Brief to the Standing Committee on Banking, Trade & Commerce

SUBMISSION OF THE WRITERS' UNION OF CANADA ON REVISIONS OF THE BANKRUPTCY AND INSOLVENCY ACT

The Writers' Union of Canada is a national organization representing the interests of Canadian writers, including our membership of over 1400 professional writers of books. We therefore welcome the opportunity to present our views on the revision of the *Bankruptcy and Insolvency Act* (the "BIA" or the "Act") to the Senate Committee on Banking, Trade and Commerce.

A major goal of the Writers' Union is to improve the economic position of writers. The average net professional income of Canadian book and freelance writers in 1998 was approximately $11,480[1] and they are hard hit when their publisher, often their sole or main source of income, becomes insolvent or bankrupt. As well as losing financially, writers may also see their works pass into limbo for a period of time and eventually, often without their consent, pass into the hands of a publisher not chosen by them.

This past year has seen a dramatic disruption in the book industry, notably the collapse of General Distribution Services and its fallout effect, on the publishers distributed by it and their authors and on the authors published by Stoddart Publishing (like GDS, owned by General Publishing). In recent years there have been less noticed changes caused by the insolvency of other publishers, including Somerville House, Press Gang and Ragweed, with lost royalties for most and much delayed royalties for a lucky few. Most recently, in January 2003, Stewart House Publishing filed for bankruptcy.

Without the creations of writers there would be no publishing industry. When a publishing company in financial difficulty goes into receivership or becomes bankrupt, writers have no special rights. Legislation that will recognize the critical role played by writers by giving them both preferred and secured creditor status is long overdue - a preference similar to that accorded to employees and security in the form of an author's lien on the publisher's inventory of books written by him or her.

Writers may be able to protect themselves to some extent in the contracts they negotiate, including by granting a licence rather than making a copyright assignment and by clauses providing semi-annual or even quarterly payments rather than annual payment, advances large enough to cover the entire print run, an accounting with payment within 30 or 60 days rather than 90 days or more following the end of the royalty period, rights to purchase copies at a favourable price, a prohibition on assignment of the contract without the author's consent, and reversion of rights in instances of non-payment or the appointment of a receiver or trustee in bankruptcy or liquidation. However, most authors do not have much bargaining power and even those who can protect themselves by such provisions frequently do not understand or anticipate the need for these protections. Moreover, the validity of clauses reverting rights on receivership and bankruptcy is often challenged.[2] Although contractual provisions may cushion the blow somewhat when a publishing house fails, authors are never able to protect themselves from losing accumulated royalties (once any advance has earned out) because they are usually paid only twice and sometimes only once a year. New, effective legislative protections for authors are needed.

OUR PROPOSALS

Preferred creditors. *We submit that authors should be treated as preferred creditors and should be entitled to receive their unpaid royalties pari passu with the unpaid wages of employees.* We submit that a provision to this effect in the BIA should be backed up by a provision in the *Canada Business Corporations Act* (and its provincial counterparts) to make the directors of corporations jointly and severally liable for the royalties of authors. This will make publishers more cautious about using royalties owed to authors for new projects when their future revenues are in doubt.

We further submit that authors, although they do not own the physical copies of their works, should be treated in a manner akin to the treatment of unpaid suppliers to repossess their goods proportional to unpaid amounts. Furthermore, they should have a lien akin to the special right for farmers, fishermen and aquaculturalists. The claim of an unpaid supplier to repossess goods ranks above all other claims (other than a subsequent purchaser for value without

notice).[3] A publisher's "goods" are more than the physical inventory of a work, as they include the author's intellectual property. If that intellectual property has not been fully paid for, the author should have a lien on the physical books to the extent of the accrued royalties or other shortfall in payment. What we are asking for is comparable to the special right of farmers, fishermen and aquaculturists to a charge against the bankrupt's inventory securing unpaid amounts for their products.[4]

Reversion of Rights. *We submit that rights granted to a publisher with respect to both unpublished manuscripts and published books should revert to the author immediately upon bankruptcy, that is, without paying and without waiting.* The trustee in bankruptcy should not be permitted to carry out the contract without the author's consent, as publishing is a creative business and cannot be administered by economists and accountants without risk to the artistic and literary integrity of the books produced. Legal writer and practitioner John McKeown writes:

> In the event that an agreement between an author and publisher is dependent on the reputation of the publisher, or required the publisher to fulfill duties of a personal nature and contained no provision for its assignment, the agreement may be considered to be of a personal nature and terminated by the bankruptcy of the publisher. In such cases, the trustee will have no right to publish the work which was the subject-matter of the agreement.[5]

But in these days of big publishers, how likely is this to be applicable where the author's attachment to the publisher frequently depends on a particular editor rather than the publishing house itself?

