

**A BRIEF**

**from**  
**The Literary Press Group of Canada**  
**and**  
**The Association of Canadian Publishers**

in response to

***Sharpening Canada's Competitive Edge***  
**by the Competition Policy Review Panel**

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It is a pleasure to be addressing the Competition Policy Review Panel about Canada's competitiveness and productivity. Our paper will deal with the questions about Canada's sectoral investment regime for cultural industries, and we will focus exclusively on issues that are critical to the **book publishing sector**.

The Literary Press Group of Canada (LPG) and The Association of Canadian Publishers (ACP) are both national organizations. The LPG was created in 1975 and represents 62 Canadian-owned-and-controlled book publishers that specialize in publishing literary works – defined as fiction, poetry, literary non-fiction, drama and literary/cultural criticism. The ACP represents 125 independent Canadian-owned businesses from all provinces of the country. Seven regional associations are affiliated with the ACP, as is the Literary Press Group. ACP members publish the full spectrum of books in English: fiction, educational texts, poetry, mysteries, audio books, graphic novels, drama, children's books, works of scholarship and reference books.

Both The ACP and The LPG believe that Canada becomes more productive and competitive if the federal policy on foreign investment in book publishing produces two important net benefits to Canada and Canadians:

- (1) a diverse range of books available to the Canadian public, especially Canadian-authored works that tell Canadians about themselves in stories and facts, and
- (2) an environment where individuals employed by, and companies doing business in, the book publishing sector can enjoy economic success, including wide dissemination of Canadian-authored books throughout Canada and the world.

We further believe that these net cultural benefits are achieved through two critical means:

- (1) majority ownership and effective control by Canadians of book-related enterprises generally, **including the continuation of current foreign investment restrictions on book publishing**; and
- (2) subject to a **more effective test and enforcement for net benefit to Canada of a cultural enterprise**, an openness to foreign investment in book-related enterprises other than publishing.

### *Foreign Investment Restrictions on Book Publishing*

At present, the *Investment Canada Act* requires that foreign investments in book publishing be compatible with Canada's cultural policies. Yet Canada has no official, articulated "cultural policies"—neither in the field of culture in its broadest sense, nor in its various sectors and sub-sectors. Because of this, we would respectfully suggest that when considering cultural policies, that officers of the Book Publishing Industry Development Program (BPIDP) at the Department of Canadian Heritage and the Writing and Publishing Section of the Canada Council for the Arts become active, determining participants in these decisions at Investment Canada. In this way, Investment Canada decisions wouldn't weaken, or make less effective, the initiatives that the BPIDP and the Canada Council design and implement in their intervener roles in our industry. Investment Canada's decisions would actually complement and reinforce the Canada Council's and Canadian Heritage's initiatives and interventions, which have a long history of development.

Foreign investment in new business enterprises is restricted to Canadian-controlled joint ventures, limiting the foreign investment to 49% of all shares. (Ideally, this should be changed in the book publishing sector to match Canadian Heritage and Canada Council's 75% Canadian ownership rules.) Acquisition of an existing Canadian-controlled business under financial distress, or an existing Canadian business, in excess of 49% of its shares by a non-Canadian is not permitted except if there has been full and fair opportunity for Canadians to purchase; the acquisition is of net benefit to Canada and to the Canadian-controlled sector, and it is subject to one or more commitments. These could include, as outlined in the policy:

- a commitment to the development of Canadian authors, such as undertaking joint ventures with Canadian-controlled publishers which would introduce the partner's Canadian authors to new markets both domestically and abroad;
- a commitment to support the infrastructure of the Canadian book distribution system;
- accessibility of the company's Canadian marketing and distribution infrastructure (and international networks) to interested and compatible Canadian-controlled publishers on a contractual basis; or

- a commitment to education and research through financial and professional assistance to Canadian institutions offering programs in publishing studies.

