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37 CFR Parts 201 and 210

Mechanical and Digital Phonorecord Delivery Compulsory License; Final Rule

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U.S. Copyright Office

37 CFR Parts 201 and 210

[Docket No. 2012–7]

Mechanical and Digital Phonorecord Delivery Compulsory License

AGENCY: U.S. Copyright Office, Library of Congress.

ACTION: Final rule.

SUMMARY: The United States Copyright Office is issuing a final rule to implement section 115 of the Copyright Act of 1976. Section 115 establishes a compulsory license for the making and distribution of phonorecords of nondramatic musical works. Section 115, in turn, requires the Register of Copyrights to prescribe by regulation the procedures for the monthly payment of royalties and preparation and service of monthly and annual statements of account by licensees. This final rule updates the existing payment and statement-of-account regulations in response to legal and marketplace developments, including the Copyright Royalty Board's adoption of newer percentage-of-revenue royalty rate structures for certain digital music services, and changes in accounting and industry practice in the years since the rules were last substantially amended.

DATES: *Effective Date:* November 17, 2014.

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SUPPLEMENTARY INFORMATION:

I. Background

The Copyright Act gives owners of musical works the exclusive right to make and distribute phonorecords of those works (*i.e.,* copies in which the work is embodied, such as CDs or digital files). 17 U.S.C. 106(1), (3). This right (often referred to as the ''mechanical'' right) is subject to a compulsory license under Section 115 of the Act. 17 U.S.C. 115. Under that provision—instituted by Congress over a century ago with the passage of the 1909 Copyright Act—once a phonorecord of a musical work has been distributed to the public in the United States under the authority of the copyright owner, any person can obtain a license to make and distribute phonorecords of that work. *Id.* In 1995, Congress confirmed that a copyright owner's exclusive right to reproduce and distribute phonorecords of a musical work, and the Section 115 license, extend to the making of ''digital phonorecord deliveries'' (''DPDs''). *See* Digital Performance Right in Sound Recordings Act of 1995 (''DPRSRA''), Public Law 104–39, sec. 4, 109 Stat. 336, 344–48 (1995) (codified at 17 U.S.C. 115(c)(3)(A)).

A person wishing to use the compulsory license must comply with several requirements imposed by statute and regulation. For instance, licensees must first file a notice of intention to use the compulsory license. *See* 17 U.S.C. 115(b); 37 CFR 201.18. The statute also requires payment of royalties and compliance with terms established by the Copyright Royalty Board (''CRB'') in periodic ratemaking proceedings. *See* 17 U.S.C. 115(c)(3)(C)–(D). And, as most relevant here, the statute requires licensees to make monthly royalty payments, and provide monthly and annual statements of account, in compliance with regulations issued by the Register of Copyrights. 17 U.S.C. 115(c)(5).[1]

The Copyright Office first promulgated regulations prescribing the procedures for the payment of royalties and the preparation and service of monthly and annual statements of account in 1980; those regulations were codified in section 201.19 of title 37 of the Code of Federal Regulations. *See* 45 FR 79038 (Nov. 28, 1980). In that rulemaking, the Office identified a ''guiding principle'' that is equally applicable today: That the regulations should preserve the compulsory license as ''a workable tool,'' while at the same time ''assuring that copyright owners will receive 'full and prompt payment for all phonorecords made and distributed.' '' *Id.* at 79039 (quoting H.R. Rep. No. 94–1476, at 110 (1976)). The Office accordingly evaluated proposed regulatory features using ''three fundamental criteria.'' *Id.* First, the Office stressed that ''[t]he accounting procedures must not be so complicated as to make use of the compulsory license impractical.'' *Id.* Second, ''[t]he accounting system must insure full payment, but not overpayment.'' *Id.* at 79310. Third, and finally, ''[t]he accounting system must insure prompt payment.'' *Id.*

Although the Office has amended aspects of its payment and statement-of-account regulations from time to time, the regulations have always assumed that the compulsory mechanical license will carry a flat royalty rate per phonorecord made and distributed. That assumption is no longer true. In recent years, the CRB has adopted a ''percentage-of-revenue'' model for calculating royalties for newer digital products like interactive streaming and limited downloads. *See, e.g.,* 78 FR 67938 (Nov. 13, 2013). Under that model, royalty calculations work essentially as follows, with some details omitted. First, an ''all-in royalty'' is defined to be a specified percentage of the service's revenues. Second, royalties that are separately paid to performing rights organizations for the public performance of musical works are subtracted from the all-in royalty. 37 CFR 385.12(b)(1)–(2), 385.22(b)(1)–(2). The resulting figure represents the total royalties that the service must pay to all copyright owners under Section 115, although there are ''floors'' to ensure services make at least a minimum royalty payment. The total payable royalty pool must be further allocated to individual musical works. To do so, the pool is divided by the total number of ''plays'' (*i.e.,* the total number of times the service played any phonorecord of any musical work during the relevant accounting period), and the resulting ''per-play'' royalty rate is multiplied by the number of plays of each individual musical work to obtain a ''per-work'' royalty allocation. 37 CFR 385.12(b)(3), 385.22(b)(3).

After a number of stakeholders expressed concern that the Office's statement-of-account regulations do not account for these newer royalty structures, the Office proposed amendments to those regulations and requested public comment in a notice of proposed rulemaking (''NPRM''). *See* 77 FR 44179 (July 27, 2012). The Office received five initial comments, and eighteen reply comments. In December 2013, the Copyright Office requested additional comments concerning the proposed amendments. 78 FR 78309 (Dec. 26, 2013). The Office received one initial comment, and three reply comments.[2]

[1] Although, the Copyright Royalty Board (''CRB'') has general authority to establish royalty rates and terms for the Section 115 license, *see* 17 U.S.C. 115(c)(3)(C) & (D), the Act also separately gives the Register of Copyrights responsibility for issuing regulations relating to specific aspects of that license, *see id.* 115(b)(1) & (c)(4)–(5). *See generally* 73 FR 48396 (Aug. 19, 2008) (addressing division of authority between the Copyright Royalty Judges and the Register of Copyrights under the Section 115 license).

[2] All comments received in relation to this rulemaking are available on the Copyright Office Web site at *http://www.copyright.gov/docs/docket2012-7/*.

The Office received a particularly significant set of comments from a group representing both copyright owners and compulsory licensees. That group, referred to herein as the ''Joint Commenters,'' consisted of the Digital Media Association (''DiMA''), the National Music Publishers' Association, Inc. (''NMPA''), the Recording Industry Association of America, Inc. (''RIAA''), the Harry Fox Agency, Inc. (''HFA''), and Music Reports, Inc. (''Music Reports''). The Joint Commenters reached agreement on a broad range of modifications to the proposed rule, which were reflected in a set of proposed regulations they submitted along with their initial set of comments. *See* Joint Commenters, Initial Comments Submitted in Response to U.S. Copyright Office's July 27, 2012 Notice of Proposed Rulemaking at 2–3, exh. A (Oct. 25, 2012) (''Joint Commenters Initial Comments''). After carefully evaluating the Joint Commenters' proposal against the goals outlined above, the Office has adopted many elements of that proposal as part of the final rule. At the same time, our evaluation and consideration of the comments has led us to conclude that some aspects of the Joint Commenters' proposal would be contrary to the goal of providing a workable means of licensing mechanical rights for musical works.

II. Discussion

Section 115(c)(5) of the Copyright Act directs the Register of Copyrights to issue regulations governing monthly payments and monthly and annual statements of account for the compulsory mechanical license for nondramatic musical works. Specifically, that provision states: ''Royalty payments shall be made on or before the twentieth day of each month and shall include all royalties for the month next preceding. Each monthly payment shall be made under oath and shall comply with requirements that the Register of Copyrights shall prescribe by regulation. The Register shall also prescribe regulations under which detailed cumulative annual statements of account, certified by a certified public accountant, shall be filed for every compulsory license under this section. The regulations covering both the monthly and the annual statements of account shall prescribe the form, content, and manner of certification with respect to the number of records made and the number of records distributed.'' 17 U.S.C. 115(c)(5). As the legislative history makes clear, the goal of this provision is to ensure ''that copyright owners . . . receive full and prompt payment for all phonorecords made and distributed'' and to ''increase the protection of copyright proprietors against economic harm from companies which might refuse or fail to pay their just obligations.'' H.R. Rep. No. 94–1476, at 110–11.

The final rule fulfills these directives by providing new payment and statement-of-account regulations for services subject to a percentage-of-revenue royalty rate, referred to here as ''percentage-rate usages.'' *See* 37 CFR part 385, subparts B & C. For such usages, the revised regulations largely incorporate by reference the rate calculation methodology established by the CRB. In addition, the final rule adopts regulations for services subject to cents-per-phonorecord rates (*i.e.,* physical phonorecord deliveries, permanent downloads, and ringtones, *see* 37 CFR part 385, subpart A, referred to here as ''cents-rate usages'') that closely mirror existing requirements, which were designed with cents-rate usages in mind. The final rule also makes other technical and organizational changes, some of which reflect developments in accounting and industry practice in the years since the rules were last substantially amended. Overall, the final rule is designed to be flexible, so that as the CRB makes future amendments to the rates and terms under Section 115, there will be limited need to amend these regulations.

The following sections highlight the major features of the final rule, including areas that garnered public comment or where the final rule substantially departed from the proposed rule.

A. Organizational and Technical Changes

1. Overall Structure of the Rule

The proposed rule contained two separate subparts within part 210 in title 37 of the Code of Federal Regulations. Proposed subpart B incorporated the existing regulations in section 201.19 with only minor amendments, and was designed to apply to cents-rate usages, while proposed subpart C was mostly new, and was designed to apply to percentage-rate usages. The Joint Commenters disagreed with this approach, and proposed merging subparts B and C of the proposed rule. They explained that the proposed rule was unnecessarily repetitive, and that its structure suggested that licensees operating services with different rate structures (*e.g.,* a licensee that offers a download service and an interactive streaming service) would have to provide separate statements of account for each kind of service. *See* Joint Commenters Initial Comments at 3–5. No other commenter opposed the Joint Commenters' proposal.

The Office agrees with the Joint Commenters' approach. Accordingly, the final rule adds only a single subpart—subpart B. Within that subpart, the provisions governing monthly and annual statements of account (sections 210.16 and 210.17, respectively) each have separate paragraphs governing cents-rate and percentage-rate usages.

2. GAAP Accounting Rules

Several provisions of the rule require the application of Generally Accepted Accounting Principles (''GAAP''). In the NPRM, the Office questioned whether GAAP supplied the appropriate accounting methodology. 77 FR at 44181. In the time since the Office issued the NPRM, the CRB has affirmed the temporary reliance on GAAP in the rate-calculation context and included language in its rules that contemplates the United States' eventual migration from GAAP standards to International Financial Reporting Standards (''IFRS''). *See* 37 CFR 385.11.[3] To maintain consistency between the terms adopted by the CRB and these regulations, the final rule includes a treatment of the term GAAP that parallels that in the CRB rules.

3. Defining When Phonorecords Are ''Distributed''

The final rule makes a purely organizational change that consolidates the provisions describing when phonorecords are considered ''distributed'' within the meaning of Section 115. Section 115 provides that royalties are payable ''for every phonorecord made and distributed.'' 17 U.S.C. 115(c)(2). It also provides that ''a phonorecord is considered 'distributed' if the person exercising the compulsory license has voluntarily and permanently parted with its possession.'' *Id.* The exiting statement-of-account regulations implemented these statutory provisions in two different places. First, the regulatory definition of the term ''voluntarily distributed'' generally addressed the circumstances in which *physical* phonorecords would be deemed ''distributed.'' *See* 37 CFR

[3] The Joint Commenters note that the Securities Exchange Commission (''SEC'') has long been exploring a move towards incorporating IFRS into the United States' financial reporting system. Joint Commenters Initial Comments at 9 (citing *SEC, Work Plan for the Consideration of Incorporating International Financial Reporting Standards into the Financial Reporting System for U.S. Issuers* (2012), *available at http://www.sec.gov/spotlight/globalaccountingstandards/ifrs-work-plan-final-report.pdf*).

201.19(a)(8). Second, the regulatory definition of the term ''digital phonorecord deliveries'' described the circumstances in which DPDs would be considered distributed. *See* 37 CFR 201.19(a)(7).

The final rule consolidates the provisions describing when physical and digital phonorecords are to be considered distributed under the rule's definition of the term ''distributed'' in the new section 210.12(g). No substantive effect is intended by this change. In addition, to better reflect the language used in the statute, the term ''distributed'' replaces the term ''voluntarily distributed'' throughout the final rule. *See* 17 U.S.C. 115(c)(2). Again, no substantive effect is intended, including with respect to the provisions governing involuntary relinquishment.

4. Tax Withholding

Though not addressed in the NPRM, the Joint Commenters raised an issue relating to tax withholding that may be required under federal tax law. They explain that, in certain circumstances, ''a payor may be required to take backup withholding from payments for remittance to the IRS.'' Joint Commenters Initial Comments at 28. They note, however, that the existing regulations do not address how such withholdings are to be reported in the statements of account. *Id.* Accordingly, they have proposed including a rule that requires a licensee to report such withholdings either on the monthly statement or on or with the payment itself. *Id.* No other commenter opposed that proposal.

After examining the issue, the Office agrees that, in the interests of ensuring transparency in the accounting process, statements of account should make clear when money is withheld from royalty payments to copyright owners for remittance to the IRS. The Office has therefore adopted the Joint Commenters' proposal in section 210.16(f)(7) of the final rule.

5. Provisions Relating to Incomplete Transmissions and Retransmissions

The existing rule contains several provisions regarding incomplete transmissions and retransmissions of DPDs. For instance, the rule requires the reporting of DPDs that were ''never delivered due to a failed transmission,'' or were ''digitally retransmitted in order to complete a digital phonorecord delivery.'' 37 CFR 201.19(e)(3)(i)(B). The rule also incorporates incomplete transmissions and retransmissions of DPDs into the calculations of royalty rates. 37 CFR 201.19(e)(4)(ii). The proposed rule carried forward these provisions without alteration.

The Joint Commenters proposed doing away with these provisions. Instead, they recommended that the Office add a new sentence to the definition of ''digital phonorecord delivery'' specifying that a DPD ''does not include a transmission that, as reasonably determined by the distributor, did not result in a specifically identifiable reproduction of the entire product being transmitted, and for which the distributor did not charge, or fully refunded, any monies that would otherwise be due for the relevant transmission.'' Joint Commenters Initial Comments at 29–30.

According to the Joint Commenters, the existing provisions relating to incomplete transmissions and retransmissions are problematic in several respects. For example, they noted that the existing rule defines an ''incomplete transmission'' as one in which the entire sound recording is not transmitted, and maintained that, taken literally, this definition would appear to encompass ringtones. *Id.* at 29. They also asserted that it is technically impossible to individually track all incomplete transmissions and retransmissions, and that even if such information could be comprehensively tracked, the rule would ''require delivery of what would seem to be massive amounts of useless information.'' *Id.* at 30. As a result, according to the Joint Commenters, industry practice has developed such that there is no reporting of incomplete transmissions or retransmissions. *Id.* No other commenter disputed the Joint Commenters' claims or opposed their proposal.

The Office concludes that removing the provisions requiring reporting of incomplete transmissions and retransmissions would further the goal of ensuring that these regulations are not ''so complicated as to make use of the compulsory license impracticable.'' 45 FR at 79039. In particular, given that the Joint Commenters are not aware of any reporting of incomplete transmissions and retransmissions, and given their joint agreement that such reporting is unnecessary, it would seem prudent to ensure that the regulations comport with industry practice. The final rule thus adopts the Joint Commenters' approach of excluding incomplete transmissions from the rule's definition of ''digital phonorecord deliveries.''

6. Reconciling Overpayments in the Annual Statement

The proposed rule, like the existing rule, provided that where an annual statement of account shows an underpayment by the statutory licensee, the licensee must deliver the amount of the underpayment together with the annual statement of account. *See* 77 FR at 44192; 37 CFR 201.19(f)(7)(ii). The existing rule, however, did not include any provision addressing how *overpayments* by the statutory licensee are to be handled. To address this shortcoming, the Joint Commenters proposed that the final rule specify that, where an overpayment exists, such amount ''shall be available to the compulsory licensee as a credit.'' *See* Joint Commenters Initial Comments, exh. A, at A–21. No other commenter objected to that proposal.

The Office has adopted the Joint Commenters' proposal in the final rule. The Office stresses, however, that the manner in which any such credit is taken must be consistent with GAAP.

B. Issues Presented Involving Calculations of Royalties

1. Royalty Calculation Issues in General

The existing statement-of-account regulations set forth in detail the process for calculating royalty payments each month. *See* 37 CFR 201.19(e)(4). The proposed rule carried forward these provisions for cents-rate usages. *See* 77 FR at 44188. For percentage-rate usages, the proposed rule aimed to comprehensively mirror the rate calculation methodology promulgated by the CRB. *See* 77 FR at 44194.

The proposed rule's approach to calculation of royalties for cents-rate usages was uncontroversial, and the final rule adopts the proposed rule with only minor modifications (including removal of provisions for incomplete transmissions and retransmissions of DPDs, an issue which is addressed above). For percentage-rate usages, however, the Joint Commenters highlighted several instances where the proposed rule was inconsistent with the rates adopted by the CRB, including that the rule appeared to contemplate payment for every phonorecord distributed and a separate calculation of a per-phonorecord payment by offering. Joint Commenters Initial Comments at 5–6. The Joint Commenters explained that ''[u]nder Part 385 Subparts B and C, the number of phonorecords made and distributed is not generally determinative of the rate calculation, and phonorecords of multiple configurations are generally treated together as part of a single rate

calculation.'' *Id.* at 5. The Joint Commenters instead proposed that the statements of account regulations ''take a minimalist approach to incorporating into the accounting regulations details imported from Part 385.'' *Id.* at 6. In particular, they recommended that for percentage-rate royalties the rule simply provide that the amount of the royalty payment shall be calculated as provided in the relevant portions of part 385. *Id.* at B–13 to B–14. No other commenter opposed this proposal.

The Office agrees with the Joint Commenters' critique of the proposed rule, and adopts their proposed solution. Taking a minimalist approach has a distinct advantage: It is likely that the CRB will alter the current rates in future rate periods, and incorporating the rates by reference avoids the need to revisit these rules after every such change. The Office stresses, however, that the final rule requires the licensee to include a detailed and step-by-step accounting of the calculation of royalties, to allow the copyright owner to verify the accuracy of the royalty payment.

