droits de reproduction (Copibec), licenses the copying of portions of copyright-protected works in the province of Quebec. As of the date of writing, Quebec elementary and secondary schools and the vast majority of colleges and universities remain licensed by Copibec and are thus excluded from this Assessment. For the purpose of this Assessment, “Canada” refers to Canada excluding the province of Quebec, unless otherwise noted.

A. The Context—The Canadian Educational Publishing Industry

There are many varied stakeholders in the industry that produces educational content for K-12 schools and post-secondary students in Canada (the Canadian “Educational Publishing Industry”): large, multinational organizations that offer a diverse portfolio of educational materials; authors and visual artists (together, “creators”) who write and create for publication in textbooks, trade books, and journals; and small- to medium-size enterprises, or “SME publishers,” that often focus on niche subject areas, such as Canadian history, language learning, arts, and culture. All of these stakeholders produce unique content that is read, used, and copied by students, teachers, and professors in Canada and around the world.

In the Midst of Transition toward a Digital Marketplace

Major changes have buffeted the Canadian educational publishing industry in recent years. In particular, the industry is in the midst of a transition from traditional business models, focused on print textbook publishing, to the development of innovative digital products, solutions, and services for the Canadian market. Many industry players are actively engaged in creating digital tools and content to maintain and expand their businesses, however, the transition to a digital marketplace requires significant investment.

The ability of large publishers and SME publishers to make the necessary investments is quite uneven. Large publishers are making major investments in transforming their products into more comprehensive offerings, including interactive materials, assessment tools, and practice questions. They are aiming to ensure that their customers have easy online access to their content. In general, SME publishers, too, are striving to transition to a digital based business. They have, however, been facing a shrinking market and significantly lower profitability that has made such a transformation challenging when compared to the more heavily capitalized large publishers.

Effects of a Government Spending Focus on Technology Hardware

At the same time that publishers are moving to develop digital content, provincial governments have limited spending on educational content in favour of technology hardware. The K-12 publishing sector has felt a substantial negative impact because of this decision.³ While several provincial governments have expressed interest in the development of digital content for K-12 classes, the increased spending on digital hardware for schools has not been matched by a corresponding investment in digital content. Neither has provincial government spending on digital content come close to offsetting the significant decline in spending on print materials. With less content purchased for the classroom, teachers are increasingly required to fill the void by copying and repurposing published content.

As the market shifts away from the purchase of traditional paper-bound textbooks to the adoption of digital technology, the revenues of K-12 publishers and related creators have fallen

³ See, for instance, *Consultation on K to 12 Educational Publishing in Canada*, by Glenn Rollans and Simon de Jocas (prepared under the direction of the Association of Canadian Publishers Education Committee), 2012, pp. 19-20.

dramatically. Total revenues generated in the K-12 Educational Publishing Market⁴ have declined by 40% since 2008. Any revenue gains from digital content to date have consisted primarily of an increase in *blended content*, which combines print and digital components for generally the same price as print alone. In response to a continuing demand for print and in an effort to protect their market share, publishers have borne the costs of investing in digital solutions on top of having to maintain the material they offer in print. This reality has a significant negative impact on even the large industry participants in this market.

Effects of a Move Away from Traditional Post-Secondary Textbooks

The post-secondary Educational Publishing Market is also experiencing declining sales. Sales revenue declined in the post-secondary market by approximately 12% between 2010 and 2014. The post-secondary sector has been moving away from traditional textbooks towards the offering of coursepacks (containing excerpts from multiple works) and course management systems, which enable instructors to make disaggregated content available to students electronically. This model, like the one developing for K-12 classes, depends on the copying of published content.

Many publishers have sought to offset declines in revenues from print materials with new revenue models, innovative services, and digital content that offer new learning experiences to students. These models include customized publishing, disaggregated content (such as offering e-chapters for sale through their websites), and value-added digital components, which supplement traditional materials.

Large post-secondary publishers are also intensively investing in the development of interactive digital platforms for students to supplement their print or digital textbooks.

As with the K-12 publishing sector, however, the transition costs of adopting digital content and delivery are high. Canadian-owned and small publishers have reported an inability to maintain competitiveness in the face of rising levels of technology investment.

The Education Sector's New Position on the Payment of Licensing Royalties

Over the past decade, the above negative trends have significantly weakened the publishing industry in Canada; then, at the end of 2012, a new issue arose: one relating to the interpretation of copyright legislation by educational institutions.⁵

For more than 20 years, Canadian provincial ministries of education and school boards, universities, and colleges paid royalties to creators and publishers for the copying of this content. These royalties⁶ were paid either directly to creators and publishers or through Access Copyright, a non-profit copyright collective acting on behalf of authors, visual artists, and

⁴For the purpose of our Assessment, the Educational Publishing Market is defined as the supply and demand for copyright-protected published works used by K-12 schools and post-secondary institutions—together, “educational institutions”—in Canada, excluding the province of Quebec.

⁵ See Section 4 of the Assessment for a discussion of the purpose of copyright legislation and its economic implications.

⁶ Throughout this report, revenues for the copying of portions of published works will be referred to as licensing income, revenues or royalties.

publishers of published literary works (together, “content producers”) to administer the reproduction of their works in Canada, outside Quebec.⁷

That practice began shifting in January 2013. All of the provincial governments and several universities and colleges stopped paying those royalties. The education sector now takes the position that its members are effectively not required to pay for the copying of this content by virtue of the “fair dealing” exception in the *Copyright Act*⁸. Associations representing most K-12, college, and university users in Canada developed guidelines that purport to authorize teacher, student, and professor copying of copyright-protected works for free under the “fair dealing” provision. For the balance of this report, we will refer to these documents as “the Guidelines.”

This issue introduces a new challenge to an industry striving to innovate and seize opportunities in response to demands from Canadian consumers in the digital, knowledge-based economy.

B. The Lens Through Which This Assessment Is Made

Given the implementation of the Guidelines across the country by K-12 schools, colleges, and universities, PwC was engaged to assess the economic impacts on the Canadian market for educational content and, more generally, on the Canadian economy.

In so doing, PwC has considered the issue in light of the economic theory behind copyright protection and its counterbalance, the fair dealing exception in the *Copyright Act*. The theory is that, without the proper regulation, prospective users could consume certain goods without paying for them (in other words, they could “free ride”), resulting in a “market failure.” This failure is signified by a reduction in the economic incentives to develop new creative content. A socially optimal level of copyright protection is thus essential to ensure that Canada is favourably positioned to transition to, compete in, and innovate in a digital, knowledge-based economy.

At issue is the balance between encouraging the creation of works of the arts and intellect, encouraging the dissemination of those works and obtaining just rewards for their creators: in other words, how well the purposes of copyright are being achieved. Copyright protection of original content creates a market that gives owners the ability to sell and license that content. The sales income and copyright licensing fees that are paid to creators and publishers for the reproduction of that content are designed to encourage innovation by maintaining the financial incentive to create new works. By permitting some free uses of copyright-protected content, the concept of “fair dealing” is intended to help maintain a balance between the public’s interest in giving copyright owners control over certain uses of their content while encouraging the dissemination of that content by users and owners.

Determining whether a socially optimal level of protection is being met involves assessing the impact of copying claimed to be “fair dealing” on the market for the content. This Assessment

⁷ Access Copyright’s sister collective, Société québécoise de gestion collective des droits de reproduction (Copibec), licenses the copying of portions of copyright-protected works in the province of Quebec.

⁸ The Guidelines allow royalty-free copying up to a certain threshold; however, this threshold is high enough such that it effectively eliminates all payments for materials copied by these institutions.

examines the impacts of the Guidelines on the Canadian Educational Publishing Market, both content producers and users.

C. The Impacts of the Guidelines

There are indications that the adoption of the Guidelines has already brought harm to the educational publishing industry in Canada. We expect further significant negative economic impacts, and these encompass content users, too. The following nine points set out those impacts and, where applicable, data we have observed in relation to those impacts.

1. Without licensing income—a significant source of income for content producers, especially SME publishers and creators—many Canadian publishers will not only reduce their content output, but may be forced to exit the Educational Publishing Market.

As a result of the Guidelines, licensing income from the K-12 sector has been all but eliminated. Provincial governments stopped paying licensing fees to Access Copyright for the copying of content in K-12 schools in January 2013. A similar outcome is expected in the post-secondary market once current licensing agreements expire at the end of 2015.

- The expected cessation of licensing payments for the use of parts of works would represent a loss of approximately \$30 million per year in payments to content producers.
- Licensing revenue historically received by content producers through Access Copyright has not been replaced or offset by an increase in licensing revenue from direct permissions—that is, direct payments by users to content producers for the copying of their works—from the education sector. In fact, for both large and SME publishers, licensing revenue from direct permissions has decreased significantly since 2009.
- Licensing income has a direct impact on each publisher's bottom line. It is estimated that large K-12 educational publishers alone would need to achieve an additional \$24 million worth of sales revenue each year (or an additional 18%) to make up this lost revenue. That scenario is highly unlikely given that the K-12 market has declined by 40% since 2008.
- For many SME publishers, licensing revenues represent the difference between profit and loss. The profits of SME educational publishers have declined sharply since 2008; for these publishers, EBITDA (Earnings Before Interest, Tax, Depreciation, and Amortization) declined by 81% between 2008 and 2012. In 2013, licensing revenues represented 16% of EBITDA for SME publishers, so the loss of this revenue source would have a substantial negative impact on profitability. The loss of licensing revenues is expected to cause some SME publishers to exit the Educational Publishing Market.
- Over half of SME publishers indicated that the decrease in licensing income from Access Copyright will hamper them from investing in the production of digital products and content; it will also limit the variety and number of works they publish, particularly for the education sector.

2. The Guidelines are expected to cause a further decline in sales in the Educational Publishing Market.

Copying portions of works can substitute for the purchase of the original work. The Guidelines encourage instructors to adopt coursepacks composed of copied excerpts or use course management systems instead of purchasing textbooks. By reducing the cost of copying, the Guidelines are expected to cause a further decline in sales for educational publishers, as they are replaced by “free” copies of identical or equivalent content that would otherwise be sold by those publishers. Certain content producers, such as those that specialize in anthologies, will be particularly harmed. Because the Guidelines permit royalty-free copying of excerpts, they enable and accelerate a reliance on teacher-compiled resources composed of copied works.

- K-12 teachers copy 350 million pages of published content annually - the equivalent of 1.3 million books every year. This copying competes with and substitutes for the purchase of tens of millions of books in the same time frame.
- Since the introduction of the Guidelines, the rate of annual decline in K-12 sales has accelerated, on average, by about 0.7 percentage points per annum.⁹ Outside Ontario (which recently released a new social studies curriculum), the acceleration of the decline in sales revenue is about 7.0%.
- In the post-secondary market, the rate of annual decline in overall unit sales has accelerated, on average, by about 3.2 percentage points per annum in 2012 to 2014 relative to the 2010 to 2012 period—this acceleration is more pronounced for Canadian titles compared to imported titles. The rate of annual decline in post-secondary sales revenue has accelerated, on average, by about 0.7 percentage points per annum.¹⁰
- The Guidelines authorize free copying that competes directly with innovative publisher business models designed to offer customers greater customization and choice, such as the sale of individual chapters and custom compilation services. The Guidelines thus undermine the development of monetization models based on disaggregated content and further diminish the value and likelihood that both the disaggregated content and the original, aggregated work would be purchased.

⁹ Based on a comparison of the compound annual growth rate in primary revenues from 2012 to 2014 relative to 2010 to 2012.

¹⁰ Based on a comparison of the compound annual growth rate in primary revenues from 2012 to 2014 relative to 2010 to 2012.

3. The Guidelines were introduced following a period of substantial loss of sales in the K-12 sector, resulting mainly from limited public funding of educational resources. Thus, the introduction of the Guidelines is expected, over time, to result in the elimination of much of the Canadian K-12 publishing industry.

As a result of reduced funding for educational resources and other measures instituted by K-12 schools, companies operating in this sector have experienced substantially reduced revenues and profits prior to the introduction of the Guidelines. This has weakened their ability to withstand the negative impacts of the Guidelines and some of them have already exited the market. We expect more publishers to exit the K-12 educational content market, further reducing competition in the market with potential negative impacts to innovation, quality and prices.

4. Canadian SME publishers are especially hard hit by the reduction in sales and licensing revenues precipitated by the Guidelines.

Due to their relatively small size and their limited access to external financing, the loss of sales and licensing income has a significantly larger financial impact on SMEs. As a result, we expect that many SMEs will be unable to continue their investments in digital solutions and content for the Canadian educational sector. Many SMEs will be forced to exit the Educational Publishing Market. Some are expected to direct their resources towards areas of publishing with more favourable and sustainable market conditions.

- Due to a decline in sales, SME educational publishers' EBITDA declined substantially between 2008 and 2012 (by approximately 80%). As a result, licensing income has become an increasingly important source of income for SMEs. In 2013, approximately 16% of EBITDA produced by SMEs came from licensing income (up from 5% in 2009; despite the fact that many educational institutions have already started to eliminate their payments in 2013).
- The loss of licensing, income following the introduction of the Guidelines by educational institutions further impedes the ability of SME publishers to invest in the production of digital content and services and limits the variety and number of works published for the educational market.

5. Under the Guidelines, creators have significantly lower incentives to create content for the Educational Publishing Market, or, indeed, to remain in the education sector. As a result, we expect a reduction in the number of works and amount of Canadian content.

As a result of the Guidelines, Canadian writers, authors, and illustrators will earn less income from Canadian sources—sources for which there appears to be no immediate or eventual replacement. This income decline will reduce the incentive for creators to remain in the educational sector. We expect that as a result of the Guidelines, and based on our survey of creators, approximately one in three creators will produce fewer works and will reduce focus and time spent on creating content for the education sector.

- Licensing income is an important source of income for creators. The median income for creators affiliated with Access Copyright from their written or visual works is \$15,000 per year. Licensing income represents approximately 20% of this income.
- Between 34% and 37% of Access Copyright's affiliate creators indicated that if the Guidelines were to reduce their licensing income, they would reduce the number of works created, the time they spend creating written and visual works, and their focus on creating content for the Educational Publishing Market.

6. The Guidelines and weak market are expected to cause educational publishers to reduce their investments in Canada; in turn, there will be fewer titles, including fewer titles tailored for the Canadian market, and less variety in titles produced. The pace and move towards innovative digital publishing will slow.

- Large educational publishers are expected to increase their reliance on the import and distribution of U.S. materials.
- Large educational publishers have reduced their headcount by over 10% since implementation of the Guidelines.
- Oxford University Press (one of the largest educational publishers in Canada) exited the Canadian K-12 market, citing the Guidelines and related loss of licensing revenues as a major reason.
- Nelson Education, one of the top two educational publishers in Canada, has filed for bankruptcy protection in Canada and is being restructured. The decline in the market for educational resources was identified as a key contributor to the filing.

7. The Guidelines are expected to lead to a reduction in the diversity and quality of content produced for the Educational Publishing Market, with certain courses or subject-areas becoming underserved.

Given the negative impact on profitability created by the Guidelines, we expect publishers to reduce their product offering for subject areas lacking sufficient scale or demand to justify investment in new content and capital-intensive digital solutions. Alternatives to publisher-developed resources will ultimately lower the quality of learning resources available to students.

- Fewer publishers are responding to requests for proposals to produce textbooks for new K-12 curriculum.
- Title and product rationalization are expected to occur due to reductions in investment, leading to fewer Canadian titles produced in Canada, fewer titles per course subjects, and fewer course subjects served.
- In response to declining sales, publishers have already begun to reduce the number and variety of titles produced. The impact is felt most in disciplines with high distribution costs (e.g., low enrolment and more advanced courses), where publishers are producing fewer titles and showing reluctance to develop digital solutions due to insufficient return on investment.

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- In the post-secondary market, large publishers indicated that the Guidelines will further cause them to focus on courses with high income potential, where information must be timely and relevant, particularly the scientific, technical, and medical areas. Less attention will go to creating content for such subject areas as history, arts, language, and culture.

8. The implementation of the Guidelines contributed to a significant decline in the economic footprint of the educational publishing industry between 2011 and 2013. Jobs in the publishing industry, particularly in the K-12 sector, and the overall future of the industry are at risk of further decline.

- Jobs in publishing are particularly high value jobs, which is indicative of high labour productivity. They are critical to a thriving knowledge-based economy.
- The total economic footprint of the Canadian educational publishing industry¹¹ in 2013 was significant, estimated at about \$620 million in GDP (gross domestic product) and 6,400 jobs. This figure, however, represents a significant 16% reduction from the 2011 estimated footprint of \$740 million in GDP and 7,650 jobs.
- Given the particular challenges faced by K-12 content producers, it is apparent that the economic footprint of that sector of the market¹² (estimated at approximately \$150 million in GDP and 1,600 jobs) is particularly at risk of further significant decline.

9. The apparent short-term gains that Ministries of Education, universities and colleges receive through the Guidelines mean higher prices, more work for teachers and professors and compromised content of variable quality for their students.

- The students who continue to use updated quality materials will pay higher text prices, as a result of reductions both in economies of scale available to publishers and in competition among publishers.
- K-12 teachers will have heavier workloads due to the responsibility for developing class materials.
- If individual teachers are obliged to create their own resources, there will be greater disparity in the quality of learning resources provided to students across localities.
- K-12 schools will have to rely increasingly on repurposed copied materials that are outdated or that do not meet the high education standards that Canadians have come to expect.
- Fewer works and less digital content will be developed by Canadian creators and publishers, and specialty subjects will be underserved in favour of high-enrolment subjects, leading to a decline in the availability of Canadian content for Canadians.

¹¹ Excluding the Quebec K-12 publishing industry but including the Quebec post-secondary publishing industry.

¹² Excluding the Quebec K-12 publishing industry.

In the longer term, Canadian K-12 and post-secondary students, teachers, and professors—namely, the users of educational content—will also be subject to negative impacts from the limited availability of digital and Canadian content, a deterioration in the diversity and quality of content used in the classroom, and a market framework that eliminates incentives and discourages innovation in the Canadian digital, knowledge-based economy.

The following is the core of our Assessment.

1. Mandate

PwC's role is to assess the actual and expected market impacts of the implementation of Fair Dealing Guidelines by K-12 schools and post-secondary educational institutions in Canada.

Access Copyright is a not-for-profit copyright collective that, along with other activities, licenses and collects royalties from district school boards and ministries of education and post-secondary educational institutions in Canada outside Quebec for the copying of portions of books, magazines, newspapers and periodicals (for the purposes of this Assessment, “published works”). Access Copyright then distributes these licence fees to the authors, visual artists, and publishers of the published works.

PwC has been engaged by Access Copyright to prepare an independent and objective assessment (the “Assessment”) of the actual and expected impacts of certain fair dealing policies (“Fair Dealing Guidelines” or “Guidelines”) published in the Fall of 2012 by the Council of Ministers of Education, Canada (CMEC), the Association of Universities and Colleges of Canada (AUCC)¹³ and Colleges and Institutes Canada (CICan, formerly Association of Canadian Community Colleges) on the Canadian market for copyright-protected published works. These Guidelines, which, we understand, were developed without the input of the writing and publishing industry, claim to authorize educational institutions to make copies of portions of published works without permission from, or payment to, the copyright holder.

For the purpose of our Assessment, the Educational Publishing Market is defined as the supply and demand for copyright-protected published works used by K-12 schools and post-secondary institutions—together, “educational institutions”—in Canada, excluding the province of Quebec.¹⁴ A market is a system whereby parties engage in exchange and it encompasses the demand and the supply of goods and services. As such, impacts on either the demand or the supply of educational published works are both considered market impacts. On the demand side, our Assessment focuses on buyers located in Canada. On the supply side, the focus is on works that are supplied in Canada.

PwC’s compensation is not contingent on any action or event resulting from the use of the Assessment. This Assessment is subject to the limitations noted in the Appendix to this report.

¹³ The AUCC has recently changed its name to “Universities Canada” (<http://www.univcan.ca/media-room/news-and-commentary/new-name-new-look/>).

¹⁴ Access Copyright’s sister collective, Société québécoise de gestion collective des droits de reproduction (Copibec), licenses the copying of portions of copyright-protected works in the province of Quebec. As of the date of writing, Quebec elementary and secondary schools and most colleges and universities in Quebec remain licensed by Copibec and are thus excluded from this Assessment. For the purpose of this Assessment, “Canada” refers to Canada excluding the province of Quebec, unless otherwise noted.

2. Core Report Structure

The core report is laid out as follows:

- **Section 3** summarizes the documents and information included in our scope of review.
- **Section 4** provides background information regarding the economic theory of copyright, the economic rationale for collective licensing, the history of fair dealing in Canada, and the Guidelines.
- **Section 5** provides a profile of the Educational Publishing Market in Canada, including the publishing value chain, the characteristics of creators who provide content to the industry, and the nature of production and consumption of published works in the K-12 and post-secondary publishing markets.
- **Section 6** sets out the economics of the Educational Publishing Market, including a review of sales and licensing revenues and the total economic footprint of the industry in terms of output, gross domestic product (GDP), and jobs.
- **Section 7** summarizes the key trends facing the educational publishing industry, including emerging models of content production for the K-12 market, increasing use of digital solutions, emerging publisher business models, and routing of industry investment from Canada to emerging markets.
- **Section 8** provides our analysis regarding the expected economic impacts of the Guidelines on the Educational Publishing Market, including the impact on sales of educational published works (“sales income”), licensing income received for copying of parts of those works (“licensing income”), the importance of licensing income to creators, the ability of creators to earn a sustainable living, the motivation of creators to author future works, investment in the industry, the economic footprint and composition of the industry, and the diversity, indigeneity, and quality of the content of future works.
- **Section 9** provides our conclusions.
- **The Appendix** sets out the limitations to the use of this report.

3. *Scope of Review*

To prepare our Assessment, we have reviewed and, where appropriate, relied upon various documents and sources of information.

By general classification, these sources include

- desktop research regarding the economics of copyright, the Canadian Educational Publishing Market, and the use of copyright-protected works in Canadian K-12 schools and post-secondary institutions;
- interviews with four of the six largest K-12 publishers, five of the largest post-secondary publishers and various smaller publishers who provide content to educational institutions in Canada;
- interviews with numerous creators, teachers, professors, and representatives of industry associations and Access Copyright;
- analysis of financial data provided by post-secondary publishers, K-12 publishers, the Canadian Educational Resources Council (CERC) and the Canadian Publishers Council (CPC) to Access Copyright;
- results of the ACP Survey, a survey of publisher members of the Association of Canadian Publishers, conducted by Circum Network Inc. (Circum)¹⁵;
- results of a survey conducted by Circum of creators¹⁶ who have appointed Access Copyright as their agent for the collective licensing of their works (“creator affiliates”); and
- analysis of historical and current royalty payments from educational institutions to Access Copyright and the distribution of those payments to publishers and creator affiliates.

¹⁵ An invitation to complete the ACP Survey was sent to 119 publishers. The total number of respondents who completed the survey as at October 19, 2014, was 58, indicating a response rate of 49%. The analysis in this Assessment is based on 58 publishers who responded. Some of the respondents did not provide complete financial information in response to certain survey questions, and, as such, the certain quantitative observations are based on fewer than 58 publisher responses

¹⁶ Further details regarding Circum’s survey of creators can be found in Section 5.2.

4. Background

4.1 Basic Economic Theory of Copyright

The protection of intellectual property through copyright laws ensures that content producers obtain a fair compensation for their efforts. Such protection is thus essential to maintain the economic incentive to create new content. A strong intellectual property framework that encourages businesses to invest is key to a thriving knowledge-based economy. If copyright protection is inadequate, Canada will not be poised to lead in productivity and innovation in the digital, knowledge-based economy.

For the purpose of this Assessment, the term “creators” will refer to writers, editors, translators, and visual artists (e.g., photographers, cartoonists, multimedia artists, and illustrators). The term “content producers” will refer to publishers and creators.

Copyright gives owners exclusive rights to their original work for a certain period of time. This includes the right to reproduce or authorize the reproduction of a substantial part of a work. This means that content producers have exclusive rights to make economic decisions about their works including, but not limited to, who can reproduce, communicate, perform and adapt their works, and who can financially benefit from them.

The economic rationale behind granting copyright to original works is based largely on the premise that copyright-protected works have some characteristics comparable to those of public goods. This means that, without the proper regulation, prospective users could consume the goods without paying for them—in other words, “free ride”—resulting in a “market failure”¹⁷. The resulting impact of free riding would be a reduction in the economic incentives to develop new creative content. Thus, one major economic argument in support of copyright is that it provides an incentive to produce new, original, innovative and creative works. The absence of effective copyright protection that leads to market failure would result in the production of works below a socially desirable level¹⁸.

Market failures in the case of original works arise through two mechanisms:

- First, access to original works cannot be completely excludable, in other words it is difficult to prevent individuals from using them. As a result, some users may enjoy the benefits of the works without contributing to their production costs (free-riding).

¹⁷ Market failure is a concept within economic theory describing when the allocation of goods and services by a free market is not efficient.

¹⁸ Handke, C. 2010. *The Economics of Copyright and Digitisation*. Report for the Strategic Advisory Board for Intellectual Property Policy (SABIP) and the Intellectual Property Office, London, UK. Online: <http://webarchive.nationalarchives.gov.uk/20140603093549/http://www.ipo.gov.uk/ipresearch-economics-201005.pdf>

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- Second, content producers of new, original and creative works incur significant fixed costs in producing the initial work, whereas the variable costs associated with reproduction are relatively low. As an example, creators incur significant fixed costs in producing the initial work, particularly in a market with shrinking (or non-existent) advances. Creators usually front much of their own per-hour costs of production with the expectation of earning royalties only from sales and licensing income. In the absence of effective copyright protection, content producers would be limited to offering copies of their works at prices no higher than the pure reproduction costs and thus would not be able to recoup their investment costs in the creation of the original works.

The economic theory of copyright theorizes that these market failures would result in fewer new, original, innovative and creative works being created, below socially desirable levels.

Copyright protection, however, also contributes to the costs for content producers and consumers:

- First, the need to trade and the enforcement of copyrights result in transaction and enforcement costs.
- Second, copyright grants copyright holders a time-limited monopoly, thus potentially excluding consumers who would be willing to pay above the marginal cost of production but less than the price being charged by the content producers.¹⁹

The above costs create what is referred to in economics as “dead-weight loss” relative to perfectly competitive markets.²⁰

In the context of the economic theory described above, copyright license fees that are paid, collected and remitted to content producers are payments designed to encourage the continued innovation and creation of new, knowledge-based content in Canada.

The importance of innovation has been well documented as a driver of national prosperity in knowledge-based economies²¹ and has been identified as an area of weakness in Canada’s future potential growth.²² Policy makers across Canada are focussed on strengthening Canada’s ability to innovate by creating the right opportunities and conditions for digital transformation in a knowledge-based Canadian economy.²³ The exploitation of copyright plays an important role in the encouragement of innovation and continued content creation. Thus, achieving a socially optimal level of copyright protection is critical to the success of a digital economy.

¹⁹ See, for instance, Handke, 2010.

²⁰ Dead-weight loss is an economic term that refers to a situation where there is a loss of economic efficiency similar to the one created by the existence of a tax or a subsidy.

²¹ For example, see Michael E. Porter, “The Competitive Advantage of Nations,” *Harvard Business Review* (March/April 1990).

²² For example, see the following report prepared at the request of Canada’s Minister of Industry: “*Innovation and Business Strategy: Why Canada Falls Short*” Report of the Expert Panel on Business Innovation, June 2009

²³ Digital Canada 150, Her Majesty the Queen in Right of Canada, represented by the Minister of Industry 2014, online: www.canada.ca/digitalcanada.

4.2 Economic Rationale for Collective Licensing

The *Copyright Act* allows for the operation of copyright collective societies, which are organizations responsible for administering certain rights on behalf of a group, or collective, of copyright owners. Collective licensing is intended to enable economies of scale which help to minimize the transaction costs associated with the management or administration of copyright. If every user had to individually request permission from each copyright holder every time the user wanted to copy a portion of a work, the transaction costs would generally be prohibitive and lead to higher total costs for both content producers and users. By acting as a “one-stop-shop” for copyright clearance and related permissions, copyright collective societies reduce the transaction costs associated with administering copyright while ensuring that copyright owners are remunerated for the use of their works so that they remain incentivized to continue creating.