According to Statistics Canada's (StatsCan) latest report on book publishing, in 2004, there were 19 foreign-controlled book publishers in Canada, compared to 311 Canadian-controlled companies. Yet these 19 foreign-controlled publishers in 2004 accounted for 59% of book sales in Canada, and 67% of educational book sales in Canada.

These statistics show two elements of how effective the current policy is with respect to Canada's competitiveness. First, the restrictions have no negative impacts with respect to the choice of book titles offered to the Canadian public. Canada is an open marketplace for books. Second, compare these percentages to the latest StatsCan reports of foreign producers' market share in other cultural industries (69% of television viewing in 2002, 87% of sound recording sales in 2000, 99% of film box office in 2002) and it is evident that Canadian-controlled book publishers lead the cultural industries in their competitiveness and in their provision of net cultural benefits to Canadians.

Further to this, Canadian-controlled book publishers produced 86% of titles printed in Canada, according to the same 2004 StatsCan study, and a similar percentage of Canadian-authored titles published in Canada. This demonstrates the vast majority of research and development of Canadian authors is done by Canadian-owned-and-controlled companies. This not only benefits Canadian writers and readers, but has an impact on the publishing programs of foreign-controlled companies. While most Canadian-authored titles are published by the Canadian-controlled sector, that sector's commitment to developing and promoting Canadian writers has also had a spill-over effect among branch plant companies. Because of the success and diverse range of Canadian authors developed by the Canadian-controlled publishers, foreign-controlled publishers have had the confidence to sign many of these authors to multi-book deals. In effect, without a strong Canadian-controlled sector, the Canadian-author programs of foreign-controlled companies would also diminish.

Also, the Canadian-owned-and-controlled book publishers are responsible for the vast majority of the diversity of titles published in Canada, publishing books specific to regions, cultures etc., while foreign-owned-and-controlled companies tend to concentrate on publishing material that is very narrowly focused.

If the current restrictions to foreign investment in the Canadian book trade were lifted, would Canadian authors or previously-Canadian-controlled companies have greater access to the marketplace? There have been no restrictions on the number of Canadian authors these foreign-controlled companies could publish, or the number of distribution arrangements these companies could make with Canadian-controlled companies. (In fact, these are specifically encouraged by the foreign investment policy.) Therefore, the publishing of Canadian authors, and

access through distribution, is subject to an open marketplace, and would not improve if changes were made to this sectoral investment regime for cultural industries.

If there was another foreign investment mechanism put in place, would that improve the ability of Canadian authors or Canadian-controlled publishers to access foreign markets? Could a previously-Canadian-controlled book publisher become a global champion, if it attracted more foreign direct investment (FDI)? The statistics demonstrate otherwise. Canadian-controlled companies lead the charge for selling Canadian authors abroad, and are responsible for more than 86% of all export sales in 2004, according to Statistics Canada. Typically, a foreign-controlled book publisher only acquires the rights to publish in Canada, since the acquisition of world rights would cost more, and the Canadian branch would prefer its related companies to incur the costs to publish outside of Canada.

Furthermore, Canadian-controlled companies have been aggressive in accessing foreign markets, with a 12% increase in export sales each year on average, according to the Association for the Export of Canadian Books. If there are foreign markets for Canadian-authored books, there are other means apart from FDI available for a foreign-controlled publisher or distributor to provide capital to a Canadian-controlled company, e.g. an interest-free loan recoupable from distribution revenue. Also, Canadian-owned-and-controlled companies can create their own means of sales and distribution, and have the best opportunity to become a global champion.

While it remains true that multinational enterprises (MNEs) in book publishing outperform Canadian companies on profits, they perform only marginally better on wages. Canadian-owned-and-controlled companies paid 57% of all book-publishing wages in 2004 in Canada, despite having a lesser percentage of revenues. (Canadian-controlled companies employ two-thirds of the 25,000 Canadians employed or contracted by book publishers.) The discussion above has already shown that smaller Canadian-controlled companies outperform the MNEs on productivity and exports. Also, when it comes to innovation, Canadian-controlled companies have individually and collectively remained on the cutting edge of new technology and its opportunities, in part as supported by the Department of Canadian Heritage.