2. Accounting for Deduction of Public Performance Royalties

As noted above, the percentage-of-revenue royalty rates established by the CRB allow licensees to deduct royalties due for the public performance of musical works from the amounts owned under the Section 115 license. *See* 37 CFR 385.12(b)(2), 385.22(b)(2). In the NPRM, the Office recognized that the nature of the music licensing marketplace is such that the value of applicable performance royalty rates may be unknown or established on an interim basis at the time statements of account and corresponding royalty payments become due. 77 FR at 44181. To address this scenario, the Office proposed that licensees would be permitted to account for unknown performance royalties by using an established interim royalty rate or, if no interim rate is established, a ''reasonable estimation'' of the expected final rate.[4] In either case, the proposed rule required licensees to file amended annual statements of account and reconcile the actual amounts of royalties owed to copyright owners under the Section 115 license within six months of the establishment of a final performance royalty rate. 77 FR at 44194.

The Joint Commenters agreed that new accounting regulations should permit licensees to calculate unknown performance royalties based on interim or estimated performance rates, with a ''true-up'' occurring once the final rates for a given period have been determined. Joint Commenters Initial Comments at 6. However, they offered two refinements to the Office's proposed approach. First, they suggested that the Office only require licensees to report any amendments based on the final establishment of performance rates on the next regular annual statement of account. *Id.* at 9.[5] The Joint Commenters maintained that the cost of preparing and certifying both an annual statement and an amended annual statement for each copyright owner would be burdensome. *Id.* In addition, they noted that ''where ownership of a work may have changed over the relevant period, the only practicable approach is to make the adjustment between the licensee and the current copyright owner'' in the next regular annual statement of account. *Id.*[6] Second, Joint Commenters suggested that the rules specify that amended statements of account should only be required when performance royalties have been established for ''all works used by the service in an accounting period.'' *Id.* at 7–8. As justification for that refinement, the Joint Commenters noted that the performance royalty deduction under part 385 currently is made at the level of a service offering, not a particular work. *Id.* at 7–8.

After considering the comments, the Office maintains the basic approach set forth in the proposed rule, while making clear that amended annual statements of account will be necessary only when the final performance rates are known for all works used by the service. The Office declines to adopt the Joint Commenters' proposal to permit licensees whose prior annual statements (and corresponding payments) have been rendered inaccurate by a final performance royalty determination to rectify the inaccuracies via the ''single, regular statement of account for the year in which the final [public performance] royalty expense for the offering is paid.'' Joint Commenters Initial Comments at 9. In keeping with our statutory obligation to ensure the filing of detailed, cumulative, certified annual statements of account for each fiscal year, the Office finds it necessary to require licensees to file amended statements for each year in which a licensee's aggregate final public performance royalties were incorrectly reflected in its previously filed annual statements. *See generally* 17 U.S.C. 115(c)(5).

The appropriateness of this result is underscored, not undermined, by the Joint Commenters' observation that there may be changes in musical work ownership after initial annual statements are issued and before the final performance royalties are determined. In particular, the Office questions the assertion that where there has been such a change in ownership, any reconciliation must be made with the *current* copyright owner, rather than the owner of the copyright at the time the original annual statement was issued. The transactions transferring copyright ownership may provide for a different result as a matter of private contract, but absent such an arrangement, any underpayment or overpayment stemming from the reconciliation of final performance royalty payments may properly be attributable to the copyright owner at the time of the relevant use of the statutory license.

Nonetheless, to mitigate the cost of preparing the amended statement of account, the final rule clarifies that, in certifying such an amended statement, the Certified Public Accountant (''CPA'') may limit its examination to the licensee's recalculation of royalties. The accountant need not recertify matters that were already examined and certified in the original annual statement of account.

[4] The proposed rule called for the ''reasonable estimation'' to be made ''in accordance with Generally Accepted Accounting Principles.'' 77 FR at 44194.

[5] The Joint Commenters also recommended that the Office declare it reasonable to ''use the aggregate amount of public performance royalties then sought from the licensee by performing rights licensors'' as a basis for computing the interim or estimated public performance royalty component. Joint Commenters Initial Comments at 7. The Office declines to do so. The Office believes that GAAP will provide adequate standards for the determination of the estimate, and that the use of GAAP should mitigate the concern that licensees will adopt inappropriate estimates.

[6] Gear Publishing Company (''Gear'' or ''Gear Publishing''), the only other party to comment on this issue, suggested that, in the absence of an interim royalty rate, public performance royalty rates should be ''no less than one hundred and thirty five percent (135%) of the previously set rates.'' Gear Publ'g, Initial Comments Submitted in Response to U.S. Copyright Office's July 27, 2012 Notice of Proposed Rulemaking at 3 (Oct. 15, 2012) (''Gear Publ'g Initial Comments''). The Office notes that Gear appears to misapprehend the function of the estimated royalty rates in this context. That estimate would not, as Gear appears to believe, actually *set* the interim royalty rates for public performances of the musical works; those rates are determined under the terms of the consent decrees that govern two performing rights organizations, ASCAP and BMI. *See United States* v. *ASCAP,* 2001–2 Trade Cas. (CCH) ¶ 73,474, 2001 WL 1589999 (S.D.N.Y. June 11, 2001); *United States* v. *Broadcast Music, Inc.,* 1966 Trade Cas. (CCH) ¶ 71,941 (S.D.N.Y. Dec. 29, 1966), *amended by* 1996–1 Trade Cas. (CCH) ¶ 71,378, 1994 WL 901652 (S.D.N.Y. Nov. 18, 1994). Instead, under the current CRB rates, the estimated royalty rate is an accounting method used to offset payments under the Section 115 license until an interim or final performance royalty rate is established.

3. Negative Reserve Balances and DPDs

The accounting requirements in the proposed rule were generally uncontroversial. One area of controversy, however, related to the rule's handling of ''negative reserve balances'' for DPDs. Understanding the concept of a ''negative reserve balance'' requires a brief discussion of the concept of a ''phonorecord reserve.'' Section 115 provides that royalties are payable ''for every phonorecord made and distributed,'' and that ''a phonorecord is considered 'distributed' if the person exercising the compulsory license has voluntarily and *permanently* parted with its possession.'' 17 U.S.C. 115(c)(2) (emphasis added). In enacting that provision, Congress recognized that ''phonorecords are distributed to wholesalers and retailers with the privilege of returning unsold copies for credit or exchange.'' H.R. Rep. No. 94–1476, at 110. Thus, ''the number of recordings that have been 'permanently' distributed will not usually be known until some time—six or seven months on the average—after the initial distribution.'' *Id.* Congress observed that ''it ha[d] become a well-established industry practice, under negotiated licenses, for record companies to maintain reasonable reserves of the mechanical royalties due the copyright owners, against which royalties on the returns can offset.'' *Id.* Congress accordingly instructed the Register of Copyrights to promulgate rules governing the maintenance of such reserves. *Id.; see also* 45 FR at 79038.

Thus, the existing rule allows licensees, when making initial distributions of phonorecords, to withhold mechanical royalties based on the licensee's estimate of the number of phonorecords that will be returned by creating a ''phonorecord reserve.'' 37 CFR 201.19(a)(10). As phonorecords are returned, the phonorecord reserve is reduced, reflecting the fact that the returned phonorecords were not ''permanently distributed.'' *Id.* 201.19(c)(1). A ''negative reserve balance'' occurs when phonorecords have been returned to the licensee in an amount that exceeds the established phonorecord reserves (which can occur when more phonorecords than were expected are returned). *Id.* 201.19(a)(11). When such a negative reserve balance exists, it represents an overpayment from the licensee to the copyright owner. *See* 45 FR at 79043. Thus, a compulsory licensee can claim a credit against that balance for future physical phonorecord distributions, with the negative reserve balance reduced accordingly. 37 CFR 201.19(c)(4).

When the Office issued interim payment and accounting rules for DPDs in 1999, it concluded that there was ''no basis for adopting the concept of 'reserves' to DPDs,'' principally because such DPDs are not typically accompanied by a right of return. *See* 64 FR 41286, 41287 (Jul. 30, 1999). Thus, the existing rule makes clear that record companies cannot establish phonorecord reserves for DPDs. *See* 37 CFR 201.19(a)(9).

Since then, a further dispute has developed: if a record company has a negative reserve balance stemming from returns of physical phonorecords, should it be able to claim a credit against that balance for future DPDs? Or should the licensee be limited to only using future physical phonorecord distributions to offset that negative reserve balance? The NPRM sought comment on that issue. *See* 77 FR at 44181–82. Favoring the ability to claim a credit for DPDs were the RIAA and the American Association of Independent Music (''A2IM''). *See* RIAA, Initial Comments Submitted in Response to U.S. Copyright Office's July 27, 2012 Notice of Proposed Rulemaking 3–11 (Oct. 25, 2012) (''RIAA Initial Comments''); A2IM, Reply Comments Submitted in Response to U.S. Copyright Office's July 27, 2012 Notice of Proposed Rulemaking 2–3 (Dec. 3, 2012) (''A2IM Reply Comments''). Opposing that position were a group comprising the NMPA, HFA, the Songwriters Guild of America (''SGA''), and the Nashville Songwriters Association International (''NSAI'') (hereafter referred to collectively as the ''Joint Publishers and Songwriters'') and Gear Publishing. *See* Joint Publishers and Songwriters, Initial Comments Submitted in Response to U.S. Copyright Office's July 27, 2012 Notice of Proposed Rulemaking 5–7 (Oct. 25, 2012) (''Joint Publishers and Songwriters Initial Comments''); Gear Publ'g Initial Comments at 3.

In considering this issue, the Office is guided by the goals of the accounting regulations, particularly the requirements that ''[t]he accounting system must insure full payment, but not overpayment,'' and that ''[t]he accounting procedures must not be so complicated as to make use of the compulsory license impractical.'' 45 FR at 79039. For the reasons discussed in detail below, the Office concludes that licensees may claim a credit against negative reserve balances for future DPD distributions, but only where the DPDs have the same royalty rate as physical phonorecords (*i.e.,* under the current rates, permanent physical downloads).

a. Whether Negative Reserve Balances Can Be Applied to DPD Distributions

The Joint Publishers and Songwriters suggested that the Office had already addressed this issue in the regulatory amendments adopted in 1999, and determined that negative reserve balances could not be applied to future DPD deliveries. *See* Joint Publishers and Songwriters, Reply Comments Submitted in Response to U.S. Copyright Office's July 27, 2012 Notice of Proposed Rulemaking 10 (Dec. 10, 2012) (''Joint Publishers and Songwriters Reply Comments'') (referencing 64 FR at 41287–89). But, as the RIAA correctly observed, the 1999 interim rulemaking addressed only whether licensees could be permitted to *maintain* phonorecord reserves for DPD distributions. *See* RIAA Initial Comments at 7–8. The Office did not opine on the separate issue of whether negative reserve balances developed as a result of returns of physical product could be applied to future DPD distributions.

The NPRM here raised two questions relevant to that previously unaddressed issue. First, the NPRM asked ''whether there is statutory authority for allowing the application of a credit for negative reserve balances to digital phonorecord deliveries.'' 77 FR at 44182. The Office concludes that there is such authority. The statute broadly delegates to the Register the authority to prescribe regulations for monthly royalty payments and monthly and annual statements of account. *See* 17 U.S.C. 115(c)(2). The commenters have pointed to nothing to suggest Congress wished to constrain that authority with respect to DPDs when enacting the DPRSRA.

Second, the NPRM asked whether ''there are reasons to limit the application of credits for negative reserve balances to physical phonorecords.'' After considering the comments, the Office agrees with the RIAA that there is no sound basis for such a limitation. As the Office has previously explained, a negative reserve balance represents an overpayment from the licensee to the copyright owner. 45 FR at 79043. Thus, permitting licensees to use DPDs to offset negative reserve balances would help satisfy one of Congress's goals in enacting section 115(c)(5): That ''[t]he accounting system . . . insure full payment, but not overpayment.'' 45 FR at 79039.

For their part, the Joint Publishers and Songwriters urged that because ''digital phonorecord deliveries cannot be returned, it would be incongruous to apply the negative reserve balance accounting to DPDs.'' Joint Publishers

and Songwriters Reply Comments at 9. But that observation conflates two separate issues. The fact that DPDs cannot be returned is the reason licensees are not permitted to *develop* reserves for DPDs. *See* 64 FR at 41287. That fact has no bearing on whether a licensee can claim a credit against an existing negative reserve balance for future DPDs.

To be sure, as the Joint Publishers and Songwriters noted, Congress was concerned about ''the possibility that, without proper safeguards, the maintenance of . . . reserves could be manipulated to avoid making payments of the full amounts owing to copyright owners.'' *See* Joint Publishers and Songwriters Reply Comments at 12 (quoting H.R. Rep. No. 45–1476, at 110). But, as the Office explained in its 1980 rulemaking, that concern is principally addressed via ''the statutory requirement for an annual CPA audit, coupled with our regulatory requirements including the application of 'generally accepted accounting principles.' '' 45 FR at 79040.[7]

b. Limitations on Licensees' Ability To Apply Negative Reserve Balances to DPDs

While the Office concludes that licensees may offset negative reserve balances using future DPDs, that conclusion raises a few further questions. First is whether a negative reserve balance must be applied to future DPD distributions of the same musical work, or whether it can be applied at the statement level to other works owned by the same person. *See* 77 FR at 44182. The Office agrees with the Joint Publishers and Songwriters that the negative reserve balance should be applied at the work level, not the statement level.

As the RIAA noted, the language of the existing rule as codified in the Code of Federal Regulations is somewhat ambiguous on the issue. RIAA Initial Comments at 11–12. But when the Office first promulgating that rule in 1980, it unequivocally explained in the rule's preamble that the negative reserve balance is ''to be reduced by applying it against shipments *of the same recording under the same compulsory license.''* 45 FR at 79043 (emphasis added).

The Office sees no basis for reconsidering that determination. The Joint Publishers and Songwriters and Gear Publishing convincingly described the practical difficulties that would result from the application of negative reserve balances at the statement level. *See* Joint Publishers and Songwriters Reply Comments at 14–15; Gear Publ'g Initial Comments at 5–6. Among other things, ''[c]ompulsory accountings are generally not made and delivered to the author, but rather to a publisher or administrator.'' Gear Publ'g Initial Comments at 6. Thus, ''[i]f a compulsory licensee was permitted to cross negative royalty balances between two or more songs then the writer of one work might be unfairly punished by the application of a negative reserve balance against another author's work.'' *Id.* Indeed, the RIAA acknowledged this problem, and proposed a solution that would create obvious administrative difficulties.[8] Accordingly, to confirm that a negative reserve balance may only be applied at the work level, the Office has amended the regulations to specifically note that phonorecord reserves and negative reserve balances may only be comprised of the number of phonorecords ''made under a particular compulsory license.''

The second question is how the negative reserve balance, which is expressed in units of physical phonorecords, should be applied to DPD distributions, which are not necessarily tracked on the same basis. Balancing the competing principles discussed above, the Office concludes that the negative reserve balance should be applied to those DPDs that have the same statutory royalty *structure* and same statutory royalty *rate* as the physical product—*i.e.,* under current rates, permanent digital downloads. *See* 37 CFR 385.3 (establishing identical structure and rate for physical phonorecord deliveries and permanent digital downloads). As the RIAA noted, ''applying negative reserve balances to standalone sales of permanent digital downloads is trivial, because the statutory royalty rate is the same for downloads as for physical products.'' RIAA Initial Comments at 9. Moreover, the RIAA acknowledged that limiting the application of negative reserve balances to permanent digital downloads ''takes care of the vast majority of relevant commerce, because the overwhelming proportion of DPDs accounted for by the record companies that potentially have negative reserve balances are permanent digital downloads.'' *Id.*

The RIAA nevertheless asked us to go further, and allow record companies to apply negative reserve balances to DPDs that have a different cents rate, like ringtones, (*see* 37 CFR 385.3(b) (setting rate at 24 cents per ringtone delivery)), and DPDs that have rates that are calculated on a percentage-of-revenue basis, like interactive streams (*see* 37 CFR 385.12, 385.22). The Office declines to do so because that would run afoul of the principle that ''[t]he accounting procedures must not be so complicated as to make use of the compulsory license impractical.'' 45 FR at 79039. The complication arises because phonorecord reserves (and thus, negative reserve balances) ''have historically been measured in product units'' of physical product, not in dollars and cents. RIAA Initial Comments at 9.[9] The RIAA's solution for ringtones would be to divide the 24-cent ringtone rate by the base 9.1 cent physical phonorecord delivery rate to achieve a conversion factor, so that a delivery of a ringtone would be ''worth'' approximately 2.6374 physical phonorecord deliveries. *Id.* at 10. But that would result in reserves being expressed as fractions of physical units, which could cause problems when attempting to apply reserves to future physical phonorecord shipments. Moreover, that solution would work only for royalties that are expressed in cents terms; the RIAA offers little guidance on the manner in which credit could be claimed against negative reserves for digital distributions that carry a percentage-of-revenue royalty rate. *Id.* at 11. This would also make the accounting more difficult to understand and less transparent.

The Office notes that this problem might be dealt with more comprehensively by expressing phonorecord reserves in terms of dollars and cents rather than in terms of physical units. But that would require a significant reworking of the existing regulations, including the manner in which royalties are calculated and accounted for. *See generally* 37 CFR 201.19(d)(4)(ii). Notably, no commenter has suggested the Office make such drastic modifications to the rules. Moreover, the benefits of such modifications are uncertain, given the RIAA's acknowledgment that applying the negative reserve balances to permanent digital downloads ''takes

[7] The Joint Publishers and Songwriters claim that allowing licensees to offset the negative reserve balance using DPDs would encourage ''overshipping'' of physical product. Joint Publishers and Songwriters Initial Comments at 6. The Office does not, however, understand how that concern would justify a music publisher's retention of a royalty overpayment.

[8] RIAA Initial Comments at 12–13 (''If the record company applied a negative reserve balance to works by a writer other than the one who received the overpayment, the music publisher would need to debit the account of the writer who received the overpayment and credit the account of the writer whose work had the negative reserve balance applied to it.'').

[9] *See also* 37 CFR 201.19(a)(10) (defining ''phonorecord reserve'' in terms of ''the number of phonorecords''); *see also id.* 201.19(a)(11) (defining ''negative reserve balance'' in terms of ''the aggregate number of phonorecords'').

care of the vast majority of relevant commerce.'' RIAA Initial Comments at 9. Thus, for all of the above reasons, the Office declines to allow licensees to apply their negative reserve balances to DPDs that carry a different royalty structure or rate than the physical product.