Canada is home to numerous copyright collective societies, representing the interests of the full spectrum of copyright owners, such as authors, publishers, artists, photographers, musicians, composers, record labels and performers. As explained above, Access Copyright is a copyright collective society that acts on behalf of authors, visual artists and publishers of published literary works to administer the reproduction of their works in Canada, outside of Quebec. Copibec, Access Copyright’s sister organization, performs the same role in Quebec. Access Copyright has also entered into reciprocal bilateral agreements with copyright collectives in 29 other countries under which Access Copyright represents the copyright interests of creators and publishers in those countries.

4.3 Fair Dealing in Canada

The concept of “fair dealing” is one tool in the Copyright Act intended to help maintain a balance between the need for incentives to create original content and the desire to provide users with access to content when it is fair to do so. Fair dealing in Canada is available for certain specified purposes in circumstances that are considered to be fair and socially desirable. The specific circumstances of the use and subject market need to be considered in assessing whether a given dealing achieves such balance and is, therefore, fair.

Given the costs and benefits of copyright protection, copyright policy has been historically viewed as a balancing act between providing an incentive for the development of new and original content and the desire to provide potential users with access to that content for certain purposes in circumstances that are fair and socially desirable.

From an economics perspective, “fair dealing” is one of the tools used to achieve such balance. In seeking that balance, the Supreme Court of Canada has referred to it as a “user’s right”.²⁴ The question of whether a certain fair dealing claim creates such balance or tilts the pendulum too

²⁴ *CCH Canadian Ltd. v. Law Society of Upper Canada*, [2004] 1 S.C.R. 339, para. 48.

far in one direction can only be answered in the context of the facts and circumstances of the subject market reality.²⁵

In Canada, fair dealing is a statutory exception to copyright infringement that allows the copying of copyright-protected works without permission from or payment to the owner of the copyright for certain specific, enumerated purposes²⁶ when the dealing is considered fair. The *Copyright Act* does not define the word “fair”; however, a 2004 Supreme Court ruling²⁷ identified six principal criteria to evaluate whether a certain dealing is fair. The six fairness factors are as follows:

- i. The Purpose of the Dealing
- ii. The Character of the Dealing
- iii. The Amount of the Dealing
- iv. Alternatives to the Dealing
- v. The Nature of the Work
- vi. The Effect of the Dealing on the Work

This Assessment relates to the sixth factor: the “effect of the dealing on the work”, including the expected economic impacts of the use on the market for the copyright-protected work.

4.4 Educational Institutions’ Fair Dealing Guidelines

The Fair Dealing Guidelines announced by the education sector in 2012 were adopted by all public schools, some independent schools, and numerous post-secondary institutions. These Guidelines authorize, as purported fair dealing, the copying of portions of works to the same extent as was permitted under the licenses previously issued by Access Copyright. Many of the schools and institutions that adopted the Guidelines have stopped paying licensing fees for copying published works.

Elementary and secondary schools (K-12 schools) and post-secondary institutions in Canada are large users of copyright-protected works. They have traditionally paid licensing fees, directly or indirectly, to content producers so that educators may copy (in paper or digitally) certain portions of published works.

²⁵ For example, a certain use may have less of an impact in a growing and strong market, whereas the same use may have a greater impact in a declining and weak market.

²⁶ Section 29 of the *Copyright Act* states that, “Fair dealing for the purpose of research, private study, education, parody or satire does not infringe copyright”. Section 29.1 of the *Copyright Act* states that, “Fair dealing for the purposes of criticism or review does not infringe copyright” provided that attribution is given.

²⁷ *CCH Canadian Ltd. v. Law Society of Upper Canada*, [2004] 1 S.C.R. 339

From 1991 to 2012, all Canadian Ministries of Education and K-12 schools (excluding Quebec) paid Access Copyright for permission to copy portions of published works under consensual licences or under a tariff issued by the Copyright Board of Canada. Virtually all Canadian post-secondary institutions had licences in place with Access Copyright from 1994 to the end of 2010.

In 2012, the Canadian federal government amended the *Copyright Act* to add “education” as an enumerated fair dealing purpose. In the Fall of 2012, new fair dealing guidelines were developed and published by the CMEC for K-12 schools and by the AUCC and CICan for post-secondary institutions. These fair dealing guidelines are substantially similar to one another and are collectively referred to in this Assessment as the “Guidelines”. The Guidelines have been implemented in all public elementary and secondary schools, some independent (private) schools and the majority of post-secondary institutions in Canada.

The Guidelines authorize teachers, instructors, professors, and staff to “communicate and reproduce, in paper or electronic form, “short excerpts” from a copyright-protected work for the purposes of research, private study, criticism, review, news reporting, education, satire or parody” without permission from the copyright holder or payment of copyright royalties. The educational institutions’ definition of a “short excerpt” in the Guidelines is, as shown in Tables 1 and 2 below, similar to the types and extent of copying permitted under Access Copyright’s licences.

Table 1 - Comparison of Copying Allowed under Access Copyright K-12 Licences and CMEC Guidelines

Copying allowed by Access Copyright K-12 licence agreements and tariffs	Copying allowed by CMEC Guidelines
<ul style="list-style-type: none"> • up to 10% of a published work; 	<ul style="list-style-type: none"> • up to 10% of a copyright-protected work (including a literary work, musical score, sound recording, and an audiovisual work)
<ul style="list-style-type: none"> • an entire article or page from a newspaper, magazine or journal 	<ul style="list-style-type: none"> • a single article from a periodical • an entire newspaper article or page
<ul style="list-style-type: none"> • an entire short story, play, essay or poem 	<ul style="list-style-type: none"> • an entire single poem from a copyright-protected work containing other poems
<ul style="list-style-type: none"> • an entire entry from a reference work 	<ul style="list-style-type: none"> • an entire entry from an encyclopedia, annotated bibliography, dictionary or similar reference work
<ul style="list-style-type: none"> • an entire reproduction of an artistic work from a publication 	<ul style="list-style-type: none"> • an entire artistic work (including a painting, print, photograph, diagram, drawing, map, chart, and plan) from a copyright-protected work containing other artistic works
<ul style="list-style-type: none"> • an entire chapter that comprises 20% or less of a book 	<ul style="list-style-type: none"> • one chapter from a book
<ul style="list-style-type: none"> • an entire reproduction of a musical work provided that, if taken from a book, does not comprise more than 20% of that book 	<ul style="list-style-type: none"> • an entire single musical score from a copyright-protected work containing other musical scores
<ul style="list-style-type: none"> • up to 100% of reproducibles, including assignment sheets and blackline masters 	
<ul style="list-style-type: none"> • an entire choral, orchestral work, or other commercially available sheet music 	

Table 2 - Comparison of Copying Allowed under Access Copyright Post-Secondary Licences and AUCC and CICA Guidelines

Copying allowed by Access Copyright post-secondary license agreements and tariffs	Copying allowed by AUCC and CICA Guidelines
<ul style="list-style-type: none"> • up to 10% of a copyright-protected work; 	<ul style="list-style-type: none"> • up to 10% of a copyright-protected work (including a literary work, musical score, sound recording, and an audiovisual work)
<ul style="list-style-type: none"> • up to 20% of a copyright-protected work as part of a “course collection”²⁸ 	
<ul style="list-style-type: none"> • an entire newspaper or periodical article 	<ul style="list-style-type: none"> • a single article from a periodical • an entire newspaper article or page
<ul style="list-style-type: none"> • a single short story, play, poem, essay or article from a Published Work that contains other Published Works (i.e., from an anthology) 	<ul style="list-style-type: none"> • an entire single poem or musical score from a copyright-protected work containing other poems or musical scores
<ul style="list-style-type: none"> • an entire entry from an encyclopedia, annotated bibliography, dictionary or similar reference work 	<ul style="list-style-type: none"> • an entire entry from an encyclopedia, annotated bibliography, dictionary or similar reference work
<ul style="list-style-type: none"> • an entire reproduction of an artistic work (including any drawing, painting, print, photograph or other reproduction of a work of sculpture, architectural work or work of artistic craftsmanship) from a Published Work that contains other Published Works 	<ul style="list-style-type: none"> • an entire artistic work (including a painting, print, photograph, diagram, drawing²⁹, map, chart, and plan) from a copyright-protected work containing other artistic works
<ul style="list-style-type: none"> • one chapter, provided it is no more than 20% of a book 	<ul style="list-style-type: none"> • one chapter from a book

For the purpose of this Assessment, the limitations on copying authorized by the Guidelines are referred to as “excerpts”, even though in cases such as artistic works, articles, short stories and poems, the Guidelines authorize, as purported fair dealing, the copying of an entire copyright-protected work.

²⁸ Course collections refer to paper and digital coursepacks.

²⁹ Certain institutions have not specifically referred to drawing in their fair dealing policy.

Effective January 1, 2013, following the release of the Guidelines, all public K-12 schools stopped making licensing royalty payments to Access Copyright for the copying of published works. Some independent K-12 schools have also ceased paying royalties.³⁰

Universities and colleges that have implemented the Guidelines have either stopped paying royalties to Access Copyright or are still paying Access Copyright because they are bound by licensing agreements that were entered into prior to the release of the Guidelines.

As of January 1, 2015, 134 universities and colleges (or 48% of all post-secondary educational institutions) are operating under license agreements with Access Copyright that remain in force until December 2015. Many of these institutions have indicated that they intend to stop paying once their agreements expire. A total of 144 universities and colleges (or 52%) are unlicensed. Those schools and institutions that have stopped making payments are referred to in this report as “unlicensed institutions”.

³⁰ Independent schools are private non-profit schools that are independent of national or local government for their finances and governance. The royalties paid by those independent schools that remain licensed represent a nominal proportion of royalties historically paid by the K-12 educational sector.

5. Profile of the Market

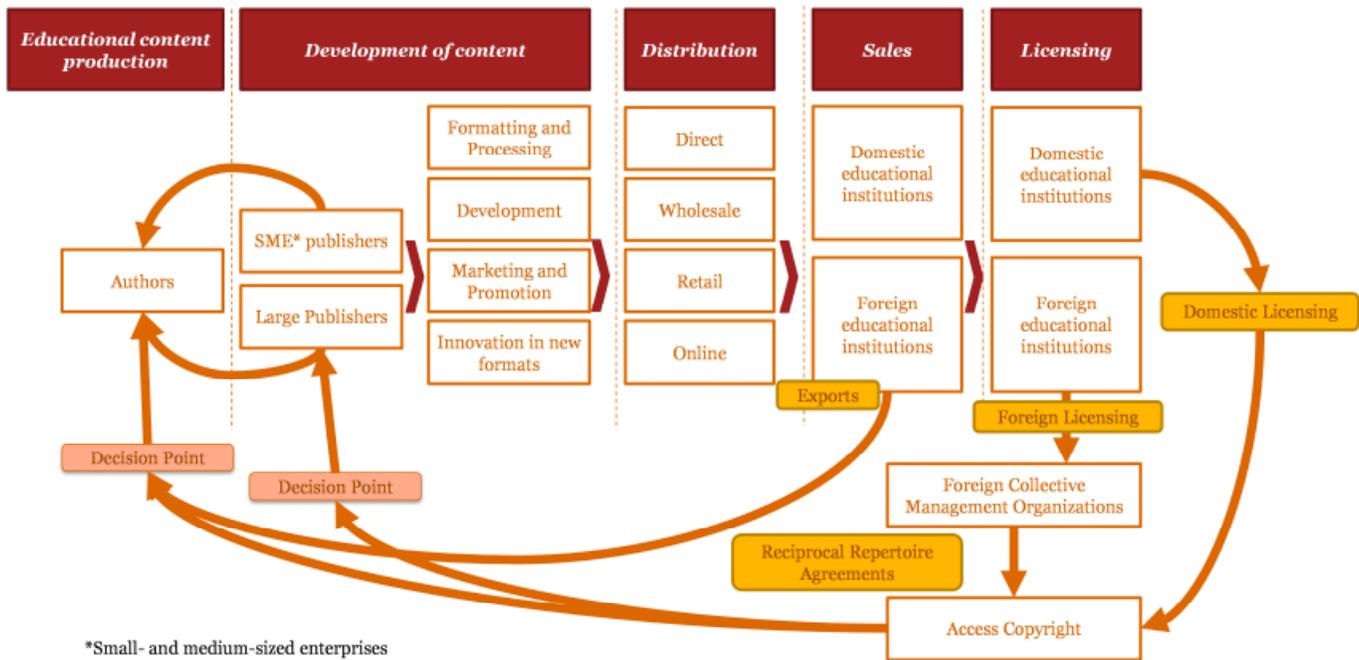
This section describes the players in the Educational Publishing Market and the mechanisms through which content for educational institutions is created and consumed. We describe the relationships between content producers and users of content, including the ways in which the content is consumed and paid for. The content consumed includes both originally published copyright works and copies of that original content. We also provide an overview of the typical production models of publishers who create content for the K-12 and post-secondary markets.

5.1 Publishing Value Chain

The publishing value chain of educational published works in Canada involves numerous stages of development and interactions between creators, publishers, distributors, educational institutions, and licensing agencies. Income flows to publishers and creators through sales and licensing revenues. It is used to help finance the production of new content.

The creation and consumption of educational published works involves numerous players, including creators, publishers, educational institutions (including teachers, professors, librarians and students) and licensing agencies. A simplified representation of the publishing value chain is illustrated in Figure 1.

Figure 1 – Publishing Value Chain



Source: PwC analysis

At the front of the value chain, creators generate new educational materials, which are often conceived and/or commissioned by educational publishers. Educational publishers often work closely with creators in the conception, development and design of the resources to ensure that they meet the education sector's rigorous pedagogical standards. Publishers then develop, design, format, process, print and market the content to users.

Income flows to publishers and creators through both sales and licensing income received when their works are copied by teachers, professors or students. The income received by content producers from both sales and licensing helps fund and incentivise the creation of new content.

5.2 Profile of Creators

In 2014, more than 11,000 creators were affiliated with Access Copyright. Half identified their primary occupation as a self-employed writer or visual artist. Most noted that they spend at least half of their professional time creating and that they derive a significant portion of their total income from this. The median income for Canadian creators is \$15,000 per year, with three quarters of creators receiving less than \$25,000 per year from their works. More than 20% of that income is derived from Access Copyright licensing income.

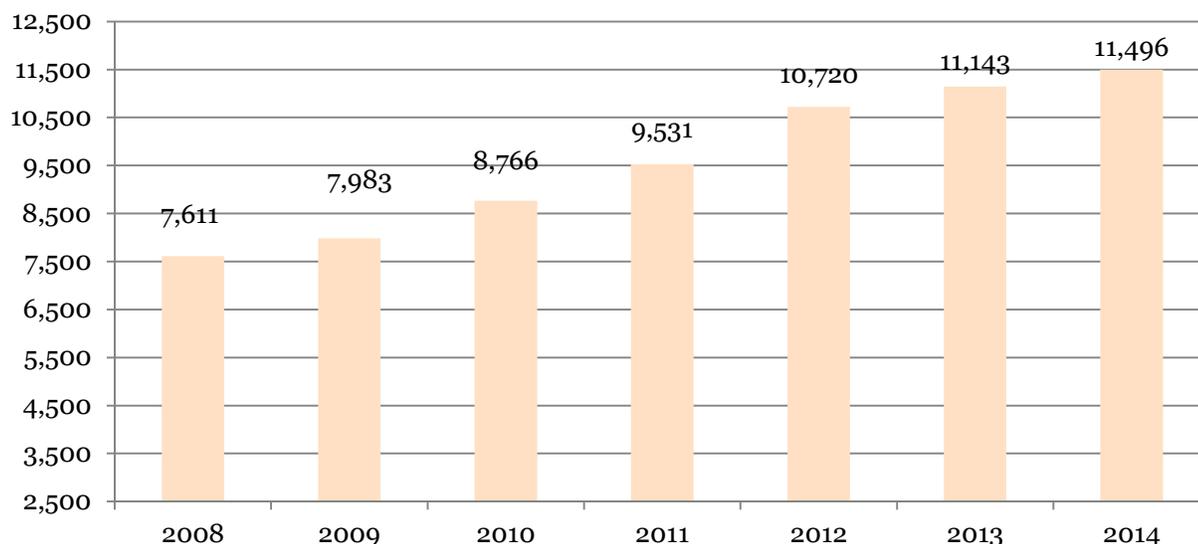
For the purposes of this Assessment, creators include those writers and visual artists who produce content that is used in K-12 schools and/or post-secondary institutions. Some of the works written by these creators are intended specifically for educational purposes (e.g. textbooks for specific curricula) and other material is written primarily for non-educational purposes, but subsequently finds use in K-12 schools or post-secondary institutions (e.g. fiction trade books which become part of English literature curricula). This section presents a profile of Canadian creators, based on data provided by Access Copyright and a survey conducted by Circum of Access Copyright's creator affiliates.

The figure that follows illustrates that over 11,000 Canadian creators affiliated with Access Copyright received payments from Access Copyright for works used by K-12 schools and post-secondary institutions from 2008 to 2014.³¹ It should be noted that this figure underestimates the number of Canadian creators who receive licensing revenues, as some creators received licensing income from their publishers only.³²

³¹ Based on author and visual artist payments data provided by Access Copyright.

³² In 2013, approximately 31% of the royalties paid to publishers by Access Copyright were passed on to the respective creators. See 2014 Access Copyright Annual Report, page 8: http://www.accesscopyright.ca/media/91810/2014_ar_final.pdf

Figure 2 – Number of Creators Who Received Licensing Income from Access Copyright for Copying by Educational Institutions (2008 to 2014)



As part of this analysis, Circum conducted a survey of all creator affiliates of Access Copyright (“Circum Survey”)³³. An invitation to complete the survey was sent to 9,466 creators on July 24, 2013³⁴. The total number of respondents who completed the survey was 3,601³⁵ indicating a response rate of 42%. The analysis in this Assessment is based on creators who responded that there was some likelihood that their written or visual works have been copied in support of teaching in either the K-12 sector (totalling 2,238 creators) or the post-secondary sector (totalling 2,871 creators)³⁶.

Among other things, the creators of these works vary according to

- whether they spend all or only some of their time working as professional creators, which affects the importance to their livelihood of income from writing; and
- whether or not they write specifically for K-12 or post-secondary education.

³³ PwC collaborated with Circum Network Inc. on developing the questionnaire for the survey.

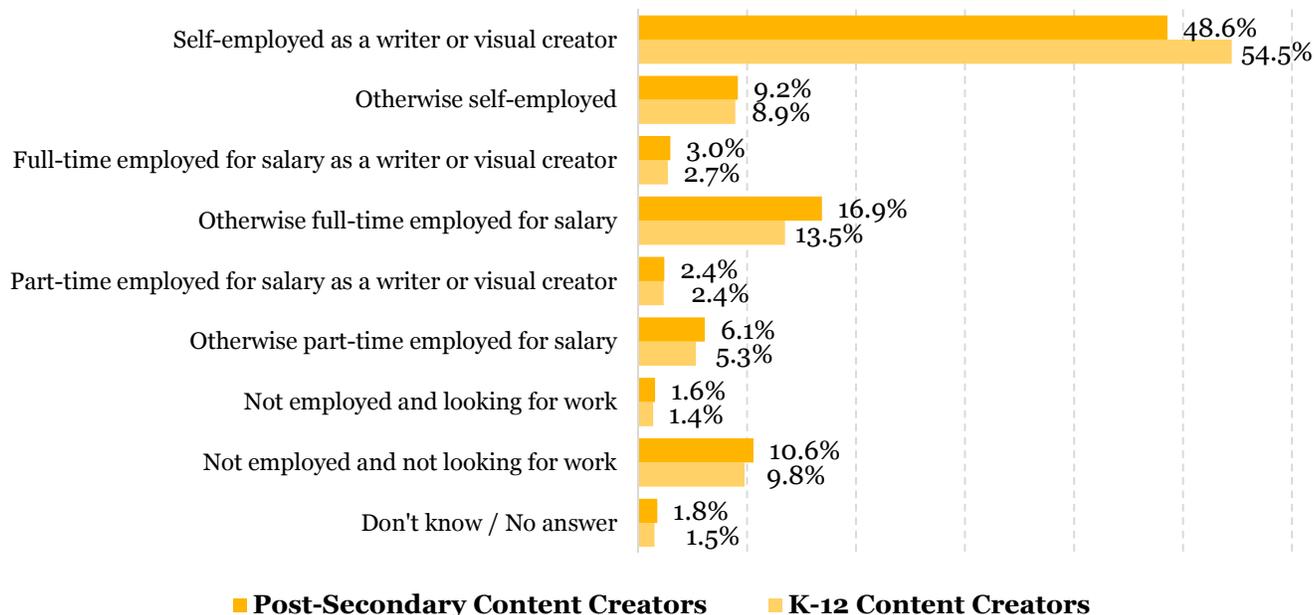
³⁴ All author affiliates for whom Access Copyright had e-mail addresses were asked to participate

³⁵ This number excludes 317 respondents who had not produced content in the last three years

³⁶ There is some overlap between K-12 and post-secondary creators.

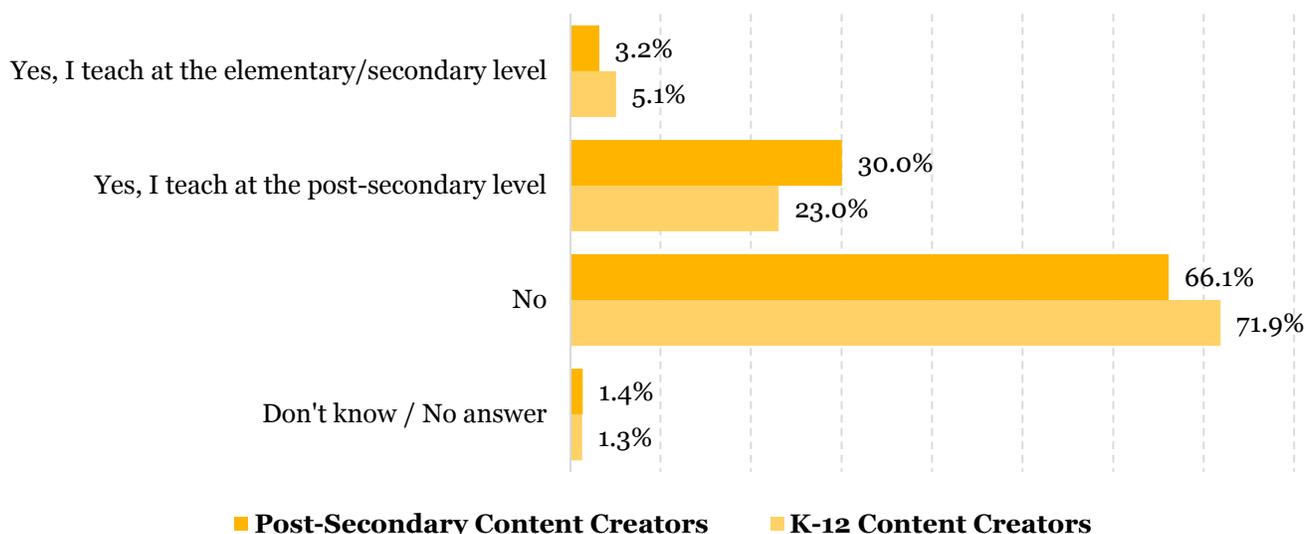
As seen in Figure 3 below, approximately half of respondents indicated that their main employment status is “self-employed as a writer or visual creator”.

Figure 3 – What is your main current employment status?



As seen in Figure 4 below, the majority of creators affiliated with Access Copyright are not employed in teaching positions by schools or post-secondary institutions.

Figure 4 – Does your employment involve teaching at the elementary/secondary or post-secondary level?

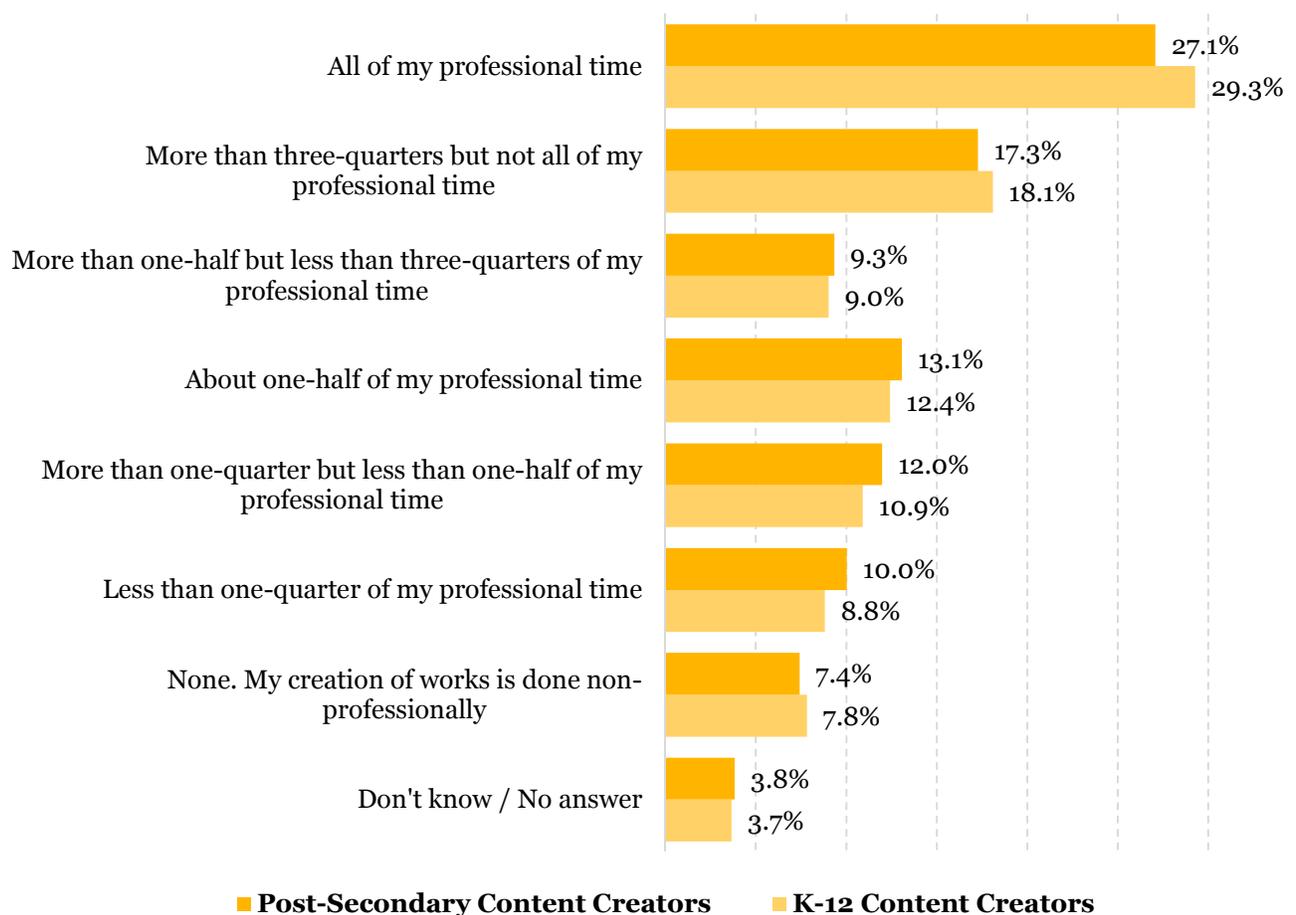


5.2.1 Importance of Income from Written or Visual Works

The importance of creators' income that is derived from producing written or visual works used in K-12 schools and post-secondary institutions can be identified from the time spent producing these works as well as the income generated from these works.

