

DOCUMENTARY  
ORGANIZATION OF CANADA  
DOCUMENTARISTES  
DU CANADA

215 Spadina Avenue  
Suite / Bureau 126  
Toronto, Ontario  
M5T 2C7  
416.599.3844  
1.877.467.4485  
www.docorg.ca

National Board of Directors

Michael McNamara - Chair

Betsy Carson

Michaelin McDermott

Tina Hahn

Chuck Lapp

John Christou

Kirwan Cox

Linda Desormeaux

Jeremy Edwards

Gita Hosek

Ava Karvonen

Nigel Markham

Michael McMahon

Andrea Nemtin

Sheila Petzold

Peter Wintonick

Merit Jensen Carr

Alan Goldman

Rosie Dransfeld

October 1, 2008

Mr. Pierre Mercier, Manager  
Canada Revenue Agency  
Film Advisory Services  
112 Kent Street, Place de Ville  
Tower B, 19th Floor  
Ottawa, Ontario K1A 0L5

Dear Mr. Mercier,

We welcome and appreciate the opportunity to respond to Canada Revenue Agency's (CRA) Draft Guidelines for determining the reasonableness of producer fees for the purposes of the provincial and federal film and video tax credit programs.

THE DOCUMENTARY ORGANIZATION OF CANADA, l'association des DOCUMENTARISTES DU CANADA (DOC) is a national non-profit bilingual professional arts association of independent documentary producers, directors, craftspeople and service providers. It was founded in 1983 and now has over 800 members working in both official languages in all provinces and territories in Canada. With the addition this year of a Chapter in Alberta, we are now organized into eight Local Chapters in British-Columbia, Alberta Winnipeg, Toronto, Ottawa-Gatineau, Québec, Atlantic and Newfoundland and Labrador.

The members of our industry are deeply concerned by the issues raised in CRA's Draft Guidelines and especially by three key points: retroactive application of these Draft Guidelines by CRA auditors in the field, placing a cap on producers fees that are counted as eligible labor towards the tax credit and the definitions of which expenses should be included within the producer fee cap. These changes to long-standing administrative practices has resulted in undue financial hardship and instability throughout the documentary industry.

### The Documentary Reality

Documentaries are hard to make, take years to complete, are often produced with shoestring budgets, and are driven by the passion of the producer who is also at times, the director, the grip, the bookkeeper and everything else in between. DOC would like to stress the significant difference that exists between a big budget dramatic feature film and a small budget documentary. DOC would further like to stress that CRA's rules and their application need to take these differences into account when considering appropriate guidelines for the administration of the Federal Tax Credit Program.

In 2007, DOC published "Getting Real, Volume 3, 2007" ([http://www.docorg.ca/pdf/Getting\\_Real\\_III\\_b.pdf](http://www.docorg.ca/pdf/Getting_Real_III_b.pdf)), an economic profile of Canadian documentary production. Our research showed that in 2005-6, the average production budget of a one-off documentary produced in English was \$419 000. In that same year, Federal tax credits on average accounted for 10% of the financing structure for those one-off documentaries. Most documentaries fall into this low budget category. Federal Tax Credits play a crucial part in the financial structure of these films. If introduced, any small measure of uncertainty related to the amount received in tax credits would place an enormous and disproportionate burden on documentary filmmakers, not to mention the financial burden placed on productions whose tax credits are reduced due to the newly proposed decrease in federal tax credits.