Finally, the Joint Publishers and Songwriters noted that, in practice, the rates for permanent digital downloads and physical products may not be the same because of the prevalence of controlled-composition rates for physical distribution, and the limitation on such rates in the DPRSRA. *See* Joint Publishers and Songwriters Initial Comments at 12–14; *see also* 17 U.S.C. 115(c)(3)(E). Accordingly, they are concerned that allowing licensees to offset a negative reserve balance expressed in terms of physical units carrying a lower royalty under such private agreements using digital distributions that may have a higher royalty under the statutory license would give the record companies a windfall. *See* Joint Publishers and Songwriter Initial Comments at 13–14.

That concern, however, is purely the result of terms of private licenses—specifically, the fact that such licenses apparently ''incorporate the regulations attendant to Section 115, including the reserve accounting rules.'' *Id.* at 13. Such private agreements could avoid the problem by instead adopting different reserve accounting rules. To the extent there may be an underpayment of royalties as a result of the terms of private agreements, ''resolution of [that] issue in particular cases is best left to application of general legal principles in the appropriate forum.'' 45 FR at 79041.

4. Degree of Rounding for Decimal Points

In drafting the proposed rule, the Office recognized the need for new regulations that determine the appropriate degree of rounding (in terms of the number of decimal places, based upon a fraction of a dollar rate) when licensees compute percentage-rate royalties associated with limited downloads, interactive streams, and incidental DPDs. 77 FR at 44182. The NPRM solicited comments on the extent to which licensees are to calculate per work royalty allocations. It also requested that commenters address whether a variance can be allowed in the degree of rounding based on the technical capabilities of various accounting systems, or whether reporting to a certain decimal place should be completely uniform. *Id.*

In addressing these issues, the Joint Commenters maintained that rounding does not inherently favor one party over another. Joint Commenters Initial Comments at 10. They suggested that the new regulations require payors to calculate ''actual or constructive per-play allocations (the number that is then multiplied by the number of plays to determine the per-work royalty allocation)'' to at least six decimal places, provided their systems are technologically able to do so. *Id.* They further suggested that the new regulations require payors that are not technically equipped to make a six-decimal place calculation round to four decimal places. *Id.* The Joint Commenters did not view the benefits of the additional precision (rounding to six places as opposed to four) as sufficient to require reengineering of already existing accounting systems. However, they did note that where payors are capable of making a calculation beyond four decimal places, the added precision is desirable.[10] The only additional commenter on this issue, Gear Publishing, asserted that rounding should be limited to three decimal places and that ''rates should never be less than 1/10th of a penny.'' Gear Publ'g Initial Comments at 6–7.

The Office agrees with the general proposition that the benefits and detriments of calculating actual or constructive per-work royalty allocations to six digits rather than four are essentially random, will generally be very small, and do not inherently favor the payee or the payor. As such, the Office has implemented language in the final rule that requires all compulsory licensees to make royalty calculations to at least four decimal places.

Regarding the Joint Commenters' request that the new regulations mandate additional precision based on technical accounting capabilities, the Office declines to include language in the final rule that would create a regulatory distinction between compulsory licensees with accounting systems designed to make royalty calculations to four decimal places and compulsory licensees whose systems are capable of making royalty calculations beyond four decimal places. The Office finds that the degree of reporting from licensee to licensee need not be completely uniform, provided all licensees make royalty calculations to at least four decimal places. Licensees may utilize additional precision beyond four decimal places where desirable, but the final rule does not require that they do so.

C. Issues Presented Involving Method of Payment and Delivery of Royalties

1. Electronic Payment

The existing regulations provide that monthly statements of account shall be ''served on the copyright owner or the agent with authority to receive Monthly Statements of Account on behalf of the copyright owner to whom or which it is directed, together with the total royalty for the month covered by the Monthly Statement, by mail or by reputable courier service. . . .'' 37 CFR 201.19(e)(7)(i).

In the NPRM, the Office proposed maintaining the current default requirement that payment be sent by mail or courier service. 77 FR at 44182. The Office also proposed amending the existing regulations to allow copyright owners and licensees to independently agree to alternative payment methods, including electronic payment. *Id.* Finally, the Office proposed adopting a regulation that echoed the existing requirement that ''when both the Monthly Statement of Account and payment are sent by mail or courier service, they should be sent together,'' but permitted licensees participating in independent agreements that authorize the sending of statements and payment by means other than mail or courier service to send them contemporaneously. *Id.*

The final rule reflects the commenters' general agreement with the Office's proposal to retain service by mail or courier service as the default requirement. Likewise, it reflects the commenters' general support of a rule that provides for independently agreed upon alternative payment methods.

Regarding the timing of service requirements, the final rule deviates from the Office's proposal that when a licensee serves statements and payment via mail or courier service, they must be sent together. The Joint Commenters' explanation of the often-times separate processes for generating paper checks and paper royalty statements has persuaded the Office that it is sometimes impractical for licensees to send statements and payments simultaneously.[11] Thus, the Office has

[10] The Joint Commenters explained: ''[t]he issue is that older royalty accounting systems originally designed primarily for physical configurations may not have been designed to perform royalty calculations to more than four decimal places, while newer systems generally would. As a result, the Joint Commenters understand that many, but not all, payors have the capability to make this calculation to at least six decimal places, and view that degree of precision as desirable where available.'' Joint Commenters Initial Comments at 10.

[11] *See* Joint Commenters Initial Comments at 12 (explaining that ''[p]aper checks sometimes

included language in the final rule that reflects the Joint Commenters' suggestion that payments may be sent together or separately, but if sent separately, the payments must include information reasonably sufficient to allow the payee to match them with corresponding statements. The final rule remains consistent with the existing requirement that both monthly statements of account and payment shall be served on or before the 20th day of the immediately succeeding month.

2. Electronic Statements of Account

The existing regulations require compulsory licensees to serve statements of account via mail or reputable courier service. 37 CFR 201.19(e)(7), (f)(7). At the urging of stakeholders, the NPRM contemplated adopting a rule that would alter the existing regulations by compelling licensees to serve, and copyright owners to accept, statements of account via electronic transmissions. 77 FR at 44182–83. Although the proposed rule did not go so far as to fully require stakeholders to serve and accept electronic statements of account, it did include provisions whereby a copyright owner could notify a licensee of its willingness to accept statements by means of electronic transmission and require licensees whose statements covered more than 50 works to serve them electronically. The proposed rule also included a provision that would permit stakeholders to agree upon a procedure for verification of authority, other than a handwritten signature, when statements of account are served electronically.

a. Electronic Statements in General

Most commenters agreed in principle with the proposed rule's attempt to reconcile the various stakeholder preferences concerning the format and method of delivery for statements of account. In this vein, the Joint Commenters proposed that the Office adopt regulations whereby ''[e]ach payor could in the first instance choose its preferred mode of delivery, but if a payee requests the other approach, that request would be honored within a reasonable grace period.'' Joint Commenters Initial Comments at 13. They further proposed that, to ''minimize disruption,'' the new regulations should only permit a payor to change its elected preference once annually. *Id.* In support of their proposal, the Joint Commenters explained: ''What has happened in practice is that services and agents making large scale use of the compulsory license have defaulted to electronic delivery, but when some payees have requested paper statements, they have provided them. Conversely, record companies have defaulted to paper statements, and still use them for many payees, but deliver statements electronically when requested.'' *Id.* at 12–13.

The final rule takes into account the general agreement among commenters that the new regulations should authorize electronic service of statements of account by adopting provisions that permit copyright owners to elect the format (paper or electronic) in which they receive statements. However, contrary to the Joint Commenters' proposal, the Office declines to authorize licensees to unilaterally elect to serve statements of account electronically. Instead, consistent with Gear Publishing's proposal, the final rule retains its requirement that licensees submit statements of account by mail or reputable courier by default, and provides copyright owners with the option to demand electronic statements. *See* Gear Publ'g Initial Comments at 8–9. The final rule does not restrict the copyright owners' ability to amend their elected service preference. However, licensees will not be required to make such changes effective until the first accounting period ending at least 30 days after the receipt of a copyright owner's election.

b. Mode of Electronic Delivery

The proposed rule included language that suggested various acceptable means of formatting and delivering electronic statements of account. The Joint Commenters disagreed with this approach, suggesting that the Office should avoid specifics and instead address mode of electronic delivery with ''only a general statement concerning format and security.'' Joint Commenters Initial Comments at 13. Specifically, they stated: ''In practice, electronic statements are generally sent by email, made available for download from a portal, or uploaded to an FTP site. Since electronic delivery is accomplished in many ways, and future technological changes could bring further changes in the way statements are delivered, the Joint Commenters believe that regulations should not address this subject in detail.'' *Id.*

The Office agrees with the Joint Commenters and has adopted language in the final rule that requires licensees to submit statements of account in ''a readily accessible electronic format consistent with prevailing industry practices applicable to comparable electronic delivery of comparable financial information.'' *Id.,* exh. A, A–14. The Office declines, however, to adopt the Joint Commenters' further proposal that the rule specify that ''[r]easonable measures, consistent with prevailing industry practices applicable to comparable electronic delivery of comparable financial information, shall be taken to limit access to the Annual Statement of Account to the copyright owner or agent to whom or which it is directed.'' *Id.* The Joint Commenters nowhere explain the rationale for this provision's inclusion in their proposal, and thus the Office has no basis in the record for adopting it. Moreover, for reasons explained *infra,* the Office declines to include language in the regulations that may be construed as permitting ''confidentiality'' provisions intended to limit access to the statements of account to the copyright owner or agent to whom the statement is directed.

c. Verification of Authority

The NPRM proposed an exception to the requirement for a handwritten signature when service is made electronically. 77 FR 44183. Specifically, the proposed rule specified that if a statement is served electronically, the licensee and copyright owner are to agree upon a procedure for verification of authority.

The Joint Commenters have pointed out that this aspect of the proposed regulations is ''impracticable for large-scale uses of the compulsory license'' and creates the risk of unnecessary strain on the licensing system. Joint Commenters Initial Comments at 13. Specifically, they state: ''Federal law supports the use of electronic signatures, *see* 15 U.S.C. § 7004(b); sending of unauthorized mechanical accounting statements has not been a problem; and there is no reason to believe that unauthorized mechanical accounting statements are more likely to be a problem with electronic transmission than paper-based transmission.'' *Id.*

The Office agrees that the proposed approach has the potential to create an unnecessary administrative burden, and that electronic signatures are an acceptable means for verifying electronic records. *See* 15 U.S.C. 7006(4)–(5). Accordingly, the final rule allows for the use of electronic

originate from a payor department other than the department that generates royalty statements, and the printing and mailing of checks is sometimes outsourced to a third party,'' and that ''some payees of mechanical royalties prefer to have their payments sent to their lockbox service, while receiving their statements themselves'').

signatures on electronic statements of account.

3. Minimum Amount for Payment

The NPRM recognized that, under the current rates for the making and distribution of physical and digital phonorecords, there is potential for the transactional costs associated with making a particular monthly royalty payment to a given copyright owner to outstrip the actual value of the payment (for both copyright owners and compulsory licensees). 77 FR at 44183. To address such a scenario, the NPRM queried whether it would be permissible under the statute for the Office to implement a rule that requires royalty payments to meet a minimum threshold before they become due. *Id.* The Office also sought comment on what would constitute an acceptable minimum threshold. *Id.*

The Joint Commenters urged that it was within the Office's authority to adopt a minimum payment threshold, and proposed that the Office implement regulations that give licensees discretion to set a minimum payment threshold of up to $50, with payment of any royalty accrual that remains less than that amount to be deferred until either the time of the annual statement or whenever the royalty accrual exceeds $50, whichever comes first. Joint Commenters Initial Comments at 15. Gear Publishing agrees in principle with the Joint Commenters' approach, but proposes that the Office adopt a default threshold of one cent and place the burden of obtaining the optional $50 minimum on the licensee. Gear Publ'g, Add'l Reply Comments Submitted in Response to U.S. Copyright Office's Dec. 26, 2013 Request for Add'l Comments at 1–3 (Feb. 14, 2014) (''Gear Publ'g Add'l Reply Comments'').

After carefully considering the issue, the Office concludes that it has only very limited authority to establish a minimum payment threshold. Although, as the Joint Commenters note, the statute gives the Office discretion in setting forth the scope and form of any monthly payments made under the statute, the statute also cabins the Office's ability to alter the basic schedule of royalty payments.[12] In particular, the statute states that ''the royalty under a compulsory license shall be payable for every phonorecord made and distributed in accordance with this license,'' and that a phonorecord is ''distributed'' when the licensee ''has voluntarily and permanently parted with its possession.'' 17 U.S.C. 115(c)(2). In addition, the statute specifies that ''[r]oyalty payments shall be made on or before the twentieth day of every month and shall include all royalties for the month next preceding.'' *Id.* 115(c)(5). Thus, when read as a whole, the statute provides that royalties are payable when the phonorecords have been made and distributed by the licensee, and that all royalties payable for the prior month must be made by the twentieth of every month.[13]

But while the statute on its face appears to leave the Office little discretion to alter the basic rules regarding when royalties must be paid, the Office does have the inherent authority to allow the withholding of amounts it determines are *de minimis.* As the DC Circuit has explained, ''inherent in most statutory schemes'' is the power for administrative agencies to ''overlook circumstances that in context may fairly be considered *de minimis.''* *Ala. Power Co. v. Costle,* 636 F.2d 323, 360 (DC Cir. 1979). The court explained that ''[t]he 'de minimis' doctrine that was developed to prevent trivial items from draining the time of the courts has room for sound application to administration by the Government of its regulatory programs.'' *Id.* (internal quotation marks and citation omitted). The court stressed that ''[t]he ability . . . to exempt de minimis situations from a statutory command is not an ability to depart from the statute, but rather a tool to be used in implementing the legislative design.'' *Id.* Thus, there is ''likely a basis for an implication of *de minimis* authority to provide exemption when the burdens of regulation yield a gain of trivial or no value.'' *Id.* at 360–61.

Accordingly, the Office concludes that a regulation permitting licensees to defer royalty payments that do not meet a *de minimis* payment threshold would be consistent with the Office's regulatory authority, but that the Office lacks authority to establish a higher threshold.

In determining the appropriate *de minimis* payment threshold, the Office notes as an initial matter that the calculation mechanisms in the rates established by the CRB are such that payments to some copyright owners may amount to only fractions of a cent. Given the impossibility of paying a fraction of a cent via commonly used banking systems, it is obvious that our authority to declare certain otherwise payable royalties as *de minimis* would allow setting a minimum payment threshold of one cent. *See* Joint Commenters Initial Comments at 14 (''Because the banking system cannot process payments for less than a cent, a minimum royalty threshold of a cent is simply necessary''). Accordingly, the final rule provides for a mandatory minimum payment threshold of one cent and permits a compulsory licensee to defer delivery of monthly statements of account and any associated royalty payments until the cumulative unpaid royalties that it owes a copyright owner equal at least one cent.

The Office further concludes, however, that its authority to declare certain payments as being *de minimis* extends beyond that bare minimum threshold. There appears to be some understanding among the parties that, in the specific circumstances associated with the Section 115 license, the transaction costs involved with making a royalty payment could possibly justify a threshold of up to $50. *See generally* Joint Commenters Initial Comments at 14–15. In particular, the licensee must incur cost to generate and deliver the monthly statement and payment, and the copyright owner must incur cost in processing those statements and payments in their financial and royalty systems. *Id.* at 14. Thus, as the Joint Commenters explain, ''[t]he effort and expense required on each side can dwarf the payments sometimes generated from use of less popular songs.'' *Id.* at 14. The Office does not believe, however, that the record in this rulemaking can support the finding that all payments of under $50 are *de minimis.* The Office instead finds, based on our understanding of the transaction costs involved, and limited to the specific circumstances associated with the Section 115 license, that royalty payments of under $5 can fairly be described as *de minimis. See Ala.*

[12] 17 U.S.C. 115(c)(5) (''Each monthly payment shall be made under oath and shall comply with requirements that the Register of Copyrights shall prescribe by regulation'').

[13] The Joint Commenters focused on the language of paragraph (c)(5), arguing that ''determining precisely what are the 'royalties for the month next proceeding' is a topic for the accounting regulations.'' Joint Commenters Initial Comments at 14–15. But that view fails to account for the language of paragraph (c)(2), which appears to provide that royalties are ''payable'' when phonorecords are made and distributed. The Joint Commenters' reliance on the provisions for reserve accounting is similarly misplaced. *See* Joint Commenters Initial Comments at 14–15. The reserve accounting rules specify that, in certain cases, a licensee need not make a royalty payment when a record is sold with a return privilege. *See* 37 CFR 201.19(c). But those rules are based on the logic that phonorecords that have been sold with a return privilege have not been ''distributed'' within the meaning of the statute, and thus royalties are not yet ''payable.'' *See* 17 U.S.C. 115(c)(2) (providing that a phonorecord is considered ''distributed'' when the licensee ''has voluntarily and permanently parted with its possession''); *see also* H.R. Rep. No. 94–1476, at 110–11. In contrast, a DPD is distributed on the date that it is digitally transmitted.

Power, 636 F.2d at 360–61 (holding that there is ''likely a basis for an implication of *de minimis* authority to provide exemption when the burdens of regulation yield a gain of trivial or no value''); *cf.* 37 CFR 201.11(i)(3) (establishing a five-dollar threshold for payment of interest charges for any royalty underpayment or late payment).

To be sure, the Office recognizes that this assessment of the transaction costs is inexact, and that certain copyright owners may wish to receive statements of account and payments where the royalties owed are less than five dollars in a given month.[14] The Joint Commenters' proposal, however, addresses these concerns by allowing a copyright owner to opt-out of the minimum threshold. *See* Joint Commenters Initial Comments at 15 (''[T]he Joint Commenters' proposed regulations provide a mechanism for a copyright owner to obtain a monthly payment anytime it has at least a cent in royalty accruals.''). In addition, the Joint Commenters' proposal requires payment of *any* cumulative unpaid royalties, even if they are below the threshold amount, at the time of delivery of the annual statement of account. *Id.*

Accordingly, in addition to setting the mandatory minimum threshold of one cent described above, the final rule gives licensees the discretion to set a default minimum payment threshold of up to $5 for payments to any copyright owner. (The Office stresses that this is a *per-copyright-owner* threshold, and not a *per-work* threshold). It allows the licensee to defer production of statements of account and payment of any royalty accrual that remains less than that amount until the earlier of the time for rendering the annual statement of account, the time for rendering the monthly statement of account for the month in which the compulsory licensee's cumulative unpaid royalties meet or exceed the minimum threshold, or the time for rendering the monthly statement of account that is due no sooner than 30 days after the copyright owner provides written notice of its desire to receive payments that are less than the minimum threshold established by the licensee.