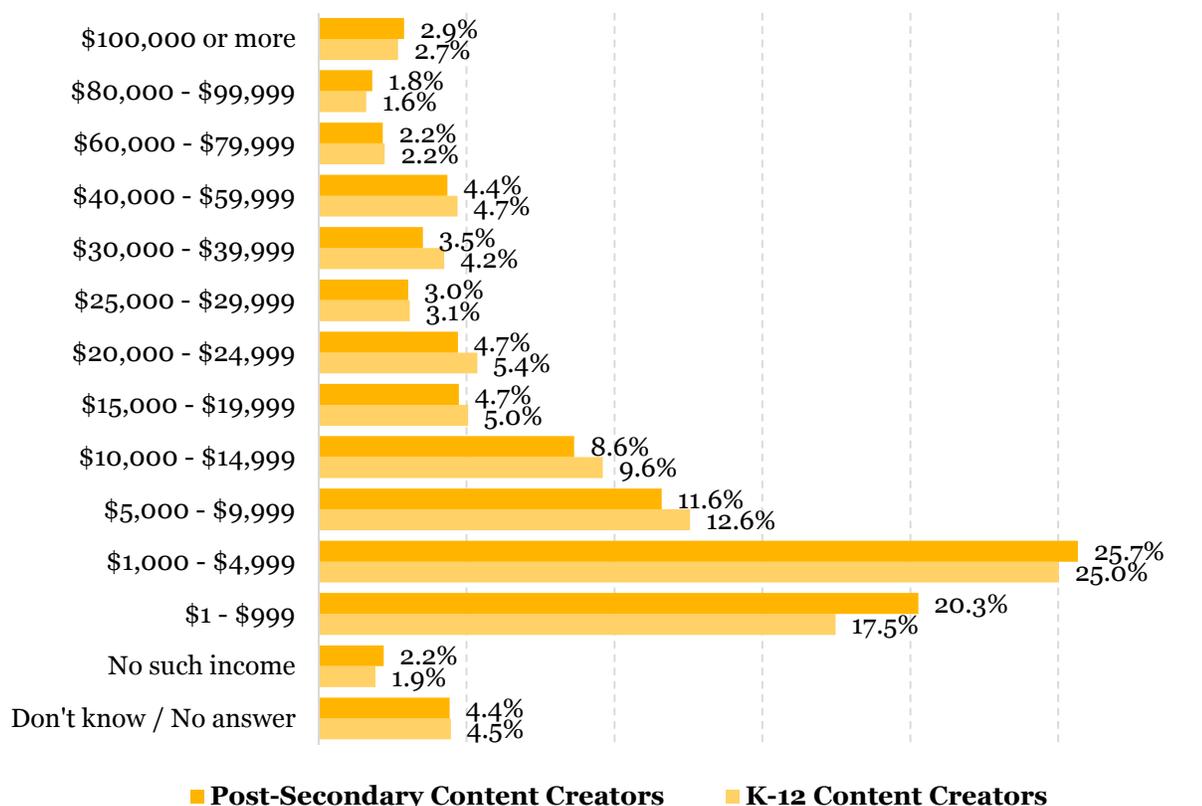
As seen in Figure 5 below, the majority of creators affiliated with Access Copyright devote about half or more of their professional time to creating written or visual works.

Figure 5 – How much of your professional time do you devote to creating written or visual works?



As can be seen from Figure 6 below, creators affiliated with Access Copyright receive varied amounts of income from written or visual works, ranging from lower than \$1,000 to above \$100,000. Based on the ranges provided in the Circum Survey, the median income in 2012 from written or visual works for survey respondents was approximately \$15,000.

Figure 6 – Total Income³⁷

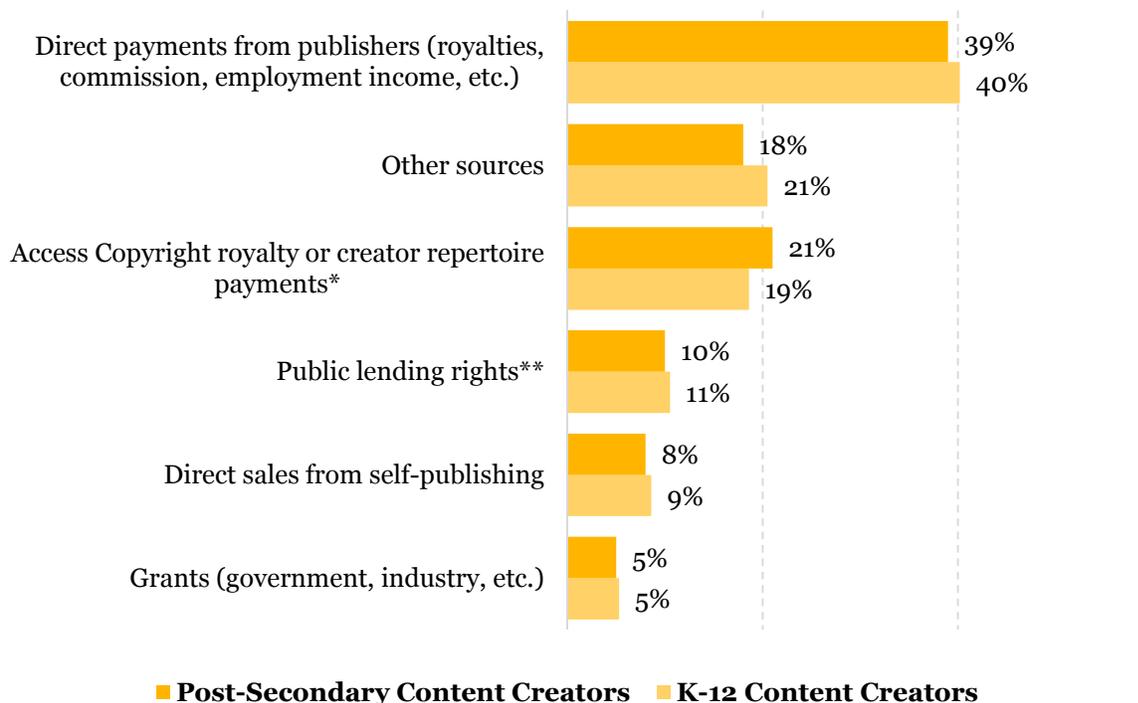


Creators earn their income from a variety of different sources, including royalties and advances related to the sales of their works, licensing income for the copying of their works, government grants and several other sources. All of these different sources of income are individually important.

Based on Figure 7, which follows, creators affiliated with Access Copyright receive the bulk of their income for written or visual works directly from publishers. On average, approximately 40% of their income from written or visual works came from publishers as direct payments. Royalty payments from Access Copyright are also an important source of income, at approximately 20% on average.

³⁷ Survey question: Consider your 2012 income from all sources associated with written or visual works you created. Include direct payments from publishers (royalties, commissions, employment income, etc.), Access Copyright royalty or Creator repertoire payments, direct sales from self-publishing, public lending rights, grants (government, industry, etc.), and any other sources of pertinent income.

Figure 7 – Approximately what percentage of your 2012 income that was derived from your written or visual works was from each of the following categories?



*Access Copyright's creator repertoire payments (or 'Payback') refer to the portion of its distributions that are paid in recognition of the value that creator affiliates bring to the repertoire.

** Public lending rights refer to payments distributed by the Canada Council for the Arts to creators as remuneration for access to their works in public libraries.

These creators may be employed by publishers or may be self-employed independent contractors who write either full- or part-time, for educational or other purposes. However, the majority of creators profiled in this Assessment are generally professional writers and visual artists whose works are used by the educational sector, the majority of whom

- spend more than half of their time writing and creating;
- make, on average, \$15,000 per year from their creative input and therefore must supplement their income with other income; and
- typically do not obtain income through teaching at either the K-12 or post-secondary educational level.

5.3 Profile of Publishers in Canada

The Canadian publishing industry is diverse, with a mix of large firms and small- to medium-size enterprises (SMEs) providing both general and specialized content to educational institutions in Canada. Much of this content is Canada specific, and a significant proportion is developed specifically for the Canadian education sector.

The Canadian educational publishing industry is composed of a variety of organizations that publish content used by educational institutions.

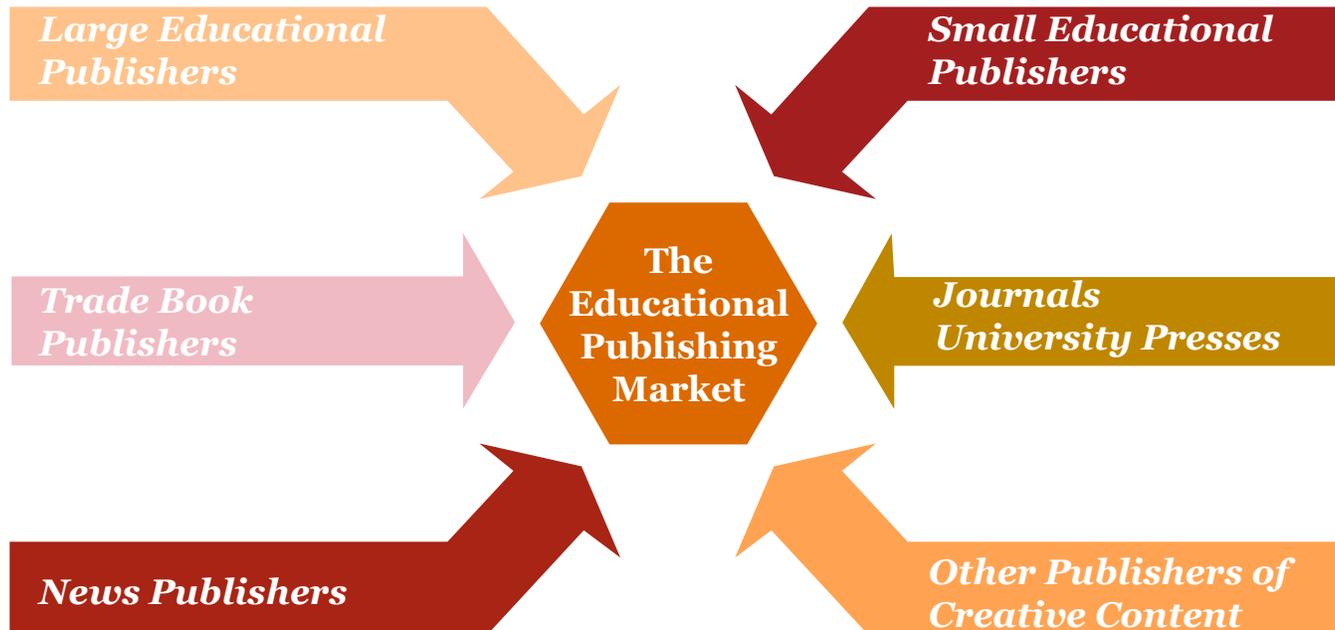
The industry comprises seven large publishers and roughly 65 small-medium enterprises (SMEs) that publish textbooks and books for the Canadian K-12 and post-secondary markets. In addition to these book publishers, the industry includes a number of scholarly or university presses. Some publishers are dedicated solely to developing educational content and others also publish content for the general public. The large, often multinational, organizations offer a diverse portfolio of educational materials (e.g., multiple titles across various subject areas) while SMEs tend to focus on particular subject areas, a single type of material (core or supplemental resources³⁸) and products dedicated to those niche areas. Trade books, which are intended for general readership, are also used by educational institutions.³⁹ Many publishers also publish under various imprints, or trade names.

University presses are typically affiliated with large research universities and publish works that have been reviewed by scholars in the field. Journals are also an important source of content for post-secondary institutions. Academic journals are peer-reviewed and serve as forums for the introduction and critique of research. Most academic journals are supported financially by universities or professional organizations. University presses offer many journals to libraries and individuals on a paid subscription basis. Some of these journals are offered on an open access basis. Some journals (mostly medical and scientific) are produced by commercial publishers such as Elsevier and John Wiley, and sold to libraries and individuals. Various other entities publish works that are used in the K-12 and post-secondary markets but that are not specifically created for use in that sector, including newspaper and magazine publishers, associations, corporations and museums. The economic impacts of the Guidelines on these other copyright-protected works and publishers of these works are outside the scope of this Assessment.

³⁸ See Section 5.4.2 for a definition of core and supplemental resources.

³⁹ Some trade titles, especially trade series, are used in schools as library volumes or library sets, in reading centres, in classrooms, or as resources for areas of study such as language arts, social studies, health, philosophy, history and law. Trade books, however, do not exhibit the same sales cycles as resources conceived specifically as K-12 educational resources.

Figure 8 – The Educational Publishing Market



K-12 Publishers

The K-12 industry comprises a few large publishers and a number of SMEs that publish books for the Canadian K-12 Market. The largest K-12 publishers are members of the Canadian Educational Resources Council (CERC): Nelson Education, Pearson Canada, McGraw-Hill Ryerson, Scholastic Education, Chenelière Education, and Oxford University Press⁴⁰. Aside from Nelson Education and Chenelière Education, these largest publishers are foreign-owned Canadian publishers. Despite the foreign ownership of many of the larger publishers, the majority of the content used by and sold to K-12 schools originates in Canada. For instance, two of the largest K-12 publishers reported that between 60 and 80% of their sales were from Canadian content developed specifically for the Canadian market.

Several SMEs also publish books either designed for or used by the K-12 market. Many of these SMEs are members of ACP, including

- Annick Press, founded in 1975 with a mandate for creating quality resources for children and youth, an example of which are the works authored by Robert Munsch⁴¹;
- Portage and Main, a Winnipeg-based publisher of K-12 educational resources, including textbooks, hands-on resources, assessment books, and Indigenous literature⁴².
- Kids Can Press, the largest Canadian-owned children's book publisher, operating since 1973⁴³;

⁴⁰ Oxford University Press has closed its K-12 Publishing Division. Oxford continues to be a member of CERC because some of its previously published materials are still sold to K-12 schools.

⁴¹ <http://www.annickpress.com/>

⁴² <http://www.portageandmainpress.com/>

⁴³ www.kidscanpress.com

- OwlKids Books, a children’s book publisher based in Toronto, that developed from the success of *OWL Magazine*. OwlKids publishes a range of subject areas, from picture books to activity books to non-fiction for children aged two to thirteen⁴⁴; and
- Orca Book Publishers, based in Victoria, B.C., an award-winning Canadian children’s book publisher.⁴⁵

All of ACP members’ firms are 100% Canadian owned.

Post-Secondary Publishers

Similarly, the post-secondary publishing market consists of a few large publishers and a large number of SMEs that publish textbooks and books specifically for the Canadian post-secondary market.

Many of the large publishers are members of the CPC’s Higher Education Group, including Pearson Canada, Nelson Education, McGraw-Hill Education and John Wiley & Sons. Aside from Nelson Education, these publishers are foreign-owned Canadian publishers. A number of other publishers are also members of CPC, including LexisNexis Canada, HarperCollins, and Penguin Random House Canada.⁴⁶

A number of SMEs also publish books that are used by the post-secondary market, the majority of whom are members of the ACP. These SMEs tend to be smaller niche publishers that produce more specialized post-secondary resources, often with an emphasis on Canadian content, including (among others):

- Fernwood Publishing and its literary imprint, Roseway, that publishes political books, often with a focus on Canadian authors and the Canadian context;
- Broadview Press, an independent academic Canadian publisher, that publishes a number of anthologies and has a broad range of titles in Literature/English Studies and Philosophy with a Canadian emphasis⁴⁷; and
- Irwin Law, an independent Canadian legal publisher.⁴⁸

University presses in Canada sell thousands of books to post-secondary institutions each year—both specifically designed for courses and used as secondary texts. The largest presses, such as University of Toronto Press, McGill Queens University Press, and University of British Columbia Press derive a significant proportion of their income from sales to post-secondary institutions. We understand that though university presses are non-profit organizations that operate either as departments of universities or as incorporated non-profit entities, university presses in Canada are expected to cover most of their costs from their revenues.

⁴⁴ <http://www.owlkids.com/books/>.

⁴⁵ http://www.orcabook.com/client/client_pages/landingpage.html. A full list of ACP members is publicly available here: <http://publishers.ca/images/downloads/Membership%20Directory.pdf>.

⁴⁶ A complete list of CPC’s Higher Education Group members is publicly available here: <http://www.pubcouncil.ca/membership.php>.

⁴⁷ <https://www.broadviewpress.com/home.php>.

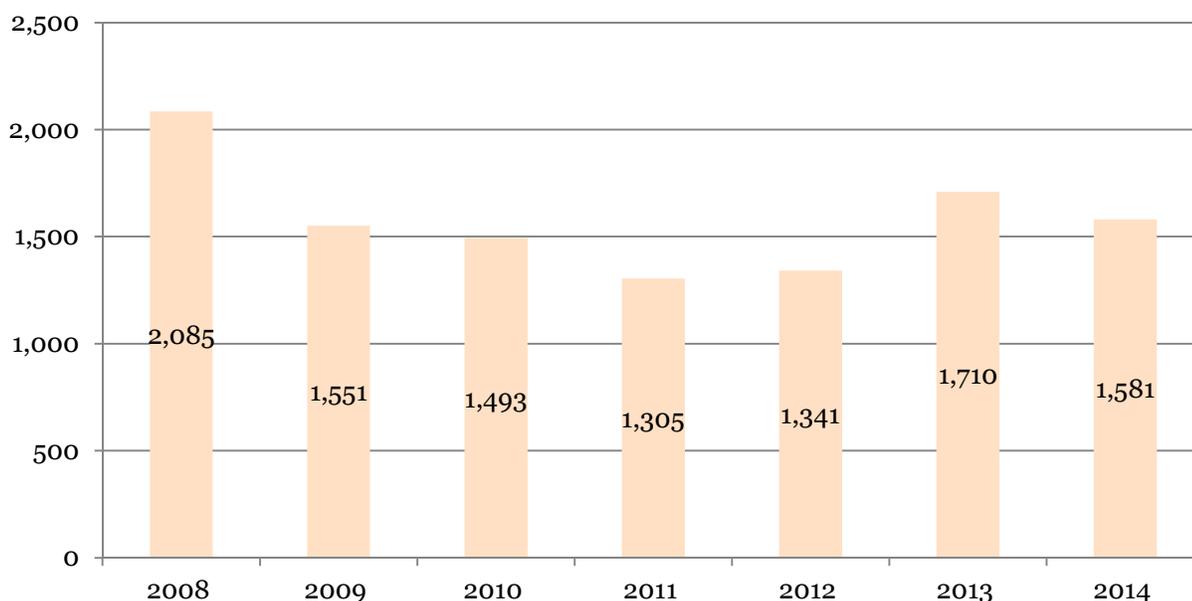
⁴⁸ <http://www.irwinlaw.com/about-us>.

In Canada, Canadian content appears to be a large share of business for all post-secondary publishers, whether large or SME. Large post-secondary publishers also reported a high proportion of adapted content, or content developed by authors outside of Canada and adapted for the Canadian market by Canadian authors.

Publishers Receiving Royalties from Access Copyright

A broad cross-section of Canadian publishers receive payments from Access Copyright for the copying of their works by K-12 schools and post-secondary institutions. The figure below illustrates that in aggregate over 2,000 Canadian publishers and their imprints received payments from Access Copyright for works used by K-12 schools and post-secondary institutions from 2008 to 2014.⁴⁹

Figure 9 – Number of Publishers Who Received Licensing Income from Access Copyright for Copying by Educational Institutions (2008 to 2014)



Publishers Included in This Assessment

For the purposes of measuring the economic footprint of the Educational Publishing Market in Canada and for assessing impacts of the Guidelines on this market, we have used data provided by CERC, CPC, the ACP and their members who produce content for and whose works are used by K-12 and post-secondary educational institutions.

The scope of this Assessment generally excludes the measurement of the Guidelines' impacts on other publishers whose works are used by the education sector, such as newspaper and magazine publishers. As a result, most of the publisher findings in this Assessment relate to book publishers whose content is used by educational institutions.

⁴⁹ Based on publisher payments data provided by Access Copyright.

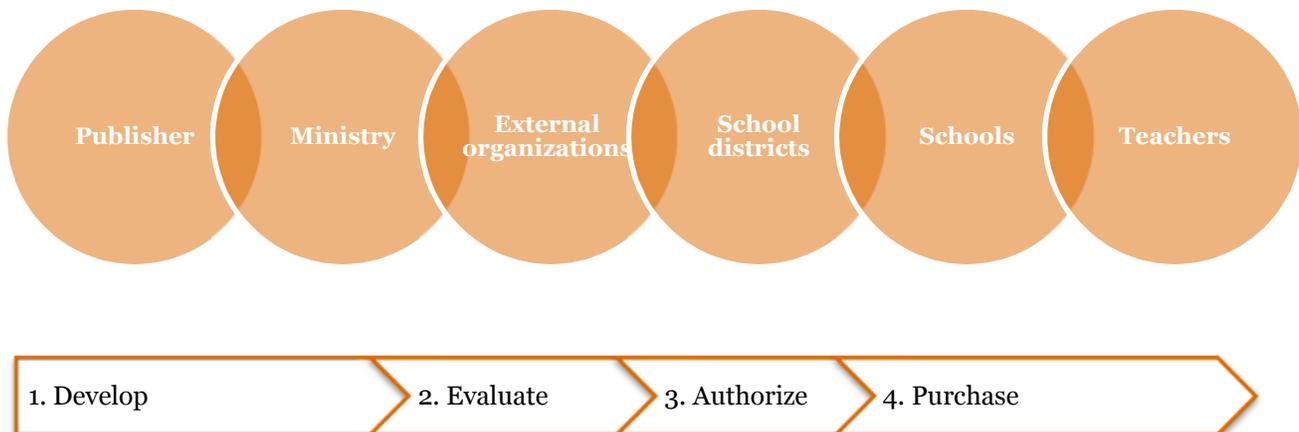
5.4 Production and Consumption of Educational Published Works

5.4.1 Publisher-Based Production Model for K-12 Materials

K-12 materials in Canada are produced in response to ministry-set curricula and are subject to a rigorous evaluation process at the provincial or regional level. This process involves significant development costs. Further, the variation in curricula among provinces means that economies of scale are limited for K-12 content producers.

K-12 materials in Canada have a unique production model. Before reaching the hands of students, K-12 learning resources traditionally pass through a rigorous process involving a number of different decision makers before a purchasing decision is made. The sale of learning resources in the K-12 sector in Canada has traditionally been driven by cycles of curriculum renewal and resource authorization at the provincial level. While there are significant differences in structure and process across all provinces, the figure below is a simplified representation of the four main stages in the purchasing process and the six players involved in the production of content and the purchasing decisions.

Figure 10 – Publisher-Based Model



Develop. The provincial Ministry of Education first sets curricula. K-12 publishers then develop resources based on the latest curricula established by each province in order to be eligible for approval and sale to schools. Individual curricula are regularly reviewed and major changes in curriculum occur at intervals of roughly seven to 10 years. Publishers spend a number of years working with creators to develop new learning resources that correspond to provincial curricula. A core group of writers—sometimes employed by the publisher and sometimes “freelance” writers—typically write the content and the internal publishing team edits, designs and polishes the product. Publishers work in tandem with ministries and schools

and new resources are often tested at schools and with teachers as part of the development process.

Evaluate. Before a core learning resource is approved for use in a classroom, it must be evaluated and approved at either the provincial or regional level. This second step further ensures the quality and specificity of the learning resources developed by publishers. Evaluation criteria may include curriculum fit, social considerations, and age or developmental appropriateness.⁵⁰ Some ministries evaluate resources in-house while others use outside organizations to do so.⁵¹

Authorize. In most provinces, the ministries approve resources and create a list of recommended resources. In some cases, publishers must complete a small print run in order to be considered for approval. Some ministries approve only core resources (e.g., Ontario and Alberta) while others approve both core and supplemental resources in some instances (e.g. Saskatchewan). In the case of Alberta, school districts and boards must approve all resources before they can be used in the classroom. Schools may be either required (e.g., in New Brunswick) or not required (e.g., in Saskatchewan) to buy approved resources.

Typically, Canadian ministries and educators require that educational resources reflect Canadian context, values and experience. This requires that many aspects of educational resources be written or customized to reflect that Canadian context, including pedagogy, images, spellings, geographic and historical references, expectations of general knowledge, assumptions about culture and ethnicity, examples from literature, specialized language, gender-neutral language, regulatory and professional references, and units of measurement.

The rigorous development, evaluation and authorization process described above requires significant levels of investment by the publisher. A typical core resource will cost between \$400,000 and \$800,000 to develop prior to acceptance by the Ministry of Education.⁵² Thus, these publishers incur significant investment costs in developing a product that is tailor-made to a particular provincial curriculum without any assurance that the resource will either be approved or ultimately purchased. Moreover, the requirements to tailor resources to provincial or regional curricula result in a market that is fragmented and unable to leverage significant economies of scale. The regional and curricular specificity of the materials also limit the export potential of these resources.

⁵⁰ See British Columbia Ministry of Education website: http://www.bced.gov.bc.ca/irp_resources/

⁵¹ In BC, a voluntary organization (the Educational Resource Acquisition Consortium, or ERAC) evaluates resources submitted by publishers for a fee. In Ontario, Curriculum Services Canada – a non-profit agency – evaluates textbooks. Publishers are charged an evaluation fee for each resource submitted.

⁵² Rollans, Glenn, and Michel de la Chenelière. *Study of the Canadian K to 12 Educational Book Publishing Sector*. August 2010, p. 28.

5.4.2 Consumption in K-12 Schools

K-12 schools consume a variety of paper and digital materials procured through different processes across the country. Copying of published content is widespread, estimated to total 350 million pages of books, magazines, newspapers, consumables and sheet music annually in Canadian K-12 schools outside Quebec.

In Canada, schools and school boards buy most educational content using money funded by the particular province. The ministries of education typically allocate funding on a per student basis to school boards. Boards then decide how to spend that money, with the bulk of the funding dedicated to salary and the remainder used for discretionary spending, including learning resources and technology. Some school boards make their own resource purchase decisions but most delegate resource decisions to the principal of each school.⁵³ School boards may purchase content directly from the publisher or distributor or through a government purchasing consortium (e.g., the Nova Scotia School Book Bureau).

Purchasing decisions in the K-12 sector involve various stages and a number of stakeholders, and the process varies greatly from jurisdiction to jurisdiction. As described above, ministries of education are involved in the development, evaluation, and authorization of K-12 resources. Schools and their boards make the final decisions to purchase. All purchasing decisions are ultimately constrained by budgets.

The copyright-protected works used in K-12 schools represent a variety of learning resources, including texts, videos, software, and other materials that teachers use to assist students in meeting the expectations for learning defined by provincial or regional curricula⁵⁴. Learning resources may include the following⁵⁵:

- **Core resources.** Core resources deliver substantially all of the requirements of a curriculum or program of study. Textbooks are usually, but not always, core resources.
- **Supplemental resources.** Supplemental resources are materials that help deliver curriculum requirements and build skills, but are not comprehensive reflections of a curriculum. They may however be developed and marketed based on specific curricular links, and sometimes cross-curricular links. Supplemental resources include:
 - **Consumables.** Consumables are resources that are designed and priced by the publisher to be used by a single student, such as workbook that a student writes in, and then kept by that student or discarded. Historically, consumables have been

⁵³ Often, department heads will make a pitch to the principal for which resources should be purchased.

⁵⁴ Definition according to the British Columbia Ministry of Education website:

http://www.bced.gov.bc.ca/irp_resources/

⁵⁵ Rollans, Glenn, and Michel de la Chenelière. *Study of the Canadian K to 12 Educational Book Publishing Sector*. August 2010.

extensively copied by K-12 teachers without authorization or payment even though publishers do not generally permit or intend for these works to be copied⁵⁶.

- **Reproducibles**, such as blackline masters, are designed by the publisher as a master for teachers with the expectation that they will be copied by teachers and provided to students in the form of a worksheet. Permission is given by the publisher to “reproduce” the masters.
- **Teacher resources** (e.g., lesson plans, recommended activities, assessment instruments). Teacher resources aim to guide teachers in the use of corresponding student resources. They are particularly important in supporting core student resources.
- **Other resources** (e.g., journal, magazine or newspaper articles, levelled texts, novels, dictionaries, atlases, and software instructional guides and other materials). Other resources may be selected by a teacher and distributed to students to supplement the other categories of educational resources listed above.

All of these learning resources can be purchased or copied. Copies may be provided to each student enrolled in a class or course as

- **a print copy**, which is selected by a course instructor, copied, and distributed to students as a class handout;
- **a digital copy**, in which case, the learning resource is posted to a Course (or Learning) Management System (CMS) or another digital repository. The CMS allows the distribution of content online by a teacher for use by students and often provides features for online collaboration. A CMS is generally password-protected or otherwise restricted to teacher, students, and sometime parents of a school, school board, or Ministry. School boards often maintain their own repositories or databases that can be used to store and share content.

Copying of published works in schools is widespread according to industry experts and market participants. The paper copying budget per student is estimated to be about \$15 whereas the overall resource budget (not including photocopying) is in the range of \$60 to 70 per student⁵⁷. A study conducted for the Copyright Board’s 2010-2015 K-12 tariff proceedings revealed that approximately 350 million pages of books, magazines, newspapers, consumables, and sheet music are copied annually by K-12 schools in Canada (excluding Quebec).⁵⁸ This estimate excludes digital copying that has been increasing in recent years due to technological advancements.

⁵⁶ Circum estimates that over 110 million pages of consumables are copied each year by K-12 schools.