Section 83(1) of the BIA provides for reversion of rights in an unpublished work without financial cost to the author if the work is unpublished and no expense has been incurred by the publisher. If expense has been incurred, the author is only entitled to a reversion if he or she pays the trustee an amount to cover those expenses. If the author declines to pay those expenses, the rights will revert only if six months after the date of the bankruptcy the trustee decides not to carry out the contract, by which time a book may be out of date and may have lost value and the author will likely have suffered loss or delay of royalties. In the case of a published book, the author apparently has no entitlement to a reversion of rights whatsoever in any circumstance, though the trustee may not assign the copyright or license the work exception terms that will guarantee the author royalties at the same rate as was payable by the bankrupt publisher.[6] Even if the author is prepared to buy all the copies or if the trustee sells off all of the copies to booksellers or jobbers (rather than to a publisher who commits to producing further copies), the BIA does not specifically require the trustee to reassign the copyright to the author.[7]

No rights assignment as of right by the trustee. The trustee in bankruptcy is permitted to sell off the author's copyright or interest in copyright if assigned to a publisher, on terms that guarantee the author payment of royalties or profit share at a rate no less than what the bankrupt was obligated to pay. *We submit that the trustee should not be permitted to transferor assign the copyright or any interest in it.* Even if the author has assigned copyright to a publisher, the relationship between the writer and the publisher is a personal one, and the writer should be free to make his or her own alternative arrangements for publication on the insolvency or bankruptcy of his or her chosen publisher - in effect the right to choose not to be published by a receiver or trustee in bankruptcy or by another publisher to whom the receiver or trustee might assign the copyright or interest in copyright.[8]

As the law now stands, if the trustee in bankruptcy assigns any rights under section 84, subject to 83(2)(b, to a person who reassigns them to another person, the writer may be even more out of luck. He or she may be unable to enforce his or her "entitlement" to royalties against the purchaser of the rights even if the purchaser knows the terms of the original contract with the writer![9] This is clearly a risk to which the writer should not be exposed. *We submit that any purchaser (if assignment of the copyright continues to be permitted) should be required to give a written guarantee directly to the author to ensure that the royalty terms and other contractual terms with the bankrupt will be honoured and that the copyright or contract cannot be assigned again without a similar commitment directly to the author from <u>any subsequent</u> purchaser.*

First right to acquire inventory. *We submit that writers should have the right to purchase immediately at the audited depreciated inventory cost any or all the inventory of the books they have written. Subsequent to this, they should have the right to purchase at the same price the receiver or trustee is willing to accept from any other person.*

The right to purchase at a reduced price is a standard provision of most but not all publishing contracts. There was unfortunately no such clause in Stoddart Publishing's standard contract with the result that few authors were able to afford copies at the price demanded first by the receiver and subsequently by the liquidator.

It is extremely important for a writer to be able to control the inventory of his or her book, as it may be impossible to find a new publisher if that publisher is going to face competition from books sold by a receiver or trustee, through regular retail outlets or otherwise. Very often such sales are at "remainder" or bargain prices, and if sold below the manufactured cost of the book to a remainder house or book jobber, there would often be no royalties payable to the author. The books would turn up on bookstore discount tables and likely kill the market for a new edition from which the writer might benefit.

If the trustee intends to pulp books because there is no market for them, we submit that the author should be entitled to obtain them for the cost of shipping.