While the Office contemplated adopting Gear Publishing's proposed approach, it finds it too onerous a burden to force licensees to proactively negotiate minimum payment thresholds with all copyright owners. Further, it would defeat the purpose of permitting a minimum threshold—which is to implement a default means of preventing situations where the transactional costs associated with a given royalty payment outweigh the actual value of the payment (for both copyright owners and compulsory licensees).

D. Issues Presented Involving Reporting on Statements of Account

1. Statement of Account Issues in General

The existing rule set forth detailed requirements for the content of monthly and annual statements, including information about the licensee and the licensee's use of the compulsory license. *See* 37 CFR 201.19(e)(2) and (3); 201.19(f)(3) and (4). The proposed rule carried forward these basic requirements both for cents-rate and percentage-rate usages, with only minor alterations to account for the newer royalty rate structures. *See* 77 FR at 44188–89, 44194.

The Joint Commenters recommended a number of technical changes to the reporting information. *See generally* Joint Commenters Initial Comments, exh. C. For instance, the Joint Commenters recommended the Office require the reporting of International Standard Recording Codes (''ISRC''), an international standard code for uniquely identifying sound recordings, where that code is known. According to the Joint Commenters, this will further the ability to automatically match large statements to repertoire databases. For the same reason, the Joint Commenters also recommended that the Office require the reporting of the writers of the musical work, when that information is known.

The Office has largely accepted these technical suggestions, which garnered no opposition from other commenters.[15] The final rule, however, includes a few minor changes to the amendments proposed by the Joint Commenters. The Joint Commenters proposed that the ISRC not be reported for cents-rate usages and for multi-recording products in a music bundle. The Office concludes that these carve-outs would add needless complication to the rule. Instead, the Office has adopted a broad rule requiring the reporting of ISRCs when that information is known. The Office has also added to the writer name requirement to permit the reporting of other unique identifiers, such as the International Standard Name Identifier (''ISNI'') of the writer, or the International Standard Musical Work Code (''ISWC'') for the musical work. In addition, the Joint Commenters' proposal would have not required the reporting of writer name information for statements with fewer than 50 lines. Again, if that information is known, the Office sees no reason to exclude it from the statements of account.

More substantively, the Joint Commenters criticized the proposed rule's requirement that, for all percentage-rate usages, the statements of account must report information such as the number of phonorecords involved broken down by configuration. The Joint Commenters explained that ''[u]nder Part 385 Subparts B and C, the number of phonorecords made and distributed is not generally determinative of the rate calculation, and phonorecords of multiple configurations are generally treated together as part of a single rate calculation.'' *Id.* at 5. Thus, as with the royalty calculation provisions addressed above, the Joint Commenters recommended a minimalist approach, requiring simply a ''separate listing of the information required'' to calculate the rates under part 385. Joint Commenters Initial Comments, exh. A, at A–9. No other commenter opposed that proposal.

The Office agrees with the Joint Commenters' critique of the proposed rule and largely adopts its recommendation to incorporate by reference the requirements of the rates in part 385. The final rule makes clear, however, that licensees are obligated to provide a detailed and step-by-step calculation of royalties under that part.[16]

[14] For instance, David Lowery, the lone objecting commenter addressing this issue, urged that licensees should ''pay [copyright owners] what they owe when they owe it like everyone else.'' David C. Lowery, Comments Submitted in Response to U.S. Copyright Office's July 27, 2012 Notice of Proposed Rulemaking at 2 (Dec. 10, 2012).

[15] The Office has not adopted the Joint Commenters' proposal to specify that the ''copyright owner and the compulsory licensee or authorized agent may agree upon alternative methods of accounting and payment'' and that statements of account or payments ''provided in accordance with such an agreement shall not be rendered invalid for failing to comply with the specific requirements of'' the regulations. Joint Commenters Initial Comments, exh. A, at A–15, A–22. Inclusion of these provisions is unnecessary. The statute itself provides that ''[l]icense agreements voluntarily negotiated at any time . . . shall be given effect in lieu of'' the rates and terms established by the CRB. 17 U.S.C. 115(c)(3)(E)(i). It necessarily follows that such agreements can also diverge from the Register's payment and statement-of-account regulations, because those regulations are so closely intertwined with the rates and terms adopted by the CRB.

[16] In so providing, the rule incorporates the essential features of the detail requirements that the Copyright Royalty Judges had adopted in the latest Section 115 rate proceeding, but that the Register determined would impermissibly encroach on the Register's authority to establish requirements for monthly and annual statements of account. *See* 78 FR 28770 (May 16, 2013); *see also* Joint

Continued

2. Reporting of Promotional Digital Phonorecord Deliveries

As the NPRM explained, ''[p]romotional Digital Phonorecord Deliveries are often an important tool for record labels and services to attract new listeners, create awareness about a particular artist, and increase plays.'' 77 FR at 44183. In light of these considerations, the CRB established a royalty rate of zero for certain promotional interactive streams and limited downloads and for free trial periods for mixed service bundles, paid locker services, and limited offerings. *See* 37 CFR 385.14; 385.24. (There is no promotional rate for cents-rate usages.) The CRB imposed detailed limitations on the use of the promotional rates, including recordkeeping requirements. *See* 37 CFR 385.14(a)(2),(3); 385.24(a)(4)(i), (b)–(c).

This raised the question of whether and how promotional DPDs should be accounted for in the statements of account. The proposed rule noted that ''[e]ven though no royalty is owed in these circumstances, it is unclear whether licensees should give a full accounting of all the phonorecords made under the license in the Statement of Account.'' 77 FR at 44183. The NPRM thus asked ''whether the statute requires that Statements of Account contain play information on promotional digital phonorecord deliveries.'' *Id.* It further asked ''[i]f the conclusion is that there is no statutory requirement, . . . whether digital phonorecords offered at a promotional rate or for a free trial period should be reported and with what frequency, *e.g.,* monthly or annually.'' *Id.* The proposed rule required detailed accounting of promotional DPDs, on the theory that such a requirement ''would not seem to be a hardship on the licensees,'' because the CRB's recordkeeping rules ''require[] retention of complete and accurate records of the relevant authorization, identification of each sound recording of a musical work made available through the free trial period, the activity involved, and the number of plays and downloads for each recording.'' *Id.*

The Joint Commenters opposed any requirement to report promotional uses as part of statements of account, on the ground that any such requirement would be administratively burdensome. *See* Joint Comments at 15–19. Gear Publishing supported the imposition of such a reporting requirement, citing the utility of such information for copyright owners. Gear Add'l Reply Comments at 4.

After careful consideration, the Office has decided not to require detailed reporting of promotional uses. Instead, the final rule only requires the licensee to affirmatively provide the copyright owner with detailed instructions on how to obtain the records of any promotional uses that are required to be maintained under the CRB's existing rules.

First, the Office concludes that the statute does not unambiguously require statements of account to include detailed information (like play counts) about licensees' use of DPDs for promotional purposes. The statute generally grants the Register broad discretion to adopt regulations governing monthly and annual statements of account. It states that ''[e]ach monthly payment . . . shall comply with requirements that the Register of Copyrights shall prescribe by regulation,'' and requires the Register to ''prescribe regulations under which detailed cumulative annual statements of account . . . shall be filed[.]'' 17 U.S.C. 115(c)(5). The only arguable limitation on that generally broad delegation of rulemaking authority comes in the last sentence of section 115(c)(5): ''The regulations covering both the monthly and annual statements of account shall prescribe the form, content, and manner of certification with respect to the number of records made and the number of records distributed.'' *Id.*

Properly understood, this sentence instructs the Register to prescribe (1) the ''form'' of the statements, (2) the ''content'' of the statements, and (3) the ''manner of certification'' of the statements ''with respect to the number of records made and the number of records distributed.'' *Id.* The last clause requires only that the ''manner'' of certification relate in some way to the number of records made and distributed by the licensee. *Cf. Landmark Legal Found.* v. *IRS,* 267 F.3d 1132, 1136 (D.C. Cir. 2001) (noting ''the extremely general character of the connecting phrase—'with respect to' ''). The clause does not, however, require statements of account themselves to reflect the exact number of records made and distributed in all circumstances.[17]

Second, given that the statute does not clearly require statements of account to track distributions of promotional DPDs, the Office must instead consider whether such a requirement would nevertheless be appropriate in light of the overall purposes of the statute, including the goals of preventing ''economic harm from companies which might refuse or fail to pay their just obligations'' and of ensuring the administrability of the statutory license. H.R. Rep. No. 94–1476, at 111.

Several competing considerations are relevant to that analysis. On the one hand, as Gear Publishing notes, information regarding promotional uses may have value for copyright owners, and could help ensure that licensees are complying with the conditions imposed by the CRB for use of the promotional rate. Gear Publ'g Add'l Reply Comments at 4. On the other hand, promotional uses carry a zero rate, and such uses thus have little direct financial impact on the copyright owners. Moreover, the Joint Commenters—representing both copyright owners and compulsory licensees—have described in detail the administrative burden associated with reporting promotional uses in the statements of account. Joint Commenters Initial Comments at 15–19. According to the Joint Commenters, many promotional uses are conducted by third-party licensees, as with the ''streaming of preview clips from download stores,'' but detailed information regarding play counts and the like are typically not reported into the royalty accounting systems of compulsory licensees. *Id.* at 16. Thus, ''[i]mposing a new reporting requirement would necessitate creating new reporting processes.'' *Id.* In addition, as noted, the CRB already requires licensees to keep records of promotional uses and make them available to copyright owners on request, and thus the proposed rule was largely duplicative of provisions already in effect. *Id.* at 18.

Balancing these considerations, the Office has decided not to require detailed reporting of promotional uses in the monthly and annual statement of account. In particular, we believe that the needs of copyright owners are largely satisfied by the recordkeeping terms the CRB has adopted for

Commenters, Add'l Comments Submitted in Response to U.S. Copyright Office's July 27, 2012 Notice of Proposed Rulemaking (Jan. 30, 2013) at 2–3 (urging the adoption of these ''detail requirements'').

[17] *See also Village of Barrington, Ill.* v. *Surface Transp. Bd.,* 636 F.3d 650, 661 (D.C. Cir. 2011) (explaining that a statute must ''unambiguously'' foreclose the exercise of agency discretion). The Office acknowledges that it has, on an earlier occasion, suggested that the statute mandates that statements of account contain an individual accounting of promotional DPDs. *See* 74 FR 4537, 4543 (Jan. 26, 2009) (''There is no statutory authority for an exception to this requirement for certain types of ''phonorecords' or for the participants to alter this provision by agreement.' ''). That sentence, however, was not directly relevant to the issue that was being addressed on that earlier occasion, which was related to the relevant division of authority between the CRB and the Register with respect to statements of account. *Id.*

promotional uses, which give copyright owners the right to obtain records of promotional uses on request. *See* 37 CFR 385.14(a)(2), (3); 385.24(a)(4)(i), (b)–(c). At the same time, the Office is concerned that some copyright owners may not know how to invoke that right. Accordingly, the final rule provides that statements of account must include detailed instructions on how a copyright owner may obtain the records of promotional uses that are required to be maintained or provided under section 385.14 and section 385.24, or any other similar regulation the CRB may promulgate in the future, including records that are required to be maintained or provided by third-party services that are authorized by the licensee to engage in promotional uses.[18] Where licensees are themselves engaged in promotional uses of the copyrighted works (*e.g.,* a record label Web site that streams free previews), providing this basic information should be a trivial burden. Where a licensee has authorized a third-party service to engage in promotional uses, the annual statement should disclose sufficient information to allow the copyright owner to request the material that the service is required to maintain under the terms adopted by the CRB. This modest requirement will ensure that copyright owners are regularly informed of their right to request records of promotional uses.

3. Reporting the Identification of Third-Party Licensees

The NPRM highlighted the ongoing disagreement between copyright owners and compulsory licensees regarding the identification of authorized third-party distributors of DPDs and ringtones in statements of account.[19] FR at 44183–84.19. The Office accordingly solicited comments on whether new regulations should require licensees to issue statements that include both the identities of the third-party services they authorize to distribute DPDs and ringtones and the number of DPDs and ringtones each such service distributes. *Id.*

The responses received were consistent with the summary of the disagreement laid out in the NPRM. 77 FR 44183–84. Commenting copyright owners—represented by the Joint Publishers and Songwriters group, and Gear Publishing—favored amending the existing regulations to require compulsory licensees to identify each third-party service that distributes a DPD or ringtone in connection with the compulsory license as well as the total number of DPDs and ringtones that specific service distributed. *See* Joint Publishers and Songwriters Initial Comments at 3; *see also* Gear Publ'g Initial Comments at 14–15. The copyright owners claimed that, without such information, publishers and songwriters have no way of determining what third-party services are authorized to distribute DPDs and ringtones. *Id.* They further asserted that, given the rise in the number of third parties providing digital distribution services, permitting original licensees to ''cloak'' the identities of sublicensees deprives them of valuable information and limits their ability to participate in the expanding digital marketplace. Joint Publishers and Songwriters Initial Comments at 4–5. Regarding the ease with which licensees could implement such regulations, the copyright owners claimed that third-party services already track and report DPD and ringtone distributions to compulsory licensees, making the licensees' identification of third-party services in their statements of accounts ''not only reasonable, but also necessary to ensure transparency in the digital environment.'' Joint Publishers and Songwriters Initial Comments at 3–4.

Commenting compulsory licensees—represented by RIAA and A2IM—took the opposing view. RIAA Reply Comments at 11–17; A2IM Reply Comments at 3–4. They disagreed with the copyright owners' assertion that this aspect of the Section 115 license requires additional transparency and maintained that ''[t]he mere fact that some publishers are curious to have this information is not a sufficient reason to require record companies to reengineer their royalty reporting systems to provide it.'' RIAA Reply Comments at 15; *see also* RIAA Initial Comments at 13–14. In this regard, the RIAA claimed that separately calculating and reporting usage figures for each third-party distributor would lead to a multiplication in the volume of data processed by record companies, would cause an increase in the size of the statements delivered to copyright owners, and would require record companies with ''legacy royalty accounting systems'' to make ''significant changes to business processes and systems, at a substantial cost.'' RIAA Initial Comments at 14. Likewise, A2IM claimed that small- and medium-sized record companies often do not have access to this information (where digital distribution is handled through an aggregator) and that, even if they could obtain this information, a requirement to report it in the manner the commenting copyright owners suggested would ''dramatically increase'' their administrative burden. A2IM Reply Comments at 3.

After careful consideration of the comments, the Office has decided to amend the regulations to require licensees to issue statements of account that identify authorized third-party distributors, and list the number of DPDs and ringtones each such party distributes. The Office is of the opinion that transparency is critical where copyright owners are compelled by law to license their works. As the Joint Publishers and Songwriters pointed out, information regarding the breadth of the distribution of their works has the potential to influence their future business decisions and impact the scope of their involvement in the digital music industry. Joint Publishers and Songwriters Initial Comments at 5. In addition, increasing transparency of the uses of music is likely to enhance the copyright owners' faith in the accuracy of the accounting statements. The Office fails to see the advantages in permitting licensees to withhold such basic information as: What services are exploiting their works, who is authorizing the services to exploit their works, and the frequency with which the works are being exploited. To the contrary, the music industry stands to profit from increased transparency among copyright owners and the licensees who exploit protected works pursuant to the compulsory license.

The Office is cognizant that compulsory licensees will have to bear some administrative burden in implementing this amendment. As the RIAA correctly noted, the Office has previously cautioned against the implementation of regulations that would ''substantially multiply necessary paperwork'' and ''put compulsory licensing beyond the means of many record companies.'' 45 FR at 79039. Nevertheless, the Office is not persuaded by the licensees' argument that the burden in this instance would

[18] The Office notes that the CRB regulations do not appear to require services to maintain per-play counts of promotional uses of interactive streaming of clips. *See* 37 CFR 385.14(a)(1)(iii)(A), (d). At this time, the Office is not requiring the collection of that information in its statement-of-account regulations, on the ground that the parties in the proceedings before the CRB believed that such detailed recordkeeping was not necessary for those specific uses.

[19] For percentage-rate usages, information about third-party distributors is provided to copyright owners as a matter of course. As the RIAA notes, ''[t]he percentage rate calculation is specific to a particular service offering, so it is only natural that the offering would be identified in applicable statements. Moreover, this usage is typically accounted for by the services [who pay a percentage rate] themselves, making identification of the distributor trivial.'' RIAA Initial Comments at 14. The final rule codifies the practice of identifying the distributor or third-party distributor for percentage-rate usages.

be unreasonable. Based on the information the Office received over the course of numerous rounds of stakeholder comments, it is not convinced that tracking and reporting works across multiple distributors is cost- or resource-prohibitive. As discussed, the new regulations will only require a change in reporting practices with respect to DPDs and ringtones distributed by third-party licensees. Our understanding is that most third-party licensees already collect and report relevant usage information to compulsory licensees for payment purposes. *See* Joint Publisher and Songwriter Reply Comments at 5 & nn.2–3. The licensee's only burden, then, is to report the information that they already receive to copyright owners. Thus, balancing all the factors, the Office believes the added transparency will benefit rather than harm the compulsory licensing marketplace.

4. CPA Certification of Annual Statements of Account

The statute requires the Register to ''prescribe regulations under which detailed cumulative annual statements of account, certified by a certified public accountant, shall be filed for every compulsory license.'' 17 U.S.C. 115(c)(5). The statute also instructs the Register to issue regulations that ''prescribe the form, content, and manner of certification with respect to the number of records made and the number of records distributed.'' *Id.* As the Office explained in the NPRM, the certification requirement ''should assure that copyright owners receive the royalties to which they are entitled, but . . . should not burden the licensee to the point that it would prevent the compulsory license from being a practical option for record companies or services.'' 77 FR at 44184.[20] For purposes of the proposed rule, the Office retained the existing regulations for CPA certification of annual statements of account, which had been in place since 1980. 77 FR at 44191, 44196. The NPRM nevertheless asked whether there were ''alternative certification methods that . . . should be considered by the Office.'' *Id.* at 44184.

Commenters broadly agreed that the existing certification regulations should be revised, and agreed in general terms about the basic structure and many of the specific elements of the revised certification provisions. After considering fully the comments received, the Office has adopted the structure and uncontroversial elements of the Joint Commenters' proposal regarding certification of the annual statements of account in the new section 210.17(f), with conforming revisions to the certification requirements for the monthly statements of account in the new section 210.16(f). At bottom, the Office has designed the CPA certification rule to provide copyright owners with firm assurance that the annual statement accurately reflects, in all material respects, the compulsory licensee's usage of musical works, the statutory royalties applicable thereto, and any other data that is necessary for the proper calculation of the statutory royalties in accordance with the statute and applicable regulations. *See* H.R. Rep. No. 94–1476, at 111 (explaining that the annual statement requirement should ''increase the protection of copyright proprietors against economic harm from companies which might refuse or fail to pay their just obligations'').