⁵⁷ Estimates are based on our conversations with industry consultant Glenn Rollans.

⁵⁸ Volume estimates are based on an expert report prepared by Circum on behalf of Access Copyright, publicly filed as Exhibit AC-67 as part of Access Copyright’s case during the 2010-2012 and 2013-2015 K-12 tariff proceedings before the Copyright Board of Canada

5.4.3 Publisher Production Model for Post-Secondary Materials

Post-secondary materials are not subject to the same centralized development and approval process that exists for K-12 materials. As such, there is a greater range of market participants and greater use of imported content than in the K-12 sector. Developing post-secondary materials is a time- and capital-intensive process.

The publisher production model to create published works for post-secondary institutions differs significantly from the K-12 production model. While some works relating to professional or trade subjects are developed according to standards set by industry bodies, there is generally no formal approval process involving direct collaboration with education ministries or post-secondary institutions for the development of works in this market. Rather, publishers seek to produce post-secondary works that align with course content that will therefore be selected by individual professors, faculties or departments.⁵⁹ The lack of a single approved work (as compared to the K-12 sector) results first, in the existence of a greater number of market participants (the number of publishers receiving royalties from Access Copyright in the post-secondary segment was more than triple the number in the K-12 sector in 2014); and second, a higher use of imported works.

The production of post-secondary works involves significant development costs; for instance, the Association of American Publishers has estimated that the production of a new or revised textbook will require between \$0.5-\$3 million in costs, 7,000 hours of research and writing and the input of nearly 200 scholars.⁶⁰ As a result of these costs, large enrolment subjects and the more standardized curriculum of first-year courses offer the greatest scale advantages to publishers. New editions of textbooks are generally published every three to four years.⁶¹

5.4.4 Consumption in Post-Secondary Institutions

When it comes to selecting materials in post-secondary institutions, professors are the primary decision-makers. Materials are made available to students through the mandatory purchase of books or coursepacks (a collection of copied excerpts), or through online course management systems.

Students are the ultimate main consumers of both original and copied published works in the post-secondary Educational Publishing Market. As a result, students usually incur the purchasing costs. However, course instructors are the driving force behind their decisions to consume. Professors are key decision makers and, in practice, act as agents for students. There

⁵⁹ See, for instance, *Study of the Canadian K to 12 Educational Book Publishing Sector*, by Glenn Rollans and Michel de la Chenelière, August 2010, Department of Canadian Heritage.

⁶⁰ *11 Things You Don't Know about Textbooks and Publishers*, Association of American Publishers, August 11, 2014, <http://publishers.org/news/11-things-you-didnt-know-about-textbooks-and-publishers-o>.

⁶¹ See, for instance, *Study of the Canadian K to 12 Educational Book Publishing Sector*, by Glenn Rollans and Michel de la Chenelière, August 2010, Department of Canadian Heritage.

are multiple potential factors that may influence the decision of an instructor as to what material to require and provide their students. The factors include the following⁶²:

- **Appropriateness:** What is the most appropriate vehicle for teaching the course? For instance, compilations of articles and chapters may be appropriate for advanced courses but not for introductory courses.
- **Convenience:** What is the most convenient format for both instructors and students? Textbooks require the least amount of effort on behalf of instructors, whereas designing course collections are likely to be more labour intensive⁶³. Instructors may also consider the convenience and ease of access to students, for whom material posted online may be easier to retrieve.
- **Cost to students:** Affordability of material may play a role in the instructors' decisions.
- **Financial incentives:** Instructors may benefit financially from using material that they have themselves created, for example, a textbook they wrote.

For any course, the instructor may generate the use of published works by students through any of the following:

- **By requiring or recommending that students purchase a book (textbook, anthology, or other).** The student pays for the original work at the point of sale. Payment for the purchase of the work is made to the copyright owner.⁶⁴ The student may also purchase a used book in which case no payment is made to the copyright holder.
- **By requiring or recommending that enrolled students purchase a coursepack.** A coursepack is a collection of works (journal, magazine or newspaper articles, book excerpts and other materials) selected and compiled by a course instructor and copied and bound into a collection for distribution and sale to students. Coursepacks can represent the core or only resource for a course or can be used as a supplementary resource that complements other content. When coursepacks are created and sold, they often substitute for the purchase of the original material contained within the compilation.

Coursepacks are usually produced by bookstores within post-secondary institutions or copy shops servicing those institutions. Those bookstores and copy shops historically obtained permission from copyright holders or Access Copyright and embedded copyright fees for the right to copy in the price of the coursepack. Copyright fees for the right to copy content into paper coursepacks are paid and collected at the point of sale.

⁶² Factors identified through discussions with industry stakeholders including direct conversations with professors at colleges and universities across Canada

⁶³ This may be less so for digital coursepacks than for print coursepacks.

⁶⁴ In this circumstance, the purchaser only pays for the primary consumption: the payment does not include the right to copy the book or any additional consumption.

Universities and colleges engage in extensive copying of published works for use in coursepacks. Between 2010 and 2012, the average volume of paper coursepack copying reported by post-secondary institutions to Access Copyright was approximately 125 million pages per year.⁶⁵

- **By posting material online on their Course Management System, or CMS.** The CMS allows the distribution and copying of content online by a professor for use by students and often provides features for online collaboration. The CMS is often used to provide required, supplementary and ancillary materials (such as problem sets) to students. As digitization progresses in post-secondary education, it is expected that digital coursepacks⁶⁶ will continue to gradually substitute for the purchase of paper coursepacks. At this time, there is no point of sale for the payment and collection of copyright fees for these materials. We refer to the term “course collections” to encompass both print and digital coursepacks.

The above forms of uses are not mutually exclusive. Students are often consumers of both original and copied materials for a given course (e.g., they may purchase a textbook and access copies of the same or different content online or on a CMS to which they have access).

⁶⁵ Volume estimates are based on an expert report prepared by Circum Network Inc. on behalf of Access Copyright, filed as Exhibit AC-5 as part of Access Copyright’s case for the proposed 2011-2013 Post-Secondary Educational Institutions Tariff before the Copyright Board of Canada. This volume does not take into account other copying of published works, such as paper handouts and copying on CMSs.

⁶⁶ Digital coursepacks are identical in concept to paper coursepacks but may differ in format; they could be made of different files and posted on a CMS, compiled as one PDF and posted, or emailed.

6. *Economics of the Market*

In this section, we provide an overview of the income derived by content producers from sales income and licensing income. We also discuss the economic contribution of the Educational Publishing Market to the Canadian economy.

6.1 *Sales Revenues*

Sales are generated, for the most part, from schools and school boards in the K-12 market and from bookstores or direct sales to students in the post-secondary market. Sales revenues in both markets have declined quite sharply in recent years.

As discussed in Section 5.4.2, most K-12 published works are purchased by schools and school boards using funds allocated by provincial ministries of education. Based on data provided by CERC and interviews with industry experts, we estimate the total revenue earned by producers of K-12 content from sales was approximately \$137 million in 2013. Sales revenues have been declining since 2008, and the pace of this decline has accelerated significantly since 2012, as discussed in more detail in Market Trends (Section 7) below.

Post-secondary publishers sell directly to post-secondary institutions, often through university bookstores, or directly to students. These sales result in compensation from the consumer (university/college, instructor, student) to the publisher and ultimately to the creator, who is paid in the form of royalties based on sales revenues. Based on data provided by CPC and interviews with industry experts, we estimate the total revenue earned by post-secondary publishers⁶⁷ from sales was approximately \$403 million in 2013. Sales have also been declining in the post-secondary market, as outlined in Section 7.

6.2 *Licensing Income*

Licensing income is generated for content producers through Access Copyright licences and direct permissions licences between content producers and educational institutions. Revenues from both sources have been falling in recent years.

Licensing income is paid by content users to content producers when works, or portions of works, are copied. Historically, content producers in Canada receive licensing income in two ways:

⁶⁷ This figure includes only revenues collected by large educational publishers and SMEs publishers whose works are used by the education sector. It does not include certain other content producers whose works may be used in the education sector, for instance newspaper and magazine publishers, and therefore underestimates the revenue generated by activities leading to the supply of works to the education sector.

- through Access Copyright (or Copibec in Quebec), who collect royalty payments from users under licence and distribute those royalties to creators and publishers (referred to in this report as “collective licensing”); and
- from direct permissions licensing, where content users request licences from and pay income directly to creators and publishers for the right to copy their content (referred to as “permission licensing requests”).

In 2012 (the last year before the introduction of the Guidelines) Access Copyright distributed approximately \$18 million in licensing fees to content producers.⁶⁸ In 2014, immediately following the introduction of the Guidelines, the amount distributed to content producers declined to approximately \$10 million, primarily because the provincial government Ministries of Education (outside Quebec) stopped paying the Access Copyright licensing fees as of January 1, 2013.

Figure 11 – Value of Distributions from Access Copyright to Content Producers of Works Used in Post-Secondary Institutions and K-12 Schools⁶⁹



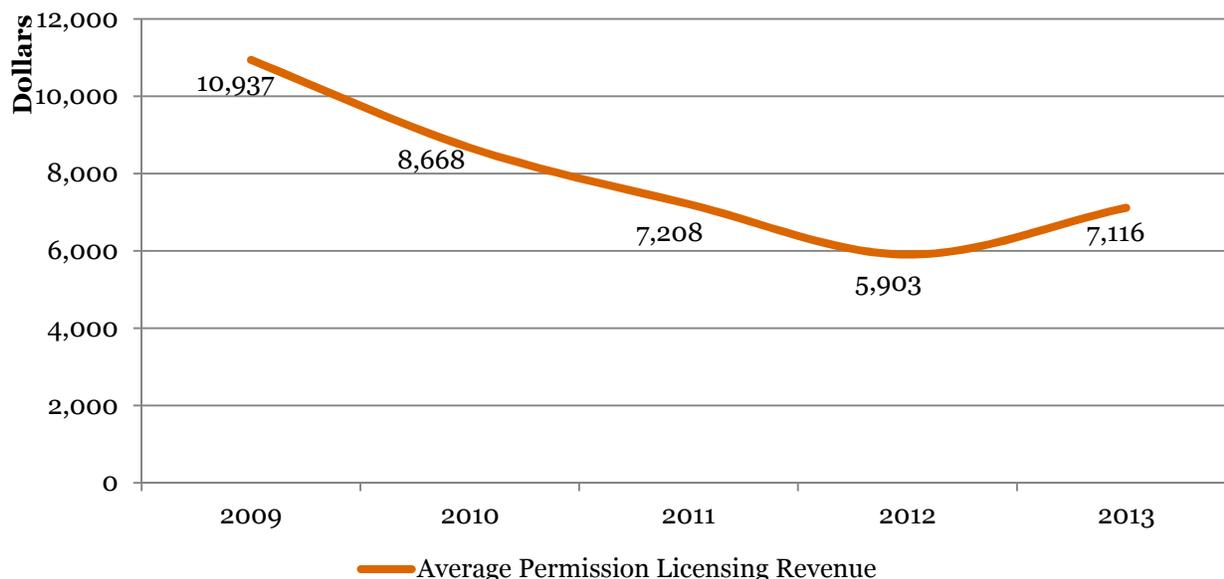
Complete data on direct permissions licensing income and the number of permission licensing requests was not available from publishers. However, a review of partial data that we have received from large publishers suggests that both the number of permission licensing requests and direct permissions licensing income received by large publishers declined significantly from 2009 to 2014. Further, since 2009 direct permissions licensing income has been an insignificant portion of total licensing income (less than 10%) and total revenues (less than 1%).

⁶⁸ This amount does not include a special distribution made in 2012 of retroactive funds resulting from the Copyright Board ruling related to the 2005 to 2009 K-12 tariff.

⁶⁹ In 2012, publishers and creators received a retroactive distribution for 2005 to 2009. We have allocated the approximate amount of this distribution to 2008 and 2009 based on an equal annual allocation for each year in the 2005 to 2009 period.

For SME publishers⁷⁰, permissions licensing revenues decreased in absolute dollars by close to 50% between 2009 and 2012, with a slight rebound in 2013.⁷¹ Permissions licensing revenues remain down 35% from 2009. The trend in the average permissions licensing revenues for SME publishers is shown in Figure 12 below.

Figure 12 – Average Permissions Licensing Revenues for SME Publishers



6.3 Economic Footprint of the Educational Publishing Market

The Educational Publishing Market has a significant footprint in the Canadian economy in terms of output, jobs, GDP, and tax revenue, but this footprint has shrunk greatly since 2011. Publishing industry jobs are relatively high value, with an average industry salary of \$69,000, more than 40% higher than the Canadian average across all industries. High-value jobs are indicative of high labour productivity, critical to the development and success of a knowledge-based economy.

Methodology for measuring the educational publishing industry’s economic footprint⁷²

The fundamental premise behind economic footprint analysis is that spending on goods and services has attendant impacts throughout the economy. For instance, spending on textbooks generates demand for the inputs to those services (including labour) that in turn generates

⁷⁰ Data were obtained from the ACP Survey from all publishers who provided complete data with respect to permissions licensing (i.e. publishers who provided permissions licensing data for all years from 2009 to 2013).

⁷¹ This increase was primarily the result of an increase in permissions revenue for one publisher.

additional demand that extends beyond the initial spending. Input-output analysis permits the estimation of this cascading effect by using the multipliers calculated by Statistics Canada based on an input-output model of the Canadian economy.⁷³

Economic footprints are estimated by the following standard measures of economic activity:

- **Gross output** is the total gross value of all business revenue. The broadest measure of economic activity, it indicates the total sales and transactions triggered by operations.
- **Value added or GDP** refers to the value added to the economy, or the unduplicated total value of goods and services. GDP includes only final goods to avoid double counting of products sold during a certain accounting period.
- **Employment** refers to the number of jobs created or supported. It is expressed as the number of equivalent full-time jobs indicated in person years.
- **Direct footprint** results from the publishing industry's spending on suppliers and employees.
- **Indirect footprint** arises from the activities of the firms providing inputs to the publishing industry's suppliers (in other words, the suppliers of its suppliers).
- **Induced footprint** is the result of consumer spending by employees of the businesses stimulated by direct and indirect expenditures.
- **Total economic footprint** equals the sum of the direct, indirect, and induced economic footprints.

Estimated economic footprint

In 2013, total gross revenue earned by content producers (publishers and creators) from post-secondary content was estimated to be approximately \$417 million, and total revenue earned by producers of K-12 content was approximately \$137 million. Comparatively, in 2011, prior to the introduction of the Guidelines, total gross revenue from post-secondary content was \$487 million and K-12 was \$177 million.⁷⁴ These figures include only sales and licensing revenues collected by large educational publishers and SMEs publishers whose works are used by the educational sector. Quebec revenues are excluded from the K-12 amounts noted above, but are included in the post-secondary amounts due to data limitations. Further, these figures do not

⁷² Input-output analysis, used to estimate economic impacts, does not address whether the inputs have been used in the most productive manner or whether the use of these inputs in a given industry promotes economic growth by more than their use in another industry or economic activity. Nor does input-output analysis evaluate whether, when or where these inputs might be employed elsewhere in the economy if they were not employed in a given industry at this time. Input-output analysis studies the direct, indirect and induced economic impacts that can reasonably be expected to result in the economy when these inputs are used in a given industry, based on historical relationships within the economy.

⁷³ The multipliers used in this report are those calculated by Statistics Canada for the newspaper, periodical, book, and directory publishing industries.

⁷⁴ These amounts include primary sales and secondary revenue from royalties collected by Access Copyright and primary sales revenue from the CPC (Canadian Publisher's Council) and CERC (Canadian Educational Resources Council), which include the seven largest publishers in the post-secondary segment and the six largest publishers in the K-12 market. Based on discussions with these organizations, we have developed a market share assumption to estimate the size of the remainder of the market (large and SME publishers).

include revenues earned by certain other content producers whose works may also be used in the educational sector, for instance newspaper and magazine publishers, and therefore underestimate the total economic footprint of the Educational Publishing Market.

As shown in Table 3 below, the total economic footprint of the educational publishing industry in Canada⁷⁵ is significant – representing approximately \$1.2 billion in output and \$620 million in GDP in 2013. That being said, the economic footprint of the educational publishing industry is substantially lower than its 2011 total output of \$1.4 billion and GDP of \$740 million.

Table 3 – Total Estimated Economic Footprint⁷⁶

	Output (millions)		GDP (millions)		Jobs	
	2011	2013	2011	2013	2011	2013
Post-secondary market	\$1,060	\$900	\$550	\$470	5,610	4,800
K-12 market	\$380	\$300	\$200	\$150	2,030	1,580
Total Educational Publishing Market⁷⁷	\$1,440	\$1,200	\$740	\$620	7,650	6,380

Employment

As shown above, the educational publishing industry⁷⁸ has a significant economic footprint in the country, comprising over 6,000 jobs (on a full-time equivalent basis) in Canada across numerous industries in 2013. Despite its significance, the 2013 GDP and employment footprints reflect a decline of more than 15% since 2011.

This footprint is enhanced by the fact that publishing industry jobs are high value jobs that are critical to a knowledge-based economy and are paid significantly more than the average income in Canada—the average publishing industry salary is approximately \$69,000, more than 40% higher than the Canadian average across all industries of \$48,000.⁷⁹

The relatively high salary of publishing industry jobs could be indicative of relatively higher labour productivity in the industry compared to the economy overall. Statistics Canada data indicates that the average real labour productivity per hour in the information and cultural industries in Canada (of which the publishing industry is a part) is approximately 60% higher than the overall average for the Canadian economy.⁸⁰ Globalization has created formidable

⁷⁵ Excluding the Quebec K-12 publishing industry but including the Quebec post-secondary publishing industry.

⁷⁶ Based on Statistics Canada’s Input-Output National Multipliers, Tables 3.1, 3.2, and 3.5.

⁷⁷ Differences from the sum of the totals shown due to rounding.

⁷⁸ Excluding the Quebec K-12 publishing industry but including the Quebec post-secondary publishing industry.

⁷⁹ Based on a comparison of average weekly earnings from November 2013 to November 2014 of all industries and the publishing industry (except Internet-based publishing)—NAICS code 511. Obtained from Statistics Canada Table 281-0026, Average weekly earnings.

⁸⁰ CANSIM Table 383-0029, labour productivity in chained (2007) dollars per hour for the total economy and the information and cultural industries (NAICS code 51) in 2013.

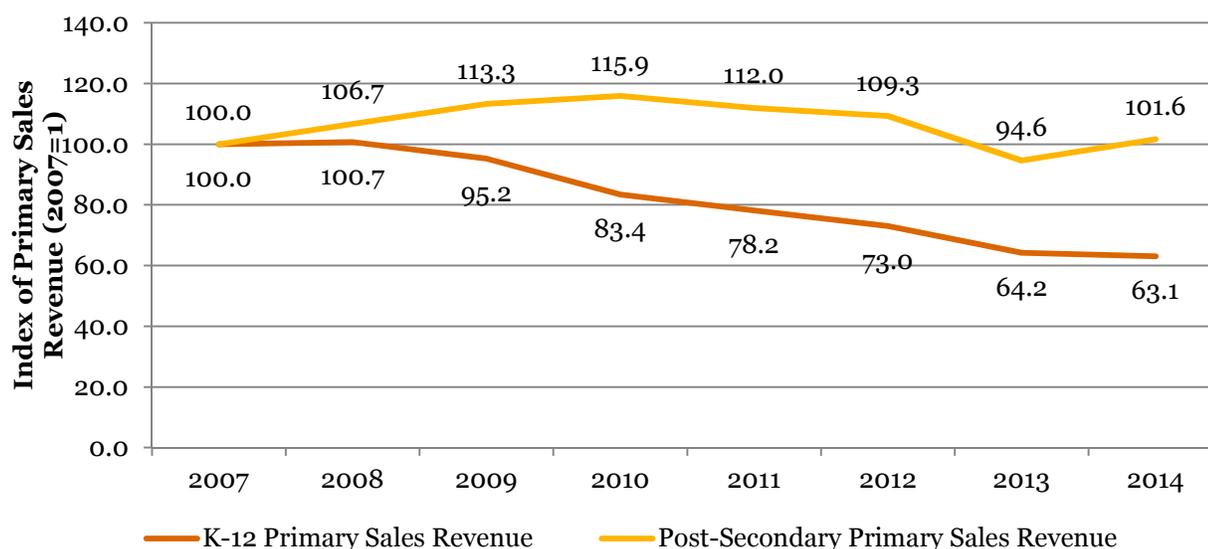
challenges to developed countries such as Canada in maintaining a high standard of living while avoiding economic polarization in their societies. It is widely accepted that the answer to those challenges is the creation of a knowledge-based economy which produces high-productivity jobs in industries such as the publishing industry.

7. Market Trends

The prevalence of copyright infringement and of unpaid copying, constraints on buying K-12 content, and pressures both to develop and compete with digital alternatives have subjected the Canadian Educational Publishing Market to significant change.

The size of the Educational Publishing Market has been declining in recent years. Figure 13 depicts the trend in the annual sales revenues by large educational publishers (representing a significant share of the market) in the K-12 and post-secondary markets. Between 2008 and 2014, sales revenue declined by 40% in the K-12 market. In the post-secondary market, sales revenue declined by 12% between 2010 and 2014. The trend of negative growth (starting in 2008 for K-12 and 2010 for post-secondary) indicates that declines in the print educational materials market have not been compensated by increases in the digital educational content market. With this decline in sales, publishers are facing the challenging task of changing their business model to develop and incorporate innovative digital content, services and delivery (discussed in Section 7.1.2 below) while experiencing reduced revenue that leads to reduced profitability. This indicates a significant level of vulnerability by publishers to further adverse changes in the future.

Figure 13 – Index of Primary Sales Revenues for Educational Publishers (2007 Base Year)⁸¹



⁸¹ Revenue amounts for the K-12 publishing industry exclude Quebec. Revenue amounts for the post-secondary publishing industry include Quebec due to data limitations. These amounts reflect the sales of all material, including print, digital and blended formats.

The declining size of the Educational Publishing Market is driven by the following factors:

- a decline in public funding for educational content in the K-12 sector;
- the transition to digital publishing (although creating an opportunity for some publishers, the transition to digital content is substituting for and displacing print material while creating avenues for new sources of competition, including self-publishing and open access content);
- the growth of the used book market (the used book market has become increasingly centralized and coordinated, allowing students to forego new purchases of textbooks);
- rental programs for post-secondary textbooks (book rentals have increased through providers such as Amazon and specialist providers⁸²);
- the prevalence of copyright infringement and piracy, as evidenced in an increase in peer-to-peer file-sharing and downloading; and
- the prevalence of unpaid copying (teachers/professors and students are copying without paying royalties; professors are putting content on their CMS without paying royalties).

These factors and other trends impacting the Educational Publishing Market are discussed in further detail in the sections below.

7.1.1 Emerging Models for K-12 Materials

Limited funding for educational content is shaping the emerging model for the development of K-12 materials. The model primarily consists of repurposing published content. Digital file-sharing facilitates the use of copied content under this model.

Public education has been generally perceived as underfunded in recent years. In particular, new funding to allow the purchase of new learning resources has not been a priority. It is difficult for teachers to obtain the learning resources they need for their classrooms, and some teachers purchase their own content.⁸³ Teachers often use learning resources that have not been evaluated and recommended at the provincial or district levels.

Faced with shrinking budgets, ministries, schools districts, schools and teachers are looking for more inexpensive avenues to acquire learning resources. Administrators in K-12 education tend

⁸² “Pearson: J Wiley read-across: no relief near.” Liberium Capital, 8 Mar. 2013, available from Thomson Reuters, accessed 5 July 2013. Amazon for example rents digital textbooks for a cost that can be as low as 20% of the original hardcover cost. Mathis, Joel. “Grading Apple’s digital textbook technology.” Macworld, 28 May 2013. Web. 24 July 2013.

⁸³ See, for instance, Alberta Teachers’ Association, “Teachers Spend Own Money to Buy School Books and Materials,” *ATA News* Volume 35 2000-01.

to view educational content as discretionary spending and as a flexible item in their budgets.⁸⁴ Indeed, since content is not tied to a specific share of the school budget, unlike salaries and other expenses, these learning resources are commonly targeted during budget cuts.

As a result of the search for low cost delivery of education, there are initial indications that the K-12 sector in Canada is trying to develop new models that will partially or fully replace the Publisher-Based Production Model (discussed in Section 50 above) by, among other things, resorting to technology.⁸⁵ A number of new offerings and disruptive business models increase the ability of administrators to substitute away from the Publisher-Based Production Model to save money.

In recent years, provinces are increasingly decentralizing the purchasing process and allowing for greater flexibility at the local level⁸⁶ and are thus developing alternatives to the Publisher-Based Production Model.⁸⁷

Some of the common aspects of the decentralization appear to be as follows:⁸⁸

- a collaborative digitally based learning environment;
- the co-creation of curriculum involving various stakeholders; and
- fewer learning outcomes in the curriculum to allow for local flexibility.

The digitization of content is seen as an opportunity for education administrators to minimize outside purchasing and curtail purchases from the publishing sector. This is being achieved through the following mechanisms:

- generating content in-house, including the digitization of copyright-protected content and in-house development of materials, whether at the teacher, school board or ministry level⁸⁹;

⁸⁴ *Consultation on K to 12 Educational Publishing in Canada*, by Glenn Rollans and Simon de Jocas (prepared under the direction of the Association of Canadian Publishers Education Committee), 2012, p. 11.

⁸⁵ Rollans, 2012, p.28

⁸⁶ Alberta Education. Curriculum Redesign: Shifts for Provincial Curriculum. Online: <https://education.alberta.ca/department/ipr/curriculum/about/what-will-change/> Accessed on November 15, 2013.

⁸⁷ In British Columbia, the Ministry of Education is pursuing a grassroots and continuous approach to curriculum development, enlisting the help of school districts and schools. BC Ministry of Education. Exploring Curriculum Design: Transforming Curriculum and Assessment. January 2013. Online: http://www.bced.gov.bc.ca/irp/docs/exp_curr_design.pdf. Alberta is in the midst of a Curriculum Redesign Project that will “seek out opportunities to partner with teachers, publishers, post-secondary institutions, school authorities, resource developers and information technology companies in curriculum development.” In August 2013, Alberta Education invited publicly-funded Alberta school authorities to serve as lead vendors in developing proposals for the co-development of new digitally based curriculum for K-12. Proposals must include identified and/or developed learning resources. The Alberta Teachers’ Association. Memorandum: Alberta Education’s New Curriculum Renewal Process. 26 Sept. 2013. Online: <http://www.guidancecouncil.ca/wp-content/uploads/2013/10/Scanned-from-a-Xerox-multifunction-device.pdf>.

⁸⁸ Alberta Education, 2013.

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- increasing copying and sharing of published content between schools and teachers;
 - increasing use of content sourced from the Internet; and
 - making more use of open-source educational content, that is, publicly available or publicly funded content that can be copied and shared for free.

Many of the above emerging models rely to a large extent on copying of existing published works (as opposed to original content produced by teachers) as a source for content. As discussed below, the Guidelines facilitate the transition to this model by promoting the free copying of portions of published works.

Open Educational Resources (OER) are a threat to traditional publishers as they provide textbook and course materials for free⁹⁰. Some school boards have access to digital content developed by the Ministry and/or teachers free of charge. Most provinces already have repositories of learning resources generated by schools and teachers locally. For example, school boards participating in e-Learning Ontario have access to the Ontario Educational Resource Bank, which offers thousands of digital resources contributed by teachers and teacher-librarians to support instruction in all grades.⁹¹

For now, exchanges of content between provinces remain limited however this is expected to increase in the future.⁹² As purchasing and authorization become more decentralized, this will facilitate collaboration and exchanges of content between jurisdictions.

Major media players such as Apple and Google are also emerging as a new source of disruption to the K-12 publishing industry by seeking to introduce new business models and alternative content distribution channels.⁹³

⁸⁹ Open School BC creates educational resources owned by the BC Ministry of Education. Schools and districts are also developing their own resources. The ERAC offers to help schools and districts market resources they have developed. LearnNowBC offers a variety of free online resources including locally developed online resources from schools and school districts. The e-Learning department in the Learning Division of the BC Ministry of Education has links on its website to both Open School BC and LearnNowBC. The mission of the department is to “monitor existing and emerging educational technologies and work with stakeholders to promote and support their integration into K-12 teaching practices”. Ministry of Education, Learning Division. Online: <http://www.bced.gov.bc.ca/departments/learning/>.