That leads to a very important argument to maintain the current foreign investment policy for book publishers. The Department of Canadian Heritage invests approximately \$38 million annually in Canadian-controlled book publishers (that is, those with foreign investment no more than 25% of their shares), and the evaluations of these DCH programs prove that this investment is critical to the profitability of these Canadian-controlled book publishers. Such investment from the Canadian taxpayer in building a Canadian-controlled asset should not be turned over to a foreign investor, except in extraordinary circumstances and only with a net benefit to Canada as outlined in the both the

current foreign investment policy, and as additionally determined by the Department of Canadian Heritage.

These foreign investment restrictions for book publishing are also consistent with similar policies for periodical and magazine publishing.

### *Foreign Investment Restrictions on Book Distribution*

The foreign investment restrictions on book distribution in Canada – including wholesalers, distributors, and retailers – are the same as the restrictions on book publishing, and consistent with a similar policy for film distribution in Canada. To recap, the *Investment Canada Act* requires that foreign investments in book distribution be compatible with Canada’s cultural policies. Foreign investment in new business enterprises is restricted to Canadian-controlled joint ventures, limiting the foreign investment to 49% of all shares. Acquisition of an existing Canadian-controlled business under financial distress, or an existing Canadian business, in excess of 49% of its shares by a non-Canadian is not permitted except if there has been full and fair opportunity for Canadians to purchase; the acquisition is of net benefit to Canada and to the Canadian-controlled sector, and it is subject to one or more commitments. These could include, as outlined in the policy:

- a commitment to the development of Canadian authors, such as undertaking joint ventures with Canadian-controlled publishers which would introduce the partner's Canadian authors to new markets both domestically and abroad;
- a commitment to support the infrastructure of the Canadian book distribution system;
- accessibility of the company's Canadian marketing and distribution infrastructure (or international networks) to interested and compatible Canadian-controlled publishers on a contractual basis; or
- a commitment to education and research through financial and professional assistance to institutions offering programs in publishing studies.

These foreign investment restrictions on book distribution in Canada have contributed to Canadian competitiveness in selling books in Canada. Canadian-controlled companies in book distribution stock predominantly foreign authors. While this is one difference from Canadian-controlled book publishers, it also shows that Canada is one of the most open marketplaces in the world for books.

Would a change in the sectoral investment regime for book distribution improve Canada’s competitiveness? It is possible, since Canadian book publishers currently face a near-monopsony in Indigo Books & Music. A 2007 study commissioned by the Department of Canadian Heritage reports that the market share for Indigo is 44%, or a Herfindahl-Hirschman Index of 1,936, well above the maximum 1,000 threshold for a competitive marketplace, and even above the

1,800 minimum to be considered a highly concentrated marketplace. While Indigo could become a global champion in book retailing, bringing Canadian authors to the world, it is highly unlikely to take on such a corporate strategy due to the presence of Barnes & Noble and Borders in the U.S., Waterstone's and W.H. Smith in the U.K., and Angus & Robertson and Dymocks in Australia. The same Canadian Heritage report outlines that two French-language chains in Quebec, Renaud-Bray and Archambault, also hold a 44% market share. It remains puzzling to us that the Canadian Competition Bureau has both allowed this situation to emerge, and then to persist, and has not mandated a restructuring of the Canadian retail trade for books that provides for a much greater level of competition in this sector for Canadian investors. It seems counterproductive for Canada as a nation to even contemplate addressing this very clearly "made in Canada" problem of competition by substituting a "foreign solution" to it.

When it comes to the wholesale sector of the Canadian book trade, because Canada's population is thinly spread over a large geographical area, no Canadian-owned-and-controlled wholesaler has been able to become as productive or competitive as either Ingram Book Company or Baker & Taylor in the U.S.