One of the key features of this new rule is the accommodation for alternative methods of certification for small-scale users and large-scale users. According to the commenters, the existing regulations appeared to assume individual review and certification of all statements of account, a step that is impracticable for large-scale use of the compulsory license.[21] The Office agrees. The revised rule thus provides that, where the accountant determines in its professional judgment that the volume of data involved would render individual review and certification of annual statements of account impracticable, an accountant certifying the annual statement of account may instead examine the internal processes and controls of the licensee to determine whether they were suitably designed and operated effectively to accurately calculate royalties and generate compliant statements of account. A similar provision applies to monthly account statements.[22]

Another notable revision is the removal of the requirement that the CPA use specific certification language. Instead, consistent with the commenters' proposals, the final rule now specifies the scope of the examination and the general substance of the opinion the CPA must render after that examination. Although this departs from our conclusion in 1978,[23] the Office believes it is appropriate to do so in light of the following factors: First, the commenters in this proceeding, who have dealt with the certification language under the existing rule for many years, all agreed that the Office should not specify the certification language. Second, as the Joint Commenters pointed out, ''[i]f the required substance of the certification is anchored in appropriate professional standards, it is not necessary to provide exact certification language to have a rigorous certification process.'' Joint Commenters Reply Comments at 6. Finally, our understanding is that the language used in opinions rendered by CPAs is largely dictated by the American Institute of Certified Public Accountants' (''AICPA'') standards.[24] The Office is wary of requiring the use of specific certification language that could interfere with those standards.

Beyond these uncontroversial changes, there were three areas of disagreement between Music Reports and the Joint Publishers and Songwriters about the particulars of the manner of certification, particularly as they related to large-scale uses of the compulsory license. As explained below, the Office largely agreed with the Joint Publishers and Songwriters on each of these points, and the final rule reflects their proposal.

[20] The Office recognizes that some commenters requested the establishment of a right to audit the records kept by users of the compulsory license as part of these statement-of-account regulations. The Office declines to adopt such audit provisions because it is not apparent that the statute authorizes the Register to do so. However, the Office reiterates its conclusion that the CRB does have the authority to issue requirements regarding audit of records that are required to be kept as part of the terms of the compulsory license. *See* 73 FR at 48398.

[21] *See* Joint Commenters Reply Comments at 5–6; Music Reports, Reply Comments Submitted in Response to U.S. Copyright Office's July 27, 2012 Notice of Proposed Rulemaking at 9 (Dec. 10, 2012) (''Music Reports Reply Comments''); *see also* RIAA Reply Comments at 2, 18 (urging the Office to adopt a certification option for small-scale use of the compulsory license).

[22] Although no commenter has disputed our statutory authority to adopt this amendment, the Office has independently concluded that this bifurcated certification procedure is consistent with the statutory instruction to ''prescribe the form, content, and manner of certification with respect to the number of records made and the number of records distributed.'' 17 U.S.C. 115(c)(5). As indicated above, the statutory language gives the Register broad discretion with regard to certification of the processes used to track usage of the license *Cf. Landmark Legal Found.* v. *IRS,* 267 F.3d 1132, 1136 (DC Cir. 2001) (noting ''the extremely general character of the connecting phrase—'with respect to'''). The statute does not mandate an individual count of records in all cases.

[23] 43 FR at 4515–16.

[24] *See* AICPA, *Statements on Standards for Attestation Engagements* at 101.114, *http://www.aicpa.org/Research/Standards/AuditAttest/DownloadableDocuments/AT-00101.pdf* (examples of examination reports) (last updated June 1, 2013).

a. Requirement for a Single Certification

Many compulsory licensees outsource royalty accounting services to a third-party service provider like Music Reports, which raises the question of how the CPA certification should operate in those circumstances. Music Reports proposed that two separate CPAs would issue two separate and essentially unrelated certifications—the CPA for the licensee would certify the statement to the extent it contains usage and other data used to calculate royalties, and the CPA for the service provider would certify the process used to generate the statement. Music Reports, Add'l Reply Comments Submitted in Response to U.S. Copyright Office's Dec. 26, 2012 Notice of Proposed Rulemaking at 8–9 (Feb. 14, 2014). By contrast, the Joint Publishers and Songwriters proposed requiring a single certification from a CPA engaged by the compulsory licensee. *See* Joint Publishers and Songwriters Reply Comments at 15–16. Under that proposal, to the extent the licensee relies on a third-party service provider for royalty accounting services, the licensee's CPA would be able to rely on a report and opinion generated by the service provider's CPA certifying the process used to generate the annual statement. *Id.* Gear Publishing proposed that, where the licensee's CPA relies on a report of the CPA of the third-party service provider, the licensee's CPA should be required to disclose that they have relied on such a report. Gear Publ'g Initial Comments at 16.

After careful consideration of the comments, the Office adopts in general Gear Publishing and the Joint Publishers and Songwriters' proposals. Allowing different CPAs to certify different portions of annual statements would substantially detract from the chief goals of the CPA certification requirement—assuring transparency and certainty of royalty payments. Permitting piecemeal certifications creates a risk that no person bears responsibility for examining the process as a whole to ensure that it is suitably designed to generate compliant annual statements. Under the statute, a compulsory licensee bears full responsibility to produce accurate and complete annual account statements, and should ultimately be responsible for shortcomings in those statements no matter their source. *See* 17 U.S.C. 115(c)(5). The CPA engaged by the compulsory licensee should similarly bear responsibility to provide a certification as to all aspects of the statement.

The final rule thus provides that the licensee's CPA must certify the statement as a whole, even where a third party provides services related to the annual statement. The Office appreciates Music Reports' concern that requiring the licensee's CPA to base its certification on a report received from a third-party service provider's CPA could introduce complexity into the certification process. *See* Music Reports Reply Comments at 8. In response to that concern, the final rule makes clear that the licensee's CPA may rely on the report produced by the service provider's CPA, if that fact is disclosed in the certification. Whether in a particular case the licensee's CPA might be required to assess the bases for the third-party report is a matter that the Office entrusts to the judgment of the licensee's CPA under the pertinent professional standards. The Office notes, however, that nothing in the rule prevents the *same* CPA from examining and rendering an opinion with respect to both the licensee and the third-party service provider.

b. Requirement To Examine the Process by Which Usage Data Is Generated

The second area of dispute relates to the examination of large-scale licensees who use third-party services (like Music Reports) to generate annual statements of account. Typically, such licensees supply usage and other data relevant to the royalty calculation (*e.g.,* revenues, performance rights payments, play counts, and subscriber counts) to the third-party service, which in turn is responsible for actually generating the statements of account based on that data. Music Reports argues that, for such licensees, the CPA examination should exclude the processes used by the licensee to track usage and other royalty data supplied to the third-party service. Instead, Music Reports appears to take the view that the accuracy of that data should be taken at face value. Music Reports Add'l Reply Comments at 6–7. In particular, Music Reports suggests that this data is already ''highly scrutinized'' by ''the CFO of the licensee, by the sound recording owners and performance rights organizations, [and] by the licensee's potential investors.'' *Id.* at 8. The Joint Publishers and Songwriters take the opposite view, urging that an examination of the processes used to generate the usage and other data is necessary to ensure that the annual statements are accurate. *See* Joint Publishers and Songwriters Reply Comments at 3–5.

The Office agrees with the Joint Publishers and Songwriters. As explained, the purpose of the CPA certification requirement is to give the copyright owner firm assurance that it is receiving all the royalties to which it is entitled. Given that goal, Music Reports nowhere explains how an acceptable CPA examination can realistically take place for large-scale licensees without examining the reliability of the processes used to track the data used in royalty calculation. *See generally* Music Reports Reply Comments at 8. Music Reports' assertion that licensees ''have had no reason under current law and regulation'' to think that these processes would be subject to examination (Music Reports Add'l Reply Comments at 7), is difficult to fathom. It should have been obvious to any licensee that a fair assessment of the accuracy of royalty payments necessarily requires an examination of the accuracy of the data used for the royalty calculations and, if necessary, of the processes used to track that data.[25]

c. Underlying Auditing Standard

The third and final area of disagreement relates to the professional standards that the CPA must employ when examining annual statements. Under the current rule, the CPA must certify that they have examined the annual statement in accordance with ''generally accepted auditing standards,'' or GAAS. 37 CFR 201.19(f)(6)(ii)(A). The Joint Commenters explained, however, that GAAS is not the most directly applicable standard under modern accounting practice. According to them, GAAS provides specific standards for the audits of corporate financial statements rather than the activities contemplated by Section 115. *See* Joint Commenters Reply Comments at 3–4. Instead, ''[t]he certification required by the current regulations is more akin to the certification that applicable professional standards contemplate when a CPA completes an examination under the AICPA Attestation Standards,'' a different set of professional standards for CPAs. *Id.* at 4.[26] Christian Castle reinforced this

[25] For that reason, Music Reports also missed the mark when it asserted that the Joint Publishers and Songwriters' proposal would ''require a process audit of the Usage and Royalty data in high-volume contexts, but not require a process audit in low-volume contexts,'' and that the proposal thus ''creates a double standard which discriminates against DSPs vis a vis [sic] record companies.'' Music Reports Add'l Reply Comments at 7. A low-volume context would presumably be one in which it is unnecessary to examine the processes used to generate annual statements because it is relatively easy to examine the annual statements and the underlying data directly.

[26] *See also* AICPA, *Clarified Statements on Auditing Standards* AU–C § 200.01, *http://*

Continued

point, proposing that the Office ''specify . . . that the certified public accountant certifying Annual Statements of Account must perform their certification review in accordance with the attestation standards designated by the Copyright Office.'' Christian L. Castle, Initial Comments Submitted in Response to U.S. Copyright Office's July 27, 2012 Notice of Proposed Rulemaking at 11 (Oct. 25, 2012) (''Castle Initial Comments'').

Thus, there appears to be general agreement that the AICPA's ''attestation standards'' are appropriate in at least some circumstances. Music Reports, however, proposed that our regulation specify the use of these attestation standards *only* for high-volume uses of the compulsory license, and even then only for the CPA's examination of the processes used to generate the annual statements (either by the licensee or a third party) and not for the examination of the usage and other data used in the royalty calculation. Music Reports Reply Comments, exh. A, at A–2 to A–3. For those other situations, Music Reports proposed leaving the particular standard open-ended, by providing that the examination must take place ''in accordance with the professional standards of the American Institute of Certified Public Accountants.'' *Id.,* exh. A, at A–2. The Joint Publishers and Songwriters, in contrast, urged the specification of attestation standards in all circumstances. Joint Publishers and Songwriters Reply Comments at 15–18. And notably, the RIAA, whose members are typically small-scale users of compulsory licenses, disagreed with Music Reports, and proposed the use of the attestation standard for CPA examination of annual statements generated by such users. RIAA Reply Comments at 18.

After full consideration of the comments on this issue, the Office agrees in general with the Joint Publishers and Songwriters' proposal, and rejects Music Reports' competing proposal. Most problematically, the reference to ''professional standards'' in Music Reports' proposal is non-specific, and could encompass examinations that are not especially demanding.[27] Moreover, as the Joint Publishers and Songwriters convincingly explain, requiring CPAs to employ the attestation standards, and by further specifying that the attest engagement must include an ''examination'' of the annual statements followed by an ''opinion'' that those statements accurately reflect the relevant information, ''provide[s] a high level of assurance that compulsory licensees were complying [with] Section 115 and the attendant regulations.'' Joint Publishers and Songwriters Reply at 17.[28] The Office believes that adopting those standards is thus likely to fulfill Congress's overarching goal in enacting the certification requirement, *i.e.,* ''to increase the protection of copyright proprietors against economic harm from companies which might refuse or fail to pay their just obligations.'' H.R. Rep. No. 94–1476, at 111.[29] Accordingly, the final rule requires the use of the AICPA's ''attestation standards'' in all circumstances, and further specifies that the CPA must conduct an ''examination'' and render an ''opinion'' regarding the annual statements under those standards.

Certain commenters asked us to go even further and provide more detail regarding the precise manner of examination. For instance, the Joint Publishers and Songwriters proposed that the rule provide detailed guidance regarding the CPA's examination. *See* Joint Publishers and Songwriters Reply Comments at 23. Similarly, the Joint Publishers and Songwriters and Music Reports together urged that the Office specify that the CPA examination of third-party service providers take place under the AICPA's Statement on Standards for Attestation Engagements No. 16 (SOC), Type II. Songwriters Reply Comments at 18. Similarly, Christian Castle proposed that the Office adopt ''specific attestation standards.'' *See* Castle Initial Comments at 10.

The Office declines to provide more detail governing the conduct of the CPA's examination. Among the concerns the Office has is that the AICPA amends or recodifies its standards with some regularity.[30] It would thus be inappropriate to embed specific standards into the rule. Accordingly, the final rule simply provides the examination of third-party providers should simply take place under the AICPA's attestation standards generally. The Office believes details of how a CPA will conduct its examination in accordance with the standards set forth in the regulations are best left to the CPA's professional judgment, and trusts that CPAs will choose the specific standards and procedures that are most appropriate for each examination.

5. Adjustment of Timetables for Reporting

The NPRM proposed extending the deadline for filing annual statements of account from three months after the close of the licensee's fiscal year to six months after the close of the licensee's fiscal year. 77 FR at 44184. The Joint Commenters agreed that the increased complexity of compiling annual statements of account that include percentage-of-revenue based royalty allocations warrants a deadline extension.[31]

Gear Publishing, however, opposed an extension, claiming ''[t]he digital age is supposed to make things faster not slower'' and ''[a] summary of streams related to any musical work should be available at any time.'' Gear Publ'g Initial Comments at 17. They countered the proposed extension with a request that the time to produce an annual statement be reduced from three months to forty-five days. *Id.* A number of independent commenters also opposed the extension, claiming extending the deadline creates a ''new safe harbor'' which provides licensees with additional time to meet obligations they could have easily fulfilled under the existing regulations. *See, e.g.,* Castle Initial Comments at 9–10.

www.aicpa.org/Research/Standards/AuditAttest/DownloadableDocuments/AU-C-00200.pdf (last updated June 1, 2013); AICPA, *Statements on Standards for Attestation Engagements* AT § 101.01, *http://www.aicpa.org/Research/Standards/AuditAttest/DownloadableDocuments/AT-00101.pdf* (last updated June 1, 2013).

[27] For example, CPAs can be engaged to conduct ''compilations'' or ''reviews,'' which provide comparatively lower levels of service. *See* AICPA, *What is the Difference Between a Compilation, a Review, and an Audit?, http://www.aicpa.org/InterestAreas/PrivateCompaniesPracticeSection/QualityServicesDelivery/KeepingUp/Downloadable Documents/Brochure%20Customizable-%20Difference%20between%20Comp%20Review Audit.pdf* (last visited July 31, 2014).

[28] *See* AICPA, *Statements on Standards for Attestation Engagements, supra* note 21, § 101.54, (noting that ''an attest engagement designed to provide a high level of assurance'' is ''referred to as an *examination''*); *id.* § 101.69 (''In an engagement to achieve a high level of assurance (an examination), the practitioner's conclusion should be expressed in the form of an opinion.'').

[29] Music Reports also asks us to provide a view of whether the AICPA's attestation standards require use of an ''independent'' auditor. *See* Music Reports Reply Comments at 8. The Office is not in a position to provide such a view.

[30] Indeed, it appears that the AICPA is currently engaged in an effort to clarify and recodify several of its professional standards, including the attestation standards. *See* AICPA, *Proposed Statement on Standards for Attestation Engagements* (July 24, 2013), *http://www.aicpa.org/Research/ExposureDrafts/AccountingandAuditing/DownloadableDocuments/20130724a_ED_Attestation_Standards_1to4.pdf.*

[31] In their initial comments, the Joint Commenters explain, ''Large-scale use of the compulsory license, particularly for percentage-rate usages, has made preparation and auditing of annual statements a complex process. In addition, it is important to remember that the first month of the annual statement period is necessarily devoted to completing the monthly accounting for the last month of the year, since the monthly statements can't be tallied until the last one is done. Two months after preparation of the last monthly statement is completed is not long to complete the whole annual statement process.'' Joint Commenters Initial Comments at 20.

The Office concludes that the accounting requirements are sufficiently complex to justify extending the period for statutory licensees to file their annual statements from three to six months. The Office also believes this extended deadline will generally benefit copyright owners by allowing sufficient time for the robust CPA examination and certification contemplated by the regulations.

6. Reporting for Periods Prior to Enactment of New Regulations

As noted, one key purpose of this rulemaking is to amend the existing statement-of-account regulations to reflect the CRB's establishment of new rate structures for DPD configurations not previously subject to the Section 115 license. *See* 37 CFR part 385. One question the NPRM addressed was whether statements of account that complied with these new accounting rules would have to be filed for reporting periods occurring after those rates took effect on March 1, 2009. 77 FR at 44184. The proposed rule required the delivery of statements of account for any prior accounting period within 180 days after the new statement-of-account regulations took effect. *Id.*

The Joint Commenters objected to providing statements of account for past reporting periods, on the ground that it would be a needless administrative burden. Joint Commenters Initial Comments at 21–23. They observed that monthly statements of account produced by the digital music services already take into consideration percentage-rate usages. *Id.* At the same time, they noted that with respect to annual statements ''certain licensees making large-scale use of the compulsory license for percentage rate configurations have not been providing annual statements,'' because it was ''difficult or impracticable to do so'' in the absence of regulatory guidance. *Id.* at 23. In recognition of that fact, the Joint Commenters proposed a rule providing that ''when an annual statement for a fiscal year after March 1, 2009 was not provided because it was impracticable for the licensee to provide it'' the copyright owner may demand a statement that confirms with the new statement-of-account regulations. *Id.* Notably, no other commenter opposed the Joint Commenters' proposal.[32]

After carefully weighing the issue, the Office adopts the Joint Commenters' approach. Based on the representation that ''[r]estating several years of monthly statements that have passed without objection would be a massing undertaking serving no useful purpose,'' the final rule does not require the preparation and service of compliant monthly statements of account for periods prior to the effective date of these rules. Joint Commenters Initial Comments at 23. But as suggested by the Joint Commenters, the final rule will allow copyright owners to request annual statements of account for fiscal years ending after March 1, 2009 and before the effective date of this rule, where the copyright owner did not receive any annual statement of account for any reason.[33]

7. Record Retention (AKA Documentation)

In the NPRM, the Office proposed extending the existing regulations that require licensees to retain all records and documents necessary to support information set forth in annual statements of account and monthly statements of account from three years from the date of service to five years from the date of service. 77 FR at 44184–85. The commenters agreed in principle that it would be appropriate to extend the general record retention requirement, though some proposed the Office adopt an even longer mandatory retention period. *See* Joint Commenters Initial Comments at 24; *see also* Gear Publ'g Initial Comments at 18. The final rule adopts the Office's original proposal to extend the retention period from three to five years from the date of service.