⁹⁰ “Pearson: not yet.” Morgan Stanley Research, 17 May 2013, available from Thomson Reuters, accessed 5 July 2013.

⁹¹ <https://resources.elearningontario.ca>.

⁹² As an example, Alberta’s Learning Resources Centre offered some content developed for BC, but sales were negligible. The Resources Centre has since closed.

⁹³ Rollans, 2012, pp 20-21.

7.1.2 Emerging Publisher Business Models

In response to rapid technological change, publishers have developed innovative revenue models, including customized publishing, disaggregated content, and digital platforms. These models are intended to offset revenue declines from traditional print-resource offerings.

The digitization of materials requires post-secondary publishers to invest heavily in content platforms. SME publishers compete with a number of heavily capitalized larger publishers, which makes it particularly difficult to service multiple channels and maintain competitiveness in a shrinking market. To date, gains in digital content sales in the post-secondary market have been made mostly in blended (paper and digital) offerings; however, these do not generate more revenue relative to paper-only offerings.

In the K-12 market, the purchase of digital content has not kept pace with hardware investments or with declines in government spending on print content. The imbalance reduces the incentive for publishers to invest in digital solutions for this market. Large K-12 publishers are generally pessimistic about the economic viability of content creation for this market and are endeavouring to shift their focus to creating platforms upon which content may be delivered rather than the content itself.

Professors and students in post-secondary institutions have been embracing the internet and digital offerings have been increasing to try to match this growing demand. Some industry experts believe that in the future, online learning alternatives such as “massive open online courses” (MOOCs) may offer open content to displace traditional published works. Should this trend materialize, it is expected to put additional pressure on traditional educational publishers.

In response to this trend, many publishers have attempted to offset declines in revenues from print materials with new revenue models and content that offer new learning experiences to students. These models include customized publishing, disaggregated content, digital platforms, and value added digital components which supplement traditional materials:

- **Customized publishing** enables professors and teachers to draw from libraries of texts and collections and their own original material to design learning solutions for their students. This has enabled publishers to tailor products to their customers but also to provide them with a range of price points.
- **Disaggregated content**, such as e-chapters, is being offered by some publishers through their websites.⁹⁴ As with custom publishing, this provides customers with the convenience and ability to ‘mix-and-match’ as well as the ability to pay only for content that they require on various platforms.

⁹⁴ See, for example, NelsonBrain.com, which offers students various format options including e-chapters, e-books and traditional print format: <https://www.nelsonbrain.com/shop/discover/DiscoverHome.html>

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- **Digital platforms** are the focus of large post-secondary publishers. These publishers are intensively investing in the development of interactive innovative digital platforms for students to supplement their (print or digital) textbooks, such as study and practice guides and homework features. These enhancements link back to the text of the textbooks and include elements that enhance the learning experience, such as sample quizzes, interactive homework solutions, animations, video links, and games.

However, the transition costs of developing and adopting digital content and delivery are relatively high. Canadian-owned and small publishers have reported their inability to maintain competitiveness in the face of rising levels of technology investment⁹⁵. SME publishers are competing with more heavily capitalized larger publishers, which puts them at a disadvantage. Serving multiple channels and ever-increasing demands for functionality in a shrinking market is challenging for SME publishers. Unlike their large and mostly internationally-based counterparts, these publishers are unable to leverage the same economies of scale and broad range of products in developing publishing technology platforms, as they typically serve a narrower customer base. Many SMEs focus on niche educational areas, which do not have the potential market size as high enrolment courses such as engineering or science.

Despite these challenges, we understand that a significant number of SME publishers are innovating, embracing technological changes and the related changes in their business models. As examples on the digital front, Brush Education is

- developing new titles in an xml-first workflow, which allows efficient multi-channel publishing (digital and print) and secure, application-agnostic archiving,
- publishing all new titles in both print and digital formats,
- testing print/digital bundles,
- selling ebooks directly to consumers through its website (as well as through all major e-retailers),
- bundling audio and video with some titles,
- developing app versions of selected titles, and
- experimenting with “chunked” digital content for selected titles.

Seventy-five percent (75%) of Portage and Main Press’s content is now digitized. Portage and Main

- is publishing books in multiple formats and selling ebooks through numerous partners,

⁹⁵ *Supporting Canada’s Educational Publishing Sector in a Digital Economy* (Nelson Education, 2010). Online: <http://www.ic.gc.ca/eic/site/O28.nsf/eng/OO213.html>

-
- will host a subscription service with access to e-units of study on World History, Canadian History, accompanying teacher guides and other resources (launching in August 2015),
 - is creating interactive activities for science and is selling digital reproducible masters (often as a “bundle” with print books), and
 - is partnering with a web development firm to create assessment software.

While SMEs are actively pursuing these innovative projects and business models, they remain very cautious about the projects they choose to digitize given their low profit margins, the significant costs of investing in digital and the uncertain market conditions.

Large post-secondary publishers focus investment in digital solutions on high enrolment courses with sufficient scale to generate a profit and/or courses in lucrative study fields where updated content is essential. Introductory courses in science and engineering, for instance, require updated material and generally exhibit high enrolments. These are the subject areas where publishers are most likely to recoup their investments in new interactive digital platforms. By contrast, upper year social sciences courses with lower enrolment and a lesser emphasis on recent material will likely not benefit significantly from the digital transformation.

In spite of the strategic focus on the digital transition, digital content still accounts for a relatively small share of sales in the Canadian Educational Publishing Market. Between 2013 and 2014, the share of revenue from digital works for the seven largest post-secondary publishers in Canada increased from 3% to 6%.⁹⁶ This increase in digital resource revenues has not offset the significant decline in revenues from print materials, which continue to represent the large majority of publisher revenues. Further, most gains in digital content to date have consisted primarily of an increase in blended content, which combines print and digital components for generally the same price as print alone. As a result, publishers have borne the costs of investing in digital solutions, on top of having to maintain their material offered in print in order to protect their market share and in response to continuing customer demand for print. As such, notwithstanding their size, there are also concerns that, in an era of declining profits, even the large players will face cost pressures, which may hinder their transition to digital⁹⁷.

The K-12 educational system in Canada has also stated that it wishes to transition to digital content and away from print content. However, this transition is still in its infancy. While some school districts have made significant investments in hardware to make their classrooms “digital ready”, many other schools report difficulties in implementing digital ready classrooms. Moreover, any investment in hardware has, for the most part, not been matched by an increase in purchased content and many schools appear unwilling or unable to pay for digital content. Thus, the sales of digital content to K-12 schools remain a relatively small portion of the

⁹⁶ CPC data.

⁹⁷ Macquarie Equities Research, 2013

educational content market—estimated by one industry expert to be 5% of total K-12 sales.⁹⁸ Print content continues to comprise the vast majority of all K-12 sales.

Large K-12 publishers are generally pessimistic about the economic viability of content creation for this market and have started to shift their focus to the platforms upon which content may be delivered rather than the content itself. By moving into new areas of IT services and software, publishers can also help schools better manage data and operate more efficiently.

Pearson, for example, is building a broader services business globally, which will include providing more software (e.g., MyLab, a digital platform), data and IT services (e.g. e-learning). Publishers are hoping that by bringing an entire suite of products to market they will successfully compete against traditional technology providers such as Apple⁹⁹.

Although some K-12 publishers are hoping to replace sales losses with the above noted services, the ability of the K-12 market to absorb these services is questionable given the budget restrictions in K-12 schools. Hence, it is unclear whether publishers will make the required substantial investment and whether such initiatives will be successful. According to analysts, “it’s difficult to size the market, growth potential or profitability”¹⁰⁰. From interviews with executives in the educational publishing industry, we understand that large publishers are generally committed to invest in transformation for the post-secondary market, but are hesitant to do so in the K-12 market, given the bleak prospects of content purchasing and the slow transition to digital environment in the K-12 market.

7.1.3 Emerging Markets Are Driving International Investment

Emerging markets are providing a more attractive business environment for publishers, so multinational publishers are likely to invest in them instead of a declining Canadian market.

Revenues from emerging markets are increasing substantially for multinational publishers and are outpacing the slower growth in developed markets. Pearson PLC (the parent company of Pearson Canada), for example, was expecting a 1% growth in its higher education revenues in North America (United States and Canada) from 2013 to 2014 but an 8% growth in its international education revenues¹⁰¹. Oxford University Press reported strong growth in emerging markets, with a 12% increase in sales in 2012¹⁰².

⁹⁸ Rollans, 2012, p.19.

⁹⁹ “Pearson: high quality but tough timing.” Macquarie Equities Research, 27 June 2013, available from Thomson Reuters, accessed 5 July 2013.

¹⁰⁰ “K-12 and the Common Core: a watershed moment for education.” Macquarie Equities Research, 11 April 2013, available from Thomson Reuters, accessed 5 July 2013.

¹⁰¹ “Pearson: Age of Uncertainty.” Macquarie Equities Research, 10 Jan. 2013, available from Thomson Reuters, accessed 5 July 2013.

¹⁰² “Digital and emerging market boost for Oxford University Press.” University of Oxford, 27 June 2013. Web. 24 July 2013.

International education growth is expected to continue as emerging market nations look to assign increasing resources to education. For example, public expenditure on education as a percentage of GDP has increased from 2.8% to 3.3% in Southern Asia, reducing the gap relative to the EU and North America, which spend 5.4% of their GDP on average on education¹⁰³. Governments in emerging countries are focusing on improving education and will therefore boost spending on educational books and related products¹⁰⁴.

The enrolment ratios¹⁰⁵ in developing economies also indicate the potential upside to the educational system of these economies. Indeed, the average enrollment ratio in North America and Western Europe is 95%, compared to 75% in Central Asia, 57% in Sub-Saharan Africa, and 66% in Arab States.¹⁰⁶

As their education enrolment increases and as their copyright laws strengthen, developing economies such as China and India are becoming more attractive propositions for multinational publishers relative to the Canadian market. Governments in many countries are focusing on improving education and will therefore boost spending on educational books and related products¹⁰⁷. Countries such as India now largely support strong copyright protection in response to a burgeoning local publishing industry that benefits from copyright laws¹⁰⁸. Compliance is also increasing in China, where piracy has traditionally been high. As such, investment in emerging markets is becoming increasingly attractive.

¹⁰³ “Pearson: a compelling 2014 story.” Credit Suisse Equity Research, 29 April 2013, available from Thomson Reuters, accessed 5 July 2013.

¹⁰⁴ Global Book Publishing. IBISWorld Industry Report C1712-GL. IBISWorld, Aug. 2012.

¹⁰⁵ An enrolment ratio is the number of pupils enrolled in a given level of education expressed as a percentage of the official school-age population corresponding to that level of education.

¹⁰⁶ Credit Suisse Equity Research, 2013.

¹⁰⁷ Global Book Publishing. IBISWorld Industry Report C1712-GL. IBISWorld, Aug. 2012.

¹⁰⁸ Altbach, Philip. Chapter 23: Book Publishing. Bellagio Publishing Network, nd, available from UNESCO, accessed 29 July 2013.

8. Economic Impacts of the Fair Dealing Guidelines

In the short term, the Guidelines will lead to a transfer of wealth from content producers to users of content. In the long term, content producers are expected to adapt by creating less content, which will, in turn, compromise the quality, diversity, indigeneity, and affordability of published works for content users. Some or all large publishers will likely exit the K-12 market. As for SME publishers, many will eventually be forced to exit the Canadian Educational Publishing Market or direct their investment and resources to more profitable publishing areas.

This section describes the likely economic impacts on the Educational Publishing Market as a result of the implementation of the Guidelines by K-12 schools and post-secondary institutions in Canada.

The predictive economic impacts presented here were developed on the basis of economic theory and the specific characteristics and circumstances of the Educational Publishing Market.

We present both immediate impacts resulting directly from the implementation of the Guidelines by the educational sector and longer-term impacts that will be shaped by the attempts of content producers to adapt their behaviours to the Guidelines.

Our assessment of the economic impacts of the Guidelines was developed, informed, and supported by data that we obtained from multiple sources, including (1) interviews with publishers, creators, teachers, professors, and representatives of industry associations and Access Copyright; (2) analyses of data provided by CERC, the CPC, publishers, and Access Copyright; (3) a survey conducted by Circum of publisher members of the Association of Canadian Publishers (the ACP Survey)¹⁰⁹; and (5) a Circum Survey of creators (previously referred to in Section 5.2).

The full effect of the Guidelines on the Educational Publishing Market has not yet been experienced.¹¹⁰ Given the early stage of implementation of the Guidelines, more weight than otherwise would be the case was put on the qualitative data we collected. The collection of quantitative data was mainly targeted at the immediate economic impacts of the Guidelines.

¹⁰⁹ Please see Section 3 for further details regarding the ACP Survey. PwC collaborated with Circum Network on developing the questionnaire for the survey.

¹¹⁰ As noted earlier in this report, the Guidelines are relatively new: they were implemented in late 2012. In addition, some post-secondary institutions continue to pay licensing royalties because they remain bound by licence agreements with Access Copyright until the end of 2015.

We are of the view that, as a result of the Guidelines, there will be a transfer of wealth from content producers to content users in the short term. In the long term, that transfer of wealth will force content producers to adapt by reducing the production of content, which will in turn negatively impact the quality, diversity and affordability of published works for content users and will reduce the availability of Canadian content for the Canadian market. It appears likely that some or all large publishers will exit the K-12 market. Many SME publishers will not be able to adapt successfully to the new circumstances and may also exit the Educational Publishing Market.

8.1 Licensing Income

Licensing income is a significant source of income for content producers, especially SME publishers and creators. As a result of the Guidelines, licensing income from the K-12 market has already almost stopped; a similar outcome is expected in the post-secondary market once current licensing agreements expire at the end of 2015. The reduction in this source of income has led to employment losses among large publishers and is expected to cause some SME publishers to exit the Educational Publishing Market. The Guidelines will ultimately lead to a virtual elimination of this source of income from the market, which would represent a loss of at least \$30 million per annum for content producers.

As noted previously, content producers traditionally received licensing income when their published works were disaggregated and copied. The Guidelines purport to allow students, professors, teachers and staff members in K-12 schools and post-secondary institutions to freely copy portions of works without paying licensing fees.

As shown in Tables 1 and 2, the allowable copying under the Guidelines closely mirror the copying limits allowed under Access Copyright licences. It appears that K-12 schools and most post-secondary educational institutions take the position that the copying they do is either covered under the Guidelines or is authorized elsewhere in the *Copyright Act*. Therefore, they posit that no payment is required.¹¹¹ We believe that if the Guidelines are implemented across Canada, the licensing fees historically paid by educational institutions to Access Copyright and the downstream payments from Access Copyright to content producers will be practically eliminated. We also expect that direct permissions licensing income to content producers (i.e. licensing income paid directly to publishers by educational institutions) will decline and/or be virtually eliminated.

The effect of the Guidelines may also impact the copying behaviour of educational institutions, resulting in an increase in copying within the thresholds permitted under the Guidelines. In addition, the opportunity cost of copying over the limits specified in the Guidelines will increase. In other words, the Guidelines are creating an incentive to copy within the limits fixed by the Guidelines, which may mean that consumers of educational material will move to creating more

¹¹¹ Given that all public K-12 school boards and Ministries of Education stopped paying the Access Copyright licence effective January 1, 2013, this is a reasonable assumption.

coursepacks that copy excerpts from different published works. The cost of copying less than 10% of a textbook will be reduced to the actual cost of copying (which in the case of digital copying is practically zero), while the cost of copying one more page over 10% would still be subject to a copyright fee. This may lead to a change in behaviour on the part of schools and their instructors who will increase copying within the limits of the Guidelines and reduce both the copying outside these limits and the purchasing of whole books. The following section examines the economic impacts of the loss of this licensing income on Canadian publishers and creators.

8.1.1 Impacts on Publishers

Reduction in Licensing Income

K-12 Collective Licensing Income

All licensing income that was historically paid to content producers by public K-12 schools through Access Copyright has already been eliminated as a result of the Guidelines. (As of January 1, 2013, all public K-12 schools have stopped paying Access Copyright.) In addition, a number of independent K-12 schools have terminated their licenses, some of whom have expressly cited the Guidelines as the reason for their termination¹¹². These terminations have virtually eliminated licensing income formerly received by content producers from the K-12 sector.

In order to understand the impact of the loss of this licensing income, the figure below tracks the historical licensing payments made by K-12 schools to Access Copyright.

¹¹² The few remaining licensed independent schools represent an insignificant portion (1%) of the royalties previously received from the K-12 sector.

Figure 14 – Total Licensing Fees Paid by K-12 Public and Independent Schools (Millions), 2005 to 2014¹¹³

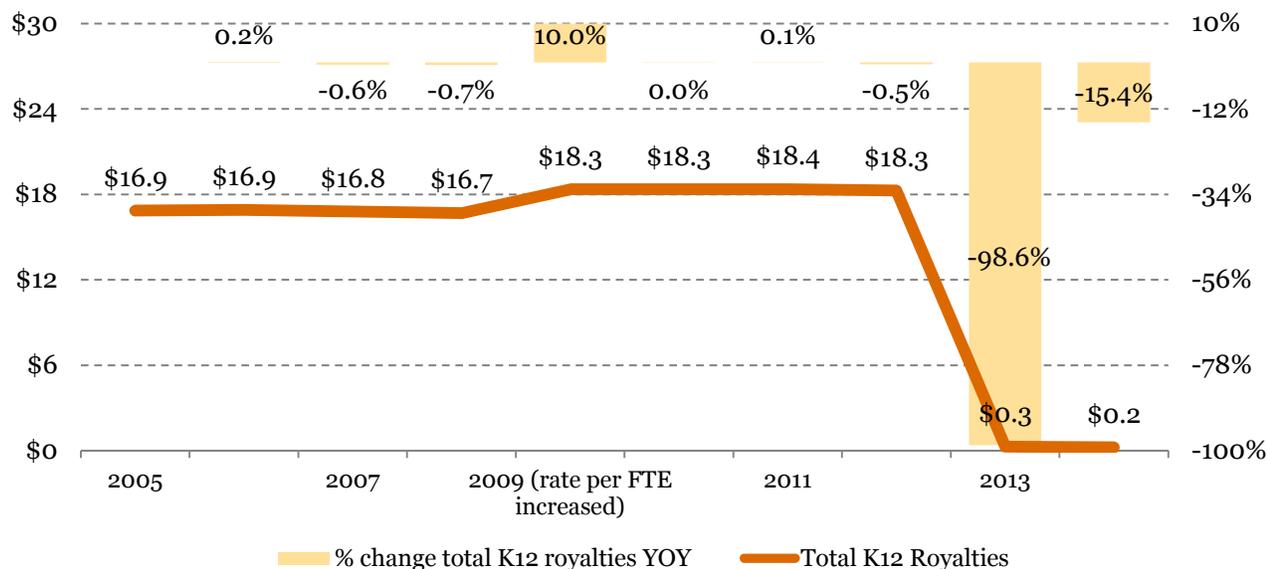


Figure 14 indicates that total licensing income paid by K-12 schools were relatively constant between 2005 and 2012¹¹⁴. However, since the introduction of the Guidelines by the K-12 sector in late 2012, total licensing fees paid by K-12 public and independent schools have been virtually eliminated. This change represents a loss of approximately \$18 million in licensing fees per year.

Post-Secondary Collective Licensing Income

The trend in licensing fees paid by post-secondary institutions is more complex. The income fluctuated historically based on the amount of coursepack copying reported and paid for by the institutions.¹¹⁵ In addition, and as discussed in Section 4.4, some institutions continue to pay licensing fees to Access Copyright because they are bound by licensing agreements entered into with Access Copyright prior to the implementation of the Guidelines. Other institutions did not sign licences after 2011 and have thus ceased paying royalties.

¹¹³ The fees represented in Figure 14 have been adjusted to reflect the average annual rates after accounting for retroactive payments owing as a result of the initial certification of the 2005-2009 K-12 tariff by the Copyright Board in 2009. In 2009, the Copyright Board certified a discounted rate for the years 2005-2008 and a full rate starting in 2009 (at \$5.16 per FTE, later reduced to \$4.81 to reflect the ruling of the Supreme Court of Canada regarding fair dealing).

¹¹⁴ The income was relatively constant because K-12 schools paid Access Copyright licensing fees based on a flat fee per full-time equivalent student (“FTE”): the only fluctuations in the total income were a result of an increase or decrease in the number of FTEs for each year.

¹¹⁵ Until 2011, post-secondary educational institutions paid a flat FTE rate of \$3.38 (for universities and community colleges) or \$3.58 (for proprietary colleges), plus a per page rate for every copy made and sold in a paper coursepack.

Figure 15 – Total Licensing Fees by Unlicensed Institutions Relative to Licensed Institutions (Millions)¹¹⁶

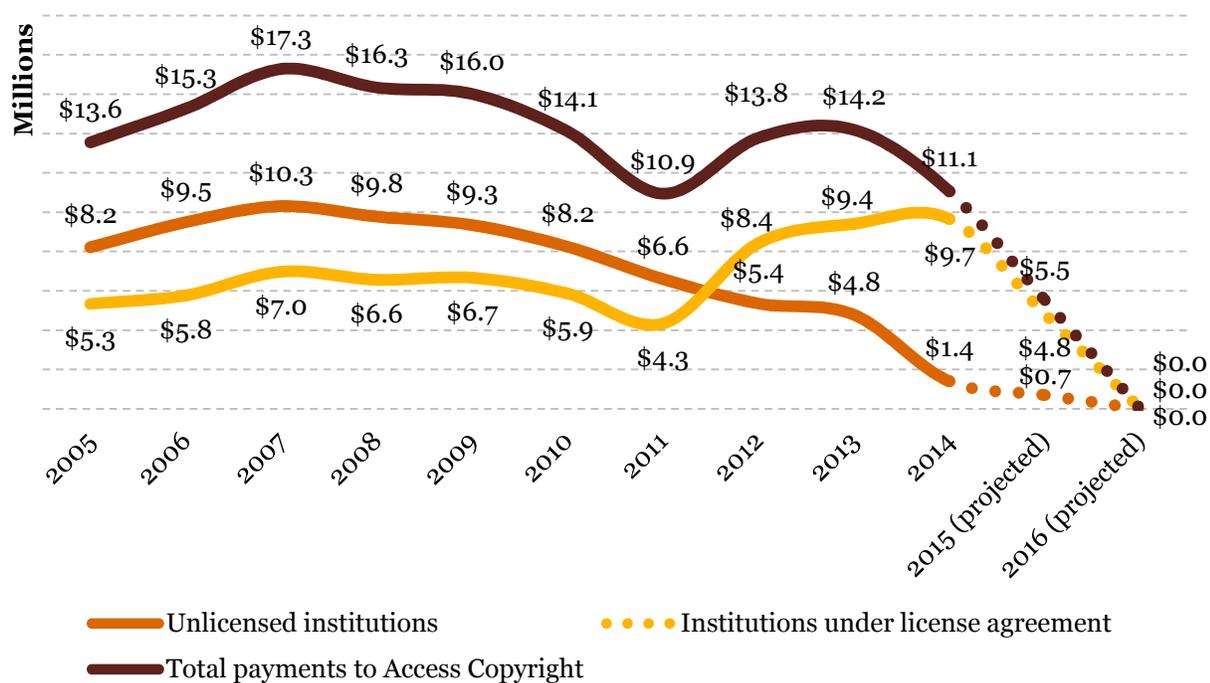


Figure 15 indicates that total fees have been trending downward since 2007, likely primarily as a result of declining paper coursepack uses and corresponding increasing digital uses which were not covered under the Access Copyright licence that was in place until the end of 2010. Total fees rebounded slightly in 2012 when some institutions signed licence agreements with Access Copyright that included a licence for digital uses.¹¹⁷

In Figure 15, payments made by copyshops for copying on behalf of unlicensed institutions are recorded as unlicensed institution revenue. Between 2010 and 2014, fees paid by institutions that are now unlicensed have declined by approximately \$6.8 million or 81%. Fees paid for copying by unlicensed institutions (through copyshops) continued to decline following the introduction of the Guidelines (approximately 74%, or \$4 million, from 2012 to 2014). Revenues from unlicensed institutions have not yet reached zero because some professors at unlicensed institutions continue to use external copyshops to produce paper coursepacks. Those copyshops continue to remit payments to Access Copyright for this copying. Access Copyright forecasts that all copyshop revenues associated with currently unlicensed institutions will be almost completely eliminated in 2016.

¹¹⁶ Projections assume all licensed institutions will not renew their licenses and that unlicensed institutions will remain unlicensed.

¹¹⁷ A similar analysis was conducted based on each FTE student and the divergence in licensing fees was similar thus indicating that the number of students was not driving the results.

In addition, we expect that, barring some new circumstance, most post-secondary institutions currently licensed with Access Copyright will decline to renew once their current agreements expire in December 2015. Thus, we expect, in the short term, to see a virtual elimination of this source of income in the post-secondary sector.

Projected Total Loss in Collective Licensing Income

Given the above, we estimate the elimination of licensing fees from K-12 schools and post-secondary institutions paid through Access Copyright to be over \$40 million per annum in current dollar terms (based on the complete elimination of the \$18 million in K-12 revenues and a loss of approximately \$22 million in post-secondary revenues based on a licence cost of \$26 per FTE). Taking into account Access Copyright's administrative fees, this loss translates to a reduction of approximately \$30 million per year in payments direct to content producers. Moreover, given indications of increased copying activity¹¹⁸ (especially digital copying) we expect that this annual loss to content producers will increase in the future. But for the Guidelines, we expect that licensing fees would have increased from their notional current level. Therefore, the actual loss is greater than past Access Copyright revenues would indicate.

Permissions Licensing Income

Some unlicensed post-secondary institutions have indicated that they seek direct licences from publishers for the copying of their works rather than relying on collective licensing from Access Copyright. If that is the case, it is reasonable to assume that permissions licensing would have increased significantly after 2011, when many post-secondary institutions ceased paying royalties to Access Copyright.

As noted previously, we have not received complete data on direct permissions licensing income paid to publishers by educational institutions. However, based on partial data received from publishers, it appears that, since the Guidelines were introduced, there has been no significant change in those payments to large publishers. Moreover, direct permissions licensing income received by large publishers has declined significantly from 2009 to 2014—this source of revenue did not increase after 2011 as one would have expected if unlicensed institutions were simply choosing to deal directly with publishers rather than Access Copyright. For large publishers (for whom complete data was available), direct permissions licensing income represented less than 10% of total licensing revenue. This indicates that this source of licensing income is relatively small compared to the licensing income collected by Access Copyright prior to the introduction of the Guidelines and does not materially offset the loss of Access Copyright licensing income.

For SME publishers, there is some evidence that direct permissions licensing income and requests have generally declined since 2009¹¹⁹. Again, the data does not support the claim that unlicensed institutions are offsetting licensing fees historically paid to Access Copyright by paying publishers directly. Permissions licensing income represents a more significant share of

¹¹⁸ Based on an estimate made by Circum, the level of copying in the K-12 sector in the period 2006 to 2012 has increased by approximately 17%.

¹¹⁹ Based on Figure 12, direct permissions licensing income for SME publishers increased in 2013, but this related primarily to a single publisher who received significant direct permissions licensing income in 2013. Moreover, 2013 permissions licensing income is still significantly (35%) lower than 2009 levels.

total licensing income for SME publishers than it does for large publishers. Based on a review of the historical direct permissions licensing income earned by a subset of these publishers¹²⁰, it appears that such income as a percentage of total licensing income has declined since 2009.

It thus appear that that the expected annual loss of over \$30 million of licensing income to content producers from Access Copyright will not be offset by any significant increase in direct permissions licensing. Moreover, it is expected that, given the trends in copying behaviour we are seeing in educational institutions, direct permissions licensing income will experience a decline or complete elimination in the future, thus leading to a larger annual loss than estimated above.

The Significance of Licensing Income to Educational Publishers

Based on the ACP Survey and discussions with SME publishers of educational content, we observe that licensing income is generally a significant contributor to earnings of SME publishers. In some cases, licensing income is greater than publishers' total earnings—that is, the licensing income represents the difference between profit and loss for these publishers. Without the licensing income, those publishers will be operating at a loss.

The loss of licensing income has an impact on both large and SME publishers. However, as a result of the relative significance of licensing income for SME publishers, the implementation of the Guidelines has, in many cases, caused certain segments of SME's businesses to begin to generate losses.

The following figure depicts the trends in profitability and licensing income for SME publishers between 2009 and 2013¹²¹:

¹²⁰ A number of ACP publishers did not provide complete historical information with respect to direct permissions licensing.