Section 83(3) of the BIA requires the trustee in bankruptcy to offer the author the right to purchase the manufactured or marketable copies of the book on such terms and conditions as the trustee may deem fair and proper before selling them or authorizing their sale to anyone else. This has been interpreted as requiring the author to purchase all of his or her books. *We submit that the author should be able to purchase some of the inventory - he or she may not be able to afford all of it - and that the price should be specified to be no more than the price which the trustee is willing to accept from any other purchaser.*

We further submit that the purchase price of books sold to the author should be reduced by the amount of the unpaid royalties and that the author should have the first right to purchase his or her books at a reasonable price no more than what they may be offered for sale to anyone else. Even if there is no prospect of a new edition and no need to control the market for the book, writers often wish to purchase their books and are frequently successful in selling their own work long after bookstores have lost interest other than as a remainder at slashed prices.

Books as security for royalty payments. *We submit that writers should be secured creditors with respect to their unpaid, accrued royalties in a receivership or bankruptcy. Their security should be the inventory of their own books with respect to which they should have priority overall other preferred and secured creditors including employees and financial institutions.*

Where the author chooses to acquire all or some of the copies himself or herself, the author should be liable only for the purchase price in excess of the unpaid royalties; if less, the royalties owing the author would be reduced by the amount attributed to the author's "purchase". If the author chooses not to acquire the inventory of his or her book, the author should be entitled to receive the revenues from its sale to the extent of his or her unpaid royalties. Sale of bound copies or sheets remaining in inventory at the time of the receivership or bankruptcy should not only guarantee the author the royalties on those copies (as it does now under the BIA for sales marketed by the trustee in bankruptcy), but also all revenues from any such sales by the trustee or collected by the trustee until such time as he or she has received all royalties owing. This would amount to an author's lien on bound copies and printed sheets of his or her own work.

In practice this amounts to giving the writer the option of taking books in lieu of royalties. It doesn't put bread on the table or pay the rent, but it is better than nothing, which is the author's usual fate in a receivership or bankruptcy.

If all copies of the writer's book are not acquired by him or her, either in lieu of royalties or on payment of a reduced price (we have suggested the audited depreciated cost), we submit that there should be a legal obligation on the purchaser of books to pay a royalty no less than the royalty stipulated in the agreement with the bankrupt publisher. Last year the receiver manager at GDS, prior to its bankruptcy, sold all the inventory of Stoddart Kids to Fitzhenry & Whiteside, a publisher who also offered to buy the Stoddart Kids publishing contracts - a purchase that was subject to author consents. The acquiring publisher offered to pay royalties on its sales of this inventory, but only to those authors who consented to the purchase of their contracts, and not to those who did not give their consent, even though the authors' books were likely to be sold to bookstores at normal prices. Although the purchaser was legally entitled to do as it did, the few who refused to consent perceived this as unfair. We agree.

Back royalties. *We submit that a trustee in bankruptcy or receiver who decides to carry on selling an author's books should be required to pay that author royalties on previously sold books for which the trustee collects payment, as well as royalties on copies actually sold by the trustee or receiver.* Section 83(2) (a) of the Act provides only for royalties on sales by the trustee in bankruptcy. In other words, the author is not entitled to receive royalties on sales made by the publisher or a receiver prior to the appointment of the trustee, even though these royalties, by their very nature, amount to a modest percentage of the sums collected by the trustee for such past sales.

Applicability of the BIA and the Companies' Creditors Arrangement Act ("CCAA"). There is some uncertainty regarding the applicability of the BIA to publishing contracts. The 2nd edition of *Fox on Copyright*. Summarizes the law as follows:

> In the case of royalty agreements, where the publisher is under obligation to pay royalties to the author, but the copyright remains vested in the author, and the publisher goes into bankruptcy, such an agreement is terminated by the bankruptcy of the publisher and the trustee in bankruptcy is not permitted to continue the publication of the work even on terms of continuing the royalty to the author. In such case, however the trustee will have the right to dispose of stock in hand.[10]

Sections 83 and 83(2)(b) and (c) of the Act deal with the author's reversionary rights and the trustee's rights to carry out the contract or to assign copyright. These provisions are applicable when an author has assigned the "copyright or any interest in a copyright in whole or part" to a publisher going into bankruptcy, though it is sometimes unclear in law whether a publishing agreement is a partial assignment of copyright or a licensing agreement under which the author retains the copyright. In other instances, in the practical world, trustees may dispute whether an exclusive licence conveys such an "interest in a copyright" as may be properly regarded as an assignment for the purpose of the BIA, although clearly not an assignment of copyright under the regime provided by the *Copyright Act*.