The final rule also includes language that requires licensees to retain all records and documents necessary to support information set forth in amended annual statements of account for five years from the date of service of the amended statements. This additional regulation is intended to alleviate the Office's concern, as expressed in the NPRM, regarding the timing of record retention in situations where a licensee files an annual statement of account prior to public performance rates having been set for the time period covered therein. 77 FR at 44185.

8. Harmless Error Provision

The NPRM noted that ''[b]ecause of the detailed requirements in the regulations, licensees' accounting statements may contain inadvertent errors.'' 77 FR at 44185. The Office accordingly sought comment on ''the Office's authority to include a harmless error provisions and whether such a provision in the Statement of Account regulations would be useful as a way to protect licensees from inadvertent errors that do not materially affect the adequacy of the information provided on the Statement of Account.'' *Id.*

The Joint Commenters favored the inclusion of such a provision, essentially for the reasons identified in the NPRM. Joint Commenters Initial Comments at 24–25. Gear Publishing, on the other hand, disagrees with the inclusion of a harmless error provision. They claim that an inquiry into whether an error was harmless ''has the potential to become the focus of many copyright infringement claim.'' *See* Gear Publ'g Initial Comments at 18–19. There was no dispute that the Office possessed the authority to adopt a harmless error rule.

After carefully weighing the comments, the final rule provides that errors in statements of account that do not materially prejudice the rights of a copyright owner shall be deemed harmless and shall not render the account statement invalid or provide a basis for the exercise of remedies under 17 U.S.C. 115(c)(6). As the Office noted, the accounting regulations here require licensees to provide a detailed accounting of their use of the statutory license. Requiring licensees to provide this information serves Congress's goal of protecting copyright owners from ''economic harm from companies which might refuse or fail to pay their just obligations.'' H.R. Rep. No. 94–1476, at 111. But that requirement carries with it the risk that account statements will occasionally contain insubstantial deviations from the strictures of these regulations. It would be unduly severe to treat such inconsequential mistakes as equal to errors that result in material prejudice to the copyright owner.

Indeed, as the NPRM noted, similar considerations led the Register to adopt a harmless error provision as part of the rules governing notices of intention. *See* 37 CFR 201.18(f); 66 FR 45241, 45243 (Aug. 28, 2001). To Gear Publishing's point that adoption of such a rule would be difficult to apply in the context of infringement litigation, our experience with section 201.18(f) belies that concern: The Office is not aware of any difficulties with applying the harmless

[32] In the only other comments the Office received on this aspect of the proposed rule, Gear Publishing urged that the rule had been confusingly drafted. Gear Publ'g Initial Comments at 17. Since the Office is departing substantially from the proposed rule, that comment is moot.

[33] The Joint Commenters' proposal would have required licensees to provide compliant statements for past reporting periods only where ''it was impracticable for the licensee to provide'' the statement earlier. See Joint Commenters Initial Comments, exh. A, at A–22. The final rule does not contain this limitation; if the annual statement was not provided, the reason for that failure is irrelevant.

error rule in the notice of intention context.

9. Confidentiality

In the NPRM, the Office noted that the rates the CRB had originally proposed included provisions that would have restricted a copyright owner's ability to disclose the contents of statements of account received pursuant to Section 115. See 77 FR 29259, 29262, 29267–68 (May 17, 2012) (proposed sections 385.12(f) and 385.22(e)). Specifically, the provisions stated that a ''licensee's statements of account, including any and all information provided by a licensee with respect to the computation of a subminimum, shall be maintained in confidence by any copyright owner, authorized representative or agent that receives it.'' *Id.* at 29262. Accordingly, under the CRB proposal, copyright owners and their authorized representatives or agents could use the statements of account only ''for purposes of reviewing the amounts paid by the licensee and verifying the accuracy of any such payments,'' and for no other purpose. *Id.*

The Office observed in the NPRM that these proposed requirements illustrated a ''general desire among licensees and licensors for maintaining confidentiality of information contained in statements of account,'' but questioned the validity of such a ''broadly framed'' provision. 77 FR at 44185. Accordingly, the Office solicited comments regarding the Office's authority to adopt regulations that would require copyright owners to keep information contained in statements of account confidential, as well as the appropriate limits of any such regulations. *Id.* The Office did not include a confidentiality requirement as part of the proposed rule.

In response to the NPRM, the Joint Commenters urged the Office to either allow the CRB to adopt the confidentiality provision proposed as part of the rates and terms for the statutory license, or to itself adopt an identical provision in the Office's statement-of-account regulations. Joint Commenters Initial Comments at 25–28. Specifically, the Joint Commenters noted that, in the case of percentage-rate usages, the statements of account would reflect ''competitively sensitive'' information like the licensee's overall revenues, royalty payments to record companies and performance rights organizations, and overall usage. *Id.* at 27. Gear Publishing, by contrast, did not believe that a confidentiality provision for a statutorily obtained license should be permitted. It stated: ''There should be no restriction on what a copyright owner does with their own royalty information under a compulsory license. Once again, if a music user wishes to secure confidentiality provisions then they are free to negotiate directly with the copyright owner to achieve such an arrangement.'' Gear Publ'g Initial Comments at 19.

Since the NPRM issued and these comments were received, the Office has further analyzed the confidentiality issue in proceedings outside of, but related to, this rulemaking. On June 25, 2013, the CRB referred a novel material question of substantive law to the Register, inquiring whether the CRB is authorized to adopt regulations imposing a duty of confidentiality upon copyright owners where, like the proposed requirement, the duty is ''included in a voluntarily negotiated license agreement between copyright owners and licensees in a proceeding under section 115 of the Act.'' 78 FR 47421 (Aug. 5, 2013). The Register answered the CRB's question in the negative, finding the CRB lacked the authority under 17 U.S.C. 115(c)(3)(C) to restrict what a copyright owner may do with information in a statement of account after that statement has been prepared and served in accordance with the Office's regulations. *Id.* at 47423. As particularly relevant to this rulemaking, the Register noted that, as a matter of policy, ''government actors should err on the side of transparency'' where transparency ''serves to provide maximum confidence in the law for all who rely upon it, including those who require access to the details of license records.'' *Id.* at 47423. In addition, the Register noted the general legal principle ''that statutory licenses must 'be construed narrowly' '' as applied ''against the rights of copyright owners.'' *Id.* at 47424 (quoting *Fame Publ'g Co.* v. *Ala. Custom Tape, Inc.,* 507 F.2d 667, 670 (5th Cir. 1975)).

These previously announced policy decisions dictate the outcome here. The competitive concerns raised by the Joint Commenters are insufficient to overcome the strong policy that ''in the context of statutory licenses, government actors should err on the side of transparency.'' 78 FR at 47423. Thus, the Office concludes that once the statements of account have been delivered to the copyright owners, there should be no restrictions on the copyright owners' ability to use the statements or disclose their contents.

Indeed, an examination of the Joint Commenters' sweeping confidentiality proposal only buttresses that conclusion. The proposal would have restricted not only the *disclosure* of the statements of account, but also the permissible *uses* of those statements. 77 FR at 29262 (providing that the statements can only be used ''for purposes of reviewing the amounts paid by the licensee and verifying the accuracy of any such payments''). As written, the proposal would also have barred copyright owners from disclosing the contents of the statements of account to other parties who were downstream beneficiaries of the statutory royalties (such as songwriters entitled to receive a share of the royalties as part of their publishing contracts). And, most troublingly, the Joint Commenters' proposal would have burdened copyright owners' ability to disclose to the public the royalties they received under the statutory license. The Office is particularly reluctant to so drastically restrict copyright owners' ability to freely discuss the effects of government policy.

List of Subjects

37 CFR Part 201

Copyright.

37 CFR Part 210

Copyright, Phonorecords, Recordings.

Final Regulations

For the reasons set forth in the preamble, the U.S. Copyright Office amends 37 CFR part 201 and adds part 210 as follows:

PART 201—GENERAL PROVISIONS

■ 1. The authority citation for part 201 continues to read as follows:

Authority: 17 U.S.C. 702.

■ 2. Revise paragraph (b) of § 201.18, to read as follows:

§ 201.18 Notice of intention to obtain a compulsory license for making and distributing phonorecords of nondramatic musical works.

* * * * *

(b) *Agent.* An agent who has been authorized to accept Notices of Intention in accordance with paragraph (a)(4) of this section and who has received a Notice of Intention on behalf of a copyright owner shall provide within two weeks of the receipt of that Notice of Intention the name and address of the copyright owner or its agent upon whom the person or entity intending to obtain the compulsory license shall serve Statements of Account and the monthly royalty in accordance with § 210.11(e) of this chapter.

* * * * *

§ 201.19 [Removed and reserved]

■ 3. Remove and reserve § 201.19.

■ 4. Add part 210 to read as follows:

PART 210—COMPULSORY LICENSE FOR MAKING AND DISTRIBUTING PHYSICAL AND DIGITAL PHONORECORDS OF NONDRAMATIC MUSICAL WORKS

Subpart A—[Reserved]

Sec.
210.1–210.10 [Reserved]

Subpart B—Royalties and Statements of Account Under Compulsory License

210.11 General.
210.12 Definitions.
210.13 Accounting requirements where sales revenue is ''recognized.''
210.14 Accounting requirements for offsetting phonorecord reserves with returned phonorecords.
210.15 Situations in which a compulsory licensee is barred from maintaining reserves.
210.16 Monthly statements of account.
210.17 Annual statements of account.
210.18 Documentation.
210.19 Harmless errors.

Authority: 17 U.S.C. 115, 702.

Subpart A—[Reserved]

§§ 210.1–210.10 [Reserved]

Subpart B—Royalties and Statements of Account Under Compulsory License

§ 210.11 General.

This subpart prescribes rules for the payment of royalties and the preparation and service of statements of account under the compulsory license for the making and distribution of phonorecords of nondramatic musical works, including by means of a digital phonorecord delivery, pursuant to 17 U.S.C. 115 and the rates and terms in part 385 of this title.

§ 210.12 Definitions.

As used in this subpart:

(a) A *Monthly Statement of Account* or *Monthly Statement* is a statement accompanying monthly royalty payments identified in 17 U.S.C. 115(c)(5), and required by that section to be filed under the compulsory license to make and distribute phonorecords of nondramatic musical works, including by means of a digital phonorecord delivery.

(b) An *Annual Statement of Account* or *Annual Statement* is a statement identified in 17 U.S.C 115(c)(5), and required by that section to be filed under the compulsory license to make and distribute phonorecords of nondramatic musical works, including by means of a digital phonorecord delivery. Such term, when used in this rule, includes an Amended Annual Statement of Account filed pursuant to § 210.17(d)(2)(iii).

(c) A *digital phonorecord delivery* is each individual delivery of a phonorecord by digital transmission of a sound recording which results in a specifically identifiable reproduction by or for any transmission recipient of a phonorecord of that sound recording, regardless of whether the digital transmission is also a public performance of the sound recording or any nondramatic musical work embodied therein. The reproduction of the phonorecord must be sufficiently permanent or stable to permit it to be perceived, reproduced, or otherwise communicated for a period of more than transitory duration. Such a phonorecord may be permanent or it may be made available to the transmission recipient for a limited period of time or for a specified number of performances. A digital phonorecord delivery includes all phonorecords that are made for the purpose of making the digital phonorecord delivery. A digital phonorecord delivery does not include any transmission that did not result in a specifically identifiable reproduction of the entire product being transmitted, and for which the distributor did not charge, or fully refunded, any monies that would otherwise be due for the relevant transmission.

(d) *Ringtone* shall have the meaning given in § 385.2 of this title.

(e) The term *copyright owner,* in the case of any work having more than one copyright owner, means any one of the co-owners.

(f) A *compulsory licensee* is a person or entity exercising the compulsory license to make and distribute phonorecords of nondramatic musical works as provided under 17 U.S.C. 115, including by means of a digital phonorecord delivery.

(g) A phonorecord is considered *distributed* if the compulsory licensee has voluntarily and permanently parted with possession of the phonorecord, which shall occur as follows:

(1) In the case of physical phonorecords relinquished from possession for purposes other than sale, at the time at which the compulsory licensee actually first parts with possession;

(2) In the case of physical phonorecords relinquished from possession for purposes of sale without a privilege of returning unsold phonorecords for credit or exchange, at the time at which the compulsory licensee actually first parts with possession;

(3) In the case of physical phonorecords relinquished from possession for purposes of sale accompanied by a privilege of returning unsold phonorecords for credit or exchange:

(i) At the time when revenue from a sale of the phonorecord is ''recognized'' by the compulsory licensee; or

(ii) Nine months from the month in which the compulsory licensee actually first parted with possession, whichever occurs first. For these purposes, a compulsory licensee shall be considered to ''recognize'' revenue from the sale of a phonorecord when sales revenue would be recognized in accordance with GAAP.

(4) In the case of a digital phonorecord delivery, on the date that the phonorecord is digitally transmitted.

(h) A *phonorecord reserve* comprises the number of phonorecords made under a particular compulsory license, if any, that have been relinquished from possession for purposes of sale in a given month accompanied by a privilege of return, as described in paragraph (g)(3) of this section, and that have not been considered distributed during the month in which the compulsory licensee actually first parted with their possession. The initial number of phonorecords comprising a phonorecord reserve shall be determined in accordance with GAAP.

(i) A *negative reserve balance* comprises the aggregate number of phonorecords made under a particular compulsory license, if any, that have been relinquished from possession for purposes of sale accompanied by a privilege of return, as described in paragraph (g)(3) of this section, and that have been returned to the compulsory licensee, but because all available phonorecord reserves have been eliminated, have not been used to reduce a phonorecord reserve.

(j) *GAAP* means U.S. Generally Accepted Accounting Principles, except that if the U.S. Securities and Exchange Commission permits or requires entities with securities that are publicly traded in the U.S. to employ International Financial Reporting Standards, as issued by the International Accounting Standards Board, or as accepted by the Securities and Exchange Commission if different from that issued by the International Accounting Standards Board, in lieu of Generally Accepted Accounting Principles, then an entity may employ International Financial Reporting Standards as ''GAAP'' for purposes of this subpart.

§ 210.13 Accounting requirements where sales revenue is ''recognized.''

Where under § 210.12(g)(3)(i), revenue from the sale of phonorecords is ''recognized'' during any month after the month in which the compulsory

licensee actually first parted with their possession, said compulsory licensee shall reduce particular phonorecord reserves by the number of phonorecords for which revenue is being ''recognized,'' as follows:

(a) If the number of phonorecords for which revenue is being ''recognized'' is smaller than the number of phonorecords comprising the earliest eligible phonorecord reserve, this phonorecord reserve shall be reduced by the number of phonorecords for which revenue is being ''recognized.'' Subject to the time limitations of § 210.12(g)(3)(ii), the number of phonorecords remaining in this reserve shall be available for use in subsequent months.

(b) If the number of phonorecords for which revenue is being ''recognized'' is greater than the number of phonorecords comprising the earliest eligible phonorecord reserve but less than the total number of phonorecords comprising all eligible phonorecord reserves, the compulsory licensee shall first eliminate those phonorecord reserves, beginning with the earliest eligible phonorecord reserve and continuing to the next succeeding phonorecord reserves, that are completely offset by phonorecords for which revenue is being ''recognized.'' Said compulsory licensee shall then reduce the next succeeding phonorecord reserve by the number of phonorecords for which revenue is being ''recognized'' that have not been used to eliminate a phonorecord reserve. Subject to the time limitations of § 210.12(g)(3)(ii), the number of phonorecords remaining in this reserve shall be available for use in subsequent months.

(c) If the number of phonorecords for which revenue is being ''recognized'' equals the number of phonorecords comprising all eligible phonorecord reserves, the person or entity exercising the compulsory license shall eliminate all of the phonorecord reserves.

(d) Digital phonorecord deliveries shall not be considered as accompanied by a privilege of return as described in § 210.12(g)(3), and the compulsory licensee shall not take digital phonorecord deliveries into account in establishing phonorecord reserves.

§ 210.14 Accounting requirements for offsetting phonorecord reserves with returned phonorecords.

(a) In the case of a phonorecord that has been relinquished from possession for purposes of sale accompanied by a privilege of return, as described in § 210.12(g)(3), where the phonorecord is returned to the compulsory licensee for credit or exchange before said compulsory licensee is considered to have ''voluntarily and permanently parted with possession'' of the phonorecord as described in § 210.12(g), the compulsory licensee may use such phonorecord to reduce a ''phonorecord reserve,'' as defined in § 210.12(h).

(b) In such cases, the compulsory licensee shall reduce particular phonorecord reserves by the number of phonorecords that are returned during the month covered by the Monthly Statement of Account in the following manner:

(1) If the number of phonorecords that are returned during the month covered by the Monthly Statement is smaller than the number comprising the earliest eligible phonorecord reserve, the compulsory licensee shall reduce this phonorecord reserve by the total number of returned phonorecords. Subject to the time limitations in § 210.12(g)(3)(ii), the number of phonorecords remaining in this reserve shall be available for use in subsequent months.

(2) If the number of phonorecords that are returned during the month covered by the Monthly Statement is greater than the number of phonorecords comprising the earliest eligible phonorecord reserve but less than the total number of phonorecords comprising all eligible phonorecord reserves, the compulsory licensee shall first eliminate those phonorecord reserves, beginning with the earliest eligible phonorecord reserve, and continuing to the next succeeding phonorecord reserves, that are completely offset by returned phonorecords. Said compulsory licensee shall then reduce the next succeeding phonorecord reserve by the number of returned phonorecords that have not been used to eliminate a phonorecord reserve. Subject to the time limitations in § 210.12(g)(3)(ii), the number of phonorecords remaining in this reserve shall be available for use in subsequent months.

(3) If the number of phonorecords that are returned during the month covered by the Monthly Statement is equal to or is greater than the total number of phonorecords comprising all eligible phonorecord reserves, the compulsory licensee shall eliminate all eligible phonorecord reserves. Where said number is greater than the total number of phonorecords comprising all eligible phonorecord reserves, said compulsory licensee shall establish a ''negative reserve balance,'' as defined in § 210.12(i).

(c) Except where a negative reserve balance exists, a separate and distinct phonorecord reserve shall be established for each month during which the compulsory licensee relinquishes phonorecords from possession for purposes of sale accompanied by a privilege of return, as described in § 210.12(g)(3). In accordance with § 210.12(g)(3)(ii), any phonorecord remaining in a particular phonorecord reserve nine months from the month in which the particular reserve was established shall be considered ''distributed''; at that point, the particular monthly phonorecord reserve shall lapse and royalties for the phonorecords remaining in it shall be paid as provided in § 210.16(d)(2).