¹²¹ Data was obtained from the ACP Survey from 14 publishers who provided financial data and for whom revenues from sales to K-12 schools and/or post-secondary institutions was greater than 20% of their total revenues. Note that this analysis excludes publishers whose revenues from sales to K-12 schools and/or post-secondary institutions was less than 20% of their total revenues, and university presses. University presses are analyzed separately in Figure 18.

Figure 16 – Impact of Licensing Fees Paid to SME Publishers¹²²

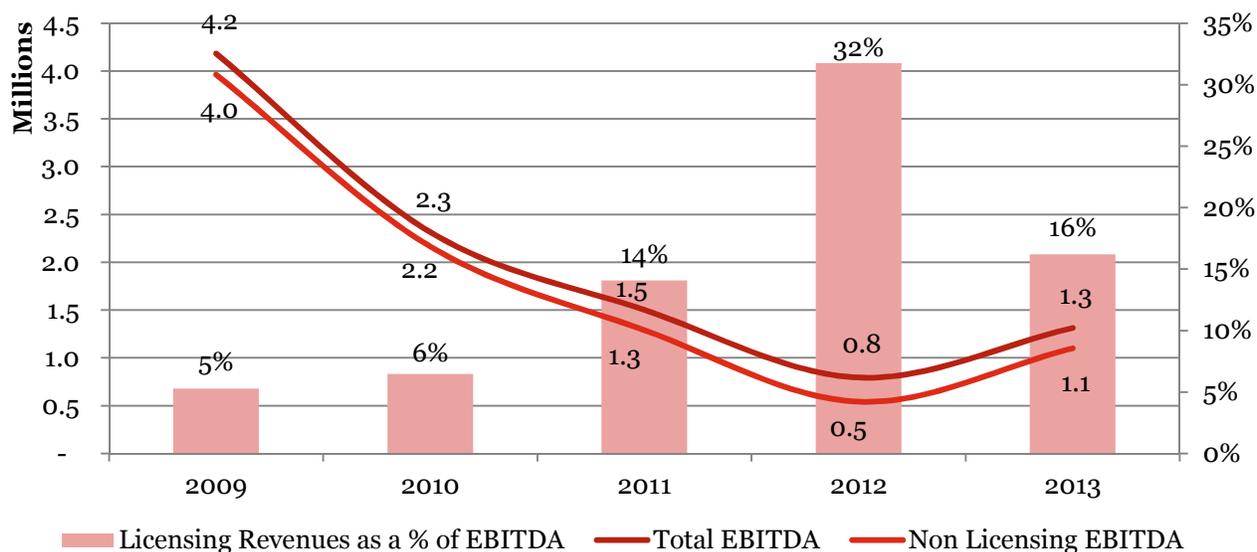


Figure 16 demonstrates the impact of the negative trends noted previously in relation to the Educational Publishing Market. EBITDA (i.e. earnings before interest, tax, depreciation and amortization) has declined by over 81% from 2009 to 2012. As a result, by 2012 licensing income comprised 32% of total EBITDA. This suggests that as a result of the negative trends in the Educational Publishing Market, prior to the introduction of the Guidelines, licensing income had become an increasingly important source of income for SME publishers. In 2013, EBITDA for these entities improved, mainly as a result of cost cutting measures implemented by SME publishers despite a significant reduction in licensing income (from approximately \$300,000 in 2012 to approximately \$200,000 in 2013). Despite this decline, licensing income still represented a significant share of EBITDA (16%) for SME publishers in 2013.

As can be seen from the following figure, the above trend is even more pronounced for publishers whose revenues are primarily generated from sales to K-12 schools or post-secondary institutions (i.e. more than 50%).¹²³

¹²² We note that licensing revenues reported by the SME publishers are impacted by retroactive payments that were made in 2012. The impact of the retroactive payments depends on the year in which each SME publisher would have reported the payment (i.e. the impact is dependent on the fiscal year end of each SME publisher). However, this does not alter our view of the increasing importance of licensing income in an environment of declining sales.

¹²³ We note that this data is based on only 5 publishers who provided complete financial data.

Figure 17 – Impact of Licensing Fees Paid to SME Publishers Whose Revenues Come Primarily from Sales to K-12 Schools and Post-Secondary Institutions

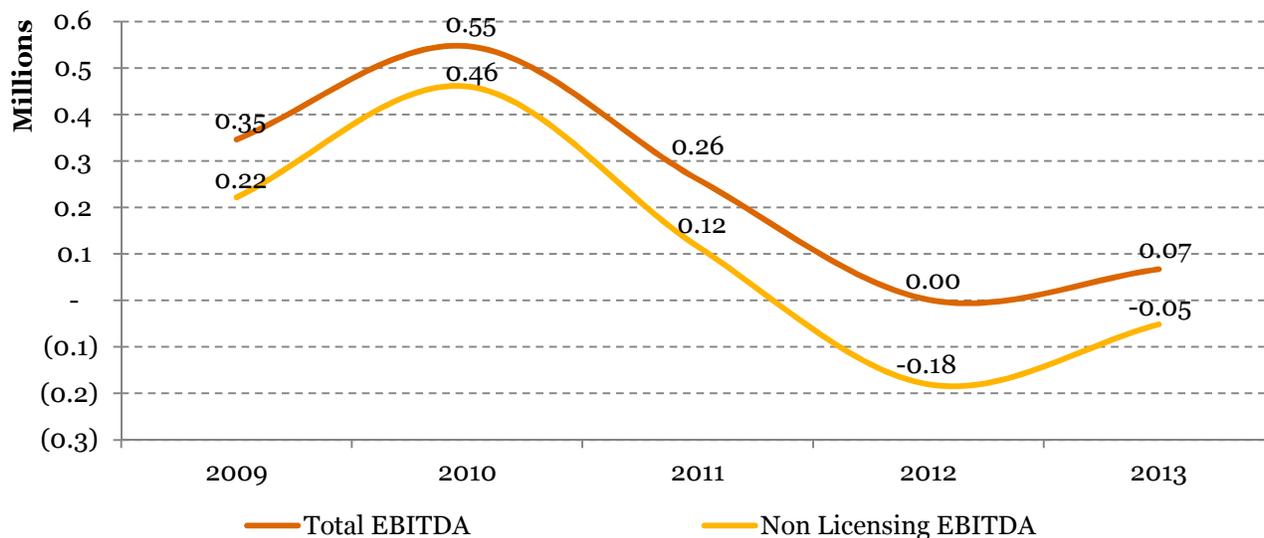
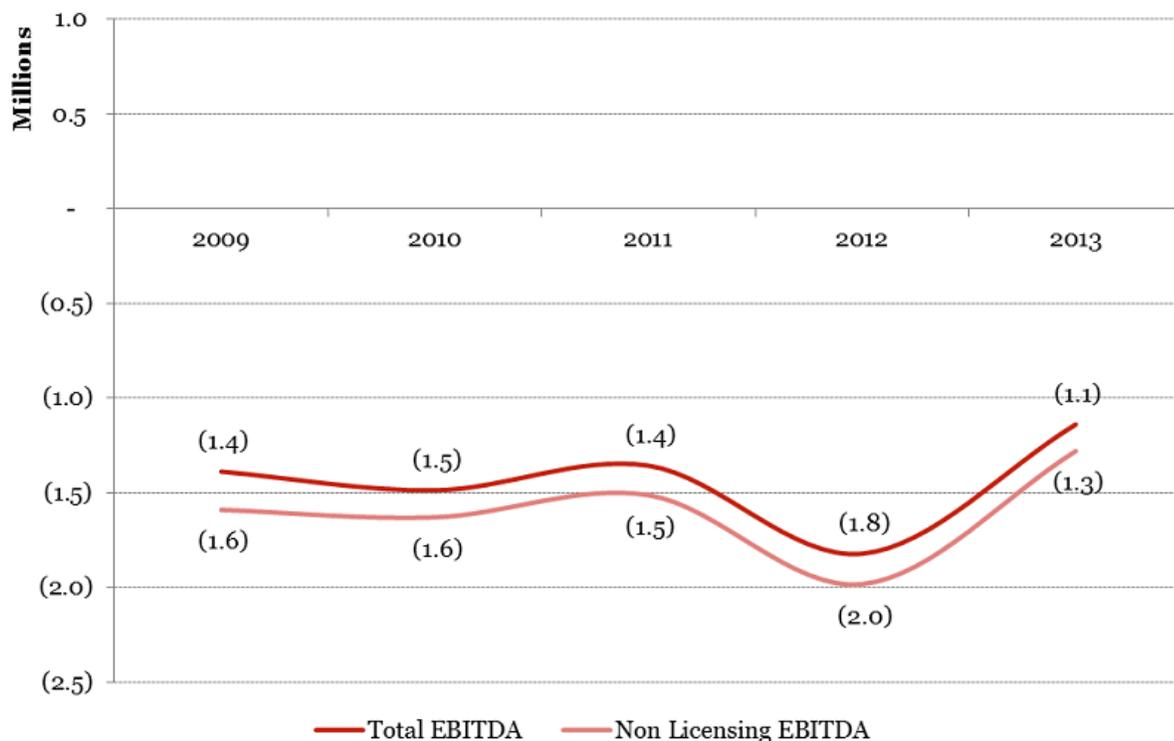


Figure 17 indicates that for SME publishers whose revenues are primarily generated from the Educational Publishing Market, the loss of licensing income may lead to negative profitability and as such may force them to exit the Educational Publishing Market.

As noted above, university presses were not included in Figures 16 and 17. University presses receive varying degrees of subsidy from their host institutions, and in return they have important responsibilities to those institutions; this makes their business considerations distinct from those of other publishers. In Figure 18 below, we have analysed the trend of EBITDA and licensing income in university presses.¹²⁴ Since we have not received sufficient information with respect to permissions licensing income, the licensing income in the following chart includes only licensing income received from Access Copyright.

¹²⁴ Based on data collected by PwC through the ACP Survey from three university presses.

Figure 18 – Impact of Licensing Fees Paid to University Presses

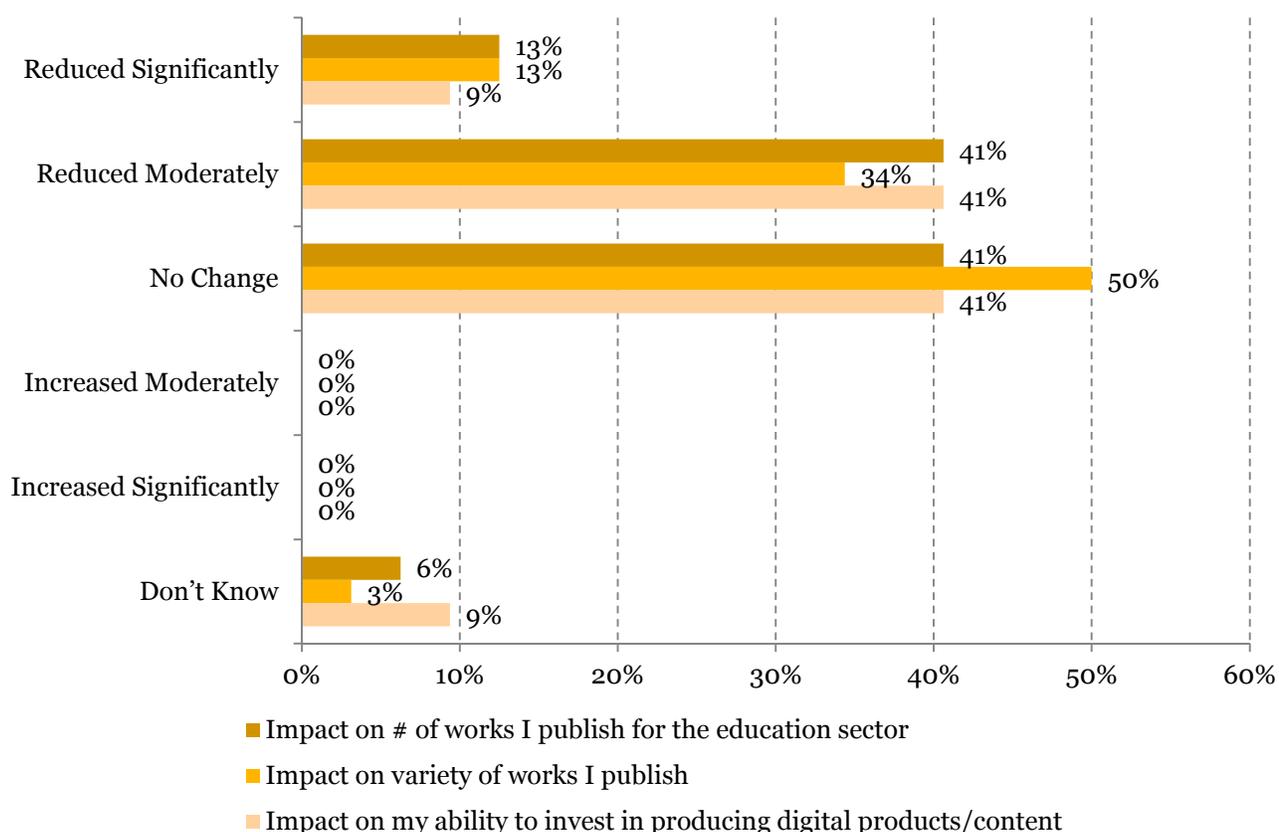


As can be seen from Figure 18, the aggregate EBITDA of our sample of university presses has been negative throughout the analysis period. Between 2009 and 2013, licensing income contributed between \$100,000 and \$200,000 per annum to EBITDA.

Due to the negative trend in EBITDA for university presses, we have measured licensing income as a percentage of revenue as opposed to a percentage of EBITDA (which would be consistent with the metric considered in relation to SME publishers). Licensing income as a percentage of revenue fluctuated during the period, but ranged from a high of 2.8% in 2009 to a low of 1.9% in 2013.

In response to a question asked of ACP member firms, Figure 19 below indicates that over 50% of the SME publishers believe that the decrease in licensing income from Access Copyright would reduce either moderately or significantly their ability to invest in producing digital products/content, the variety of works published and the number of works published (particularly for the education sector). These factors would have a negative impact on such publishers, leading to their potential exit from the Educational Publishing Market.

Figure 19 – As a result of the implementation of the fair dealing policies, the revenue you receive from Access Copyright may diminish or cease entirely. What will be the likely impacts of this situation on your business over the next five years?



We understand that many other publishers are contemplating either exiting the educational publishing industry or focussing on other areas of publishing, in particular because their size does not permit them to offset the loss in revenues while also making sufficient investments in digital production that may be necessary to generate profits through alternate business models. This is especially true in the post-secondary market, where digital penetration and demand has been relatively high.

The exit of SME publishers is expected to reduce the availability of specialized content for the educational sector. As noted in Section 5.3 above, many SME publishers occupy niche positions

in the publishing market that are not served by large publishers. This impact is discussed further in Section 8.7.

For large publishers, licensing income is not as significant a percentage of EBITDA as it is for SME publishers. Notwithstanding that fact, it still has a noticeable financial impact. Specifically, we have observed that licensing income directly impacts each publisher's "bottom line" as there are no significant direct expenses associated with earning this income. (Contrast this to the sale of new products, which requires the investment of development, marketing and production expenses). One publisher stated that it would have to make up five times the revenues it receives in licensing income in sales to replace it.

Making up the loss of licensing revenue through increased sales would be difficult to do, particularly given the declining sales trend in the Educational Publishing Market. For example, the average annual K-12 royalties paid to CERC publishers from Access Copyright between 2005 and 2012 was \$4.8 million. To make up the lost licensing revenue, these publishers would need to achieve an additional \$24 million¹²⁵ worth of sales revenue each year. The replacement of lost licensing income would require the industry's total sales revenue to increase by 18% – a highly unlikely scenario given the fact that the K-12 market has experienced year-over-year decline amounting to 40% since 2008.

Thus, the only other option available to these publishers is to reduce costs, including by laying off staff. Our review of financial statements of the industry's largest publishers indicates that employee wage and benefit expenses are being reduced relative to total revenues, consistent with employment losses due to layoffs or attrition. Publishers have confirmed that job losses have been the direct consequence of the loss of licensing income.¹²⁶

The introduction of the Guidelines and threatened loss of licensing income has already caused one large educational publisher to exit the Canadian K-12 market entirely. In February 2014, Oxford University Press announced that it was shutting its Canadian K-12 division and cited "...changes to Canadian copyright law, as well as the decision of several provincial school boards to opt out of Access Copyright licences, as influencing the company's decision". Additionally, licensing revenues from Access Copyright were "...a significant factor in making school publishing viable here, even in the wake of declining sales of the materials themselves."¹²⁷

Nelson Education Ltd., among the leading K-12 publishers and the largest Canadian-owned educational publisher recently filed for bankruptcy protection under the *Companies' Creditors*

¹²⁵ This is based on the assumption that publishers must make up to five times the revenues they received in licensing revenues in sales to replace this lost revenue (i.e., \$4.8 million/year x 5)

¹²⁶ See, for example, witness statement of Nancy Gerrish dated December 16, 2013, presented as Access Copyright Exhibit AC-5 before the Copyright Board of Canada, para 26. In her testimony, Nancy Gerrish indicated that the McGraw-Hill Ryerson reduced their staff size by 25 people in November or December of 2013, of which 10 people are from the McGraw-Hill Ryerson School Division. This move is prior to consideration of the closing of McGraw-Hill Ryerson's distribution centre, which would result in further reductions.

¹²⁷ Julie Baldassi, "OUP Shuttters School Division, Lays Off Three," *Quill and Quire*, February 10, 2014.

Arrangement Act (CCAA).¹²⁸ We understand that significant pressures on revenues, to which the Guidelines may have been a contributing factor, were the primary cause.¹²⁹

8.2 Sales Income

Copying portions of works can substitute for the purchase of the original works. The Guidelines reduce the cost of copying, making this option more attractive to users. They will likely cause a further decline in content sales for educational publishers, as their resources are replaced by royalty-free copies of identical or equivalent content that the publishers would otherwise sell. Certain content producers, such as those that specialize in anthologies, poets and short story authors, will be particularly hard hit. Because the Guidelines permit “free” copying of excerpts, they enable and accelerate the transition towards relying on teacher-compiled resources of copied works.

The impact of the Guidelines on the purchase of original copyright-protected works will depend on whether copies made under the Guidelines substitute for the original work.

Two goods are substitutes if an increase in the price of one of the goods leads to an increase in the demand for the other good. Substitutes need not be perfect substitutes, since a marginal increase in the price of one good may lead to significant, though not a complete, substitution of that good. For example, a decrease in the price of Starbucks would not completely remove the demand for Tim Hortons since some consumers have a strong taste preference for Tim Hortons.

There are indications that the current volume of copying is substantial – in K-12 schools, it is estimated that the equivalent of approximately 1.3 million books and consumables are copied annually.¹³⁰ It should be noted that these estimates do not include digital copying and were made prior to the introduction of the Guidelines, and therefore likely substantially understate the current volume of copying.

The Guidelines are expected to lower the price of excerpts (as defined by the Guidelines). Whereas users of copyright works historically paid for copying of excerpts under their licensing arrangement with Access Copyright or their direct arrangements with publishers, they will be paying for the marginal cost of copying only under the Guidelines. That is, while content producers were compensated for the substitution of sales with excerpts under an Access

¹²⁸ *Apax Partners, Omers Private Equity Inc said to hand over publisher Nelson Education Ltd to funds*, Cecile Gutscher and Laura J. Keller, Bloomberg News, March 31, 2015, via Financial Post.

¹²⁹ See, for instance, the Pre-Filing Report of the Proposed Monitor for the Plan of Compromise or Arrangement of Nelson Education Ltd., May 11, 2015, Section 4.6. Accessible at: [http://cfcanada.fticonsulting.com/NelsonEducationLtd/docs/Nelson%20Pre-filing_Report%20of%20the%20Monitor%20May%2011%2015%20\(final\).pdf](http://cfcanada.fticonsulting.com/NelsonEducationLtd/docs/Nelson%20Pre-filing_Report%20of%20the%20Monitor%20May%2011%2015%20(final).pdf)

¹³⁰ Based on a 2014 Circum report publicly filed (as Exhibit AC-67) for the in the K-12 tariff proceedings, we estimate that there are approximately 220 million pages of books and 110 million pages of consumables copied every year. Based on a 2014 Circum report publicly filed with the Copyright Board on October 14, 2014, the average length of the works from which the copies were made was 330 for books and 165 for consumables. The copying is therefore equivalent to copying approximately 666,000 books and 666,000 consumables annually.

Copyright licence agreement or a Copyright Board tariff, the Guidelines will eliminate this compensation. As an example, the price of a class handout that contains an excerpt within the limits of the Guidelines will be equal to the relatively low cost (in the case of physical copying), or zero cost (in the case of digital copying) of reproduction, as the excerpt will no longer be subject to a licensing fee.

In those cases where excerpts can be suitable substitutes for original works, the demand for original works will therefore also likely decline.

Some copyright-protected works are more prone than others for substitution. For example, in the case of anthologies, which are by their nature collections of works, there is near perfect substitution¹³¹, as a course collection could use the same source materials and bypass the purchase of the anthology entirely. Digital excerpts can also be perfect substitutes for chapters or disaggregated content that is sold individually by publishers. The Guidelines are also expected to increase the substitutability of the copying of excerpts for the purchase of books. The Guidelines allow for a chapter of any length to be copied without permission or a fee. This increases the incentive for consumers to replace textbooks with standalone chapters sourced from various textbooks.¹³² In addition, if the Guidelines lead to various chapters being copied from multiple editions of one textbook, a course collection could become a near perfect substitute to that textbook.¹³³

In K-12 schools, teachers have developed learning resources by copying portions from a number of professionally produced educational resources. This kind of teacher-developed resource is made by disaggregating and copying professionally produced content and re-aggregating that content into a compilation derived either solely from professionally-created resources or from a combination of teacher created and professionally-created resources. Often this resource contains little or no original authorship from the teachers. Prior to the implementation of the Guidelines, the published content used in these resources was paid for through a licensing fee. Given that the Guidelines now authorize teachers to copy entire chapters or 10% from a number of published works, without payment of a licensing fee, it is reasonable to expect that teachers may increasingly resort to this kind of copying behaviour because it may be done on a no fee basis. This is particularly so given the shrinking budgets available to teachers for the purchase of original content.

Prior to the implementation of the Guidelines in the post-secondary market, licensing fees were paid for each chapter, article or page compiled and copied into paper coursepacks for sale to students. Given that the Guidelines now authorize professors and students to copy entire

¹³¹ The substitution is not perfect since the entire anthology itself cannot be reproduced, but the various excerpts could be sourced from different anthologies.

¹³² The substitution effect described above (i.e. decrease in price of one good leads to decrease in consumption of other good) assumes that the buyer or consumer is the sole decision maker. However, as noted previously, in the case of post-secondary educational material, the decision to replace a book with a course collection is made by the instructor. Given that in general instructors consider the cost to their students in their decision regarding course materials (see previous discussion), which acts as incentive to reduce the use of textbooks, we expect that the Guidelines will provide instructors more opportunities to substitute towards course collections.

¹³³ The degree of substitution is less evident in the case of fiction books where there is some dependence or continuity from chapter to chapter.

chapters, articles and up to 10 per cent from a published work for free, and include them in a paper coursepack or post them on a course management system, it is similarly reasonable to expect that professors may increasingly resort to this kind of copying behaviour over the purchase of original content. This is particularly so given the increasing cost of education and pressures on professors to reduce costs for students.

The expected increase in the copying behaviour described in both circumstances above is expected to substitute for the purchase of content from which this content may now be freely copied. This substitution will cause educational publishers to sell fewer of the resources from which the copies are made.

Sales of digital content will be lower than otherwise expected due to expected substitution with copied material, discouraging industry innovation in this area

Many publishers have attempted to offset the decline in the sale of textbooks by developing new revenue models such as customized publishing, offering disaggregated content (e.g. e-chapters sold as single chapters) and other value-added digital components.

Customized publishing enables teachers and instructors to draw from libraries of texts and collections to tailor a learning solution for their students. In response to that demand, publishers are selling custom publications which may be compilations from various titles and which select only the chapters or content that teachers want.

The Guidelines allow the creation of these custom compilations for free. As a result, the Guidelines threaten and create direct competition with custom publishing and disaggregated content offerings. Free excerpts will increase the opportunity cost for K-12 schools and post-secondary institutions and will discourage them from purchasing digital solutions from publishers notwithstanding the real needs of schools for such solutions. Thus, publishers will sell fewer print resources and may be discouraged from investing in digital resources, as they might have if the Guidelines were not in place.

8.2.1 Evidence of the Impact of the Guidelines on Sales Revenues to Date

Evidence from K-12 Schools

The decline in K-12 sales has accelerated since the introduction of the Guidelines

Between 2010 and 2012, K-12 sales in Canada have declined at an annual average rate of approximately 6.5%, while in 2013 and 2014, after the introduction of the Guidelines, this rate accelerated to approximately 7.1%. This decline was partially masked in Ontario due to the release of a new social studies curriculum – excluding Ontario, K-12 sales in Canada declined at an average annual rate of 1.5% between 2010 and 2012 compared to a rate of 8.4% in 2013 and 2014. This provides a preliminary indication of the negative impact of the Guidelines on sales in the K-12 sector.

Single orders from K-12 schools are increasing, in part, due to copying of materials that would otherwise be purchased in larger volumes

A number of publishers have seen an increase in the number of single orders received (i.e. an order for one book rather than a set of books) in 2013. This is an indication that the level of copying has further increased following the Guidelines, and that sales have decreased, with schools buying one resource per class and then copying portions of it for all students¹³⁴.

There is an increase in the use of class sets in K-12 schools

According to publishers the use of class sets (i.e. fewer books than students in a given class or a set of textbooks that is shared between multiple classrooms) is on the rise. The purchase of fewer books for a class increases the need for copying: students are unable to take a book home for homework, so the text must be copied.

Prior to the implementation of the Guidelines, the impact of the use of class sets on sales was partially offset by the licensing income that flowed through to content producers from Access Copyright as compensation for this copying. Under current conditions, sales continue to decrease due to the use of class sets but publishers receive no compensation for the copying that makes the purchase of class sets a viable option for schools.

Instances of textbooks being posted online, where they could otherwise be purchased, have increased

Publishers have also indicated that, in lieu of photocopying, some teachers have posted partial or full textbooks on the teacher's or school board's websites or course management systems without authorization. This facilitates students' ability to download and use these textbooks without the purchase of the textbook.

The Guidelines are threatening the viability of new digital solutions designed to provide greater customization of resources

As explained above, many publishers have been moving towards offering customers the option of purchasing disaggregated content (e.g., e-chapters) and of creating their own custom compilations. For example, Nelson Education offers e-chapters through its NelsonBrain website, giving users the option to purchase individual chapters rather than an entire book.¹³⁵ Nelson has found a number of examples of such chapters copied and either posted on a course management system or copied into coursepacks, without permission or payment. Nelson also offers custom publishing services, allowing teachers to mix and choose content from Nelson and Cengage's library of content to create a customized textbook. The Guidelines compete directly with this product, as instructors would be able to compile excerpts from different sources and create customized material for a course, without royalty payment or purchase.

¹³⁴ This is an imperfect measure as single orders are also used for sampling purposes by schools, although most samples are provided by publishers free of charge.

¹³⁵ See <https://www.nelsonbrain.com/shop/en/CA/storefront/canada?cmd=CLBrowseCategory&catKey=601117>.

As a second example, prior to the implementation of the Guidelines, McGraw-Hill Ryerson developed “iLit” - a collection of short literary works for the K-12 market authored by Canadian writers. These collections were made available both in aggregated and disaggregated formats: as a set of eight published print anthologies and as a database containing all of the short literary works contained within these anthologies, along with additional works and resources. Schools have the option to either purchase the pre-printed anthologies or to create their own custom compilations in either print or digital format using the works in the iLit database.¹³⁶ The content was developed in response to the market, which indicated interest in contemporary Canadian literature, particularly short works. The ability to create custom collections was developed in response to teachers’ views that not every school would be interested in teaching the same short works in their classroom – for example, certain works appealed to schools in certain geographic areas.

As a result of the Guidelines, teachers have expressed that, instead of purchasing the iLit anthologies or ordering custom iLit compilations, they can photocopy from either previous iLit custom collections or from the eight published anthologies and create their own collection for free.¹³⁷ This practice (encouraged by the Guidelines) competes directly with and may substitute for the service offered by McGraw-Hill Ryerson through iLit. Given the outcome of iLit McGraw-Hill Ryerson may be discouraged from similar innovative investments.