In order to determine the exact impact of the new guidelines on Tax Credits received by documentary producers, we asked CMA Sherrill Sirrs, who is a production accountant based in BC, to review previous projects and determine what impact, if any, the changes would have on tax credits. This is what she determined:

"Twenty completed Canadian content shows were reviewed to see what affect CRA's new draft regulations would have on the tax credits. All twenty had producer fees at the standard percentage of B+C. The following results are:

- 7/20 or 35% would not have any adjustment in the final tax credit calculation, as the sum of the other eligible labour still exceeded the caps involved in calculating the tax credits.
- 13/20 or 65% had a negative impact on the production with the combined reduction in tax credits (both BC and Federal combined) ranging for 0.18% to 23.34% with an average loss of 10.13% of the total tax credits.
- The shows with smaller budgets tend to be hurt the most and in the shows that were under \$300,000 total budget would likely not have been produced as they were as those are the shows that seemed to have put all their tax credits in the financing plan.
- The shows with the smaller budgets also tended to be newer producers in the industry without access to multiple other sources of financing. This draft guideline may permanently harm the industry as it would be an increased deterrent for young film makers to develop their craft."

In short, the resulting information demonstrates that the CRA's proposed new guidelines will adversely affect documentary production and documentary

producers in Canada, especially those productions working with the narrowest profit margins and the highest level of risk; productions frequently produced by emerging producers who are least able to absorb such losses.

### **Industry Consensus**

We have reviewed the response by the Canadian Film and Television Production Association (CFTPA) to CRA's Draft Guidelines and agree with their position. We wish to draw attention to the following comments and recommendations from their submission that we are in full agreement with:

- 1) The Draft Guidelines, in their current proposed form, unduly attempt to give priority to consistency over fairness, without providing producers and stakeholders with sufficient certainty that the full amount of the expected Film Tax Credit will be received in order to complete the funding of a production, this is currently creating severe financial hardship for producers. It is jeopardizing the completion of existing projects, and is crippling the ability to finance future projects because financing institutions are reluctant to interim finance to the normal 90% value of the tax credit due to the uncertainty that these proposed guidelines have created.
- 2) Following consultation with the industry, an implementation date must be provided in order to permit a smooth transition for our members when any new guidelines (when and as finalized) are adopted by the CRA.
- 3) Reasonableness: The usefulness of the vetting process of a production budget all along the funding chain by various arm's length stakeholders should not be discounted when determining whether an expenditure is "reasonably attributable" to the production and is "reasonable in the circumstances". Guidelines that fail to recognize this reality will destabilize the funding system of Canadian productions by breeding unpredictability and uncertainty. The Canadian film and television system's funding process already includes a built-in process for ensuring that producer fees are reasonable.
- 4) Industry standards: when determining industry standards, the CRA should look at all practices developed by the film industry as a whole, rather than simply applying the most conservative of those practices. Third party approvals (such as broadcasters or private investors) should be regarded with relevance when determining "industry standards".
- 5) Big budget productions: Since the Draft Guidelines are meant to ensure that the concept of reasonableness is applied in a consistent manner, this consistency should apply to all productions, unless the facts of a particular case

require an alternative position. Otherwise, producers will not be able to establish their financing structure with the certainty required to make a “big budget production”.

6) Low budget productions: It is imperative that a higher threshold be maintained for “low budget productions” to reflect market realities.

7) Inclusion: the definition of “producer” found in Income Tax Regulation 1106(1) is much more appropriate under the circumstances and the Draft Guidelines include an overly broad approach to the definition of “producer”. The only individuals considered as producers by this policy should be those who have a controlling interest in the development, financing, production and subsequent exploitation and revenue management of the production: this is best defined as those parties who have copyright ownership in the production and whose fees and overhead are at risk either through investment, deferral, or participation in overages. Removal of all third parties from the cap will improve stability and internal strength of production companies.

8) Transitional measures: prior to the publication and application of new guidelines, transitional measures must be implemented for projects which have commenced or completed production; specifically, projects for which the producer has applied for Part A certification. It would be unfair to introduce the Draft Guidelines without any transitional measures to protect completed films or films that are currently in production. The courts have found on a number of occasions that the government must not give retroactive effect to a change of administrative policy. Furthermore, draft policies that have already been applied should be reversed on projects, as they were not in effect at the time of undertaking the production.