(d) Where a negative reserve balance exists, the aggregate total of phonorecords comprising it shall be accumulated into a single balance rather than being separated into distinct monthly balances. Following the establishment of a negative reserve balance, any phonorecords relinquished from possession by the compulsory licensee for purposes of sale or otherwise, shall be credited against such negative balance, and the negative reserve balance shall be reduced accordingly. Digital phonorecord deliveries may be credited against such negative reserve balance, but only if such digital phonorecord deliveries have the same royalty rate as physical phonorecords under part 385 of this title. The nine-month limit provided in § 210.12(g)(3)(ii) shall have no effect upon a negative reserve balance; where a negative reserve balance exists, relinquishment from possession of a phonorecord by the compulsory licensee at any time shall be used to reduce such balance, and such phonorecord shall not be considered ''distributed'' within the meaning of § 210.12(g).

(e) In no case shall a phonorecord reserve be established while a negative reserve balance is in existence; conversely, in no case shall a negative reserve balance be established before all available phonorecord reserves have been eliminated.

§ 210.15 Situations in which a compulsory licensee is barred from maintaining reserves.

Notwithstanding any other provisions of this section, in any case where, within three years before the phonorecord was relinquished from possession, the compulsory licensee has had final judgment entered against it for failure to pay royalties for the reproduction of copyrighted music on phonorecords, or within such period has been definitively found in any proceeding involving bankruptcy, insolvency, receivership, assignment for

the benefit of creditors, or similar action, to have failed to pay such royalties, that compulsory licensee shall be considered to have ''Permanently parted with possession'' of a phonorecord made under the license at the time at which that compulsory licensee actually first parts with possession. For these purposes the compulsory licensee shall include:

(a) In the case of any corporation, the corporation or any director, officer, or beneficial owner of twenty-five percent (25%) or more of the outstanding securities of the corporation;

(b) In all other cases, any entity or individual owning a beneficial interest of twenty-five percent (25%) or more in the entity exercising the compulsory license.

§ 210.16 Monthly statements of account.

(a) *Forms.* The Copyright Office does not provide printed forms for the use of persons serving Monthly Statements of Account.

(b) *General content.* A Monthly Statement of Account shall be clearly and prominently identified as a ''Monthly Statement of Account Under Compulsory License for Making and Distributing Phonorecords,'' and shall include a clear statement of the following information:

(1) The period (month and year) covered by the Monthly Statement.

(2) The full legal name of the compulsory licensee, together with all fictitious or assumed names used by such person or entity for the purpose of conducting the business of making and distributing phonorecords.

(3) The full address, including a specific number and street name or rural route, of the place of business of the compulsory licensee. A post office box or similar designation will not be sufficient for this purpose, except where it is the only address that can be used in that geographic location.

(4) For each nondramatic musical work that is owned by the same copyright owner being served with the Monthly Statement and that is embodied in phonorecords covered by the compulsory license, a detailed statement of all of the information called for in paragraph (c) of this section.

(5) The total royalty payable to the relevant copyright owner for the month covered by the Monthly Statement, computed in accordance with the requirements of this section and the formula specified in paragraph (d) of this section, including detailed information regarding how the royalty was computed.

(6) The amount of late fees, if applicable, included in the payment associated with the Monthly Statement.

(7) In any case where the compulsory licensee falls within the provisions of § 210.15, a clear description of the action or proceeding involved, including the date of the final judgment or definitive finding described in that section.

(8) Detailed instructions on how to request records of any promotional uses of the copyright owner's works that are required to be maintained or provided under § 385.14 or § 385.24 of this title, or other applicable provision, including, where applicable, records required to be maintained or provided by any third parties that were authorized by the compulsory licensee to engage in promotional uses during any part of the month. If this information is provided, Monthly Statements need not reflect phonorecords subject to the promotional royalty rate provided in § 385.14 or § 385.24 of this title, or any similar promotional royalty rate of zero that may be provided in part 385 of this title.

(c) *Specific content of monthly statements*—(1) *Accounting of phonorecords subject to a cents rate royalty structure.* The information called for by paragraph (b)(4) of this section shall, with respect to each nondramatic musical work as to which the compulsory licensee has made and distributed phonorecords subject to part 385, subpart A of this title or any other provisions requiring computation of applicable royalties on a cents-per-unit basis, include a separate listing of each of the following items of information:

(i) The number of phonorecords made during the month covered by the Monthly Statement.

(ii) The number of phonorecords that, during the month covered by the Monthly Statement and regardless of when made, were either:

(A) Relinquished from possession for purposes other than sale;

(B) Relinquished from possession for purposes of sale without any privilege of returning unsold phonorecords for credit or exchange;

(C) Relinquished from possession for purposes of sale accompanied by a privilege of returning unsold phonorecords for credit or exchange;

(D) Returned to the compulsory licensee for credit or exchange; or

(E) Placed in a phonorecord reserve (except that if a negative reserve balance exists give either the number of phonorecords added to the negative reserve balance, or the number of phonorecords relinquished from possession that have been used to reduce the negative reserve balance).

(iii) The number of phonorecords, regardless of when made, that were relinquished from possession during a month earlier than the month covered by the Monthly Statement but that, during the month covered by the Monthly Statement either have had revenue from their sale ''recognized'' under § 210.12(g)(3)(i), or were comprised in a phonorecord reserve that lapsed after nine months under § 210.12(g)(3)(ii).

(iv) The per unit statutory royalty rate applicable to the relevant configuration; and

(v) The total royalty payable for the month covered by the Monthly Statement (*i.e.,* the result in paragraph (d)(2)(v) of this section) for the item described by the set of information called for, and broken down as required, by paragraph (c)(1) of this section.

(vi) The phonorecord identification information required by paragraph (a)(3) of this section.

(2) *Accounting of phonorecords subject to a percentage rate royalty structure.* The information called for by paragraph (b)(4) of this section shall, with respect to each nondramatic musical work as to which the compulsory licensee has made and distributed phonorecords subject to part 385, subparts B or C of this title, or any other provisions requiring computation of applicable royalties on a percentage-rate basis, include a detailed and step-by-step accounting of the calculation of royalties under § 385.12, § 385.22, or other provisions of part 385 of this title as applicable, sufficient to allow the copyright owner to assess the manner in which the licensee determined the royalty owed and the accuracy of the royalty calculations, including but not limited to the following information:

(i) The number of plays, constructive plays, or other payable units, of the relevant sound recording for the month covered by the Monthly Statement for the relevant offering.

(ii) The total royalty payable for the month for the item described by the set of information called for, and broken down as required, by paragraph (c)(3) of this section (*i.e.,* the per-work royalty allocation for the relevant sound recording and offering).

(iii) The phonorecord identification information required by paragraph (c)(3) of this section.

(3) *Identification of phonorecords in monthly statements.* The information required by this paragraph shall include, and if necessary shall be broken down to identify separately, the following:

(i) The title of the nondramatic musical work subject to compulsory license.

(ii) A reference number or code identifying the relevant Notice of Intention, if the compulsory licensee chose to include such a number or code on its relevant Notice of Intention for the compulsory license.

(iii) The International Standard Recording Code (ISRC) associated with the relevant sound recording, if known, and at least one of the following, as applicable and available for tracking sales and/or usage:

(A) The catalog number or numbers and label name or names, associated with the phonorecords;

(B) The Universal Product Code (UPC) or similar code used on or associated with the phonorecords; or

(C) The sound recording identification number assigned by the compulsory licensee or a third-party distributor to the relevant sound recording.

(iv) The names of the principal recording artist or group engaged in rendering the performances fixed on the phonorecords.

(v) The playing time of the relevant sound recording, except that playing time is not required in the case of ringtones or licensed activity to which no overtime adjustment is applicable.

(vi) If the compulsory licensee chooses to allocate its payment between co-owners of the copyright in the nondramatic musical work, as described in paragraph (g)(1) of this section, and thus pays the copyright owner (or agent) receiving the statement less than one hundred percent of the applicable royalty, the percentage share paid.

(vii) The names of the writer or writers of the nondramatic musical work, or the International Standard Name Identifiers (ISNIs) or other unique identifier of the writer or writers, if known.

(viii) The International Standard Musical Work Code (ISWC) or other unique identifier for the nondramatic musical work, if known.

(ix) Identification of the relevant phonorecord configuration (for example: compact disc, permanent digital download, ringtone) or offering (for example: limited download, music bundle) for which the royalty was calculated, including, if applicable and except for physical phonorecords, the name of the third-party distributor of the configuration or offering.

(d) *Royalty payment and accounting*—(1) *In general.* The total royalty called for by paragraph (b)(5) of this section shall be computed so as to include every phonorecord ''distributed'' during the month covered by the Monthly Statement.

(2) *Phonorecords subject to a cents rate royalty structure.* For phonorecords subject to part 385, subpart A of this title, or any other applicable royalties computed on a cents-per-unit basis, the amount of the royalty payment shall be calculated as follows:

(i) *Step 1: Compute the number of phonorecords shipped for sale with a privilege of return.* This is the total of phonorecords that, during the month covered by the Monthly Statement, were relinquished from possession by the compulsory licensee, accompanied by the privilege of returning unsold phonorecords to the compulsory licensee for credit or exchange. This total does not include:

(A) Any phonorecords relinquished from possession by the compulsory licensee for purposes of sale without the privilege of return; and

(B) Any phonorecords relinquished from possession for purposes other than sale.

(ii) *Step 2: Subtract the number of phonorecords reserved.* This involves deducting, from the subtotal arrived at in Step 1, the number of phonorecords that have been placed in the phonorecord reserve for the month covered by the Monthly Statement. The number of phonorecords reserved is determined by multiplying the subtotal from Step 1 by the percentage reserve level established under GAAP. This step should be skipped by a compulsory licensee barred from maintaining reserves under § 210.15.

(iii) *Step 3: Add the total of all phonorecords that were shipped during the month and were not counted in Step 1.* This total is the sum of two figures:

(A) The number of phonorecords that, during the month covered by the Monthly Statement, were relinquished from possession by the compulsory licensee for purposes of sale, without the privilege of returning unsold phonorecords to the compulsory licensee for credit or exchange; and

(B) The number of phonorecords relinquished from possession by the compulsory licensee, during the month covered by the Monthly Statement, for purposes other than sale.

(iv) *Step 4: Make any necessary adjustments for sales revenue ''recognized,'' lapsed reserves, or reduction of negative reserve balance during the month.* If necessary, this step involves adding to or subtracting from the subtotal arrived at in Step 3 on the basis of three possible types of adjustments:

(A) *Sales revenue ''recognized.''* If, in the month covered by the Monthly Statement, the compulsory licensee ''recognized'' revenue from the sale of phonorecords that had been relinquished from possession in an earlier month, the number of such phonorecords is *added* to the Step 3 subtotal.

(B) *Lapsed reserves.* If, in the month covered by the Monthly Statement, there are any phonorecords remaining in the phonorecord reserve for the ninth previous month (that is, any phonorecord reserves from the ninth previous month that have not been offset under FOFI, the first-out-first-in accounting convention, by actual returns during the intervening months), the reserve lapses and the number of phonorecords in it is added to the Step 3 subtotal.

(C) *Reduction of negative reserve balance.* If, in the month covered by the Monthly Statement, the aggregate reserve balance for all previous months is a negative amount, the number of phonorecords relinquished from possession by the compulsory licensee during that month and used to reduce the negative reserve balance is subtracted from the Step 3 subtotal.

(v) *Step 5: Multiply by the statutory royalty rate.* The total monthly royalty payment is obtained by multiplying the subtotal from Step 3, as adjusted if necessary by Step 4, by the statutory royalty rate set forth in § 385.3 or other provisions of part 385 of this title as applicable.

(3) *Phonorecords subject to a percentage rate royalty structure.* For phonorecords subject to part 385, subparts B or C of this title, or any other applicable royalties computed on a percentage-rate basis, the amount of the royalty payment shall be calculated as provided in § 385.12, § 385.22, or other provisions of part 385 of this title as applicable. The calculations shall be made in good faith and on the basis of the best knowledge, information, and belief of the licensee at the time payment is due, and subject to the additional accounting and certification requirements of 17 U.S.C. 115(c)(5) and this section. The following additional provisions shall also apply:

(i) A licensee may, in cases where the final public performance royalty has not yet been determined, compute the public performance royalty component based on the interim public performance royalty rate, if established; or alternatively, on a reasonable estimation of the expected royalties to be paid in accordance with GAAP. Royalty payments based on anticipated payments or interim public performance royalty rates must be reconciled on the Annual Statement of Account, or by

complying with § 210.17(d)(2)(iii) governing Amended Annual Statements of Account.

(ii) When calculating the per-work royalty allocation for each work, as described in § 385.12(b)(4), § 385.22(b)(3), or any similar provisions of part 385 of this title as applicable, an actual or constructive per-play allocation is to be calculated to at least the hundredth of a cent (*i.e.,* to at least four decimal places).

(e) *Clear statements.* The information required by paragraphs (b) and (c) of this section requires intelligible, legible, and unambiguous statements in the Monthly Statements of Account without incorporation of facts or information contained in other documents or records.

(f) *Certification.* (1) Each Monthly Statement of Account shall be accompanied by:

(i) The printed or typewritten name of the person who is signing and certifying the Monthly Statement of Account.

(ii) A signature, which in the case of a compulsory licensee that is a corporation or partnership, shall be the signature of a duly authorized officer of the corporation or of a partner.

(iii) The date of signature and certification.

(iv) If the compulsory licensee is a corporation or partnership, the title or official position held in the partnership or corporation by the person who is signing and certifying the Monthly Statement of Account.

(v) One of the following statements:

(A) I certify that (1) I am duly authorized to sign this Monthly Statement of Account on behalf of the compulsory licensee; (2) I have examined this Monthly Statement of Account; and (3) all statements of fact contained herein are true, complete, and correct to the best of my knowledge, information, and belief, and are made in good faith; or

(B) I certify that (1) I am duly authorized to sign this Monthly Statement of Account on behalf of the compulsory licensee, (2) I have prepared or supervised the preparation of the data used by the compulsory licensee and/or its agent to generate this Monthly Statement of Account, (3) such data is true, complete, and correct to the best of my knowledge, information, and belief, and was prepared in good faith, and (4) this Monthly Statement of Account was prepared by the compulsory licensee and/or its agent using processes and internal controls that were subject to an examination, during the past year, by a licensed Certified Public Accountant in accordance with the attestation standards established by the American Institute of Certified Public Accountants, the opinion of whom was that the processes and internal controls were suitably designed to generate monthly statements that accurately reflect, in all material respects, the compulsory licensee's usage of musical works, the statutory royalties applicable thereto, and any other data that is necessary for the proper calculation of the statutory royalties in accordance with 17 U.S.C. 115 and applicable regulations.

(2) If the Monthly Statement of Account is served by mail or by reputable courier service, certification of the Monthly Statement of Account by the compulsory licensee shall be made by handwritten signature. If the Monthly Statement of Account is served electronically, certification of the Monthly Statement of Account by the compulsory licensee shall be made by electronic signature as defined in section 7006(5) of title 15 of the United States Code.

(g) *Service.* (1) The service of a Monthly Statement of Account on a copyright owner under this subpart may be accomplished by means of service on either the copyright owner or an agent of the copyright owner with authority to receive Statements of Account on behalf of the copyright owner. In the case where the work has more than one copyright owner, the service of a Statement of Account on at least one co-owner or upon an agent of at least one of the co-owners shall be sufficient with respect to all co-owners. The compulsory licensee may choose to allocate its payment between co-owners. In such a case the compulsory licensee shall provide each co-owner (or its agent) a Monthly Statement reflecting the percentage share paid to that co-owner. Each Monthly Statement of Account shall be served on the copyright owner or the agent to whom or which it is directed by mail, by reputable courier service, or by electronic delivery as set forth in paragraph (g)(2) of this section on or before the 20th day of the immediately succeeding month. The royalty payment for a month also shall be served on or before the 20th day of the immediately succeeding month. The Monthly Statement and payment may be sent together or separately, but if sent separately, the payment must include information reasonably sufficient to allow the payee to match the Monthly Statement to the payment. However, in the case where the compulsory licensee has served its Notice of Intention upon an agent of the copyright owner pursuant to § 201.18 of this chapter, the compulsory licensee is not required to serve Monthly Statements of Account or make any royalty payments until the compulsory licensee receives from the agent with authority to receive the Notice of Intention notice of the name and address of the copyright owner or its agent upon whom the compulsory licensee shall serve Monthly Statements of Account and the monthly royalty fees. Upon receipt of this information, the compulsory licensee shall serve Monthly Statements of Account and all royalty fees covering the intervening period upon the person or entity identified by the agent with authority to receive the Notice of Intention by or before the 20th day of the month following receipt of the notification. It shall not be necessary to file a copy of the Monthly Statement in the Copyright Office.

(2) A copyright owner or authorized agent may send a licensee a demand that Monthly Statements of Account be submitted in a readily accessible electronic format consistent with prevailing industry practices applicable to comparable electronic delivery of comparable financial information.

(3) When a compulsory licensee receives a request to deliver or make available Monthly Statements of Account in electronic form, or a request to revert back to service by mail or reputable courier service, the compulsory licensee shall make such a change effective with the first accounting period ending at least 30 days after the compulsory licensee's receipt of the request and any information (such as a postal or email address, as the case may be) that is necessary for the compulsory licensee to make the change.

(4)(i) In any case where a Monthly Statement of Account is sent by mail or reputable courier service and the Monthly Statement of Account is returned to the sender because the copyright owner or agent is no longer located at that address or has refused to accept delivery, or the Monthly Statement of Account is sent by electronic mail and is undeliverable, or in any case where an address for the copyright owner is not known, the Monthly Statement of Account, together with any evidence of mailing or attempted delivery by courier service or electronic mail, may be filed in the Licensing Division of the Copyright Office. Any Monthly Statement of Account submitted for filing in the Copyright Office shall be accompanied by a brief statement of the reason why it was not served on the copyright owner. A written acknowledgment of receipt and filing will be provided to the sender.

(ii) The Copyright Office will not accept any royalty fees submitted with Monthly Statements of Account under this section.

(iii) Neither the filing of a Monthly Statement of Account in the Copyright Office, nor the failure to file such Monthly Statement, shall have effect other than that which may be attributed to it by a court of competent jurisdiction.

(iv) No filing fee will be required in the case of Monthly Statements of Account submitted to the Copyright Office under this section. Upon request and payment of the fee specified in § 201.3(e) of this chapter, a Certificate of Filing will be provided to the sender.