In allowing the free copying of portions of works, disaggregated from the original source of those works (such as a full textbook), the Guidelines inhibit the development of innovative digital solutions that provide content producers and consumers with the ability to market and purchase disaggregated content. Various digital offerings and services offered by educational publishers today – such as the sale of e-chapters, subscription models and ‘chunked’ digital content – allow consumers to buy only what they need. This transition towards offering disaggregated content is similar to the music industry move from albums to individual song sales. The Guidelines undercut the development of these models and purport to allow the same offerings and services for content producers’ content, for free. The Guidelines thus undermine – and may ultimately chill – the development of all monetization models based on disaggregated content and further diminish the value and likelihood that both the disaggregated content and the original, aggregated work would be purchased.

Evidence from Post-Secondary Institutions

The impact of the Guidelines is also borne out by sales in the post-secondary market.¹³⁸ Specifically¹³⁹:

¹³⁶ *What is iLit?*, <http://www.mheducation.ca/school/files/2011/10/iLit-brochure-web6.pdf>.

¹³⁷ Testimony of Nancy Gerrish, President of the School Division at McGraw Hill Ryerson Limited during the 2010-2012 and 2013-2015 K-12 tariff hearing before the Copyright Board of Canada on April 30, 2014. Transcript, Vol. 2, p.395.

¹³⁸ Note that these revenue figures include Quebec sales due to data limitations.

¹³⁹ Based on data provided by the CPC.

- **The rate of annual decline in overall post-secondary unit sales has accelerated**, on average, by approximately 3.2 percentage points per annum in 2012 to 2014 relative to the 2010 to 2012 period.
- **The decline in unit sales of Canadian titles has accelerated** from an average annual decline of approximately 2.5% between 2010 and 2012 to 6.5% between 2012 and 2014.
- **This acceleration in the average decline of unit sales was faster for Canadian titles than for imported titles**, specifically, Canadian titles' average decline accelerated by 4.0 percentage points - greater than the acceleration observed for sales of imported titles, which was approximately 2.6 percentage points during the same period.
- **The average decline in overall net revenues accelerated** from 2.9% between 2010 and 2012 to 3.6% between 2012 and 2014.
- **Revenues from Canadian titles have transitioned from a slight decrease to a more rapid decline**; specifically, revenues from Canadian titles decreased, on average, by 0.2% between 2010 and 2012, compared to an average decline of approximately 3.2% between 2012 and 2014.
- **This acceleration of the decline in Canadian title revenues compares to a deceleration for imported titles**; the acceleration in the average decline in Canadian title revenues of approximately 3.0% compares to a deceleration of the decline of approximately 1.3% for imported titles.
- **Prices of Canadian titles (print, digital or blended) have increased** between 9.6 and 14.9%.

The above provides a preliminary indication of the negative impacts of the Guidelines in the post-secondary market leading to acceleration of the decline in sales, a shift away from Canadian publishers producing Canadian titles (and a corresponding increasing reliance on imported titles) and a significant increase in prices.

The Guidelines are encouraging instructors to select coursepacks composed of copied excerpts at the expense of textbooks

As noted previously, sales of published works within the post-secondary market are driven by professors who determine readings for their courses. Through interviews with professors, it was confirmed that they are the key decision-makers and that they consider various factors in selecting required readings. The cost to students is one of the considerations, along with appropriateness, convenience, and financial incentives to professors. Some professors indicated that they balance the need to assign relevant readings against the risk of deterring students from their course by assigning expensive textbooks.

Professors stated that they were more likely to tailor advanced courses and therefore use course collections or digital options to reference works specific to course matter. Textbooks tend to be more appropriate at lower level courses as these courses are more general in nature.

Professors at some unlicensed institutions indicated that they received advice with respect to changes in copyright communications from their institution. Specifically, some were advised to no longer log copied material; others received communications that they were allowed to now freely upload articles onto their CMS, whereas it was previously restricted. Therefore, there is reason to believe that, in general, professors have received some direction from their institutions.

Some post-secondary institutions appear to be encouraging professors to increase the use of course collections. Douglas College for example states on its website that “coursepacks represent a valid supplement or alternative to textbooks and ensure that students only pay for materials essential for success in their course”¹⁴⁰. A number of publishers stated that they had seen a decline in textbook sales at unlicensed institutions that is attributable to the Guidelines. Our review of sales data from three large publishers corroborated that claim, in that the growth rate in sales to unlicensed institutions was significantly lower than the growth rate in sales to licensed institutions between 2011 and 2013.

Prices of post-secondary materials are increasing to offset lower volumes

Our analysis of post-secondary sales revenues in the publishing industry indicates that gross revenue per unit have increased across printed, digital and blended media between 2012 and 2014 by 9.1%, 15.1% and 9.1%, respectively.¹⁴¹ We understand from our analysis as well as from interviews with publishers that these increases are mainly driven by the loss of economies of scale as sales decline. Thus, users who need to continue to purchase materials are effectively subsidizing those who use copied materials and would otherwise have purchased the materials.

Additional Evidence

A lack of clarity regarding the Guidelines may be leading to an increase in the practice of unlimited (and unauthorized) copying of works

Publishers interviewed for this Assessment indicate that they have observed widespread copying in K-12 schools and post-secondary institutions, in excess of the amounts specified in the Guidelines. Significant anecdotal evidence also points to the use of class websites for posting material for which no royalty has been paid. One small post-secondary publisher noted that requests to post excerpts of material online have ceased entirely following the announcement of the Guidelines. Other reported instances of unauthorized electronic copying include the online sharing of electronic resources provided for free as samples for instructors or as resource support for students with special needs. This type of behaviour appears to be driven partially by misunderstanding of the Guidelines, but also by an atmosphere that has been created following

¹⁴⁰ Douglas College. Coursepacks. <http://www.douglascollege.ca/student-services/essential-resources/bookstore/faculty/coursepacks>

¹⁴¹ CPC Data.

the introduction of the Guidelines, which provides educational users a feeling of impunity in relation to copying. The increasing challenges to publishers to detect or monitor infringing activity, and the relative difficulty and expense of enforcing copyrights, compound this problem.

This widespread copying has become a significant factor that is driving and will continue to drive a reduction of sales for the publishing industry.

8.3 Creators' Decisions to Produce

The Guidelines are expected to lead to a reduction in the number of works produced by creators for consumption by educational institutions. Over one third of Access Copyright's affiliate creators indicated that if they were to lose licensing revenue, they would reduce the number of works created, the time spent creating written or visual works, and their focus on content for the Educational Publishing Market.

The initial creation of educational works by creators depends on their incentives to invest their time producing educational content. For a creator, the decision whether and how to invest his time creating educational content reflects a combination of economic and non-economic factors that potentially influence the decision whether to increase or decrease creative activity.

Copyright exists to ensure that content producers have appropriate economic incentives to produce new content.

Focusing on these economic incentives, three aspects are important to a content producer's decision to create¹⁴²:

- The expected income – the typical income the creator can expect to receive for working in a creative occupation;
- The profile and timing of income – in general, individuals prefer a more predictable income that is evenly distributed over time, rather than a more variable income over time, which means that some favour a portfolio approach to income¹⁴³; and
- The potential income if highly successful – creative occupations often exhibit a “winner takes all” structure, with many low paid individuals or small businesses competing to become the “next Margaret Atwood”.

Royalties from both sales and licensing contribute to creators' incentives to create. Licensing income received by creators, which as indicated in Section 0 represents approximately 20% of the total income they receive from their works, impacts creators' expected income and the

¹⁴² PwC. *An economic analysis of education exceptions in copyright*. UK: PwC, Mar. 2012. Print.

¹⁴³ This concept is commonly referred to as “income smoothing” in economics. It reflects the theory that individuals prefer to maintain a consistent standard of living throughout their life rather than experiencing volatility (i.e., a mixture of opulence and poverty).

timing of that income. In general, a creator earns the portion of his income from sales of his book over a relatively short period after his work is sold or licensed to a publisher¹⁴⁴. Licensing income provides regular, annual sources of income (thereby smoothing the profile of expected income). In this way, licensing income has a positive impact on the incentives for creators to continue to produce new content.

The Guidelines already have or are expected to substantially reduce or eliminate creators' licensing income (in addition to sales income from publishers) for the educational use of their works. As a result, it is expected that some creators will no longer have an economic incentive to produce content and will either switch occupation (for full time writers) or dedicate their time to their other occupation(s) (for part time writers). Potential new creators may decide not to enter the creative industry due to the reduction in economic incentives. Some creators will have sufficient incentives to remain in the industry but may reduce the time they spend on producing creative content – for instance focusing on areas of highest demand.

There are strong links between the incentives of educational creators and those of educational publishers. The same reductions in licensing income and sales are expected to lead to decreases in content production by publishers (as discussed above) which will in turn affect the creators of those works. Lower revenues mean lower market incentives for publishers to invest in the creation of new content, which means lower demand for Canadian creators' services. The reduction in the creation of indigenous content (i.e., content produced in Canada for the Canadian market) by publishers in Canada will relocate the demand for creation from Canadian creators to American or other international creators. Similarly, the narrowing in the breadth of published content and less content diversity will reduce the demand for creators that specialize in niche areas, including uniquely Canadian content and subject areas.

In the context of works for K-12 schools, teachers may be increasingly generating their own content for use in the classroom, by schools and by ministries of education. It is uncertain to what degree they are being compensated for these creations. Given the cost imperatives in the school system in Canada, it can be expected that teachers will receive little or no direct compensation for generating these kinds of teacher-developed learning resources. Teachers who are already pressed for time and resources cannot reasonably be expected to devote significant time to developing content, such that they can be expected to fill the void left by professional creators and publishers withdrawing from the K-12 market.

In summary, the Guidelines are expected to lead to both a reduction in the number of creators and/or a reduction in the time spent by creators producing content. This will be a direct result of the reduction in creators' economic incentives through the loss of licensing revenues, but also a result of the impacts that the Guidelines have had, and are expected to have, on publishers' decisions to decrease the number and types of works they publish.

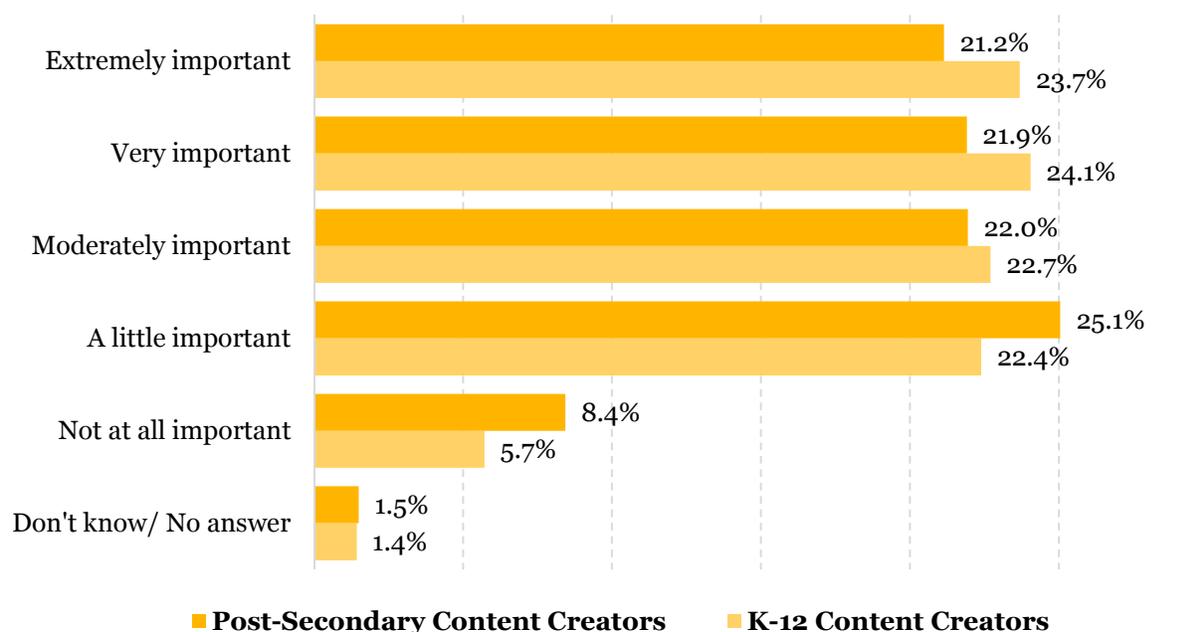
¹⁴⁴ PwC, 2012.

Data on Creators' Decision to Produce

Based on the results of the Circum Survey, the Guidelines are expected to have a material impact on the amount of knowledge-based content created by Canadian professional creators.¹⁴⁵ As noted previously, 66% of post-secondary creators and 72% of K-12 creators receiving licensing income from Access Copyright indicate that their employment does not involve teaching at any level. It is this group – Canadian professional authors and visual artists -- that is expected to reduce knowledge-based content creation in the face of reduced royalties due to the adoption of the Guidelines.¹⁴⁶

The figure below illustrates the importance of Access Copyright licensing income to the livelihood of creators.

Figure 20 – How important is the amount that you receive from Access Copyright to your livelihood?



Creators that create for the K-12 and post-secondary sector consider the licensing income that they receive from Access Copyright as important to their livelihood. As seen in Figure 20, the majority (66% and 71% for post-secondary and K-12, respectively) of creators affiliated with

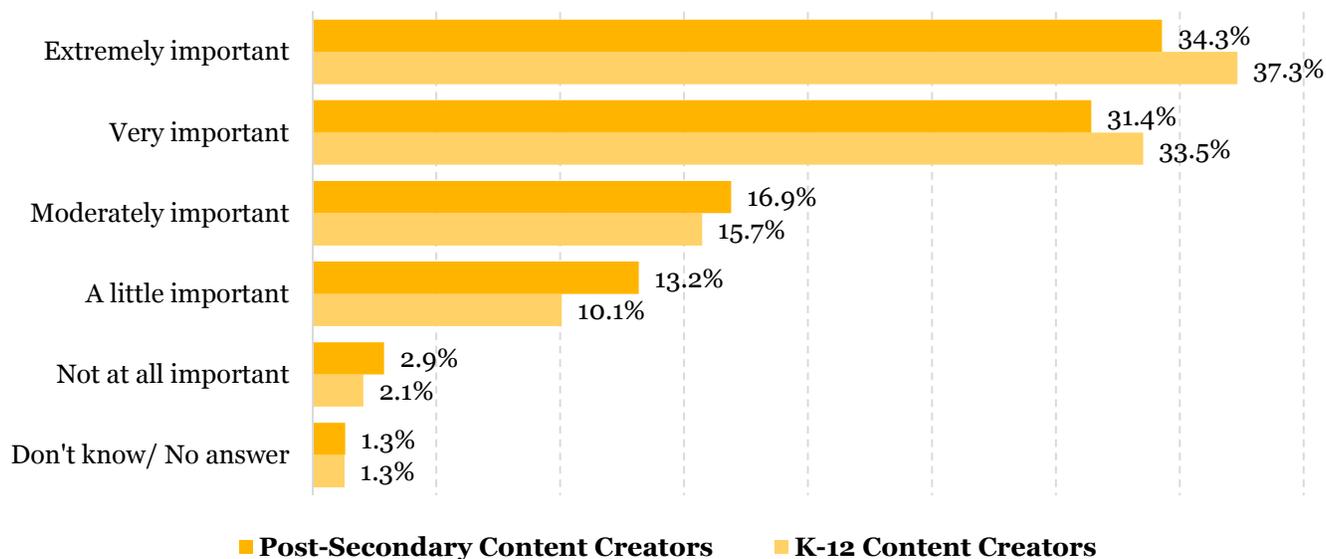
¹⁴⁵ These are authors and visual artists who are not employed by K-12 or post-secondary institutions. Results of the Circum Survey indicate that this category represents the majority of creators affiliated with Access Copyright (see Figure 4 above).

¹⁴⁶ Creators who are employed by post-secondary institutions are, conversely, less likely to limit production as a result of changes to licensing income. Many of these creators write to receive tenure and professional stature. Their employer requires them to publish in learned journals and provides their primary income stream in exchange for the reputational enhancement that comes from publishing in these journals. Licensing income is considered a secondary or tertiary income stream and is derived mostly from textbook authorship.

Access Copyright consider this income as moderately to extremely important to their livelihood. Only 8% of post-secondary creators and 6% of K-12 creators consider the amount unimportant.

The figure below illustrates the importance of Access Copyright income to educational creators, based on responses from the Circum Survey.

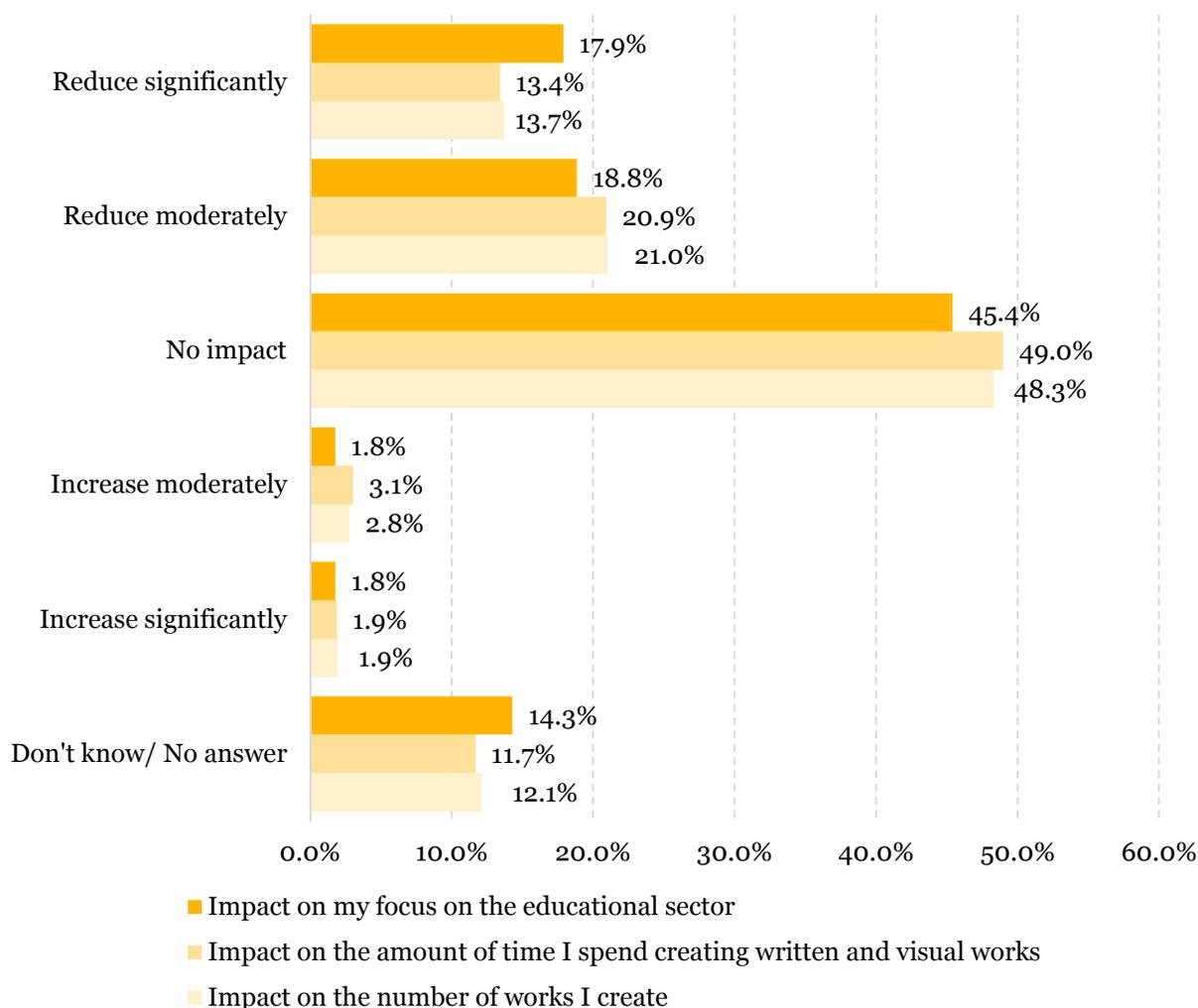
Figure 21 – How important is the amount you receive from Access Copyright to you as a Creator?



While Figure 20 demonstrates the importance of licensing income to creators' livelihoods—that is, their ability to earn a reasonable wage—Figure 21 considers the intrinsic value (e.g., reputational, personal, professional value) of this income to them as creators. As seen in Figure 21, the majority of creators (65% of post-secondary and 71% of K-12) affiliated with Access Copyright consider the income that they receive from Access Copyright as very or extremely important to them as creators. No more than 3% consider the amount unimportant.

The figure below illustrates the expected change in the number of works these authors and visual artists will create, the time spent creating and the focus on educational content if the Guidelines result in reduced licensing income.

Figure 22 – Impact on Creators’ Work in Response to Adoption of the Guidelines by Educational Institutions:¹⁴⁷



As seen in Figure 22, between 34 and 37% of creators affiliated with Access Copyright indicated that, if the Guidelines resulted in reduced licensing income, they would reduce the number of

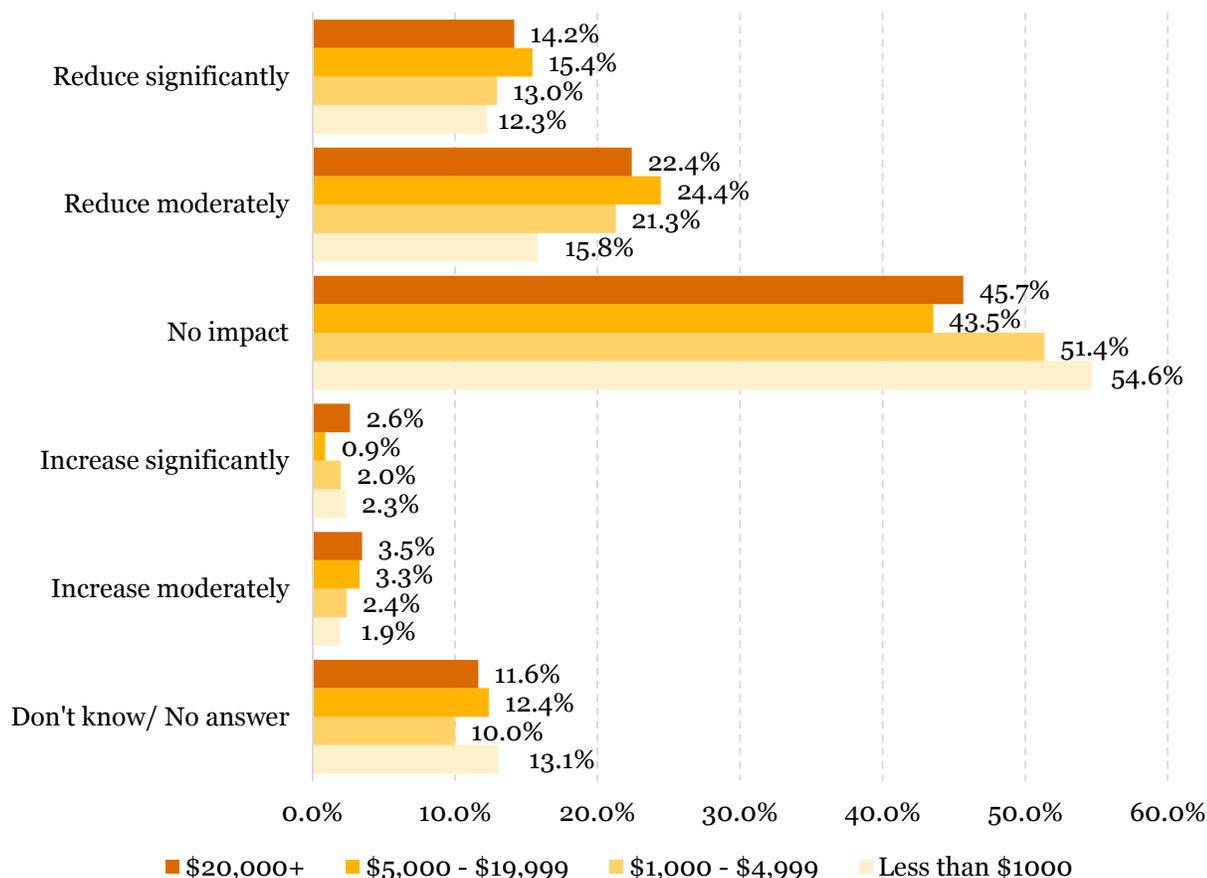
¹⁴⁷ Survey question: If the post-secondary/K-12 took the position that copying 10 percent of a book, or a chapter, or an entire article for free publisher income would likely diminish. Imagine that this would translate into a reduction of the income you derive from direct payments from publisher (royalties, commission, employment income, etc.) and from direct sales from self-publishing by [random number inserted into survey– 25, 50 or 75 percent]for your works copied by the post-secondary/K-12 sector. What would be the likely impacts of this situation on your written and visual creation?

works created, the time spent creating and their focus on creating content for the Educational Publishing Market.

Extrapolating these results to the entire population of Access Copyright creator affiliates who receive licensing revenues from the educational sector suggests that over 3,900 Canadian authors would reduce their output of new educational content as a result of the implementation of the Guidelines.

The figure below illustrates the expected impacts of the Guidelines on the number of works produced by educational creators according to their overall income derived from those works.

Figure 23 – Impact of the Guidelines on the Number of Works Produced, Segregated by Creators’ Annual Income¹⁴⁸.



As seen from Figure 23, the expected reduction in the number of works created by creators affiliated with Access Copyright is highest among creators that earn between \$5,000 and \$19,999, with approximately 40% of them indicating that they would reduce moderately or significantly the number of works created if the Guidelines were implemented and resulted in a

¹⁴⁸ Survey question: If the post-secondary/K-12 took the position that copying 10 percent of a book, or a chapter, or an entire article for free publisher income would likely diminish. Imagine that this would translate into a reduction of the income you derive from direct payments from publisher (royalties, commission, employment income, etc.) and from direct sales from self-publishing by [random number inserted into survey – 25, 50 or 75 percent] for your works copied by the post-secondary/K-12 sector. What would be the likely impacts of this situation on your written and visual creation? Cross tabulated with survey question: Consider your 2012 income from all sources associated with written or visual works you created. Include direct payments from publishers (royalties, commissions, employment income, etc.), Access Copyright royalty or Creator repertoire payments, direct sales from self-publishing, public lending rights, grants (government, industry, etc.), and any other sources of pertinent income.

reduction of licensing income. Approximately 37% of creators of educational content who earn \$20,000 or more from written or visual works, indicate that the Guidelines would also result in a reduction in their production of knowledge-based works.

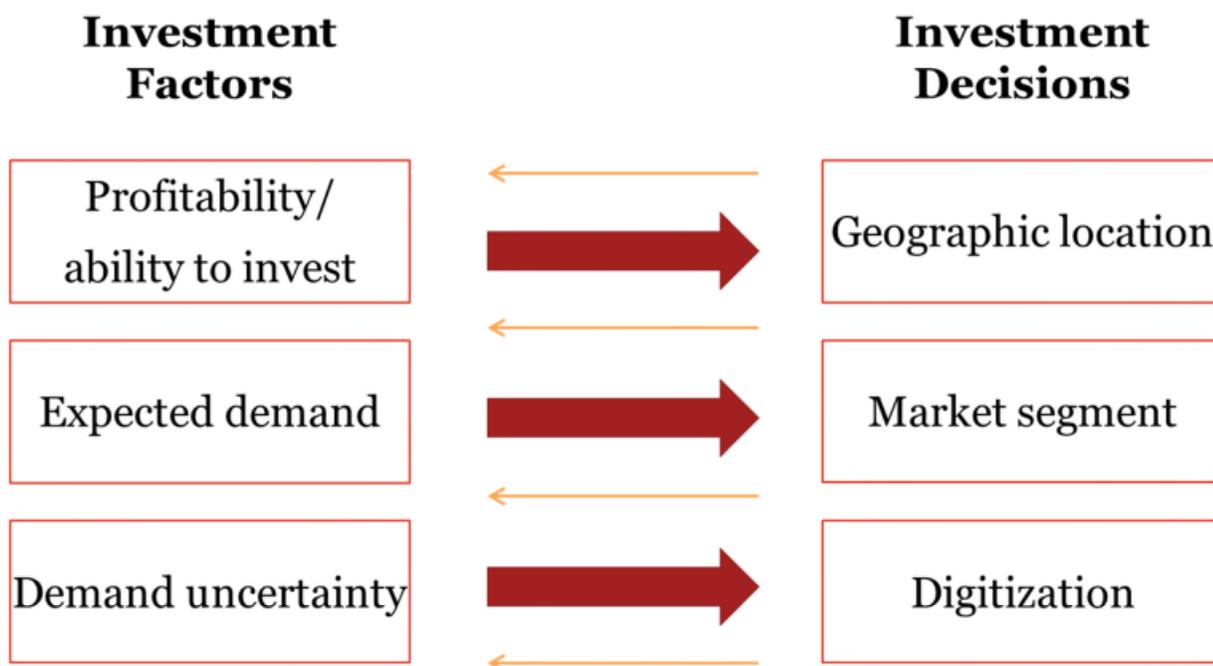
8.4 Investment

The Guidelines are expected to cause a reduction in investment by educational publishers in the Canadian market, leading to fewer titles, including those tailored for the Canadian market, and less variety in the titles produced (particularly for low enrolment courses). There will also be a slowing in the pace and extent of the conversion to digital publishing. The negative impacts of the Guidelines on investment in the Canadian market are already evident in reductions in staff at large educational publishers, the closure of the K-12 division at Oxford University Press, and the pending bankruptcy filing of Nelson Education.