Section 83(2) of the Act provides that "the trustee is entitled to sell, or authorize the sale or reproduction of, any copies of the published work" under conditions including payment of royalties to the author. This is an important clause because it guarantees the author royalties from sales under the auspices of the trustee and it should apply to the disposition of all books owned by the bankrupt publisher, whether published under licensing agreements or assignments of copyright. However, despite the language of this provision, where rights have reverted to the author because the agreement is a licence, the trustee can have no right to authorize the reprinting of a book or other reproduction of the work. This is, to say the least, confusing.

Inapplicability of the BIA may be to an author's advantage or disadvantage depending on the circumstances (e.g. published or unpublished, treatment of inventory etc.). If applicable, it may prompt a quick release of the author's rights or it may put them into limbo for a time or for all time. In addition to the confusion with respect to the application of section 83, the Act also provides that where a notice of intention to file a proposal or a proposal has been filed in respect of an insolvent person, no person can terminate or amend an agreement with the insolvent person for this reason or because the person is insolvent.[11] Court orders under the BIA and the CCAA sometimes also contain prohibitions intended to prevent any persons including authors from exercising their rights as a result of any default by the debtor.

Many, if not most, trade book contracts are licences for publication rather than copyright assignments, and authors who have only licensed rights have the advantage of a rights reversion even if trustees are often reluctant to provide any acknowledgment of this. However a writer who has licensed rather than assigned rights may lose other benefits the BIA may bring, for example, the right to acquire illustrations or other product of any expenses incurred by the publisher on payment of those expenses. Whether or not the BIA is applicable, most authors will lose royalties and all will be caught up in their publisher's bankruptcy if there is remaining inventory and the trustee has the right to sell the copies of their books.

The CCAA is more often applicable than the BIA and it contains no special provisions to protect authors. We intend our recommendations for protection for authors to have application to the CCAA as well as to the BIA.

CONCLUSION

As discussed above, the existing law - both legislation and case law - is confused and confusing and does little to protect writers, who are currently entirely without preference or security and are unable to protect themselves adequately by contract or to afford to litigate against a trustee or receiver who disputes what rights they do have. The CCAA makes no mention of copyright or books and the BIA seldom applies. But if and when it does, frequently the limited protection it provides for writers may be of diminishing or no use, because of delay or sometimes because a receiver or the trustee in bankruptcy may already have assigned rights and sold the inventory, short circuiting the statutory reversion of rights, depriving the author of possible revenues from sales, and interfering with the author's future opportunities for republication.

We call on the Government to make changes to legislation that will ensure fair treatment for authors in publishers'

insolvencies.

ALL OF WHICH IS RESPECTFULLY SUBMITTED
BY THE WRITERS' UNION OF CANADA by its counsel
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[1] According to a survey by *Quill and Quire,* September 1999.
[2] In an Ontario Superior Court of Justice case involving copyright in songs that had been assigned to a bankrupt company, the judge decided that clauses providing for termination on bankruptcy or insolvency and prohibiting assignments without the author's consent were unenforceable against the trustee (although on the former point he heard no submissions to the contrary): *Re Song Corp.* [2002] O.J. No.13, Bankruptcy Court File No. 31-388643.
[3] BIA, section 81.1
[4] BIA, section 81.2
[5] John S. McKeown, *FOX Canadian Law of Copyright*, 3rd edition (Carswell, Toronto, 2000), page 388.
[6] BIA, section 83(2)(b)
[7] It is unclear what happens if the trustee does not reassign the copyright to the author. Arguably, paragraph 83(1)(c) applies to published works on the market (as well as to unpublished works) if the trustee has not assigned or licensed the author's rights.
[8] *Re Song Corp.*, referred to above, also held that the trustee was entitled to assign the copyright regardless of whether the agreements were personal service contracts.
[9] Lazar Sarna, *Authors and Publishers,* 2nd edition (Butterworths, Toronto and Vancouver, 1987), page 38.
[10] Harold G. Fox, *The Canadian Law of Copyright,* 2nd edition (Carswell, Toronto, 1967), page 566.
[11] BIA, section 65.1.