9) Consistency and predictability: It would be inherently unfair if the “rules of the game” were changed after producers have prepared their production budgets, arranged financing, made business decisions and planned their affairs. Canadian courts have held that an organization exercising administrative powers (such as the CRA) has a duty to act fairly when dealing with persons subject to its administration (such as taxpayers). A system can only be fair if it is consistently applied, without any retroactive amendment. Consequently, the Draft Guidelines should only apply to productions in respect of which Part A certification has not been requested from the Canadian Audio Visual Certification Office (“CAVCO”) prior to the publication of the Draft Guidelines.

### **Impact on the documentary production industry**

We are deeply concerned that CRA has applied this draft policy before the completion of a full consultation and without proper warning. It is especially

concerning that these Draft Guidelines have been retroactively enforced by CRA auditors through recent field audits of Canadian film and television projects completed as much as two years ago.

The immediate economic impact of this change in practice by CRA auditors to apply a threshold to producer fees of 10% of the B + C budgets has created an unstable and unpredictable business environment for both indigenous and offshore production companies in Canada. There are profound financial implications for our most successful documentary production companies.

Furthermore, the uncertainty created by CRA's application of the proposed guidelines has had a direct impact on the banks' willingness to interim finance the tax credits. Our financial institutions have been hesitant to interim finance as much of the credits as they used to prior to the cap being applied. The ability to interim finance the tax credit is crucial to this industry, as it allows producers to cash flow their productions. Anything that hinders the interim financing process is severely detrimental to the industry.

### **Recommendations specific to the Documentary Industry**

In addition to our support of the CFTPA recommendations, DOC would like to propose 3 recommended amendments to the draft guidelines that are most important to documentary filmmakers.

1) For low budget productions under \$500 000, DOC believes that a threshold of 30% (of B + C) producer fees (and overhead) above the line be allowable as eligible labour as a standard, and allowed by the CRA for the purposes of calculating the tax credit. To evaluate this on a case-by-case basis – as suggested in your draft guidelines would place a level of uncertainty in the financial structure of low budget productions that would add an unacceptable level of uncertainty and pressure on individual producers and productions.

2) The second recommendation we would like to make involves “arm’s length” producer fees. The work by producers who have creative and financial control over a production, who own the copyright and are thus responsible for raising funds, have final creative control and are responsible for budget overages should be the only producer considered in the “above the line” producer fee threshold. This position is distinct from “arm’s length” producers, for example such as executive producers who do not hold a copyright interest in the project, line producers, associate producers or consulting producers, which are positions that should more properly be considered by CRA as below the line labour along the lines of a production manager or production coordinator. DOC recommends that the CRA should allow fees paid to executive producers,

associate producers, line producers, consulting producers and production managers who are properly credited in the production – to be included as eligible labour and that those fees be excluded from the producer fee threshold. If a producer is also a production manager, he/she should have the ability to pay themselves as a production manager and have that amount of money be excluded from the producer fee threshold in the same way as a director, cameraman or editor would be.


3) DOC recommends that the CRA immediately stop the retroactive application of the draft guidelines and that the CRA selects a date on which the new rules will apply as well as a transition period. Any retroactive application of the CRA guidelines jeopardizes the financial structures of many documentary productions, especially lower budget productions and creates a level of uncertainty that will disrupt the ability of companies to obtain interim financing. Choosing a date and having a transition period will ensure a level of continuity and stability.

As such, we believe the Draft Guidelines should not be implemented in their current form. Going forward, any new CRA guidelines should take into account the issues raised above in regards to reasonableness, industry standards, inclusions, transitional measures, consistency and predictability.

Additionally, we strongly recommend that in future CRA conduct a full consultation with industry stakeholders prior to implementing new policies and significant changes to administrative practice.

Thank you very much for taking the time to consider our recommendations. Please do not hesitate to contact us if you have any questions, comments or concerns regarding our submission.

Sincerely,

A handwritten signature in black ink, consisting of a horizontal line followed by a stylized, cursive name that appears to be 'John Christou'.

John Christou  
Advocacy Chair