However, there is no evidence to suggest that simply removing restrictions on foreign ownership in book distribution, without alternative mechanisms to effectively regulate competition in this sector, would remedy these situations. To the contrary, two competing big-box bookstore chains could easily lead to aggressive measures towards their suppliers, which was what took place in 1998 to 2001 that led to upheaval in the book sector, including the bankruptcies of several companies such as General Publishing, the largest of the Canadian-owned companies at the time, and a distributor for dozens of Canadian-owned-and-controlled companies that had to absorb tens of millions of dollars of lost receivables, reducing their competitiveness in the face of growing foreign competition at home even further.

What is needed most of all in the Canadian retail trade in books is the re-growth of the independent book retailers, providing a greater number of local bookselling entrepreneurs that will improve access for the Canadian public to the diverse range of Canadian-authored books available. Since the big-box book retail wars between 1998 and 2001 that caused the demise of mini-chains such as Lichtman's, Edwards, and Duthies, several new mini-chains have emerged, such as McNally Robinson (which also opened a store in New York City, unique among Canadian-controlled booksellers), Book City, and Type Books. This rebuilding trend should be fostered and encouraged by the Canadian Competition Bureau.

If any, what alternative mechanisms could replace foreign investment restrictions? The requirement of a Canadian-based buying office might appear to counter the concern that the potential foreign-controlled book wholesaler or retailer would operate only from a head office located in a major foreign centre, requiring Canadian book publishers to travel abroad to sell titles. However, this

would work only so long as the foreign-controlled company doesn't fetter that Canadian office with a lack of staff (for instance, a Canadian-authored title is 34% more likely to be in stock at amazon.com than it is at amazon.ca, which has only one buyer), extensive restrictions on the budgets or product mix, or the requirement that books need to be sourced through the company's foreign distribution centre (which would require that a Canadian publisher has the means to distribution in that country). Companies such as Random House and Simon & Schuster recently relocated their distribution centres from Canada back into the U.S. The danger from foreign companies acquiring existing Canadian operations could be similar pullbacks. An existing wholesaler like Ingram or Baker & Taylor would not open new warehouses in Canada since both companies have warehouses already close to the border.

Other requirements could include the purchase of books from an agreed percentage of Canadian-owned-and-controlled publishers, or an agreed percentage of Canadian-authored titles in the product mix, in order to ensure a diverse range of titles. After BMBC bought the Canadian-controlled wholesaler John Coutts in 2000 (and recently bought by Ingram in 2006), sales of Canadian-authored titles dropped by more than half. Distributors could be required to contract with an agreed number of Canadian-controlled publishers, since foreign-controlled distributors in Canada only take the Canadian publishers with at least \$1 million in sales as a benchmark. Many smaller publishers depend on such distributors as Georgetown and Fraser Direct, and these companies in turn depend on a number of foreign clients to attain enough critical volume to operate effectively. If these distributors were to lose such clients to a foreign-controlled entry in the distribution sector, Canadian publishers would be left without effective and competitive Canadian distribution alternatives.

However, none of these mechanisms – including the current foreign investment restrictions – will be effective unless we improve the process for determining and enforcing the commitments necessary to provide a net benefit to Canada.

The current definition of “net benefit” used by the Department of Canadian Heritage in reviewing foreign investment has sound examples of commitments to Canada:

- promoting the creation, dissemination and preservation of diverse Canadian content (commitments to the creation, production, distribution, marketing and preservation of Canadian cultural products in Canada, through traditional and new media)
- cultural participation and engagement (commitments to nurturing new Canadian talent, to employment of diverse Canadians, to autonomy for executives of Canadian companies, to learning opportunities for staff, to partnerships/alliances with Canadian companies and/or learning institutions, particularly in relation to enhancing Canadian infrastructure through technology, know-how, e-commerce, training, internships, etc.)