(5) Subject to paragraph (g)(6) of this section, a separate Monthly Statement of Account shall be served for each month during which there is any activity relevant to the payment of royalties under 17 U.S.C. 115. The Annual Statement of Account described in § 210.17 of this subpart does not replace any Monthly Statement of Account.

(6) Royalties under 17 U.S.C. 115 shall not be considered payable, and no Monthly Statement of Account shall be required, until the compulsory licensee's cumulative unpaid royalties for the copyright owner equal at least one cent. Moreover, in any case in which the cumulative unpaid royalties under 17 U.S.C. 115 that would otherwise be payable by the compulsory licensee to the copyright owner are less than $5, and the copyright owner has not notified the compulsory licensee in writing that it wishes to receive Monthly Statements of Account reflecting payments of less than $5, the compulsory licensee may choose to defer the payment date for such royalties and provide no Monthly Statements of Account until the earlier of the time for rendering the Monthly Statement of Account for the month in which the compulsory licensee's cumulative unpaid royalties under section 17 U.S.C. 115 for the copyright owner exceed $5 or the time for rendering the Annual Statement of Account, at which time the compulsory licensee may provide one statement and payment covering the entire period for which royalty payments were deferred.

(7) If the compulsory licensee is required, under applicable tax law and regulations, to make backup withholding from its payments required hereunder, the compulsory licensee shall indicate the amount of such withholding on the Monthly Statement or on or with the payment.

(8) If a Monthly Statement of Account is sent by certified mail or registered mail, a mailing receipt shall be sufficient to prove that service was timely. If a Monthly Statement of Account is sent by a reputable courier, documentation from the courier showing the first date of attempted delivery shall be sufficient to prove that service was timely. If a Monthly Statement of Account or a link thereto is sent by electronic mail, a return receipt shall be sufficient to prove that service was timely. In the absence of the foregoing, the compulsory licensee shall bear the burden of proving that the Monthly Statement of Account was served in a timely manner.

§ 210.17 Annual statements of account.

(a) *Forms.* The Copyright Office does not provide printed forms for the use of persons serving Annual Statements of Account.

(b) *Annual period.* Any Annual Statement of Account shall cover the full fiscal year of the compulsory licensee.

(c) *General content.* An Annual Statement of Account shall be clearly and prominently identified as an ''Annual Statement of Account Under Compulsory License for Making and Distributing Phonorecords,'' and shall include a clear statement of the following information:

(1) The fiscal year covered by the Annual Statement of Account.

(2) The full legal name of the compulsory licensee, together with all fictitious or assumed names used by such person or entity for the purpose of conducting the business of making and distributing phonorecords.

(3) If the compulsory licensee is a business organization, the name and title of the chief executive officer, managing partner, sole proprietor or other person similarly responsible for the management of such entity.

(4) The full address, including a specific number and street name or rural route, or the place of business of the compulsory licensee (a post office box or similar designation will not be sufficient for this purpose except where it is the only address that can be used in that geographic location).

(5) For each nondramatic musical work that is owned by the same copyright owner being served with the Annual Statement and that is embodied in phonorecords covered by the compulsory license, a detailed statement of all of the information called for in paragraph (d) of this section.

(6) The total royalty payable for the fiscal year covered by the Annual Statement computed in accordance with the requirements of § 210.16, and, in the case of offerings for which royalties are calculated pursuant to part 385, subparts B or C of this title, or any other provision requiring computation of applicable royalties on a percentage-rate basis, calculations showing in detail how the royalty was computed (for these purposes, the applicable royalty as specified in part 385, subpart A of this title shall be payable for every phonorecord ''distributed'' during the fiscal year covered by the Annual Statement).

(7) The total sum paid under Monthly Statements of Account by the compulsory licensee to the copyright owner being served with the Annual Statement during the fiscal year covered by the Annual Statement.

(8) In any case where the compulsory license falls within the provisions of § 210.15, a clear description of the action or proceeding involved, including the date of the final judgment or definitive finding described in that section.

(9) Any late fees, if applicable, included in any payment associated with the Annual Statement.

(d) *Specific content of annual statements*—(1) *Accounting of phonorecords subject to a cents rate royalty structure.* The information called for by paragraph (c)(5) of this section shall, with respect to each nondramatic musical work as to which the compulsory licensee has made and distributed phonorecords subject to part 385, subpart A of this title, or any other provision requiring computation of applicable royalties on a cents-per-unit basis, include a separate listing of each of the following items of information:

(i) The number of phonorecords made through the end of the fiscal year covered by the Annual Statement, including any made during earlier years.

(ii) The number of phonorecords which have never been relinquished from possession of the compulsory licensee through the end of the fiscal year covered by the Annual Statement.

(iii) The number of phonorecords involuntarily relinquished from possession (as through fire or theft) of the compulsory licensee during the fiscal year covered by the Annual Statement and any earlier years, together with a description of the facts of such involuntary relinquishment.

(iv) The number of phonorecords ''distributed'' by the compulsory licensee during all years before the fiscal year covered by the Annual Statement.

(v) The number of phonorecords relinquished from possession of the compulsory licensee for purposes of sale during the fiscal year covered by the Annual Statement accompanied by a

privilege of returning unsold records for credit or exchange, but not ''distributed'' by the end of that year.

(vi) The number of phonorecords ''distributed'' by the compulsory licensee during the fiscal year covered by the Annual Statement.

(vii) The per unit statutory royalty rate applicable to the relevant configuration.

(viii) The total royalty payable for the fiscal year covered by the Annual Statement for the item described by the set of information called for, and broken down as required, by this paragraph (d)(1).

(ix) The phonorecord identification information required by paragraph (d)(3) of this section.

(2) *Accounting of phonorecords subject to a percentage rate royalty structure.* (i) The information called for by paragraph (c)(5) of this section shall identify each offering for which royalties are to be calculated separately and, with respect to each nondramatic musical work as to which the compulsory licensee has made and distributed phonorecords subject to part 385, subparts B or C of this title, or any other provision requiring computation of applicable royalties on a percentage-rate basis, include the number of plays, constructive plays, or other payable units during the fiscal year covered by the Annual Statement, together with, and which if necessary shall be broken down to identify separately, the following:

(A) The total royalty payable for the fiscal year for the item described by the set of information called for, and broken down as required, by paragraph (d)(3) of this section (*i.e.,* the per-work royalty allocation for the relevant sound recording and offering).

(B) The phonorecord identification information required by paragraph (d)(3) of this section.

(ii) If the information given under paragraph (d)(2)(i) of this section does not reconcile, the Annual Statement shall also include a clear and detailed explanation of the difference.

(iii) In any case where a licensee serves an Annual Statement of Account based on anticipated payments or interim public performance royalty rates prior to the final determination of final public performance royalties for all musical works used by the service in the relevant fiscal year, the licensee shall serve an Amended Annual Statement of Account within six months from the date such public performance royalties have been established. The Amended Annual Statement of Account shall recalculate the royalty fees reported on the relevant Annual Statement of Account to adjust for any change to the public performance rate used to calculate the royalties reported. Service shall be made in accordance with paragraph (g) of this section. Certification of the Amended Annual Statement shall be made in accordance with paragraph (f) of this section, except that the CPA examination under paragraph (f)(2) of this section may be limited to the licensee's recalculation of royalty fees in accordance with this paragraph.

(3) *Identification of phonorecords in annual statements.* The information required by this paragraph shall include, and if necessary shall be broken down to identify separately, the following:

(i) The title of the nondramatic musical work subject to compulsory license.

(ii) A reference number or code identifying the relevant Notice of Intention, if the compulsory licensee chose to include such a number or code on its relevant Notice of Intention for the compulsory license.

(iii) The International Standard Recording Code (ISRC) associated with the relevant sound recording, if known; and at least one of the following, as applicable and available for tracking sales and/or usage:

(A) The catalog number or numbers and label name or names, used on or associated with the phonorecords;

(B) The Universal Product Code (UPC) or similar code used on or associated with the phonorecords; or

(C) The sound recording identification number assigned by the compulsory licensee or a third-party distributor to the relevant sound recording;

(iv) The names of the principal recording artist or group engaged in rendering the performances fixed on the phonorecords.

(v) The playing time of the relevant sound recording, except that playing time is not required in the case of ringtones or licensed activity to which no overtime adjustment is applicable.

(vi) If the compulsory licensee chooses to allocate its payments between co-owners of the copyright in the nondramatic musical work as described in paragraph (g)(1) of § 210.16, and thus pays the copyright owner (or agent) receiving the statement less than one hundred percent of the applicable royalty, the percentage share paid.

(vii) The names for the writer or writers of the nondramatic musical work, or the International Standard Name Identifiers (ISNIs) or other unique identifier of the writer or writers, if known.

(viii) The International Standard Work Code (ISWC) or other unique identifier for the nondramatic musical work, if known.

(ix) Identification of the relevant phonorecord configuration (for example: Compact disc, permanent digital download, ringtone) or offering (for example: Limited download, music bundle) for which the royalty was calculated, including, if applicable and except for physical phonorecords, the name of the third-party distributor of the configuration or offering.

(e) *Clear statement.* The information required by paragraph (c) of this section requires intelligible, legible, and unambiguous statements in the Annual Statement of Account without incorporation by reference of facts or information contained in other documents or records.

(f) *Certification.* (1) Each Annual Statement of Account shall be accompanied by:

(i) The printed or typewritten name of the person who is signing the Annual Statement of Account on behalf of the compulsory licensee.

(ii) A signature, which in the case of a compulsory licensee that is a corporation or partnership, shall be the signature of a duly authorized officer of the corporation or of a partner.

(iii) The date of signature.

(iv) If the compulsory licensee is a corporation or partnership, the title or official position held in the partnership or corporation by the person signing the Annual Statement of Account.

(v) The following statement: I am duly authorized to sign this Annual Statement of Account on behalf of the compulsory licensee.

(2) Each Annual Statement of Account shall also be certified by a licensed Certified Public Accountant. Such certification shall comply with the following requirements:

(i) Except as provided in paragraph (f)(2)(ii) of this section, the accountant shall certify that it has conducted an examination of the Annual Statement of Account prepared by the compulsory licensee in accordance with the attestation standards established by the American Institute of Certified Public Accountants, and has rendered an opinion based on such examination that the Annual Statement conforms with the standards in paragraph (f)(2)(iv) of this section.

(ii) If such accountant determines in its professional judgment that the volume of data attributable to a particular compulsory licensee renders it impracticable to certify the Annual Statement of Account as required by paragraph (f)(2)(i) of this section, the

accountant may instead certify the following:

(A) That the accountant has conducted an examination in accordance with the attestation standards established by the American Institute of Certified Public Accountants of the following assertions by the compulsory licensee's management:

(*1*) That the processes used by or on behalf of the compulsory licensee, including calculation of statutory royalties, generated Annual Statements that conform with the standards in paragraph (f)(2)(iv) of this section; and

(*2*) That the internal controls relevant to the processes used by or on behalf of the compulsory licensee to generate Annual Statements were suitably designed and operated effectively during the period covered by the Annual Statements.

(B) That such examination included examining, either on a test basis or otherwise as the accountant considered necessary under the circumstances and in its professional judgment, evidence supporting the management assertions in paragraph (f)(2)(ii)(A) of this section, including data relevant to the calculation of statutory royalties, and performing such other procedures as the accountant considered necessary in the circumstances.

(C) That the accountant has rendered an opinion based on such examination that the processes used to generate the Annual Statement were designed and operated effectively to generate Annual Statements that conform with the standards in paragraph (f)(2)(iv) of this section, and that the internal controls relevant to the processes used to generate Annual Statements were suitably designed and operated effectively during the period covered by the Annual Statements.

(iii) In the event a third party or third parties acting on behalf of the compulsory licensee provided services related to the Annual Statement, the accountant making a certification under either paragraph (f)(2)(i) or paragraph (f)(2)(ii) of this section may, as the accountant considers necessary under the circumstances and in its professional judgment, rely on a report and opinion rendered by a licensed Certified Public Accountant in accordance with the attestation standards established by the American Institute of Certified Public Accountants that the processes and/or internal controls of the third party or third parties relevant to the generation of the compulsory licensee's Annual Statements were suitably designed and operated effectively during the period covered by the Annual Statements, if such reliance is disclosed in the certification.

(iv) An Annual Statement of Account conforms with the standards of this paragraph if it presents fairly, in all material respects, the compulsory licensee's usage of the copyright owner's musical works under compulsory license during the period covered by the Annual Statement, the statutory royalties applicable thereto, and such other data as are relevant to the calculation of statutory royalties in accordance with 17 U.S.C. 115 and applicable regulations.

(v) Each certificate shall be signed by an individual, or in the name of a partnership or a professional corporation with two or more shareholders. The certificate number and jurisdiction are not required if the certificate is signed in the name of a partnership or a professional corporation with two or more shareholders.

(3) If the Annual Statement of Account is served by mail or by reputable courier service, the Annual Statement of Account shall be signed by handwritten signature. If the Annual Statement of Account is served electronically, the Annual Statement of Account shall be signed by electronic signature as defined in section 7006(5) of title 15 of the United States Code.

(4) If the Annual Statement of Account is served electronically, the compulsory licensee may serve an electronic facsimile of the original certification of the Annual Statement of Account signed by the licensed Certified Public Accountant. The compulsory licensee shall retain the original certification of the Annual Statement of Account signed by the licensed Certified Public Accountant for the period identified in § 210.18, which shall be made available to the copyright owner upon demand.

(g) *Service.* (1) The service of an Annual Statement of Account on a copyright owner under this subpart may be accomplished by means of service on either the copyright owner or an agent of the copyright owner with authority to receive Statements of Account on behalf of the copyright owner. In the case where the work has more than one copyright owner, the service of the Statement of Account on one co-owner or upon an agent of one of the co-owners shall be sufficient with respect to all co-owners. Each Annual Statement of Account shall be served on the copyright owner or the agent to whom or which it is directed by mail, by reputable courier service, or by electronic delivery as set forth in paragraph (g)(2) of this section on or before the 20th day of the sixth month following the end of the fiscal year covered by the Annual Statement. It shall not be necessary to file a copy of the Annual Statement in the Copyright Office. An Annual Statement of Account shall be served for each fiscal year during which at least one Monthly Statement of Account was required to have been served under § 210.16(g).

(2) If an Annual Statement of Account is being sent electronically, it may be sent or made available to a copyright owner or its agent in a readily accessible electronic format consistent with prevailing industry practices applicable to comparable electronic delivery of comparable financial information.

(3) If the copyright owner or agent has made a request pursuant to § 210.16(g)(3) to receive statements in electronic or paper form, such request shall also apply to Annual Statements to be rendered on or after the date that the request is effective with respect to Monthly Statements.

(4) In any case where the amount required to be stated in the Annual Statement of Account under paragraph (c)(6) of this section (*i.e.,* the total royalty payable) is greater than the amount stated in that Annual Statement under paragraph (c)(7) of this section (*i.e.,* the total sum paid), the difference between such amounts shall also be served on or before the 20th day of the sixth month following the end of the fiscal year covered by the Annual Statement. The Annual Statement and payment may be sent together or separately, but if sent separately, the payment must include information reasonably sufficient to allow the payee to match the Annual Statement and the payment. The delivery of such sum does not require the copyright owner to accept such sum, or to forego any right, relief, or remedy which may be available under law. In any case where the amount required to be stated in the Annual Statement of Account under paragraph (c)(6) of this section is less than the amount stated in that Annual Statement under paragraph (c)(7) of this section, the difference between such amounts shall be available to the compulsory licensee as a credit.

(5)(i) In any case where an Annual Statement of Account is sent by mail or by reputable courier service and is returned to the sender because the copyright owner or agent is no longer located at that address or has refused to accept delivery, or the Annual Statement of Account is sent by electronic mail and is undeliverable, or in any case where an address for the copyright owner is not known, the Annual Statement of Account, together

with any evidence of mailing or attempted delivery by courier service or electronic mail, may be filed in the Licensing Division of the Copyright Office. Any Annual Statement of Account submitted for filing shall be accompanied by a brief statement of the reason why it was not served on the copyright owner. A written acknowledgment of receipt and filing will be provided to the sender.

(ii) The Copyright Office will not accept any royalty fees submitted with Annual Statements of Account under paragraph (g)(5)(i) of this section.

(iii) Neither the filing of an Annual Statement of Account in the Copyright Office, nor the failure to file such Annual Statement, shall have any effect other than that which may be attributed to it by a court of competent jurisdiction.

(iv) No filing fee will be required in the case of Annual Statements of Account submitted to the Copyright Office under paragraph (g)(5)(i) of this section. Upon request and payment of the fee specified in § 201.3(e) of this chapter, a Certificate of Filing will be provided to the sender.

(6) If an Annual Statement of Account is sent by certified mail or registered mail, a mailing receipt shall be sufficient to prove that service was timely. If an Annual Statement of Account is sent by a reputable courier, documentation from the courier showing the first date of attempted delivery shall be sufficient to prove that service was timely. If an Annual Statement of Account or a link thereto is sent by electronic mail, a return receipt shall be sufficient to prove that service was timely. In the absence of the foregoing, the compulsory licensee shall bear the burden of proving that the Annual Statement of Account was served in a timely manner.

(h) *Annual Statements for periods before* November 17, 2014. If a copyright owner did not receive an Annual Statement of Account from a compulsory licensee for any fiscal year ending after March 1, 2009 and before November 17, 2014, the copyright owner may, at any time before November 17, 2014, make a request in writing to that compulsory licensee requesting an Annual Statement of Account for the relevant fiscal year conforming to the requirements of this section. If such a request is made, the compulsory licensee shall provide the Annual Statement of Account within 6 months after receiving the request. If such a circumstance and request applies to more than one of the compulsory licensee's fiscal years, such years may be combined on a single statement.

§ 210.18 Documentation.

All compulsory licensees shall, for a period of at least five years from the date of service of an Annual Statement of Account or Amended Annual Statement of Account, keep and retain in their possession all records and documents necessary and appropriate to support fully the information set forth in such Annual Statement or Amended Annual Statement and in Monthly Statements served during the fiscal year covered by such Annual Statement or Amended Annual Statement.

§ 210.19 Harmless errors.

Errors in a Monthly or Annual Statement of Account that do not materially prejudice the rights of the copyright owner shall be deemed harmless, and shall not render that statement of account invalid or provide a basis for the exercise of the remedies set forth in 17 U.S.C. 115(c)(6).

Dated: August 8, 2014,

Maria A. Pallante,

Register of Copyrights.

James H. Billington,

Librarian of Congress.

[FR Doc. 2014–22235 Filed 9–17–14; 8:45 am]

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