The decline in sales and licensing revenues as a result of the Guidelines will impact the size and nature of investments made by educational publishers. An investment is defined as a purchase of goods that are not consumed today but are used in the future to create wealth. Decisions about whether to invest and where to invest depend on the current means to invest and the expected return on investment. The Guidelines will impact both these factors, since they reduce current revenue and profit streams from sales and licensing and increase the uncertainty of future income.

Figure 24 illustrates the factors that affect investment decisions and how these may be impacted by the Guidelines.

Figure 24 – Investments Factors and Decisions



As discussed earlier, the Guidelines appear to have already led to and are expected to continue to accelerate the elimination of licensing revenue and a decline in sales. In addition, the adoption of the Guidelines signals to publishers a trend of declining respect for copyright or copyright protection, which also increases the level of uncertainty for publishers in terms of future demand.

As a result of decreased profitability, expected lower future demand and increased uncertainty, publishers have already reconsidered the areas in which they invest and will likely continue to do so.

In particular, the nature of the K-12 market, wherein core resources are customized to the curriculum of each jurisdiction, has resulted in a fragmented market with limited cross-jurisdictional sales and exports. As such, the economies of scale that can be realized in the K-12 market are limited. Because the investment requirements to produce a core K-12 resource are significant (\$400,000-\$800,000 per title),¹⁴⁹ the ability of publishers to remain in the K-12 market will be seriously undermined as licensing revenue and sales decrease.

Publishers may select specific segments within the K-12 and post-secondary markets where their return on investment will be higher, thus narrowing their breadth of offerings to areas that are expected to be less impacted by the Guidelines. For example, post-secondary books catering to first or second year courses (e.g. Psychology 101) are generally associated with higher sales since enrolment is greater and curricula vary less from one institution to another. Also, certain fields, such as medicine, may attach more importance to timely and relevant information, and

¹⁴⁹ Rollans, 2010, p28.

consumers therefore may be willing to pay a premium for new editions as opposed to using copies of earlier editions.

Similarly, K-12 publishers will be more likely to develop resources for higher enrolment courses since these will be associated with higher sales and a higher return on the monies spent to develop the resource. Upper level elective or optional high school courses are expected to see the greatest decrease in investment and resource production. As a result of publishers focus on certain high-enrolment courses, other courses such as “Canadian History since WWI”, “Canadian Literature”, “Aboriginal Governance,” “Extended French”, “Media Arts”, “Canadian and World Politics”, “Green Industries” and “Families in Canada” may become underserved.¹⁵⁰

Reduced investment may also lead to a shift in the type of content distributed in Canada. The largest expected impact for large publishers is a growth in the use and distribution of imported and adapted U.S. content in Canada, at the expense of Canadian created and curated content. It is far less costly for publishers to adapt material developed by their U.S. counterparts than it is to develop original content for the Canadian market. So, large Canadian publishers will increasingly turn to adapting U.S.-created content for the Canadian market, rather than investing in the creation of Canadian-made, or indigenous, content. Publishers may also reduce their investments in adaptations of U.S. content, and will instead simply act as distributors for U.S. content. It is thus expected that imported content will grow at the expense of indigenous Canadian content.¹⁵¹

Publishers, particularly multinationals, are also expected to increase their investment in emerging markets outside of Canada, where revenue and profit prospects are higher. Developing economies such as China and India offer opportunities in higher education publishing¹⁵² because governments in these countries are focusing on improving education. That focus will boost spending on educational books and related products¹⁵³. Weaker copyright protection in Canada will reduce one of the remaining key advantages that a country like Canada has historically provided publishers as compared to developing countries. In turn, this will increase the attractiveness of investing in these countries at the expense of Canada.

The Guidelines may also impact the level of investment in digital technology. As noted previously, digital publishing is in its infancy and requires substantial investment in order to create enhanced interactive solutions that go beyond the traditional e-book. The Guidelines directly limit the cash flow available for this investment. Canadian-owned and small publishers will be further constrained in making the appropriate investments in digital technology and will suffer in terms of competitiveness. Indeed, smaller publishers will feel the impact of the decline in licensing income (as shown earlier) more severely, leaving them with less funds available for investment and making them less able to continue to make the necessary investments to service the digital economy.

¹⁵⁰ These examples were taken from the Hamilton-Wentworth District School Board secondary school course calendar: <http://www.hwdsb.on.ca/wp-content/uploads/2012/05/secondary-course-calendar.pdf>.

¹⁵¹ As noted previously the data on primary sales between 2012 and 2014 appears to suggest that such a trend is already underway.

¹⁵² IBISWorld, 2012.

¹⁵³ IBISWorld, 2012.

The expected increase in copying as a result of the Guidelines also creates uncertainty as to the level of demand for digital solutions in particular and the future of copyright protection in general. Increased uncertainty on the demand side reduces the willingness of investors to take a risk and thus reduces investment.

Data on investment

In 2014, Oxford University Press, one of the largest publishers in Canada, announced it was closing its K-12 publishing division, resulting in job losses.¹⁵⁴ As explained in Section 8.1.1 above, Oxford indicated that changes to the *Copyright Act* and the loss of licensing income from Access Copyright were contributing factors in the closure.

Further, Nelson Education has recently filed for bankruptcy protection in Canada and is being restructured. Declining public spending on educational resources was identified as a key contributor to the bankruptcy.¹⁵⁵

McGraw-Hill Ryerson announced, in 2013, that it was “consolidat[ing] its distribution capabilities into McGraw-Hill Education’s U.S.-based distribution system” such that orders from Canadian customers will now be distributed from a warehouse in Columbus, Ohio. This change included the closure of the company’s warehouse facility in Whitby, Ontario.¹⁵⁶ The loss of licensing income was a contributing factor to the facility closure.¹⁵⁷

Another large publisher indicated to us that, since the Guidelines, the investment and staff in their K-12 division have declined to approximately half its previous levels. The following figure shows that headcount in large educational publishers has declined significantly after the Guidelines were introduced in 2012, at a rate of 6% and 5% in 2013 and 2014, respectively. Headcount can be considered a leading indicator for future investment.

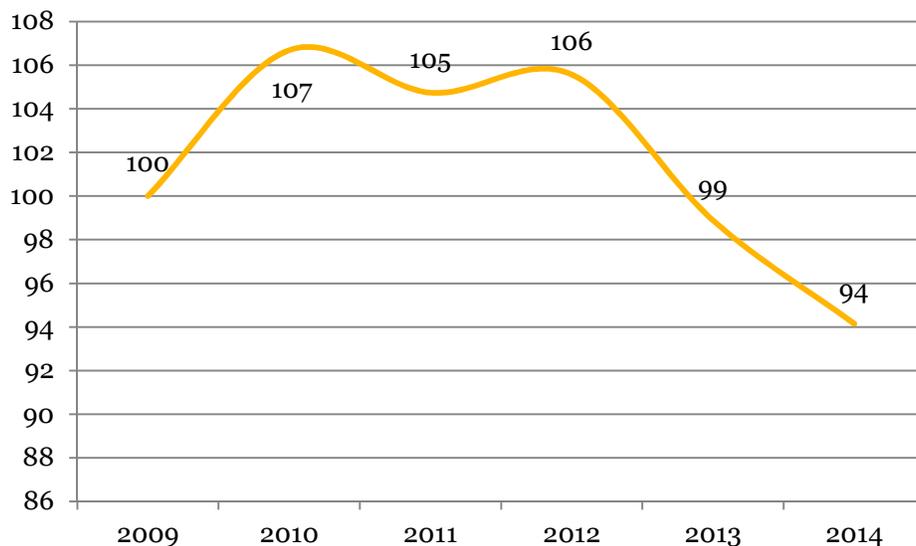
¹⁵⁴ Why the loss of Access Copyright royalties could be devastating for educational publishers, Julie Baldassi, May 29, 2014, Quill & Quire.

¹⁵⁵ See, for instance, the Pre-Filing Report of the Proposed Monitor for the Plan of Compromise or Arrangement of Nelson Education Ltd., May 11, 2015, Section 4.6. Accessible at: [http://cfcanada.fticonsulting.com/NelsonEducationLtd/docs/Nelson%20Pre-filing_Report%20of%20the%20Monitor%20May%2011%2015%20\(final\).pdf](http://cfcanada.fticonsulting.com/NelsonEducationLtd/docs/Nelson%20Pre-filing_Report%20of%20the%20Monitor%20May%2011%2015%20(final).pdf)

¹⁵⁶ “McGraw-Hill Ryerson Limited Announces Strategic Initiatives,” Press Release, November 21, 2013.

¹⁵⁷ Witness statement of Nancy Gerrish dated December 16, 2013, para 26, presented as Access Copyright Exhibit AC-5 in the proposed Elementary and Secondary Schools Tariff, 2010-2015 before the Copyright Board of Canada.

Figure 25 – Annual Change in Headcount at Large Publishers (Index using 2009 as base year)¹⁵⁸



Based on the responses from the ACP Survey (see Figure 19) and discussions with SME publishers in Canada, there is also a trend among SMEs in the sector to narrow their business focus and reduce their product offerings.

During publisher interviews, it was stated by publishers that broad adoption of the Guidelines is already resulting in reduced investment in the Canadian Educational Publishing Market. The following observations were made by publishers:

- Fewer titles are now being produced for the Educational Publishing Market. In reaction to reduced revenues and profitability, publishers have reduced investments made in creating new titles. The reduction varies significantly between different fields.
- Large post-secondary publishers are focusing relatively more efforts on scientific, technical and medical study fields, where students have expectations of high income jobs and require access to state of the art content that is complete (as opposed to disaggregated or excerpted). In contrast, study fields such as humanities and social sciences are generally losing favour with publishers.
- K-12 publishers are focusing more effort on high enrolment courses that are associated with a large amount of sales, while reducing efforts on courses with lower enrolment (e.g. elective or optional courses).
- Publishers are also reducing their investment in certain learning resources. For example, some publishers indicated that they had already ceased to produce consumables as a result of increased, uncompensated copying.

¹⁵⁸ Data on post-secondary headcount for one of the publishers was not available.

- There has been a reduction in the number of titles tailored for the Canadian Educational Publishing Market. The majority of large publishers in Canada are multinational organizations that make investment decisions on a global basis. Reduced relative profitability of the publishing industry in Canada is encouraging these publishers to focus resources on developing content for other geographic markets where sales and profits are higher.
- The Educational Publishing Market is in a period of transition from paper to digital revenue streams. The transition to digital requires significant investment. One publisher described the transition as an evolutionary process where much investment is needed today. Any impediment to the transition, such as the loss of revenue and uncertainty created by the Guidelines, would be equivalent to “changing the undercarriage when the airplane is in flight”. Reduced investments in Canada could cause the publishing industry in Canada to fall behind the progress towards a digital, knowledge-based economy being made in other countries. Publishers noted that Canada was already behind in its transition and the Guidelines may further widen the gap.

8.5 Industry Economic Footprint

Implementation of the Guidelines contributed to a significant shrinking of the industry’s economic footprint between 2011 and 2013. It is expected to further accelerate the shrinking of the industry’s economic footprint.

As noted in Section 6.3, the total economic footprint of the Canadian educational publishing industry in 2013 was significant, amounting to approximately \$620 million in GDP and 6,400 jobs.¹⁵⁹ However, this represents a significant (16%) reduction from its 2011 economic footprint of \$740 million in GDP and 7,650 jobs.

The K-12 sector has been in drastic decline since 2008. Before the introduction of the Guidelines, the economic footprint of the K-12 educational publishing industry was \$200 million in GDP and 2,030 jobs. By 2013, the economic footprint of the K-12 educational publishing industry had declined to approximately \$150 million in GDP and 1,600 jobs (a decline of 25% since 2011).

The introduction of the Guidelines and the elimination of licensing revenues will contribute to a further deceleration in sales and corresponding loss of revenues. This makes this sector particularly vulnerable. Substantial segments of the K-12 industry are expected to be eliminated as a result of the loss of both sales and licensing income and the limited public funding of educational resources. Given the challenges faced by K-12 content producers, it is apparent that the economic footprint of that segment of the market is particularly at risk of further decline and the viability of the market itself is at risk.

¹⁵⁹ Including direct, indirect, and induced impacts.

A K-12 publishing model that allows teachers to create content without compensation, would have a significantly smaller economic footprint than the industry has today.

Moreover, the re-alignment of the publishing industry away from content production and toward the distribution of imported US-produced content is expected to impact the footprint of economic activity associated with the sector in Canada. Ultimately, more Canadian money and investment, and corresponding jobs, will flow out of the country.

Given that publishing industry jobs are particularly high value and the skills of individuals employed are relatively specialized, it is also possible that job losses in the industry will be long-lasting. This further exacerbates the negative economic impacts caused by the Guidelines.

8.6 Industry Composition

The Guidelines will have negative structural impacts on publishers, likely causing much of the K-12 publishing industry to shut down. The impacts will be felt most by SME publishers because of intense competition from larger publishers, low profit margins, and an inability to scale. Some SME publishers may redirect investment into more profitable areas of the publishing industry.

Both large and small publishers are expected to exit the K-12 Educational Publishing Market as a result of the Guidelines. This consolidation of the industry in the K-12 market means that competition will be reduced with potential negative impacts to continued innovation, quality and prices.

The actual and expected future reductions in revenue from declines in sales and licensing income are expected to have greater negative consequences on smaller publishers. SME publishing has been described as an increasingly difficult sector¹⁶⁰. Competition within the industry is high and favours larger players. Creators are often attracted to well-known publishers that have the financial flexibility to invest in brands. Large post-secondary publishers also have the ability to exert more influence on the prices of downstream retailers, which can give them an advantage over smaller firms¹⁶¹. SMEs have a more limited ability to shift focus geographically or between course subject-areas. As a result, some SME publishers may struggle to survive in the Educational Publishing Market, despite their commitment to transitioning to the digital marketplace. Some may ultimately be forced to decide to exit this market or direct their resources towards areas of publishing with more favourable and sustainable market conditions.

Furthermore, with probable declines in revenues and profits, the ability of SME publishers to continue to invest in digital will be significantly impaired. As a result, they may become less competitive relative to larger publishers in the long-run, which will also threaten their ability and desire to continue to publish for the Educational Publishing Market.

¹⁶⁰ Altbach, Philip, Chapter 23: Book Publishing. Bellagio Publishing Network, available from UNESCO.

¹⁶¹ IBISWorld, 2012.

With the introduction of the Guidelines and the education sector's interpretation that they can now disaggregate the content and copy the vast majority of it for free, educational publishers' position in the market has become even more precarious. The Guidelines are also expected to lead to increased concentration in the publishing industry. As a result, competition among publishers will decrease and prices and incentives to innovate may be impacted.

Data on Industry Composition

Change to industry composition is a longer-term impact that cannot be meaningfully measured in the short term. Thus our evidence in this regard is based on expectations of publishers expressed during interviews.

From our interviews, we understand that SME publishers expect that there will be fewer publishers in the educational sector. Large publishers echoed this concern, expecting additional mergers (and acquisitions) in the industry and the closure of some publishers or publishing divisions. In particular, given the impact of the loss of licensing and sales revenue on the profitability of SME publishers, there is concern that SME publishers will produce fewer books, have to consider downsizing and laying off staff, may decide to shift their resources away from the Educational Publishing Market and may exit the market altogether. This is particularly so for publishers that derive over 10% of their revenues from the Educational Publishing Market. Some SME publishers indicated that they would shift away from educational publishing to other publishing segments. Similarly, large publishers have already downsized and are looking to divert their investments outside of Canada in response to the Guidelines.

8.7 Content Diversity and Quality

The Guidelines are expected to lead to a reduction in the diversity and quality of content produced for the Educational Publishing Market. Certain courses or subjects may become underserved. Alternatives to publisher-developed content will ultimately lower the quality of learning resources available to students and consequently lower educational outcomes.

According to the economic theory of copyright, the reduction of copyright protection reduces the economic incentives to produce content and induces under-production. Although copyright users may benefit in the short run from less expensive access to copyright-protected content, they will be harmed in the long run by having reduced content diversity.

Users of copyright works are expected to experience reduced content diversity through two mechanisms: first, title and product rationalization; and second, fewer SME publishers in both the post-secondary and K-12 markets.

Title and product rationalization are expected to occur due to the reductions in investment, leading to

- fewer indigenous titles (users will have less access to indigenous books and content in favour of content adapted from mostly American content);

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- fewer titles per course area (the range of options for a given course area will be reduced as publishers reduce the production of titles); and
 - fewer course subject-areas served (when publishers focus on more profitable areas, certain areas may become underserved).

The rationalization of content may be further aggravated by the reduction in diversity of works as a result of fewer works produced by smaller publishers. Small publishers publish more works from Canadian creators and are considered to be essential to the dissemination of Canadian ideas. Smaller publishers are also an essential component of the creative landscape because they often focus on the publication of innovative and avant-garde ideas. Small presses have traditionally been associated with experimental and avant-garde writing, while large publishers are generally geared to books that are guaranteed to be profitable and are more likely to focus on widely accepted and recognized concepts and ideas.

The concentration in the Educational Publishing Market (described previously in this Assessment) is expected to be accelerated by the Guidelines, resulting in a “squeeze out” of SMEs in this sector. This would lead to a decline in the number of innovative and avant-garde ideas that find a “voice” in the public discourse. This would impact the diversity of works available to students.

The K-12 education system is contemplating filling the void left by publishers with creating and using freely available material, including the “free” copying of excerpts from professionally published content that is sanctioned by the Guidelines. By decentralizing the purchase of learning resources and by loosening the requirements for resource authorization, education systems in Canada are facilitating this transition away from the traditional Publisher-Based Production Model.

During the interviews, publishers highlighted the role they play in the educational content publishing value chain. For one, publishers spend a large amount of time and expense in order to test and evaluate content. Publishers of core resources for example will select classrooms across Canada and allow teachers to test the resources and suggest improvements. The entire process of developing a resource can take four or five years. Publishers go through a rigorous process to ensure quality in terms of alignment with curriculum, scientific accuracy, absence of bias and educational usefulness.

Teachers on the other hand are not professional resource developers. It is expected that teacher-developed and open-sourced resources may suffer from the following limitations, as compared to publisher-developed resources:

- Experience in developing age-appropriate resources: Most Canadian publishers have published in the K-12 sector for many years and have gathered a wealth of knowledge that they apply to create a resource. They are experts in the pedagogy of learning resources. Teachers, though skilled at teaching, may lack this experience.

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- **Equity:** There will be greater disparity in the quality of learning resources provided to students across jurisdictions if individual teachers become responsible for creating their own resources.
 - **Review process:** Publishers currently face a stringent review and approval process for the resources they develop. The alternative that has been suggested is for teacher-developed resources to be peer reviewed. Given the prevailing conditions in the K-12 system and the increasing pressures on teachers, it is doubtful that teachers have the time or financial incentives to fill the void in this regard.
 - **Cost-effectiveness in developing resources:** Publishers are cost effective because of their experience, professional network, and scale in the process of resource development. It is unclear whether a de-privatized publishing industry would be more cost effective or efficient than the private publishing industry.

Published materials are the end product of extensive research and development by highly experienced and expert creators. The quality of these materials would be exceedingly difficult for an individual teacher to recreate and the creation of additional materials would constitute a significant burden on teachers' time. In the event teachers are obligated to spend time producing materials and are therefore less able to accomplish other tasks, students could be negatively impacted. Teachers that are provided with quality and comprehensive content have more time to dedicate to improving the student experience in the classroom. To the extent that teachers, school boards and provincial education ministries lack sufficient resources to create their own material, we would also expect an increased reliance on outdated material, material that does not fully match curricula or course requirements (particularly for K-12 content) or material that is not tailored to the Canadian market.

Data on Content Diversity and Quality

The rationalization of publisher-generated content and reductions in content quality are long-term impacts, whose full effect is not yet felt, however publishers pointed to evidence that supports this expectation.

Publishers have already observed initial indications of a reduction in competition and investment. Publishers stated in interviews that they have seen a decrease in the number of publishers responding to requests for proposals to produce textbooks for the new K-12 curriculum. During the interviews, a large K-12 publisher indicated that in response to recent changes to the social studies curriculum in Ontario, only one publisher developed content at certain grade levels. Previously, several publishers would be expected to compete in the market at each grade level.

The impact is felt more in disciplines with high distribution costs (e.g. low enrolment and more advanced courses), where publishers are producing fewer titles and where potential returns do not justify the investment required to develop digital solutions. This will lead to content in such courses being less updated and reflecting fewer different points of view.

Copying of chapters under the Guidelines will particularly impact content producers of anthologies. For instance, poets, short story writers and visual creators who publish their works

in collections are expected to be negatively impacted as the entirety of their stand-alone works from their anthologies are copied as chapters under the Guidelines, replacing sales and licensing royalty revenues. One SME publisher indicated that it had ceased publishing collections of poetry and plays in response to the Guidelines.

As mentioned earlier, some publishers have stopped producing consumables for the K-12 market given the prevalence of copying of these materials and the position taken by K-12 schools that portions of consumables can be copied for free. We expect this trend to continue, resulting in a reduction in the quality of the educational material produced for the K-12 market in Canada.

In the post-secondary market, large publishers indicated that the Guidelines will further cause them to focus on courses with high income potential where information needs to be timely and relevant. Indeed, copying of existing material is less likely to substitute for textbooks or content in disciplines that require the most up to date information. Examples of such disciplines include scientific, technical and medical areas while examples where publishers are withdrawing include history, languages, arts and culture. Publishers have also been focusing increasingly on first and second-year courses where enrolment and return on investment is high and where standard textbooks tend to be preferred over course collections. One publisher cited the introduction of the Guidelines as a major factor leading to their decision to cease production of political science and Canadian history textbooks.

In both K-12 and post-secondary markets, the Circum Survey indicated that creators place significant importance on the income they receive from Access Copyright licensing fees. As noted previously, over one third of educational creators indicated that a loss of income from licensing fees in circumstances like the widespread adoption of the Guidelines by institutions would lead to a reduction in the number of works they produce. This loss of income would compound trends already underway, including the adoption of digital materials which may require more investment on the part of publishers and therefore leave lower margins available for creator compensation.

Finally, we note that the expected reduction in diversity and content will be accompanied by higher prices, so copyright users will be paying more for less.

9. Conclusions

The evidence and analysis presented in this Assessment leads us to the conclusion that the educational publishing industry in Canada, which has been facing numerous challenges in recent years, cannot withstand the additional negative economic impacts of the Guidelines. These Guidelines have fundamental implications for the structure and size of the industry in Canada. In the short term, we expect the Guidelines to lead to a transfer of wealth from content producers to content users. In the long term, content producers will likely adapt by reducing content production, which will, in turn, adversely affect the quality, diversity, and affordability of resources to content users.

The educational publishing industry is in a period of transition from traditional textbook publishing to digital solutions, content, and services, but this transition requires significant investment on the part of publishers. The Guidelines limit the educational publishing industry's ability and incentives to invest in the digital, knowledge-based economy in Canada.

A number of SME publishers will not be able to adapt successfully to the new circumstances, to seize digital opportunities, or to successfully transition to the digital market. They are, therefore, expected to exit the Educational Publishing Market or pursue other areas of publishing with more favourable market conditions. In addition, substantial portions of the K-12 publishing industry may be eliminated as a result of the loss of sales and licensing income as well as limited public funding of educational resources. Authors, visual artists, and publishers are expected to produce less content for the Canadian educational system and to invest less in the Canadian market.

Specifically, there are various levels of evidence of the following:

- The Guidelines have caused an atmosphere where unlimited copying has become commonplace, while content producers are unable to assert their intellectual property rights in any meaningful way.
- Large publishers have started to exit the K-12 content market, reducing competition in the market with potential impacts on incentives to innovate and prices.
- Large Canadian educational publishers are reducing their production of Canadian content and increasing their reliance on distribution of U.S. materials.
- Creators are expected to respond to losses of income due to the Guidelines by reducing the number of works they create, the time they spend creating, and their focus on creating content for the Educational Publishing Market.
- Many SME publishers producing educational content are expected to exit the business as a result of eliminated revenues (including licensing income, a significant source of revenues for SME publishers) and insufficient scale to make investments in digital solutions to compete with large publishers.

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- Publishers will reduce product offerings for subjects without sufficient scale, demand, and requirements for current content to justify investment in capital-intensive digital solutions.

These developments will have significant implications for the industry's economic footprint in Canada, which totalled approximately \$620 million in 2013. Negative impacts will emerge as reduced investment limits productivity growth, the industry shifts from content production in Canada to the distribution of imported content, and affected content producers are challenged to find alternative employment positions given the high value of jobs in the publishing industry.

In the longer term, Canadian K-12 and post-secondary students, teachers, and professors—namely, the users of educational content—will also be subject to negative impacts from the limited availability of digital and Canadian content, a deterioration in the diversity and quality of content used in the classroom, and a market framework that eliminates incentives and discourages innovation in the Canadian digital, knowledge-based economy.

Appendix: Limitations

To conduct this Assessment, PwC relied upon the completeness, accuracy, and fair presentation of all information, data, advice, opinions or representations obtained from various sources which were not audited or otherwise verified. These sources (collectively, the “Information”), include

- surveys of Canadian publishers;
- surveys of Canadian creators;
- publishing industry data from the Canadian Educational Resources Council and the Canadian Publishers’ Council;
- data regarding distributions to publishers from Access Copyright;
- economic input-output tables from Statistics Canada;
- publicly available studies and reports; and
- other publicly available data and information.

The findings of this Assessment are conditional upon such completeness, accuracy and fair presentation of the Information, which has not been verified independently by PwC. Accordingly, we provide no opinion, attestation or other form of assurance with respect to the results of this Assessment.

Given the relatively short time that has elapsed since post-secondary institutions started not renewing their licences with Access Copyright (some institutions declined to renew in January 2011) and since the Guidelines were put in place (autumn 2012), some of the effects of the Guidelines are in their infancy and so are difficult to detect and other effects have yet to be experienced. Further, some licensing agreements with post-secondary institutions have not yet expired (at which point the impacts of the Guidelines are expected to manifest more intensely). Also, the short time frame and the limited frequency of transactions may not allow appropriate control for cyclicity in sales. Therefore, substantial quantitative data regarding the majority of the economic impacts is not yet available. The data collected as part of our Assessment relates mainly to early signs and indications of these expected impacts.

We further note that given the context of the Assessment, PwC was limited in its ability to gather data from certain stakeholders such as university bookstores, and professors in unlicensed institutions.

Given the above limitations, it is important to emphasize that lack of quantitative data at the present time regarding some of our expected market impacts does not reduce the validity of those economic impacts. Moreover, in assessing the impact on the Educational Publishing Market of the Guidelines at this time, the qualitative information is crucial to our Assessment. Since there has been insufficient experience with the Guidelines to provide the data required for a thorough quantitative analysis, in many instances qualitative information is the best data available.

PwC reserves the right at its discretion to withdraw or make revisions to this Assessment should we be made aware of facts existing at the date of the Assessment that were not known to us when we prepared this Assessment. The findings are as of June 2015. PwC is under no obligation to advise any person of any change or matter brought to its attention after such date which would affect the findings, and PwC reserves the right to change or withdraw this Assessment.

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