- fostering and strengthening connections among Canadians (commitments to the distribution and marketing of Canadian cultural products, and sponsorship of events and initiatives that showcase Canadian talent and stories)
- active citizenship and civic participation (commitments to providing philanthropic contributions or in-kind gifts to cultural training institutions, studies, and initiatives designed to enhance Canada’s civic life)

These “net benefit to Canada” tests, in order to become effective in fostering the Canadian book trade in such a way as to improve access, by Canadians, to their own books and authors in every sector and at every stage in their lives, need to be procedurally strengthened by the implementation of the following two recommendations:

#### RECOMMENDATION ONE:

In order to determine the value of any commitments made by potential foreign investments under review at Investment Canada, the government needs the input of the industry, and perhaps even more importantly and effectively, the input of the Government of Canada’s own sister-Ministries, Crown Corporations and Regulatory Agencies (such as the DCH; the Canada Council; and the Competition Bureau) that continue to act in an effective public-private sector partnership with Canadian-owned-and-controlled book publishing companies. While individual or corporate public comments cannot be solicited in the Investment Canada review process since confidentiality is required until the acquisition or entry of the prospective foreign investor has been approved, we recommend that the above government agencies, along with the appropriate representatives from the associations of Canadian-owned-and-controlled publishers – the Association of Canadian Publishers and the Association nationale des éditeurs de livres – be actively involved in the confidential review process at Investment Canada in this sector.

#### RECOMMENDATION TWO

Furthermore, it is possible (and it has happened) that “undertakings” and/or commitments made by successful foreign investors in the Canadian book trade as a condition of their allowance to invest in Canada will not be undertaken. Under the current guidelines, if a major undertaking and/or commitment has yet to be fulfilled by the evaluation made 18 months after the implementation of the approval of the investment, the government can only determine a future time for a further follow-up with the investor. Therefore, we also recommend that the guidelines be amended to give the government the ability to place the acquisition or entry under “probation,” so that if major commitments are not underway by the 18-month evaluation, final approval can be denied, or, in the most extreme cases of non-compliance, can be reversed.

These two recommendations are the mechanisms that need to be applied to the current foreign investment restrictions in the book sector. They would allow the

sector to achieve both economic and cultural policy objectives, while also ensuring maximum competitiveness.

A very important thing to note is that this “net benefit to Canada” screening procedure simply assures that the new entrant or acquiring company is going to be an active participant in Canadian cultural enterprise, and not simply a platform for importing foreign cultural product. These are not the kind of restrictions or screening procedures criticized by the Organization for Economic Co-operation and Development (OECD) or global executives, especially now that the United Nations Educational, Scientific and Cultural Organization (UNESCO) protocol on the preservation of cultural diversity in all international trade agreements and investment decisions has been established. A large cultural enterprise, especially in book distribution or retail, has the potential to damage Canada’s long-term competitive and cultural interests if left unregulated and unchecked. But without the implementation of these two recommendations in our cultural industries sector, any other alternative mechanisms to determine the outcome of the “net benefit to Canada” test would be ineffective, and the current sectoral restrictions would be preferable.

In defining book-related enterprises to which ownership restrictions apply, the policy must not be limited to print books, but should extend equally to books in digital format (“e-books”). For all the reasons that Canadians are well served by ensuring that traditional publishing, distribution, and retailing enterprises remain in Canadian hands, it is important that the full supply chain of e-book publishing, distribution and retail be regulated throughout the supply chain in order to ensure the equitable availability of Canadian choices. In terms of e-books themselves, this is best accomplished through the same ownership restrictions which apply to print publishers. As new distribution and retail channels emerge, it is essential that research be undertaken to determine the best means of achieving this end, and that the results of this research are promptly acted upon.

#### *A Final Note*

The rise of the Canadian dollar is having a tremendous impact on the Canadian book sector, as there is a strong push to lower Canadian prices down to the same price as in the U.S. However, labour costs and taxes are lower in the U.S., and there is a larger market and a concomitant beneficial economy of scale, all of which results in generally lower cost of sales for American book publishers than Canadian ones. Other changes within the Canadian book market could augment this negative volatility. As is so often stated, good business depends on stability and predictability. Now is the time for predictability.

We appreciate the opportunity to address the Competition Policy Review Panel on these important matters, and we applaud its efforts to make Canada more competitive and productive.